Labor and Globalization

Christoph Scherrer (Ed.)

The Transatlantic Trade and Investment Partnership (TTIP): Implications for Labor

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Edited by Christoph Scherrer

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Photo: Shawn Baldwin/NYT/Redux/laif: A safety inspector looks over containers alongside the Jebel Ali Free Zone, the oldest and largest free trade zone in Dubai, United Arab Emirates.

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Acknowledgments

While searching for information for a study on the envisaged Transatlantic Trade and Investment Partnership (TTIP), I found a lot of brief studies on the Internet, but located neither a comprehensive assessment of the likely consequences of TTIP nor an explicit analysis of the impact on labor. However, once the study was done, I discovered that a number of very interesting papers had been published in the meantime, which together do provide such a comprehensive assessment with a focus on the impact on workers and their organizations. Therefore, I asked the authors of these studies whether they would be interested in contributing an updated version of their studies to a volume on TTIP and its implications for labor. I am very pleased that the authors responded positively and also got permission from the organizations that previously published their studies as working papers.

The contribution of Stephan Beck in this volume builds on a study which was published in German in the spring of 2014 with the financial support of the Hans-Böckler-Foundation (Beck / Scherrer, 2014: Das transatlantische Handels- und Investitionsabkommen (TTIP) zwischen der EU und den USA, Arbeitspapier Nr. 303, Hans Böckler Stiftung, Düsseldorf). The contribution of the team led by Werner Raza is taken from a study commissioned by the GUE-NGL group in the European Parliament (ASSESS_TTIP). To avoid overlap with other contributions to this volume, some passages of their study that are not directly related to the assessment of the econometric studies are not included in this volume. Pia Eberhardt's contribution is a slightly updated version of a paper for the Friedrich Ebert Stiftung's "Dialogue on Globalization" series, published in July 2014 (The TTIP and the Future of International Investment Law). Lance Compa's contribution was also published in July 2014 as paper for the Transatlantic Stakeholder Forum of the Center for Transatlantic Relations in the Paul H. Nitze School of Advanced International Studies at The Johns Hopkins University, together with the Friedrich Ebert Stiftung Washington Office.

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Christoph Scherrer, Berlin, October 2014

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Introduction: The Challenge of TTIP

Christoph Scherrer

A deeper division of labor facilitated by trade across borders is a fountain of material wealth for societies. The more efficient execution of tasks frees up labor for the production and delivery of more products and services. It also potentially allows for more leisure time. However, deepening the division of labor across borders does not come without costs. Some costs are just of a short-term nature, a product of adjustment to new competitive circumstances. For some categories of workers within countries and for some working populations of whole countries, the costs can become quite permanent. Workers with low skills in capital rich countries have seen their living standards eroding in the last decades thanks to globalization (and technological change) and in some capital and skill poor countries most of those of working age have met a similar fate (e.g. Sub-Saharan Africa). In other words, while the liberalization of trade and investments may contribute to the "Wealth of Nations", the distribution of the spoils can be highly uneven to the point of outright losses for parts of the working population or even for whole countries. Therefore, any further steps to liberalize trade and investment need to be broadly discussed by society.

For the currently negotiated Transatlantic Trade and Investment Partnership (TTIP), broad public deliberations are of particular pertinence as TTIP is supposed to go much further than to reduce or to eliminate tariffs. Because most tariffs are already quite low for transatlantic trade, TTIP mainly aims at reducing “non-tariff barriers”. While tariffs on goods crossing borders have been imposed with an eye to foreign competition, most of the non-tariff barriers are the laws and regulations "constructed over decades of struggle by labor and social movements to protect the collective political, economic and social rights of working people" (IUF in this volume). These laws and regulations cover employment, environmental protection and public health. The negotiators on both sides of the Atlantic especially target public ownership and public provision of services as barriers to the free flow of goods, services and investments. Not only should the power of the democratically elected bodies to provide infrastructure and services according to need and not just to the purse be circumscribed by the new trade agreement, the negotiators also want to grant corporations the right to sue states for compensation in case new laws or regulations might lower future profits. This so-called investor-to-state dispute settlement process will sidetrack the normal legal procedures as it will establish arbitration courts run by the business community.

TTIP is clearly driven by a corporate agenda. In the preparation for drafting the negotiation positions for the United States and the European Community, trade unions and civil society organizations had only a very marginal presence if at all. While labor was not invited to the fora formulating the negotiating positions, it is certain that labor will feel the impact of these negotiations once concluded. It is therefore pertinent to assess the likely impact in detail. The assessment of future events is always riddled with uncertainty. In the case of the TTIP, the look into the future is made even more difficult as the negotiations are held in secrecy. However, public statements by corporations and governments about what they consider as trade barriers as well as leaked documents allow speculations about the likely content of the final agreement. Against the background of past experience, it is possible to assess the likely impact of different negotiation scenarios on labor.

Channels of impact on trade unions

Not all trade unions are directly affected by TTIP. Indirectly, however, the whole labor movement will feel the impact of increased corporate power. In the following, I will briefly sketch the various channels of impact.

Public-sector unions and their members are most directly in the focus of TTIP. As mentioned above, TTIP aims at opening up the public sector for private competition by defining public services that are to be exempted from the agreement very narrowly and by lowering the threshold for open competitive bidding in the public procurement market (Fritz 2014). These measures will lead to further privatizations which on average have undermined collective bargaining in fields previously covered by the public sector. Employees with scarce qualifications will particularly suffer income losses and harsher working conditions (Schmelzer-Roldán 2014: 21-36). TTIP will also affect privately delivered services, especially in retailing, but also in the health sector. Lower standards for data protection will accelerate online shopping and fewer possibilities for municipalities to restrict big-box retailing will push smaller chain stores to the margins. Limits on public health services and, again, lower data protection will further the concentration in the hospital sector, among pharmacies and, if online medical consultation spreads, among physicians.

Members of trade unions in small scale agriculture will come under severe pressure. Even proponents of TTIP have calculated job losses for smaller farms (Bureau et al. 2014). In manufacturing, the impact will vary according to competitive strength and size. Members of trade unions in large companies that are highly competitive, for example German auto companies, can expect that output of their companies will increase and overall employment levels of their companies will increase. However, it is not guaranteed that the additional employment will accrue in those factories where the trade unions have a strong presence. TTIP is very much an investment agreement which facilitates cross-border investment and thereby also increases the discretionary powers of management to allocate work across borders. This increased leverage will not strengthen the bargaining position of the trade unions in the TTIP "winner" industries. Furthermore, trade liberalization logically implies a larger market and a larger market means more room for scale economies, which in turn will lead to further concentrations. Therefore, employees in smaller manufacturing companies, unless they command a technological lead, are likely to feel the competitive pressure from the big companies. In addition, some of those benefits from harmonized standards through TTIP, such as safety requirements in relation to lights and brakes on automobiles mentioned by the European Commission (2013: 3), might actually lead to fewer jobs because fewer tasks are necessary to adapt the product to local regulations.

Members of trade unions are not only producers but also consumers. As consumers they might profit from lower prices thanks to TTIP induced efficiency gains. However, since most of the significant changes are to be expected in the public sector, members of trade unions living in countries with more or less functioning public sectors are likely to experience limited access to these services if they have to live on a small budget, and deteriorating quality of services, especially when the services depend on a large physical infrastructure such as public transportation or water supply and disposal (because private investors tend to neglect maintenance in favor of short-term profits). Lower standards for food quality and data protection have been highlighted in the media. There is one area where US negotiators are pushing

for higher standards and this is the protection of intellectual property, especially for pharmaceutical companies. While this may benefit these companies, and it even may trickle down to their employees (if the monopoly rent is not used to uphold the stock market price), it will increase the medical bills of most ordinary people.

Workers are also tax payers. TTIP will lead to lower tariffs and therefore to lower income for states, though not to a very significant extent because tariffs are already quite low (see Raza et al. in this volume). Of greater importance could be the greater ease for cross-border investments and thereby for tax avoidance. The possibilities for corporations to file compensatory claims for forgone income due to new government regulations can, if present trends are any indication, lead to very hefty expenses for government entities (see Eberhardt in this volume).

Finally, workers are also citizens with rights to participate in the political process. Many of the clauses foreseen for the TTIP aim at making the agreed upon liberalizations irreversible. The investor-to-state dispute settlement process in particular will limit policy space since municipalities or higher levels of the state will face costly lawsuits and high claims for compensation in ad hoc arbitration courts outside the normal legal processes in case they decide on new regulations protecting workers, consumers, and the environment (see Eberhardt in this volume). The introduction of a minimum wage or raising the minimum wage may trigger such lawsuits by foreign investors (or the foreign subsidiaries of domestic investors) claiming that the resulting higher wage bill will lower their profit expectations. The same may hold true for providing workers with more rights or better protection at the workplace (see Compa in this volume). In sum, the broad scope of TTIP will limit its impact not to the export and import businesses but will affect workers as producers, consumers, citizens and as collective actors.

Acting on the challenge of TTIP

Liberalization of trade can be wealth creating, as mentioned above. The TTIP, however, is less about trade than about increasing the power of corporations. Since corporations are already powerful and have been able to line up the governments on both sides of the North Atlantic in favor of TTIP, labor faces an uphill battle in preventing the most egregious power grabbing aspects of this very complex agreement. In this uphill battle, fortunately, labor is not standing alone. Many organizations of civil society have become aware of the dangers of a TTIP if the current agenda of the chief negotiators are realized. Therefore, campaigns on the issues of TTIP also offer the opportunity to strengthen organized labor's ties to civil society.

Any campaign has to start with the members, since trade unions are not advocacy organizations but membership-based mass organizations. Issues of trade are far removed from the shop floor and, quite naturally, seldom on the minds of the members. It is therefore adamant to analyze the likely impact of the demands put forward by the negotiators for the workplaces of the respective trade union members. This analysis should not rely on the standard models used by economists. These models rely on dubious assumptions and completely neglect any social benefit arriving from regulation (see the contribution by Raza et al. in this volume). Instead, the analysis should rely on a careful reading of previous experiences, an assessment of the current and projected competitive position of their respective company or industry, and an awareness of the company or industry labor relations strategy. Even if this analysis comes up with

a positive balance in terms of employment perspectives, the respective trade union should consider the impact of the TTIP on the broader movement. If labor is weakened overall, it is quite likely that even the lucky workers will eventually see their position vis-a-vis capital eroded. Without solidarity from other workers, even workers with a strong market position will lose out to capital in the end. Capital commands not only market power, but has also political power, and the more of the latter, the weaker the labor movement is overall. And it will make use of it, as we have seen in the attacks on the last bastions of US trade unionism, the public sector in the wake of the financial crisis (Adler 2011).

Jobs and working conditions are dearest to trade union members, but these work-related issues do not define them. To various degrees they are also interested in consumer and citizen issues. Since TTIP covers so many issues, it should not be too difficult to mobilize the membership with a context-sensitive framing of the issues. Nevertheless, without pointing out avenues to influence the outcome of the trade negotiations, TTIP campaigns will likely be limited in that capacity to mobilize. As has been shown for other international trade negotiations, there are many routes for trade unions and civil society organizations to influence trade negotiations. These differ from country to country and have to be carefully but also creatively identified (McGuire and Scherrer et al. 2010). In this respect, the European trade union movement is at a disadvantage in comparison to the Canadian or the US movement because for most workers the European Commission and the European policy process remains a mystery. And the European Commission knows its advantage and has made use of it by rejecting the European Citizens' Initiative on TTIP and the Comprehensive Economic Trade Agreement with Canada (CETA) in September of 2014.[1]

However, civil society organizations can even make a difference in the European Union. If the TTIP turns out to be as comprehensive as envisaged by the chief negotiators, the text of the agreement will have to be presented to the parliaments of the EU member states. Therefore, the national parliaments remain a good target. In the event the agreement does not turn out to be so comprehensive then it is also not so threatening. In the event the agreement is comprehensive but the European Court of Justice concurs with the European Commission and declares the agreement fully in the competence of the European Commission (and not as "mixed agreement" that requires the ratification by national parliaments, Mayer 2014), two avenues for civil society remain open: the European Parliament and the national governments. A majority in the European Parliament as well as a qualified majority in the European Council (which is comprised of the governments of the member states) have to approve of the agreement before ratification. Therefore, a TTIP campaign should address the European Parliament and its members as well as the national governments. The national governments can also influence the negotiations while ongoing even if the EU Commission has exclusive competence. In the case of exclusive competence, the Commission is the sole negotiator but has to consult national experts on a continuing basis. If the final TTIP agreement covers the field of trade in cultural and audiovisual services or in social, education and health services (which is quite likely), the European Council has to approve it unanimously, i.e. a "no" vote by the government of one country will suffice to stop the agreement from adoption. Success in using these

[1] This initiative was supported by more than 250 civil society organizations in 21 member states. The European Citizens' initiative (ECI) provides a platform for citizens to present a legislative proposal to the Commission if they collect over one million signatures. See, http://www.euractiv.com/sections/trade-industry/commission-opposes-european-citizens-initiative-against-ttip-308406

avenues rests on the ability to reach out to trade unions and civil society in the other member states. If the campaign is seen mainly as being carried out by just one or a few countries, it will not likely resonate with the rest of Europe and its governments. Since the Canadian and the US American trade unions and many civil society organizations in both countries also take a skeptical look at the corporate agenda manifested in the negotiating positions of their respective governments, joint activities might help the campaigns on both sides of the Atlantic to avoid the stigma of national chauvinism which the corporate lobbyists love to stick on anyone who criticizes liberalizing trade and investments across borders (for lessons to be learned from union mobilization against trade agreements, see McGuire 2013).

Structure of the book

This volume intends to contribute to the debate about the impact of TTIP on labor by providing an overall introduction to the negotiations of TTIP, by assessing the reliability of the studies in support of TTIP, by highlighting specific problematic items of the negotiations and by presenting the position of organized labor from both sides of the Atlantic as well as from the international level.

The first part of this volume provides a general assessment of TTIP and a critique of the econometric studies commissioned by supporters of TTIP. It starts out with a study by Stefan Beck from the University of Kassel which was financially supported by the Hans Böckler Foundation, the foundation of the German trade unions. Beck provides a general introduction to the TTIP negotiations. He examines first the historical and political context of the negotiations by discussing the strategic orientation of the European Commission, the development of the world trade regime and the actors driving the process. He then maps the aims, objects and scope of the negotiations which allows him to sketch different scenarios for the negotiation outcomes. He then proceeds to quantitatively assess the possible economic, political and social consequences of the various scenarios. Given the priorities of the negotiators, he pays particular attention to the fields of public procurement and services. He comes to the conclusion that the prosperity effects claimed by TTIP supporters will be insignificant and have to be assessed against serious risks for the public in general and labor in particular. He also raises the issue of the lack of transparency of the negotiations in violation of democratic principles.

The team led by Werner Raza, the director of the Austrian Foundation for Development Research in Vienna, assesses the four most frequently cited econometric studies in support of TTIP. Their study was commissioned by the GUE-NGL group in the European Parliament. To avoid overlap with other contributions to this volume, some passages of their study that are not directly related to the assessment of the econometric studies are not included in this volume. Raza et al. begin with a detailed overview of the projected benefits of TTIP by these influential econometric studies. They come to the same conclusion as Stefan Beck, i.e. even the studies in support of TTIP estimate only small economic effects. They then highlight the potential macroeconomic adjustment costs as well as the social costs of regulatory change that are generally neglected in these econometric studies. They point to the likely occurrence of balance of payments problems for individual EU member states, to losses for the public budgets of the EU and its member states because of the elimination of the remaining tariffs, and to the difficulties of re-employing less skilled workers in import competing sectors who lose their jobs because of increased competition. As social costs, they identify threats to consumer safety, public health and the environment.

Since the North American Free Trade Agreement (NAFTA) is frequently cited as a showcase example for successful trade liberalizations, Raza et al. compare the ex-ante assessments and the ex-post experiences of NAFTA. This comparison reveals that the ex-ante projections substantially overestimated the economic effects. For Mexico, NAFTA even diminished GDP growth, cut into real wages, and increased income inequality. Their study continues with a detailed analysis of the theoretical background and the technical specifications of the applied models. This analysis includes a discussion of the models' origins, the way trade costs and non-tariff barriers are estimated, and the assumptions of two commonly used computable general equilibrium models. These assumptions turn out to be unrealistic. In addition, Raza et al. assess to what degree the innovative methodology of one of the four studies, the Bertelsmann/ifo study, overcomes the other studies' deficits. This latter study suffers from an unrealistic labor market model. Finally, Raza et al. discuss the estimations on the effects of income derived from foreign direct investment. This very detailed and technical assessment of key studies in support of TTIP questions the very selling point of TTIP: employment gains.

The second part of this volume highlights the unequal treatment of investors and workers in the envisaged TTIP. Pia Eberhardt, who works with Corporate Europe Observatory and is an alumna of the Global Political Economy Master program at the University of Kassel, looks at a specific privilege for corporations foreseen in the TTIP: the right for foreign investors to sue the United States as well as the European Union and its member states before private international tribunals. Such tribunals are quite common to international investment agreements, but have so far been seldom agreed upon between rich democratic states. The most prominent investor protection clause in a trade agreement among democratic countries is included in NAFTA. An even more comprehensive protection clause is now envisaged for transatlantic investments protecting not only direct investments but also investments in financial instruments. Eberhardt argues convincingly that such investment protections bypass the rule of law with their private parallel law for corporations and present an encroachment on the regulatory autonomy of states. They thereby undermine democracy in favor of the private property rights of foreign investors.

She begins her contribution with a review of the development of international investment law followed by an identification of problem areas and a discussion of the current controversies surrounding the protection of investors. Her analysis of the current position of the EU Commission on investor protection includes the most recent reform proposals. In response to widespread criticism, the EU made its proposal for an investor-to-state dispute settlement process for TTIP public. The EU Commission invited civil society to comment on its proposal in the summer of 2014. Eberhardt finds these reform proposals fall short of addressing the substantial democratic deficit of such private tribunals. However, she welcomes the politicization of investor protection as an opportunity for a fresh start in investment policy. Specifically, she calls for investment agreements that do not go beyond the protection of private property as stipulated by national constitutions that oblige investors to respect human and workers' rights and that do not restrict the regulatory autonomy of the state.

While the trade negotiators intend to grant special privileges for investors, they see no need for protective measures for workers. Lance Compa, who teaches at Cornell University's School of Industrial and Labor Relations, shows otherwise in his contribution. He argues that many areas of labor law, labor rights, labor standards, and social protections on both sides of the Atlantic have severe flaws. He underpins his claim with a number of concrete examples of the violation of workers' rights by US- as well as EU-based

corporations. The investor-to-state dispute settlement process discussed in the previous chapter particularly threatens minimum-wage policies and considerations for social standards in public procurement, as well as health and safety standards. He recommends that Europe and the United States bring the social dimension of a trade agreement to new, higher standards of both substance and process.

Part three of this volume features the position of organized labor on TTIP. The purpose of this part is to overcome national insularity in the labor movement in discussing TTIP. The sophisticated position papers show that trade unions on both sides the Atlantic share a lot of common concerns. They also reveal some differences in priorities that deserve further discussions.

Part three begins with a position paper written by the American Federation of Labor and Congress of Industrial Organizations (AFL-CIO). It was submitted to the British House of Lord's Subcommittee for its Inquiry into TTIP already on October 10, 2013. This paper contradicts the frequently made argument in Europe that the TTIP negotiations only worry the European labor organizations. The AFL-CIO is equally concerned that the TTIP continues the low-road, neoliberal model and substitutes corporate interests for people's interests. The federation worries that workers in the US and the EU will continue to pay a high price in the form of suppressed wages, a more difficult organizing environment, and general regulatory erosion. The position paper covers in great detail the various dimensions of the envisaged TTIP. It calls for a broad definition of public services; it opposes the use of negative lists for any service commitments; it argues for leaving adequate policy space, flexibility, and authority to effectively regulate financial services; it rejects investor-to-state dispute settlement; it supports the rights of all governments to use procurement policies to create jobs in their respective areas and it defends worker, consumer, and food safety protections of the EU.

While these positions are very much in line with positions of trade unions in Europe (see the contributions of CGIL and ver.di in this volume), the paper also includes some positions specific to the United States that might not be shared by all European trade unions, i.e. concerning the maritime and the transport sectors and so-called offsets that are frequently an integral part of international defense contracts (subcontracts or technology transfer required by foreign governments when purchasing weapon systems). It also calls for effective intellectual property protection, but not at the expense of access to affordable medicines. Overall the AFL-CIO recommends that the United States and the European Union pursue a new approach to trade policy. Trade policy should prioritize benefits for working families. A trade agreement must include the promotion of the ILO's fundamental labor rights and the preservation and expansion of public services.

The second trade union position paper was drafted by the Italian General Confederation of Labor (CGIL), the largest trade union federation in Italy. First published in June 2014, the paper starts out with a general critique of the bilateral approach to trade negotiations exemplified in the TTIP negotiations. These bilateral negotiations undercut the multilateral approach within the World Trade Organization (WTO), where developing countries also have a say. Because the rich industrialized nations do not want to remove their massive agricultural subsidies, negotiations within the WTO have broken down. The bilateral approach is now used by these rich countries to impose their demands on the rest of the world without much compensation. The CGIL criticizes this agenda on two accounts. First, these bilateral trade agreements do not address the trade imbalances among nations. Second, the bilateral trade agenda, with

its focus on the non-tariff barriers, will limit government policy space. As a particular threat for democracy, the paper highlights the envisaged Regulatory Cooperation Council (RCC) and the already mentioned investor-to-state dispute settlement process (ISDS). The RCC is supposed to prevent laws and regulations which may negatively impact the level of trade liberalization achieved by TTIP. CGIL therefore rejects the inclusion of RCC and ISDS in TTIP and calls instead for the inclusion of enforceable clauses regarding environmental, social and labor standards.

The third trade union position paper was written by a Global Union Federation, the International Union of Food, Agricultural, Hotel, Restaurant, Catering, Tobacco and Allied Workers' Associations (IUF). It was published in the spring of 2014 and focuses especially on the investor-to-state dispute settlement process envisaged for TTIP. It provides evidence from past law suits by companies for example against the Canadian state in the framework of NAFTA or against Slovakia on the basis of the Netherlands-Slovakia Bilateral Investment Treaty to highlight the dangers such private arbitration courts pose to the capacity of governments to regulate in the public interest. It calls for widespread public opposition to investment treaties. Such opposition can build on the previous successful mobilizations against the Multilateral Agreement on Investment (MAI) and the Free Trade Agreement of the Americas.

The final trade union position paper was drafted by the German United Services Union (ver.di) in response to the call of the EU Commission to comment on its proposal for an investor-to-state dispute settlement process (ISDS). It answers the questions raised by the Commission one by one; the proposal for a reformed ISDS is inserted in the Annex. It was written by legal experts and comes to the same conclusion as Pia Eberhardt in this volume: there are no sufficient reasons to integrate such a mechanism into TTIP. Despite the reform proposals, significant room for interpretation in the arbitral tribunals and the structural bias towards investment protection remain, including the thereby enabled potential to threaten other socially and democratically justified aims and rights to regulate.

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I. Assessing TTIP and Its Supporting Studies

1. TTIP: Possible Negotiating Outcomes and Consequences

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1.1. Introduction

The promises sound enticing – an enormous boost to growth, hundreds of thousands of new jobs, bigger incomes and higher real wages. Even better, all of this can apparently be achieved with scarcely any national debt increases or social cuts. It would be hard to imagine anything better for the crisis-hit economies and debt-laden public budgets of Europe and the US.

Since early 2013, the European Commission, representatives of the German Federal Government and the free market media and think tanks have been beating the drum for a Transatlantic Trade and Investment Partnership (TTIP). A (further) liberalization of transatlantic trade and the facilitation of mutual investments – by dismantling customs duties and "unnecessary" regulations - will, it is claimed, not only help to pull the countries concerned out of crisis, but also strengthen their economies and enterprises for competition with the dynamic, upwardly mobile economies of, in particular, Asia, while giving a new impetus to the currently sluggish (multilateral) liberalization of world trade. It all looks like one more confirmation that it takes a crisis to sweep aside "petty" differences and push innovations through.

But a closer look reveals a much more nuanced picture. The transatlantic trade liberalization motif is by no means new or innovative. In fact, this aim has been pursued for many years now by transnationally active US and European firms. Nor are many of the existing regulations "unnecessary" or even "hidebound". Rather, they are the result of social debate and also often of social, ecological and economic achievements. Here, regulatory and institutional differences are not just historical baggage, as may be seen for instance from comparative economic studies (e.g. Amable 2003). Rather, they are an expression of societal preferences and compromises *and* they are a functional or institutional corollary of the economic specialization concerned and the competitive advantages that go with it. The division of labour and international trade are based on existing (or emerging) differences, not on levelling.

Just as questionable are the promised gains in prosperity, along with their much-vaunted backing from economic studies and scientific experts. Because in fact, these studies are based on closed, deterministic models and are of limited significance. They share the premise that "the market" is necessarily the most effective form of allocation and that a corresponding liberalization or deregulation will *per se* generate greater prosperity. Quite apart from the question of an ahistorically and asocially constructed, abstract market model, it has long been known that this is not necessarily the case (e.g. Polanyi 1944). While the assumptions and constructions underlying such models are problematic, the political uses to which they are put are at least equally so. The predicted prosperity effects are regularly based on the most optimistic scenarios within these studies, although the studies themselves treat the optimistic scenarios as somewhat unrealistic. Moreover, the epistemologically reductive approach taken in the econometric studies is never mentioned. They usually set out to quantify the prosperity gains induced by dismantling regulations that

inhibit *external* trade. The function of regulations is more or less reduced to their impact at the frontier of the economic area concerned. In fact, though, the functions of most national state regulations (or "behind the border" regulations, to use trade parlance – and these are the ones that we are mainly concerned with here) are motivated by home market considerations. The prosperity or distribution effects resulting from them, such as social or ecological impacts, are not quantified in the studies. This places the modelling studies in a logical quandary - which is, however, masked from the outset by the underlying assumptions. The prosperity and distribution effects thus calculated are in particular based (neoclassical models aside) on the distributive impacts of precisely those types of regulation that are now to be called into question from the perspective of external trade liberalization.

So TTIP is about much more than the prosperity gains that might be made in the short or medium term by boosting trade. In view of the proposed sanctions in case of violations of investors' rights and "lock-in" effects (such as standstill clauses forbidding new regulations) that the more recent trade agreements provide, and which are also envisaged in the TTIP, the real issue is the long-term societal or democratic ability to shape institutions that are relevant to allocation, distribution and prosperity. Thus, alongside the immediate economic, environmental or social effects, the longer-term economic *and* political distribution impacts are to the fore here – and this begs the question of the interests and motives driving these developments.

High-profile disputes about things like "chlorine hens", "meat hormones", "GM food" or "fracking" are just the tip of the iceberg in these negotiations, as are the regular debates about customs tariffs or agricultural subsidies. Also at stake is the scope for long-term democratic decision-making and distribution goals, both nationally and internationally. This is about shaping and guiding public service provision, as well as the possibilities for democratically setting and pursuing social or environmental policy aims.

This chapter will therefore focus more particularly on the possible medium- and long-term social, economic and political consequences of a possible transatlantic agreement. To assess the thrust and possible consequences of the TTIP, the negotiations first need to be examined in their historical and political context, for instance the strategic orientation of the European Commission, the development of the world trading regime, or the actors and interests driving the process. The aims, objects and scope of the negotiations will then be mapped out in the light of the documents used to prepare or launch them, as far as those documents are available. In the nature of things, the possible outcomes of the negotiations are uncertain, and estimates of the possible consequences therefore draw on various different scenarios. But there will be some short discussion of at least those points of dispute that have already become apparent and, where appropriate, of differences that are relevant to the negotiations. In this way, at least the prospects on the horizon can be qualitatively described, in addition to the quantitative scenarios. Finally, the possible economic, political and social consequences will be discussed. As well as the quantitative economic prosperity expectations and the political and regulatory risks of the way the negotiations have been designed, particular attention will be paid to the fields of public procurement and services, and possible distribution-relevant social and labour policy consequences will be discussed.

1.2. Subject and Aims of the TTIP Negotiations

1.2.1. TTIP: Long in the Making

The current negotiations on a trade and investment agreement between the US and the EU continue a transatlantic dialogue of many years' standing, as well as many initiatives to institutionalize cooperation on regulation issues (cf. Pollack et al. 2003). Back in 1990, just after the end of the Cold War, the EU and the US already agreed in the Transatlantic Declaration that representatives of the US government, the European Commission and the European Council would meet regularly to discuss the aim of economic liberalization, as well as cooperation on security and cultural issues. However, beyond its specified aims, the agreement remained rather insubstantial, and with the Competition Policy Agreement of 1991 solely one concrete economic policy agreement was ratified.

The relationship was given a fresh boost by the 1995 New Transatlantic Agenda, which aimed notably to help promote trade and investment relations and improve exchanges at the non-governmental level, for example through recognition of the role of the Transatlantic Business Dialogue. After additional reinforcement by the Transatlantic Economic Partnership in 1998, nine further formal agreements followed between 1997 and 2002 on cooperation in a whole range of regulatory fields, such as technical regulations or mutual recognition of standards in various sectors. There were also many informal talks, which passed almost unnoticed by the public, on virtually all aspects of regulation in the US and the EU (ibid., p. 34). After the 2002 adoption of the Guidelines for Regulatory Cooperation and Transparency and the more systematic Roadmap for EU-US Regulatory Cooperation and Transparency (2004 and 2005), which embodied 15 sector-specific projects, various other dialogue forums followed, including the EU-US Regulatory Dialogue on Financial Services in 2002 (cf. Posner 2009) and the High-Level Regulatory Cooperation Forum in 2005.

However, despite all the initiatives, success on regulatory issues remained limited. For instance, various agreements on mutual recognition were never implemented, due to a lack of mutual trust. In some cases, unilateral regulations were not in line with the agreements, thus provoking disputes. In other fields, a lack of coordination or of political commitment meant that hardly any material progress was made. Against this backdrop, German Federal Chancellor Merkel, who was also President of the EU Council at that time, US President Bush and EU Commission President Barroso set up the Transatlantic Economic Council (TEC), within the Framework for Advancing Transatlantic Economic Integration between the United States of America and the European Union. The TEC was intended to provide stronger political support, at the ministerial level, for cooperation initiatives. It is advised by the Transatlantic Legislators' Dialogue (European Parliament and US Congress), the Transatlantic Consumer Dialogue and the TransAtlantic Business Dialogue (Ahearn 2009). And it was the TEC that, at the behest of the EU-US summit, set up the High-Level Working Group on Jobs and Growth in November 2011. That working group prepared the current TTIP negotiations.

From at least the mid-1990s, the liberalization of transatlantic trade has been seen as an important project, particularly by big firms in the EU and the US. In Europe, with the conclusion of the GATT Uruguay Round in 1993, the free trade supporters gained the upper hand over the "europrotectionist" faction (De Ville 2013a) – as Apeldoorn (2000) demonstrated in the case of the European Round Table of

Industrialists (ERT). The achievement of a transatlantic free trade agreement then became the explicit mission of the Transatlantic Business Dialogue (TABD), which had been founded in 1995. At the beginning of 2013, following a merger with the European-American Business Council (EABC), it was renamed the Trans-Atlantic Business Council (TABC). Alongside individual sector-specific firms, the TABC in particular had been an integral advisory component of the transatlantic regulatory dialogue and had a major influence on the negotiations. Correspondingly, in the three rounds of consultations held by the Commission concerning the work of the High-Level Working Group, almost 80% of all submissions already came from individual firms and their associations or interest groups, such as the ERT, the TABD, Business Europe, the European Services Forum (ESF), the Association of German Banks and the German Chambers of Industry and Commerce (DIHK). The remaining submissions were from state representatives, trade unions, consumer associations, non-governmental organizations and individuals.

Finally, a possible transatlantic trade and investment agreement has to be seen in the context of the (internal) European and international developments in trade policy. Once the free trade faction among the European firms had won through, the direction of European trade policy also changed. When the then EU Trade Commissioner Sir Leon Brittan presented the new "Market Access Strategy" in 1996, the EU Commission made a clear commitment to further trade liberalization, stronger competition and the aim of opening up markets outside Europe. And although in the 1990s, the export of market-correcting environmental or social standards still had a certain part to play in the EU's trade policy discourse, these aims were more and more clearly subordinated to those of competitiveness and market development (De Ville/Orbie 2011). Not long after the conclusion of the Uruguay Round, the EU was already pushing for further types of trade liberalization, and during the preparations for the WTO Doha Round, it advocated the inclusion of what are known as the "Singapore issues" – investment, competition law, public procurement and trade facilitation. The question of the social regulation of trade, however, was soon taken out of the WTO negotiations, and responsibility for it was handed over to the International Labour Organization (ILO), while environmental regulations were more and more devalued and, in line with the logic of "negative integration", i.e. mutual recognition of different (potentially lower) standards instead of an agreement on one common standard, were reinterpreted (De Ville 2013b).

With its growing orientation towards market opening and negative integration, the EU's trade strategy also corresponded to the development of the EU internal market on the basis of the Dassonville and Cassis de Dijon rulings of the European Court of Justice. This correspondence has been particularly apparent since the Lisbon Agenda was drawn up in the year 2000, initially through the "New Labour"-style reformulation of labour market and social policy along supply-side lines and its subordination to competitiveness, and then through the neoliberal shift to a "Growth and Jobs Strategy" in 2005. With the "Global Europe" and "Trade Growth and World Affairs" strategies, presented in 2006 and 2010 respectively, the Commission explicitly confirmed the link between external market opening and the European internal market reforms – i.e. in both cases the dismantling of "unnecessary" regulations, as part of the overarching aim of competitiveness (De Ville 2013b, p. 96; Siles-Brügge 2011). So the liberalizing strategy for trade policy is not motivated by neomercantilist considerations alone – especially in the context of the Eurozone's weak growth, which has been aggravated by austerity policies. It also serves as a justification for structural reforms of the internal market and the neoliberal disciplining of the

less "deregulation-happy" actors within the EU (cf. Hay 2007; De Ville 2013a). This means that the negotiations on a transatlantic trade and investment agreement have to be seen against the background both of internally and externally oriented political efforts and of the possible socio-economic effects, given the international economic relationships and the dynamics and regulation of the European internal market.

1.2.2. Ambitions for a Comprehensive Agreement

Only very limited information has been made public so far about the concrete subjects, positions and strategies for negotiation. The following presentation therefore draws upon the few sources available, particularly the final report of the High Level Working Group on Jobs and Growth (HLWG 2013), the EU mandate (EU 2013), position papers published or leaked by the Commission (EC 2013b-g) and information on the first negotiating round in July 2013.

According to the recommendations of the bilateral High Level Working Group on Jobs and Growth, an agreement between the EU and the US, and the EU's CETA agreement with Canada, should be comprehensive. Alongside a further reduction of tariffs and of restrictions on the trade in goods, and above all a liberalization of the service sector, it should also cover the dismantling of "domestic" non-tariff trade barriers and/or State regulations, the adaptation or harmonization of regulatory standards (e.g. technical ones), thoroughgoing protection of investments including intellectual property rights, the opening up of state procurement systems, and competition policy measures such as the abolition of favourable state treatment and of local content clauses. Finally, environmental and social protection criteria are to be laid down in a separate *sustainable development* chapter (cf. HLWG 2013).

Horizontally, across all sectors, the agreement is to set new market access standards for trade in both goods and services, for investments and for public procurement. These standards are to go beyond the provisions of trade agreements reached between the EU and the US up to now. In other words, they are to entail the almost complete abolition of tariffs, liberalization of services to a greater extent than achieved to date, the highest investment protection level ever achieved, and access to public tenders at all levels in line with the national treatment principle. Non-tariff trade barriers and regulations, meanwhile, are to be cut to a minimum, or else they are to be made more transparent and efficient through increased compatibility, harmonization and mutual recognition, and/or reductions in "unnecessary" costs. In particular, as regards sanitary and phytosanitary measures (SPS) and technical barriers to trade (TBT), the provisions within the relevant WTO agreements are to be taken over and further developed. Alongside the horizontal, sectoral or suprasectoral provisions, the agreement is to include more specific accords for individual sectors, such as raw materials and energy, small and medium-scale enterprises and intellectual property rights.

1.2.3. A Blueprint for the Rest of the World

However, the ambitions that are bound up with the negotiations on a transatlantic agreement are in no way confined to the immediately expected economic gains. Neither the US negotiators nor the European Commission have made any secret of the fact that the trade policy aims involved go beyond purely bilateral relations. In particular, both parties are out to set new standards for world trade in those critical

fields where progress at the multilateral level would be significantly more difficult to achieve – or would entail more extensive concessions, for example to the developing countries. In particular, these critical fields include the "Singapore issues", but also even stronger protection for intellectual property rights – for instance, stronger patent protection for medicines in relation to the development and sale of generics, as well as further liberalization (i.e. market opening) of services. The EU and US intend not only to provide templates for future World Trade Organization negotiating rounds on these issues, but also at the same time to use their joint political and economic sway to open up third country markets for their firms, through direct pressure for adjustment, and to push back the regulations that these countries have adopted, often for development policy reasons – for instance, rules about local content. After all, for both parties, this is about halting their loss of trade policy clout, particularly vis-à-vis the Asian region. This concern is due to the simultaneous US negotiations with the Asia-Pacific region (TPP), but it applies even more to the EU (cf. Josling/Crombez 2013; Berger/Brandi 2013).

Bilaterally, the ambitions – as formulated, at least - are no less far-reaching. One major aim is to agree upon, or more or less irreversibly establish, the highest possible levels of liberalization, trade facilitation or - in the case of investments and intellectual property rights – protection, as compared with the agreements reached up to now (e.g. bilateral agreements, GATS, TRIPS, GPA). At the same time, each side is determined to open up the other's most protected or regulated fields. Examples of such regulation in the US are public procurement and the so-called "Buy American" rules. On the European side, there are the agricultural sector and the restrictions on GM food. But it remains to be seen how far these aims can be achieved. On the one hand, it may be expected that these fields will be used as bargaining chips, as for example the automotive sector was in the agreement between the EU and South Korea (cf. Siles-Brügge 2011). On the other hand, it is precisely in these fields that the decision-making competences and combinations of interests at the various levels are complex within both negotiating camps.

The interplay among the different regulatory levels creates a particular direction of thrust, notably in the European Commission's negotiating strategy. As mentioned, the Commission is following not only a market opening strategy beyond EU borders, but also, led by the influential Directorates-General for Trade and for Competition, a liberalization and deregulation strategy aimed at the internal market and against regulation by national states. So it would be wholly reasonable to expect that the Commission, pursuing a sort of "two-level bargaining" strategy, will try to use the transatlantic negotiations to move forward on its own projects for the internal market, such as the water supply privatization plans debated in connection with the services concessions directive. Since, particularly in the service sectors, liberalization provisions are generally taken further within bilateral or regional agreements than in multilateral ones (van der Marel 2013), the Commission might also try to use the negotiations as leverage for stronger implementation of the EU services directive (or the liberalization of fields that are exempted from that directive, such as financial services).[1]

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[1] Such a secondary effect is, for example, also anticipated by the authors of the CEPII study in their "reference scenario" (Fontagné/Gourdon/Jean 2013, p. 8).

1.3. The EU Negotiating Position

After the European Parliament had, in a resolution on 23 May 2013 [2013/2558(RSP)], supported the launching of negotiations on a transatlantic trade agreement, the Council of the European Union on 14 June adopted a negotiating mandate for the Commission to begin the negotiations. The TTIP mandate (EU 2013), which was kept secret at first but leaked out that July, is in line with the recommendations of the High Level Group and provides the EU with a concrete negotiating position. It defines the overall framework, principles, and aims. The framework includes conformity with the WTO, comprehensiveness extending beyond WTO agreements, and binding force upon all levels of government. The principles include an affirmation of values held in common, sustainable development and legitimate policies in the interests of the general good. The aims encompass increasing the volume of transatlantic trade and investment, preventing "social dumping" or "environmental dumping", not impinging upon cultural diversity. The mandate also contains more concrete provisions on *market access*, *regulations and non-tariff barriers,* and *rules.*

Before the first negotiating round on 8-12 July 2013, the Commission drew up *Initial EU Position Papers* on various issues, and subsequently published them – or some of them at least[2] (EC 2013b-g):

- Cross-cutting disciplines and institutional provisions
- Technical barriers to trade
- Sanitary and phytosanitary issues
- Public procurement
- Raw materials and energy
- Trade and sustainable development.

As well as more concrete proposals for structuring individual sections of the agreement, the *position papers* give more detail on the main points of the Council mandate and expand them. They also include proposals on the institutional structure and on further liberalization negotiations that are provided for in the agreement ("inbuilt agendas"). So it is possible to give a rough sketch of the Commission's initial negotiating position.

1.3.1. Improved Market Access

For the *trade in goods,* tariffs, quantitative restrictions, fees etc. are to be abolished or phased out as completely as possible – save for any exceptions that may be made. Sectors that are explicitly under negotiation include, in particular, agriculture, automobiles, chemicals, pharmaceuticals and medical technology, energy and raw materials. This means not only scrapping the remaining tariffs, which are still quite substantial in some sectors, but also, for example, harmonizing regulations on origin and designations of origin, such as certificates of origin. In the energy and raw materials sector, export restrictions are also to be abolished, price regulation is to be reduced and negotiations are to take place on

2 The version leaked before the start of the negotiations also included sections on the automobile sector, chemicals and pharmaceuticals, as well as anti-trust and mergers, government influence and subsidies. http://www.iatp.org/files/TPC-TTIP-non-Papers-for-1st-Round-Negotiatons-June20-2013.pdf

issues concerning access to infrastructure networks.[3] Moreover, in line with WTO rules, the agreement is to include clauses on anti-dumping and compensatory measures. But at the same time, there is also to be a safeguard clause in case of serious damage due to an over-rapid increase in imports and exceptions are to be decided under Articles XX and XXI of the GATT.

As for *services*, in accordance with Article V of the GATS, regardless of the sectors and modes of delivery concerned, the highest degree of liberalization in each respect is to be adopted and remaining barriers are to be dismantled. In addition, the parties are to commit to transparency, impartiality, lawful authorization procedures and the national treatment principle and are to facilitate mutual recognition of professional qualifications. Up for negotiation are not only sectors such as communications and transport, but also, for instance, financial, health and care services. Although exemption provisions in line with Articles XIV and XIV bis of the GATS are not ruled out, uncertainties about terms or definitions and competing interests mean that the possible negotiating outcomes and their consequences are difficult to predict. For example, national entry and residence regulations are supposed to remain applicable, provided that they do not run counter to the aims of the agreement, and regulations by the EU and its Member States on conditions of work and employment are also to stay in force. But just how reliably or consistently such reservations will ultimately be pursued or applied is still an open question. The same goes for the definition of services supplied in the exercise of governmental authority, under GATS Art. I.3, or the provisional exemption of audiovisual services. In this respect, the Commission emphasizes that, in principle, no field is to be treated a priori as an exception, and the explicit swing towards a negative list approach (a list of explicitly exempted fields), at least in the case of public services, highlights the Commission's preference for liberalization. A more or less reliable assessment of the Commission's negotiating strategy is made all the more difficult by the TTIP's parameters, which differ from those of other recent agreements. In the agreement with Korea (KOREU), it was mainly the opening of the *Korean* service and procurement market that took centre stage. In return, the Commission was prepared to open up the European automotive market bilaterally. In the negotiations with Canada (CETA), the Commission for the first time had exclusive negotiating competence for the field of investments, and it switched from a positive list approach to a negative list one. In the negotiations with the US, a further element makes any prognosis more difficult – the particular importance of bilateral trade and investment relations, a similar level of development and, last but not least, development-relevant complementary specializations or trade asymmetries (services v. industrial goods, public procurement).

Finally, as regards *public procurement,* in line with the WTO's revised Government Procurement Agreement (GPA), mutual market access to public provision is to be expanded at all levels. Foreign bidders are to be put on an equal footing with local ones and barriers to access, such as local content clauses, production requirements or exemption rules, are to be dismantled. Here, one important point for

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[3] From the sector-specific provisions, it is already clear that where market access is concerned, tariff and non-tariff regulations, standards and competition regulations overlap in various ways. So negotiations are also underway about which fields or issues should be dealt with in the suprasectoral *horizontal* chapters and which in sector-specific annexes (more flexible and focused). Moreover, particularly on the EU Commission's side, various aims overlie each other. As well as protective or regulatory interests, which are being articulated mainly at the nation state level, the Commission is pursuing the competing aim of market opening – together, as described above, with strategies to increase competitiveness, for example by establishing bilateral or multilateral standards that are intended to give European firms a "first mover" advantage.

negotiation will no doubt be the reduction of thresholds for public tenders – towards EU-standards - as it was the case in the negotiations with Canada. In this respect, the Commission specifically cites the construction industry, IT services (such as cloud-based services), transport and rail traffic, but at the same time it declares that the aim is not a positive list (a list of specified fields for further liberalization) but a *negative* list (a list of explicitly exempted fields). Regarding the US, where public procurement is considerably more closed to foreign bidders, high priority is given to opening up, for instance by means of catch-all clauses, those fields that have so not been covered by either the Government Procurement Agreement (GPA) or bilateral agreements (e.g. those subject to "Buy American" preference programmes). To boost the effectiveness of the agreements, there are also to be linkages (so far unspecified) between the chapters on procurement, investment and services.

1.3.2. Regulations and Non-tariff Barriers

If economic estimates are to be believed, the non-tariff trade barriers and regulations are equivalent to tariff rates of 10% to 70% (cf. for instance Fontagné/Gourdon/Jean 2013: 8). The ifo-BMWi study even puts the figure at 155% for US imports into Germany (Felbermayr et al. 2013: 89). In principle, i.e. "horizontally" across all sectors, the agreement is therefore supposed to dismantle "unnecessary" regulations and barriers to trade and investment, and/or to achieve efficient regulation through greater compatibility, harmonization or mutual recognition, and where necessary to deepen this by means of sector-specific provisions. However, according to the Commission, the right to regulate on health care, public safety, social and environmental standards and cultural diversity is to remain, provided that the aims and measures are regarded as "appropriate" or "legitimate".

Particularly for *sanitary* and *phytosanitary measures* and *technical regulations,* the line of the relevant WTO agreements is to be followed as regards greater transparency and convergence, forms of cooperation and possibilities for the recognition of equivalent or compliant procedures. The right to take unilateral protective measures is, particularly in the absence of sufficient scientific evidence[4], to be restricted to the protection of life and health.

Finally, the agreement is to provide for additional liberalization, harmonization and bans on the creation of new non-tariff barriers in specific, jointly *agreed goods and services sectors* (sectoral provisions). These are to include, but not be limited to, the automotive industry, the chemical, pharmaceutical and health industry, information and communications technologies, and financial services.

[4] However, the Commission's interpretation (cf. EC 2000) can also be seen as paving the way for the abandonment of the precautionary principle. This principle is rooted in (democratically) justified doubts about the reliability of existing scientific proofs (for instance, due to the possibility of long incubation periods or to methods that have not yet been sufficiently developed). If, however, the applicability of the precautionary principle is made dependent on the (scientific?) judgement of the existing scientific evidence as to its sufficiency or otherwise, then the principle itself is being subjected to scientific criteria and the burden of proof is reversed. As its name implies, the precautionary principle urges caution and reflects doubts, for whatever reason, about existing scientific proofs. So its basis lies beyond science. If the applicability of the principle were made subject to a *scientific* assessment of the available scientific evidence, this would lead to an absurdity. Democratic assessment would then become a tautology and all that remained would be power-driven or interest-driven assessment.

1.3.3. Rules and Investment Protection

Building on the Agreement on *Trade-Related Aspects of Intellectual Property Rights* (TRIPS), *intellectual property rights,* and particularly the protection of European designations of origin (e.g. Cognac, specific sorts of cheese, or "Schwarzwälder Schinken"), are to be strengthened (but according to the Commission, this will not be a made-over repeat of controversial aspects of the failed Anti-Counterfeiting Trade Agreement [ACTA]).

On investment protection, for which the Commission has had sole competence since the 2009 Lisbon Treaty took effect, the mandate goes beyond the report of the High Level Working Group on Jobs and Growth, although definitive provisions are to depend on negotiations with the Member States and on the quality of the agreements. The maximum amount of liberalization and protection achieved so far is also to be laid down for fields in which competence is shared between the EU Commission and the Member States, such as portfolio investments. Standards for the treatment of foreign bidders are, in particular, to abide by the principles of national and most-favoured-nation treatments and are to rule out "unreasonable", arbitrary or discriminatory types of treatment. In addition to issues of security, investment protection is to extend to forms of direct and indirect expropriation, for which it should include "adequate" compensation rights, as well as to unimpeded flows of capital. Investment protection, which would be binding at all levels of state governance, is be ensured through an independent, comprehensive *investor-to-state* dispute settlement system, as well as *state-to-state* arbitration and an *umbrella clause*. The *investor-to-state* dispute settlement system, in particular, is to protect enterprises against "unjustified" claims (see the contribution of Eberhardt in this volume).

In addition, the agreement is to contain *competition policy provisions* on state aid, monopolies, state enterprises and other exclusive benefits, liberalization in the field of *raw materials and energy,* trade-related aspects of *small and medium-size enterprises, transparency rules* and full-scale liberalization (including a standstill clause – i.e. a ban on any further regulation) *of payments and capital movements,* except in case of grave monetary or currency policy dangers or tax-relevant aspects. To minimize state influence on competition, the forms of state influence or of favourable treatment of individual firms, sectors or regions are to be broadly defined. It will be difficult to evade such categorization – or else the legitimate exceptions will be tightly defined. State enterprises or those granted favourable treatment are to be obliged, beyond the tasks concerned here, to adopt a commercial orientation, and cross-financing in non-monopolistic markets is to be prohibited (similarly to GATS Art. VIII). Finally, transparency rules for subsidies, going beyond the existing WTO regulations, are intended to have a demonstration effect on other countries and speed up progress on equivalent global regulations.

1.3.4. Environmental and Social Standards

Social and environmental standards are to be promoted through the application of internationally recognized norms, including the core ILO labour standards, an accompanying *Sustainability Impact Assessment* (SIA), and provisions for monitoring the implementation of these standards. Civil society actors are to be involved in this, and complaints procedures are to be established. For inclusion in the chapter on sustainable development, the Commission proposes the 1998 ILO *Declaration on Fundamental Rights and Principles at Work*, as well as the 2006 *Declaration on Social Justice for a Fair*

Globalization and trade-related elements of the *Decent Work* Agenda. But apart from references to internationally recognized standards, voluntary initiatives or *corporate social responsibility* practices, the proposals on implementation and monitoring are still not very concrete. The involvement of those concerned and of civil society actors is mostly restricted to the rights to be informed and to be heard. There is no mention of any clearly defined scope for influence or sanctions.

Finally, to implement the regulatory aspects of the agreement (on SPS and TBT, for instance), the Commission proposes an institutional framework that should include bilateral consultation processes on regulatory initiatives, simplified procedures for sectoral extensions (without national ratification processes), and institutionalized bodies such as sectoral working groups. These groups would, for example, oversee the implementation of the regulatory agreements, verify sectoral extensions, and circulate proposals for further regulatory alignments and cooperation initiatives.

1.4. Conflicting Negotiating Aims and Possible Negotiating Outcomes

1.4.1. Possible Points of Contention between the EU and the US

Despite the interest shown by both sides in reaching an agreement, and the bilaterally developed proposals from the High Level Working Group, neither the success of the negotiations nor their results are foregone conclusions. On the contrary, the particular importance of the trade and investment relations between the US and the EU, the political dynamics during the negotiations (e.g. elections) and the far-reaching objectives, which go beyond those of previous agreements, make an assessment all the more difficult. Moreover, as the negotiations are not public, only sparse, mostly well-controlled information about their progress reaches the outside world. So any evaluation of possible blockages and disagreements within the negotiations can be based only on insights gained from other agreements and background information on the negotiating topics. In addition to obvious regulatory differences, pointers for this may include bilateral or multilateral agreements that are recent or still under negotiation, such as the agreements with Korea (KORUS, KOREU), the recently concluded agreement between the EU and Canada (CETA) or the plurilateral Trade in Services Agreement (TISA)[5], which is still being negotiated, as well as recent or current WTO disputes and, finally, the positions and civil society issues expressed on the fringes of the negotiations. Although it cannot claim to be complete, the following analysis will discuss possible points of contention that may influence the course of the negotiations (cf. inter alia Schott/Cimino 2013; Johnson/Schott 2013; Gerstetter et al. 2013; Rostowka 2013):

The *agricultural sector* is one of the manifestly contentious issues. Not only have the tariffs in this sector remained above-average, the "production models" are also very different on either side, and each has its own practices and regulations. US agriculture is characterized by big farms with an average usable area of 447 hectares (2007, MacDonald et al. 2013: iii), whereas the average holding in Germany is about 56 hectares – and in Bavaria, just 32 hectares (2010; Statistische Ämter 2011, pp. 10-11). The production methods are correspondingly different, and include the widespread use of genetically modified organisms (GMOs) in the US. Nor are the achievable economies of scale the same. In addition, the regulatory

[5] This is, of course, made more difficult by the fact that neither the results of the TISA negotiations nor those of the EU-Canada agreement CETA have so far been made public.

interests are very different as regards production methods (e.g. the use of hormones and chemicals), especially as regards sanitary and phytosanitary regulations, on which the US wishes to negotiate in connection with agriculture. The European side, on the other hand, would like stronger protection for designations of origin and the regionalization of export permits (for instance, in case of regional disease outbreaks). Another critical aspect is subsidies, some of which are high. As subsidy payments also affect other countries' exporters, they are not usually negotiated within the framework of bilateral agreements. What may be envisaged, however, is the negotiation of compensatory payments to the exporters. Just how serious a problem the agricultural sector may become for the negotiations cannot yet be foreseen, especially as the opposition from farmers and civil society is considerable, particularly in Europe. However, the multiplicity of problematic issues does also provide opportunities for compromise. Indeed, the most problematic aspects could possibly be set aside or negotiated separately.

Also at issue is *sea and land transport*. Both of these transport modes are relatively closed markets in the US, due to national regulation (e.g. the *Jones Act*), and among those opposed to opening them up is the US trade union confederation AFL-CIO (2013). While the EU would like to negotiate on these sectors within the framework of the TTIP, the US side points explicitly to the *Air Transport Agreement* that already exists between the EU and the US.

It is not yet clear whether the possible inclusion of the *financial sector* will turn into a stumbling block for the negotiations. While the financial industry is massively in favour of inclusion, it faces opposition from politicians and civil society actors. On the European side, the Commission clearly supports the inclusion of the financial sector, but it has to bear in mind that, if the negotiations were successfully concluded, the financial sector might be one of the aspects that drew criticism from the European Parliament or Member States. On the other side of the Atlantic, opinion is even more sharply divided on this. The Office of the U.S. Trade Representative (USTR), which is conducting the negotiations, also favours inclusion of the financial sector, but others, including the U.S. Department of the Treasury and the supervisory and regulatory authorities, object that this could weaken the reforms developed in response to the crisis (mainly the Dodd-Frank Act). These actors would prefer to negotiate financial sector regulation issues in other forums, and not as part of the TTIP (cf. Johnson/Schott 2013).

Especially in relation to agriculture and some aspects of health protection, there is a whole series of contentious issues about *sanitary and phytosanitary rules.* Behind such hotly debated items as "gene food" and "chlorine chickens", there are indeed fundamental differences of conception about approval or labelling requirements for certain processes or products. While the European side prefers to apply the precautionary principle in cases where the scientific evidence for health safety is deemed insufficient, the US side insists on precedence for scientifically supported risk assessments. This is, for example, the basis of the "substantial equivalence"[6] principle applied to genetically manipulated food in the US, where there is no GM labelling requirement. However, given the powerful lobby in the US (including Monsanto), greater opening of the European market is likely to enjoy high priority, and the interest in labelling requirements, an interest that also exists to some extent in the US, could strengthen efforts to reach a

6 The substantial equivalence principle assumes that a newly developed foodstuff is just as safe as an existing one if it has the same composition, and therefore does not require any further safety tests.

compromise, while on the European side, the precautionary principle appears to be less important to the Commission than to other European actors or individual Member States (cf. Bartl/Fahey 2014).

Each side also has different regulatory environments for the *chemical and pharmaceutical industry* and for the authorization of *medical technology products*. For example, the authorization and registration requirements placed on the chemical industry in Europe by REACH (Registration, Evaluation, Authorization and Restriction of Chemicals) are markedly tighter than those in the corresponding US provisions (Toxic Substances Control Act, TSCA). There are also differences in, for instance, the requirements to divulge pharmaceutical product test data or the authorization procedures for medical technology products.

On *raw materials and energy,* not only do practices differ regarding the authorization of specific processes, views also diverge on how various issues should be tackled in any agreement. For example, the EU Commission would like to deal separately with issues about setting energy prices, breaking up monopolies or promoting fossil fuels (e.g. fracking), whereas the US side wishes to tackle them as part of the overall "horizontal" chapters. Depending on which view prevails, this could well influence the degree of specificity of the provisions and perhaps also the possibilities (even in future) for making exceptions or special arrangements.

As regards *protecting intellectual property rights* and *designations of origin,* it is mainly the latter issue that may cause problems. Unbridgeable differences about this already emerged during the TRIPS negotiations. But for the European side, protecting designations of origin is a high priority. Differences on other points are likely to be significantly smaller – for instance, on the duration of patent rights or third-party use of test data, as a means of delaying or preventing the possible introduction of generics or biosimilars. The US is more aggressive about, for example, criminalizing "Internet piracy", while the Commission may have learnt its lesson from the ACTA's failure to get through the European Parliament. Similarly, the discussions about the protection of private data, reinforced by the latest bugging scandals, are more likely to impinge on the talks from the outside than from within.

Now that the Commission has, for the first time, negotiated on an *investment chapter* in the CETA agreement, which comes close to the Americans' model investment agreement, it is also unlikely that any unbridgeable differences will arise about investment protection. However, differences do still exist about the scope to be given to the word *investment.* The Commission does not want to extend investment protection to the market entry (*pre-establishment*) phase, whereas the US insists on extending protection to the whole investment cycle (*life-cycle of the investment*). Moreover, the European side, in line with the Commission's mandate, wishes to reserve the right to introduce safeguard provisions if needed, or to make its acceptance of an investment chapter dependent on that chapter's being balanced. Finally, investment protection, particularly a possible *Investor-State-Dispute Settlement* (ISDS) provision, may well also be one of the critical points when seeking European Parliament approval. Probably less important in that regard would be the US practice of linking investment protection to social and environmental standards, as the EU standards are equally high or in some respects higher and the risk of the Europeans' gaining a competitive advantage through lower standards is comparatively small.

Agreement on *public procurement* may be more difficult to achieve. Estimates assume that the US procurement market, particularly due to "Buy American" and similar provisions, is significantly more "closed" than the European one, and that, for example, only one-third of American procurement, as against 90% of that in the EU, is covered by the plurilateral Government Procurement Agreement (GPA) (Fontagné/Gourdon/Jean 2013, p. 5). Consequently, opening up procurement is a high priority for European firms and also for the Commission. However, the regulatory means and competences in this field are spread across different levels of American government (*federal* and *subfederal*) and have not been fully clarified. Thus, individual US states, such as *Maine*, regularly insist on exceptional provisions in bilateral and multilateral trade agreements (Maine 2013). So the US negotiators, contrary to practice in other fields, have expressed scepticism about the negative list approach that the Commission has been taking on this issue. Not least because of the considerable asymmetry and the different distribution of potential gains and losses in case of deregulation, there is also considerable resistance to this within US civil society. On the other hand, the US side would like to subject EU structural funding to closer examination, and this could also provoke stronger resistance at regional and local level in the EU.

On *competition policy,* the issue of subsidies – among other things, to state-owned (SOE) or state-privileged enterprises (SER), as well as agriculture - could complicate the negotiations. In this connection, the differences between the "state action doctrine"[7] on the US side and the exceptions under Article 106 of the TFEU on the European side ought to be clarified. For instance, the subsidy dispute that has been going on for years now between Airbus and Boeing at the World Trade Organization will not have a very positive impact on the negotiations.

Finally, there are also some differences in *social and labour standards*. Some of these are certainly higher in Europe, which is why American trade unions are hoping or even insisting that any agreement should foster improvements in these standards (Josling/Crombez 2013). However, experience with trade agreements so far does not exactly encourage hopes that they can be used as a lever for raising standards. True, the US did build dispute arbitration mechanisms, including on social standards, into past agreements (e.g. KORUS), whereas the EU did not (e.g. KOREU). However, these mechanisms are generally aimed at breaches of standards by the trading partner, not in the homeland. And the US is unlikely to put much effort into making social standards enforceable under an agreement with the EU, if – as with other agreements under the TTIP - these may then come to be regarded as a model for the development of the world trade regime.

On the other hand, standards or interests in the fields of *environmental and health protection* may well play a more important role. While the Commission has increasingly subordinated these aims to those of opening up markets and strengthening competition (cf. De Ville 2013b), they do still play a stronger part in European civil society and national policies, and they also carry influence in the European Parliament. It may therefore be supposed that the Commission will not be able to give up European standards completely or unconditionally. Contentious points here may include, as well as the already mentioned sanitary and phytosanitary rules or standards in the chemical industry, some (potentially) environmentally damaging processes for extracting raw materials or energy, such as fracking, or emissions regulations

[7] The legislator's right to empower public bodies to restrict competition.

such as, in particular, the European air traffic emissions trading, which was introduced in connection with the Kyoto Protocol and has already led to cases at the European Court of Justice.

This account of just a few of the contentious points up for negotiation between the US and the EU makes it clear that there will be many hurdles along the way to an agreement, but also many opportunities for compromises or trade-offs. But given the slow progress of previous attempts at transatlantic regulatory dialogue, it may be supposed that far more differences exist within the sector-specific or field-specific regulations that have not (yet) been politicized but which may nonetheless be relevant to competition. It is quite in keeping with the functional logic of a comprehensive agreement to separate such differences out from the often rather inflexible and technocratic discussions between sectoral experts and make them available "across the board" – in other words, as elements of a negotiating strategy. In this way, objects of regulation are politicized, so that it is no longer possible, from the dynamics of the negotiation, to make a quantitative prediction of the outcome on the basis of functional criteria.

The following discussion of possible negotiating outcomes and their consequences should be seen in this light, i.e. that precisely in relation to non-tariff regulations, a more or less horizontal or linear reduction in trade restrictions - say by 25%, although even the underlying quantifications are very uncertain - is highly improbable. Far more likely are sectorally asymmetrical negotiating outcomes, which will strongly depend on the political dynamics and the weight of the various (economic) interests.

1.4.2. Possible Negotiating Outcomes

As no (interim) results are available so far, and neither the negotiating details nor the real negotiating strategies are being made public, any assessment of the consequences that might flow from the negotiations will be hypothetical. Such assessments, not least because they could themselves feed back into the negotiations, will also entail considerable uncertainty. Nonetheless, in what follows, the probability of various negotiating outcomes will first of all be estimated qualitatively, on the basis of the scenarios in the economic studies and the qualitative evaluation of difficulties in specific areas of the negotiations. However, as this cannot lead to either precisely identifiable outcomes or a comprehensive estimation of the consequences, selected fields will then be examined in greater depth.

Due to the strategy adopted by the EU Commission, and other supporters of an agreement, of justifying it in terms of the expected gains in economic prosperity, a look at the corresponding studies is essential. On closer examination, the figures, which are often quoted out of context, will need to be relativized. Also, the models and methods employed will raise questions as to the validity of the results. For the most part, *Computable General Equilibrium* (CGE) models are used, and these are based on assumptions and methods that are by no means uncontroversial from a scientific point of view (see Raza et al. in this volume).

As the outcomes of the negotiations will be largely determined by their conduct, plus the wider social arguments around the TTIP, it also worth taking a look at how the negotiations are being run. The secrecy surrounding them and the unevenly distributed means of influencing them are not just regrettable side issues. They are a functional core element of the negotiating and implementation strategy and are thus highly relevant to the outcomes.

Critical questions also need to be asked about investment protection, particularly the intention so far to include a special right of complaint for corporations. On the one hand, incorporating this into the agreement seems to be less a matter of the negotiating partners' willingness to reach a deal and more a question of social and political problematization. On the other, it would entail political and economic redistribution effects whose influence on other regulatory fields, such as public procurement or labour standards, is virtually impossible to predict. So these impacts, too, would have to be built into the prosperity calculations.

Finally, the possible effects on specific fields will be investigated. Among the areas that could be structurally altered by the agreement, possibly with considerable social consequences, are public procurement and various services, including public ones. The TTIP could adversely affect the possibilities for democratic influence on local or regional development, the quality of public supply services and the quality of labour conditions and employment relationships.

1.4.3. The Probability of Various Scenarios

At first sight, a very comprehensive agreement ("maximum agreement") affecting central elements of services and agriculture seems less likely than a minimum agreement, which would simply abolish the remaining tariffs on goods. This is because a comprehensive agreement would not only make the negotiations themselves more complex, it could well also increase the problematization around them and possibly strengthen resistance in the political sphere. This in turn would lower the prospects for any significant progress on liberalization, which major business organizations are interested in achieving. Moreover, after so publicly beating the drum for an end to trade barriers, the participating governments and the EU Commission want some substantial negotiating outcomes to show for it all.

So if the negotiators stubbornly cling to (overly) "ambitious" aims, a complete failure of the talks cannot be ruled out. However, if in the meantime the agreement between the EU and Canada were ratified and the negotiations between the US and the Pacific region were successfully concluded, the failure of the transatlantic negotiations would be an embarrassment. Therefore, when assessing the possible negotiating outcomes and their consequences, it is useful not only to contrast a "minimum" agreement with a "maximum" one, but also to envisage an intermediate scenario under which many sectors would be covered, but at different depths of liberalization.

The *minimum* agreement scenario entails a far-reaching elimination of the remaining tariffs, but in other respects, such as services, public procurement or standards and regulations, it would not go much beyond existing agreements such as the GATS, GPA, SPS or TBT. As regards tariffs, the recently negotiated agreement with Canada may be taken as a pointer. For instance, under that agreement, 93.5% of all tariffs in the EU agricultural sector are to be completely dismantled, for the most part as soon as the agreement comes into force or in some cases after a transition period of up to 7 years. Additionally, in contentious areas such as beef, pig meat and maize, the tariff-free import quotas are to be raised slightly. For industrial goods, 99.3% of all tariffs are to be abolished when the agreement comes into force, rising to 100% after a seven-year transition period (cf. GC 2013; EC 2013h). Such a negotiating outcome would be roughly equivalent to the "tariffs-only" scenarios discussed in Chapter 4.1, and will not be examined further here, in view of its low impact on the fields under consideration.

However, an agreement purely on tariffs does not seem very likely, in view of the disproportionate extent to which the agricultural sector would be affected. Given the inequality of the US and European agricultural production models, as described above, and the linkage to the contentious sanitary and phytosanitary issues, the European side would probably not be keen to conclude such an agreement unless it received compensation in other respects, such as public procurement. Even less so as the end effect would probably be just to shift the problem from tariffs to compensatory subsidies.

At the other end of the scale, the *maximum* scenario corresponds to the "ambitious" scenarios described below. In addition to the dismantling of tariffs, they imply far-reaching liberalization in all the fields under negotiation, i.e. (public) services, public procurement, regulations and standards, competition law etc., as well as extensive investment protection, including investor-state dispute settlement and increased protection for intellectual property rights. However, such a far-reaching agreement is not thought to be very likely. But the fields for which stronger liberalization will be negotiated are in no way preordained, any more than those in which liberalization would be less thoroughgoing. So this scenario can be seen as a comprehensive set of possible building blocks for various compromises. That being the case, all of the consequences discussed below would be possible under a scenario of this kind.

In the present study, however, an *intermediate* scenario is considered to be the most probable. Its breadth of scope is similar, but the depth of liberalization would vary from one field to another and there would be specific exceptions such as, possibly, for financial market regulations or water supply. Arguments for such a middle-of-the-road solution, as opposed to the minimum scenario, include the lofty economic and political ambitions on both sides, the WTO's minimum condition that bilateral agreements should contain more comprehensive liberalization than the corresponding multilateral agreements, and not least the orientation towards parallel agreements like CETA, the TPP or the negotiations on a plurilateral agreement on services (TISA). On the other hand, a middle course is also more probable than the maximum scenario, as the many points of contention make it likely that trade-offs or concessions (corresponding to two-level or multi-level bargaining) will take place between the negotiating partners. These concessions could then be sold as successes to the opposition forces back home (e.g. the EU parliament, national or local government, environmental organizations and trade unions).

Recent agreements or negotiations may point to the kind of negotiating outcomes that may be expected, but it is just as likely that the peculiarities of the bilateral relationship between the US and the EU will create a very specific negotiating dynamic. Moreover, on the European side, the Commission's strategy is difficult to assess. It is markedly more functional or technocratic than tends to be the case for nation states' representatives, who are more directly subject to social discourse and power play. The Commission does not represent any national state regulatory interests. On the contrary, its interest is in dismantling national state regulation, both in external trade policy and domestically – i.e. as regards the European internal market.[8] The balance that nation states typically wish to strike between opening up markets and protecting interests back home is nowhere to be seen in the Commission's case. In practice, this means that it is by no means clear what negotiating strategy value the Commission places on sector-

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[8] A particularly clear example of this is the treatment of audiovisual services. These have been only provisionally taken out of the negotiations, after particular pressure from France. The Commission, on the other hand, has made it clear that it does not want to exclude any field *a priori* from the negotiations (vgl. Rostowska 2013).

specific protective provisions or on the precautionary principle as applied to health or environmental protection. In the final analysis, the Commission is not independent of the approval of the European Parliament and of the Member States in the European Council. However, it is the Commission that controls the information available about the negotiations and prepares the "official" expertise, i.e. the interpretations. So it is in a position to exert considerable influence on the actors who control it. Later on, individual governments will find it difficult to ditch the whole negotiated package just because some of their interests have been harmed.

Other pointers can be found in the assessments made by interested stakeholders. A survey to that effect was conducted in the spring of 2013 by the *Atlantic Council of the United States* and the *Bertelsmann Foundation,* who may be regarded as supporters of a transatlantic agreement. It found that some 90% of those interviewed expected an agreement to be concluded, but a small majority (55%) thought the agreement would remain rather modest. Only 37% believed in a comprehensive agreement (Barker/Workman 2013). Among the agreement provisions that the interviewees regarded as the most important but also the most difficult to achieve were a clear regulatory convergence across many sectors, including industrial products, and agreements on sanitary and phytosanitary rules. They also regarded agreements on genetically manipulated organisms and agriculture, data protection issues, regulations on financial markets or pharmaceuticals, and public procurement as difficult, but less important. Seen as even less significant, but nonetheless difficult, were agreements on designations of origin, environmental standards, investment facilitation or labour standards. On the other hand, further dismantling of tariffs and stronger protection of intellectual property rights were seen as easier to attain, but nevertheless important. Finally, also regarded as rather easier to achieve, but somewhat less significant, were joint standards vis-à-vis third countries, for instance on subsidies and issues surrounding the local share of total value added, and the liberalization of energy exports (ibid.).

In line with the differentiated assessments, Barker and Workman believe a scenario is possible that, while ambitious, would nonetheless either leave out some contentious areas or aim at only limited liberalization of them. Examples might be genetically engineered organisms and agriculture, public procurement rules or environmental standards. On the other hand, if the negotiations did remain strongly focused on the critical areas, a failure similar to that of the WTO's Doha Round could not be ruled out. Then again, in our opinion, the conclusion of a comprehensive agreement that included the contentious areas would require a high degree of support from political leaderships on the sides of the US, the European Commission and influential Member States, as well as from the US Congress and the European Parliament.

Recent agreements, although comparable only to a certain extent, do provide some further indications. Apart from the abovementioned reduction of goods tariffs, the agreement with Canada (CETA; cf. GC 2013) contained few far-reaching measures in the regulatory sphere. On *sanitary and phytosanitary rules,* for instance, the CETA does not go much further than existing agreements. Farther-reaching agreements on this and other regulatory issues, such as technical barriers to trade, are often restricted to establishing forms of consultation and cooperation. For *public procurement,* the threshold values for tenders at the various levels were indeed by and large adjusted to the sums applied in Europe (e.g. €400,000 for public supply services or €200,000 for local and regional contracts, for instance from hospitals, schools and

universities). However, exceptions will continue to apply (ports and airports, broadcasting, postal services, ship-building) and it will still be possible to set social or environmental criteria or, beneath the threshold values, to give preference to domestic firms. In addition, specific special or exceptional provisions were agreed for individual Canadian provinces.

As regards *services,* on the one hand the agreement with Canada is to liberalize important fields, such as financial services (including the availability of the investor-state dispute settlement process to investors in the financial sector), energy or telecommunications. And future liberalizations are to be made irreversible. On the other hand, health services, state education, the cultural sphere and other social services are to be exempted. An innovation in the European Union's treaty is the inclusion of a chapter on *investment protection,* which also contains an investor-state dispute settlement procedure. However, this procedure is to be limited to the phase after the activation of the investment (*post-establishment*), which is also what the Commission has set out to achieve in the negotiations with the US.

Compromises were also agreed on the protection of *designations of origin,* which the European side regards as important. In part, however, this protection extends only to designations in a specified language, not to translations of them. And for various composite designations of origin (e.g. "Gouda Holland") the protection does not apply to the use of individual components ("Gouda").

Finally, the CETA provisions on environmental and social standards may be seen as a template for a transatlantic agreement. Beyond the usual acknowledgements of international standards, such as the ILO's *Declaration on Fundamental Principles and Rights at Work,* the CETA does contain the beginnings of an arbitration mechanism. However, this is limited to consultative procedures and the right to formulate recommendations. No provision is made for "hard" sanctions (e.g. trade sanctions), beyond the domestic enforcement of existing national laws.

In the final analysis, a comprehensive agreement is being made more difficult not only by political resistance in critical fields but also by the complexity of the negotiating items themselves and the differing institutional models and competences. For example, regulatory authorities are responsible to the legislature and, correspondingly, their willingness to hand over competences is limited (Ahearn 2009; Muscat 2013). So in many fields of regulation, it may be expected that the negotiations on the agreement will not in themselves lead to concrete harmonization provisions or rules for mutual recognition, but rather that institutional forms of cooperation will be agreed, aimed at later harmonization. It is by no means certain how far these forms of cooperation will then still enjoy the current political support, and thus to what extent they will be more successful than the various approaches taken to regulatory dialogue so far. In view of that, expectations as to the economic benefits of the agreement must also be relativized.

1.5. Possible consequences of the TTIP

1.5.1. Regulatory and Democratic Risks of the Negotiating Process

As the discussion of the prosperity calculations shows, the gains to be expected from a transatlantic agreement are by no means as great as they may at first seem (see Raza et al. in this volume). And even these expectations are uncertain. So questions about the dangers, the possible losses and the balance

between opportunities and risks now come to the fore. Here, some of the basic political and regulatory risks of the agreement will first be discussed. These concern not only the possible outcomes, but also the preparation, design and character of the negotiations. In various respects, they suggest a functional, none too democratic mentality, and this seems to justify fears that the negotiating aims and the outcomes being sought will also have unequally shared consequences.

One aspect that has already been much criticized is the socially very unequal distribution of opportunities to influence the negotiations. Big corporations and those representing their interests have been intensively involved in the transatlantic dialogue for many years now, and in the consultative rounds ahead of the TTIP negotiations, their share of 80% or more meant that they were clearly overrepresented in relation to other civil society and state participants (cf. above and CEO 2013). These imbalances are not solely due to the impact that an agreement would have on enterprises. They also reflect what is often privileged access to representatives of the Commission, for instance through existing contacts or shared patterns of perception, and a biased appreciation and use of expertise (cf. Bartl/Fahey 2014). In the position papers that became known before the first negotiating round, the Commission explicitly confirms this impression, in connection with regulatory issues in the chemical and pharmaceutical industry:

> *"The purpose of this paper is to outline the main elements of a possible approach under TTIP to promote regulatory convergence and recognition in the chemicals sector. These elements build on the ideas put forward jointly by Chemicals Industry Associations of the EU and US. ...*
>
> *The purpose of this paper is to present some possible elements for a TTIP annex on pharmaceutical products. It is based on ideas put forward by EU and US industry and builds on existing cooperation between EU and US regulators in this area. It is anticipated that stakeholders will continue to support the process and could play an active role towards the implementation of some of the identified objectives."*[9]

In view of the fact that negotiations on a comprehensive agreement like the TTIP concern a broad range of European laws, rules and standards that are part of the *acquis communautaire*, it may well be asked who decides the negotiating agenda and which values and interests it represents (cf. Bartl/Fahey 2014). A first insight into the workings of these negotiations was provided back in the preparatory stages, by the *High Level Working Group on Jobs and Growth* (HLWG). Despite repeated requests from *Corporate Europe Observatory,* the Commission was not even prepared to reveal the composition of this group. After the US side made the group's composition known, it became apparent that, for example, no experts on either environmental issues or social aspects were involved on the European side.[10]

The specific aims of the negotiations and the attitude to regulation, particularly on the Commission's part, are further expressed in repeated declarations of the intent to dismantle and prevent "unnecessary" regulations. This indicates a regulatory approach based on a commitment to free trade, thus favouring liberalization while the relative importance of other, possibly competing, aims is downgraded. And this one-sidedness has potentially far-reaching consequences. Formulated as an overarching objective in the horizontal chapter, it applies in principle to all the negotiating topics and at the same time it guides the institutionalized negotiating or working groups foreseen in the "institutional provisions". These groups

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[9] However, these passages occur only in the version that became known beforehand (http://www.iatp.org/files/TPC-TTIP-non-Papers-for-1st-Round-Negotiatons-June20-2013.pdf). The position papers later made public by the Commission do not contain the corresponding sections.

[10] cf. http://corporateeurope.org/trade/2013/06/who-scripting-eu-us-trade-deal

overwhelmingly consist of a mixture of corporate expertise and/or corporate interests, and experts on regulation. So any corrective positions are, *a priori,* normatively subordinated and, as far as interests and cognitive positions are concerned, are underrepresented. Moreover, as a "living agreement", the TTIP is to include, within the framework of an *inbuilt agenda,* a general mandate for further consultation processes and liberalization proposals. So the door is being left open for further expansions of the agreement's scope even after the negotiations have been concluded – at which time it will presumably attract less public attention. This mandate includes the submissions to, and negotiations in, other bodies that are part of the international trade regime (cf. Bartl/Fahey 2014).

Meanwhile, the possibilities for monitoring and correcting the process must be regarded as limited. The European Parliament does have rights to information and to a veto under Article 218 of the TFEU.[11] However, the effectiveness of these rights is limited. One factor here is that the negotiations are for the most part secret and documents are not accessible – or at best, they become available later on. The Commission confirmed this line in the run-up to the TTIP negotiations, and the European Court of Justice also, in connection with the ACTA negotiations, confirmed the right to keep information secret for reasons of negotiating strategy. Another is that the Commission provides not only (limited) information but also a substantial proportion of the expertise and assessments for the negotiations. Some it prepares itself, such as the Impact Assessment (EC 2013a). Others it commissions, such as the CEPR study. But these studies more or less reflect the Commission's position and, due to the Commission's exclusive knowledge, they essentially shape public discourse. The parliament can only vote for or against the finished package after the negotiations are over, or "after the fact" (Bartl/Fahey 2014), and this may increase its readiness to accept some critical individual aspects.

In such an extensive project, the Commission's one-sided approach, combined with the limited possibilities for corrections and monitoring, poses considerable risks to opportunities for democratic participation and the pursuit of alternative sets of values. The liberalizing intentions pursued in the TTIP negotiations promote privatization trends and generally put environmental and social standards on the line, as they are deemed to inhibit trade. Taken together with the principles that are foreseen at least for individual fields, particularly the negative list approach, the fixing of the liberalization level achieved in each case and mechanisms for the mutual recognition of standards, this can trigger a competitive deregulation of standards that it will be very difficult to halt or reverse later on. A particularly critical area in this regard, namely a privatization of law through the investor-state dispute settlement mechanism, is discussed in detail by Eberhardt in this volume.

1.5.2. Possible Effects on Public Procurement

The public procurement field is particularly significant in terms of economic and employment policy. Through procurement, which accounts for almost 20% of the EU's GDP, the public purse can provide

[11] Whether the national parliaments of EU Member States would need to approve a TTIP agreement depends firstly on whether the agreement reached is a so-called "mixed agreement" or includes provisions that exceed the competences of the EU, i.e. that fall within the Member States' purview, and secondly on the relevant national provisions. Under German law, the Bundestag (first chamber of the federal parliament) and the Bundesrat (second chamber) must, in accordance with Art. 59 paragraph 2 subparagraph 1 of the Basic Law, approve a mixed agreement. Current assessments, for example by the federal government, assume that the TTIP is a mixed agreement.

economic and regional development stimuli, and via the tendering rules, it can exert influence on social, environmental or quality standards. Firms are attracted by the size of the public procurement market. So it may be assumed that access to the procurement market will be one of the major, hard-fought negotiating items.

In the TTIP negotiations, it is mainly the EU Commission that is calling for further opening of the public procurement market. Whereas about 90% (some €350bn's worth) of the European procurement market is open to external bidders, the same goes for only around 32% (about €180bn) of procurement in the US. In particular, the call is for a deregulation of what are known as the "Buy American" rules, which give preference to US suppliers. In return, the Commission seems to be prepared to bring the threshold values for tenders down to those applying within Europe, in a similar way to that agreed in the CETA. There might possibly be some reciprocal exceptions at the regional or local level (cf. CG 2013).

Whereas in the US, the trade unions, civil society groups and several federal states are strongly interested in preserving exceptions to liberalization in the case of public procurement, Europe's agenda is more about the detail of regulation, i.e. which fields might possibly be exempted and what should be the possibilities for regulation in the fields that are opened up. At present, the exceptions agreed in the CETA also seem quite likely candidates for TTIP exemptions (ports, airports, broadcasting, postal services and shipbuilding). The US does not wish to liberalize these areas either, mainly for reasons of sovereignty. As regards regional economic development and cohesion funds, which are not exempted in the CETA, the low volume of cross-border tendering inside Europe to date (less than 5%; Van den Abeele 2012: 5) suggests that, at least in the medium term, there will be no significant effects going beyond those of the existing level of liberalization in the European internal market.

Probably of more relevance is the intended forerunner effect in relation to other trade agreements and the WTO's *Agreement on Government Procurement* (GPA), as the procurement market is considerably more closed in other countries, particularly developing and threshold countries. If, by pointing to the TTIP, a significant opening of the procurement market can be pushed through in these countries, they risk losing a potentially important instrument of economic development.

Moreover, the possibilities or provisions for bringing environmental or social standards into public tendering are inadequate. For example, this is a shortcoming in the GPA, which does not include any references to social standards. So far, the proposals for reforming the relevant EU directives are also inadequate in this respect (Van den Abeele 2012). For one thing, the possibility of bringing in appropriate clauses ought not to be restricted. Also, specifications on, for instance, certain certification or labelling requirements should be regarded critically, not least in the field of social standards. The types of certification or *corporate social responsibility* declarations often preferred by business federations are for the most part insufficient, as they do not include trade union rights and generally lack reliable monitoring and verification procedures (cf. Beck 2013). So there needs to be an effort to ensure that any chapter on environmental and social standards is not tilted towards "alibi standards".

1.5.3. Sector-specific Consequences for Services

While it is not to be expected that the trade in services will, following liberalization, grow by anything like the share of services in the Gross National Product of the OECD countries, considerable increases

may nonetheless be anticipated. First, some parts of the trade in services, for instance in the financial sector, are characterized by globally oriented firms. Secondly, various services are more or less closely associated with goods production and the goods trade (e.g. transport and business services). In addition, there may conceivably be reciprocal effects, some of them deliberate, among the various regulatory regimes (GATS, EU services directive(s), TTIP), which could trigger further liberalization effects. Usually, bilateral and regional agreements are significantly broader in scope than multilateral ones, i.e. GATS, although they are associated to differing degrees with the various *modes* of provision. Usually, liberalization is taken further for Modes 1 (*cross-border trade*) und 2 (*consumption abroad*) than for Modes 3 (*commercial presence abroad*) and 4 (*movement of natural persons*). However, in fields such as distribution or transport for instance, liberalization is more far-reaching for Mode 4 (van der Marel 2013). Moreover, the liberalization measures set out in the EU services directive have not yet been fully implemented. So any agreements containing a level of liberalization roughly equivalent to that in the directive could promote stronger implementation of the directive's provisions, or even foster initiatives going beyond that. As discussed above, this could help to fulfil the Commission's intentions.

If, in addition, a *negative* list approach were to be agreed for the services field, then it cannot so far be ruled out that liberalization in the framework of the TTIP would move beyond the GATS exceptions for the public supply sector and also beyond the EU services directive (2006/123/EC), in which, for example, services in the fields of health, finance, transport and temporary agency work are exempted. The Commission favours a narrow interpretation of the exempted "non-economic services of general interest", and it regards other public utilities, such as water supply, education and healthcare as at least partly commercial and, to that extent, as furnishable by private bidders within a competitive environment. The exemption provisions for public utilities relate only to restrictions on the number of bidders, and not to any discrimination between domestic and foreign bidders (EC 2011). So it is quite conceivable that the Commission is pursuing farther-reaching liberalization intentions within the framework of the TTIP. Certainly, strict competition rules for public suppliers or publicly preferred suppliers (e.g. a ban on cross-financing or a requirement to adopt a commercial orientation) could contribute to a narrowing of the fields covered by exceptional provisions.

Finally, the simultaneous referencing of both international (GATS) and European definitions (Treaty on the Functioning of the European Union), as well as the swing from a positive list to a negative list approach, could help to bring about regulatory ambiguities, which would ultimately reduce the possibilities for the delivery or regulation of public services (cf. Krajewski 2011).

Unlike the EU Commission, which has so far kept rather quiet about the exceptions sought, the US side has been quite explicit about its reservations in some areas. As well as sea and air transport and postal services, the US wants the financial sector, in particular, to be kept out of the TTIP. The extent to which financial services will be brought into the negotiations seems to be one of the most uncertain factors so far. While the financial sector itself is clearly interested in being included, and it is suspected that US firms in both this sector and business services would derive competitive advantages from inclusion, the regulatory authorities have reservations about this and would prefer other negotiating arenas. Comprehensive inclusion of the financial sector could certainly have serious consequences for future regulation possibilities (e.g. transaction taxes, or restrictions on the transport of, and trade in, hazardous

products) and for financial stability. However, it is also conceivable that market access issues could be separated out from regulatory issues.

The European Commission is not alone in supporting liberalization (for instance, cf. Bieling/Deckwirth 2008). Interest and lobby groups are also taking part in the campaign for the TTIP, such as the Association of Germany Banks and the European Services Forum. Some of these have altogether privileged access to the Commission, and they have high hopes of what a comprehensive agreement would bring (cf. CEO 2013). However, the possible impacts in the services field do not depend solely on the liberalization measures agreed. Equally important are the existing volume of sector-specific trade, the height of the present barriers in each case, and the elasticity of the response to liberalization from the various channels and/or variables, such as direct investments or labour migration. The Ecorys study, for instance, estimates that the EU's current non-tariff barriers on services trade with the US are highest for business services, information and communication services, and financial and insurance services. In the fields of transport, personal and cultural services, and construction it finds lower-than-average barriers (CEPR 2013: 20).[12] Based on these estimates and the elasticities assumed, the CEPR expects the biggest absolute growth in exports from the US to Europe folllowing services liberalization to be in business services, financial services, and personal and communications services. Under an ambitious scenario, EU imports in these fields would grow by about three to six percentage points, while corresponding US exports to the EU would grow by roughly five to fourteen per cent (CEPR 2013: 64ff.). The direct effects of the bilateral trade in services are further relativized by the below 12 percent per cent share of imports from the US in EU-imports as a whole in 2010, although a little over 30% of these were services. So in terms of the nominal EU-GDP, imports from the US accounted for less than 0.02 per cent. Correspondingly, service imports' share of total service production is even smaller. Even if, as one ifo Institute scenario assumes, US exports were to grow by 10 and 20 per cent in certain fields, such as communications, financial services or business services, just the quantitative effect of possibly stronger competition would probably be small. However, the same would not apply to the longer-term regulatory effects of corresponding liberalization measures, which could, for instance, have an impact on the employment regime as a result of increased privatization or commercialization.

1.5.4. Employment and Labour Policy Risks

The discussion of the various areas points both to a clear relativization of the promised gains in prosperity and to wholly realistic losses or specific risks. First of all, clear growth in employment, income and wages is not very probable. And even if it did happen, it would not be noticeable for several years.

The scenarios' implicit assumptions about the labour market and the distribution dynamics are for the most part unrealistic (see Raza et al.in this volume). Given the strong increase over recent years in the prevalence of atypical, low-paid employment, the growing income inequalities, the continuing austerity policies and the decline in collective bargaining coverage, in the EU as well as in the U.S., it may just as well be expected that possible liberalization measures, outsourcing and deregulation will, particularly in

[12] In contrast, the ifo Institute study finds that the highest EU barriers against US imports are in the construction sector, maritime transport, insurance and financial services. But it also notes clear barriers to public services, at almost 30% (Felbermayr et al. 2013a, p. 45).

services but perhaps also in the agricultural sector, be used mainly to create atypical, low-paid employment. That in turn would have knock-on effects on general pay levels and "normal employment relationships". What is more, the adjustment and transition losses, and the employment transfers too, would be greater than the studies show. Against this backdrop, it may even be feared that deflationary trends could be fostered by the price cuts that are in some cases assumed.

However, to return to the services sector, quantitative estimates of impacts on employment or wage trends are very difficult to make. Even if the TTIP negotiations produced an extensive liberalization that went beyond previous agreements under GATS, it is debatable whether this would have clear effects on, for example, Modes 3 or 4, due to the volume of bilateral trade (cf. Kemekliene/Watt 2010). But in the medium to long term, the TTIP negotiations could, as part of a "forum shifting" strategy, contribute to the adoption of liberalization steps that would, through interaction with the GATS, the TISA negotiations and the liberalization of the European internal market, go hand in hand with noticeable changes (cf. Raza 2008). Given the employment policy significance of individual service sectors, even smaller impacts may be relevant in some fields. The fields that might be more strongly affected by the TTIP could include business services, financial services or information and communications services. In these areas, for example, cross-border supply under *Mode 1* (e.g. Internet or telephony) or direct investments (branches or subsidiaries) under *Mode 3* could lead to competition effects or displacement effects. Thus, the Ecorys study for instance estimates a tiny rise of about 0.1% in the financial sector's production within the EU, but a slight decline of up to 0.2% in communications services (Ecorys 2009). True, the trade in these types of service is mainly marked by higher qualifications and incomes (cf. Kemekliene/Watt 2010: 18ff.), but this will not necessarily be so in every case. A stronger market presence of the larger US finance corporations could, just like the expansion of Internet-based services, further increase the competition and rationalization pressures[13], particularly on the retail side. The upshot would probably be a continuation of the employment flexibility trend, increased use of socially unprotected "freelances" and stronger pressure on the wages of low-qualified and standardized occupations.

The employment-intensive sectors include, in particular, healthcare and social services. Even if the volume of trade in these fields is comparatively low, impacts on the quality of employment cannot be ruled out. Here, the possible effects of increased US-EU trade in *Modes 1* and *4* would probably be negligible. However, despite the liberalization measures already in place, easier market access in *Mode 3* could lead to increased activity by US service firms. Taken together with Commission's keen interest in commercializing services of general interest to the greatest extent possible (e.g. through quasi-markets), the increasing needs and the existing pressure on costs in the health sector, this could spell work intensification, use of atypical forms of employment (e.g. home care) and continuing pressure on wages (cf. for instance Lethbridge 2011).

Similar effects may be feared for public (supply) services in general, except any that are explicitly exempted as non-economic. Especially for water and energy supply and local public transport, profit interests exist on the part of (big) private corporations, which are pressing for further liberalization or privatization. The Commission did claim in passing that it does not plan to include the water sector.

[13] Moreover, it is precisely in the financial sector that stronger competitive pressure could once again prompt the search for riskier forms of investment, thus provoking financial instability.

However, in view of past liberalization initiatives, such announcements – just like the provisional ringfencing of audiovisual services – are not very reliable. Among the problematic points here is not only the possible increase in foreign private investment in these fields, but also the complex interplay between the narrowest possible definition of non-economic services of general interest, tougher competition regulations and liberalization of public procurement. Due to the often fuzzy definitions involved, the results of that interplay are not entirely predictable. Liberalization of public services opens them up not only for US firms, but also for European ones. The various consequences of this include not only formal or material privatizations in the strict sense, but also, in line with the ideas of New Public Management, other forms of competition, such as quasi-markets, benchmarking or competitive tendering calls. Economization of this kind has often gone together with employment losses, pay cuts, exclusion from collective bargaining coverage and dwindling co-determination rights (Schulten/Brandt/Hermann 2008).

Finally, in case of liberalization, impacts should also be expected in the education sector. For instance, universities and other education providers in the US or other English-speaking countries have for quite some time now been more internationally oriented, and they enjoy competitive advantages conditioned both by experience and by language. Especially through *Modes 1+3,* this could lead to competition effects that would put providers in other countries under pressure to adapt, for instance through staffing adjustments.

From a macroeconomic and political point of view, moreover, the intended investor-state settlement procedure is harmful (see Eberhardt in this volume). It produces negative distribution, growth and development effects, and in the middle-to-long term it could, selectively at least, prove detrimental to employment standards and social standards. The durability criteria laid down in connection with social standards cannot halt such developments, as there are no sanctions mechanisms, but also because it is rare for the ILO core labour standards or CSR principles to be seriously brought to bear on labour market and employment standards in developed economies.

The TTIP will probably not help to tackle the slow growth in Europe. Instead, it is feeding Europe's present competition fixation. The austerity policy currently being pursued, declaredly in order to regain competitiveness, would no doubt be further prolonged by a TTIP-induced rise in competitive pressure. In addition, trade diversion from European neighbours towards the US would further worsen Europe's demand deficiency.

Negative social effects in these countries, or indeed at the international level, cannot be ruled out. In some countries, the intensified transatlantic trading relations are likely to be accompanied by displacement effects, losses of jobs and income and stronger wage competition. Counted among the possible losers are, in particular, those countries that already have agreements with the US or the EU (e.g. Mexico, Chile, Turkey and the countries of North Africa) or which trade intensively with the US and therefore stand to lose structural advantages (cf. Felbermayr et al. 2013). And finally, the liberalization of procurement and the levelling of regulation possibilities could undermine efforts to achieve socially and environmentally responsible public procurement, or else they could enshrine often ineffective international standards.

1.6. Conclusions and Recommendations

The transatlantic free trade agreement currently under negotiation between the European Union and the US entails a number of risks. First off, even if they emerge at all, the prosperity effects claimed by its supporters will be insignificant, and in any case they may well be unevenly distributed. Secondly, perceptibly negative effects for workers in various sectors, and for democracy, are at least as likely to result. Competition effects due to the stronger presence of foreign bidders or, for example, an increased Internet-supported supply of services, may particularly affect employment standards and intensity in various sectors. This concerns fields, such as business services, financial services or ICT services, in which stronger trade impacts are expected from the agreement, but also employment-intensive fields such as healthcare and social services, public supply services and education. In principle, the negative effects, among other things through outsourcing, atypical forms of employment or a reduction in collectively bargained standards, may be expected mainly in less qualified jobs. However, examples from Internet-supported business services or education services show that more highly qualified occupations are not necessarily immune. Finally, it is unlikely that transatlantic trade negotiations will be seriously used to agree upon measures to enforce or even improve social and labour standards. This would not correspond either to the liberalizing intentions of the negotiating partners or to the interests of the influential corporations.

Moreover, the way in which the negotiations are being conducted is objectionable from a democratic point of view, as are the liberalization and investment protection measures being sought. The planned agreement is mainly a project pursued since the mid-1990s by big transnationally active companies on both sides of the Atlantic. This is not just about facilitating trade or potential savings through regulatory easing. It is also more particularly about getting into business fields that hold out the promise of big profits, such as public services or procurement, or dismantling regulatory restrictions, for example those related to health or the environment. Thus, existing regulations are to be reined in, as is the possibility of creating regulations in future, regardless of their democratic credentials. But an agreement of this kind also reflects the global trade and economic policy interests of the EU and the US. Both are looking for ways of maintaining economic supremacy, particularly vis-à-vis the rising economies of Asia. At the same time, through this attempt at bilateral standard-setting, they are seeking to motivate (or force) other countries to take further liberalization steps, i.e. to open up for American and European firms. On the European Commission’s side, this drive also corresponds to the aim of further liberalizing the European internal market, with competitiveness as the prime goal of economic policy. Regardless of whether bilateral agreements hamper or foster the development of the multilateral world trading order, a transatlantic agreement may be expected not only to have negative trade and income effects in third countries, but also to contain provisions which, if established internationally, would probably compromise other countries’ ability to develop.

On the European side in particular, the agreement represents a neomercantilist-leaning anti-crisis strategy that regards austerity policies, wage competition and social cutbacks as growth-promoting. In fact though, both before the crisis and even more since the crisis, this strategy has contributed to increasingly unequal distribution and international asymmetries. Even if a transatlantic agreement did have positive prosperity effects, these would take several years to materialize and they would be too small to compensate for the

negative consequences of this strategy. On the contrary, some elements sought in the agreement, notably an investor-state dispute settlement process, imply forms of redistribution that are not only damaging in terms of democracy and policy but also adversely affect growth and development.

At least for as long as the negotiations are conducted largely in secret and there are no adequate means of exerting democratic influence on them, and on any future negotiating arenas established by them, in a timely, well-informed manner, then there is more to be said against such an agreement than for it. In particular, the Commission's mandate and negotiating aims include a number of elements whose implementation should be rejected. Alongside the investor-state dispute settlement procedure, for which there is no justification at least in the case of democratically developed and institutionally reliable legal systems, the introduction of a negative list approach in the field of (public) services or procurement should be rejected, as should the adoption of any standstill clauses that would restrict the future possibilities for regulation. Public supply services should be excluded, and so should (de)regulation of the financial sector. Financial regulation should be negotiated with economic stability and possible allocation and distribution effects in mind – and not in the context of a deregulation-oriented trade liberalization that ignores the crisis-causing or crisis-aggravating effects of past liberalizations.

Better democratic control of the negotiations and of the influence exerted by big corporations and their interest groups is also required, in order to prevent possible negative consequences, for example in agriculture, as regards environmental, health, social and employment standards. The Commission's promises to maintain such standards are no more reassuring than the formulation of corresponding chapters on durability, with no provision for any kind of enforcement or sanctions.

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2. An Economic Assessment of the Claimed Benefits of the Transatlantic Trade and Investment Partnership (TTIP)[1]

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The United States (US) and the European Union (EU) are negotiating a free trade agreement: the *Trans-Atlantic Trade and Investment Partnership* (TTIP). This report presents a critical assessment of four key studies on the projected economic benefits of such an accord: Ecorys (2009), CEPR (2013), CEPII (2013),[2] as well as Bertelsmann/ifo (2013).[3]

Trade flows between the EU and the US, which both account for almost half of world GDP, have a substantial influence on the world economy. Including trade within the EU, exports and imports of the potential TTIP member states represented more than 43 % of world trade in 2012 (World Bank data). The US is still EU's single most important trade partner, accounting for almost 20 % of extra-EU exports in goods and services and more than 15 % of imports in 2012, even though the bilateral EU-US trade as a share of world trade has lost some importance in recent year. Several studies say that TTIP would not only stop this trend but, more importantly, give a boost to global economic growth. Most prominently, the European Commission estimates the potential economic stimulus because of TTIP at €120 billion for the EU economy, €90 billion for the US economy and €100 billion for the rest of the world.[4] But how are these benefits of TTIP derived?

One commonly applied method to calculate costs and benefits of trade liberalization is a *computable general equilibrium* (CGE) model. A CGE model falls within the general category of empirical economy-wide models. It is based on a Social Accounting Matrix (SAM), which depicts detailed data on relations of production and distribution between the main socio-economic agents in an economy. The model adds behavioral relationships to the accounting; econometric evidence is applied to calibrate relevant parameters. The complete model can then be used to calculate counterfactuals in response to assumed shocks and policies – for example, tariff removal.

In the case of trade between the US and EU, most tariffs are already very low. Removing remaining tariffs is expected to have very limited effects. Therefore the focus of negotiating and modeling efforts is on *non-tariff measures* (NTMs), or non-tariff barriers. These are procedures, laws and regulations other than tariffs or quotas that impede trade in goods and services between two countries. In order to apply NTMs to a CGE model, these barriers need to be estimated, including what share of them is practically

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1 This article is based on a study commissioned by the GUE-NGL group in the European Parliament. Any remaining errors are of course the exclusive responsibility of the authors.

2 The CEPR (2013) report is listed in the references as Francois et al. (2013), the CEPII (2013) policy brief as Fontagné/Gourdon/Jean (2013) and Ecorys (2009) as Berden et al. (2009). Throughout the main text, we will refer to these simply as the Ecorys, CEPR and CEPII study, respectively.

3 The Bertelsmann Foundation has published a study on TTIP with two parts. Our analysis is based in particular on part 1: macroeconomic effects. This report is listed in the references as Felbermayr/Heid/Lehwald (2013) and referred to as Bertelsmann/ifo throughout the main text.

4 See http://ec.europa.eu/trade/policy/in-focus/ttip/about-ttip/ (last accessed 03/24/2014).

removable (or *actionable*). A different (and much less common) method to calculate potential benefits is to *assume* that TTIP will create a certain increase in trade between the United States and European Union. A general equilibrium model of the world economy can then be used to calculate the necessary NTM removal to produce such gains.

Three of the four studies reviewed here follow the standard procedure. (Table 1 presents a quick overview.) These are Ecorys (2009), CEPR (2013) and CEPII (2013). All three build on the same set of NTM estimates provided in Ecorys (2009), feeding these into a CGE model. Ecorys and CEPR employ the same model, which is based on the popular GTAP model. The CEPII model, called MIRAGE, differs in the details, but rests on the same conceptual foundations. The fourth study, Bertelsmann/ifo (2013), i.e. financed by Bertelsmann Foundation and conducted by the ifo institute, estimates a *gravity trade* model, and employs a quite different simulation strategy. Thus, the procedures to estimate gains differ, but all four models have important similarities, which ensure that adjustments to liberalization work their way through the economy via price changes.

Specifically, a country's domestic prices decrease in response to the removal of its trade barriers. Falling prices reflect, on the one hand, increases in productive efficiency, as labor and capital are moved to economic activities where a country has a comparative advantage. On the other hand, they reflect decreases in mark-ups or rents, as firms with substantial market power face higher competitive pressures. Together, these changes imply higher production levels, higher incomes and higher real wages. The gains from trade are then, simply put, the result of the removal of distortions – may they be differing regulations or tariffs – combined with the assumption that labor and capital *can easily be moved between activities* – the full employment assumption. In other words, economic performance is determined from the supply side.

In this sense, the estimation and simulation procedures applied in all four studies build on the old idea that the market left to its own devices produces the best of all possible worlds. Our contribution to this volume critically assesses the building blocks of that endeavor. In the next chapter, we begin with a detailed overview of the projected benefits of TTIP by the four most influential studies (chapter 2.1). This is followed by insights on potential macroeconomic adjustment costs and other issues that are generally neglected in these studies, in particular the social costs of regulatory change (chapter 2.2). Furthermore, a comparison of ex-ante assessments and ex-post experiences of NAFTA is provided, since the latter is often cited as a show-case example for successful trade liberalization (chapter 2.3). Finally, the theoretical background and the technical specifications of the applied models are analyzed in detail (chapter 2.4). This is started with a discussion of the origins of these models in chapter 2.4.1. Chapter 2.4.2 reviews the issue of trade costs in general and the estimation of NTMs in Ecorys (2009) specifically. Chapter 2.4.3 discusses the two CGE models that were mostly used (GTAP, MIRAGE) and their closure and elasticities' assumptions. Chapter 2.4.4 considers the different methodology underlying the Bertelsmann/ifo study, as it pertains to NTMs and calculated gains. Chapter 2.4.5 provides a note on the estimations on the effects of income derived from foreign direct investment (FDI). Finally, Chapter 2.5 provides a summary of the main results of our analysis.

2.1. Main Findings of Studies on TTIP

2.1.1. Overview of Results

The message is clear in the influential empirical studies on TTIP: all EU member states and the USA will benefit from TTIP. Consistently the studies by Ecorys, CEPR, CEPII and Bertelsmann/ifo that are reviewed in this report predict such a positive economic impact on real income and trade for both sides of the Atlantic.

Given the similar data base (GTAP 7 and 8) and the closely related methodological approaches, it is not surprising that Ecorys (2009), CEPR (2013) and CEPII (2013) report gains in real income and trade flows within a similar range for all participating countries. The variations in the quantified effects can be attributed to variations in the approach to calculate tariffs equivalents of NTMs and modifications of the CGE model, for instance, the inclusion of spill-over effects to the rest of the world in the CEPR model. In contrast, the Bertelsmann/ifo findings mark the most pronounced benefits also due to larger bilateral trade effects of TTIP, higher implied trade costs and the assumption that trade costs are resource consuming.[5] Despite diverging assumptions and differences in the set-ups of the general equilibrium models, all analyzed reports follow the fundamental question: How does a reduction of trade costs between the EU and the US work through the two economies?

All studies simulate various scenarios by comparing policy changes to a baseline calibration. The forecast periods are set by researchers individually and typically a period of 10 years is assumed until the full effect of TTIP is reached. We consider the “limited scenario” in Ecorys (2009), the “ambitious experiment” in CEPR (2013) and the “reference scenario” in CEPII (2013) as major scenarios. In all of these scenarios, a cut in trade costs of roughly 25 % is assumed. In the Bertelsmann/ifo study, the “comprehensive liberalization scenario” is regarded as the most important simulation. This experiment is also comparable to the “NTB-scenario” in BMWT/ifo in which trade costs are also cut by 25 % (p92). The basic similarities allow for a comparison of the results with regard to changes in real GDP, trade flows and distribution among sectors in the two economic areas. In addition, the implications for real wage and employment can be summarized. Table 1 provides an overview with additional details on the assumptions and specifications and a summary of the main findings. A detailed description of the applied methodologies is provided in the chapters 2.4.2 – 2.4.4 of our contribution.

[5] The Bertelsmann/ifo report is based on a study performed by Felbermayr et al. (2013), also referred to as BMWT/ifo in the main text, on behalf of the German Federal Ministry for Economic Affairs and Technology (BMWT). The comprehensive BMWT/ifo findings are only partially included in the Bertelsmann/ifo report. For a comparison of all studies, results of Chapter II and III of the BMWT/ifo study are partially used. We aggregate these results to a trade- and GDP-weighted EU-27 average, if possible. An illustration of the relationship between the BMWT/ifo and Bertelsmann/ifo is provided in the Annex, Figure 1-A.

Table 1: Overview on basic assumptions and findings

	Ecorys (2009)*	CEPII (2013)	CEPR (2013)	Bertelsmann/ifo (2013)
Basic Assumptions				
CGE	GTAP	MIRAGE	GTAP	Simulation of gravity model
Data	GTAP 7	GTAP	GTAP 8	not specified
Non-tariff measures (NTM)	Ecorys	CEPII & Ecorys	Ecorys	ifo
Forecast period	2008-2018	2015-2025	2017-2027	10-20 years
No. Of Scenarios	7	5	5	3
Tariffs reduction	100 % of goods 75 % of services	100 %	98 - 100 %	100 %
NTM reduction in reference scenario	25 %	25 %	25 %	Reduction corresponding to trade creation effect
Main Findings (different scenarios, percentage changes compared to baseline scenario within forecasting period)				
EU GDP	0.32 - 0.72	0.0 - 0.5	0.02 - 0.48	0.52 - 1.31[++]
US GDP	0.13 - 0.28	0.0 - 0.5	0.01 - 0.39	0.35 - 4.82[++]
EU bilateral exports	not specified	49.0[+]	0.69 - 28.0	5.7 - 68.8[++]
EU total exports	0.91 - 2.07	7.6[+]	0.16 - 5.91 (extra-EU only)	not specified
EU real wages	0.34 - 0.78	N/A	0.29 - 0.51	not specified
Unemployment rate in EU-OECD countries (avge. %-points)	unchanged (assumption)	unchanged (assumption)	unchanged (assumption)	- 0.42 (deep liberalization)

Source: Ecorys (2009), CEPII (2013), CEPR (2013), Bertelsmann/ifo (2013)
* Findings for ambitious and limited scenarios only;
[+] Reference scenario only
[++] Derived from BMWT/ifo (2013), aggregated to EU-27 level

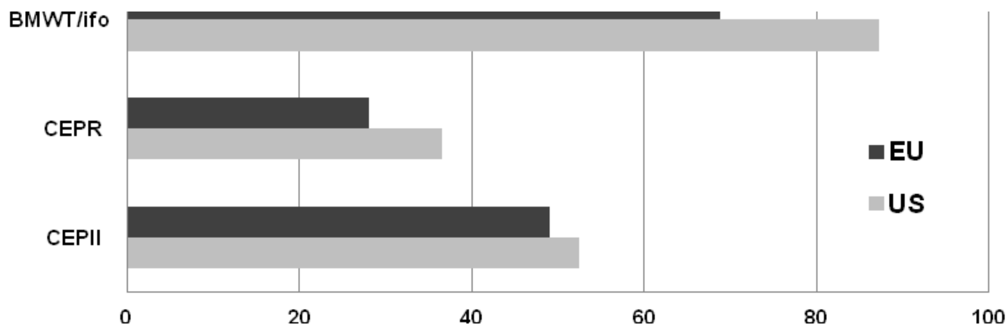
2.1.2. Trade Flows

The most obvious impact of a TTIP is the change in the EU-US trade flows. Three out of four reports state these long run changes in bilateral exports explicitly. Consistently, the export creating effect for US exports to the EU is higher than vice versa. The largest effect in export changes for the US and the EU is reported by Bertelsmann/ifo (2013).[6] These changes are not a result of a CGE model but the econometrically measured trade creation from observed free trade agreements. On average, bilateral exports between the US and all 27 EU members are assumed to increase by around 80 % (see chapter 2.4.4 for more details). In the CEPR report, these trade creating effects are significantly smaller with an increase of bilateral US exports by 36.6 % and bilateral EU exports by 28.0 % (Figure 1).

The impact of TTIP on *total exports* (excluding intra-EU trade) is very similar to the pattern in bilateral exports but significantly smaller. The highest reported changes are predicted by CEPII (2013) with a plus of more than 10 % in US exports and 7.6 % in EU exports. In the study by Ecorys (2009) the increases in total exports are 2.7 % for the US and only 0.9 % for the EU (Figure 2).

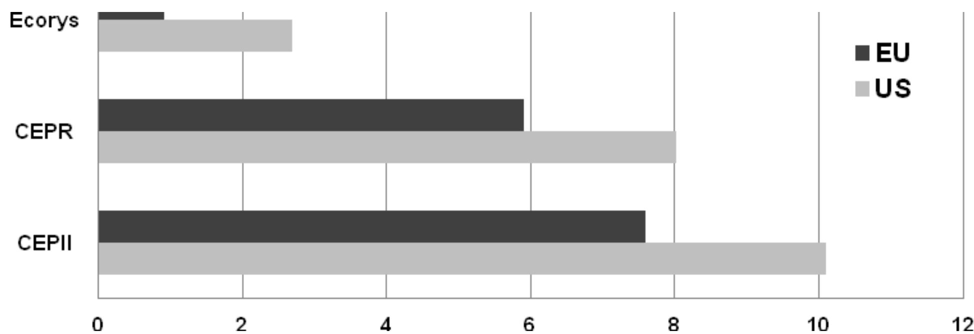
6 The aggregated bilateral trade data for EU-27 and the US are derived from "NTB-Scenario" in BMWT/ifo, 2013, Chapter III, in order to allow for a rough estimation.

Figure 1: Estimated percentage change in bilateral exports



Source: Ecorys (2009), CEPR (2013), CEPII (2013), own calculation based on BMWT/ifo (2013)
Major scenarios, compared to baseline scenario

Figure 2: Estimates percentage change in total exports



Source: Ecorys (2009), CEPR (2013), CEPII (2013)
Major scenarios, compared to baseline scenario, excluding intra-EU trade

The overall positive impact of TTIP on total exports conceals large trade diversion effects. In particular, intra-EU trade is negatively affected as cheaper imports from the US and the rest of the world (ROW) can displace products and services that were exchanged within the EU before. CEPII (2013, p10) reports that the increase in EU exports would be limited to 2.3 % compared to the 7.6 % increase, when intra-EU exports are excluded, as depressed intra-EU trade weighs on the total export performance. Intra-EU trade diversion is also reported by CEPR. In the ambitious experiment, trade among EU member states is expected to decline by €72 billion (p55). However, higher exports to the US and the ROW (€187 billion and €33 billion) would still amount to an increase in exports from EU member states.

In the Bertelsmann/ifo report and other ifo publications (e.g. Felbermayr and Larch 2013b) the trade diversion effects of TTIP are highlighted, based on the pure gravity framework (BMWT/ifo 2013, chapter II). In a deep liberalization scenario, TTIP would even "…alter the trade diversion effects currently in force in the EU [that came about as a result of preferential treatment of intra-EU trade flows]" (Bertelsmann/ifo, p14) influencing trade flows of most EU member states negatively. Details on changes in trade flows among 25 major economies with regard to trade volume reveal that only total exports from the US (+13 %), Greece and from some non-EU countries among these countries would benefit from TTIP (BMWT/ifo 2013, p162, Table A.III.1; also partially presented in Bertelsmann/ifo section 4). In

contrast, the intra-EU exports among the selected EU countries would fall by 25 to 41 % (see last column of Table 2). Applying these changes to actual 2007 trade data (UN comtrade and UN service trade) shows that intra-EU trade value would drop by more than US$900 billion. In total, this would not only cause total export from EU countries to decline, but even force total trade volume among the selected 25 countries to fall by US$380 billion. Overall, the negative trade diversion effects would considerably exceed trade creation effects of TTIP in such a scenario (Table 2).

Table 2: Possible trade diversion effects of TTIP

		Importers													
		AUT	**BEL**	**GER**	**ESP**	**FRA**	**GBR**	**GRC**	**ITA**	**NLD**	**POL**	**SWE**	**USA**	**Exports to 24 countries***	**Intra EU exports**
Exporters	**AUT**		-21	-24	-29	-18	-37	-25	-24	-23	-21	-31	108	**-13**	**-25**
	BEL	-21		-26	-31	-21	-39	-27	-27	-26	- 24	-33	100	**-14**	**-27**
	GER	-24	-26		-34	-23	-41	-30	-29	-28	- 26	-35	94	**-10**	**-29**
	ESP	-29	-31	-34		-29	-45	-35	-34	-33	-31	-40	80	**-24**	**-34**
	FRA	-18	-21	-23	-29		-36	-25	-24	-23	- 21	-31	108	**-8**	**-26**
	GBR	-37	-39	-41	-45	-36		-42	-41	-41	-39	-46	61	**-10**	**-41**
	GRC	-25	-27	-30	-35	-25	-42		-31	-30	-28	-36	90	***2***	**-33**
	ITA	-24	-27	-29	-34	-24	-41	-31		-29	-27	-36	92	**-13**	**-30**
	NLD	-23	-26	-28	-33	-23	-41	-30	-29		-26	-35	95	**-17**	**-29**
	POL	-21	-24	-26	-31	-21	-39	-28	-27	-26		-33	100	**-20**	**-27**
	SWE	-31	-33	-35	-40	-31	-46	-37	-36	-35	-33		75	**-16**	**-37**
	USA	108	100	94	80	108	61	90	92	94	100	75		***13***	**Avg: - 30**

Source: calculations based on BMWT/ifo (2013, p165) and UN comtrade and UN service trade data (base year 2007)

* other counties include Argentina, Australia, Brazil, Canada, China, Indonesia, India, Japan, Mexico, Russia, South Korea, Switzerland and Turkey

In general, the authors of the BMWT/ifo emphasize that several studies typically found negative trade diversion effects for third countries due to bilateral trade agreements and mutual recognition agreements (Felbermayr/Larch 2013b, p8). In contrast, CEPR sees a positive impact of TTIP for all other regions in the world due to the inclusion of spillover effects in their model.[7] This would cause exports to increase between 0.6 % and 2.3 %. Also CEPII sees negative consequences for exports of selected ROW countries in their reference scenario, but a positive impact if spill-overs are included (Appendix p A.9, Table A.7). Thus, the assumptions of spill-over effects enable CEPR and CEPII to avoid a conflict with the EU's commitment to Policy Coherence for Development. PCD stipulates that the EU's policies must not counteract the EU's development objectives and policies. Any negative effects from trade diversion as indicated in the data (from other trade agreements) and Bertelsmann/ifo could thus undermine the EU commitment to eradicate poverty in developing countries (Article 208 of the Lisbon Treaty; see also next section on GDP effects).

All analyzed studies report an increase of total imports to the US and the EU. The TTIP effect on imports as a percentage change is generally lower than the change in total exports. For instance, CEPR (2013) expects total US and EU imports to increase by 4.74 % and 5.11 %, respectively. On the other hand,

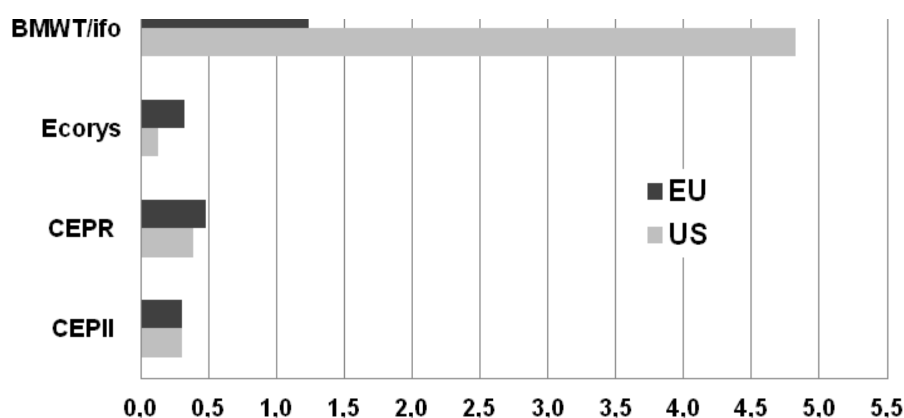
7 It is assumed that trade costs for third countries exporting to the EU and the US decline by 20 % of the bilateral fall in EU-US trade costs and that trade costs for EU and US exports to third countries decline by 10 % of the bilateral trade cost reductions (CEPR 2013, pp28-29)

calculations based on BMWT/ifo estimates (NTB-Scenario, p93) reveal that EU imports from ROW (excluding intra-EU trade) would decline by 4.0 % (or 53 billion USD; based on 2007 UN comtrade data). On the other hand, EU imports from the US would increase by 87.3 % (or 217 billion USD).

2.1.3. GDP and Household Income

The TTIP impact on economic income, measured in changes of real GDP, is limited compared to changes in trade. Although percentage changes of US total and bilateral trade flows are expected to exceed shifts in EU trade throughout all analyzed studies, only two studies forecast the same pattern for changes in GDP. Based on a higher value added composition of EU exports, CEPR (2013, p46) expects real GDP growth in the EU to exceed US GDP growth despite smaller EU trade effects. Overall, the impact of TTIP on real GDP, given the major scenarios is positive, ranging from 0.13 to 4.82 % for the US economy and from 0.32 to 1.31 % in the EU (see Figure 3). The oft-cited large real per capita income changes in the Bertelsmann/ifo study (US: 13.9 %, EU: 5.3 %) are based on the concept of equivalent variation and are not considered in this comparison of real GDP change (see chapter 2.4.4 for more details). Instead, the BMWT/ifo data on real GDP changes are reported here (see Figure 1-A for interconnection between BMWT/ifo und Bertelsmann/ifo).

Figure 3: Estimated percentage change in real GDP



Source: Ecorys(2009), CEPR (2013), CEPII (2013), own calculation based on BMWT/ifo (2013)
Major scenarios, compared to baseline scenario

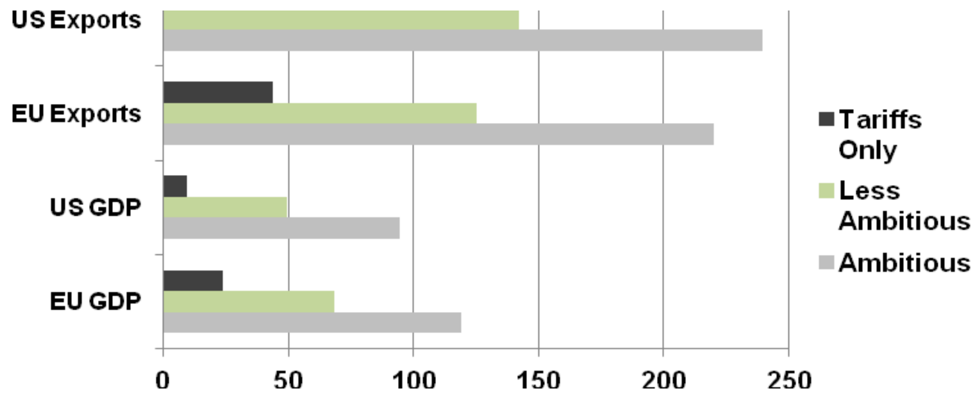
However, the interpretation of these results has to be handled with care as the estimates refer to a change relative to a baseline scenario at a specific point in time. In the case of CEPR, the simulation period is set between the years 2017 and 2027. The estimated increase of 0.48 % in EU GDP is therefore the value addition due to TTIP up to 2027 compared to a projected benchmark without TTIP.[8] In other words, all studies estimate by how much the level of GDP is elevated due to TTIP in the long-run. As this level effect continues to exist, once it is established, the studies speak of "percentage gain per year in 2018" (Ecorys 2009, p xiv), "annual long run increase in national income" (CEPII 2013, p10) or "disposable income gain […] annually in the EU." (CEPR 2013, p47)

The magnitude of real GDP growth is highly dependent on scenario assumptions. Even in major experiments which assume a substantial cut in NTMs, the *relative* impact on GDP growth is limited,

[8] Data from GTAP 8 (2007) projected to 2027 with IMF estimates

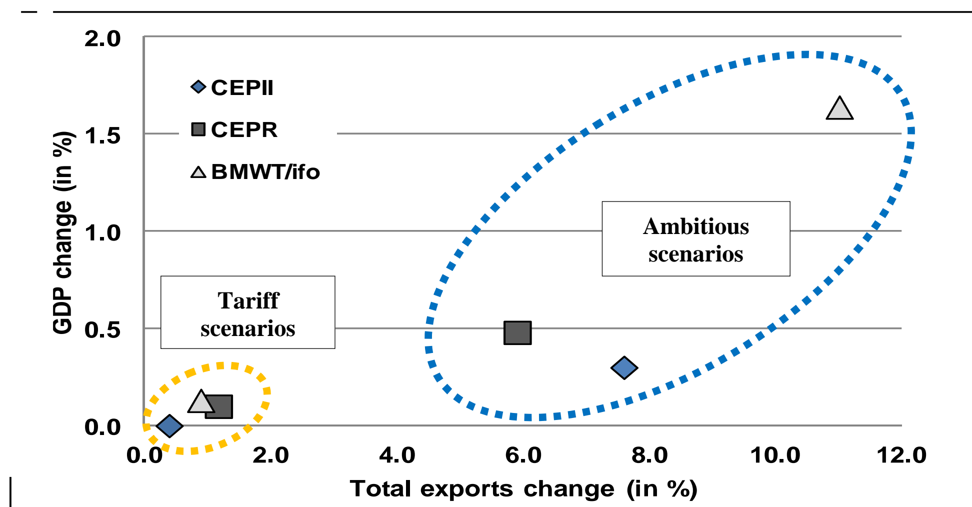
despite the prospect of value addition as high as €120 billion until 2027 (see Figure 4). An elimination of all tariffs without changes in NTMs ("Tariffs Only") would hardly have an effect on export growth as well as GDP level change (Figures 4 and Figure 5). Contrary, the positive effect of almost €24 billion of EU value added until 2027 is also associated with foregone EU tariff revenue of more than €7.3 billion according to CEPR calculations (p54).

Figure 4: CEPR scenario results for Exports and GDP



Source: CEPR (2013)
In billion €, Changes compared to baseline scenario

Figure 5: Comparison of total exports and GDP changes (in %)



Source: CEPR (2013), CEPII (2013), own calculation based on BMWT/ifo (2013)
Changes compared to baseline scenario; BMWT/ifo results based on "NTB-Scenario" (p93 – trade weighted changes with 2007 comtrade data)

Despite the relatively small upside potential in GDP, the reports all make an effort to present the income gains in simplistic, if not misleading ways. For instance, Ecorys (2009, p xiv) states that elimination of all 'actionable' NTMs (around 50 % of NTMs) would be equivalent to an extra €12,300 (in 2008 prices) per EU household over a working lifetime (starting in 2018), without any details on this calculations. Also, CEPR (2013, pp47-48) calculates an annual income gain of up to €545 per EU household (family of 4),

however, only after the full effect of TTIP is in action after 2027. Finally, BMWT/ifo (2013, p99) forecasts an average GDP per capita increase in Germany of €500 (2011 prices) in the long run. Taking into account the long transition period of 10 years or more, and the strong assumptions with regard to NTMs reductions, the absolute benefit per person from TTIP remains highly unrealistic. Besides, it conceals that very likely the distribution of gains amongst the population will be uneven.

Due to global trade diversion, the TTIP would also influence the GDP growth potential of all other countries around the globe. Scrutinizing the BMWT/ifo results (Chapter 2 and Table A.II.6, p159, 126 countries) on real GDP changes in a deep liberalization scenario underlines possible negative effects on non-TTIP economies due to trade diversion effects (Table 3).

Table 3: Real GDP Change by Income Groups (according to World Bank classification)

Income Groups (number of countries included by ifo)					
Low Income (18)	Lower Middle Income (25)	Upper Middle Income (36)	High Income: non-OECD (16)	High Income OECD (31)	TTIP Countries (28)
-1.40 %	-1.75 %	-1.90 %	-1.52 %	1.44 %	2.93 %

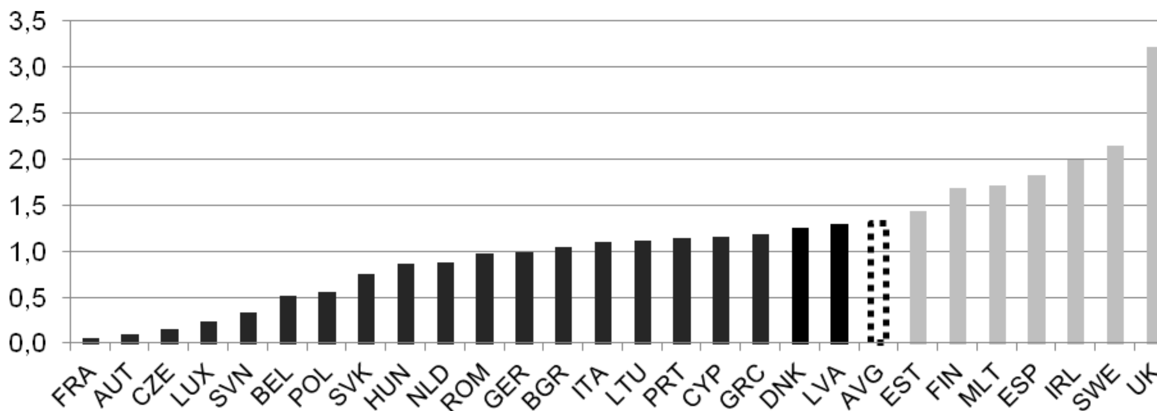
Source: own calculations based on BMWT/ifo 2013, Table A.II.6
Weighted average by 2007 GDP data

While TTIP economies would see an increase in real GDP close to 3 %, most countries in the lower income group would suffer from TTIP in terms of output. In particular, economies with closer trade relationships to the US and Europe like Canada, Mexico, Norway and Russia might face declines in real GDP. Also low income countries would get hurt (-1.4 %) – a clear violation of EU's coherence principle. Moreover, Latin America (-2.8 %) and Sub-Saharan Africa (-2.1 %) would be among the main losers from TTIP according to the BMWT/ifo results. These unequal effects, however, are not seen as a problem by the authors of the Bertelsmann/ifo study. In their view, potential negative effects of TTIP would increase the willingness of third countries to adopt TTIP standards or to enter into bilateral and multilateral trade agreements in order to gain from free trade (p29).

In contrast, CEPR (2013) expects a positive impact for all regions worldwide as positive trade creation in third countries (spill-over effect) exceeds negative trade diversion. In total, this would amount to an addition of almost €100 billion or 0.14 % to world GDP compared to a 2027 baseline scenario. However, in a separate publication, the Bertelsmann and ifo authors stress that these results are based on specific assumptions contradicting the experience with trade diversion so far (Felbermayr/Larch 2013b, p12).

In addition, TTIP would lead to potential 'losers and winners' in different scenarios among the EU-27 countries. Although all EU countries would benefit from TTIP, changes in real GDP range from 0.06 % (France) to 3.22 % (UK) within the forecast period of up to 20 years in the BMWT/ifo experiment (Table A.II.6, pp159-161). The GDP-weighted average of 1.31 % (2007 GDP data, Eurostat) is mainly surpassed by UK, the Scandinavian countries as well as Spain and Ireland. Almost unchanged would be the GDP in France, but also Germany and Italy would see below-average growth rates in this scenario (Figure 6).

Figure 6: GDP changes in EU-27 countries



Source: BMWT/ifo 2013, Table A.II.6, pp159-161
GDP-weighted average with 2007 Eurostat data

Despite a more positive value-added effect for Germany, CEPII also sees diverging GDP results within the EU. In particular, France, as well as the Southern and Eastern European countries would see relative weak effects compared to Germany, UK and the Northern European states (CEPII 2013, Appendix pp A.7-A.8). CEPII also mentions potential conflicts among EU players due this unequal distribution of potential economic benefits (p11). In sum, it would seem that as a tendency countries which already have competitive export sectors would benefit disproportionately from TTIP.

2.1.4. Sectoral Effects

The decomposition of aggregated macroeconomic estimates of trade and value added by sectors reveals one of the basic mechanisms how a free trade agreement could work through the economy. More competitive sectors in an economy will benefit from enhanced access to a combined market. Consequently, output and exports of a competitive sector will increase and the corresponding sector in the other economy will suffer as cheaper imports replace domestic production. However, the trade volume in most sectors should benefit from lower import prices and untapped trade potential in general.

A sectoral analysis was performed by Ecorys (2009) with details on potential NTM reductions and effects by sector. Three core messages are highlighted in the Ecorys (2009) report. Firstly, all sectors in the EU and the US (except for the US insurance sector) contribute positively to national income[9] compared to the benchmark, even if output in several sectors declines. Secondly, total gains from an economy-wide alignment of NTMs (in all sectors) are four times larger than the sum of sector-specific gains from TTIP (NTM reduction in one sector while all other NTMs remain constant). In other words, the gains from TTIP shrink dramatically if an agreement does not include NTM reductions in a large number of sectors. This is also stressed by CEPR (2013, p63). And thirdly, even if output and employment in a sector might decline, the contribution to national income might still be positive. This indicates the importance of price effects for TTIP benefits.

[9] National income includes price changes. Prices are expected to decrease due to lower trade costs and elimination of economic rents (Ecorys 2009, p xxii).

These conclusions are also valid for the CEPR (2013) report as the methodology is very similar to the Ecorys (2009) study. As expected, the changes in sectoral output show the effects of increased bilateral competition within the sectors: competitive sectors in one economic area benefit from TTIP and increase trade as well as output, while the corresponding sectors in the country of the trading partner shrink (see Table 4). In motor vehicles, for instance, the EU could increase output by 1.54 % in the ambitious scenario of CEPR, while the motor vehicle output in the US would decline be 2.78 % (pp60-61). However, total and bilateral trade in this sector would still increase on both sides of the Atlantic with a plus of EU exports to the US of 87 % and US exports to Europe of 346 % (!). In general, the motor vehicles sector would generate around 43 % of total changes in extra-EU trade exports, as estimated by CEPR. Again, the total output change in the EU motor vehicle sector is quite small due to decreasing intra-EU trade and a strong increase of imports, mainly from the US.

A reverse case in output changes can be seen in the sectors "metals and metal products" and "other transport equipment" (aerospace) where the US output increases while EU output is expected to decline. Interestingly, electronical machinery which includes electronics and office information & communication is expected to decline in the EU and the US as spill-over effects would lift exports from ROW countries to TTIP countries (CEPR 2013, p63).

Table 4: Increasing and decreasing output by sectors and regions

EU sectors	
+	-
Motor vehicles	Electronical machinery
Water transport	Metals and metal products
Insurance	Other transport equipment

US sectors	
+	-
Other machinery	Motor vehicles
Other transport equipment	Electronical machinery
Metals and metal products	Insurance

Source: CEPR (2013)
Ranked by percentage change

Overall, sectoral changes in output are mainly positive but small. Even the most pronounced positive change in output in one sector, the 1.54 % increase in EU motor vehicles, is almost negligible as the output of this sector accounted for 2.2 % of total EU-27 output in 2009 (Eurostat). However, aggregation on an EU-basis hides substantial differences in the sectoral structure between EU member states. Studies that were conducted to analyze single-country effects of TTIP, for instance on UK, Sweden, Netherlands and Austria[10] report diverse sectoral effects. For instance, Ecorys (2012) sees the output of motor vehicles in the Netherlands to decline by 2.9 %, while EU-26 output would go up by 1.2 %.

An indication for the diverse effects among EU members is given by CEPII (2013) as trade and GDP effects are reported for agriculture, industry and services in six EU regions/countries (detailed results in CEPII appendix). In terms of value addition, the EU industrial sector is expected to have the largest percentage increase of 0.6 %, pulled by Germany (0.9 %) and Northern Europe (0.8 %). In total, the CEPII sees GDP changes above average in Germany, the UK and Northern Europe (due to a strong

[10] See CEPR/BIS (2013), Kommerskollegium (2012), Plaisier et al. (2012) and Francois and Pindyuk (2013).

industrial base in Germany and a large service sector in the other two regions). The other EU regions and countries (France, Eastern and Southern Europe) would hardly benefit from TTIP (GDP change of 0.2 % compared to baseline in 2025).

These sectoral examples underline the large estimated bilateral trade effects of TTIP in contrast to the limited output effect. In other words, more goods are exchanged, but not produced.

2.1.5. Real Wages and Employment

Besides trade and value added, the change in real wages is reported in three studies. The wage effects are very similar to GDP changes and follow the same logic: cost saving due to lower input prices increases average productivity which than leads to a higher compensation for labor. CEPR and Ecorys differentiate between unskilled and skilled labor. For unskilled labor, the two studies expect real wages in the EU to increase between 0.36 % and 0.51 %. Wages for skilled employees would be lifted between 0.34 % and 0.50 % compared to the benchmark. However, both studies assume a fixed supply of labor in the long run meaning that unemployment is not affected by the agreement. Thus, only wages adjust to higher labor demand stemming from more competitive sectors of an economy in the long run.[11]

Sectoral reallocation of labor, as shown in CEPR (2013), therefore entails the shift of employment from less competitive (importing) sectors towards more competitive (exporting) sectors. In the sector "motor vehicles" in which CEPR sees the highest output change in the EU (see above), total employment is expected to increase by around 1.28 %. In contrast, the US motor vehicles sectors will lose around 2.76 % of its labor force as output is expected to decline.

The ifo model-based studies take another path with regard to labor markets (see for a detailed discussion of the method chapter 2.4.4). BMWT/ifo expects both, an increase in real wages and a positive employment effect for the EU and the US. In total, unemployment should decline by 193,000 people (124,000 in the EU and 69,000 in the US, NTB-Scenario, p100) in the TTIP member countries. These results represent a net gain and jobs are reallocated between and within sectors due to increased productivity. Interestingly, ROW countries would suffer by losing 165,000 jobs due to trade diversion effects.

In the Bertelsmann/ifo report the changes in employment are more pronounced with an employment effect in the US of more than one million new jobs due to TTIP in their deep liberalization scenario, and of 1.3 million for the EU. Also Germany would see 181,000 additional jobs created. This is almost seven times the reported effect of 25,000 new jobs in Germany in the "NTB-scenario" in BMWT/ifo (Chapter III, p100). For the US, the job creation effect would even be elevated by a factor of ten. While the BMWT/ifo model is based on the "new" new trade theory by Melitz (2003) to allow for job reallocation from less to more productive companies and includes search unemployment, the model applied in Bertelsmann/ifo is an extension of the gravity model with a search and matching framework, but apparently without heterogeneous firms (see Heid/Larch 2013). In addition, the BMWT/ifo model is calibrated for Germany, USA and three aggregated regions to model global effects of TTIP, based on 2007 data. The Bertelsmann/ifo report focuses on 28 OECD countries only, which enables the authors to

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[11] Under the assumption of flexible labor supply, wages would be fixed and employment would adjust (CEPR 2013, p71).

include labor market data variables like wage replacement rates. Data used are from 2010, implying higher unemployment rates because of the global financial crisis. Based on their search and matching framework, it is shown that economies with higher market frictions (higher unemployment rate and/or higher unemployment benefits) experience larger unemployment effects. Thus, trade liberalization and the associated price reductions lead to a higher reduction in unemployment. In addition, the missing reallocation mechanism à la Melitz causes net employment effects in the Bertelsmann/ifo report to be elevated as job losses in less productive companies are not included (see also Stephan 2014). In our view, these two factors explain the difference in employment effects between the BMWT/ifo paper and the Bertelsmann/ifo report. In addition, it must be stressed that it is really unclear when these effects materialize, since they are derived from the long term adjustment process to a steady state. That could well take 20 years or more. Against this time frame, the reported large effects appear rather small on a per annum basis.

Overall, the three studies with estimations for changes in labor markets see a positive impact of TTIP, at least on real wages. Bertelsmann/ifo models labor markets explicitly and forecasts positive real wage as well as employment effects, a strong statement given that standard neoclassical labor market models assume lower wages in order to create employment. However, the adjustment process between and within the sectors is associated with short term unemployment. These negative effects are widely ignored or understated in the studies by stressing the long run effect. Therefore, we will illustrate possible short run disturbances and costs associated in particular with estimated labor market reallocations in the next section.

2.2. Adjustment Costs and Regulatory Change

2.2.1. Macroeconomic Adjustments Costs

Trade agreements entail many changes to the public sector, the private sector as well as households. These changes are both positive and negative, and the adaption to them confers benefits as well as costs upon society and particular social groups, respectively. Both benefits and costs may be of a transitory or more permanent nature. In the former case, these costs are usually labelled as adjustment costs. These transitory adjustment costs are to some extent recognized by conventional impact assessments, while it is generally assumed that trade agreements do not entail long term costs for society.

In the following, we intend to focus our attention on types of adjustment costs that were either underestimated by the four scrutinized TTIP studies, or were neglected outright. A class of adjustment costs refers to macroeconomic variables, which are crucial to economic policy in any advanced country. These are (i) the current account balance, (ii) the public budget balance, and (iii) the level of unemployment.

The Current Account Balance

Trade agreements by their very purpose lead to changes in trade as well as capital flows. If for instance, imports rise disproportionately vis-à-vis exports immediately after trade liberalization, a trade deficit might emerge. A large trade deficit might eventually require a devaluation of the national currency, with negative repercussions on the domestic price level or on local businesses with outstanding debts in

foreign currency. Similarly, if a country receives substantial amounts of foreign direct investment after trade liberalization, a certain fraction of the profits of that FDI will be repatriated by the parent companies, thus creating a constant drain of resources in the current account. Countries that attract FDI by low tax rates are particularly prone to these kind of practices. Ireland is the classic case in point here.[12] If not handled with care, further investment liberalization due to TTIP might aggravate such problems, particularly for smaller and less competitive EU countries, which receive large amounts of US FDI. If the trade agreement also includes portfolio investment in its definition of investment, as is the case with the more recent EU trade agreements (e.g. CETA), the structural vulnerability vis-à-vis short term and speculation-driven capital movements might become even more relevant. All of the four studies do explicitly deal with these issues. While we would consider it plausible to assume that liberalized trade flows under TTIP will not lead to a substantial change in the bilateral trade balance, which currently stands at an EU surplus of nearly €100 billion (2012, goods and services),[13] the issue of capital movements has not been dealt with systematically in the TTIP studies (see chapter 2.4.5 for a more detailed discussion). Given the experiences with the financial crisis since 2008, and the recurrent fluctuations of short term capital flows, as for instance recently into and out of emerging economies, it would seem to us that the effects of TTIP on the capital account merit considerably more attention.

The Public Budget Balance

Public budgets are impacted by trade liberalization both on the income and expenditure side. We will here focus on the income side, and take up the expenditure side when discussing labour market adjustment costs in the next section.

A straightforward consequence of trade agreements is the reduction, if not elimination of tariffs. The latter, however, form part of public revenues. Thus, all other things equal, trade liberalisation will reduce public revenues and hence increase the government deficit. While tariffs still account for up to 40 % of public income in many LDCs, public revenue from tariffs in the EU and US is rather small. However, tariff revenues are an important income source for the EU budget. In 2012, roughly 12 % of the EU budget was financed via tariff revenues. In 2012, according to the European Commission (2013a, p55), tariffs levied on US imports amount to €2.6 billion, or 12 % of total EU tariff revenue. Depending on the simulation scenario, CEPR (2013, p54) reports reduced tariff income between €5.4 – €7.3 billion on a yearly basis by 2027, i.e. after the full implementation of TTIP. Thus, if we conservatively estimate the long-term or structural loss of tariff income to the EU to be in the range of €5 billion per year, of which 75 % (€3.75 billion) go into the EU budget as traditional own resources, that amounts to a permanent annual revenue loss of at least 2.7 % for the EU budget in its current magnitude. Though it is plausible that an increase of EU exports and thus output because of TTIP will also lead to an increase of GNI own

[12] While the trade surplus stood at €32.5 billion in 2009, Ireland had a current of account deficit of €3.7 billon, which was mainly caused by a large deficit in the net income from abroad, in the order of €28 billion. Though in the meantime the current account deficit in Ireland has vanished because of the economic crisis, the large deficit in net income from abroad has not significantly changed. (see Irish Central Statistics Office, http://www.cso.ie/multiquicktables/quickTables.aspx?id=bpca2_n1103, see also M. Burke "Who benefits from Ireland's (im)balance of payments?", http://www.progressive-economy.ie/2010/08/who-benefits-from-irelands-imbalance-of.html (last accessed 03/26/2014).

[13] Data from European Commission/DG Trade website, http://ec.europa.eu/trade/policy/countries-and-regions/countries/united-states/ (last accessed 03/26/2014).

resources for the EU budget, which will at least partially compensate for the lost tariff income, we would argue that in the short to medium term, a net loss to the EU budget will be likely. This owes to the fact that tariff revenue losses will happen immediately, while EU exports will only gradually increase over time. Thus, we would expect a need to adjust the EU financial framework over the short and medium term, after TTIP eventually enters into force. Though the European Commission in its impact assessment report does not expect any problem in compensating tariff losses by other funds (European Commission 2013a, p55), we would argue that although 2.5 % seem to be a manageable amount, in the prevailing austerity environment the political will of member states to give more money to the EU budget might be limited.

The Level of Unemployment

As shown before, the potential benefits from TTIP can only be generated by a sectoral reallocation of the production factors labor and capital. This long-term process necessarily involves job displacements in the short to medium run as sectors facing strong import-competition after liberalization have to reduce output and employment. It is widely recognized that adjustment costs are distributed unequally as certain individuals or groups, for instance older and less skilled workers in manufacturing bear a substantial burden of trade-related adjustments (OECD 2005). It is also likely that some output is foregone until all production factors will adjust to the new equilibrium which in consequence will lead to less employment, income and tax revenues for some period of time.

In general, trade related adjustment costs include private costs for labor such as unemployment, retraining costs or obsolescence of skills as well as adjustment costs for capital, for instance investments to become an exporter. In addition, increased spending for unemployment benefits, retraining and social security programs, as well as and lower tax revenues are likely to constrain the government budget (see also Laird/de Córdoba 2006, for more details). The inclusion of potential adjustment costs into an assessment of trade agreements is essential as it reveals possible winners and losers from trade liberalization beyond average welfare gains as well as the uneven distribution of possible benefits and costs within and between economies in a trade agreement. In addition, economic shocks during the long term adjustment process (10-20 years) might increase the cost of adjustment and potentially reduce or eliminate gains from trade agreements.

In the analyzed studies on TTIP such negative effects on labor markets are understated with a commonly used argument: unemployment is a temporary phenomenon during an adjustment process that is overcompensated by higher income streams in the long run. The CEPR does not model long run unemployment at all in order to "… gather clearer insights on what would be the impact of the agreement on labor markets in the long-run" (European Commission 2013b, p15), meaning that the fixed labor supply will be fully employed after a transition period of 10 years. The BMWT/ifo report suggests that all adjustment processes are completed within five to eight quarters (p14). BMWT/ifo also refers to Trefler (2004) for the speed of adjustment. Trefler (2004), who analyzed adjustment processes in Canada after the free trade agreement (FTA) with the US in 1988, found evidence for likely aggregate welfare gains but reported substantial job losses associated with the FTA – 12 % for the import-competing industries and 5 % for manufacturing. And the author suggests, "… albeit not conclusively, that the transition costs were short run in the sense that within ten years the lost employment was made up for by employment

gains in other parts of manufacturing" (p879). Evidence from changes in labor markets after NAFTA also raises questions whether trade-related negative impacts are only transitory or not (see chapter 2.3 for more details).

In 2005, the OECD evaluated trade-adjustment costs in the labor market of its member states with interesting findings: Firstly, adjustment costs for trade-displaced workers are moderately higher than for other job losers due to slower re-employment (EU) and lower wages in new jobs (US). Secondly, displacements in EU manufacturing hits older, less skilled workers more likely, a characteristic which makes re-employment more difficult. However, differences to other displaced workers are limited. Finally, many displaced workers find a new job again in the same industry, but with slightly lower wages. Workers that switch industries even faced substantially lower earnings, in particular in the US. Also Francois et al. (2011) refer to this study and emphasize that labor bears the bulk of adjustment costs und that "…trade reform can add significantly to job displacement if undertaken when the job market is already under stress, such as situations of economic recession or major structural change" (p224).

Regarding potential adjustment costs under TTIP, only rough estimations and suggestions based on CEPR (2013) and Bertelsmann/ifo (2013) findings on employment effects are possible. As fixed labor supply is assumed, CEPR reports only net reallocations among sectors in the EU and US. A displacement index shows how many workers have to move across sectors in order to regain balanced job markets. In the case of less skilled workers in the EU only less than 7 workers per 1,000 have to switch to another sector, in the US it is less than 5 workers out of 1,000. This is no surprise, given the limited changes in output and the different relevance of goods in EU-US trade and labor markets. In 2012, trade in goods amounted to 75 % of total EU trade volume but less than 30 % of the workforce was employed in the related sectors (Eurostat). Still, when putting the displacement number into perspective, within the EU between 0.43 and 1.1 million workers would be affected by such a transition. Although CGE models foresee an improvement for people due to a switch from low to more productive sectors with higher wages, the empirical evidence shows that a switch to another industry typically includes a loss in income (OECD 2005). CEPR also argues that a displacement index around 0.6 % is relatively small compared to normal labor turnover in the EU of more than 3.7 % since the crisis in 2008 (p78). However, the displacement index does not capture all relevant changes in labor markets "…as displacement across firms is widely ignored in this literature [on adjustment costs in CGE models]" (Francois et al. 2011, p226).

CEPR publishes only sectoral net employment changes which are the outcome of larger gross job flows within a sector. Given heterogeneity of firms, reallocation of jobs mainly happens within sectors (OECD 2005, p36). This is also true for less competitive sectors that loose in terms of average productivity, output and real wages. Taking into account the high risk of long-term unemployment faced by older and less skilled workers in manufacturing once displaced (OECD 2005), and the reality of increasing long-term unemployment in OECD countries, a substantial part of the displaced workforce might be worse off with TTIP, even if average real wages as a whole are expected to increase. Furthermore, the assumption of no long-term unemployment in the case of the EU also implies sufficient labor mobility across EU member states. Given the diverging wage levels within the EU, labor movements from higher to lower wage countries are however most unlikely (see also EuroMemo Group 2014).

The Bertelsmann/ifo and the related BMWT/ifo studies try to overcome some of the conceptual limits of the other CGE models by modeling labor markets explicitly. The authors include search unemployment and heterogeneity of firms. Thus, productivity gains are translated into aggregate employment *and* wage effects (flexible labor supply). In addition, gross job flows are shown, at least for Germany (BMWT/ifo, p103). The employment effect in the BMWT/ifo study is relatively small with a decline in the unemployment rate of around 0.05 % in the EU and the US given the preferred NTB-Scenario, also due to rigid labor market institutions (p105).[14] In absolute terms, the net increase in employment, and therefore the decline in unemployment, amounts to 124,000 new jobs of which 25,000 would be in Germany. In more detail, this would result from a loss of more than 22,000 jobs in Germany but the loss would be overcompensated by more than 47,000 new jobs due to TTIP (p103). BMWT/ifo sees job displacements mainly in small, labor intensive companies while new jobs occur in mid-size companies that become new exporters.[15] Therefore, 90 % of total job creation should emerge in companies which are becoming new exporters.

Overall, it has to be stated that none of the studies provides an exact estimation of possible adjustment costs in labor markets. However, such an assessment would be crucial. A simple hint towards positive long-term effects understates the need for policy measures to mitigate the risk of welfare and employment losses for specific groups and individuals. In particular, the distressed situation in several European labor markets increases the need for the assessment of potential adjustment costs of TTIP even more.

Potential Macroeconomic Adjustment Costs – A Rough Calculation

After discussing the different types of macroeconomic adjustment costs, that are relevant for the TTIP negotiations, we would like to illustrate the likely magnitude of these costs by offering a rough calculation. The calculation includes loss of public revenue and the costs of unemployment. It is our objective (i) to provide a conservative estimate and (ii) to provide a plausible number that indicates the order of magnitude we will likely have to tackle with. The loss of public tariff revenue is estimated on the basis of the reported number on tariff income from US imports in 2012 (European Commission 2013a), representing the lower bound, and the estimated tariff income loss in 2027 from the most ambitious liberalization scenario of the CEPR study, thereby assuming that over a 10 year period annual losses would reach the upper bound of €5.4 billion in 2027. Unemployment numbers were also taken from labour displacement estimates of the CEPR study, and assumed to be in the range of 430,000 – 1,100,000. Compared to the reported US job losses due to NAFTA (see chapter 2.3), we consider these numbers to be plausible. However, given the difficult labour market situation in many EU member states and the evidence from the empirical literature (see discussion above), we assume that 10 % of the displaced persons will not find another (full-time) employment and will thus become long-term unemployed. We assume that the average length of their unemployment is five years during the ten year implementation period of TTIP. In accordance with most national unemployment benefit schemes, we further assume that during the first year workers will receive a higher net replacement rate (66 %) than for the following four years (41 %). For annual wages and replacement rates we use averages derived from OECD statistics. In

[14] Real wage effects, +1.63 % in the EU and +2.15 % in the US, are more relevant than changes in employment (BMWT/ifo 2013, p100).

[15] BMWT/ifo is even more precise: new jobs will only be created in companies with 50-250 employees which were responsible for only 8 % of total employment in 2007.

contrast, we assume that 90 % of displaced workers will become re-employed after six months on average, without a loss compared to their pre-TTIP income level – again we are on the optimistic side. We also consider the foregone public income from taxes and social contributions from unemployment. Even if during the transition period, new jobs will be created in the sectors driven by additional exports, we would argue that much of that represents a net loss to the public budget, since exports will react more slowly than imports to TTIP implementation, so that in the best of cases net employment will only be at a higher level after the ten year implementation period. Upon that basis, we calculate a lower and an upper bound of cumulative adjustment costs of TTIP during the ten year implementation period. Our lower bound is €33 billion, our upper bound €60 billion. On an annual basis that would amount to €3 billion to €6 billion. Of these between €0.5 – €1.4 billion will come from unemployment benefits, and €0.4 – €1 billion from foregone income from taxes and social contributions.

Table 5: Macroeconomic adjustment costs – a rough calculation (in €, 2012 prices)

Macroeconomic Adjustment Costs - a Rough Calculation				
1. Loss of Public Revenue	**Lower Bound (p.a.)**	**Lower Bound (cumulative, 10 year period)**	**Upper Bound (p.a.)**	**Upper Bound (cumulative, 10 year period)**
Annual Loss of Tariff Revenues of 2.6 bn	2.600.000.000	26.000.000.000		
Annual Loss of Tariff Revenues of (€2.6+€5.4)*0.5			4.000.000.000	40.000.000.000
Adjustment Margin for Phase-Out Periods, and Carve-Outs for sensitive products (10%)	260.000.000	2.600.000.000	400.000.000	4.000.000.000
Sub-Total	***2.340.000.000***	***23.400.000.000***	***3.600.000.000***	***36.000.000.000***
2. Costs of Unemployment				
a. Unemployment Benefits				
43,000 long-term unemployed post-TTIP (Year 1)	681.120.000	681.120.000		
110,000 long-term unemployed post-TTIP (Year 1)			1.742.400.000	1.742.400.000
43,000 long-term unemployed post-TTIP (Year 2 - 5)	423.120.000	1.692.480.000		
110,000 long-term unemployed post-TTIP (Year 2 - 5)			1.082.400.000	4.329.600.000
387,000 short term unemployed post TTIP (6 months)		3.065.040.000		
990,000 short term unemployed post TTIP (6 months)				7.840.800.000
Sub-Total		***5.438.640.000***		***13.912.800.000***
b. Foregone Public Income from Taxes and Social Contributions				
43,000 long-term unemployed post-TTIP (Years 1 - 5)		2.039.705.000		
111,000 long-term unemployed post-TTIP (Years 1 - 5)				5.217.850.000
387,000 short-term unemployed post TTIP (6 months)		1.835.734.500		
990,000 short-term unemployed post TTIP (6 months)				4.696.065.000
Sub-Total		***3.875.439.500***		***9.913.915.000***

Sources: OECD Employment Statistics, Benefits and wages statistics, www.oecd.org/els/benefitsandwagesstatistics.htm (03/27/2014); Eurostat Labour Market Statistics, CEPR (2013), European Commission (2013a)
Assumptions: Average duration of long-term unemployment during TTIP implementation phase: 5 years; Average duration of short-term unemployment during TTIP implementation phase: 0.5 years; Number of displaced persons post-TTIP: 430,000 (lower bound) – 1,100,000 (upper bound), of which 90 % short-term and 10 % long-term unemployment
Notes: EU-27 average annual net income (3 family types, 100 % AW, 2012): €24,000; EU Net Replacement Rate (60 month unemployment, simple average of 4 family types and two earning levels (67 %, 100 % average wage)): 41 %; EU Net Replacement Rate (initial unemployment phase, simple average of 6 family types and three earning levels (67 %, 100 %, 150 % average wage)): 66 %; Implicit tax rate on labour (EU 27 2011): 35.80%; EU-14 average gross annual income (2011): €26,500;

If we compare these numbers to the maximum annual budget of the European Globalisation Adjustment Fund and the European Social Fund – €150 million and €10 billion respectively, it should be expected that TTIP will be a substantial additional burden on the budget of these facilities. Given the historically high levels of unemployment in many EU member states, many-fold needs to fund employment policies do already exist and will have to compete for funds with TTIP adjustment policies. An increase of financial resources for these funds should thus be seriously considered by EU policy-makers.

2.2.2. The social costs of regulatory change

A type of adjustment costs conveniently ignored, but particularly relevant in the case of TTIP, refers to the regulatory change resulting from the agreement. This type of cost appears in various forms. Firstly, harmonization of NTMs, e.g. technical standards, will imply both a short-term adjustment cost for public institutions and for firms required to align their administrative procedures, production processes and products to the new standards. Secondly, mutual recognition of regulations and standards between trading partners will increase information costs for consumers, since the latter will be confronted with a more complex and potentially less transparent multiplicity of permissible standards, e.g. on goods and services. Thirdly, the elimination of NTMs will result in a potential welfare loss to society, in so far as this elimination threatens public policy goals (e.g. consumer safety, public health, environmental safety), which are not taken care of by some other measure or policy. Though subject to considerable insecurity, these types of adjustment costs might be substantial, and require careful case-by-case analysis. As we will see in the following, although the social costs of regulatory change are of particular relevance for the analysis of TTIP because of its emphasis of regulation issues, they have not been dealt with properly by the four scrutinized TTIP studies.

As already mentioned, around 80 % of the estimated economic benefits of TTIP stems from the dismantling of NTMs or their alignment. In their assessment of NTMs, two out of the four scrutinized TTIP studies draw on the work of Ecorys (2009). The other two study, CEPII and Bertelsmann/ifo employ a somewhat different methodology, but essentially share the same underlying philosophy with regard to NTM reduction. NTMs are basically understood as “all non-price and non-quantity restrictions on trade [...]. This includes border measures (customs procedures, etc.) as well as behind-the-border measures flowing from domestic laws, regulations and practices...” (Ecorys 2009, p xiii). The study focuses on both elimination of NTMs and of regulatory divergence, i.e. the existence of different regulations with the same purpose, e.g. technical standards for turn signals in the EU and US. The latter should be aligned, e.g. by negotiating a common new standard. These NTMs are understood to hinder the deep economic integration of the EU and US economies. Thus, their elimination or alignment to some common standard becomes desirable, as this would facilitate further economic integration. Ecorys then purports to estimate the quantitative significance of these NTMs by way of an elaborated procedure. Most importantly, in a survey companies and experts were asked to assess the level of restrictiveness of NTMs in bilateral trade.[16] Upon that basis indexes were constructed which were then used to estimate the impact of NTMs on trade and investment flows, or in other words, to calculate trade cost equivalents of existing NTMs. In a further step, again with the help of experts, levels of actionability were established, i.e. assessments with regard to “the degree, to which an NTM or regulatory divergence can potentially be reduced...” (Ecorys 2009, p15). Actionability levels were determined to range from 35 to 70 %, with the average for the EU at 48 % and 50 % for the US. In a last step, these actionability levels were taken as inputs for the CGE scenario estimations in the three studies by Ecorys (2009), CEPR (2013) and CEPII (2013). In the optimistic scenarios, a reduction of actionable NTMs of 50 % and 25 % (e.g. by CEPR) were typically assumed (see chapter 2.4.2 for details).

[16] We should note that it remains unclear to us, how the survey manages to extract answers from respondents on regulatory divergence given the questions it asked. In our judgement, the latter only allows to establish overall restrictiveness levels (see Question A12a in Box 3.1., (Ecorys 2009, p10)).

Though we have a number of reservations with regard to the details of the methodology (see chapter 2.4.2 for a discussion), our concern here relates to the methodological approach in more general terms. First and foremost, the Ecorys study implicitly assumes that a substantial dismantling and alignment of NTMs between the EU and the US is possible without a change to the regulatory quality, i.e. the ability of a certain regulation or standard to safeguard a defined public policy goal. Only upon that basis, Ecorys is able to restrict itself to estimating the savings to companies because of NTM removal, while completely neglecting the social costs concomitant with that removal. Consequently, it arrives at in general small, but positive economic gains.

Overall, we think that using such an approach is not warranted, given that the Ecorys study derives very high gains from regulatory alignment in exactly those sectors – e.g. chemicals, cosmetics and pharmaceuticals, or food and beverages –, where substantial and partly incommensurable differences in regulatory approaches and standards between the EU and US exist. Any dismantling must have an effect on regulatory standards and thus infer a cost upon that society, which ends up with a lowered standard. In general, it must be recognized that a change in a standard will always alter the distribution of costs and benefits between social actors, e.g. between firms and consumers. Alternatively, also firms might be unevenly affected by regulatory change, the latter might e.g. favour big companies, while inferring an additional burden on small companies.

Undoubtedly, NTM dismantling will make sense in some cases, e.g. because the dismantled regulation has proven ineffective in serving a particular public policy goal, or continues to exist for purely historical reasons (e.g. differing track gauges between national railway systems). This may be true in individual cases, but must not be assumed as a general rule. Typically, regulations serve a public policy goal. If that regulation is changed – either dismantled or aligned to some other standard, its effectiveness in serving the public policy goal will eventually be affected. This might infer a social benefit, if the new standard is higher than the old one, or a social loss, if the new standard is lower than the old one or has been eliminated without substitution. The latter case is obviously the focus of the Ecorys study. Though without doubt difficult, the study does not make any effort to quantify social losses, but exclusively looks at the benefits of NTM reductions to companies and the economy. Social losses might come in the form of temporary adjustment costs, e.g. for harmonising and implementing legislation, or be of a long-term nature to society, e.g. if standards for poisonous chemicals were relaxed and resulted in higher public health costs because of a higher incidence of allergies amongst the population. This non-consideration of social costs is especially problematic, since the study estimates the trade cost reductions of TTIP to be particularly high in sensitive sectors such as chemicals, pharmaceuticals and cosmetics, food and beverages, or automotives (see Ecorys 2009, Table 4.2, p23). Thus, in order to arrive at its optimistic welfare estimations, strong reductions/alignments of NTMs in precisely those sectors are necessary, where the safeguarding of public policy goals is perhaps most crucial. For instance, above average actionability levels were chosen for the sectors chemicals, cosmetics, food & beverages (see Ecorys 2009, Table 3.3, p16).

Not surprisingly, the overall welfare effect, which is computed by the CGE simulations, is very sensitive to the assumed actionability level. The higher actionability of NTMs, the higher the welfare gains. Actionability is defined as "the degree to which an NTM or regulatory divergence can potentially be reduced (through various methods) by 2018, *given that the political will exists to address the divergence*

identified' (Ecorys 2009, p15, *emphasis added*). Actionability thus depends on political will, which however is assumed as given. This definition is highly problematic, since the political process is effectively assumed away, and substituted for by an ad-hoc assessment of a sample of mostly business-related experts, which we would suspect exhibit a certain tendency to overestimate actionability. Thus, the determination of actionability levels is basically a more or less sophisticated guess of a group of persons with vested interests, and is not grounded on any kind of robust methodology.

This bias in the selection of respondents is clearly visible in the study. The study has primarily asked firms (5,500 in business survey) and business associations in the EU with regard to the restrictiveness of US regulations and vice versa. One should however suppose that firms and business associations have a tendency to overestimate the cost of complying with foreign standards, since they want to lower the cost of doing business abroad, and thus have a vested interest. In order to counter-balance this and increase the robustness of results, at the very least, one should have also asked US firms on their assessment of the cost of complying with US regulations, and EU firms on EU regulations. In addition, one might have asked experts with diverse professional backgrounds, e.g. people representing labor interests, consumers, human rights groups etc. for their assessment.

In terms of the robustness of its results, the study states that it has cross-checked its restrictiveness estimates with other existing measures, in particular the OECD FDI restrictiveness index (Ecorys 2009, p16). However, cross-checking the Ecorys NTM indexes with the OECD FDI restrictiveness index amounts to comparing apples with peaches. The latter focuses on four specific types of discriminatory measures: equity restrictions, screening and approval requirements, restrictions on foreign key personnel, and other operational restrictions – such as limits on purchase of land or on repatriation of profits and capital (Kalinova/Palerm/Thomsen 2010). Though there may be partial overlaps, the two indices essentially refer to different types of measures: while the Ecorys NTM indexes refer mostly to behind the border measures, which typically are not discriminatory, the FDI restrictiveness index refers primarily to specific types of discriminatory measures. In sum, it is questionable, whether the FDI restrictiveness index is a suitable vehicle for a robustness check of Ecorys' NTM indexes.

Also, the magnitude of income effects from NTM reductions in the Ecorys study is inflated by a factor of four for the EU and three for the US, by assuming that NTMs will not be aligned sector by sector, but economy-wide, i.e. reductions of NTMs in all sectors of the EU and US economies will occur simultaneously (Ecorys 2009, p27). This multiplication is justified on the grounds of sector inter-linkages, i.e. cost savings from NTM alignments, which are passed on to other sectors and thus reduce input costs and prices of end products. Similarly, the simultaneous reduction of NTMs across all sectors has a strong effect on output and exports, and investment in the affected sectors is expected to increase. We do not dispute that sector-linkages have a role to play. If, however, one makes the more realistic assumption that as a result of the TTIP negotiations NTM reductions/alignments will occur only in a subset of sectors – i.e. in some sectors, while not in others, because of e.g. national security or consumer protection reasons – the effects on income, output and exports will shrink substantially, as mentioned in chapter 2.1.

By way of summarizing, we would posit that the four scrutinized studies have largely neglected a careful analysis of adjustment costs and the social costs of regulatory change. While to some extent this can be explained by the biases of applied theoretical framework, it must be stressed that in particular adjustment

costs relating to the EU budget and labour market policies (retraining, unemployment benefits) will be substantial, and need to be dealt with at the political level. The social costs of regulatory change are by their very nature difficult, if not impossible to quantify. Nevertheless, they can be very large and thus require careful analysis, in particular in those areas where they relate to public security & health as well as environmental safety. It should also be stressed that a methodological approach for such an impact analysis is needed, that is characterized by inter-disciplinarity and the participation of all affected stakeholders. Last but not least, an investor-to-state dispute settlement mechanism (see Eberhardt in this volume), if included in TTIP, could lead to compensation payments by governments and have a disciplining effect on future regulation in the public interest.

2.3. Lessons from Other Trade Liberalizations: NAFTA

Much of the discussion about TTIP focused on the possible effects on welfare and employment. Supporters of TTIP typically dismiss opposing arguments by highlighting that trade liberalization promotes the general welfare of society. This is frequently supported by commissioned research. Within the EU, the European Commission, in particular DG Trade, regularly uses commissioned studies demonstrating the positive effects of trade liberalization in order to support its proposals to initiate new negotiations on Free Trade Agreements. With regard to TTIP, for instance, Trade Commissioner Karel de Gucht frequently refers to the CEPR study and its alluring promise of an increase of €545 in the annual disposable income per household in the EU. This strategy is not new and has been applied in many similar instances in the past. Before the North American Free Trade Agreement (NAFTA) came into force 20 years ago in 1994, a campaign with a wide array of promises was launched under the headline of the promotion of growth and the creation of new jobs. President Bill Clinton argued on the basis of an optimistic interpretation of studies conducted by Hufbauer and Schott (1992, 1993), that NAFTA would result in boosting employment in the US by creating a net gain of 200,000 jobs within two years (Hufbauer/Schott 2005, p8).

Even though estimation techniques may have evolved to a more sophisticated level, the basic principle of simulating an uncertain future on the basis of questionable assumptions has endured. In this section, we will use the show-case example of NAFTA in order to argue that ex-ante projections of the impact of NAFTA had a tendency to overestimate welfare, wage and employment effects. Furthermore, nearly all ex-ante studies completely ignored that workers had to pay the vast bulk of adjustment costs. With respect to the current debate on TTIP, it is evident that ex-ante projections again play a crucial role in justifying trade liberalization and thus should be treated with the appropriate skepticism. Scrutinizing the scientific debate on NAFTA should thus serve as a cautionary tale for the on-going TTIP discussion.

The objective of this section is to examine the accurateness of ex-ante studies that presented projections on the economic impact of NAFTA. It is *not* the primary task to examine the methodology of the studies. Instead we try to draw a picture of possible differences between ex-ante projections and ex-post evaluations on the impact of NAFTA. The literature on the effects of NAFTA is extensive, thus we cannot claim completeness. Our analysis will nonetheless capture the general tendencies that emerged from some of the most widely cited studies.

Whereas forecasting methods rely mainly on CGE models, various approaches have been used to assess the actual impact of NAFTA. Most ex-post studies apply qualitative and quantitative research, as well as econometric analysis. The major limitation of ex-ante projections is their basis: shaky assumptions, in particular with regard to the results of the negotiations. On the other hand, ex-post evaluations suffer foremost from the very difficult task of distinguishing between what happened *since* NAFTA and what happened *because of* NAFTA. The quality of results varies widely, since not all studies pay the attention necessary to these issues. For this reason, all presented results should be interpreted with caution**.** Another important matter is the difference between the scenarios as defined for the purpose of CGE modeling and the actually concluded trade agreement. Regarding tariffs, ex-ante simulations generally modeled the abolishment of all tariffs. These scenarios are roughly in line with NAFTA regulations, despite a few minor exceptions. Even though NAFTA was not fully implemented until 2008, most provisions were already put into effect around the millennium. Ex-ante simulations commonly also included NTMs and foreign direct investment (FDI). Because NAFTA did include a wide array of directives regarding the reductions of NTMs, CGE simulations accounting for the impact of NTMs should be included in our survey. Furthermore, NAFTA also covered the interests of foreign investors by applying national treatment, and by introducing investor to state dispute settlement (NAFTA 1992; Hufbauer/Schott 1993, 2005). Since the Canadian-US Free Trade Agreement (CUFTA) was already in place and Mexico had implemented comprehensive trade liberalization measures in the 1980s, Pacheco-López and Thirlwall (2004) believe the major effect of NAFTA to be on FDI. For this reason we also need to include ex-ante FDI scenarios in our comparison.

2.3.1. Ex-ante Projections of Real GDP, Real Wages and Employment

In this section we will try to assess the overall tendencies of ex-ante projections for NAFTA. A summary on the basis of 11 studies and 22 different experiments is presented in Table 6 and Figure 7. Further information on the cited studies is presented in Table 7. All results are based at least on tariff elimination. In addition, some studies include NTM reductions and a few FDI flows. Taking into account the actual importance of NTMs and FDI in the NAFTA agreement, some of the defined ex-ante scenarios do not seem to capture the full scope of NAFTA and therefore should present relatively conservative estimations, while more comprehensive scenarios should represent the concluded agreement in a more adequate manner.

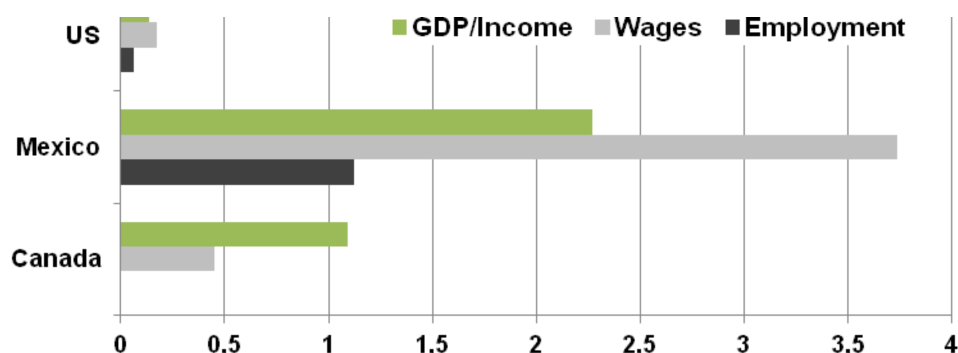
Ex-ante projections of real GDP and national income were relatively homogeneous. For the US, NAFTA was expected to have only a small positive impact. Most predictions range between 0.1 % and 0.3 % real GDP growth as a result of NAFTA (Table 7). For Mexico, the expectations were more optimistic. Including NTMs in the scenarios, most studies projected real GDP growth well above 2 %. The consideration of FDI raised impact projections for NAFTA even further. To illustrate, Brown, Deardorff and Stern (1992) calculated a GDP gain of 5 % and Hinojosa-Ojeda and Robinson (1991) an increase of 6.4 % when including tariffs, NTBs and FDI in their experiments. Overall, we find a median of 0.14 % GDP growth for the US, 2.27 % for Mexico and 1.1 % for Canada (Figure 7).[17]

[17] By analyzing results of studies surveyed by the US International Trade Commission, Baldwin and Venables (1995) present a median of 0.16 % GDP growth for the US, 2.5 % for Mexico and 3.26 % for Canada.

The effects of NAFTA on real wages were expected to be positive for all three countries. The smallest impact was calculated for the US, generally projecting no more than 0.2 % of real wage growth. For Mexico, the estimated wage gains were enormous – also depending mainly on the inclusion of FDI in the CGE experiments. Whereas calculations without increasing FDI inflows as a result of NAFTA projected an impact of below 1 %, FDI would boost expectations for real wage growth in Mexico on the order of 6 – 9 % (Table 7). The most optimistic projection was given by Sobarzo (1991), presenting an impact of 16.2 % by holding employment fixed. For Canada, the limited literature shows relatively small gains of 0.4 – 0.5 % in the case of Brown, Deardorff and Stern (1992) and relatively large gains of 1.3 % in the case of Cox and Harris (1992).

Even though expected employment gains were used as the major sales argument in the US, ex-ante projections did not necessarily support this on a broad basis. The often cited free-trade advocates Hufbauer and Schott (1992, 1993) calculated a net gain of 130,000 to 170,000 jobs due to NAFTA, to materialize within a few years. DRI/McGraw-Hill (1992) expected an *annual* growth of 160,000 to 221,000 jobs in the US (1993-2000). Roland-Holst, Reinert and Shiells (1994) projected an increase between 0.08 % and 2.47 % in employment – depending on the set of assumptions (Table 7). Nonetheless, most studies did not expect a meaningful impact on the US labor market (O'Leary/Eberts/Pittelko 2012). For Mexico, expectations were however high. Most notably, the studies of KPMG Marwick (1991), Sobarzo (1991) and Roland-Holst, Reinert and Shiells (1994) calculated employment gains between 2.4 % and 6.6 %.

Figure 7: Results of ex-ante simulations for NAFTA



Sources: Francois/Shiells 1992: Table 2a, 2b, 2c; Brown/Deardorff/Stern 1992: Table 1, 2; CBO 1992
Median change in %; Own calculations based on 11 studies and 22 different experiments. Not sufficient data for Canadian employment available. Data on real GDP/income reflects GDP except for two experiments.

Table 6: Simulation results of most cited ex-ante studies

	United States	Mexico	Canada
Real GDP	0.0 to 2.07	-0.35 to 11.39	0.12 to 10.57
Real wages	-0.7 to 0.95*	0.4* to 16.2	0.04 to 1.3**
Employment	-0.3 to 2.47	-0.1 to 6.6	0.61 to 11.02

Source: extended table of Brookhart et al. 1993: Table 2-1; see also Francois/Shiells 1992: Table 2a, 2b, 2c and Brown/Deardorff/Stern 1992: Table 1, 2. For more specific information about most of the here considered studies see Table 7. In %; Summary based on 11 studies and 22 different experiments. *unweighted average of four different job classifications, **comparison base is the impact of the Canadian-US Free Trade Agreement.

2.3.2. Ex-post Evaluations on Real GDP, Real Wages and Employment

The impact of NAFTA on real GDP and welfare as evaluated by ex-post studies seems to be significantly lower than expected by ex-ante projections, even though the literature is not extensive. Caliendo and Parro (2014) estimated an impact on welfare between 1993 and 2005 due to NAFTA tariff reductions to 0.08 % for the US, 1.31 % for Mexico and -0.06 % for Canada. This is by far the most optimistic estimate and is already well below most ex-ante expectations. A study conducted by the Congressional Budget Office (2003) estimates the annual impact of NAFTA on US-GDP to be between 0.001 – 0.005 % in 1994 and between 0.006 – 0.042 % in 2001. Similarly, the US International Trade Commission (Okun et al. 2003, p332) finds the effect of NAFTA on US-welfare to be negligible. A World Bank study (Lederman/Maloney/Serven 2003) quantifies the increase of Mexican GDP per capita as a result of NAFTA to be at 4 – 5 % until 2002. Weisbrot, Rosnick and Baker (2004) show that the data used in the World Bank model is biased. By using the same model as the World Bank study with reasonable data, they find that NAFTA actually slowed the growth rate for Mexico. Along the same lines, Romalis (2007) discovers no effect of NAFTA on US and Canadian GDP, but a decrease of 0.3 % in Mexican GDP.

After NAFTA came into effect, real wages in member countries were either stagnating, or – as in the case of Mexico due to the peso-crisis – decreasing (Polaski 2006). While this development occurred *since* NAFTA, it cannot be automatically attributed *to* NAFTA. Caliendo and Parro (2014) believe the impact of NAFTA tariff reductions on real wages between 1993 and 2005 to be positive for the US (0.11 %), Mexico (1.72 %) and Canada (0.32 %). Again, this study is relatively optimistic. Polaski (2006) attributes the decoupling of productivity growth from wages in the US and Mexico to the decreasing bargaining power of labor unions as a result of FTAs. A study on plant-closing threats in connection with NAFTA conducted by Bronfenbrenner (2000) supports this idea. McLaren and Hakobyan (2010) show that wage growth for workers in US-industries affected by NAFTA was substantially lower. Waldkirch (2008) believes that increased FDI inflows as a result of NAFTA raised productivity in Mexico, but FDI's *"[...] effect on average compensation per worker is negative or zero at best"* (p3). Hanson (2003) finds that NAFTA contributed to rising income inequality in Mexico, with an unknown effect on the general wage level. Wage growth for high skilled workers and workers in the north with exposure to foreign markets and FDI turned out to be significantly higher than for unskilled workers and workers in the south. Generally, the link between increasing income inequality and NAFTA seems to be widely accepted

(Abbott 2004, p12ff.). As a conclusion, most ex-post evaluations do not find a noteworthy positive effect of NAFTA on real wages – quite to the opposite. The few studies that do find a positive impact still cannot fulfill the big promises announced by ex-ante assessments (Figure 7).

Because the political discussion prior to the implementation of NAFTA focused especially on employment, the discussion on the actual impact of NAFTA has been heated. Nonetheless, the broad consensus is that expectations were not confirmed. Even the free-trade advocates Hufbauer and Schott, who's results were widely referred to before 1994, seem to have lost faith, stating that *"[...] NAFTA is no more than a blip on US employment picture"* (Hufbauer/Schott 2007, p85). Furthermore, the general discussion shifted from ex-ante projections trying to assess the job gains induced by NAFTA, to ex-post evaluations focusing on the question of net losses. Scott (2011) believes that 682,900 jobs in the US were displaced between 1994 and 2010 as a result of the NAFTA related trade deficit with Mexico. In his simple calculation, 791,900 jobs were created by US exports to Mexico and 1,474,800 jobs were lost due to US imports from Mexico. Kletzer (2002) estimates that the US lost 1,238,593 jobs due to NAFTA related imports, accounting for 24-27 % of manufacturing job losses and 10.7 % of total job losses between 1993 and 1999. Hinojosa-Ojeda et al. (2000) concludes that 94,000 jobs in the US were "*put at risk*" every year due to NAFTA-related imports (Data: 1990-1997). A highly recognized estimate for US job losses is presented by the Trade Adjustment Assistance (TAA), an institution implemented to absorb negative effects of free-trade related job displacement. Data from the NAFTA-TAA suggests that a minimum of 845,000 US workers were displaced due to increased imports from Canada and Mexico since 1994 (Public Citizen 2014). For Mexico, one would expect more positive estimates due to the longer lasting trade surplus with the US, but this is not the case. Polaski (2006) finds that NAFTA has only produced a disappointingly small net gain in jobs: *"Data limitations preclude an exact tally, but it is clear that jobs created in export manufacturing have barely kept pace with jobs lost in agriculture due to imports"* (p1). Polaski believes that increasing productivity is a major job killer in Mexico (p1ff.). Salas (2006) concludes that approximately one-sixth of the Mexican population with jobs in the agricultural sector got displaced since the beginning of the 1990s – in part as a result of NAFTA. The biggest loss occurred in the corn production sector, accounting for 1,013,000 displaced jobs. Salas (2006, p49) also notes that FDI inflows into Mexico have grown significantly since NAFTA, but that these were mostly used to purchase existing assets and thus did not affect the real economy as much as was hoped.[18] This is particularly interesting since the highly optimistic ex-ante projections for Mexico were mainly an outcome of FDI flows.

In sum, our review of the available literature suggests that a significant gap exists between ex-ante projections and ex-post evaluations with regard to NAFTA's effects on GDP, wages and employment. Most ex-ante models had a tendency to overestimate the benefits and underestimate the costs of free-trade. Even though estimation techniques may have evolved to a more sophisticated level during the last two decades, the basic impact assessment methodology for trade liberalization has remained largely unchanged. Policy makers should thus treat the results of ex-ante projections on TTIP with the appropriate skepticism.

[18] Nonetheless, Waldkirch (2008) finds a connection between non-maquiladora FDI and productivity increases in Mexico.

2.4. Technical Critique of TTIP Impact Assessment Studies

2.4.1. Origins and Development

One can think of the origins of the various models along two different lines. One retraces the academic discourse from Ricardo's comparative advantage to today's theoretical trade models. The other – necessarily intertwined – strand retraces the development of the applied trade policy models that are put forth in debates such as this one regarding TTIP.

Let us briefly consider theoretical developments first. Ricardo's (1817) theory of comparative advantage states that countries can mutually gain from trade by specializing in the production of the goods at which they are relatively proficient. Gains materialize even if one country is less efficient in the production of any of the goods than all other countries. In all countries, average productivity rises with specialization in the *relatively* more productive sectors. Hence, the gains from trade arise from technological differences – from differences in labor productivity. The Heckscher-Ohlin trade model introduces capital as a second factor. The gains from trade are then driven by factor endowments: the relatively capital abundant country exports capital intensive goods, and imports labor-intensive goods. Still, differences in factor endowments determine patterns of comparative advantage, which drive changes in productivity and, consequently, *prices*. With this crucial extension, the theory of comparative advantage predicts trade between developed and developing economies, as the former are relatively capital abundant, the latter relatively capital scarce. These trades are "machines for t-shirts," meaning inter-industry trade. While trade does occur along these lines, the vast majority of trade occurs between relatively capital abundant countries, trading "cars for cars," meaning intra-industry trade.

The introduction of imperfection competition, scale economies and "love for variety" addressed this puzzle. Firms in an industry with imperfect competition have market power and can charge prices in excess of marginal costs, thus extracting economic profits. Average costs of these firms are falling, which implies that efficiency increases with output. Crucially, a firm's output is a *differentiated product*, so that it is, however marginally, different from a competitor's product – think of a Samsung versus Sony flat screen TV. The last piece of the puzzle is that consumers' value variety: the more such products to choose from, the higher is the consumer's "utility."[19] Now suppose a firm gains access to a new market, and demand for its product increases. Costs, and, in consequence, prices decrease – again driving the gains from trade.

The market structure underlying this model is monopolistic competition. The assumption of monopolistic competition is convenient because it means that firms behave as if they had a monopoly, while their products, though differentiated, are (imperfect) substitutes. This precludes strategic interaction, but maintains pricing power, falling average costs, and explains intra-industry trade. Adam Smith was an early proponent of this type of trade. The modern reformulation is commonly attributed to Krugman (1979, 1980) and Helpman (Helpman and Krugman 1985).

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[19] These are *Dixit-Stiglitz preferences*, following Dixit and Stiglitz (1977).

Table 7: Summary of most cited ex-ante CGE studies on NAFTA

Sources: Original studies; CBO 1992; Francois/Shiells 1992: Table 2a, 2b, 2c; Brown/Deardorff/Stern 1992: Table 1

Summary of most cited ex-ante CGE studies											
Author, Year	**Metho-dology**	**Experi-ment**	**Key Findings**								
			Real GDP / Real Income			**Wages**			**Employment**		
			US	***MEX***	***CAN***	***US***	***MEX***	***CAN***	***US***	***MEX***	***CAN***
Brown, Deardorff and Stern, 1992	IRS, Static, IC	2	0.1	1.6	0.7	0.2	0.7	0.4	-	-	-
		3	0.3	5	0.7	0.2	9.3	0.5	-	-	-
KPMG Peat Marwick, 1991	CRS, Static, PC	2	0.02	0.3	-	0.02	-	-	-	0.9	-
		3	0.04	4.6	-	0.03	-	-	-	6.6	-
Hinojosa-Ojeda and Robinson, 1991	CRS, Static, PC	2	0	0.3	-	0.175*	0.4*	-	-	-	-
		3	0.1	6.4	-	0.175*	8.65*	-	-	-	-
		4	0.1	6.8	-	0.95*	6.55*	-	-	-	-
Roland-Holst, Reinert and Shiells, 1994	CRS, Static, PC	1	0.06	0.13	0.38	-	-	-	0.08	0.33	0.61
		2	1.34	2.27	7.22	-	-	-	1.88	1.49	8.96
	IRS, Static, IC	2a	1.3	2.57	5.82	-	-	-	1.79	1.73	7.29
		2b	2.07	3.38	10.57	-	-	-	2.47	2.4	11.02
Cox and Harris, 1992	IRS, Static, IC	1c	-	-	1.49**	-	-	1.3**	-	-	-
Sobarzo, 1991	IRS, Static, IC	1d	-	1.7	-	-	-	-	-	5.1	-
		1e	-	1.9	-	-	-	-	-	5.8	-
		1f	-	8	-	-	16.2	-	-	-	-
McCleery, 1992	CRS, Dynamic, PC	2	0.22	0.01	-	-	-	-	-	-	-
		3	0.32	3.09	-	-	-	-	-	-	-
		3g	0.51	11.39	-	-	-	-	-	-	-
Young and Romero, 1992	CRS, Dynamic, PC	1h	-	2.6	-	-	-	-	-	-	-
		1i	-	8.1	-	-	-	-	-	-	-

(1) = Tariff abolishment, (2) = 1 + NTM reductions, (3) = 2 + and FDI/capital flows, (4) = 3 + labor migration; (a) = Cournot competition, (b) = Contestable markets, (c) = comparison base is the impact of CUFTA, (d) = fixed wage, capital stock and trade balance, (e) = fixed wage, capital stock and exchange rate, (f) = fixed employment and exchange rate, international mobile capital, (g) = endogenous productivity, (h) = fixed interest rates at 10 % in Mexico, (i) = interest rates fall to 7,5 % in Mexico; CRS = Constant return to scales, IRS = Increasing return to scales, IC = Imperfect competition, PC = Perfect competition; *unweighted average of four different job classifications. See Francois/Shiells (1992) for a more detailed discussion of the models.

More recent developments focus on firm heterogeneity. Important stylized facts in this context are that (1) firm populations in an industry have substantially differing productivity levels, and (2) that only the most productive firms in an industry export. In fact, the vast majority of international trade is conducted by a tiny minority of firms. Here, gains from trade liberalization reduce cost barriers for the firms "near the exporting threshold," which then see average costs falling, productivity rising, and prices falling. As low productivity firms exit the industry, average productivity rises – and prices fall, driving the gains from trade.[20]

[20] See Melitz (2003) as well as Bernard et al. (2003) for important theoretical contributions. Bernard et al. (2007) provides a survey. The BWMT/ifo study includes firm heterogeneity; and is discussed in more detail in chapter 2.4.4.

These theoretical models are *general equilibrium models*. In their various guises, they assume that agents are able to calculate and obtain their optimal economic allocations: firms maximize profits subject to costs and market structure, and households maximize utility subject to their budget (and time) constraint. The resulting equilibrium *maximizes welfare*, in the sense that nobody (or no group) could be made better off without making somebody else (or some other group) worse off. Two issues are relevant here.

First, the theory of general equilibrium has been in shambles for a while. One important issue relates to the so-called *Sonnenschein-Mantel-Debreu* (SMD) result. The SMD result is that individual rationality and "normal" preferences – such that demand decreases when the price increases – do not imply such a demand function in the aggregate. In consequence, there can be multiple equilibria, and they might not be stable. Further, a key assumption of general equilibrium theory is that all economic transactions are undertaken *at equilibrium prices*. If trades are made out of equilibrium, endowments change, which in turn change the not-quite-so-general equilibrium. These and other criticisms are raised within the bounds of the methodology of general equilibrium theory. One can, of course, go beyond that and consider the validity of assumptions. Among these, individual rationality is seen as a most unrealistic starting point. Despite all of these known problems associated with questionable assumptions and dead-end theorizing, standard trade models continue to build their analyses on the fairy tale of the welfare theorems (e.g. Mas-Colell/Whinston/Green 1995; critically: Syll 2014).

Second, when we proceed to an *applied CGE model* we inevitably move from the realm of pure microeconomic theory to a world where macroeconomic constraints matter. General equilibrium *theory* rests on a purely theoretical, idealized construct of individuals exchanging endowments. Theoreticians such as Arrow and Hahn therefore recognize that general equilibrium carries no meaning for real world analysis, but only provides a vision for what *the world would need to be like for the welfare theorems to matter*. In sharp contrast, applied CGE models describe firms and households and governments and consumption and investment – and, therefore, describe a *macroeconomy*. Invariably, the proponents of these models want to highlight and hold on to microeconomic theoretical foundations, rather than discuss the implicit macroeconomic narratives.[21]

It should further be noted that early versions of these policy models were decidedly not general equilibrium models. In this sense, the label *computable general equilibrium* model is a misnomer. Equilibria described by these models are general only in the sense that they satisfy all the accounting constraints of a macroeconomy, but are not general in the sense that they describe an optimal welfare allocation among microeconomic agents. For reviews of these and related issues, see Robinson (2003), Mitra-Kahn (2008) and Taylor (2011).

[21] For example, in a review of the model in CEPR (2013), it is argued that "[t]he CGE model used by CEPR is state-of-the-art. It needs to make assumptions about the economy in order to work but these are *as reasonable as possible to make it as close to the real world as possible*. For instance, it is able to account for the effects of economies of scale, different skill-levels of employees, imperfect competition between companies and many other features of the real world economy." (European Commission 2013b, p3-4, our emphasis) Note that all these 'reasonable' assumptions refer to *microeconomics*; no macroeconomic assumptions – full employment, balanced budget, etc. – are discussed.

2.4.2. The Quantification of Non-tariff Measures

Non-tariff measures (NTMs) are, as the name implies, impediments to trade *other than tariffs*. NTMs are one crucial – since potentially *actionable* – component of overall *trade costs*. NTMs can be regulations, laws, procedures, or safety standards – in short, any domestic policy measures that do affect trade flows.[22] Here we briefly introduce some of the key issues. In the following sections, we discuss trade costs more generally, as well as how the studies by Ecorys and Bertelsmann/ifo have addressed these issues.

To get started, note that the key idea behind NTM removal – as is the case with tariff removal – is to increase economic efficiency. Very often, macroeconomic processes and constraints complicate that simple sounding task. We will discuss NTMs, the models, and the reports through that lens, which means in turn that we will not focus on potential but fundamentally unknown costs to removal of NTMs. Specifically, consider genetically modified GMO foodstuffs. The US position is that current science suggests GMO food is safe. The European position is that precaution should be applied; and GMO food should not generally be approved. If there turn out to be downsides that 'current science' does not foresee, and costs arise, these would have to be added to the arguments against TTIP. None of the studies ventures into such terrain, and neither will we.

That said, how do NTMs differ from tariffs as they relate to the vaunted economic efficiency? Removal of NTMs is quite a different animal than tariff removal. Tariffs are a revenue generating policy instrument that affects firm costs. Historically, and still in some developing countries, tariffs are *the* prime source of revenue generation. Other than that, the purpose of tariffs is to provide a degree of protection to domestic firms. Removal changes costs, prices, government revenue and trade flows, and increases competition for domestic firms.[23]

NTMs, on the other hand, do not usually generate revenue, and their purpose is not necessarily to insulate domestic firms from competition, though that is certainly possible. For firms, NTMs can be cost increasing, or rent producing. NTMs produce rents if they restrict market access for foreign firms. These do insulate the domestic firm from competition, and enable it to charge higher prices. NTMs that increase costs are rather "like a tariff" for the foreign firm.

Let us consider examples to highlight these issues. One market access restricting NTM could be a quota for imports of genetically modified soy. Another market access restricting NTM would be a ban on genetically modified soy imports. A cost increasing NTM would be differing requirements for documentation of origin of genetically modified soy products. The quota and the ban produce rents, but presumably only the quota's purpose is to limit competition. Documentation requirements increase costs

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[22] Ecorys and Bertelsmann/ifo use slightly different definitions of NTMs. Ecorys considers NTMs as those policy measures affecting trade other than tariffs and quotas, while ifo lumps quotas into NTMs. ifo does as well label regulations affecting trade as "trade policy" (Bertelsmann/ifo 2013, p7). The 'gravity literature' usually considers as well inferred barriers associated with language, culture, and currency, among others, as NTMs. In this introduction, we focus on a broad conceptualization to motivate later, more detailed, discussions.

[23] Removal of policy measures is specifically relevant when they alter government revenues. These imply macroeconomic fiscal effects. As will be seen later, these need to be "assumed away" to maintain supply side determination of output.

"like a tariff," and thus reduce competition. Rather unlike a tariff, documentation requirements or a ban might be driven by cultural differences and difficult to overcome.[24]

These issues matter greatly in the estimation of potential benefits from NTM removal – since, in the first place, *the higher the estimated NTM to be removed, the higher the potential benefits*. Moreover, the larger the "removable" (or *actionable*, in Ecorys's terminology) share of the estimated NTM, the higher the potential benefits. Removable here means that one considers a (market access restricting or cost increasing) NTM to be potentially lowered or eliminated. In the above example, Europeans might not be willing to accept genetically modified soy imports, and instead prefer to pay slightly higher prices than otherwise for genetically unmodified soy.

It matters further whether barriers are cost or rent producing. Cost increasing NTMs represent a "welfare loss," in general equilibrium parlance, since the equilibrium without the distortion would be more efficient, or "pareto superior," to the equilibrium with the distortion. Rent producing NTMs, in contrast, lead to redistribution from consumers to producers, since the latters market power would be higher than without the distortion. All of this will be important further below when we discuss scenario design and simulations. Next, we discuss the estimation of *trade costs* in general.

Trade Costs

What are trade costs? Anderson and van Wincoop (2003, 2004; henceforth referred to as AVW) present estimation of trade costs and a detailed survey. Both Ecorys (Annex III, Section III.2.6, p208-210) and Bertelsmann/ifo (2013, p8) refer to these two papers as principal sources. That warrants a closer look. First, consider the following definition:

> *"Trade costs, broadly defined, include all costs incurred in getting a good to a final user other than the marginal cost of producing the good itself: transportation costs (both freight costs and time costs), policy barriers (tariffs and nontariff barriers), information costs, contract enforcement costs, costs associated with the use of different currencies, legal and regulatory costs, and local distribution costs (wholesale and retail)." AVW (2004, p691)*

This definition highlights the inherent problem in estimating trade costs: many components of these costs are unobservable. Even if they are in principle observable, data availability is spotty. In AVW's (2004, p693) words, "[t]he grossly incomplete and inaccurate information on policy barriers available to researchers is a scandal and a puzzle."

Regarding NTMs, a further difficulty arises: Where data is available, it concerns their *incidence* rather than their *restrictiveness*. In other words, and following "Jon Haveman's extensive work," (AVW 2004, p696), available data on NTMs provides sectoral coverage ratios by country. This work classifies NTMs narrowly defined as "basically price and quantity control measures and quality control measures, while broad coverage is the narrow classification plus threat measures related to antidumping." (AVW 2004, p699) Table 8 shows this narrow and broad measure for the US and EU, which puts the broad trade weighted coverage ratio at about 38 % of products for the US and 10 % of products for the EU. The large discrepancy between narrow and broad measures for both US and EU suggests that threat measures loom

[24] It should be noted that within the perverse logic of a general equilibrium model, the "cultural barriers" meant here could be overcome through compensation, or, more aptly maybe, bribes to the unwilling populations. One might ask them, "what's it worth to you?" and then arrange the relevant transfers. This is obviously quite different than the potential though unknowable future costs of experimentation with the world's gene pool discussed previously.

particularly large. Sectoral data reported in Table 4 of AVW (2004) further indicates that agriculture, food products, textiles & apparel and wood & wood products feature the highest coverage ratios.

Table 8: NTM coverage ratio

NTM	Narrow Ratio	Trade weighted	Broad Ratio	Trade weighted
EU	0.8	4.1	9.5	10.6
US	1.5	5.5	27.2	38.9

Source: Adapted from AVW (2004, p699, Table 3). We reproduce here the caption from AVW.
Notes: The data are from UNCTAD's TRAINS database (Haveman repackaging). The "narrow'' category includes, quantity, price, quality and advance payment NTBs, but does not include threat measures such as antidumping investigations and duties. The "broad'' category includes quantity, price, quality, advance payment and threat measures. The ratios are calculated based on six-digit HS categories.

What is the *tariff equivalent* of these measures? In other words, how much do these measures *restrict* trade? This question has been addressed in a variety of ways in "gravity equation" frameworks. The intuition of gravity trade models is straightforward, and borrows from physics: the closer two bodies are to each other, and the larger they are, the stronger is their gravitational pull towards each other. Gravity trade theory suggests that economies will trade more with each other if they are larger and closer. Size is measured by income, and the income elasticity is usually assumed to be one: 1 % growth in GDP leads to 1 % growth in imports. The closeness of economies is measured by their geographical distance. A variety of other variables are then employed to make this "closeness" more precise. Examples include a shared language, shared colonial history, and other socio-political factors, as well as whether they share a land border and the like.

The remaining key variable then is a product's *price*. Thus, controlling for economic size and a host of measures of "closeness," demand for a product depends on its relative price. This price variable contains a distribution factor: the same product will cost *p* in Austria, but *pt* in Texas. These distribution costs are labeled iceberg trade costs. The analogy is that floating the block of ice from Austria to Texas will lead to proportional melting; to deliver the whole product, Austria must send off a value of *pt*. Now, here lies the crux of the matter. Iceberg costs can be thought of as an index of all relevant trade costs, such as transportation costs *as well as costs driven by non-tariff measures*.

AVW (2003, p174) complain that "[t]he empirical literature [on gravity trade models] pays no more than lip service to theoretical justification." They derive a gravity equation from a theoretical general equilibrium model, which produces a standard gravity equation plus a term describing *multilateral resistance*. Thus, standard gravity presumes that a country pair's trade depends on their closeness, whereas augmented gravity presumes that a country pair's trade depends on their closeness *relative to all other countries, including itself*. As summarized in Bertelsmann/ifo (2013, p8), "[t]hey show that the trade costs within other pairs are important for making an accurate estimate of trade costs within a country pair. For example, how much geographical distance restrains trade between two countries also depends on the average distance of these two countries from their other trading partners." In AVW's (2004, p708) words, "[t]he main insight from the theory is that bilateral trade depends on the *relative* trade barriers."

So far, so theoretical, so good. In practice, unobservable trade costs must be proxied by observables: for the delivered price *pt*, a trade cost function must explain *t*. If *z* is a vector of observables – such as geographic distance, language, currency, NTMs, etc. – with *m* elements, the tax equivalent of trade barriers due to variable z_m can be approximated as $\frac{\lambda_m(z_m - 1)}{1 - \sigma}$, see AVW (2004, p713). Here, λ_m is the estimated coefficient and σ the elasticity of substitution. On this elasticity of substitution, the literature leads AVW (2004, p713) "to conclude that σ is likely to be in the range of five to ten."[25]

AVW present an overview of various routes to estimate the elasticity of substitution. One way – followed by Ecorys – is to interpret the tariff coefficient in the trade cost function as the elasticity of substitution. In this context, it is important to emphasize that the resulting estimate of the tariff equivalent of trade costs is quite sensitive to the estimate of the elasticity of substitution. Table 9 reports such sensitivity for elasticities ranging from 5 to 10. Simple averaging suggests, roughly, that a 1 % increase in the assumed elasticity of substitution implies a 1.2 % *decrease in the tariff equivalent of trade costs*.

Table 9: Tariff equivalents of trade costs, and their sensitivity to the assumed elasticity of substitution

	$= 5$	$= 8$	$= 10$
Head and Ries (2001)	97	47	35
AVW (2003)	91	46	35
Eaton and Kortum (2002)	123-174	58-78	43-57

Source: Adapted from AVW (2004, p717, Table 7). All three studies employ a gravity equation that includes multilateral resistance a la AVW. Head and Ries is based on disaggregated data; the other two on aggregated data. The sensitivity calculations have been made by AVW based on estimates reported in the respective papers.

Hence, the lower the assumed elasticity, the higher are the implied and potentially actionable trade barriers, and the higher are the potential gains from trade. This negative effect from high elasticities of substitution on gains from trade liberalization stands in contrast to a positive effect: the higher the trade (price) elasticities, the more strongly does demand react to changes in international prices following liberalization, and the more do countries benefit. Before we get into discussion of these matters, however, let us consider – finally – a decomposition of trade barriers:

> *"Direct evidence on border costs shows that tariff barriers are now low in most countries, on average (trade-weighted or arithmetic) less than 5 percent for rich countries [..]. Our overall representative estimate of policy barriers for industrialized countries (including nontariff barriers) is about 8 percent. Inferred border costs appear on average to dwarf the effect of tariff and nontariff policy barriers. An extremely rough breakdown of the 44-percent [estimate of border-related trade costs] is as follows: an 8-percent policy barrier, a 7-percent language barrier, a 14-percent currency barrier (from the use of different currencies), a 6-percent information cost barrier, and a 3-percent security barrier for rich countries." AVW (2004, p693)*

[25] It should be noted here that functional forms assumed play a significant role for the evaluation of elasticities. For example, in AVW (2003, 2004) – meaning the gravity estimations – as well as GTAP à la Francois – meaning the CGE model in Ecorys (2009) and CEPR (2013) – demand is *homothetic*. Homothetic preferences imply that expenditures shares are independent of income. Since demand patterns undergo structural changes as income rises, this is a problematic assumption. MIRAGE, in contrast, assumes that below a "first-tier Cobb-Douglas function, the preferences across sectors are represented by a LES-CES (Linear Expenditure System – Constant Elasticity of Substitution) function. Without excessive complexity, this allows to account for the evolution of the demand structure of each region as its income level changes. With this kind of utility function, the elasticity of substitution is constant only across the sectoral consumptions over and above a minimum level." (Decreux/Valin 2007, p9)

In other words, following AVW (and Haveman), and roughly speaking, NTMs add about 3 - 4 % to the price of a traded good or service between two industrialized countries. These 3 % correspond to about 7 % of total trade costs. Most crucially, nontariff policy barriers as identified in the authoritative paper all four here reviewed studies build on *are so small that significant gains from trade cannot be expected to materialize from their removal*. In the next section, we consider how Ecorys addressed this issue.

À la Ecorys

The Ecorys study makes two contributions: It provides estimates of actionable non-tariff measures (NTMs), and applies these to a CGE model to calculate potential benefits from TTIP to EU-US trade. The NTM estimates figure in three of the four studies reviewed here, so that we discuss the methodology in some detail. Let us begin with the definition of NTMs put forth by Ecorys (http://ntm.ecorys.com/):

> *"Non-Tariff Measures are defined as 'all non-price and non-quantity restrictions on trade in goods, services and investment, at federal and state level. This includes border measures (customs procedures, etc.) as well as behind-the-border measures flowing from domestic laws, regulations and practices' (Study Terms of Reference of the Study, p7). In other words, non-tariff measures and regulatory divergence are restrictions to trade in goods, services and investment at the federal or (member) state level." Ecorys (2009, p xiii)*[26]

Thus, Ecorys's definition of NTMs is quite different than the standard approaches discussed in AVW (2004). Quotas – usually a non tariff trade policy measure – are excluded, while domestic regulations and laws are included. As will be seen, Ecorys's estimates of NTMs across sectors are substantially larger than the ranges suggested in AVW – a result that appears to be driven by the different definition applied. Implicitly, this suggests that the gains from trade calculated based on Ecorys estimates squarely rest on *regulatory and legal convergence*, rather than border measures.

Indeed, it can be difficult to compare these various definitions of NTMs. In Anderson and van Wincoop (2004, p699), an NTM is "basically price and quantity control measures and quality control measures […] plus threat measures related to antidumping." In Ecorys (2009), NTMs include as well "behind-the-border measures flowing from domestic laws, regulations and practices." Surveyed firms might perceive this to be essentially *anything*. Figure 1 of Bertelsmann/ifo (2013, p7) illustrates the problem: NTMs related to *trade* policy are probably very small, NTMs related to "other policies" appear ill-defined.

Let us consider the methodology in more detail. Chapter 3 of the main report concerns the methodology applied (Ecorys 2009, p9-19). Crucially, Ecorys combined literature reviews, econometric analysis, business surveys, interviews with sector experts, and consulted existing indices on restrictions and regulations. The sectoral averages across results from these different methodologies is then interpreted as the relevant index of NTMs. Figure 3.1 in chapter 3 (p9) illustrates the procedure.[27] The business surveys and interviews are detailed in Annexes. The "actionability" of NTMs is assessed there, and we will revisit the question of actionability when we discuss scenario design.

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[26] Ecorys suggests here that NTMs exclude quantity restrictions, which presumably refers to quotas. There appears to be a contradiction with CEPR (2013, Box 1, p16), where explanation of Ecorys's NTM methodology includes the following statement: "[t]raditional NTBs, like import quotas, are an example where NTBs [restrict] market access." This is noteworthy since at least one author (J. Francois) worked on both studies. While it is not clear where the confusion lies, quotas probably do not play a large role in US-EU trade.

[27] Note that Figure 3.1 presents NTMs as a percentage of trade costs. (If these are representative for estimation results, Ecorys's NTMs might be up to three times larger than those suggested by AVW.) In contrast, as will be discussed further below, Annex III outlines how NTM estimates are translated into a "tariff-equivalent" cost. In the CGE model, reduction of these tariff equivalent costs represents the liberalization policy.

According to Ecorys (2013, Annex VI, p250), the survey results "show us the *perception* of firms on both sides of the Atlantic as well as from third countries regarding the overall levels of restrictiveness (we recall Question 12a of the survey) in terms of NTMs and regulatory divergence of systems that they feel they face."[28] The emphasis is theirs – the business survey appears to have been designed to take firms' pulse on how difficult they feel it is to export (or invest) in a foreign country. Question 12a:

> *"Question A12a. Consider exporting to the US (EU), keeping in mind your domestic market. If 0 represents a completely 'free trade' environment, and 100 represents an entirely closed market due to NTMs, what value between 0 – 100 would you use to describe the overall level of restrictiveness of the US (EU) market to your export product (service) in this sector?" Ecorys (2009, p10)*

Thus, firms answers to this question produce an index, which then feeds into the econometrics. That is interesting, but it seems as well *very different* than measuring NTMs as they are traditionally – by Anderson and van Wincoop or Havemann – conceived of. Specifically, it is unclear whether respondents had a somewhat uniform or "correct" understanding of what question 12a meant by NTMs. It did certainly not mean language or cultural or currency barriers. That respondent's answers imply much higher NTMs than traditional observation of actual border measures in place – see the following paragraphs –suggests that firms might possibly have misunderstood the question. Alternatively, one might surmise that Ecorys's design of the survey is questionable.

That said, let us now take a look at what the index leads to in Ecorys's gravity estimation. Annex III, titled "Detailed methodology," explicates the econometric techniques used. As mentioned above, the econometric methodology directly builds on AVW (2003, 2004). Annex III details the derivation of the tariff equivalent, taking NAFTA and EU internal trade into account. Based on that, Table 4.2 (Ecorys 2009, p23) reports the trade costs for US exports to the EU and EU exports to the US attributable to NTMs. Table III.1 in Annex III.3 CGE Tables, page 214, lists the same and includes as well the "estimated price elasticities," which are derived from the tariff coefficient. The second and third column show, respectively, the calculated tariff equivalent of NTMs for exports from and to the US, which is based on the elasticity of substitution and the NTM indexes derived from business surveys (etc). The last row – not in the original – shows a simple average across the column, as we do not have sectoral weights of this disaggregation. These averages for both exports from and to the US round to seventeen, which is *a multiple of the three percent discussed in AVW (2004)*.

In summary, while Ecorys (2009) builds on state-of-the-art methodology regarding the estimation of the gravity framework, the NTM variable that enters the regression appears to differ significantly from the "standard" NTM measure. Considerable effort has gone into the business survey to construct these new measures of restrictiveness. Nevertheless, it is difficult to ascertain that Ecorys's conceptualization does not introduce an upward bias: the higher the estimated NTMs, the higher the potential benefits from its reduction. As will be seen, Ecorys considers roughly 50 % of NTMs "actionable," and feeds this policy change into a CGE model. Below, we dissect the CGE.

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[28] The "Summary of the Business Survey Results" on http://ntm.ecorys.com/ is unaivalable for download (2/20/14). In response to email requests, Dr. Koen Berden from Ecorys confirmed that *only question 12a* was used in the NTM indexes applied in the regressions.

2.4.3. Two CGE Models, a Common Heritage: GTAP and MIRAGE

In this section we discuss the two computable general equilibrium (CGE) models used for simulations. As mentioned in the introduction, Ecorys (2009) and CEPR (2013) use the same model, which is based on GTAP. Joseph Francois, an expert on neoclassical CGE models and a key figure in the GTAP research community, is the main author for both reports as far as the CGE models are concerned. The second model, applied by CEPII (2013) as well as BMWT/ifo (2013, chapter IV), is called MIRAGE.

MIRAGE is in principle quite similar to GTAP, but differs in some details. The key common features are nested production and demand structures, with some differences in the specification of imperfect competition and the product varieties available. These differences are, overall, quite marginal. As has been documented elsewhere, what really matters for the results a model produces are its *closures*. Essentially, the macroeconomic accounting restrictions that must be imposed on any economy-wide model leave few degrees of freedom available for additional 'behavioral' assumptions. Making these assumptions determines which variables are exogenous, which endogenous, and how these are determined – thus, how the model is "closed."

These closures, in turn, are informed by the analyst's view of the world. Put differently, the closures represent what the analyst considers to be *defensible and reasonable assumptions*. To try an analogy: while speed, comfort, and gas efficiency of different cars varies widely, you will ultimately end up where you decided to drive to independently of the car you took. In that sense and for the purposes of this review we will focus on closures. Further below, we consider elasticities and scenarios.

GTAP

Let us begin with GTAP à la Joseph Francois. This is the model used in Ecorys (2009) and CEPR (2013). Ecorys (2009) provides technical detail only on the general equilibrium model that underlies the gravity estimation; this was discussed in a previous section.[29] For details on closures, we therefore rely on CEPR (2013), Annex 2, and selected background papers. Key among these are Francois, McDonald and Nordstrom (1996) and Francois, van Meijl and van Tongeren (2005).[30] Both offer relevant insights, and we will let the latter get us started:

> *"The theoretical backbone of the model is the standard textbook Helpman-Krugman model that combines elements of the 'new' trade theory that emphasizes increasing returns and imperfect competition with elements of the 'old' trade theory that stresses factor endowment and technology differences. […] In all regions there is a single representative, composite household in each region, with expenditures allocated over personal consumption and savings (future consumption) and over government expenditures. The composite household owns endowments of the factors of production and receives income by selling them to firms. It also receives income from tariff revenue and rents accruing from import/export quota licences (when applicable). Part of the income is distributed as subsidy payments to some sectors, primarily in agriculture. […]*

[29] Ecorys (2009) suggests in Annex III.2, p203, that "[t]hese estimated partial effects can then be employed in various computable general equilibrium (CGE) economic models to determine the overall gross domestic product (GDP) and economic welfare effects of the elimination of Transatlantic (EU-US) nontariff barriers. CGE models allow for feedback effects on this flow of other variables and behavior in the two countries and the rest-of-the-world (ROW) to generate a 'general equilibrium' impact." Ecorys (2009) offers no further documentation of the model used. Joseph Francois has confirmed in email communications that Ecorys (2009) and CEPR (2013) employ the same model. CEPR (2013) includes a technical Annex 2. Further, Joseph Francois maintains a website that catalogs model versions, see http://www.i4ide.org/people/~francois/Models/index.htm. He has helped us through the maze on several occasions.

[30] A wealth of material on the core of the GTAP model is available on https://www.gtap.agecon.purdue.edu/. Francois, Manchin and Martin (2013) is particularly relevant for the imperfect competition market structure, which is not our key concern.

And further:

> *"On the production side, in all sectors, firms employ domestic production factors (capital, labour and land) and intermediate inputs from domestic and foreign sources to produce outputs in the most cost-efficient way that technology allows. Perfect competition is assumed in the agricultural sectors [… and in …] these sectors, products from different regions are assumed to be imperfect substitutes in accordance with the so-called 'Armington' assumption. […] Prices on goods and factors adjust until all markets are simultaneously in (general) equilibrium. This means that we solve for equilibriums in which all markets clear. […] We model manufacturing and services as involving imperfect competition. The approach followed involves monopolistic competition, [… which …] involves scale economies that are internal to each firm, depending on its own production level." Francois et al. (2005, p362-364)*

This is a succinct summary of – most – of the relevant issues; we will have to turn our attention to international linkages in a moment. For now, though, consider the statement that *prices on goods and factors adjust until all markets are simultaneously in (general) equilibrium*. If all markets clear through price adjustments, there is no space for quantities to play a role. Sure enough, firm production levels change, and demands for final and intermediate products change, and so on – but aggregate demand does not factor into the macroeconomic process of equating incomes and expenditures. In other words, the goods market closures rests on price flexibility. And, as there are no quantity adjustments in the goods market, there are as well no quantity adjustments in the labor market: prices on factors adjust until their markets clear. In other words, these models assume that real wages fall until anybody who wants to have a job.

Similar structures are suggested in CEPII (2013). The authors argue that CGE models are the best tools to analyze trade agreements because

> *"[t]heir reliance on sound microeconomic modeling of agents' behavior makes it possible to analyze, in a consistent way, how they might react to the new environment following a policy shock, given their respective objectives and constraints. Meanwhile, the general equilibrium framework ensures that the analysis takes due account of the feedbacks from income effects and labor or capital markets, and the interdependencies across economies." CEPII (2013, p8)*

The representative agent takes her income as given, observes prices, and maximizes utility – the paradigm of price flexibility rules. The relevant background papers are Bchir et al. (2002) and Decreux and Valin (2007). The latter updates the former, so that the content of the two papers often overlaps. However, Bchir et al. (2002) does not discuss the labor market. Decreux and Valin (2007, p16) feature a section on the labor market that focuses on an add-on for developing economies, but offers no general discussion of closures. The appendix, however, states the equations for "full use of factor endowments," (Decreux/Valin 2007, p34), thus confirming that despite possible add-ons full employment emerges.

This turns out to be a strong assumption. To illustrate, let us consider the EU und US. Currently, a lot of involuntary unemployment exists in both these large economies, as they seek recovery from the Great Recession. However, over the course of a half century or so, and abstracting from demographic changes (due to aging, for example), the ratio of employment to population is roughly constant. In other words, in the very long run it seems that the unemployment rate is roughly constant. Does that justify the assumption that real wages adjust *within a year* to generate full employment? Absolutely not: it is both empirically false and distracts from the relevant issues. First, the labor market theory underlying these CGE models presumes that where necessary *real wages will fall to produce full employment*. In the real world, however, nominal wages are downwardly rigid. And, as Keynes (1936) forcefully argued, even if nominal wages were to decline, prices would follow, holding the real wage roughly constant. Second,

trade (and technological change) can have substantial impact on labor demand patterns. The existence of poor, immobile, unemployed working class households in former industrial centers attests to the difficulties to move across sectors. For this reason, real world trade policy includes public expenditure to ease transition. In other words, a credible model should focus on where transition problems might arise, rather than assume them away. But in the models under discussion unemployment simply does not exist.

Similarly, the government does not (quite) exist. The government is subsumed into the representative household. Government revenues from policy – taxes, tariffs, etc. – accrue as income to the household, who distributes part of it to certain sectors as subsidies. Further, the household buys government services from herself, so to speak. What does that imply for the budget deficit? In Annex 2 of CEPR (2013, p108), it is argued that "[w]here we assume fixed expenditure shares, then [sic] we also have a fixed savings rate. […] We maintain a fixed-share allocation between public and private consumption." Put differently, the *budget deficit is assumed to be constant*. If revenues change, government expenditures must adjust endogenously to satisfy the fixed budget deficit. To be sure, tariff revenue looms large neither in the US nor in the EU. However, casual observation of the real world makes it entirely obvious that even if the government would want to, say, reduce spending on education to balance its books after a change in tariff policy, it tends to not be able to. In the real world, government budget deficits are the norm, can be large, and are not usually reduced by expenditure reductions. Instead, deficits tend to be reduced by growth-driven increases in revenues. Clearly, the causal structure assumed is highly questionable. In essence, it serves the purpose of assuming the government as a macroeconomic entity away.

MIRAGE

MIRAGE basically mirrors these assumptions. Decreux and Valin (2007, p9), first, nod to GTAP: "[T]he nineties witnessed the increasing spreading [sic] of the GTAP database (Global Trade Analysis Project, Purdue University), that marked the sharing of the heavy data work required for this kind of models [sic], making their access far easier. The MIRAGE model builds on this literature […]." Further, the government is assumed to balance its books, but does so not through expenditure adjustment but a non-distortionary replacement tax. Decreux and Valin (2007, p10) state that

> *"[t]otal demand is made up of final consumption, intermediate consumption and capital goods. Sectoral demand of these three compounds follows the same pattern as final consumption. The regional representative agent includes the government. He therefore both pays and earns taxes, and no public budget constraint has to be taken into account explicitly: this constraint is implicit to meeting the representative agent's budget constraint. Unless otherwise indicated (modelling a distorting replacement tax does not raise any technical problem), this implicitly assumes that any decrease in tax revenues (for example as a consequence of a trade liberalisation) is compensated by a non-distorting replacement tax."*

It is not further clarified what this tax is or whom it affects; it might be a lump-sum tax. While a "representative household" might consider, for example, a uniform sales tax non-distortionary, real world households would think it regressive; thus, worthy of further discussion. But be that as it may, the key is that budget deficits are constant, because the government reduces expenditures or raises other revenues.

Next, let us think through issues related to investment. Here, the two models differ as well only in detail. First, investment and savings are specifically addressed in Francois etal. (1996). The authors suggest there that one might assume a constant savings rate of the representative household. Given income (from full employment output with the available technology), this implies aggregate savings available for investment. That corresponds to the workhorse neoclassical Solow growth model. In a multi-sector

model, such *savings-driven* aggregate investment would be distributed across sectors; most commonly with fixed sectoral shares. Alternatively, one might assume that the savings rate adjusts to its rate of return: the representative household saves more if the real rate of return on the real asset financed with the savings increases. Given income (from full employment output with the available technology), this again implies aggregate savings available for investment. This setup correponds to the Ramsey growth model. CEPR (2013, p109) assumes such "a basic Ramsey structure with constant relative risk aversion (CRRA) preferences." That implies that aggregate investment adjusts endogenously to the optimal aggregate level of savings.

MIRAGE, in contrast, assumes that cross-border investment matters especially:

> *"This is why an original modelling of FDI is used here, aiming at combining empirical realism and theoretical consistency. The latter objective requires, in particular, that domestic investment's setting be consistent with FDI's one, and that savings allocation behaviour be rational. In this context, the rate of return to capital is a natural determinant of investment sharing across sectors and countries. […] Practically, a single generic formalisation is used for setting both domestic and foreign investment. It stems from allocating savings across sectors and regions, as a function of the initial savings pattern, of the present capital stock and of the sectoral rate of return to capital" Decreux and Valin (2007, p15)*

Thus, the flow of savings allocated to a region and there channeled into real investment rises with a higher rate of return to that asset. The specific functional form differs, and the motivation differs. Crucially, there is no reference to Ramsey-style intertemporal utility maximization. But the end result is that available savings drive aggregate investment, which is of course a restatement of Say's Law as well as the fundamental rule of price flexibility to bring about macroeconomic balance.

Does not the international link present a crucial difference? It does not seem so. Macroeconomic balance, whether with full employment and reference to a microeconomic general equilibrium or not, implies that aggregate injections equal aggregate leakages. In other words, the accounting system underlying macro or CGE or any model implies that investment less private savings plus government expenditures less revenues plus exports less imports are identically equal zero.

The above discussion suggests that both GTAP à la Francois and MIRAGE let (1) external accounts adjust to changing relative prices (and the international investment position), force (2) the government to keep its deficit constant, and make (3) the savings rate an increasing function of returns to capital. Then, to satisfy the macroeconomic balance equation, (4) aggregate investment adjusts. All that is rounded off with the full employment assumption to create a Panglossian view of whatever trade negotiators might come up with.

Scenarios and Elasticities

How does the causal structure of the models described above then produce the headlines and talking points that a comprehensive free trade agreement can produce such-and-such gains in GDP? Essentially, the further inputs needed are scenarios and elasticities.

Scenario refers to the policy change applied to the baseline calibration. The baseline in turn is the model run repeatedly over ten or fifteen "years," so as to, presumably, get at the long run changes. This baseline is based on GDP projections that are exogenous to the model. In other words, based on forecasts of GDP growth rates of the relevant countries and regions over the next fifteen or so years, the model produces GDP levels for, say, the year 2027. The model is then solved again – year by year – with the gradually

implemented policy change. The final year's GDP levels can be compared to baseline GDP levels – the difference is attributed to the policy change, which here essentially means removal of NTM (CEPR 2013: Table A3 p111; CEPII 2013, p7).

The key scenarios employed in Ecorys (2009) and CEPR (2013) are the *ambitious* ones, and concern the *long run*. Since the overall effects of liberalization are quite small, it seems reasonable to focus here on the biggest possible gains. Ecorys's (2009, p xvii) ambitious long run scenario assumes that "by 2018 around 50 % of all NTMs and regulatory divergence are addressed." It should be highlighted that these 50 % present an average across sectors. Tremendous effort has gone into a sector-by-sector assessment of the relevant issues. Annex IX presents a long list of regulatory divergences by sector, with sources varying from sector experts to the survey to literature reviews. Further, an additional "Annex III: Stylized overview literature review" presents a sector-by-sector assessment of whether these barriers are *actionable*. It says there, for example (p468) that "US exporters of agricultural biotechnology products have been affected by a de facto EU moratorium on approving new products," which implies a "very high" NTM, and that "[a]ction could be expected following the WTO ruling."

It is not clear from this statement whether the ambitious scenario implies that EU citizens are assumed to accept, post-TTIP, genetically modified agricultural products. But, Ecorys presumably used all of this information to produce Table 3.3 in the main report (Ecorys 2009 p16), which details "actionability levels per sector." As it turns out, potential NTM reduction averages at 50 % and 48 % for EU-US and US-EU exports, respectively, with a standard deviation of only about eight across the two columns. Thus, about half of the tariff equivalent (reproduced by sectors in our Table 10) is reduced.

The ambitious scenario in CEPR (2013) is titled "comprehensive ambitious scenario," see Table 4, CEPR (2013, p28). It is based on Ecorys's data, but assumes that only 25 % of NTMs are eliminated – meaning only half of all actionable NTMs. The report states (p28) that "[t]he scenarios reported here are therefore far less ambitious than under the original Ecorys study, where full elimination of actionable NTBs was assumed." CEPII (2013) offers four scenarios, the first assuming tariff removal only. The three others assume varying degrees of NTM removal, including one build on Ecorys's scenario and another including "harmonization spillovers," which refers to the possibility that some other countries will want to adopt TTIP standards. CEPII (2013, p8) explicates:

> *"For NTMs, a complete phasing out would be neither desirable nor realistic. As mentioned above and stated repeatedly by European leaders, the objective of an agreement would be not to lower the level of regulations but to make regulations as compatible as possible across the Atlantic to reduce unnecessary additional costs for exporters. Achievement of this objective is not easy in practice, but cross-sector differences are difficult to gauge."*

In a footnote to this paragraph, it is stated that "Ecorys (2009) […] attempt [at measuring actionability at 50 %] is essentially an ad hoc evaluation." In the following paragraph, CEPII proceeds to state that their simulations rest on the ad hoc evaluation that 25 % of NTMs are actionable.[31] Neither CEPR nor CEPII provides any rationale for the reduction of actionability.

[31] CEPII does as well build on a different set of NTM estimates, referring to Kee et al. (2009) and Fontagne et al. (2011). These do not differ substantially in terms of magnitude from Ecorys (2009) – meaning in turn that they *do differ substantially* in magnitude from the stricter definition of NTMs in Anderson and van Wincoop (2003).

Be that as it may, we can conclude that all three CGE applications – GTAP à la Francois in Ecorys (2009) and CEPR (2013) and MIRAGE in CEPII – use Ecorys's estimates of NTMs, though they do assume different degrees of actionability. Even the reduced degrees of actionability imply that the trade cost tariff equivalent of NTMs is on average about twice as large as the one inferred through observation of actual policy barriers.

Now, on to the *elasticities*. The elasticities are so important in this endeavor because they determine how strongly the model will react to the policy change. (Since the 'result' of the baseline calibration is set from projections external to the model, the elasticities do not impact these GDP levels.) An elasticity describes the percentage change in a variable in response to a percentage change of another variable. Crucial for trade analysis is the question by how many percent exports of a product increase if its price relative to a relevant index decreases by 1 %. This is the price elasticity of trade, or *the elasticity of substitution*.

We can link the elasticity issue back to our earlier discussion of the various sources of the gains from trade. Fundamentally, the gains from trade materialize through price decreases. As trade costs are reduced – and specialization takes place, and scale economies matter, etc. – prices are reduced. The assumption of full employment in turn ties down aggregate income. Falling prices with constant or rising incomes leads to 'welfare gains.' Under conditions of monopolistic competition, every firm in every country produces its own, unique variety of a product. *It follows that the higher that price elasticity, the stronger does demand in one country react to a lower price of the unique variety from the other country, and vice versa*.

How high are the elasticities used? The discussion of elasticities in Anderson and van Wincoop (2003) suggests, as mentioned before, that the elasticity might fall in a range of five to ten. The elasticities used in Ecorys (2009) are reproduced in our Table 10, with an (unweighted) average of six. A similar set of elasticities is reported in Table A1 of Francois et al. (2005, p384) which rounds as well to an unweighted average of six. CEPR (2013) reports elasticities in Table 5, which round to an unweighted average of six. CEPII (2013) does not report elasticity values, but it seems safe to assume that the values applied average around at least five. These ranges of estimates of elasticities are based on disaggregated data, often at the product level. It should be noted that estimates of elasticities at the macroeconomic level usually fall in a range of one half to two – maybe three, but not five or ten. (For recent discussions, see Kwack et al. (2007) as well as Bahmani-Oskooee and Kara (2005). Table III, p174, in the latter, for example, presents a simple average of trade price elasticities across twenty eight countries of 1.3.). Standard CGE models have been criticized repeatedly for the use of high average elasticity values; for examples and further references, see Taylor and von Arnim (2006).

The various reports using CGE models do not provide sensitivity analysis. This is particularly important in light of the fact that the elasticities *matter twice*. First, a high elasticity value reduces the implied NTM, which reduces the potential reduction of barriers and hence reduces the potential gains from trade. Second, though, and as discussed here, a high elasticity value increases the gains from trade to the amplification of demand responses. Without sensitivity analysis of the relevant models, it is hard to tell which effect will dominate. It is clear, though, that (1) *the elasticity value applied far exceed reasonable macroeconomic trade price elasticities*, and that (2) *once the NTM index has been calculated, a higher elasticity value leads to higher gains from trade*.

Table 10: Price elasticities and tariff equivalents of NTMs

	Price elasticity	US exports to EU	EU exports to US
Services (excluding travel & transport)	-2.0	13.0	7.6
Travel			
Transport			
Financial services	-2.0	11.3	31.7
ICT services	-3.2	14.9	3.9
Insurance	-3.2	10.8	19.1
Communications	-3.2	11.7	1.7
Construction	-4.2	4.6	2.5
Other business services	-3.2	14.9	3.9
Personal, cultural & recreation services	-8.7	4.4	2.5
Chemicals	-5.1	23.9	21.0
Pharmaceuticals	-9.6	15.3	9.5
Cosmetics	-4.8	34.6	32.4
Machinery	-9.7		
Electronics	-12.2	6.5	6.5
Office & communication equipment	-7.1	19.1	22.9
Medical, measuring & testing appliances	-7.0		
Automotive	-7.1	25.5	26.8
Aerospace	-7.1	18.8	19.1
Food & beverages	-2.5	56.8	73.3
Metals	-13.0	11.9	17.0
Textiles & clothing	-7.2	19.2	16.7
Wood & paper products	-8.0	11.3	7.7
Average	***-6.2***	***17.3***	***17.1***

Source: Adapted from Ecorys (2013, Table III.1 in Annex III.3, p214). Essentially the same table reappears in CEPR (2013, p20).
The first column shows the estimated sectoral bilateral (EU-US) price elasticities (or elasticities of substitution). These are based on the coefficient of the tariff factor in the trade cost function (Ecorys 2009, Annex III, p208-210). The second and third column show, respectively, the calculated tariff equivalent of NTMs, which is based on the elasticity of substitution and the NTM indexes derived from business surveys (etc.). The last row – not in the original – shows simple average across the column, as we do not have sectoral weights of this disaggregation.

That is not the case, however, in the studies conducted by ifo. Here, a higher elasticity leads to *lower* GDP gains. The elasticity underlying macroeconomic simulations in Bertelsmann/ifo (2013) is eight. This is discussed in more detail in BMWT/ifo (2013, p75), albeit in German. Sensitivity analysis presented therein (Table A.II.6, p159) suggests that the elasticity and GDP gains are indeed negatively related. A quick calculation indicates that the model produces for a one percentage point increase in the elasticity of

substitution a *reduction* in (unweighted) average GDP gains of about two thirds of one percentage point.[32] Why? The reason lies in the different simulation method – discussed in more detail in the following section. In short, ifo first estimates the trade creation effect of a free trade agreement across existing agreements, then estimates a gravity model, and uses that model to calculate NTM reduction necessary to produce the previously estimated trade creation. Now recall that the elasticity matters twice – first in the calculation of the implied NTM, and second in the calculation of the trade response. We have to assume that ifo's work emphasizes the former rather than the latter – and therefore shows a negative link between elasticity values and GDP gains.

In summary, the scenarios that are fed into the CGE models all rest on Ecorys's estimates of NTMs. These reflect *subjective statements from firms on their perception of NTMs*, rather than policy measures actually in place. We recognize the difficulty in measuring the specific restrictiveness of existing regulation, customs procedures, etc. We must note, however, that the indices constructed exceed the estimates from an authoritative study (Anderson/van Wincoop 2004) on NTM trade costs *other than language, currency, culture, etc*. by a multiple. Even after making assumptions about actionability (from 25-50 %), the reduction in NTMs still seems high on average. Further, the elasticities that are fed into the CGE models are much higher than reasonable macroeconomic elasticities. Since the reduction in NTMs and model closures in combination with elasticities drive all gains, the calculated gains in Ecorys (2009), CEPR (2013) and CEPII (2013) from TTIP seem very optimistic on average.

2.4.4. Bertelsmann/ifo: A different Approach

The methodologies applied by ifo in the work on TTIP differ substantially from the other studies. Where the other studies ask what effect a reduction in trade cost has on trade flows, IFO asks what reduction in trade costs produces a previously estimated level of trade flows. This is quite ingenious and novel, but therefore as well difficult to put in context, and, basically, somewhat "untested." In this section, we provide a brief review of the methodology. We begin, though, with a brief explanation of the various reports that document IFO's work.

First, ifo published BMWT/ifo (2013), which was commissioned by the German government (and is available only in German) to assess the effect of a free trade agreement – then still called TAFTA – with the US. In this report, ifo presents in chapter II econometric work on the determinants of a free trade agreement as well as gravity estimations of world trade, including, of course, EU and US trade. The relevant background paper is Egger et al. (2011). In chapter III BMWT/ifo extends this framework to include a New Keynesian labor market, which enables analysis of the *structural dimensions* of TTIP effects on the labor market. Relevant background is presented in Felbermayr et al. (2011) as well as Felbermayr et al. (2012). These two chapters form the basis of the macroeconomic part of the Bertelsmann/ifo study, which is listed in our references as Felbermayr/Heid/Lehwald (2013).[33] As

[32] We calculate the average percentage change of GDP gains across countries based on the two different elasticities – see Table A.II.6, p159 – which turns out to be -0.37, and divide the percentage change in the elasticity (0.6) by that to get -0.62.

[33] Chapter IV of BMWT/ifo (2013) presents furthermore sectoral results based on an application of the MIRAGE model. Since ifo's contribution to the debate is its novel simulation strategy, and ifo's emphasis in the reports lies on these, we will here refrain from further discussion of MIRAGE.

previously mentioned, Bertelsmann/ifo (2013) is *very short* on any details regarding methodology. We therefore rely here largely on the government study; unless otherwise noted all page numbers refer to BMWT/ifo (2013).

Now let us try to provide an intuitive explanation of the research strategy. First, BMWT/ifo asserts that free trade agreements are not random. In other words, countries that negotiate a free trade agreement very often are relatively close to each other, have deep historical and political ties, and share other relevant characteristics. Instrumental variable regressions are put forth to provide evidence. See, specifically, Table II.2 p65. These results directly draw on Egger et al. (2011). The instruments are COLONY, which indicates whether one country once has been the other country's colony, as well as COMCOLONY, which indicates whether the two countries once had the same colonial master, and SMCTRY, which indicates whether the two countries once have, in fact, formed one country. These variables are "only relevant for the decision regarding formation of a free trade agreement, but not for the determination of trade flows" (p66, own translation).

Second, BMWT/ifo estimates a gravity framework by accounting for free trade agreements as *endogenous*, through use of the previously established instruments. See, specifically, Table A.II.1 and Table A.II.2. on p148-149. Now, crucially, assuming the formation of TAFTA/TTIP in this gravity framework leads to large trade creation effects – which grow substantially if the potential free trade agreement between the US and EU is considered endogenous. Table II.4, p71, reports results from different regression models, with trade creation effects varying between roughly 60 % and 160 % – meaning, trade flows on average are estimated to double. These are, as the study notes (p69, own translation), large:

> *"The reported effects are to be understood as broad long run effects. They are broad, because they consider* all *trade creation effects [...]. That means, as has been emphasized, that the estimation implies removal of tariffs as well as non-tariff barriers. Additionally, effects are created through processes triggered by the free trade agreement. These include investments in bilateral infrastructure, gaining of knowledge and competence regarding the partner, growth of informal networks, etc. [...] These reported effects are long run effects, which reach their full impact only after 10-20 years."*

ifo's implicit definition of "removable trade barriers" is even much broader than Ecorys's. In the estimation strategy, the observed trade creation effects of past agreements rest on common infrastructure investments, informal networks, and so on. Therefore, the estimated trade creation effect of an EU-US agreement must be interpreted in that light. This does raise the question whether one can extrapolate from past agreements – such as the EU, or NAFTA – to today's situation between the US and EU. Especially EU integration in the post-WWII decades must loom large in the data, and it is not immediately clear whether European trade growth in the Sixties is a good guide on what to expect from TTIP.

Nevertheless, building on these trade creation estimates, BMWT/ifo calculates "welfare effects." These are here measured as 'equivalent variation', which report the change in real income that allows consumers to obtain the same utility level after a change in prices, due to trade liberalization, for example, as before, but at the original relative prices. Equivalent variation is not a meaningful measure: it is quite void of empirical substance, since prices, after liberalization, really do change. "Welfare" itself is, as discussed above, a theoretically problematic concept, as the presumed social optimality of such a general equilibrium cannot be affirmed – recall problems of existence as well as stability of general equilibria after the Sonnenschein-Mantel-Debreu results, and the vacuousness of the welfare theorems if trades at

out-of-equilibrium prices occur. For all these reasons, changes in real GDP are the relevant measure to work with. That the welfare changes reported by BMWT/ifo are grossly inflated relative to real GDP changes only adds to this assessment. For the US, welfare changes are 13 %, whereas real GDP growth is 5 %. On average, reported welfare changes are ten times higher than GDP changes (Table A.II, p159-161).

Key model results, however, are reported in chapter III. This chapter takes the gravity framework with endogenous formation of free trade agreements as well as firm heterogeneity and augments it with a New Keynesian labor market á la Pissarides (2000). This labor market model is often labeled *search unemployment*, as it explicitly models a firm's search costs as well as a 'matching function' to describe the negotiation between potential employer and employee. The model allows for *involuntary unemployment*, and thus presents an important improvement relative to the competitive, clearing labor market in GTAP and MIRAGE. However, unemployment is *structural* – it is equilibrium unemployment, and in this sense not fundamentally different from other New Keynesian NAIRUs. (Even supposing that such a steady state exists, convergence to it might be very slow.) Unemployment here exists because labor markets are imperfect: It costs firms money to find the right employee.

The causal mechanism for gains from trade – and employment effects from trade – is as follows. First, firm heterogeneity finds its expression in different productivity levels. Only the most productive firms are exporters. Following a reduction of trade costs due to, say, implementation of TTIP, firms that were just on the cusp can become exporters. As prices fall due to the reduction in trade costs, and as competition increases, the least productive firms exit the market. A key source for the gains from trade is this *reallocation effect* from low to high productivity firms. The former shrink, the latter grow, and as they do, they hire:

> *"It follows that the average firm faces lower search costs, and at the same time faces higher revenue from expanding employment. It therefore strengthens incentives to offer jobs. To put it still differently: The average firm […] is after liberalization more productive, more profitable; and has lower search costs. Demand for labor rises. A part of these gains goes to employees, whose real wages are rising." (p86, own translation)*

However, as we have discussed before, reallocation takes time:

> *"The above described mechanism concerns effects in the long run. Short run effects are not considered. […] It is important to note that there can be negative effects in the short run: Reallocation of employees from shrinking to growing firms can, especially with non-linear adjustment costs, lead to an asymmetry: Exit occurs very fast, whereas expansion of employment opportunities in export-oriented firms occurs only slowly." (p86, own translation)*

How big are these long run effects? Let us here consider the NTM scenario, which is BMWT/ifo's preferred one. For this scenario, it is assumed that TTIP creates on average as much trade as the previously discussed estimations suggested a free trade agreement between the US and EU would – namely roughly 76 %. The imputed trade costs in the baseline calibration are then reduced until that trade creation effect is matched. (Table 11 provides an overview.) The resulting change in GDP per capita comes to about 2 %. Since this is a long run effect, the estimated *annual* contribution of TTIP to GDP growth in the US and EU is negligibly small. This remains the case despite the bells and whistles introduced throughout, especially the large trade creation effect.

Table 11: Selected parameters and results from BMWT/ifo simulations

	1	2	3	4	5
US	2	105	-25	86	2.15
EU	1.3	64	-25	73	1.67
Source	III.2	III.3	III.7	III.8	III.12

Source: Adapted from BMWT/ifo (2013, chapter III).
Column 1 reports the "matching efficiency" of the respective labor markets. The higher US value presumably reflects its smoothly functioning labor market. Column 2 reports "imputed bilateral ad valorem trade costs" in percentage points. Column 3 is the percentage reduction in these trade costs in BMWT/ifo's preferred NTM scenario, column 4 the corresponding growth of exports to the other region. Column 5, lastly, reports the growth rate of GDP per capita in the NTM scenario in response to TTIP reforms, which has to be interpreted as a fifteen year effect.

2.4.5. A Note on Foreign Direct Investment

Capital flows between countries can play an important role in the determination of a country's output and employment. Especially *foreign direct investment* (FDI) can have positive effects. (Financial flows can be volatile and unpredictable even in developed countries, as the European debt crisis has shown.) For that reason, the agreement under negotation between the US and EU is labeled as an "investment partnership." Similarly, the public debate on TTIP often emphasizes economic effects related to investment.

There are, broadly, two concerns: (1) NTMs that serve as an impediment to cross-border investment, which one might conceive of in principle quite similar to NTMs that hinder trade flows; and (2) investor-state arbitration relations, which concern competition and regulation more generally. To illustrate, consider Google: If EU authorities tell Google that it cannot, due to privacy concerns, offer "street view" services, Google's costs of operating in Europe would increase, since it might have to program or advertise its maps differently. This is a cost-increasing FDI NTM. If, on the other hand, the EU tells Google that it must unbundle its services – that its virtual search monopoly must be broken up, essentially – Google's business model in Europe would have to change, fundamentally. Such an issue would have to be addressed through investor-state arbitration mechanisms (see Eberhardt in this volume).

Free "trade" agreements increasingly do so. Usually the intention is to protect assets as well as the resulting income flows from host country government interference. Assets are physical assets – buildings, machines and computers – as well as "blueprints" or patents, which means that intellectual property right protections often feature prominently in such provisions. The key concern for our purposes is, first and foremost, to note that *the costs and benefits of investor-state arbitration mechanisms are exceedingly difficult to estimate* and remain quite fundamentally outside the scope of the reports and, more generally, modelling frameworks applied therein. To recognize this, however, is important, since it seems possible that the effects of a "deep" treatment of investment arbitration in TTIP would quantitatively outweigh the effects of NTM removal on FDI related costs.

Nevertheless, let us look at what the four studies reviewed here do say about investment. As will be seen, it turns out to not be much. First, the *GE models reviewed here do not speak to the issue of foreign direct investment*. To be perfectly clear: two of the four reports – Ecorys (2009) and CEPR (2013) – do in fact discuss FDI, but they do not within the theoretical and empirical framework of the simulation model applied. In sharp contrast, they present separate regression estimates of the effects of NTM removal on FDI activity indicators. Let us consider related concerns in turn.

First, the results from CEPII's MIRAGE model *might be* decomposable into domestic and foreign investment flows. This is suggested in the relevant background paper (see our chapter 2.4), where the macroeconomic closure specifically refers to international investment. However, in the studies where MIRAGE has been applied (chapter IV of BMWT/ifo 2013, and of course in CEPII 2013), no reference to these investment effects is made: tables showing simulation results as well as discussion and conclusion do not mention numerical FDI or investment effects. Similarly, the GTAP model à la Francois applied in Ecorys and CEPR features an endogenous trade balance. Such trade flows must be financed – there must be a transfer in the current account, or compensating capital flows. Clearly, these issues are not considered in detail. While aggregate investment in one region or country adjusts to satisfy the macroeconomic balance, this investment is not explicitly modeled as FDI.

In sharp contrast, CEPII offers an "ad hoc" evaluation *against significant investment provisions*. It is worth quoting at length:

> *"With €1,200 bn invested by each country into its partner's economy in 2010 (Eurostat), investment is potentially an important part of the agreement. [...] This willingness is consistent with the US emphasis on the inclusion of ambitious investment chapters in their preferential agreements, and with European countries' numerous bilateral investment treaties (BITs). Nonetheless, the transatlantic partnership is particular in this respect, because the need for an agreement designed to grant investors "fair and equitable treatment" as it is usually described, is not obvious. The quality and impartiality of judicial systems on both sides leaves open whether an investor-state arbitration procedure is necessary to protect investors against discriminatory measures or uncompensated expropriations of property. Such a procedure might even be a source of concern, since it would prioritize an ad hoc system of arbitration with minimal institutional underpinnings and questionable legitimacy over national judicial systems. Paradoxically, such an arbitration system might even promote discrimination if it were to provide to foreign investors rights which domestic investors are denied. All this call [sic] for great caution in the wording of the provisions that might be included in the agreement, and great attention to avoiding overly restrictive provisions that would limit the capacity of government to implement independent policy in the areas of environment and energy in particular. In addition, while some existing rules are clearly protectionist – such as the impossibility for a foreign investor to own more than 25 % of a US airline company, or the existence of a golden share in the British military aerospace industry – current regulations do not seem to be stifling investment unduly judging by the size of existing bilateral cross-investment stocks." CEPII (2013, p6-7)*

Thus, neither of the two CGE models used in three studies (Ecorys, CEPR, CEPII) is applied to analyze investment related questions. But, Fontagne et al. (2013) do suggest in the CEPII study to better stay away from far reaching FDI regulations that reach across borders.

How about the regressions? Ecorys (2009) and CEPR (2013) provide FDI analysis as an add-on to the central (trade) gravity estimation and CGE simulations. As mentioned, this means that they essentially run regressions to estimate the effects of NTMs on FDI activity indicators. Bergstrand and Egger (2007) is suggested as theoretical foundation. Curiously, that framework treats FDI as trade is treated in a standard gravity framework, which means that FDI activity indicators are regressed on incomes as well as relevant measures of "distance" or "FDI costs." One might then calculate a *partial effect of NTM removal on such an index of FDI activity*.

Partial is the key word here. All four studies emphasize that their main arguments on the gains from TTIP rest on *general equilibrium* analysis, be that a traditional CGE or a new trade-cum-New Keynesian labor market model. We do not argue that partial analysis has no merits, or that the use of different models for different purposes is somehow questionable. In contrast, we recognize the difficulty of comprehensively describing FDI in a CGE (or GE) macroeconomic model. However, the investment results by Ecorys and CEPR should be read with a grain of salt in light of the partial equilibrium nature.

In Ecorys, the discussion of investment related results is limited. Ecorys covers the methodology for FDI gravity regressions in some detail (2009, p11-13 and Annex III 2.7, p211). Chapter 4 on "Quantifying NTMs and regulatory divergence" first suggests that "[w]ith respect to investments and FDI, sector-specific regressions in the goods sector could not be run due to a severe lack of data," (Ecorys 2009, p22), and proceeds to state the main results on "pooled regression results for FDI":

> *"Gravity model estimations of bilateral foreign direct investment (FDI) flows between the EU and US have also been run with data stemming from Eurostat and the business survey NTM indexes, as well as additional data on tariffs and traditional gravity variables (distance, language and border). Gravity estimations are carried out at an aggregate level where all sectors are pooled, and on a disaggregate level where sectors are grouped into technology, durable goods and nondurable goods. There is not enough FDI data to carry out estimations on a sector level. Of the three gravity variables, only language turns out to have a significant impact on FDI. The positive tariff sign found, suggests FDI is driven by a tariff-jumping motive, i.e., foreign firms tend to invest in countries with high tariffs rather than serving the market through trade." Ecorys (2013, p23)*

Annex IV.3, p232, shows a table with regression results to complement this paragraph.

CEPR, in contrast, offers a full chapter (CEPR 2013, Chapter 6, p85-93). In this chapter, the emphasis lies on a discussion of FDI restrictiveness indexes as they can be constructed from various surveys, including Ecorys's data. Towards the end, regressions are suggested, of the relevant FDI NTM index on measures of FDI activity – namely FDI income, number of (foreign owned) enterprises and number of employees (in foreign owned enterprises). The results suggest that, roughly, a 1 % decrease in the NTM index would lead to a 0.5 % increase in income generated in foreign owned enterprises. Using the estimated elasticities, CEPR calculates back-of-the-envelope effects of a 25 % reduction of NTMs on the order of more than 10 % increase of income generated by foreign owned enterprise, as well as about 10 % employment increases. Needless to say, these seem large relative to the otherwise estimated impacts of TTIP.

Thus, in summary, the analysis of investment in the reviewed reports is mostly cursorily, if it exists. Arguments made are based on partial analysis and simple regressions rather than the general equilibrium simulation models applied. Overall, considerably less effort has gone into discussion and documentation of FDI analysis than that of trade.

In this sense, it might be most important to note that the FDI discussions, where available, do not consider the underlying *macroeconomic* theory seriously. For example, the macroeconomic accounting implies that whatever effects TTIP has on FDI flows must be reflected in either capital or current account, and has effects on the macroeconomic balance therein. Similarly, valuation effects both through asset prices as well as exchange rates can matter greatly. None of the studies so much as touches upon these issues.

2.5. Summary of Main Results

What are the economic effects of TTIP? In the debate, a few selected studies, mostly commissioned by the European Commission, have set the tone, suggesting that effects are positive on both sides of the Atlantic. In this article, we critically assessed these findings and their underlying methodologies. In addition, we discussed some issues, which are frequently neglected by trade impact assessments, but are nevertheless important for policy-makers. Besides, some ex-post evidence on experience with other trade liberalization ventures, in particular NAFTA was provided. In the following, we offer a summary of our main results.

The estimated economic effects are small

All of the four scrutinized studies report small, but positive effects on GDP, trade flows and real wages in the EU. GDP and real wage increases are however estimated by most studies to range from 0.3 to 1.3 %, even in the most optimistic liberalization scenarios. These changes refer to a level change within 10 to 20 years (!), annual GDP growth during this transition period would thus amount to 0.03 to 0.13 % at most. Unemployment in the EU will either remain unchanged (by assumption), or will be reduced by up to 0.42 %-points, i.e. roughly 1.3 million jobs, again over a 10-20 year period. This amounts to an annual reduction of 65.000 – 130.000 unemployed persons. In our view, this overly optimistic estimate rests upon questionable assumptions. Unsurprisingly, total EU exports are predicted to increase by 5 – 10 % because of TTIP. Since tariffs on transatlantic trade in goods are already at very low levels, roughly 80 % of the economic effects depend on the elimination of Non-Tariff-Measures (NTMs), i.e. the removal or harmonization of regulations, administrative procedures or standards. NTM reduction is thus key to arriving at positive effects. According to three studies, TTIP benefits will however come at the cost of reducing bilateral trade between EU Member States. In a deep liberalization scenario, intra-EU trade could fall by around 30 %. The reason for this is that these EU countries' exports will be substituted for by cheaper Extra-EU imports. In addition, diversion effects in global trade from TTIP could be harmful for developing countries – one study expects negative real GDP change of 2.8% for Latin America and 2.1% for Sub-Saharan Africa, as well as 1.4% for LICs. This could indicate a potential violation of the EU's commitment to Policy Coherence for Development.

Macroeconomic adjustments costs could be substantial

Adjustment costs are mostly neglected or downplayed in the TTIP studies. This refers in particular to macroeconomic adjustment costs, which can come in the form of:

Changes to the current account balance: Trade agreements by their very purpose lead to changes in trade as well as capital flows. If, for instance, imports rise disproportionately vis-à-vis exports immediately after trade liberalization, a trade deficit might emerge. Strong FDI inflows might lead to a structural drain on the current account due to profit repatriation. Short-term speculative capital in- and outflows might lead to balance of payments problems. While for the EU *in toto* this will arguably present no major problem, for individual member states such occurrences might prove problematic.

Losses to public revenues: The elimination of all or most of the remaining tariffs due to TTIP will unavoidably lead to losses for the public budgets of the EU and its member states. During the transition period of 10-20 years the lower bound for these public revenue losses will be at close to 2 % of the EU budget, i.e. €2.6 billion p.a. Thus, the EU will receive less income from its traditional own resources, a loss that only gradually might be compensated for by an increase of its GNI resources. We would thus estimate cumulated income losses to be in the order of €20 billion over a period of 10 years, also depending on tariff exemptions and phase-in periods for sensitive goods.

Changes to the level of unemployment: All four studies reject the idea that TTIP will lead to permanent unemployment. Either employment is assumed to remain constant (by three studies), or estimated to be reduced by TTIP. Any persons in import-competing sectors who lose their jobs because of TTIP are assumed to be reemployed instantaneously, i.e. with only negligible effects on their incomes and costs to the public budgets due to retraining expenses etc. According to one study (CEPR), between 430.000 and

1.1 million workers will be temporarily displaced. Other empirical studies however suggest that (i) most displaced workers will earn lower wages in their new jobs, (ii) retraining expenses particularly for less-skilled workers might be substantial, and (iii) a fraction of the displaced workers, in particular older and less-skilled persons, will in all likelihood remain unemployed for a long time, thus inferring substantial costs on national unemployment benefit schemes and social spending. These adjustment costs will be generally higher during times of economic crisis and low levels of labor mobility. Both of these conditions apply to the current situation in the EU. EU unemployment is at record heights. Labor mobility in the EU is generally low, though somewhat rising recently as a response to the economic crisis. A rough calculation yields annual expenses for unemployment benefits of between €0.5 – €1.4 billion during a TTIP implementation period of 10 years. Thus a cumulative €5 – €14 billion might be necessary to finance a part of the adjustment costs on the labor market, with additional costs for re-training and skills-acquisition not included in this amount. To this amount, a further loss of public revenue from foregone tax income and social security contributions between €4 - €10 billion has to be added.

The social costs of regulatory change can be substantial, but have been neglected

Another type of costs ignored refers to the regulatory change resulting from TTIP. All studies, but particularly the Ecorys study, assume that a reduction of NTMs is welfare-enhancing. This ignores that NTM such as laws, regulations and standards pursue public policy goals. They correct for market failures or safeguard collective preferences of a society. As such they are themselves welfare-enhancing. The elimination or alignment of an NTM thus will imply a social cost for society. This applies equally to NTM elimination, harmonization and mutual recognition. Firstly, harmonization of NTMs, e.g. technical standards, will imply both a short-term adjustment cost for public institutions and for firms required to align their administrative procedures, production processes and products to the new standards. Secondly, mutual recognition of regulations and standards will increase information costs for consumers, since the latter will be confronted with a more complex and potentially less transparent multiplicity of permissible standards, e.g. on consumer goods and services. Thirdly, the elimination of NTMs will result in a potential welfare loss to society, in so far as this elimination threatens public policy goals (e.g. consumer safety, public health, environmental safety), which are not taken care of by some other measure or policy. The analysis of NTMs in the Ecorys study completely ignores these problems. Instead, it is assumed that around 50 % or 25% of all existing NTMs between the EU und the US are actionable, i.e. can be eliminated or aligned to some international standard, while CEPR assumes a 25% actionability level. This includes sensitive sectors such as foods & beverages, chemicals, pharmaceuticals and cosmetics or automotives. In order to arrive at its optimistic welfare estimations, strong reductions/alignments of NTMs in precisely those sectors are necessary, where the safeguarding of public policy goals is perhaps most crucial. It is highly doubtful that such high levels of actionability could be implemented without any losses to the quality of regulation in the public interest. Though subject to considerable uncertainty, the incurred social costs of TTIP regulatory change might be substantial, and require careful case-by-case analysis.

In connection to this, any future regulatory act would be under the threat of being challenged under investor-to-state dispute settlement (ISDS), if the negotiating partners stick to their intention to include such a mechanism in TTIP. Thus, a social cost might be implied for society in two distinct forms: firstly, governments might abstain from enacting regulation or change it according to investor interests, for fear

of being challenged under ISDS; and secondly, in case of litigation, compensation payments issued against governments would have to be financed out of public budgets, aka from taxpayers' money.

Ex-ante & ex-post assessments of similar trade liberalization ventures strongly differ

The NAFTA agreement between the US, Canada and Mexico is often cited as a role-model for the kind of agreement that is negotiated between the EU and the US. Its conclusion was justified on the grounds of ex-ante assessments that claimed considerable economic benefits for the participating countries. Ex-post analysis of the impacts of NAFTA however suggests that ex-ante impact projections substantially overestimated the economic effects. Most of these ex-ante assessments were based on the kind of CGE-modeling, which is also used for TTIP, though in a more sophisticated way. While ex-ante studies projected net gains for all NAFTA parties, but particularly for Mexico and Canada, with real GDP increases up to 11 %, employment gains of up to 11 %, and real wages increases of up to 16 %, ex-post assessments conclude that for the US NAFTA impact on welfare and GDP were negligible. For Mexico, a number of studies suggest that NAFTA had negative effects on GDP, real wages and the distribution of income. Those few studies that do find positive effects of NAFTA are well below the estimations of ex-ante studies. On jobs, ex-post studies found US labor displacement in the range of 600.000 – 1.2 million jobs because of NAFTA, i.e. up to 10 % of total job losses in the US between 1993 and 1999. For Mexico, net job gains in manufacturing appear to be small, mainly because of increasing productivity, while job losses in agriculture amount to up to one sixth of the total workforce, with roughly 1 million jobs lost in corn production in the first ten years after NAFTA's entry into force. Though, of course, ex-ante studies were performed on the basis of assumptions about the results of negotiations, their bias to overestimate positive impacts remains, even if one controls for the difference between scenario assumptions and actual negotiation results.

Methodology is based on unrealistic and flawed assumptions

Methodological critique of Ecorys, CEPR and CEPII in a nutshell:

- Even 25 – 50 % "actionable", i.e. reducible NTMs of Ecorys's estimates (as assumed by Ecorys and CEPR) are likely too high to be realistically achievable.
- The CGE models assume full employment and balanced budgets, and thus cannot speak to key macroeconomic variables of interest.
- All models concern the long run. Possible adverse effects in the short and medium run are neglected.
- Price elasticities, which determine the quantitative reaction of demand and supply in the models used are high, typically double the size compared to the macroeconomic literature. High elasticities, however, drive the gains from trade, i.e. the higher the assumed values for the elasticities, the higher the estimated gains in exports, output and income.
- All put together, the assumptions underpinning NTM estimation and modeling likely bias the projected gains from TTIP upwards.

Quantification of non-tariff measures

How NTMs are defined and estimated matters greatly. Simply put: The higher the NTM to be removed, the higher the potential gain from 'free trade.' Broadly conceived, NTMs are trade policy instruments

other than tariffs. NTMs can be decomposed into policy barriers, meaning those related to regulations and procedures pertaining to the sale of a product across borders, and inferred barriers, meaning those related to different languages, cultures, currencies, etc. In TTIP only the former are potentially subject to removal. An authoritative study of trade costs by Anderson and van Wincoop suggests that NTMs related to border policy barriers between industrialized countries add on the order of about 3 % (or so) to cost of production, whereas inferred barriers average – roughly – 30 %. In the study by Ecorys, in contrast, NTMs are defined to include any regulatory divergence, and indices are build on firms' perceptions about the restrictiveness of these. Ecorys's estimates show an unweighted average of 17 % tariff cost equivalent, and thus are a multiple of the 3 % (or so) of Anderson and van Wincoop. Ecorys, CEPR and CEPII assume removal of 25 - 50 % of Ecorys's NTMs in their CGE scenarios, which has to be considered very optimistic. Hence, a vast overestimate of removable NTMs has very likely been fed into the models.

CGE models and closure assumptions used in the studies

The CGE models used are GTAP (Ecorys, CEPR) and MIRAGE (CEPII, as well as a chapter by IFO). Both models are standard neoclassical models of production and trade. The key assumptions of the models include (i) full employment of factors, including labor, (ii) price clearing markets and (iii) a constant government deficit. These assumptions are unrealistic. As such, these models cannot speak to aggregate employment, aggregate demand or fiscal effects of trade policy changes. Rather, the respective reports highlight microeconomic modeling detail. These concerns do not, however, matter for results nearly as much as the implicit macroeconomic structures: With models that feature full employment, trade liberalization tends to produce positive – though small – gains in GDP. None of the studies considers alternative modeling approaches that could provide a robustness check on these results and inform on key macroeconomic issues.

Bertelsmann/ifo Study:

The Bertelsmann/ifo study takes a very different approach than all other studies. The model applied is not a CGE model of the GTAP/MIRAGE type, but rather is a gravity model augmented with a New Keynesian search unemployment labor market. Bertelsmann/ifo first estimates that a free trade agreement between EU and US would create roughly 80 % growth in bilateral trade. In the calibrated gravity-cum-unemployment model trade costs are then reduced so as to produce this trade creation effect. Despite the unusually large trade creation effect, the long run gains in GDP (1.35 %) from TTIP remain small. The expected gains in employment for TTIP countries which amount to 2.4 million jobs, of which roughly 1.3 million accrue to the EU, however are very large. In our view, the latter depend on the properties of the utilized labor market model, which assumes large employment gains in EU countries with pronounced labor market frictions and high unemployment rates. In addition, job reallocations within sectors due to trade liberalization have apparently not been accounted for. Thus, employment gains from TTIP do not seem plausible to us.

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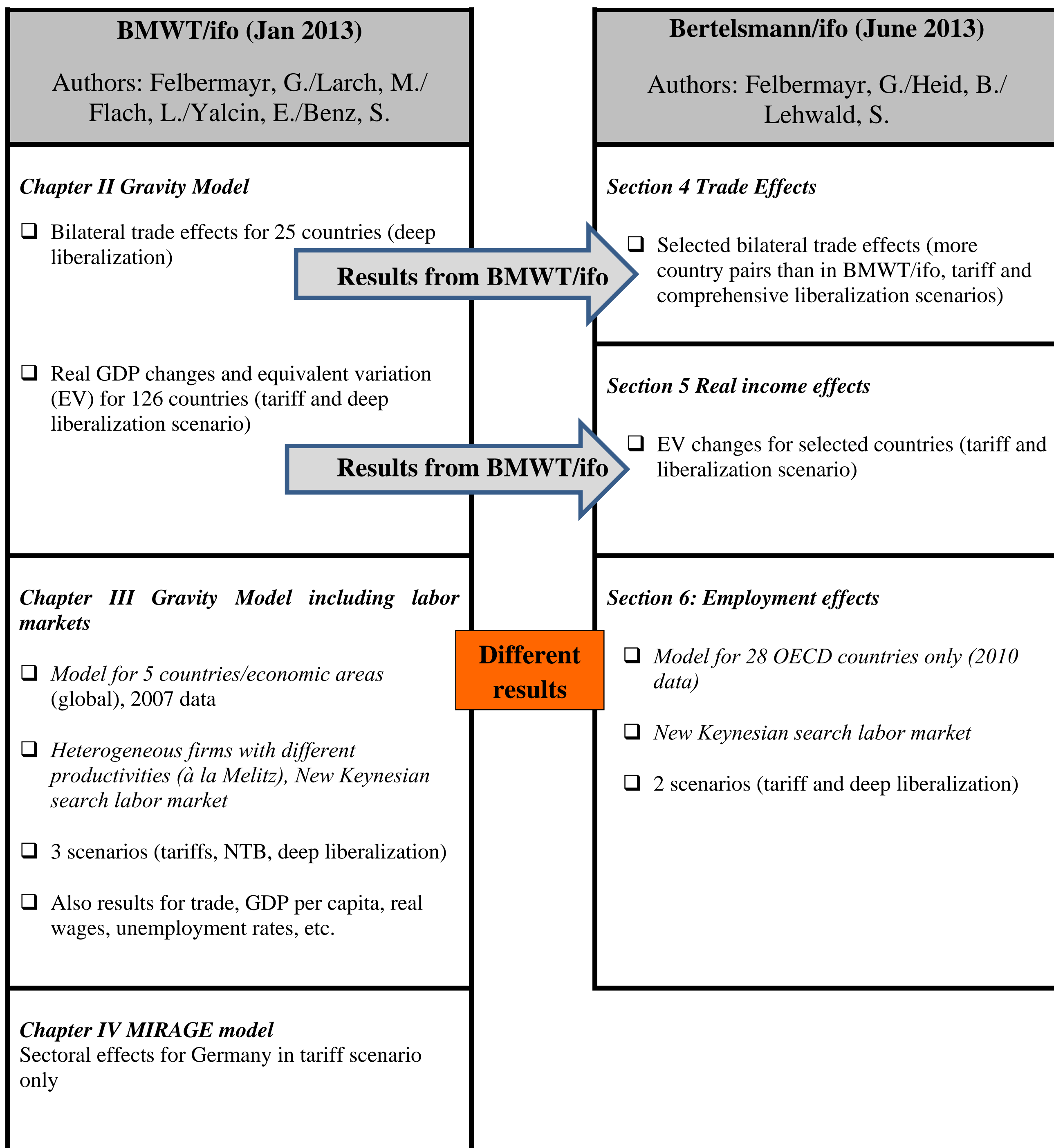
Annex

Figure 1-A: Comparing BMWT/ifo and Bertelsmann/ifo



Source: BMWT/ifo (2013) and Bertelsmann/ifo (2013)

II. Asymmetry: Investor and Labor Rights

3. Investment Protection at a Crossroads

Pia Eberhardt

With the debate surrounding the Transatlantic Trade and Investment Partnership (TTIP), the controversy over global investment law has well and truly arrived in Europe. Criticism of this »parallel justice in the name of money« (Pinzler et al. 2014) [1] is growing especially in Germany – extending even into the mainstream media and the conservative party camps. However, resistance to TTIP is also being ignited outside of Germany primarily by the planned special rights of litigation for corporations.

Worldwide there are already numerous international treaties containing these investor-state dispute settlement rights. They enable foreign investors to bring lawsuits against countries before private international arbitrational tribunals – on account of any policy that threatens their property titles and the planned profits from their investments, whether because of health and environmental regulations or as a result of social and economic policies that restrict their entrepreneurial freedom.

Thus, the Swedish power company Vattenfall is currently suing Germany because it is not happy with the nuclear phase-out. In Australia and Uruguay, Philip Morris is taking legal action against tobacco control policies. And the Canadian oil and gas company Lone Pine is suing its own government through a US subsidiary because the province of Quebec has declared a moratorium on the deep drilling technique known as fracking on account of environmental risks associated with natural gas exploration (see Box 1 for examples of ongoing lawsuits and Box 2 for examples of already concluded lawsuits).

The lawsuits are not heard before ordinary state courts, but before ad hoc private international tribunals. The three private individuals of whom the tribunals are usually composed are appointed by the parties to the dispute, and they operate in accordance with the arbitration rules specified in the relevant investment agreements. They have the power to review all measures taken within a state – laws enacted by parliaments, executive decisions and court verdicts – as regards their compatibility with the extensive investor rights, and to order states to pay large sums in damages. Their rulings are binding and can be enforced worldwide. There are no provisions for appeals procedures.

No ordinary court in the world has as much power. The arbitral tribunals violate important constitutional principles: the independence of the arbitrators is not guaranteed; their meetings are generally closed to the public, being held in hotel rooms in London, Paris or New York; and their rulings are for the most part secret. Moreover, the relative positions of the parties to the disputes are extremely unequal: investors only have rights and feature as plaintiffs, states only have obligations and hence are always the defendants. Investor protection treaties do not contain provisions for investor duties (for example, to respect human rights, workers' rights or environmental standards).

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[1] All translations of quotations from German sources are by the translator.

In the case of the transatlantic trade agreement, investor-state arbitration poses incalculable risks. Already today, over half of the foreign direct investment in the United States and the EU comes from the other side of the Atlantic. There are umpteen thousand subsidiaries of US corporations in Europe and vice versa. According to research by the organization Public Citizen (2013), investor-state dispute settlement rights enshrined in an EU-US agreement would enable 75,000 companies, either directly or through foreign subsidiaries, to attack more progressive legislation on health, environmental and workplace safety on the other side of the Atlantic. It is no wonder that the head of the domestic affairs department of the German newspaper *Süddeutsche Zeitung*, Heribert Prantl, recently described the planned exclusive special rights for large-scale investors as a »clandestine *coup d'état*«, as one of »the most dangerous assaults ever launched on democracy and the welfare state« (Prantl 2014). It is no wonder that the opposition to the TTIP is united in rejecting this »transatlantic corporate bill of rights« (Corporate Europe Observatory/ Transnational Institute/ Seattle to Brussels Network 2013).

In an attempt to take the wind out of its critics' sails, the European Commission has suspended negotiations on investment protection in the TTIP for the present. A public consultation on the issue was launched at the end of March 2014 and ran until the beginning of July (European Commission 2014). The Commission is currently analysing the 150,000 contributions (see ver.di's contribution in this volume) – a historical record when it comes to the EU's public consultation – and has announced a report on the outcome for the end of 2014. However, this consultation did not deal with the issue of *whether* and *why* investment protection is even needed in an EU-US agreement, but only with *how* it should be structured. Thus, the Commission's concern is not with a free and open-ended discussion, but only with polishing and selling its agenda.

The consultation nevertheless opens up a space for a more thorough-going debate on rules of global investment protection. Its outcome will have implications not only for the agreement between the EU and the US, but also for the global struggle against the »globalization of corporate power« (Mies/von Werlhof 2003): If social movements, trade unions, environmental organizations and other critics of investment arbitration manage to keep the latter out of the TTIP, that will provide a boost to social movements and left-wing governments throughout the world which are trying to limit the power of transnational corporations and to break out of neoliberal adhesion contracts concluded in the past. On the contrary, if the EU successfully anchors its »reformed« investor rights in the TTIP, this will enhance the legitimacy of the globally contested investment protection regime.

In an attempt to situate the debate, I will begin by reviewing the development of international investment law. In a second step, I will present problem areas of the legal field and offer some political-economic classifications. In the third section, I will outline current fractures in and conflicts over the regime of international investment law. Finally, I will trace an arc back to the current controversy within the EU: With whom is the EU negotiating on the issue of investment protection at present? What should we make of the reform agenda of the Commission? And what options are there for action leading to a more democratic, socially just and environmentally sustainable investment policy?

3.1. The Historical Development of International Investment Law

Neither transnational corporations nor global production chains would exist without foreign investment. It offers direct access to sales markets, technologies, and cheap raw materials and labour. Since it has a decisive influence on the relations of production and social relations in the recipient countries once it reaches a certain scale, it is a major factor in global power relations.

Since the postwar period, there has been an increase in intergovernmental agreements that impose certain obligations on the treaty parties in dealing with investments and investors from the other country. Such agreements can stipulate, for example, that states must immediately pay compensation for expropriations or for »measures tantamount to expropriation«, and that they grant investors direct rights to sue them before an international tribunal in cases of conflict. More than 3,200 such agreements exist worldwide, most of them on a bilateral basis (Bilateral Investment Treaties, BITs). According to the UN organisation for trade and development (United Nations Conference on Trade and Development, UNCTAD), in recent years one new investment agreement has been concluded on average per week (UNCTAD 2013: 4).

Initially, these consisted almost exclusively of North-South agreements. In the 1950s and 1960s, capital exporting countries wanted to protect their investors in their former colonies through such agreements. In the 1970s, the agreements were part of the defence against aspirations to changed economic relations, as expressed in the Declaration on the Establishment of a New International Economic Order. Finally, in the 1990s, there was a real race to invest in parts of the global South that led to an explosive increase in investment agreements. This race was fostered by the dependence on private capital flows as a consequence of the debt crisis of the 1980s, the increasingly neoliberal orientation of the programs of the International Monetary Fund (IMF) and the World Bank, as well as of the dominance of neoliberalism during this period. Accordingly, the central provisions in investment agreements are based on the idea of the »game of wealth creation« (Friedrich August von Hayek) of private capital flows in a free market immunised against state interventionism and the vagaries of democratic politics, but in need of strong, government-backed property rights in order to develop.

Why do states sign treaties that set such severe restrictions on their sovereignty? Why do they invest private tribunals with the power to review their actions, to award damages and to severely restrict government regulations? The answer involves a mixture of interests, misconceptions and ignorance – interests, because it is in the interest of capital-exporting countries to protect »their« companies abroad; misconceptions because above all developing countries hoped for more foreign investment from the treaties. However, it remains a matter of dispute whether the agreements actually lead to more investment. Quantitative studies yield contradictory results. And qualitative studies suggest that the treaties play no, or only a marginal role in the investment decisions of companies. When the EU Commission (2010: 28) polled 300 European companies, half of them did not even know what an investment agreement was (for a review of the literature, see Poulsen 2010). The promise of investment often remained unfulfilled in practice as well. When South Africa recently began to cancel bilateral investment treaties (BITs), an official declared: »We do not receive significant inflows of FDI from many partners with whom we have BITs, and at the same time, we continue to receive investment from jurisdictions with which we have no BITs. In short, BITs are not decisive in attracting investment« (Raman, 2012).

In addition to the panacea of more investment, lack of awareness of the political and economic risks of investment treaties is also an important explanation for why government enter into such agreements. In the past, negotiations often lasted only a couple of hours. Sometimes lawyers, let alone officials from ministries of justice, were not even involved. The admission by a former Chilean negotiator can serve as an example: »like most countries in the 1990s, we signed a lot of treaties not knowing sometimes what we were committing ourselves to« (Poulsen 2013: 10). The risks often become apparent only many years later when the country becomes the target of a lawsuit.

Even today, the global South most frequently finds itself in the dock in investor-state disputes. According to UNCTAD (2014: 7-8), around three-quarters of all of lawsuits that became known by the end of 2013 were directed against developing and emerging economies; in the overwhelming majority of cases – 85 per cent – the plaintiff was an investor from the global North. Argentina and Venezuela are the countries that have been most often hauled before investment arbitration tribunals. However, in times of changed capital flows, industrialised countries increasingly often also have to defend themselves: The Czech Republic is now the third most frequently sued country, with Canada ranking sixth; and almost half of the new investor-state actions initiated in 2013 are directed against industrialised countries, most of them EU member states (ibid.: 1). This trend is likely to continue, also due to the growing number of north-north investment and free trade agreements with investment protection chapters, such as the proposed agreement between the EU and the United States.

The »infringements« by states that are punishable in investor-state actions were gradually extended over the past two decades. While originally arbitrary expropriations and discrimination against foreign investors provided grounds for actions, the latter are increasingly directed against laws that were drafted democratically, in the public interest and in accordance with national law.

That these actions have any prospect of success is a result of the vaguely-formulated, but far-reaching guarantees of protection of property for investors in international investment law (Krajewski 2013, Hoffmann 2013). For example, some tribunals interpret the standard of »fair and equitable treatment« in such a way that authorities from the local to the national level always have to act completely transparently and consistently and must not disappoint the »legitimate expectations« of investors regarding the regulatory environment of their investments (Bernasconi-Osterwalder/Liu 2013). Moreover, whereas protection against »indirect expropriation« in this form is not a feature of most national constitutions, this right, anchored in investment agreements, guarantees foreign investors compensation if their property loses value as a result of regulations. Thus, a fracking moratorium is as open to attack as the German nuclear phase-out (see Box 1).

Box 1: Examples of current investor-state actions

Corporations against health protection – Philip Morris v. Uruguay and Australia: Since 2010, Philip Morris has been suing Uruguay, and since 2011 Australia. Both of these suits are directed against plain packaging for cigarettes and health warnings designed to reduce tobacco consumption. The case against Australia is being conducted via a Hong Kong subsidiary – based on the investment protection agreement between Hong Kong and Australia. Uruguay is being sued by Philip Morris International with headquarters in Switzerland – based on the Switzerland-Uruguay Agreement. The tobacco company

wants 2 billion US dollars in compensation from Uruguay, around 4 per cent of the gross domestic product of the country. The amount of the damages being sought from Australia is not known. In both cases, Philip Morris is also calling for a suspension of tobacco control laws. (Martin 2013)

Corporations against the nuclear phase-out – Vattenfall v. Germany (II): Since 2012, the Swedish power company Vattenfall has been suing the German government on the basis of investment protection rules in the multilateral Energy Charter Treaty. Vattenfall wants over 3.7 billion euros in compensation for the decommissioning of the Krümmel and Brunsbüttel nuclear power plants in the context of the German nuclear phase-out following the Fukushima disaster. Both of these fault-prone reactors were already off line when the German parliament passed the law to phase out nuclear power. This is already the second action that Vattenfall has brought against Germany (see Box 2). (Bernasconi-Osterwalder/Hoffmann 2012)

Corporations against environmental protection – Lone Pine v. Canada: The oil and gas company Lone Pine has been suing Canada since 2012 for 250 million Canadian dollars in damages. Because of the danger of environmental destruction posed by fracking, the province of Quebec issued a moratorium on the controversial deep drilling technique and in this context revoked a number of drilling licenses. Lone Pine is headquartered in Canada, but it is suing the country through a letterbox company in the US tax haven of Delaware based on the investment protection provisions in the North American Free Trade Agreement (NAFTA) between the US, Canada and Mexico. (Attac et al. 2014: 5)

Corporations against water protection – Pacific Rim v. El Salvador: Since 2009, the mining company Pacific Rim has been conducting a lawsuit against a mining moratorium in El Salvador based on the investment protection rules in the Central America Free Trade Agreement (CAFTA) between the United States and several Central American countries. The moratorium was imposed following massive popular protests against environmental destruction and water pollution from mining activities. Because Pacific Rim cannot open its planned gold mine »El Dorado« as a result, the corporation wants 301 million US dollars in compensation for the loss of the expected profits, hence about 1 per cent of the gross domestic product of the country. Pacific Rim is headquartered in Canada (which is not a party to CAFTA) and is conducting its action through a subsidiary in the US state of Nevada (see: http://www.miningwatch.ca/categories/company-country-issue/company/pacific-rim).

Corporations against compensation for environmental crimes – Chevron v. Ecuador. Since 2009, the US multinational oil company Chevron has been suing Ecuador on the basis of the United States-Ecuador investment agreement, because it had been sentenced by Ecuadorian courts to pay 9.5 billion US dollars in compensation to indigenous communities for massive environmental pollution – wrongly, according to Chevron. To date, the three-man tribunal which is hearing the case has found in favour of the corporation and has called upon the government of Ecuador not to carry out the sentence. The fact that Ecuador has rejected this by appeal to the separation of powers in its constitution is now being interpreted by Chevron as a violation of the standard of »fair and equitable negotiation« in investment law – for which Chevron is in turn seeking compensation (see: http://apoya-al-ecuador.com/en/history-of-texaco-in-ecuador/).

Corporations against the debt haircut – Poštová Banka & Istrokapital v. Greece: The Slovak Poštová Banka and its Cypriot shareholder Istrokapital have been suing Greece since 2013 on account of

the haircut on the country's sovereign debt. In 2010, Poštová Banka had bought Greek government bonds at a knockdown price. When Greece was negotiating a reduction of the debts with its creditors two years later, the bank opposed the haircut. The legal basis for the action is provided by bilateral investment agreements between Greece and Slovakia and between Greece and Cyprus. The level of damages demanded is not known. (Corporate Europe Observatory/Transnational Institute 2014: Chapter 3).

Corporations against the minimum wage – Veolia v. Egypt: Since 2012, the French utility company Veolia has been suing Egypt based on the bilateral investment agreement between France and Egypt for an alleged breach of a contract for waste disposal in the city of Alexandria. The city had refused to make changes to the contract which Veolia wanted in order to meet higher costs – in part due to the introduction of a minimum wage. In addition, according to Veolia, the local police had failed to prevent the massive theft of dustbins by the local population. According to media reports, Veolia wants 82 million euros in compensation. (Karadelis 2012)

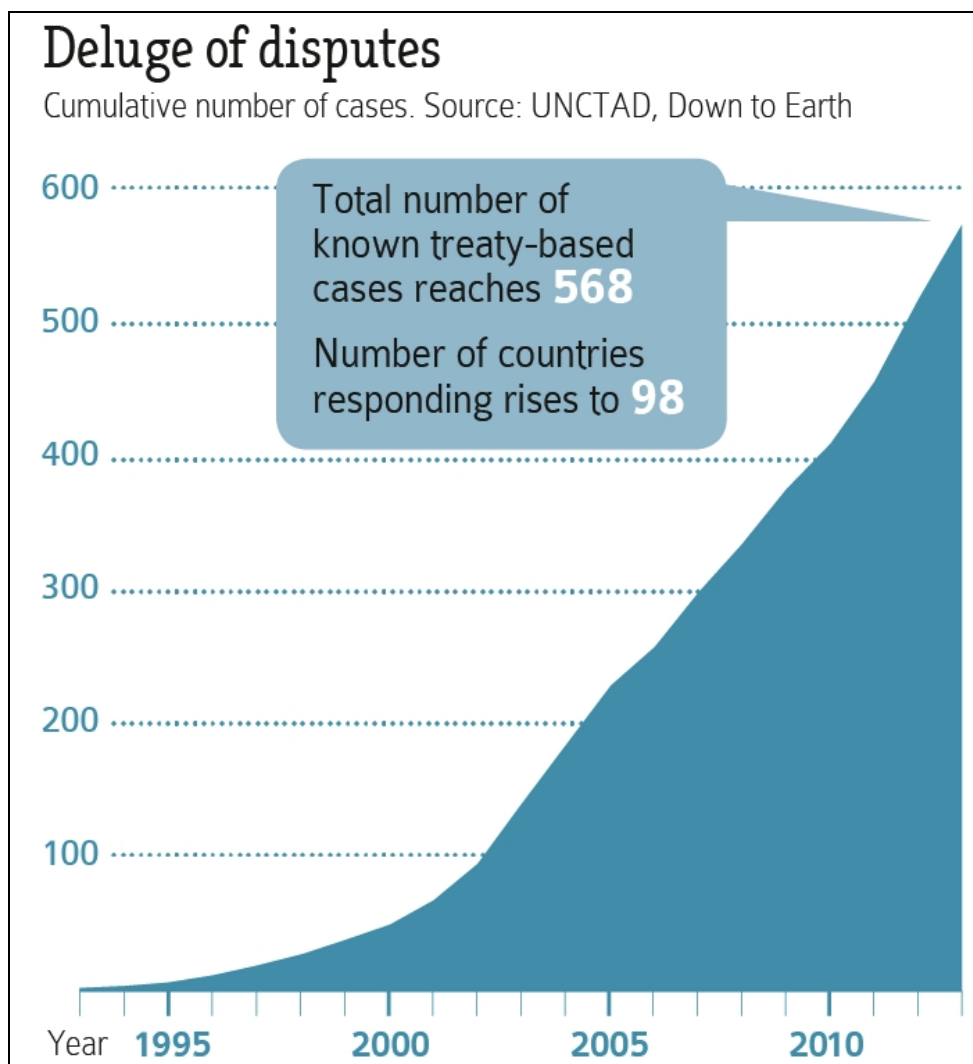
Corporations against the Arab Spring – Indorama v. Egypt: Since 2011, the Indonesian textile group Indorama has been suing Egypt because an Egyptian court ordered the re-nationalization of a textile factory that had been privatized – according to the court, unlawfully – under the Mubarak regime. The judgement had been preceded by a strike and occupations by textile workers calling for the re-nationalization of the company and for better working conditions and wages. (Perry 2011)

Corporations against patent law – Eli Lilly v. Canada: The US pharmaceutical company Eli Lilly has been conducting an action since 2013 against Canada's patent law on the basis of the investor protection in NAFTA, because Canadian courts had declared two of its patents on medicines void. The patents for Strattera to treat attention deficit and hyperactivity disorder and Zyprexa to treat schizophrenia were revoked because the promised benefit had not been adequately demonstrated in a short test phase with a small number of test persons. Eli Lilly wants 500 million US dollars in compensation and is also attacking Canadian patent law, according to which a patent is granted only if the promised benefits of an invention can be adequately proven at the time of the patent application. (Trew 2013)

Corporations against environmental protection – Renco v. Peru: Because the mining company Doe Run had not satisfied the promised environmental protection measures at a metal smelting plant in the town of La Oroya in the Peruvian Andes, the government revoked its operating licence. As a result, the corporation has been conducting a lawsuit since 2011 based on the bilateral United States-Peru free trade agreement through its US parent, the Renco Group, for 800 million US dollars in damages. Environmental organizations have repeatedly declared La Oroya to be one of the most polluted places in the world. The levels of lead, cadmium and arsenic in the blood of children living there are far too high. (Public Citizen 2012)

Several factors have significantly increased the risk of states being sued in recent years. First, investor-state lawsuits have become better known in the corporate world, with the result that there has been a corresponding explosion in the number of lawsuits – from a dozen in the mid-1990s to 568 known lawsuits at end of 2013 (UNCTAD 2014: 1). The actual figure is likely to be considerably higher due to the lack of transparency of the system. And the number is set to increase. In 2013 alone, 57 new actions

were initiated, according to UNCTAD (ibid.), only one less than in the previous year, a record year for newly initiated actions.



This wave of lawsuits has made investment arbitration into a lucrative business for the legal profession (Corporate Europe Observatory/Transnational Institute 2012), which also increases the risk of litigation. With hourly rates of up to 1,000 US dollars for lawyers in investor-state proceedings, it is not surprising that law firms continually encourage their multinational clientele to bring suits – for example, when states take measures to combat economic crises. The commercial arbitrators, who earn more the more cases that are brought, tend to interpret vague investment law broadly, and hence in favour of the investor, which increases the chances of future lawsuits (see 2.3). Finally, law firms and hedge funds reduce the financial risk for plaintiffs, because they conduct »litigation funding« as a business and assume the legal costs in investor-state lawsuits, only to collect portions of the compensation paid to the investor later.

A third development that has led to an increase in the risk of litigation in recent years is the trend towards »investment structuring« or so-called »treaty shopping« by means of an extensive network of foreign subsidiaries, in part created for this purpose. Thus, an investor A can make an investment in country B through a subsidiary in country C, for example, if an especially investor-friendly agreement exists

between countries B and C – and then sue country B on the basis of this agreement. The result of this investment structuring are lawsuits such as that of the Canadian corporation Lone Pine, which is suing its home country Canada through a letterbox company in the United States (see Box 1).

3.2. Problem Areas of International Investment Law

In the following, four problem areas of investment law and investment arbitration will be distinguished: a) the risks for public finances and the taxpayer, b) the risks for the regulatory autonomy of the state, c) constitutional problems in the context of the privatization of law, and d) the threats to democracy.

3.2.1. The Threat to Public Finances

The dangers posed by investor-state lawsuits for public finances and for taxpayers are manifest: they can lead to compensation payments running into billions of dollars or euros. The costs incurred by states in this connection are continually increasing: in 2012, an arbitral tribunal ordered Ecuador to pay thitherto historically unprecedented damages to the tune of 2.4 billion US dollars (including interest and legal costs). That is just under 3 percent of the country's gross domestic product and corresponds to the annual national health spending for seven million Ecuadorians (Public Citizen 2012a). The US company Occidental had brought – and won – a lawsuit because the country had unilaterally revoked its oil extraction contracts with the company.

The legal fees for investor-state lawsuits alone can drain the public purse. According to the OECD (2012: 19), they amount to 8 million US dollars on average per case, though they can also be considerably higher. According to media reports, the Philippine government has spent 58 million US dollars on its defence against two lawsuits brought by the airport operator Fraport – money with which they could have paid 12,500 schoolteachers or simply built two new airports (Olivet 2011: 4). Since to date the arbitral tribunals have tended to have the parties foot their own legal bills, a country may have to shoulder the legal costs even when it does not lose a lawsuit. The European Commission wants to change this, however, and to stipulate that the losing party has to bear all of the legal costs. As it happens, the German government has made a provision of 6.5 million euros to cover litigation fees and retainers for its defence against the ongoing Vattenfall suit. According to a question time in the German parliament, almost 700,000 euros have already been spent; 2.2 million euros have been earmarked in the 2014 budget, 2 million for 2015 and 1.6 million for 2016 (Deutscher Bundestag 2014: 32).

3.2.2. Encroachments on the Regulatory Autonomy of the State

A second problem area is the pressure exerted by investment agreements and investor-state lawsuits on state regulations. Sometimes even the threat of a lawsuit is enough to stifle or dilute pending legislation – »regulatory chill« as this is known in the jargon. Five years after the NAFTA free trade agreement between Mexico, Canada and the United States came into force, a Canadian government official described the phenomenon as follows: »I've seen the letters from the New York and DC law firms coming up to the Canadian government on virtually every new environmental regulation and proposition in the last five years. They involved dry-cleaning chemicals, pharmaceuticals, pesticides, patent law. Virtually all of the new initiatives were targeted and most of them never saw the light of day« (quoted in Greider 2001).

In fact, companies seem to be using international investment law today more as a weapon or for »pre-emptive strikes« in political disputes surrounding regulation than as a protective shield against encroachments by the state.[2] Thus on two occasions in Canada tobacco control laws were shelved after the tobacco industry had threatened to bring NAFTA lawsuits. In Indonesia, companies were exempted from a ban on mining in the rainforest after they had threatened to bring a corresponding case against the state before an arbitral tribunal (Tienhaara 2011). Vattenfall also achieved the dilution of an environmental restriction imposed on the controversial coal-fired power station in the Hamburg district of Moorburg (see Box 2) in the context of the settlement in its first investment lawsuit against Germany. And the New Zealand government has announced that it will delay the implementation of its tobacco control laws pending a decision in the action taken by Philip Morris against Australia (Turia 2013; see also Box 1). Even if the tobacco company loses this lawsuit, it will nevertheless have achieved the desired effect, namely delaying legislation to reduce tobacco consumption in other parts of the world at least for a couple of years. Philip Morris' profits will continue to flow freely during this time – with society as a whole incurring increased costs for health care spending.

Aside from diluting, preventing and delaying regulations, investor-state litigation can lead to the profits that individual companies have lost as a result of policy reforms being socialised, even when the regulations in question are necessary to protect the public interest. According to American author William Greider (2001), that is precisely the function of the investor rights in agreements such as NAFTA: they are part of a »long-term strategy, carefully thought out by business« to redefine »public regulation as a government ›taking‹ of private property that requires compensation«. In other words, those who regulate should pay.

Central for this »new international super basic right to unhindered exercise of investment« (Prantl 2014) is the usual protection in investment agreements against »indirect« expropriation and »regulatory takings«, thus protection against measures which, it is argued, have a similar economic effect to the seizure of property. The consequences of this doctrine of protection against indirect expropriation are far-reaching, according to Greider – and intentional: »Because any new regulation is bound to have some economic impact on private assets, this doctrine is a formula to shrink the reach of modern government and cripple the regulatory state – undermining long-established protections for social welfare and economic justice, environmental values and individual rights. Right-wing advocates frankly state that objective – restoring the primacy of property against society's broader claims« (Greider 2001).

The range of policy measures that are open to attack based on a doctrines such as the protection against indirect expropriation has been vividly described by two lawyers from the law firm Luther – as it happens, in a brochure published by the former German government with the alarming title *Help, I'm been expropriated!* In this brochure, one can read: »The potential diversity of harmful state action is virtually unlimited« and taken as a whole can indeed be tantamount to expropriation. For example, the state could introduce new taxes that make it economically pointless to continue to conduct a specific business; or it could enact environmental laws that prohibit previously manufactured goods or reduce

[2] Zachary Douglas, then still at Cambridge University and now a solicitor at the firm Matrix Chambers, mentioned this trend at the conference *50 Years of Bilateral Investment Treaties* in Frankfurt, 1.-3.12.2009.

state-regulated tariffs, for instance in the electricity, gas or telecommunications sectors or in toll roads, and thus destroy the financing of a project (Germany Trade and Invest 2011: 5).

3.2.3. Circumventing the Rule of Law

Investment arbitration involves a privatized legal system modelled on the arbitral procedure for resolving disputes between two companies. This »shadow justice in luxury hotels« (Henrich et al., 2013) is completely unsuitable for reviewing all state regulatory instruments and rulings concerning damages reaching into the millions or billions, for which the taxpayer ultimately has to foot the bill.

To recall, no regular court in the world has as much power as the private tribunals that decide on investor-state lawsuits. One of the arbitrators described this vividly: »When I wake up at night and think about arbitration, it never ceases to amaze me that sovereign states have agreed to investment arbitration at all (…) Three private individuals are entrusted with the power to review, without any restriction or appeal procedure, all actions of the government, all decisions of the courts, and all laws and regulations emanating from parliament« (quoted by Corporate Europe Observatory/Transnational Institute 2012: 34).

The »constitutional perversion« (Prantl 2014) represented by private arbitration is made apparent by the break with central constitutional principles:

- of equality before the law (The private courts are only for »foreign« investors; »normal« businesses and people have to make do with »normal« courts),
- transparency of procedures (Like the arbitral awards, they are generally secret) and
- procedural fairness (Affected third parties, such as a municipality against whose decision an action is being brought, have no right to information, to express their views or to have them taken into consideration).

Moreover, it involves a one-sided parallel law in which only investors can take actions, but not the state, when investors, for example, violate human rights or pollute the environment. No obligations are imposed on investors.

In this asymmetrical legal system, the breach of the principle of judicial independence becomes especially problematic. The cases are not heard by regular courts with judges who enjoy tenure and cannot be removed from office in the case of »unwelcome« judgments. Before such a regular court, it would be decided in advance or through a randomised procedure which judges would receive which cases. Their salaries would be assured regardless of their judgements and the number of cases they heard. These are all important institutional safeguards for judicial independence.

Investor-state cases, by contrast, are heard by ad hoc tribunals which are generally made up of three private persons appointed by the parties to the dispute and paid an hourly or daily fee per case. In the most widely-used institution for legal actions taken by investors, the Washington International Centre for Settlement of Investment Disputes (ICSID), the arbitrators earn 3,000 US dollars per day (ICSID 2013: 1). For the most part, the same arbitrators are appointed over and over again. They are known by insiders as the »club« or the »inner mafia« (quoted from Corporate Europe Observatory/Transnational Institute 2012: 36, 38). A mere 15 of them decided 55 per cent of the investor lawsuits that became known by the end of 2011 (ibid.: 38).

This points to a tangible conflict of interests. More investor-state claims ensure that these »entrepreneurial arbitrators« (Menon 2012: 15) receive more nominations and remuneration in the future. In an asymmetrical legal system in which only one side (the investor) can take actions, this is a major incentive to keep the system litigation-friendly through rulings and legal interpretations favourable to investors. An empirical study of 140 investment protection lawsuits showed that the arbitrators do in fact tend to interpret certain clauses expansively, and hence in favour of the investor (van Harten 2012). An example of an investor-friendly interpretation of the concept »foreign investor« is, for example, recognising a 98 per cent Ukrainian-owned company as a Lithuanian investor and allowing an investor-state lawsuit against Ukraine based on its investment protection agreement with Lithuania. This is what happened in Tokios Tokelés v. Ukraine (ICSID Case No. ARB/02/18).

The lack of independence and the propensity to make investor-friendly legal interpretations shows that the alleged neutrality of private arbitration, which is continually invoked by its proponents, leaves a lot to be desired. Arbitral tribunals are simply not »fairer«, to quote a recent headline from the *Frankfurter Allgemeine Zeitung* – as it happens, penned by a former investment protection lawyer (Bubrowski 2014). The inherent bias of arbitration also makes clear that there will not be »easy reforms leading to a better system« (Griebel 2014), as long as the interpretation of the law is entrusted to a private judicial machinery with a financial and career interest (see point 4).

3.2.4. Erosion of Democracy

The ultimate aim of investment law is to place restrictions on counter-hegemonic forces and democracy. A quote from two lawyers from Milbank (Nolan/Baldwin 2012: 49), one of the leading law firms in international investment law, makes this clear: »Adverse government actions do not have to take place only with autocratic rule. The populism that democracy can bring often is the catalyst for such actions.« It is no wonder that countries like Argentina and Ecuador that have revoked privatisations and nationalised companies following fierce social unrest, are among the countries that have most often been the targets of lawsuits in investment arbitration.

The research program on »new constitutionalism« which is deeply influenced by Stephen Gill is suitable for a critical analysis of international investment law. It studies political-juridical structures that safeguard neoliberalism and existing property relations through quasi-constitutional restrictions on the scope for state intervention and democratic control. The political is being redefined as a result – for example, when investment policies are depoliticised and removed from democratic control by enshrining economic principles in investment agreements.

Democracy is also being curtailed by absolutising private property rights and privileging foreign investors. Only foreign investors – or those who »heave« themselves into such a status by structuring their investments accordingly (see above) – have the opportunity to intervene in political debates over regulations by threatening to bring expensive investor-state lawsuits in a parallel legal system to which they alone have access and in which states are regularly ordered to make high compensation payments. Compared with other social groups – unions, domestic companies, citizen initiatives – this gives them a great deal of power to influence political decisions in their own interest. Only they can appeal to the excessive protection of private property in investment law, which is broader than that enshrined in most

national constitutions, and is blind to the social responsibility of ownership (see, among others, Hoffmann 2013). Thus whereas »compensable de facto expropriation« does not exist in the German constitution (Dederer 2012), according to investment law indirect appropriation always calls for compensation – even if it promotes a public purpose. Anticipated future profits are not deemed to be part of private property worthy of protection under German law either, whereas investors are regularly awarded compensation for the expected profits they have lost in investor-state lawsuits.

Another effect of investment agreements is the constitutional codification of what Joachim Hirsch has called the »internationalised competition state«, whose function is less that of a controlling instance of economic actors than to gear the national and regional levels to global competition by harmonising policies. The legal scholar David Schneiderman (2008) has studied this taking the example of numerous constitutional changes (in Latin America, for example) through which, as a result of an investment agreement, conceptions of property that restrict private property rights for the purpose of social redistribution by the state were displaced from national constitutions in favour of the liberal conception. As a result, the state is being strengthened in its function as an enforcement mechanism of private property rights, while its redistributive and social policy competences are being truncated.

Box 2: Examples of concluded investor-state lawsuits

Companies against anti-discrimination – Foresti et al. v. Republic of South Africa: In 2007, Italian and Luxembourg investors sued South Africa for 350 million US dollars in compensation, because a new mining law contained anti-discrimination elements in favour of blacks from the Black Empowerment Act. According to this law, the investors would have had to sell shares in the company to »historically disadvantaged South Africans«. The case was declared to be closed in 2010 after the investors had received new licenses, requiring a much lower divestment of shares. (IAPP 2011)

Corporations against nature conservation – Metalclad v. Mexico: The US waste disposal company Metalclad sued Mexico in 1997 on the basis of the NAFTA agreement for 90 million US dollars in damages. The background was the expansion of a waste disposal plant for toxic waste in a Mexican municipality. Although the facility had been approved by the Mexican government, the municipality had subsequently ordered a suspension of building work and the federal state declared the area to be a nature conservation zone. Metalclad sued on the grounds of expropriation and won 16.2 million US dollars in compensation. (Public Citizen 2014: 22)

Corporations against policies to combat economic crises – Investors v. Argentina: Argentina was sued a total of 41 times on account of measures it took to combat its economic crisis in 2001/2, including the devaluation of the peso, caps on water, gas and electricity charges, as well as debt restructuring measures. Up to January 2014, the country had been ordered to pay a total of 980 million US dollars in compensation. The legal defence costs in a case that is still pending alone amount to 12.4 million US dollars. (Corporate Europe Observatory/Transnational Institute 2014: 12).

Corporations against environmental and health protection – Ethyl vs. Canada: When the Canadian Parliament banned the import and transportation of a toxic petrol additive on environmental and health protection grounds in 1997, the US producer Ethyl sued on the basis of the NAFTA agreement for 201

million US dollars in compensation. Canada agreed in a settlement to pay 13 million US dollars and withdrew the trade restrictions. (Public Citizen 2014: 11)

Corporations against environmental protection – Vattenfall v. Germany (I): In the case brought in 2009 over 1.4 billion euros compensation based on the Energy Charter Treaty, the bone of contention was the coal-fired power station in the Hamburg district of Moorburg which was controversial on climate policy grounds. Vattenfall considered the requirements imposed for removing cooling water from the Elbe river to be too strict. The case was settled in 2011 by mutual agreement after the environmental requirements for Moorburg had been relaxed. The legal dispute over the power station in the German domestic courts continues. (Bernasconi-Osterwalder/Hoffmann 2012)

Corporations against national courts – Deutsche Bank v. Sri Lanka: In October 2012, an arbitral tribunal ordered Sri Lanka to pay 60 million US dollars in compensation plus interest and 8 million US dollars legal costs to Deutsche Bank for breaches of the investment agreement between Germany and Sri Lanka. Because of allegations of corruption, the highest court in the country had decreed that payments to the bank, which would have been due according to a hedging agreement with the state oil company, should be suspended. The decision has whetted appetites in the financial sector because it recognises a financial market instrument as an investment worthy of protection – even though it did not involve any physical business activity by Deutsche Bank in Sri Lanka. (Bret 2013)

3.3. Fractures in the International Investment Law Regime

However, these procedures are not free of contradictions. On the contrary, there are unmistakable fractures in and fierce conflicts over the international investment law regime. Social movements successfully scandalise individual cases; critical researchers denounce the risks for government regulation, public finances and democracy; and some states have turned their backs on parts of the regime and are trying to create alternatives. Even among proponents of the regime there is talk of a crisis of legitimacy that needs to be addressed (e.g. Waibel et al. 2010). [3]

Above all in the global South, resistance is growing to the neoliberal supra-constitution of international investment law. South Africa has cancelled agreements with several EU countries, including Germany, and declared that further treaties from the post-apartheid era, which the country had hastily concluded at the time in the hope of attracting investment, will follow. Indonesia has recently announced similar steps. According to media reports, India is drafting a model agreement for investment protection that is supposed to differ markedly from the models of the post-colonial era and of the 1990s and 2000s. Bolivia, Ecuador and Venezuela have cancelled a number of investment agreements and withdrawn from the ICSID convention which establishes the centre of the same name at the World Bank. In Ecuador, a commission is examining whether the country's agreements are compatible with national law. At a meeting of the countries of the Bolivarian Alliance for the Peoples of Our America (ALBA) in April

[3] For an overview, see the website of the Network for Justice in Global Investment: http://justinvestment.org/ (accessed 03.09..2014). See also Public Statement on the International Investment Regime 2010; Statement of Concern about Planned Provisions on Investment Protection and Investor-State Dispute Settlement (ISDS) in the Transatlantic Trade and Investment Partnership (TTIP) 2014.

2013, a review of existing treaties was likewise agreed, as well as the establishment of a separate regional institution for resolving conflicts with foreign investors.

A paradigm shift is also taking place in some industrialised countries and international organizations. The social-democratic Gillard government in Australia had declared in 2011 that it would no longer negotiate investor-state arbitration in its free-trade agreements. The conservative successor government has also recently signed an agreement with Japan which does not include investor-state dispute settlement. And whereas the UNCTAD urged countries of the South to sign investment agreements especially during the 1990s, in recent publications (2012, 2013a) it outlines options for reforming current investment policies – ranging from more clearly circumscribed rights for investors to duties for investors. In addition to UNCTAD (2013b: 3-4), even the IMF (2012: 42) now warns that investment agreements can severely restrict states in combating economic and financial crises.

3.4. The Debate within the EU over the Future of Investment Law

The debate over investment policy at European level has now broken out in the midst of this tough struggle over global investment law. Until the Treaty of Lisbon entered into force in December 2009, the EU did not have any authority to negotiate investment protection treaties and corresponding chapters in free trade agreements. This was the sole responsibility of the EU member states, which to this day are world champions in this area: they have concluded around 1,400 of the over 3,200 investment agreements worldwide; no country has more bilateral treaties than Germany (139, of which 131 are in force).[4] Moreover, investors based in the EU are assiduous litigants: most of the investor-state lawsuits that attracted worldwide attention were indeed brought by investors from the United States (127 lawsuits), but they are followed by investors from the Netherlands (61 lawsuits), the United Kingdom (43 lawsuits) and Germany (39 lawsuits) (UNCTAD 2014: 8).

A controversy has been raging since 2009 over how investment protection should be designed in future across the EU. The provisional result of the debate is a series of corporation-friendly guidelines and mandates for investment protection negotiations between the EU and Canada, India, the United States, Japan, Morocco, Tunisia, Egypt, Jordan, China and the ASEAN countries (Brunei, Myanmar, Cambodia, Indonesia, Laos, Malaysia, the Philippines, Thailand, Singapore and Vietnam).

A number of non-governmental organizations were able to use the negotiations with the United States to politicise the issue and mobilise large sections of civil society against the transatlantic corporate bill of rights. The European Commission (2013) is responding to this politicisation with an aggressive PR campaign which is designed to allay the public's concerns and promises a »new start« on the issue of investment protection. Vaguely-worded investor rights, such as »fair and equitable treatment« or protection against »indirect expropriation«, are supposed to be clearly defined, the state's »right to regulate« to be protected and the dispute settlement procedures to become transparent and independent. Lawsuits such as those of Philip Morris against tobacco control laws in Australia and Uruguay would no longer be possible under the reformed investor rights, according to the Commission.

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[4] See the overview of the bilateral investment promotion and protection agreements (IFV) of the Federal Republic of Germany: http://www.bmwi.de/BMWi/Redaktion/PDF/B/bilaterale-investitionsfoerderungs-und-schutzvertraege-IFV,property=pdf,bereich=bmwi,sprache=de,rwb=true.pdf (accessed 03.09.2014).

Closer examination of the reform proposals reveals that this is not the case.[5] First, the supposedly watertight definitions of investor rights continue to contain many loopholes for broad, investor-friendly interpretations by arbitrators. Thus, for example, the general clause »fair and equitable treatment« is framed even more broadly than for instance under the NAFTA agreement. This is extremely dangerous, because this catch-all clause has developed into an all-purpose weapon for investors with which they win most lawsuits (Bernasconi-Osterwalder/Liu 2013). The Commission now wants to extend the standard so that it expressly protects the »legitimate expectations« of an investor. Could tax increases disappoint the »legitimate« expectations of an investor when previously low tax rates promised fat profits? Could a moratorium on fracking contradict the fair and equitable treatment of a gas company if a government had previously signalled its support for the controversial drilling method? Would any change in the legal and economic environment in which an investor operates still be permissible? In view of the arbitrators' inclination to answer such questions in favour of the investor, the concern over their interpretations is certainly well founded.

Second, many of the proposals being touted by the Commission as innovations can already be found in existing treaties or are already applied by arbitral institutions such as the ICSID – for instance, the intended and rather vague code of conduct for arbitrators and rules that allow abusive actions without any legal basis to be rejected in a simplified procedure. It is unlikely that these rules will put an end to the thriving business in combatting policies through investor-state lawsuits – to date they have not managed to do so either.

Third, with the exception of the transparency of the procedure, the »constitutional perversion« (Prantl 2014) that private arbitration represents is not even broached by the Commission. Hearings and requests for arbitration, as well as other essential documents, are supposed to be published in future; but instead of equality before the law, there are still special rights and special courts for investors. Their parallel legal system remains one-sided, because the Commission's proposals do not contain obligations on investors, for example, to respect labour rights.[6] Affected third parties will still not have legal standing in the proceedings,[7] and there will still be no institutional safeguards to guarantee the independence of the arbitrators, who will continue to be appointed by the parties and to be paid per procedure in future.[8] And appeal proceedings before independent courts are not envisaged in the foreseeable future.[9]

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5 For a detailed and critical analysis of the Commission's reform proposals, see van Harten (2014), IISD (2014), Krajewski (2014), Corporate Europe Observatory (2014: Annex 1 and 2) and the statement of ver.di in this volume.

6 According to the Commission's proposals, an investor would indeed forfeit the right to file lawsuits if investment has been made in a corrupt manner, but this is not the same as a duty to prevent corruption.

7 Although, according to the plans of the Commission, NGOs or trade unions are supposed be able to submit their own opinions to the proceedings (so-called *amicus curiae* submissions), this is not the same thing as the right to intervene in and even to become a party to the dispute – for example, in the case of an affected municipality whose measure is being reviewed in an investor-state lawsuit.

8 Although the Commission has announced a code of conduct for the arbitrators in future, such a code should not be confused with institutional guarantees of judicial independence, such as tenure for judges which prevents the less agreeable among them from being suspended.

9 The European Commission has indeed announced that it wants to work towards an appeals mechanism, but such declarations of intention have existed in US contracts for years – without having led to such a mechanism. In the negotiations, the United States has already expressed scepticism regarding this proposal towards the EU.

Therefore, the Commission's reform proposals do not substantiate the promised new start in international investment law. Instead they involve marginal »mini-reforms« intended to re-legitimise the increasingly contested global legal field without touching the hard core of corporate privileges. The »reformed« investment protection à la the European Commission would also grant foreign investors more extensive private property rights than those contained, for example, in the German constitution. In addition, they would continue to have access to an exclusive corporate-friendly parallel legal system, in the form of private arbitration, to enforce these rights. Therefore, future EU investment agreements would also be part of the new constitutionalism that disciplines governments and places restriction on counter-hegemonic actors and redistribution processes.

Therefore, it is no surprise that even traditional hardliners on investment protection have overcome their initial scepticism to endorse the Commission's agenda. The recent position paper of the Federation of German Industries (BDI 2014), for example, is almost indistinguishable from the proposals of the EU bureaucracy.

When it comes to the central open questions concerning investment arbitration, however, neither the European Commission nor its friends from the BDI provide answers: Why should we grant tribunals composed of three private persons, which violate fundamental constitutional principles, the power to circumvent our legal system and review all laws enacted by our parliaments, all decisions of our governments and all verdicts of our courts, and to impose high compensation payments? And why should we grant a single group in our society – foreign investors – the power to take actions before these tribunals, and thereby to expand their power in the political process, without even a mention of imposing duties on them?

3.5. What Should be Done?

The support of the business lobby for the Commission's reform agenda already indicates that it probably does not point the way to a socially just, environmentally sustainable and democratic investment policy. Those who are concerned about this should not let themselves be distracted by the »mini-reform« proposals. Nevertheless, the current politicisation of the topic in the EU presents opportunities for a genuine fresh start in investment policy along the following lines:

- Future investment agreements should neither include the unilateral dispute settlement nor go beyond the rights of private property conferred by the protection of property enshrined in national constitutions.
- Moreover, they should stipulate binding obligations on investors, such as duties to respect human and workers' rights, to protect the environment and climate and to pay taxes in the host country.
- Existing treaties should be cancelled or renegotiated so they do not restrict the regulatory autonomy of the state and neither contradict human nor workers' rights nor other societal goals such as sustainable development, nor violate constitutional principles.

As it happens, even then foreign investors would be far from defenceless. Today already, they have instruments for insuring themselves against political risks abroad, ranging from market-based private insurance, through the public insurance provided by the Multilateral Investment Guarantee Agency (MIGA), to agreements that individual investors can conclude with the host country. Joint ventures with

companies from the host country or financing through loans from local banks also significantly reduce the risk of being arbitrarily expropriated by the host country.

The fractures in the global investment regime, which are currently being exacerbated, offer many starting points for a genuine fresh start in investment policy. The history of opposition to free trade and investment agreements has also shown that these anti-democratic neoliberal straitjackets can be prevented if the texts negotiated in secret can be made public and politicised. Thus, in the late 1990s the anti-globalization movement dragged the largely unknown Multilateral Agreement on Investment (MAI) – an investment agreement that had been negotiated within the framework of the OECD – into the public spotlight. Like a vampire, it did not survive long once caught in the rays of critical public debate. In October 1998, France put a stop to the negotiations. Forces for emancipation in Europe should do their utmost to ensure that this part of the story repeats itself in the controversy over the TTIP – and also in the case of all of the other planned corporate constitutions currently being negotiated by the EU.

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4. Labor Rights and Labor Standards in Transatlantic Trade and Investment Negotiations: An American Perspective

Lance Compa

4.1. Introduction

A new trade and investment agreement between the United States and the European Union should improve living and working conditions of peoples on both continents. To accomplish this, negotiators should sow high social standards in a transatlantic deal. Otherwise, bankers, investors, and corporations will harvest the benefits of expanded trade for themselves, while working people and their families reap the husks. Supporters of the North American Free Trade Agreement and other trade pacts since NAFTA promised that increasing the volume of trade and investment would automatically improve wages, benefits and working conditions among trading partners. But NAFTA never delivered. When parties to an agreement have wide disparities, a race to the bottom becomes the path of least resistance for profit-minded investors.

The volume of North American trade expanded under NAFTA, but resulting benefits flowed to already-wealthy elites, not to workers, their families, and the general population in any trading partner. Wages stagnated, social protections declined, and violations of workers' organizing and collective bargaining rights continued unabated (see also Raza et al. in this volume).

Other US trade agreements reproduced similar results. Many US trading partners such as Colombia, Guatemala, Honduras, Mexico, Bahrain, and Jordan have seen detention, persecution, exile and murder of trade union and human rights activists since the trade agreements were signed.

EU-US trade negotiations create an opportunity to get it right. In theory, having very similar economic and social standards in both trading partners can block a "race to the bottom" on wages and working conditions. The challenge is to put theory into practice. To accomplish this, negotiators should not proceed on the false premise that the US and the EU already have high standards, so a pact can focus on commerce and investment without purposeful enhancement of social standards.

Conventional wisdom has it that both the US and member states of the EU have high wages, extensive social protection systems, good labor laws, and well-functioning legal systems to enforce them. Under this view, the transatlantic economic relationship starts with a strong social dimension as a default feature and avoids the messy complications of labor abuses that trade deals with developing countries failed to cure.

Reality belies such complacency. Many areas of labor law, labor rights, labor standards, and social protections in the transatlantic context have severe flaws. If negotiators do not address them, on the mistaken premise that more trade automatically advances labor standards, they invite transatlantic race-to-the-bottom competition instead of an upwardtrending social dynamic.

EU and US trade negotiators have a choice. They can ignore labor rights and labor standards and open a wage-cutting, security-destroying, inequality-driving "low road" to more trade and investment. Or they

can make labor rights and standards a centerpiece of a transatlantic agreement that pushes nations and firms to advance on a high road. On this path, trading partners will aim for improved education and training, research and development, design and marketing, technology and human resources, corporate governance and industrial relations and other productivity-enhancing measures, not labor cost cutting. In short, the United States and Europe must craft a trade agreement that encourages better public policies, better management, and higher labor standards, not more exploitation of workers and widening of social and economic inequality.

4.2. Challenges

The most important challenges regarding labor relations and standards in transatlantic trade talks are these:

- Addressing inequality without fear of investors' challenges
- Protecting the social safety net and harmonizing labor standards upward to prevent "low road" competition
- Correcting the "rights imbalance" on workers' freedom of association and collective bargaining.

4.2.1. Inequality and Investor-State Dispute Settlement

An important challenge for an EU-US trade agreement is to effectively address the worsening inequality on both continents resulting from a 20-year trend of gains from trade flowing to the top of the income pyramid.

In the United States, income inequality has risen dramatically. The top 10 percent of earners took more than half of the country's total income in 2012, the highest level recorded since the government began collecting the relevant data a century ago. The top 1 percent took more than one-fifth of the income earned by Americans (Saez 2013 as cited in Lowrey 2013). Moreover, the new inequality risks becoming permanent (Panousi et al. 2013).

In Germany, the richest 10 percent accounted for 26 percent of total income in 1991, compared with 31 percent in 2010. Meanwhile, the lowest half of the population's share of national income fell from 22 percent in 1991 to 17 percent in 2010 (Schmidt and Stein 2013). Similar "hollowing" of the income structure has occurred in much of the rest of Europe, too. An OECD paper concluded:

> *Inequality in Europe has risen quite substantially since the mid-1980s. While the EU enlargement process has contributed to this, it is not the only explanation since inequality has also increased within a "core" of 8 European countries. Large income gains among the 10% top earners appear to be a main driver behind this evolution. (Bonesmo Fredriksen 2012)*

The first question negotiators should ask themselves is not "How can a trade agreement grease the wheels of commerce?" but "How can a trade agreement reverse the growing inequality in all our societies?" This means that a transatlantic accord should focus on restoring and preserving good working class jobs and allowing ample space for governments at all levels to enact targeted measures to address inequality.

A transatlantic trade agreement should not interfere in the name of free trade with national measures addressing inequality such as minimum wages, prevailing wage requirements, unemployment insurance, affirmative action for historically excluded groups, and other social protections. The same principle

should apply to state and local governments in the United States, and member states and subordinate powers in the European Union, that want to take local and regional steps against inequality.

A key starting point is curtailing the contemplated investor-to-state dispute settlement (ISDS) clause of an agreement. ISDS should never interfere with governmental measures such as these:

- Setting minimum wages more favorable to workers than national minimum wages, as many states and municipalities in the United States have done (see Box 1) (Selway and Efstathiou 2013)
- Guaranteeing "prevailing wage" standards for publicly-funded projects.
- Setting health and safety standards higher than national standards, or enacting new standards in areas not covered by federal law.
- In the United States, establishing "project labor agreements" (PLAs) with construction sector trade unions to ensure good wages and benefits, high productivity, and no work stoppages to complete development projects.
- Ensuring that local employees have access to jobs created by public procurement projects.
- Setting out "good jobs" requirements in procurement programs to prevent low bids based on low wages and benefits for employees – and the inevitably resulting low quality. Firms should not tender bids based on cutting jobs or cutting workers' wages and benefits. Instead, public authorities should be able to make bidders comply with any present or future workplace standard on wages, hours and working conditions.
- Maintaining or expanding public services that also provide good jobs to employees. Public authorities must retain the power to provide essential services in areas such as education, communications, health, energy and other sectors without being pressured by a transatlantic trade pact to privatize them. Too often, privatization results in lower-quality jobs and lower-quality services when low bids are based on low wages, eliminating opportunities to retain or attract skilled, experienced employees (see Box 2).
- Allowing governments at all levels to "debar" labor law violators from receiving procurement contracts. A recent exposé, for example, showed that the US federal government handed out tens of billions of dollars in contracts to companies that repeatedly violated laws on workplace health, safety, wages, and nondiscrimination requirements (Greenhouse 2013).

Without sharp limits on foreign investors' ability to challenge such measures because they might affect future profits – an avenue of recourse closed to domestic employers – governmental authorities would be handcuffed in efforts to protect working people and their families. A national, state or local measure should be susceptible to investor-state challenge only when it is not meant for general application to all employers, but is demonstrably intended to discriminate against a particular foreign investor.

Trade and investment agreements often make declarations in a preamble about the "right to regulate." For example, the preamble to the General Agreement on Trade in Services (GATS) recognizes "the right of members to regulate, and to introduce new regulations, on the supply of services within their territories in order to meet national policy objectives." But such hortatory language can be overtaken by specific provisions in the agreement that bring services under its disciplines and blocks or punishes new regulations seen as harmful by investors.

The U.S. Trade Representative has issued a “no worries” statement about investors’ ability to sue governments, boasting that the United States has never lost a case under other trade agreements. The statement concludes, “The United States has been a leader in developing ISDS provisions that protect the ability of governments to regulate, discourage frivolous claims, and ensure a high level of transparency. Through extensive work with stakeholders, legislators, and the public we will continue to ensure that the United States remains at the forefront of innovative trade policy.” (Office of the United States Trade Representative 2014)

But only seventeen cases have been brought against the United States by investors mainly based in Mexico and Canada under NAFTA (U.S. Department of State 2014).Whether European firms would use an ISDS chapter to challenge U.S. regulations, or U.S. firms would use it to fight new European standards (whether based on EU or member state measures) is a big unknown. A strong, sharp “No” must be built into a transatlantic agreement.

Box 1: The Living Wage Movement

Many European firms have entered the US retail market in recent years, opening stores where they pay employees the federal minimum wage of $7.25 per hour or slightly more. But in recent years, a growing “living wage” movement throughout the United States has won significant “living wage” increases in minimum wage laws (Sonn and Luce 2008). Last year, several states and municipalities decided to raise their minimum wage to levels between $8 an hour and $15 an hour. Under typical investor-state provisions in trade agreements, European firms – but not American firms – could claim that these state and local actions deprive them of anticipated profits, and that taxpayers should make up the difference. Such claims should be explicitly precluded in a transatlantic trade agreement.

A trade agreement’s ISDS chapter could also open up the risk of corporate challenges to regulations meant to protect public health and welfare, or to control health care costs. At the very least, existing regulations should stand. But this should not mean that future reform efforts could be blocked on grounds that they jeopardize investors’ returns. Instead of results like these, a transatlantic agreement should guarantee policy space for governments at all levels to regulate for the common good through universally applicable measures. Only a reform or regulation shown to be discriminatorily aimed at a specific foreign investor should be open to challenge.

If health care is not excluded from a transatlantic pact, future UK governments might be blocked or constrained from enacting measures to control costs and regulate privatized health services by claims from investors that such measures harm their interests in violation of the trade agreement. Similarly, governments could be blocked from bringing services back into the public sector if privatization fails to control costs and deliver highquality services, as they often do (Bel et al. 2007).

Box 2: Health Services in the UK

US-based health care insurance and provider corporations have penetrated many privatized systems and services of the UK National Health Service (NHS) (Lethbridge 2007). For example, United Health Group boasts, "In Britain, we support the government-funded National Health Service in its need to harness the opportunities provided by patient choice, payment by results and clinical commissioning . . . We provide support, analytical tools, training and consultancy services, develop bespoke programs . . . and work in partnership with Primary Care Trusts to manage parts of the commissioning process on either an interim or long-term basis. We currently serve approximately 138 NHS Primary Care Trusts and more than 6,500 physician practices. . . . We provide decision support tools to more than 60 percent of all National Health Service Primary Care organizations" (United Health Group 2012)

If health care is not excluded from a transatlantic pact, future UK governments might be blocked or constrained from enacting measures to control costs and regulate privatized health services by claims from investors that such measures harm their interests in violation of the trade agreement. Similarly, governments could be blocked from bringing services back into the public sector if privatization fails to control costs and deliver highquality services, as they often do (Bel et al. 2007).

4.2.2. Preserving the Social Safety Net and Harmonizing Upward

Another challenge is to prevent US insistence on a deregulated labor market from overwhelming the European social democratic tradition of protecting societies' most vulnerable and excluded people. In the 2014 farm bill, the Republican party-controlled US House of Representatives brutally cut off food assistance to millions of struggling, impoverished Americans. Then it added a *coup de grace* by ending extended unemployment insurance benefits for millions more. These measures were driven by US politicians who argued openly and shamelessly that poor people and unemployment people have only themselves to blame for their plight (Egan 2013). The way these politicians see it, making people more desperate will make them find jobs, and this will solve the unemployment problem.

This attitude should not be allowed to seep into transatlantic trade talks. The EU has already allowed severe fraying of the social safety net in its misguided, austerity-pushing policies since the economic crisis of 2008. Moderate pre-crisis steps such as German labor market reforms and Northern European "flexicurity" initiatives were one thing. Deep cuts in wages, pensions, unemployment benefits and basic social welfare programs in the rest of Europe are something else.

Belt-tightening at a time of deep economic recession only kills aggregate demand and worsens the recession instead of lifting an economy out of one (Lavoie and Stockhammer 2013). It is battered and bruised by the Europeans' own neoliberal ideologues, but the European social model should not be further assaulted in a transatlantic trade agreement that fails to block "downward harmonization" toward elimination of social protection "*à l'américaine*."

To ensure preservation of the safety net, a transatlantic trade agreement must keep social protections off the negotiating table. Publicly-funded benefit programs addressing unemployment, disability, job-related workers' compensation, family/maternity/ paternity leave and pay, health insurance, retirement and other

programs must be insulated from downward pressure by multinational investors using an investor-state dispute settlement chapter to claim that subsidies supporting such programs violate trade rules under the agreement.

The pressure of the economic crisis since 2008 has eroded labor and employment law standards in much of Europe. Still, the core of such social protections, absent in the United States, remains in place in Europe.

A transatlantic trade arrangement should not enshrine US-style labor market deregulation. In Europe, for example, employers must demonstrate 'just cause' to dismiss an employee. But the prevailing doctrine in U.S. law is the "at-will" rule allowing employers to dismiss staff or to cut pay and benefits at any moment and for any reason – including "a good reason, a bad reason, or no reason at all" – as long as it is not a reason prohibited by law.

Here is how one prominent US law firm describes the difference:

> *Employment-at-will offers American employers broad freedom to cut their staff's terms and conditions of employment, work hours, employee benefits—even compensation . . . Indeed, American bosses exercise this freedom regularly. . . . These cuts are perfectly legal . . . because . . . US law imposes no doctrine of vested employment rights. Outside the United States, by contrast, laws impose vested (sometimes called implied or "acquired") rights that constrain employers from unilaterally cutting employment terms, conditions, work hours, benefits and pay. (White & Case 2013)*

In addition to no law requiring just cause for dismissal or protection for acquired rights, no US law requires severance pay for dismissed workers based on their length of service. No law requires employers to provide pension benefits or health insurance. No law limits the power of companies to abruptly close workplaces.[1] No US law limits the amount of overtime work that employers can impose on workers. No law requires employers to provide vacation or holidays, or prohibits employers from forcing employees to cancel their vacations or to work on holidays. Only seven states have laws requiring rest breaks or meal breaks; no federal law does so.

These and other deregulatory features of US labor and employment law should not be a magnet for European investors under a new commercial agreement. A transatlantic trade agreement should ensure best practices in employment relations. In fact, it should reverse a trend already begun of introducing US-style labor and employment regimes in Europe, where an ominous "Americanization" is starting to take shape (see Box 3) (Porter 2013). A new trade agreement should prevent governments and firms from exploiting US-style deregulation to gain competitive advantage in trade.

[1] US law only requires a modest 60 days' advance notice of workplace closure, which can easily be evaded by claims of a sudden change in business conditions.

Box 3: Amazon in Germany

In Germany, the US distribution company Amazon has provoked widespread protests with its imposition of US-style management that treats employees like machine parts reminiscent of Charlie Chaplin in Modern Times, with no consideration for their personal dignity (Ewing 2013). Asked about workers' concerns, Amazon's German manager suggested that they have no qualifications, have long been unemployed, and are lucky to have a job (Thomasson and Schimroszik 2013). A transatlantic trade agreement should not sanctify these affronts to workers' dignity in the name of harmonized conditions of commerce. Instead, transatlantic trade negotiators should identify high standards and best practices that should be required in firms taking advantage of benefits under the agreement.

4.2.3. Rights Imbalance

Another challenge is to overcome the "rights imbalance" between Europe and the United States in workers' freedom of association. European labor law and practice generally comply with core labor standards of the International Labor Organization. The European Convention on Human Rights and the EU's charter strongly protect freedom of association and collective bargaining. However, European compliance with core labor standards can be undermined by American practices contrary to these norms.

When it comes to workers' organizing and collective bargaining rights, the United States is the bastion of 'union-free' management philosophy and refusal to accept international standards on freedom of association. In contrast to the EU, where every country has ratified ILO Conventions 87 and 98 on freedom of association, the right to organize and collective bargaining, the United States has not ratified them.

In its latest generation of trade agreements with Korea, Panama, Colombia and Peru, the United States insisted that trading partners "adopt and maintain" – and effectively enforce – labor and employment laws consistent with ILO core standards. On paper, the US undertook the same commitment (United States Trade Representative 2014).

But contrary to ILO core labor standards, U.S. law allows employers to permanently replace workers who exercise the right to strike. It also allows employers to mount one-sided, aggressive workplace pressure campaigns against workers' organizing efforts, marked by mandatory 'captive-audience' meetings and one-on-one supervisor-employee meetings scripted by anti-union consultants. Trade unions have no comparable opportunities at the workplace for employees to hear from union representatives or for pro-union workers to convey their views to fellow workers (see Box 4).

Equally contrary to international standards, U.S. law excludes millions of workers from labor law protection – farmworkers, household domestic workers, low-level supervisors, so-called 'independent contractors' who are actually dependent on a single employer for their livelihood, and many more. The ILO's Committee on Freedom of Association has found further violations in the U.S. labor law system because of weak and unavailable remedies for workers alongside unbalanced remedies favoring employers.

In large part as a result of weaknesses in U.S. law and practice, many American employers respond to workers' organizing and bargaining efforts with aggressive campaigns of interference, intimidation, and coercion to break them. Such campaigns are commonplace among U.S. companies that operate in a corporate culture imbued with strong anti-union beliefs and practices. Unfortunately, some European companies operating in the United States have adopted a "When in Rome" approach to labor relations. They allow their US managers to engage in the same severe union-busting practices that many American companies do (see Box 5) (Human Rights Watch 2010).

Box 4: De-unionizing for Competitive Advantage

In September 2009, management at a Boeing Corp. factory in Spartanburg, South Carolina dangled before employees the prospect of putting new production lines into the factory during the run-up to a vote on whether to decertify the union as workers' bargaining agent. State officials and statewide media took up the call, hammering a message that if employees failed to decertify the union, the new production might instead likely go to the company's main plant in Seattle, Washington – a plant known to have a strong union.

In the intense anti-union climate of South Carolina, one of the southern "right-to-work" states with a deeply rooted culture of harsh opposition to trade unions, coupled with the implicit promise of getting the new production line, workers voted to surrender bargaining rights (Gates 2009). In light of its longstanding rivalry with Europe's Airbus, Boeing's action raised a new form of unfair trade practice: de-unionizing to gain competitive advantage.

Box 5: Deutsche Telekom and T-Mobile

When the German telecommunications giant Deutsche Telekom joined the UN Global Compact in 2000, it said "This voluntary commitment is based not only on the values of the Global Compact but on the internationally recognized conventions, guidelines and standards of the International Labor Organization (ILO) and the Organization for Economic Cooperation and Development (OECD)." But in the United States, Deutsche Telekom's T-Mobile wireless telephone operation engages in practices directly contrary to these international standards.

T-Mobile management routinely holds mandatory captive-audience meetings at call centers around the country forcing workers to listen to anti-union speeches and watch anti-union films predicting dire consequences, including possible closures, if they form a union. The company has repeatedly run afoul of US labor law, settling charges with enforcement authorities in cases involving threats, coercion, interference, spying and other violations of workers' organizing rights. In effect, T-Mobile is violating workers' rights in pursuit of competitive advantage in the American mobile phone market (Logan 2009).

Most recently, in November 2013, the National Labor Relations Board found merit in charges that T-Mobile unlawfully dismissed one employee and disciplined another at the company's Wichita, Kansas call center because of their union activities. The Board ordered the case to go forward to trial before an administrative law judge (National Labour Relations Board 2013).

Just as distressing as interference with workers' rights by European firms in the United States is the ominous spread of US management-style anti-unionism in Europe. In September 2007, management at a Kettle Chips factory in Norwich, England engaged a US-based anti-union consulting firm to mount a vicious campaign against workers seeking collective bargaining representation with the British union Unite. The consultants held mandatory 'captive-audience' meetings for workers with anti-union speeches and videos, and trained supervisors to meet with workers to warn of possible closure, strikes and other fear-mongering messages. Swayed by these threats, workers voted against union representation (Logan 2008).

US-based anti-union consultants carried out similar campaigns in the UK against workers at Amazon UK, Virgin Atlantic, Honeywell, GE Caledonian, Eaton Corporation, Calor Gas, Silberline Ltd, FlyBe, Cable & Wireless and others. In Germany, American-style anti-union activity has taken the form of interfering with works council formation and operations (Behrens and Dribbusch 2013, 2012).

To stop such abuses, a transatlantic trade and investment pact should require multinational firms benefiting from it to apply the highest standards of industrial relations and workplace conditions in all their operations, wherever they are located. To begin, before concluding a transatlantic trade deal, the United States and EU member countries should undertake a mutual review of each other's labor laws and practice to identify those that do not comply with ILO core standards. The agreement should set out a procedure for countries to bring their laws into compliance and to ensure that practice is consistent with legislation, as a condition of multinational firms availing themselves of benefits under the agreement.

Another way to ensure "best practices" is to have EU Directives on company works councils apply to European firms in their US operations. This would give American employees to have the same rights to information and consultation as their European counterparts (see Box 6). Similarly, American companies operating in Europe should accept participation of US employee representatives in works council meetings and consultations in Europe.

Box 6: Volkswagen and a Works Council in the United States

A promising move by a European multinational company to apply its freedom of association principles in an US setting involved a Volkswagen factory and its 2,000 employees in Chattanooga, Tennessee. At the Tennessee factory which began operating in 2011, Volkswagen management indicated a willingness to implement a US version of the company's European Works Council system. Volkswagen and its employees created the works council system in 1992, predating European Union requirements. It is considered a model of a well-functioning employee participation system (European Foundation for the Improvement of Living and Working Conditions 2008). But works councils' activities are financially supported by employers, and US labor law prohibits employer financial support for organizations that represent workers. This law reflects the widespread phenomenon of 'company unions' in the 1920s and 1930s designed to prevent genuine union formation (Kohler 1986). As a result, VW can only implement its works council in tandem with trade union representation.

Volkswagen agreed with the United Auto Workers union (UAW) to remain neutral while workers decided on UAW representation. However, the company ran into a firestorm of opposition from anti-union Tennessee politicians. Senator Robert Corker issued a statement saying that VW would be a 'laughingstock' if it accepted UAW representation (Schelzig 2013). Tennessee governor William Haslam says that other firms will refuse to invest in the state if Volkswagen recognizes the UAW (Bennett 2014). State legislators threatened to cut financial support for a new product line if workers voted in favor of the union (Pare 2014). Under this onslaught of political pressure, employees voted 53-47 percent against UAW representation (Greenhouse 2014)

4.3. Other Models

4.3.1. Recent US Agreements

The experience of labor chapters in US and EU trade agreements with other countries offers lessons on what not to do, and what might be done, in a transatlantic accord. US agreements have evolved since NAFTA's "enforce your own laws, they don't have to meet international standards" approach in its labor supplemental agreement, the North American Agreement on Labor Cooperation (NAALC).

NAFTA's labor agreement only recognized laws on child labor, minimum wage, and occupational safety and health as binding under the agreement. It left untouched laws and practices on freedom of association and industrial relations, workplace discrimination, migrant workers' rights, and other matters covered by the NAALC but not included in its enforcement regime.

The latest US agreements with Peru, Colombia, and Korea go farther. They require parties to "adopt and maintain" labor laws that comply with ILO core standards and provide "acceptable" wages, hours and health and safety conditions – and to effectively enforce such laws. They further subject labor obligations to the same dispute settlement procedures as commercial obligations, with both fines and trade sanctions as available remedies.

This is a good starting point for US and EU negotiators. But they must go farther, especially making enforcement procedures more rapid and effective.

4.3.2. Recent EU Agreements

The EU has also evolved in its approach to the trade-labor linkage. In its 1990s trade agreements with Chile, Argentina and Mexico, labor rights as such were absent. Instead, they were subsumed under a general human rights rubric and a mutual commitment in Article 1 that "Respect for democratic principles and fundamental human rights, proclaimed by the Universal Declaration of Human Rights, underpins the domestic and external policies of both Parties and constitutes an essential element of this Agreement." The EU now insists on this "democracy clause" in all its trade agreements (Szymanski and Smith 2005: 171 – 192). There is no reason it should not be part of an EU-US agreement, especially in light of important expressions of labor rights in the Universal Declaration and evidence of continued human rights abuses in the United States in such areas as child labor, criminal justice, abuses against immigrants, workplace health and safety, and freedom of association (Human Rights Watch 2014).

Violations of the democracy clause could trigger "appropriate measures" under the EU's agreements, but they have never been tested. Instead, the agreements focus on dialogue, consultations, cooperative activities, joint projects, education, training, information, promotion and other soft measures.

Fast-forward to the recent major trade agreement negotiated by the EU with Korea in 2010. It contains extensive language on labor rights and labor standards, starting with the objective "to promote foreign direct investment without lowering or reducing environmental, labor or occupational health and safety standards in the application and enforcement of environmental and labor laws of the Parties."

Labor rights are addressed in Chapter 13 of the EU-Korea agreement titled "Trade and Sustainable Development." While they recognize that economic development and social development "are interdependent and mutually reinforcing components of sustainable development," the EU and Korea pointedly add that "it is not their intention in this Chapter to harmonize the labor or environment standards of the Parties" and "The Parties stress that environmental and labor standards should not be used for protectionist trade purposes. The Parties note that their comparative advantage should in no way be called into question."

The EU-Korea agreement contains a soft commitment to international labor standards that recalls earlier US agreements: the parties will "seek to ensure" that their laws and policies meet international norms and "strive to continue to improve" labor laws and policies, compared with the US approach of requiring parties to "adopt and maintain" labor laws consistent with ILO core labor standards.

At the same time, the EU and Korea went farther than the United States in commitment to ratification of ILO Conventions. The Parties "reaffirm the commitment to effectively implementing the ILO Conventions that Korea and the Member States of the European Union have ratified respectively. The Parties will make continued and sustained efforts towards ratifying the fundamental ILO Conventions as well as the other Conventions that are classified as 'up-to-date' by the ILO."

When it comes to binding expectations, the EU and Korea take the same "effective enforcement" and "no derogation" formulas contained in Korea's trade agreement with the United States:

1. A Party shall not fail to effectively enforce its environmental and labor laws, through a sustained or recurring course of action or inaction, in a manner affecting trade or investment between the Parties.

2. A Party shall not weaken or reduce the environmental or labor protections afforded in its laws to encourage trade or investment, by waiving or otherwise derogating from, or offering to waive or otherwise derogate from, its laws, regulations or standards, in a manner affecting trade or investment between the Parties.

But in the end, the EU and Korea flinched when it came to enforcement. Instead of a solid enforcement mechanism for labor rights and standards, they called only for consultations between themselves and with civil society advisory groups of business, labor and environmental representatives. In contrast to trade disputes that can yield hard enforcement measures, labor-related disputes that go to an arbitral panel can only result in non-binding recommendations, namely:

> *The Parties shall make their best efforts to accommodate advice or recommendations of the Panel of Experts on the implementation of this Chapter. The implementation of the recommendations of the Panel of Experts shall be monitored by the Committee on Trade and Sustainable Development. The report of the Panel of Experts shall be made available to the Domestic Advisory Group(s) of the Parties.*

In the same way, EU agreements with countries in Central and South America have the parties "strive to ensure" high labor protections alongside an obligation to effectively enforce labor legislation (EU-Colombia/Peru Free Trade Agreement 2012). A novel clause in the EU-Colombia/Peru agreement states that "the Parties agree to promote best business practices related to corporate social responsibility (Ibid., Article 271)." These agreements focus exclusively on dialogue and cooperation, and do not link labor to any dispute settlement mechanisms.

These EU agreements provide for consultation with civil society, but do not provide a complaint mechanism allowing trade unions or NGOs to allege violations. For labor advocates, however, the agreements fail to make the final leap. EU agreements with developing countries in the Americas clearly specify that no Party may have recourse to dispute settlement with respect to any issue arising under the Sustainable Development Chapter, which includes labor standards (EU-Colombia/Peru Free Trade Agreement, Article 285 (5)). The ultimate consequence for failure to comply with the commitments of these chapters is unclear, other than increased public pressure and scrutiny.

With great fanfare, the EU and Canada announced in October 2013 that they had reached a Canada-Europe Trade Agreement (CETA) (Austin 2013). But a wall of silence has descended on developments since then, and the agreement remains unconsummated (McKenna 2014).

The text of a labor chapter has not been made public. However, by all accounts the parties are replicating what the EU did with Korea, making general statements of support for ILO core labor standards and promising not to fail to enforce relevant laws. For disputes involving labor rights violations, it apparently provides only soft consultative measures with civil society advisory groups and non-binding arbitral panel recommendations to back them up[2]. This failure of EU and Canadian negotiators to advance a strong social dimension in their trade agreement – should it ever be completed

– should not be a model for EU and American talks.

[2] See, for example, a report from an employer-side Canadian labor law firm presumably privy to the agreement (Askari 2013). As with US trade negotiations, corporations have an inside track to developments not available to labor and civil society organizations.

4.4. The Multilateral Trade Dimension

If the United States and the European Union fail to build a strong social dimension into transatlantic trade and investment, they would send a signal to the rest of the world that they are not serious about labor rights and standards and that other countries and regions can ignore them, too. Conversely, strong protections for labor rights and standards will confirm their importance in the global trade system.

In the US, much attention now is turning to a proposed free trade agreement in a Trans-Pacific Partnership (TPP). But the United States and Brunei and New Zealand and Vietnam are not going to create a leadership dynamic for the global economy. Neither will having Japan's participation, or re-baking NAFTA with Canada and Mexico joining TPP talks. In contrast, the United States and Europe can create a model that combines economic dynamism and social justice. Ultimately, expanding commitment to a social dimension in US-EU trade will inspire public support for global trade and investment on a sustainable human rights foundation.

The US and EU need to take the lead in promoting high-road labor policies as a strategic component of their economic relationship. The transatlantic economic partnership is the biggest and arguably still the most important one in the world. Comprising roughly 800 million people, the United States and the European Union account for about half of world GDP, a third of global trade in goods, and an even higher portion of trade in services.

Another important economic factor is consumption. Although consumption is likely to grow faster in the emerging economies in Asia and elsewhere, the combined consumer demand of the EU and US will remain crucial for the world economy in the foreseeable future. Many emerging economies still pursue their development with strategies based on strong exports into the North American and European markets, especially in apparel, footwear, electronics, and other labor-intensive sectors. To create a global climate of respect for labor rights, labor standards, and other international human rights norms, the US and EU should harmonize their GSP and other preferential trade policies for developing countries' exports to ensure that neither is granting preference to countries that fail to halt labor abuses (see Box 7).

Box 7: GSP in Bangladesh and Guatemala

The United States placed Bangladesh on a "continuing review" of its beneficiary status under the US Generalized System of Preferences after the 2012 torture and murder of union leader Aminul Islam – a reflection of widespread suppression of trade union organizing in the apparel sector. The review intensified after a deadly fire later the same year at the Tazreen Fashions factory in Dhaka that killed over a hundred workers. In the wake of the April 2013 Rana Plaza building collapse and the death of more than a thousand workers, the United States suspended GSP trade preferences for Bangladesh (Palmer 2013). In contrast, the EU decided to keep Bangladesh's duty-free access to the European market under its GSP program (Herald 2014).

The EU has granted duty-free treatment for Guatemala's exports under the EU-Central America Association Agreement, which requires countries to "strive to ensure" high labor protections and compliance with ILO core labor standards. This gives an EU 'stamp of approval' for Guatemala's performance on workers' rights despite widespread and longstanding violations of ILO core labor standards, including assassinations of trade union activists, discrimination against women workers in garment factories, and widespread child labor. At the same time, the US is reviewing complaints by trade unions and NGOs about such violations, and whether Guatemala's continued preferential trade treatment under the US-Central America Free Trade Agreement (CAFTA) should be maintained. In sum, the two main markets for Bangladeshi and Guatemalan exports are sending conflicting signals to the government and to employers in those countries about their compliance with international labor standards.

4.5. Recommendations

Europe and the United States should bring the social dimension of a trade agreement to new, higher standards of both substance and process that go beyond their latest iterations:

- The EU should urge and the United States should accept the EU's "democracy clause" and its adherence to the Universal Declaration of Human Rights.
- Negotiators should incorporate labor provisions of the OECD Guidelines and the UN Guiding Principles into a transatlantic trade and investment agreement to hold multilateral companies, not just governments, to compliance with international labor standards.
- The US should urge and the EU should accept the US formulation to "adopt and maintain" laws consistent with ILO core labor standards. Negotiators should build on that by requiring full compliance in law and practice with the eight ILO Conventions that comprise the core labor standards. Next, they should set mutually acceptable conditions on minimum wages, working hours, and health and safety conditions.
- Transatlantic trade negotiators should also recapture one of the signal provisions of the NAALC that the United States dropped in post-NAFTA agreements: protection of migrant workers' rights. Negotiators need to ensure protection that no country allows a permanent underclass of migrant workers with substandard wages and benefits to gain an advantage in trade. One thing US and EU member countries can do is to submit a country "Action Plan" with specific measures to guarantee that migrant workers have the same workplace rights and standards as those of all workers.

- As it has in all its trade agreements, the EU should insist on US ratification of ILO core labor conventions. But ratification is a lengthy, complex procedure in the United States. Rather than insist on ratification as a precondition, negotiators should set out a timetable for US action on ratification. Then, if the United States fails to fulfil the action plan for ratification, trade measures should be permitted against companies or sectors seeking beneficial treatment for products made or services provided under conditions that violate ILO core conventions.
- Negotiators should construct an accessible, transparent, and fast enforcement mechanism allowing trade unions and other civil society organizations to file complaints against government and firms that violate a transatlantic agreement's social provisions and to participate fully as parties in the dispute resolution and enforcement process.
- The United States and the EU should coordinate their GSP policies on labor rights and labor standards to ensure consistent treatment of developing countries where severe violations occur.
- The EU and the US should back up a commitment to a strong social dimension by establishing a permanent secretariat or observatory (the name does not matter) to monitor and report on labor developments in the United States and Europe. Such a body can:
- review and evaluate multinational companies' internal systems of due diligence, communication and management of the firm's social performance;
- conduct an annual Labor Information Audit on the state of labor rights and labor standards in firms involved in transatlantic trade and investment (noting, for example, whether firms have been found in violation of national labor laws or international labor standards);
- conduct investigations and issue findings and recommendations on alleged violations of international labor standards;
- undertake research to produce an annual "addressing inequality" report on transatlantic trade's effect, and whether it is positive or negative, on inequality in states of the United States and member states of the European Union;
- assess labor conditions in countries outside the United States and the European Union to help with coordination of GSP policies and application of labor chapters in UE and EU trade agreements with those countries.

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III. Trade Union Positions on TTIP

5. An American Labor Perspective on TTIP

American Federation of Labor and Congress of Industrial Organizations (AFL-CIO)

Introduction

1. The AFL-CIO appreciates this opportunity [in front of the United Kingdom's House of Lord's Subcommittee, ed.] to comment on impending negotiations for a Trans-Atlantic Trade and Investment Partnership (TTIP or agreement).

2. The AFL-CIO believes that increasing trade between the United States (U.S.) and the European Union (EU) could have positive impacts on job creation and income growth for America's and Europe's workers, but is unlikely to have such impacts unless the U.S. and EU discard the traditional neoliberal approach to trade and instead focus on the creation of good, family-supportive jobs and broadly shared prosperity.

3. At the outset, we note that much of Europe, including the United Kingdom, seems to be heading more in the direction of the neoliberal economic policy that the United States has been following for some time now—that is, in the direction of weaker social protections (including fewer workplace rights), reduced investment in infrastructure, education, and training, and increased reliance on the market to solve its own problems. We believe this is the wrong direction, and we are concerned that if more European enterprises do business in the U.S. as a result of the TTIP, they will drag the nations of the EU further and further in that direction by demanding the same privileges they receive in America—privileges they can enjoy without corresponding and commensurate duties to their employees and communities.

4. As a general matter, the AFL-CIO supports the use of positive lists for any commitments made under the TTIP. Positive lists are less likely to create confusion regarding intended commitments and less likely to subject newly conceived laws and regulations to "necessity tests," "regulatory impact analyses," and other similar barriers. The use of negative lists needlessly constricts the policy choices that future governments can make without running afoul of trade commitments.

Discussions Should Remain Disciplined and Focused On Efforts to Create and Maintain Good Jobs

5. The focus of the TTIP should be the creation of decent work for all workers in the U.S. and the EU. Yet the studies that tout the TTIP's potential to create jobs and boost the economies on both sides of the Atlantic are not convincing. One well known such study, "Reducing Transatlantic Barriers to Trade and Investment: An Economic Assessment,"[1] has been criticized for its overly optimistic projections. For example, Dean Baker, of the U.S. think-tank the Center for Economic and Policy Research, disputed the

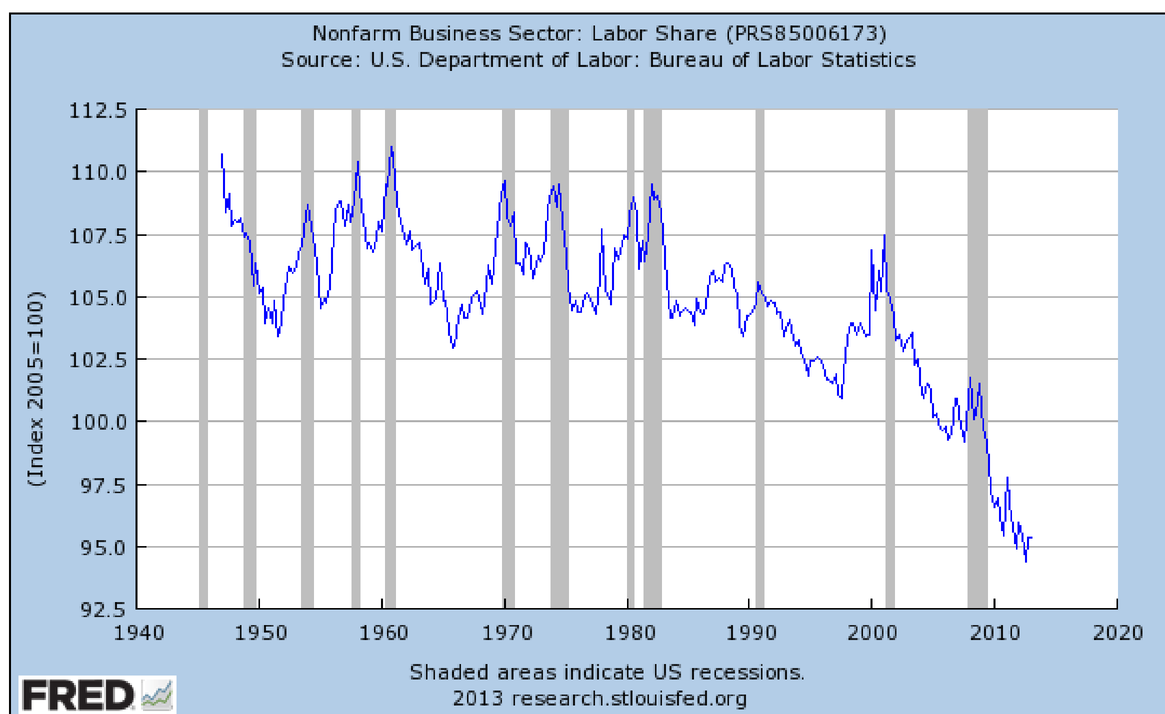
[1] Dean Baker, The US-EU trade deal: don't buy the hype," TheGuardian.com, Jul y 15, 2013, (http://www.theguardian.com/commentisfree/2013/jul/15/us-trade-deal-with-europe-hype).

characterization of the TTIP as an "economic bonanza . . . unless we define down bonanza to mean finding a quarter on the street."[2] He continued,

> *The first point to recognize is that the promised pot of gold from this trade deal is illusory. Last week, the media held out the promise of an increase in US GDP of $122bn from the trade agreement. The facts that this referred to GDP in 2027, and that the $122bn would be in 2027 dollars, were absent from the discussion.*
>
> *It also might have been worth mentioning that this $122bn was a best-case scenario in the study that was cited [Reducing Transatlantic Barriers to Trade and Investment: An Economic Assessment]. This figure assumed that the trade agreement included all plausible reductions in tariff barriers.*
>
> *The study also gave numbers for a deal that it described as "less ambitious" and, presumably, more realistic. Its projection of the increase in 2027 GDP in this scenario is 0.21% of GDP. That is roughly equal to a normal month's growth. Since it will take 14 years to achieve this gain, the boost to growth would be just 0.015 percentage points annually.*
>
> *If that sounds too small to notice, you've got the picture.*[3]

6. The potential for the TTIP to create large numbers of jobs notwithstanding, the purpose of trade agreements must be to advance domestic economic development and create level playing fields in each market, improving prospects for future sustainable growth whose benefits are broadly shared. Under today's globalized system, trade creates winners and losers, instead of winners and winners. It is the workers in the U.S. and in many of its trading partners who have been the losers—especially in the most recent decade, while global capital has taken an ever increasing share of the world's wealth.

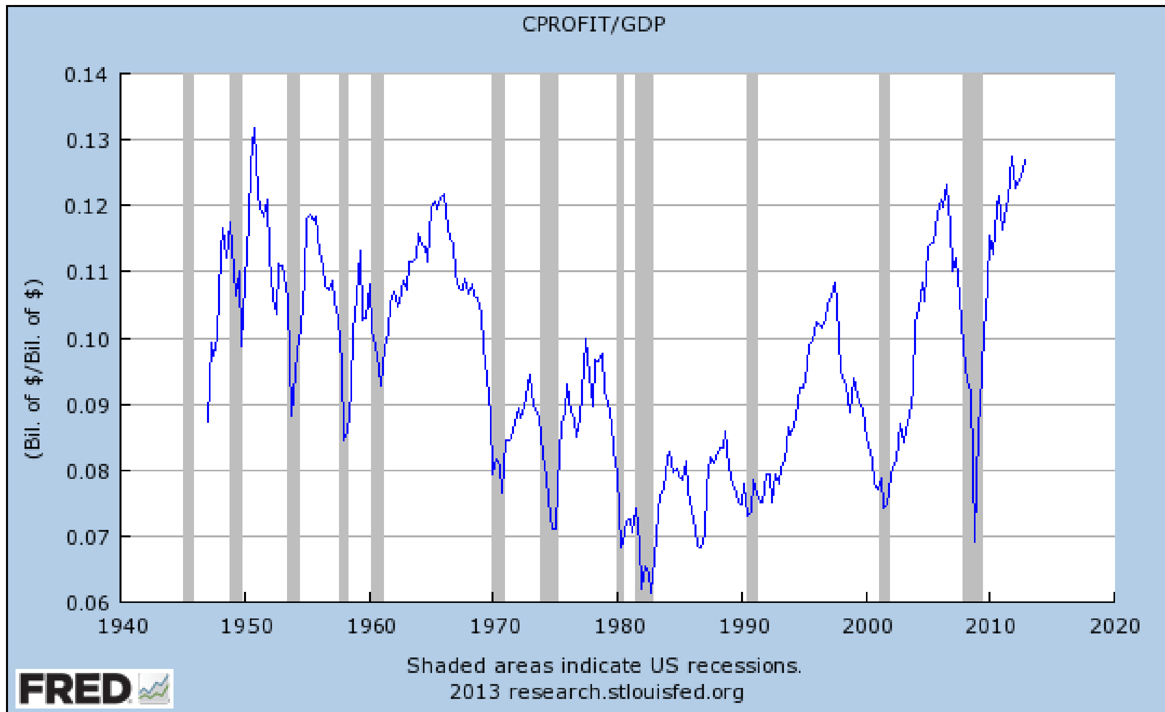
7. U.S. workers' share of national income is at its lowest level since the 1940s and is plunging:



[2] Centre for Economic Policy Research (UK), March 2013

[3] Ibd.

8. On the other hand, the share of corporate profits has reached its highest level since 1952:



Source: FRED Graphs/St. Louis Federal Reserve Bank, available at https://research.stlouisfed.org/fred2/.

9. To serve as a net benefit for any but the 1%, the TTIP must change course—more of the same will only promote the status quo, which is unacceptable.[4]

Negotiators Must Ensure that the TTIP Does Not Endanger the Provision of Critical Public Services

10. Public services are already under threat from austerity policies in both the U.S. and Europe. In a recent briefing paper released in September 2013, Oxfam compared Europe's current austerity measures to the failed "structural adjustment" programs imposed on developing countries by the World Bank and International Monetary Fund in the 1980s and 1990s. Oxfam concluded, "Europe is facing a lost decade. An additional 15 [million] to 25 million people across Europe could face the prospect of living in poverty by 2025 if austerity measures continue."[5] Given the current attack on public services by austerity policies in Europe and the austerity-driven "sequester" in the United States, it is all the more important that additional assaults on public services are not made under the guise of "trade liberalization." Good trading relationships need not, indeed must not, require countries to limit or restrict the public provision of public goods in any manner. Nor must they empower profitable corporations to game the system to avoid paying taxes—a strategy that deprives the public coffers of their due and only promotes more cuts to vital services.

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4 *See, e.g.*, Jacob S. Hacker and Nate Loewentheil, "Prosperity Economics: Building an Economy for All," 2012, available at: http://www.prosperityforamerica.org/wp-content/uploads/2012/09/prosperity-for-all.pdf.

5 A Cautionary Tale: The True Cost of Austerity and Inequality in Europe," Oxfam Briefing Paper No. 174, Sept. 2013, (http://policy-practice.oxfam.org.uk/publications/a-cautionary-tale-the-true-cost-of-austerity-and-inequality-in-europe-301384).

11. Replacing state provision with private provision of public services has often demonstrably lowered quality of services, worsened working conditions and wages for service workers, and excluded the poorest—as well as those geographically isolated and too remote from access to services to make service delivery profitable. When provided by the state, services provision is subject to democratic control and is sensitive to social goals determined by the locality, state, or nation. Most importantly, state provision has a role to play in achieving universal access to public services, in poverty alleviation, and in addressing economic inequality. Therefore, the TTIP must protect and promote public services.

12. Public services also play a major role in sustaining economic growth. Reducing inequality is increasingly understood to contribute to economic growth[6]; the public sector continues to be an important avenue for tackling income inequality. Providing transparent and accountable legal and regulatory systems free from corruption and private interest are essential to economic development. Education, health, and infrastructure address important market failures and externalities. Public sector provision, not market competition, is the most efficient way to provide most of these services. Not only are many public services critical for national security, but public sector spending has always provided important automatic stabilizers in times of economic downturn.

13. The TTIP should not promulgate regulatory restraints and disciplines that would lower the quality of services, reduce access, or affect working conditions adversely.[7] Public services, designed by the society to provide a minimum level of services for all, must not be undermined by the TTIP.

14. As such, repeating the language of GATS and prior U.S. "free trade agreements" (FTAs) is extremely problematic. GATS Article I:3 provides an extremely narrow definition of public services as "any service which is supplied neither on a commercial basis, nor in competition with one or more service suppliers." In both the U.S. and EU, essential public services such as water and wastewater services, health services, education, and public transportation are commonly provided on a commercial basis even when provided by the state—and therefore inadequately protected against the deregulatory effects of the TTIP unless a better public services exception is incorporated.[8]

15. A public services definition that is too narrow could limit the breadth of services that can be excluded from the agreement's regulatory "disciplines," market access commitments, and other requirements. Neither the U.S. nor the EU U.S. must make market opening commitments or agree to new disciplines in any public services sectors, including education and healthcare. The TTIP should not include any disciplines, barriers, or disincentives to prevent or deter national or sub-national governments from reversing privatization decisions and returning the direct delivery of public services to the public sector.

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6 See, e.g., Joseph E. Stiglitz, The Price of Inequality, W. W. Norton & Company, 2012.

7 To be clear, the AFL-CIO does not consider the provision of public services to be a commercial exercise. "Competitive neutrality" or similar principles that the U.S. and EU might consider including in the TTIP as pertains to state-owned and state-supported commercial enterprises (collectively, SOEs) in order to ensure that publicly supported widget-makers do not drive private widget-makers out of business, should not apply to the provision of public services.

8 In the past, the U.S. has exempted some existing laws and regulations from the rules of the services and investment chapters of FTAs, but left the majority of existing measures as well as all future measures open to challenge. In particular, the exemptions taken in past agreements for public services have been inadequate—failing to exempt a number of important public services, such as energy services, water services, sanitation services, and public transportation services, from coverage.

16. Finally, the AFL-CIO opposes the proposed use of negative lists for any service commitments under the TTIP. Negative lists have the impact of committing to the rules of a trade agreement laws, regulations, and public services that were not even conceived of by either party at the time of the agreement. As such, they can create a chilling effect on the future provision of public services. The AFL-CIO understands the desire for a comprehensive agreement, but a better approach would be a positive list, with periodic re-openings, either regularly scheduled or upon request of either party to the agreement.

Negotiators Must Ensure that the TTIP's Financial Services Rules Do Not Impede or Deter Financial Services Laws or Regulations

17. The AFL-CIO opposes further liberalization in trade in financial services. The GATS already provides sufficient market openings (and even that text could be improved to promote, rather than simply allow, prudential regulations).

18. This view is not inconsistent with the views of Bank of England's Executive Director Andrew Haldane, who has argued that institutions "are the perfect antidote" to the systemic risks posed by the financial sector. Unfortunately, this respect for regulatory institutions has too often been shunted aside in trade agreements as the financial lobbyists argue for looser and looser financial regulation under the guises of "free trade" and "free movement of capital." The AFL- CIO strongly cautions against repeating the mistakes of the past. Instead, to the extent that any financial rules are included in the TTIP, those rules must promote the stability of the financial system and avoid socializing the risks taken by private financial institutions.

19. In March, Attorney General Eric Holder admitted that certain financial institutions are not just "too big to fail," they are essentially "too big to jail."[9] Specifically, Holder testified that "I am concerned that the size of some of these institutions becomes so large that it does become difficult for us to prosecute them when we are hit with indications that if we do prosecute—if we do bring a criminal charge—it will have a negative impact on the national economy, perhaps even the world economy. I think that is a function of the fact that some of these institutions have become too large." The TTIP should not just allow but promote the development of new laws, regulations, policies, practices, and directives to address this concern. We need to learn from the economic disaster we are still recuperating from, rather than recreate the conditions that brought us to this point.

20. Given the size of the American and European financial sectors, should financial services disciplines be included in the TTIP, negotiators must pay special attention to the potential for unintended consequences of adopting industry-recommended language. Unlike past U.S. FTAs, the TTIP should not repeat and incorporate GATS provisions. Instead, negotiators should work together with academics, consumer advocates, national regulators, and other financial services policy experts to ensure adequate policy space, flexibility, and authority to effectively regulate: mergers and acquisitions; effective application of antitrust law; effective application of criminal and civil penalties; and prevention of

[9] "Transcript: Attorney General Eric Holder on 'Too Big to Jail,'" *American Banker.com*, March 6, 2013, available at: http://www.americanbanker.com/issues/178_45/transcript-attorney-general-eric-holder-on-too-big-to-jail-1057295-1.html?zkPrintable=1&nopagination=1.

systemic financial failures. There must be room for stronger regulations, instead of pressure to cut back on existing regulations.

21. For greater certainty, we suggest that the agreement eliminate any possible ambiguity or confusion in the prudential exception. Further, given the shift in global thinking with respect to capital controls, including the IMF's recent formalization of its policy endorsing the use of capital controls in certain circumstances,[10] the parties should not include language that inhibits the use of capital controls (see, e.g., Article 10.8 of the U.S.-Peru FTA).

22. Finally, we note again that the TTIP must not provide an additional avenue for enterprises to avoid their tax obligations. Too many U.S. and European companies already use their "home" nations as a flag of convenience, while parking money offshore in tax havens. The TTIP should include no financial services or other rules that treat a government's non-arbitrary, non-discriminatory taxation system as a barrier to trade.

The Agreement Must Not Include an Investor-to-State Dispute Settlement Mechanism And Must Set Limits on Investment Claims States Can Pursue On Behalf of Their Own Investors

23. The AFL-CIO recommends the use of state-to-state dispute settlement instead of investor-to-state dispute settlement (ISDS) for investment-related disputes in the TTIP. We strongly oppose ISDS, which privileges a single type of economic actor—foreign investors—to bring cases against sovereign governments to challenge democratically enacted laws as well as regulations and judicial and administrative decisions. While those who support ISDS often argue that it ensures the "rule of law" in nations with weak judicial institutions, the truth is the exact opposite. ISDS undermines the rules of law: it is antithetical to the core democratic values of the U.S. and the UK, replacing democratic decision making by public institutions working for the public good with the narrow, profit-seeking interests of a single private enterprise. Moreover, to the extent that the judicial system in a particular country is weak, the better approach to build the "rule of law" would be to support institution-building measures, not to provide a private, for- profit justice system to a limited few.

24. In truth, given the advanced judicial systems of both the U.S. and the EU, ISDS is an unwarranted risk to domestic policy-making at the local, state, and national levels. Investment disputes, therefore, must be resolved through a state-to-state process, just as other TTIP-related disputes will be.

25. ISDS provisions can be and have been used to challenge legitimate public-interest regulations. For example, the Metalclad Corporation, a U.S. waste disposal company, instituted arbitration proceedings against Mexico under NAFTA's ISDS provisions, arguing that Mexico wrongfully refused to grant a permit to open and operate a hazardous waste disposal facility in San Luis Potosi, despite concerns that unstable soil at the site could pollute the community's water supply. The panel found that Mexico had violated Metalclad's right to "fair and equitable treatment" under NAFTA; after a Canadian court overturned a portion of the award, Mexico eventually paid Metalclad more than $15 million. More recent ISDS cases have involved challenges to government contracts, orders to clean up toxic waste, and

[10] "The Liberalization and Management of Capital Flows: An Institutional View," International Monetary Fund, November 14, 2012 (http://www.imf.org/external/np/pp/eng/2012/111412.pdf).

requirements that patents live up to their promises in order to receive government protections. Ecuador was recently order to pay Occidental Petroleum $1.77 billion (plus interest) in a case in which Occidental had violated its contract with the government.[11]

26. As for the rest of any included investment chapter, it is important to note that there is broad, bipartisan support in the U.S. Congress for the principle that the investor protection standards contained in U.S. trade and globalization agreements should not provide foreign investors with greater rights than those enjoyed by U.S. investors in the United States. Congress first instructed U.S. negotiators to comply with the "no greater rights" principle in the Trade Act of 2002. In May of 2007, the Bush Administration and the Democratic leadership in the House of Representatives agreed that this principle would be explicitly stated in the preamble of the investment chapters of trade agreements. However, given the ad hoc nature of arbitration panels, the statement is not sufficient. The text of the investment obligations must make clear that none of them provide obligations that exceed obligations to a nation's own investors under domestic law.

27. For example, the provisions concerning indirect expropriation and the minimum standard of treatment in U.S. investment agreements are intended to reflect the relevant standards under customary international law, which is created through the "general and consistent practice of states followed by them from a sense of legal obligation." Given that the U.S. Constitution provides among the highest levels of protection for property rights of any country, standards that are based on the general and consistent practice of nations regarding the protection of property rights would generally comply with the no greater rights principle.

28. Unfortunately, arbitral tribunals, which would continue to exist even under a state-to- state system, have not based their interpretations of the "indirect expropriation" and "minimum standard of treatment" provisions of investment agreements on the actual practice of nations, but rather have simply cited the characterization of these standards by other tribunals, using essentially a common law methodology to create "evolving" standards of investor protection. This must be resolved limiting the power of arbitral tribunals to rewrite the obligations as they see fit.

29. As a preliminary matter, we believe it imperative that the TTIP place obligations on investors. At a minimum, these additional responsibilities must include:

a. Foreign investors must agree to remain neutral in union organizing drives (e.g., by entering into global framework agreements).

b. Foreign investors must agree to abide by the laws and regulations of the U.S. as well as the state and locality of their operation. If an investor asks its own government to pursue state-to-state dispute settlement on its behalf, the investor must show it has "clean hands," meaning it has no outstanding tax liabilities; has no open investigations, complaints, or violations under the National Labor Relations Act, the Occupational Safety and Health Administration, the Environmental Protection Agency, the Securities and Exchange Commission, or any state or local equivalent; is not facing criminal charges; and has no open OECD Specific Instances filed with any National Contact Point on the basis of its operations in the United States.

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[11] See "Recent Developments in Investor-State Dispute Settlement (ISDS)," in IIA Issues Note No. 1, UNCTAD, May 2013 (http://unctad.org/en/PublicationsLibrary/webdiaepcb2013d3_en.pdf).

c. Foreign investors should exhaust domestic remedies before seeking solutions under the TTIP. Failure to do so would provide "greater rights" to foreign investors—who could bypass city council hearings, meetings with elected officials, federal rulemaking procedures, Fifth Amendment taking claims in federal courts, and other procedures and remedies that similarly situated domestic investors would be obligated to use, depending on the nature of the measure complained of.

Investors should not be able to make any claims to their own governments under the investment chapter if they have not fulfilled these basic obligations.

30. In addition, the TTIP should ensure that investors replicate and expand upon the generally high level of workplace rights in the EU, rather than drive a race to the bottom. For example, the U.S. and EU should explore adopting mechanisms to provide for consultation and information disclosure between workers and trans-national investors (as outlined in the existing EU directive on European Works Councils)[12]; stronger protections for workplace safety and health; or even requirements to ensure "temporary" workers (such as those employed by third- party staffing companies) receive equal treatment with regard to pay, overtime, breaks, rest periods, night work, holidays and the like, as compared to non-temporary workers.

31. Finally, we provide specific recommendations to help clarify and set boundaries upon investment obligations:[13]

1. To avoid uncertainly about demonstrating a purported principle of customary international law (CIL), the TTIP should codify the State Department's position in Glamis Gold Ltd. v. U.S. (Glamis) regarding the standard of proof for identifying principles of CIL.[14]

2. To clarify the minimum standard of treatment with regard to foreign investors and ensure that the investment obligations provide no greater rights to foreign investors than to domestic investors, the TTIP should codify the State Department's position in Glamis regarding the content of the minimum standard of treatment.[15]

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[12] Here, we emphasize that we are referring only to Works Councils formed pursuant to the Works Council Directives of the EU, in which around 10 million workers across the EU have the right to information and consultation on company decisions at the European level through their Works Councils. The Works Council Directives apply to companies with 1,000 or more employees, including at least 150 in two or more Member States. It does not provide bargaining rights, nor does it interfere with or reduce the bargaining rights of unionized employees. This structure should be protected and enhanced to include companies with operations in the US and at least one EU Member State who otherwise meet the requirements. In this document, "Works Councils" does not refer to any kind of employer-sponsored effort to avoid or weaken unionization of workers.

[13] For additional detail on these recommendations, please see "The New U.S. Model Bilateral Investment Treaty: A Public Interest Critique," May 9, 2012, available at: http://www.ase.tufts.edu/gdae/Pubs/rp/BITResponseMay12.pdf; Report of the Subcommittee on Investment of the Advisory Committee on International Economic Policy Regarding the Model Bilateral Investment Treaty, Annex B, Sept. 30, 2009, available at: http://www.state.gov/e/eb/rls/othr/2009/131118.htm; and AFL-CIO, Testimony Regarding the Proposed United States-Trans-Pacific Partnership Trade Agreement, Jan. 25, 2010, available at: http://www.regulations.gov/#!documentDetail;D=USTR-2009-0041-0100

[14] *See* U.S. Counter-Memorial, Sept. 19, 2006, at 218-34, available at: http://www.state.gov/documents/organization/73686.pdf.

[15] Ibd.

3. The TTIP should clarify that an "indirect expropriation" occurs only when a host state seizes or appropriates property for its own use or the use of a third party, and that regulatory measures that adversely affect the value of an investment but do not transfer ownership of the investment or negate its entire economic value do not constitute acts of indirect expropriation.
4. The TTIP should narrow the definition of investment to include only the kinds of property that are protected by the U.S. Constitution. This would mean excluding the expectation of gain or profit and the assumption of risk. We also recommend excluding sovereign debt, derivatives, and carbon offset contracts from the protections of the definition of covered investment.
5. The TTIP should not allow use of the most favored nation (MFN) principle to assert rights provided by other investment agreements or treaties.
6. The TTIP should explicitly limit national treatment to instances in which a regulatory measure is enacted for a discriminatory purpose.
7. The TTIP should ensure that foreign subsidiaries cannot request that the EU or U.S. pursue an investment claim on their behalf when the other party that is the home of the subsidiary's parent company.
8. The TTIP should modify the restriction on capital controls (used for example in the U.S.- Korea FTA, Art. 11.7.1(a)) so that it allows the use of such controls—at least with regard to circumstances consistent with recent IMF guidance.[16]
9. The TTIP must include a strong exception protecting challenges against all non- discriminatory public interest measures (including but not limited to labor, the environment, public and workplace health and safety, food and product safety, and financial stability).

The TTIP Must Secure Fundamental Labor Rights

32. It is imperative that the TTIP address economic justice and the societal infrastructure that can promote it, not as an adjunct goal, but as a central part of its trade and economic development efforts. Freedom of association and the existence of free civil society organizations, including trade unions, are essential to a democracy. These institutions provide a venue for ordinary citizens to raise their voices collectively, claim their rights, advocate for policies that serve their constituents and the broader public interest, and hold government accountable. As large membership-based institutions advocating for social and economic justice for workers and citizens, independent trade unions are among the most important of these institutions.

33. Given the generally high level of worker protections in the EU, the TTIP must expand on the labor rights approach in other U.S. FTAs by improving upon the commitment to adopt, enforce and maintain core labor rights as laid out in the International Labor Organization (ILO) Declaration on Fundamental Principles and Rights at Work and instead make clear that the ILO Conventions and their jurisprudence will serve as the yardstick by which labor rights are measured.[17] A trade agreement with Europe presents

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[16] *Supra* note 12.

[17] The AFL-CIO understands that the EU requires developing country recipients of GSP+ benefits to adopt the eight ILO Core Conventions. The AFL-CIO supports U.S. ratification of all eight conventions and urges the U.S. Senate to ratify the

an opportunity for the U.S. government to go beyond the "lowest common denominator" approach to labor rights and create people-centered trade rules.

34. Guaranteeing that workers across the U.S., the UK, and the rest of Europe can exercise workplace rights and bargain with their employers for better wages and working conditions is part of an approach known as "predistribution," coined by Yale professor Jacob Hacker. Such policies, by empowering workers and their unions, can help address income inequality at its core, by ensuring that workers can make a decent living in decent conditions in the first place—rather than by relying on traditional (and often unpopular) redistributive measures such as government taxes and transfers that take from some and give to others.

35. To achieve these goals, the AFL-CIO recommends that the TTIP build upon the changes achieved in the U.S.-Peru FTA in 2007 (also known as the "May 10" provisions). In other words, the labor provisions in the TTIP must be stronger than those achieved in any prior agreement. The TTIP should fulfill the promise that the "May 10" provisions will serve as a floor, not a ceiling, on labor rights. These provisions represented an important step forward for labor rights, but did not contain all of the essential elements of an effective labor chapter.

36. Beyond using the ILO core conventions as the labor standard in the agreement and omitting a repeat of Footnote 2 from the Peru text (to help clarify that ILO jurisprudence will help give meaning to each party's labor obligations), the AFL-CIO has several additional recommendations. The labor provisions should also apply to all workers, regardless of sector or industry. Limiting available redress solely to violations that are "sustained or recurring" and "in a manner affecting trade or investment," as is the case in the Peru agreement, is too narrow. The text should be broadened because these limitations potentially exclude too many workers from coverage and make it exceedingly difficult to effectively pressure recalcitrant governments to do the right thing and protect their own workers. In addition, the TTIP should include enforceable standards for acceptable conditions of work and the treatment and recruitment of migrant workers.

37. The labor chapter's enforcement mechanism must be timely, accessible, and reliable. The TTIP's labor provisions must ensure that meritorious petitions proceed in a timely manner to the next step of the process until they are resolved (including through dispute settlement if necessary). Workers' livelihoods depend on swift justice; workers do not have the luxury of time. Should countries fail to resolve their differences during the consultation stage and proceed to the dispute settlement stage, the process must be at least as strong and swift as that available to business interests, and penalties should, where possible, be directly related to the sectors in which violations occur (in order to leverage to political power of employers) and high enough to encourage parties to engage seriously at the initial stages. Token fines unrelated to the economic sectors where the violations occur will do little to encourage private sector compliance or deter future violations. Finally, wage and hour, health and safety, labor relations, and any other labor measures must not be subject to investor-to-state dispute settlement.

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outstanding core conventions as soon as possible. It is difficult to imagine a "high-standards agreement" that fails to adopt the highest possible standards for labor protections.

The TTIP Must Protect Domestic Procurement and Other Domestic Economic Development, National Security, Environmental Protection, And Social Justice Policies

38. The TTIP must not surrender or limit the application of domestic economic development, national security, environmental protection, or social justice policies, including policies related to "buy national" and "buy local" requirements (these policies are frequently known in the U.S. as Buy American or Buy "State" policies). We support the right of all governments to use procurement policies to create jobs in their own municipality, state/region/province, or nation.

39. The AFL-CIO has long maintained that trade agreements should not constrain federal and sub-federal procurement rules that serve important public policy aims such as local economic development and job creation, environmental protection and social justice—including respect for human and workers' rights.

40. After the current record-slow recovery ends, the U.S. government must carefully consider the diminished impact of fiscal stimulus caused by procurement commitments (which decrease the ability of lawmakers to direct funds toward domestic job creation). Thus, procurement projects funded by stimulus funds appropriated in response to a verified recession should be free from TTIP disciplines.

41. Additionally, the AFL-CIO still has concerns left unaddressed by U.S.-Peru FTA. For many years, the AFL-CIO has raised concerns about technical specifications in procurement chapters. The procurement chapter of the U.S.-Peru FTA took a good step forward by providing that a procuring entity is not precluded from preparing, adopting, or applying technical specifications:

> (b) to require a supplier to comply with generally applicable laws regarding
>
> i. fundamental principles and rights at work; and
>
> ii. acceptable conditions of work with respect to minimum wages, hours of work, and occupational safety and health

42. However, the TTIP must expand the language above to include living wage laws and, for the sake of clarity, prevailing wage laws. It must also leave room for the bidding process for non-discriminatory but potentially innovative policies such as providing a better score for employers with better on-the-job safety records or excluding bidders that do not have "clean hands" (e.g., firms that have failed to pay taxes, have outstanding unfair labor practice charges, OSHA violations, or outstanding violations of other national, state, or local laws).

43. We also urge that any procurement negotiations proceed on a "positive list" approach whereby only entities that are specifically listed are covered by the agreement's procurement rules.

44. Finally, but importantly, the AFL-CIO expects that no sub-federal entities will be bound to the procurement provisions of the TTIP without their express consent and that none of the exemptions or exceptions taken from obligations undertaken in the WTO GPA will be deleted or altered in any manner (e.g., highway and transit projects).

The TTIP Must Not Simply Be a Tool to Undermine Public Interest Laws and Regulations

45. Because the TTIP will be more about so-called "behind-the-border" barriers than about tariff reductions, public interest law and regulation are amongst the core issues for the TTIP. If the regulatory

provisions in the TTIP are seen merely as a tool to undermine public preferences, it will risk legitimacy, both in the U.S. and in Europe. All we need to do is scan the headlines to find stories about corporate wish lists and efforts to tear down regulatory barriers. The U.S. Chamber of Commerce went so far as to write that "one of the biggest issues to overcome [in the TTIP is] regulatory sovereignty."[18] Negotiators must resist these pressures if the TTIP is going to work for working people.

46. While the AFL-CIO agrees that in certain areas, regulatory cooperation could increase trade and efficiency in ways that benefit workers and consumers, we also caution against any efforts to use the negotiation process as a backdoor route to attack important worker, consumer, and food safety protections, such as those included in the EU's REACH chemical safety initiative or labeling requirements for genetically modified foods.

47. The TTIP must not make it easier to avoid or block regulations meant to secure the health and safety of the public—whether that means on-the-job health and safety regulations; licensing and certification requirements that protect consumers from bogus practitioners of medicine or law; bonding or deposit requirements to ensure the ability to pay customers' claims; building codes; or any other public interest measure. Working families should not have to give up the regulatory gains made in the 20th century nor the right to needed future protections in the name of "free trade." In this regard, the TTIP should not require either party to engage in "Regulatory Impact Analysis" in order to justify particular public interest measures.

48. Indeed, the AFL-CIO believes that the goal of the TTIP should be to increase the level of protection for workers and the public in both the U.S. and Europe. To the extent that harmonization is useful to enhance trade, the TTIP should call for the adoption of the strongest protections. Moreover, the U.S. and Europe have been world leaders in developing and implementing laws and regulations to improve workplace safety, regulate toxic chemicals, and protect consumers and the environment. The TTIP should establish a framework for the U.S. and EU to draw and build upon their respective regulatory experiences to enhance protections. For example, the EU is much further ahead than the United States in the area of chemical regulation, particularly with respect to requiring the testing and registration of chemicals through its REACH legislation. The agreement should call for U.S. to adopt chemical legislation and regulations similar to REACH.

The TTIP Should Exclude New Market Access in the Maritime and Air Transport Sectors

49. We understand that the EU has asked that the ownership and control rules that pertain to airlines, the right of the carriers of two sides to operate in each other's domestic markets ("cabotage operations"), and maritime transport services be included as topics in the TTIP negotiations. For the purposes of air transport services, the AFL-CIO's comments here are limited to whether or not air traffic rights and services directly related to those rights should be included in TTIP. The AFL-CIO strongly believes that they should not. Likewise, the AFL-CIO believes that maritime transport services and U.S. maritime laws such as the Jones Act should not be included in these negotiations.

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[18] Sheryll Poe, "Trade on the Forefront: US Chamber President Chats with USTR," Free Enterprise Blog, Jul. 30, 2013 (http://www.freeenterprise.com/international/trade-forefront-us-chamber-president-chats- ustr).

50. Air transport services have historically been excluded from general trade agreements such as GATS and bilateral and multilateral free trade agreements. Rather, such services have been subject to a separate administrative regime, under which the U.S. has negotiated air service specific agreements with foreign countries. These negotiations have been led by the Department of State and the Department of Transportation, two agencies with dedicated experts on air transport services. This regime has led to the steady and dramatic removal of barriers to trade in the air transport services sector.

51. The U.S. and the EU have recently entered into such an open skies Agreement ("Agreement"). During the comprehensive discussions that resulted in the Agreement, the EU sought the exchange of cabotage rights and the elimination of restrictions on the ownership and control of airlines by the nationals of the parties. In fact, it is fair to say that consideration of altering the ownership and control rules was one of the central topics in the negotiations. Ultimately, the Agreement left in place the restrictions on cabotage. With respect to ownership and control, the Agreement left in place the statutory restrictions but did establish a Joint Committee (consisting of representatives of the two sides) that meets on a regular basis and is tasked, among other things, with considering possible ways of enhancing the access of U.S. and EU airlines to global capital markets. The existing administrative framework has been successful in opening markets and liberalizing trade in air transport services while at the same time taking into account the legitimate concerns of airline labor.

52. The request to eliminate the ownership and control restrictions raises its own set of difficult issues. If an EU airline were able to own a U.S. airline, it would be able to place the air crew of the U.S. carrier in competition with the air crew of the EU airline for the international routes flown by the previously U.S.-owned carriers. If the foreign owner sought to eliminate U.S. jobs and move this work to a foreign crew, it is unlikely that U.S. labor laws would provide an adequate remedy or protection for these workers. This is a very real threat, and the consequences of a similar arrangement are currently being felt by aviation workers in Europe where several airlines have taken advantage of the lack of a comprehensive labor law in the European common aviation area to undermine the ability of European flight crews to bargain over the flying done by their companies.

The TTIP Should Consider the Elimination of Market Distorting Mechanisms Such as Offsets and Offset-like Transactions

53. Offsets involve the transfer of technology and/or production from a U.S. company to a company in another country in return for a sale in that country. They can and have cost U.S. workers thousands of jobs. While offsets are virtually unregulated in the US, over 20 European countries have well established policies that are feeding the development of their own industries and bringing U.S. productive capacity and technology to their shores.[19]

54. Efforts to eliminate offsets were contemplated by the short-lived Presidential Commission on Offsets. That Commission, created by President Clinton, perished during the Bush Administration before it could issue a final report. Although prohibitions against offsets were reflected in the now-defunct U.S.-EU 1992 Agreement on Large Commercial Aircraft, that language was narrow, weak and, rarely (if ever) enforced.

[19] See Owen Herrnstadt, "Offsets and the Lack of a Comprehensive U.S. Policy: What Do Other Countries Know That We Don't?," Economic Policy Institute, 2008.

55. A high-level dialogue with the EU on jobs presents a tremendous opportunity to adopt new language that is robust and that will effectively eliminate EU's use of offsets and offset-like activities. Ultimately, this effort could assist U.S. and European companies that are constantly being pitted against one another by China. If both the U.S. and the EU were to agree bilaterally not to engage in offsets with each other—or when competing with one another for sales to China—jobs that would have been lost (in both the U.S. and the EU) due to offsets could be avoided.

The TTIP Must Contain Intellectual Property Rules that Support American Innovation While Promoting Access to Affordable Medicines

56. Intellectual property (IP) protections—designed to promote innovation and serve the public interest—are critical to creating and maintaining domestic jobs, as well as to increasing exports. Therefore, the TTIP should ensure that the creators of such intellectual property are protected from intellectual property theft—whether in the form of illegal streaming and downloads, counterfeit products, or inadequate protections against infringement. The IP provisions of past U.S. FTAs have not effectively deterred rampant counterfeiting or illegal downloading, a failure that resulted in lost jobs and reduced incomes for workers who rely on copyright protections for their incomes (e.g., writers, actors, stagehands).

57. To effectively promote U.S. jobs, however, strong and effective IP protections must be balanced enough to also promote legitimate generic competition—particularly in the area of medicines. Rules that prevent fair competition from generic producers not only fail to create as many jobs as they might, they also jeopardize public health both here and abroad, by ensuring that life-saving medicines are priced out of reach of many working people—in the U.S. and elsewhere.

58. Past U.S. FTAs have provided excessive protections for the producers of brand-name pharmaceuticals. Indeed, these agreements far exceeded the international standards for patent protection established in the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS). The AFL-CIO opposes TRIPS "plus" provisions because they jeopardize access to affordable medicines, particularly in developing countries.

59. The Peru FTA agreement took a significant step forward in cutting back the most onerous requirements for the IP protection of pharmaceuticals in U.S. FTAs. However, harmful language on data exclusivity remains in the Peru FTA agreement.[20]

60. Data exclusivity precludes use of clinical trial data of an originator company by a drug regulatory authority, even to establish marketing approval, normally for a defined period (five years in past U.S. FTAs). Data exclusivity can thus impose unnecessary costs—in financial and human health terms—on public health systems, which are forced to purchase brand-name pharmaceuticals at elevated prices when cheaper generic medicines would otherwise be available, but for the FTA.

61. Despite progress in the U.S.-Peru FTA to roll back TRIPS-plus requirements, U.S. trade policy has since taken a turn for the worse with regard to access to affordable medicines. For example, the AFL-CIO opposes efforts (such as those included in the U.S.-Korea FTA) to increase the power and influence of private sector drugmakers over the pricing decisions of public health systems and pharmaceutical benefit

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[20] The data exclusivity provisions are found in Article 16.10, sub-sections 2 (b) and (c) of the Peru FTA.

plans. The TTIP must not include such provisions, which could jeopardize the financial health of the National Health Service as well as several U.S. health programs. Instead, even while respecting IP rights, the TTIP can and must ensure that countries retain the policy space to expand and improve national, regional, and local health programs in a cost-effective manner.

62. Further, the U.S.-Korea FTA requires patent term extensions for new methods of use and manufacture of a pharmaceutical product.[21] It also effectively eliminates "pre-grant opposition,"[22] which allows the validity of a pharmaceutical patent to be challenged before a patent is granted, a process which makes it cheaper and quicker to dispose of bad patent applications than after a patent has been granted to an undeserving application. These provisions should not be repeated in the TTIP because they further delay legitimate generic competition that plays a role in increasing access to medicines for working families.[23]

63. The AFL-CIO strongly supports governmental efforts to control costs of medicines so as to be able to provide affordable medicines to the public. We oppose efforts to further enrich brand-name drug producers at the expense of working families and encourage negotiators to consider whether their negotiating goals will have the primary effect of raising drug costs or reducing access to affordable medicines to workers in any country, and, if so, to adjust those goals appropriately.

The TTIP Must Protect the Environment

64. Environmental protections, including obligations for countries to enforce domestic environmental laws and adopt, maintain, and enforce policies and commitments under multilateral environmental agreements, must be included, using the U.S.-Peru FTA as a floor, not a ceiling. Moreover, the agreement should require parties to adopt, maintain, and enforce measures to restrict and eliminate trade in illegally taken wildlife and illegally harvested wood and wood products (e.g., Lacey Act-type provisions). The TTIP parties should also agree to prohibit derogation from national, sub-national, and local laws and regulations that establish environmental standards or aim to protect the environment and public health. Environmental provisions must be subject to dispute settlement at least as strong and effective as that provided for other commercial commitments of the TTIP (again using the U.S.-Peru FTA as a floor). Moreover, environmental and public health protection measures must be exempt from ISDS challenges.

Telecom and Related Services Commitments Must Not Devastate Communities or Jeopardize Privacy and Data Security

65. As employers move call center operations overseas, they leave social safety net costs (including increased unemployment insurance payments, food assistance, etc.) in their wake, while simultaneously lowering their tax payments to the U.S. government. The TTIP should not make market access commitments that would exacerbate this problem in which those companies imposing greater costs on

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[21] Free Trade Agreement between the United States of America and the Republic of Korea, Art. 18.8.6 (b), available at: http://www.ustr.gov/sites/default/files/uploads/agreements/fta/korus/asset_upload_file273_12717.pdf.

[22] Ibd., Art. 18.8.4.

[23] For additional information, see Ruth Lopert and Deborah Gleeson, "The High Price of "Free" Trade: U.S. Trade Agreements and Access to Medicines," The Journal of Law, Medicine & Ethics, Vol. 41, Iss. 1, Apr. 12, 2013, available at: http://onlinelibrary.wiley.com/doi/10.1111/jlme.12014/pdf.

U.S. communities by eliminating jobs contribute fewer (or even no) taxes to help solve the problems they create.

66. This call center off-shoring trend also jeopardizes privacy and data security for all Americans. The offshoring trend has evolved into a crisis for consumers, with fraud and identity theft becoming a multi-million dollar business. For example, in one widely reported swindle, criminals used foreign call center workers to make 2.7 million calls and collect some $5.2 million through threats and intimidation, alleging that innocent consumers owed money for past loans.[24]

67. Threats to consumers' private data are not new. For at least a decade, the U.S. and European press have been reporting security breaches in overseas call centers. Foreign call center workers have peddled customers' financial and medical information to criminals, defrauded consumers of millions of dollars by posing as debt collectors, and stolen hundreds of thousands of dollars from bank customers.

68. The TTIP must go further than any previous trade deal in protecting the privacy and security of American and European families' electronic information. In particular, it should not be used to weaken the strong privacy protections that already exist in Europe. Unenforceable declarations of parties' respect for privacy are clearly insufficient in the case of global data theft schemes. Working families must be able to hold accountable—and receive compensation from—those who expose their data, no matter where the culprits operate. Otherwise, the TTIP will simply be a tool to promote more identity thieves who steal from working families while hiding behind international borders. If privacy cannot be enforced no matter where data is located, the TTIP should not agree to liberalize data markets.

Public Participation in the TTIP is Critical to Its Social and Democratic Legitimacy

69. The TTIP negotiating process should be accountable and transparent, allowing for a high degree of public participation as well as regular consultation with Congress, state and local elected officials, labor, civil society groups, and business interests. Legislatures and social partners should be integrated deeply in the negotiating and planning process, as well as the monitoring process after the TTIP is in place.

70. The monitoring process should focus on potential social and ecological impacts and the enforcement of rules laid down in the labor and environment chapters (and/or a sustainable development chapter, if included), but also on other parts of the agreement. The monitoring could be executed by a bilateral parliamentary commission (consisting of Members of the U.S. Congress and the European Parliament), in cooperation with social partners. Furthermore, a monitoring mechanism involving trade union representatives should also be included. Breaches of the agreement's labor or environmental standards, if not resolved through consultative or cooperative means, must be resolved by imposing penalties up to and including the potential loss of trade privileges (consistent with violations of the commercial provisions of the agreement).

[24] Federal Trade Commission News, "Court Halts Alleged Fake Debt Collector Calls from India, Grants FTC Request to Stop Defendants Who Posed as Law Enforcers," Apr. 11, 2012, available at: http://www.ftc.gov/opa/2012/04/broadway.shtm.

The TTIP Must Include Rules of Origin That Maximize Job Creation Among the TTIP Countries

71. Rules of origin provide the framework that governs whether a product will receive the benefits attributable to any TTIP agreement. Past U.S. trade agreements have often been insufficient in requiring the maximum amount of production and product transformation within the signatory nations so as to maximize employment gains for workers in those countries. The allowance of significant levels of production in non-signatory nations can lead to forms of venue shopping" in which corporations can directly invest, or use indirect suppliers, operating in countries with weak labor standards. Low rule of origin levels encourage the exploitation of oftentimes deplorable working or environmental conditions in non-signatory nations.

TTIP Interaction with Other Trade Agreements

72. The TTIP is being negotiated against a background of 13 existing trade and globalization for the United States, as well as the soon-to-be completed Trans-Pacific Partnership Trade & Globalization Agreement (TPP), a twelve nation endeavor being described as a "high standards, 21st Century" agreement. While the TPP includes all of the parties of the North American Free Trade agreement (NAFTA), namely Canada, Mexico, and the United States, we understand that the Office of the United States Trade Representative (USTR) does not intend for the TPP to supersede or subsume NAFTA—or any of the existing bi-lateral agreements the U.S. has with other TPP countries—meaning that countries will have a web of differing obligations to each party and, through the investment chapters of these agreements, the investors of each party. In such a framework, in which commercial entities will choose the obligation most favorable to their interests, it is possible that provisions more favorable to working families get lost in the process. After all, the question of which agreement provides the "highest level of protection" is in the eye of the beholder.

73. Moreover, the AFL-CIO is concerned that together, the TTIP and the TPP, are substitutes for a Doha Round agreement at the WTO. What developed countries like the U.S., EU, and Japan cannot achieve multilaterally at the WTO, they may be seeking to accomplish in smaller groupings where they have more leverage.[25] The TPP and TTIP combined would include 40 countries and more than 65% of the global economy. However, some of the issues being pushed in the TPP and TTIP have been discredited at the multilateral level, including a global investor- to-state dispute settlement agreement, intellectual property commitments beyond TRIPS, and further market opening by developing countries without reform of agricultural subsidies in the developed world. If the TPP and the TTIP are used to coerce developing nations into accepting neoliberal policies unachievable in a multilateral forum, it seems likely that the outcomes will not benefit working people, but rather exacerbate the negative effects of current trade policy.

[25] As USTR Ambassador Michael Froman recently told the Wall Street Journal, the Administration evaluated the Doha Development Round and concluded that it was clear that "China, India, Brazil, the major emerging economies, were not willing to play a role commensurate with their role in the global economy," so instead, the Administration decided to "pursue fresh, credible approaches to liberalization in the multilateral trade system." "Opinion: Does America Still Have a Free-Trade Agenda?," WSJ Live, Sept. 24, 2013, available at: http://live.wsj.com/video/opinion-does-america-still-have-a-free-trade-agenda/858C532F-F3C5-41CE-8F13- 5474471AB73D.html#!858C532F-F3C5-41CE-8F13-5474471AB73D.

Conclusion

74. Recent history has shown that employers worldwide are accelerating their efforts to scour the globe to find the lowest cost locations to produce, unconcerned with the standards that may be undermined and the effect on working people whose jobs they are outsourcing and offshoring. The result has been the loss of millions of good, family-supporting jobs in the U.S.—many of them in the manufacturing sector but millions more in supporting industries. We must not allow the TTIP to jeopardize more American and European families through a poorly crafted agreement that only promotes more deregulation and downward pressure on wages and benefits. Prevailing wages, labor and other standards, privacy, and other critical interests may be at risk.

6. TTIP: It Needs to Create New Quality Jobs and Sustainable Development

Confederazione Generale Italiana Del Lavoro (CGIL)

International trade and development

After the WTO negotiations in Seattle were blocked thanks to mobilisation by trade unions, civil society, and the firm position of governments in developing countries, and after international mobilisation and the opposition of several governments stopped the approval of the Multilateral Agreement on Investments (MAI), the WTO governments meeting in Doha solemnly declared their intention to improve the trading prospects of the least-developed countries through the so-called Doha Development Agenda.

That round of negotiations slowly broke down primarily due to the refusal by Europe and the United States to remove their massive agricultural subsidies, thereby ensuring - should they have taken this step - the food sovereignty of less developed countries, and a freer and more equitable trading system. On the other hand, huge changes in the global economy and the irresistible rise of the economies of the so-called BRICs, and other "intermediate" countries, have modified the balance of powers within intergovernmental WTO bodies, making it increasingly complicated to reach multilateral agreements regulating international trade, while development goals remain a sort of 'fig leaf' veiling the overriding drive to neoliberal globalisation through free trade.

Although the limited and modest Bali compromise on trade facilitation appears to ensure the food sovereignty of developing countries, in actual fact it forces poorer countries to invest huge amounts of their scarce resources in the modernisation of trade and customs procedures and free circulation of imported goods. It does not, however, ensure any mandatory return in terms of the economic, technological or knowledge-based aid required to implement these improvements, and has no real effect on their ability and capacity to export towards richer countries.

Bilateralism versus multilateralism

Meanwhile the more industrialised countries in the global world were intent on negotiating an increasing number of bilateral and multilateral agreements in all geographical areas and for all production and service sectors (for example, NAFTA in 1994 and, as regards the EU, European Partnership Agreements with countries in Africa, the Caribbean and the Pacific). Industrialised countries were focusing in particular on opening up and liberalising all public services seen as a source of new competitive investment possibilities for the private sector, export and growth. Considered as a way to weaken and influence multilateral negotiations, these bilateral and interregional Free Trade Agreements (FTA) have helped prolong the WTO negotiating deadlock which in turn has been used as "justification" for further proliferation of bilateral negotiations and agreements.

The economic and financial crisis began in 2007-2008 and remains severe and ongoing in many advanced countries, thus contributing to the relative decline in growth rates of emerging and developing economies; it has prompted western governments to focus increasingly on bilateral agreements as a possible way to

increase exports and therefore growth, and as a tool to establish new regulations (or rather de-regulations and liberalisations) which they then bring to bear during multilateral negotiations.

Although these free trade agreements promised to provide positive results for all the actors involved, none of the agreements were based on any ex-ante employment and social impact assessment – as instead requested by the trade unions. Post-agreement results (see NAFTA) now show a steady loss of jobs in competitively vulnerable sectors and countries, while no stable or quality employment growth has been recorded in "counterpart" countries.

In recent years the European Commission has been conspicuous in its efforts to expand bilateral trade agreements and negotiations, clearly stating that the way out of recession and stagnation in Europe, and especially in the Eurozone, is to increase exports towards other geographical areas.

International trade is clearly a zero-sum game; if one country increases its exports, another has to increase its imports. Obviously this is a multifaceted and complex situation: a country may increase its exports in some sectors and increase its imports in others. But in the end not everyone is a winner. If some countries have a surplus, others will have a deficit. Furthermore, in the last ten years all international organisations and even the G-20 – albeit using the suave language of diplomacy – have encouraged China to rebalance its growth model by reducing its large foreign trade surplus and shift towards its domestic market, capable of absorbing Chinese and foreign capitals and products. In turn, this would benefit other economies which constantly have trade deficits with China.

However the same problem exists in Europe. An export-based economic policy will only increase the imbalance within the EU between the strongest economies and biggest exporting countries and the weakest which, if anything, are negatively influenced by some of the trade liberalisation agreements.

TTIP: remove "non-tariff barriers", in other words environmental, social and labour laws

This is the context in which the TTIP negotiations between the EU and the USA are taking place. The European Commission has presented several preliminary studies on the consequences of the agreement. The first remark to be made is that, based on the best hypotheses proposed and promoted by the Commission, the agreement will produce a modest macroeconomic impact, with a theoretical 0.5% increase in the GDP when fully implemented, i.e., not before 2027. It's true that given the current crisis we should welcome any positive increase in growth, but using this modest figure to convince actors of the need for this agreement should be evaluated very carefully and balanced against all potential risks. Not the least because the much-touted increase in jobs ensuing from this increase in GDP is not based on any serious preliminary impact assessment per sector and country.

Negotiators are aware and acknowledge that Europe-USA trade already represents a major proportion of global trade and that tariff barriers are already at significantly low levels. In fact, the benefits cited by the Commission and the US Administration depend almost exclusively on the removal of so-called non-tariff barriers; the latter are none other than the laws, regulations and procedures now freely decided by each country, the European Union and the United States Congress. The overriding issue in these negotiations is regulation (or more precisely deregulation, at least in the intentions of large transnational companies and several political sectors of the two parties): in other words, the aim of these negotiations is to facilitate

trade exchanges by intervening on phytosanitary rules, environmental and labour laws, regulations enacted by local and national authorities, product safety and energy efficiency standards, etc.

The TTIP negotiations must respect democratic rights and processes

Trade Unions once again find themselves asking a fundamental question: whether or not it is acceptable that only two administrations - albeit democratic and governing strong and important countries or Unions in the global arena - can openly decide to determine rules which will apply to all countries in our global multilateral world.

This poses an immediate and tangible problem of internal democracy:

- In essence, secret negotiations have been ongoing for months. The European Parliament and the Parliaments of the 28 EU Member States – at least on this side of the Atlantic – are basically excluded from any information, debate, or possibility to influence the negotiations. Even governments declare they are unaware of the real contents of the proposals on the table, even those put forward by the European Commission. The Parliaments involved will probably be asked to vote on the outcome of the negotiations with a “take it or leave it” formula.
- Moreover, trade unions and civil society are basically excluded from receiving any information and participating in effective consultation. In fact, the meetings organised by the Commission with civil society are short and sporadic (roughly ten minutes) and participating representatives are only given very general information about negotiation topics. On the contrary, powerful entrepreneurial and business lobbies have daily access to the European negotiators, are informed about all discussed details, and significantly influence the way the negotiations move forward.

However, the danger for democracy and the government’s policy space (according to each country’s democratic procedures) is much more far-reaching and long-lasting, at least for two of the mechanisms that the TTIP intends to promote: the establishment of a Regulatory Cooperation Council (RCC) and an Investor to State Dispute Settlement body (ISDS).

- The Council – a body nominated by the European Commission and US Administration – is intended to supervise the harmonising measures of the legislation and regulations of the two parties and “prevent” any future modification which may negatively impact on the trade liberalisation decisions specified in the TTIP. In other words, current EU legislation and regulations will be harmonised or made more compatible with US laws and regulations. Every future legislative initiative of the European Union will be subject to prior examination by this technical and self-referential body not legitimised by any democratic mandate. The recent European elections have confirmed that a majority of European citizens support a more democratic and participatory Europe with elected bodies accountable to its citizens. Instead the Council would be an intercontinental super-body that abuses the legislative powers of democratically elected institutions!
- The so-called ISDS is an international arbitration mechanism that stands outside all the norms and controls of a normal judicial system. In the late fifties it was introduced in many Bilateral Investment Treaties (BIT) as a way to “protect” western investors in countries in which the legal

system was alleged to be particularly inequitable and inefficient. Its introduction was justified by the need to avoid any discrimination against foreign investors and grant them the same opportunities as local investors vis-à-vis the host State and its laws. In actual fact, assuming that these reasons were indeed valid, in the last ten years the huge increase in cases brought by powerful multinationals against several States – including advanced democracies – has shown that only multinationals can exploit this provision (due to the enormous costs charged to take on these cases by four or five well-established law firms based in London or Washington) and sue States and governments to the tune of hundreds of billions of euro. The reason for this is that legal provisions democratically established in the interest of citizens would either directly or indirectly trim down the profits envisaged by said businesses when they invested under certain legal conditions. A few examples will suffice: Vatterfall took on the German government seeking massive damages for the country's phase-out of nuclear power; Marlboro demanded compensation for Australia's plain cigarette packaging anti-smoking legislation; Egypt has to face a compensation claim for having increased minimum wage.

Faced with the refusal of several governments (Germany and France; the Italian government –according to a recent statement by Deputy Minister Calenda – is now favourable after initially stating its opposition), the Commission has launched a public consultation on ISDS in the TTIP (after having already agreed to it in the CETA with Canada).

The CGIL fully supports the ETUC position paper regarding the consultation in which it clearly opposes the inclusion of any ISDS provision in any future TTIP agreement. The CGIL demands that any attempt to include "new ISDS models" be forcefully rejected. There is absolutely no reason to envisage any special "protection" for US investments in Europe; nor are there any grounds to support the statement that European and US legal systems do not afford foreign investors adequate protection against potential discrimination. States must not be hindered in their right to pass laws and regulations in the interests of their citizens without being held hostage to possible legal actions by a business or private financial group.

Environmental, social, labour rights, and public services must prevail over any trade agreement

Further political and social safeguards must become inalienable provisions in the TTIP negotiations and in any trade-oriented negotiations:

- Exclusion of public procurement policies and basic public services (education, health, water, energy, public transport, postal service, etc.) from any liberalisation provisions; countries must be granted full decision-making policy space regarding these issues;
- Exclusion of any attempt to regulate migratory flows and labour market mobility which fall within the scope of fundamental human rights and the social and labour standards of the ILO;
- All trade regulations must be coherent with environmental treaties and standards and the international labour standards of the ILO, and ensure respect by foreign investors and businesses of the UN Principles on Businesses and Human Rights, the ILO Declaration, and the OECD Guidelines for Multinational Enterprises;

- In light of the negative experiences relating, for example, to the FTA between the European Union and South Korea, any future agreement must contain, in the chapter on sustainability, binding and enforceable clauses regarding environmental, social and labour standards, applicable in the same manner as trade clauses in case of violation.

The Italian government must provide information, ensure transparency, and consult social partners and civil society regarding the real impact of the TTIP negotiations

The CGIL demands that the Italian government initiate serious consultation with social partners and civil society for proper information and discussion regarding the ongoing negotiations based on a joint comprehensive and credible assessment of its possible effects on employment – sector by sector, region by region – and especially on small and medium sized enterprises. Emphasising the importance of exports for Italy is not enough: it is common knowledge that only a very small proportion of the tens of thousands of exporting companies have the solidity and structure to compete globally. On the contrary, most enterprises export either to Europe or neighbouring countries and have problems regarding access to credit and – more generally – modern technological tools and know-how. In addition, the government's "offensive" regarding "geographical denominations" has hit a steel-clad veto by the US negotiators to modify denominations, a request perhaps submitted by the entrepreneurial world of our fellow citizens who have emigrated to the US.

Only fulfilment of these conditions will make the TTIP a positive turning point for workers and citizens alike. On the contrary, should negotiations proceed along the lines adopted so far – so deeply affected, under a veil of secrecy, by the full thrust of industrial and financial lobbies which discuss and influence the official negotiations on a daily basis – then it will only serve to further progress the neoliberal policies of the past two decades and bring with it destructive and insidious consequences for employment and society at large.

As stated by the ITUC and the ETUC, trade must benefit workers and citizens, not the logic of profit.

7. Trade Deals that Threaten Democracy

International Union of Food, Agricultural, Hotel, Restaurant, Catering, Tobacco and Allied Workers' Associations (IUF)

New trade deals threaten democracy

Proponents, opponents and trade negotiators involved in the elaboration of two vast investment treaties currently under construction, the EU-US trade deal now known as the Transatlantic Trade and Investment Partnership (TTIP) and the twelve-nation Trans-Pacific Partnership Agreement (TPP) between Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, the United States and Vietnam agree on the most essential point. The agreements, which have been deliberately and misleadingly branded as Free Trade Agreements to boost their marketing, have little to do with lowering tariffs, which are generally already low. At the heart of these projects is the drive to further expand the already considerable power of transnational investors by restricting the regulatory power of governments and locking the system into place to prevent new regulatory initiatives or reverse privatizations.

The texts are officially secret; documents relating to the negotiations will be kept under government protection for decades. Neither lawmakers nor the public have access to the draft texts, which are, however, shared with corporate leaders and lobbyists. Wikileaks has provided an important public service in making available draft chapters of the TPP, and these confirm that the treaty significantly expands upon existing provisions in the WTO which have already significantly augmented corporate power and reduced public policy space.

The TPP is "WTO-plus" on, for example, public services, government procurement, state-owned enterprises (loosely defined to cover any enterprise in which the state has a commercial interest), intellectual property protection and financial regulation. It would restrict governments' capacity to legislate worker and consumer food safety standards, regulate financial flows, provide affordable medical services and protect natural resources and the environment.

The TPP incorporates the most toxic elements of the regional and bilateral trade and investment treaties which have been layered on to the WTO for expanding the scope and enforcement of transnational investment. The "right" of investors to directly challenge government laws and regulations at national and sub-national level through secret arbitration tribunals which bypass domestic courts is grounded in an expansive definition of "investment" which applies to even anticipated, future profits and purely speculative financial instruments. While WTO rules limit governments' ability to favor or support domestic producers in ways which "discriminate" against foreign investors (the national treatment/most favored nation principles), these expanded powers confer elevated, exclusive privileges on transnational capital.

The TTIP is at a less developed stage – formal negotiations began only last year , though it has long been a corporate priority - but government pronouncements and EU and US corporate wish lists setting out their goals for the negotiations show that the TTIP will bear a strong family resemblance to what we know of the TPP. There would be little point to the treaty if it too were not WTO-plus.

On the basis of the leaked texts and what we already know about the devastating impact of the WTO and the regional and bilateral agreements, the trade union movement should commit to defeating these two treaties as an urgent priority.

The background – with progress slowing at the WTO, corporations pursue the "fast track"

The WTO has been a prime mover in promoting, institutionalizing and enforcing the global neo-liberal project. The WTO is not simply about freeing cross border trade – with the important exception of agriculture, tariffs were steadily rolled back under the multilateral General Agreement on Tariffs and Trade (GATT), which preceded the WTO and whose treaties and jurisprudence were incorporated into it, and have continued to diminish. The WTO's core project is social and political: the "non-tariff barriers" to the flow of goods and services it seeks to eliminate are the laws and regulations

> *"constructed over decades of struggle by labour and social movements to protect the collective political, economic and social rights of working people by limiting corporate power and the predominance of profit over people. These include various forms of government regulation of corporate activities, such as laws on employment, environmental protection and public health. Public ownership and public provision of services are also attacked as barriers, since they place fairness and social needs before the most important need of corporations - private profit. The purpose of the WTO agreements as components of the WTO regime is to lock states in at the national and sub-national level, preventing the possibility of re-erecting these barriers. The regime is expressly designed to prevent a reversal of neoliberal policies and the corporate power it consolidates by threatening sanctions against countries whose governments attempt to re-erect these barriers or create new forms of social and/or ecological protection in response to the pressure of labour and social movements."* (The WTO and the World Food System, IUF 2002: http://www.iufdocuments.org/www/documents/wto/wto-e.pdf)

While transnational capital has made enormous gains over the WTO decades, the corporate appetite grows through eating. The WTO project has lost momentum; the Doha Round negotiations are bogged down, perhaps permanently. Important elements in the full corporate agenda have not yet been fully captured – on pharmaceuticals, biotech and intellectual property, for example, in agriculture, the perennial "bargaining chip", and in services. The WTO services agreement, the GATS, potentially offers up all services for privatizations, but governments must "opt in" on opening particular service sectors. Countries may also, with great difficulty, withdraw from their service commitments. Despite extensive privatizations, the persistence of public health, educational, postal, transport and other services is a constant irritant to hungry corporations.

So while still making full use of the WTO treaties and their capacity to impose sanctions, the corporations are pursuing more and faster tracks to their objectives. In services, one response was the creation, in 2012, of a group of some two dozen countries calling themselves. "The Really Good Friends of Services" to pursue the negotiation of a Trade in Services Agreement (TISA). The US, EU, Japan, Canada, Australia, New Zealand, Switzerland and South Korea are the wealthy core of the group. The Really Good Friends are pushing for a services agreement among themselves which would circumvent the inconveniences of GATS by liberalizing trade and investment in virtually all modes and sectors of services, public and private, and impose new regulatory "disciplines" on these services. The US and EU are pushing for "multilateralization" of the TISA, meaning the creation of a bloc of signatory governments inside the WTO GATS negotiations which would establish the hyperliberalized TISA provisions as the global services standard.

In September 2013, the IUF joined with hundreds of national and international trade union and civil society groups around the world to demand an end to the project (http://corporateeurope.org/blog/342-civil-society-groups-oppose-deregulation-andprivatisation-proposed-services-agreement-tisa).

Investor-to-state: fast track to circumventing democracy

The other corporate fast track is to broaden the reach and scope of the bilateral and regional trade and investment agreements which have proliferated since the 1994 North American Free Trade Agreement (NAFTA). There are now approximately 3,200 such agreements. Most of the approximately 300 regional and bilateral free trade agreements (FTAs) are essentially investment treaties. The thousands of bilateral investment treaties (BITs) deal exclusively with investment issues. Over 90% of these treaties provide investor-to-state dispute settlement (ISDS) provisions which allow corporations to directly sue adhering governments for damages in closed tribunals for which there is no appeals process.

Long familiar in North America thanks to a number of well-publicized NAFTA cases, investment treaties have only recently become a contentious issue in Europe in connection with the proposed inclusion of ISDS in the TTIP. But the EU and its members have signed over 1,400 bilateral investment treaties, including 9 between member states and the US. A number of these BITs are between EU member states, and EU investors have made generous use of the ISDS mechanism. Another multilateral treaty, the Energy Charter Treaty (ECT) signed by 51 member countries and the European Union, which came into force in 1998, contains binding ISDS provisions that are increasingly being made use of. Australia, Iceland, Norway, and Russia have signed but not ratified the ECT; the US and Canada are not signatories.

ISDS claims are proliferating. The figures are not definitive due to the total lack of transparency, but UNCTAD's 2013 World Investment Report records a total of 514 cases concluded, pending or discontinued. Of the 244 concluded cases, 31 percent were settled in favor of the investor, 42% in favor of the state, and the terms of the remaining 27% are confidential. In 2012 a record 58 new investor-state claims were initiated; over two-thirds of the respondents were developing or "transition" countries. The compensation settlements have also escalated since early NAFTA days. The 2012 USD 1.77 billion award to Occidental Petroleum for Ecuador's termination of a contract has now swelled to over 3 billion with the addition of compound interest calculated from the date of the "violation".

The cases are treated in closed tribunals for which there is no appeal and arbitrators are free to determine compensation and allocation of costs. The arbitration tribunals stipulated by most treaties are the World Bank's International Centre for Settlement of Investment Disputes (ICSID) and/or the United Nations Commission on International Trade Law (UNCITRAL). The tribunals consist of 3 private-sector lawyers who also serve as corporate advocates– there are no conflict of interest rules and the jurisprudence is essentially arbitrary. The average cost per case is USD 4 million, most of it lawyer fees. A handful of investment law firms have ridden the litigation boom and dominate the business. (http://corporateeurope.org/trade/2013/06/transatlantic-corporate-bill-rights).

Expanding investor "rights"

Language in these treaties varies, but the vast majority of them share elements in common, derived from NAFTA's Chapter 11. "Investment" is broadly defined to move far beyond the equity investment

normally considered to constitute foreign direct investment (FDI) to cover debt instruments including sovereign bonds, futures, derivatives, options and other speculative tools, intellectual property including patents and copyrights, licenses, franchises, authorizations and permits.

Expropriation has expanded to include "measures tantamount to expropriation", "indirect expropriation" and "regulatory expropriation", i.e. any state measure or policy which may potentially impact on profits, future profits, or "reasonable expectation of profits" even if the policy or measure is of a general nature and does not apply to the specific "investment". National treatment/non-discrimination has expanded to embrace "minimum standards" which include a wooly "fair and equitable treatment" and "maintaining a stable investment climate".

The treaties prohibit any restrictions on the repatriation of profits or funds. Governments may not impose capital controls to halt attacks on their currencies or restrict "hot money" flows in a crisis. Even the IMF has recently conceded that such controls are an essential policy measure. Argentina has had to pay out hundreds of millions of dollars as a result of investor cases based on the government's delinking of the peso from the dollar in the 2002 crisis.

Notorious NAFTA Chapter 11 cases include the 1996 suit by the US Metalclad Corporation against the government of Mexico for closing a waste treatment facility after a geological audit indicated severe threats to the local water supply. The tribunal ruled that the cancellation of a state-level zoning permit constituted regulatory expropriation and ordered the government to pay the company government USD 16.7 million in damages. In 1997 the US Ethyl Corporation sued the Canadian government for a ban imposed on its gasoline additive MMT, a proven health hazard. Ethyl claimed that the ban "expropriated" its assets in Canada and that legislative debate itself constituted an expropriation of its assets because public criticism of MMT damaged the company's reputation.

In 1998, the Canadian government withdrew the legislation banning MMT and paid Ethyl Corp USD 13 million to settle the case. In 2000, United Parcel Service sued the government of Canada for USD 160 million in damages, claiming that the public postal service's parcel and courier services put it at a competitive disadvantage. The suit was rejected nearly 7 years and millions of dollars in legal fees later on narrow technical grounds, but was a loud warning to public postal services on both sides of the border.

In 2011, the federal government of Canada agreed to a USD 130 million settlement with AbitibiBowater, a pulp and paper manufacturer based in Canada but registered in the US state of Delaware, an onshore tax haven. In 2008, the company closed its mill in Newfoundland and asserted a right to sell its timber harvesting and water use permits, which were contingent on production. Under Canada's constitution land and water use rights belong to the provinces, so the provincial government moved to take back the licenses. AbitibiBowater sidestepped the courts, filed a Chapter 11 claim and won, setting a precedent which effectively privatizes Canada's public ownership of natural resources (http://www.canadians.org/media/trade/2011/08-Mar-11.html) by allowing foreign companies to assert ownership claims. "By recognizing a proprietary claim to water taking and forest harvesting rights, Canada has gone much further than any international tribunal established under NAFTA rules, or to our knowledge, under the rules of other international investment treaties," a lawyer for the public interest advocacy group Council of Canada explained to Parliament in 2011. He pointed out that a government statement asserting that the settlement would not set a precedent was meaningless under NAFTA's

national treatment clause which grants foreign companies treatment no less favorable than national companies under similar circumstances.

In November 2012, the US pharmaceutical company Eli Lilly launched a suit to attack Canadian court decisions rejecting monopoly patent protections on two of its drugs after finding insufficient evidence that the drugs could deliver the promised results:

> *"The first attempt by a patent-holding pharmaceutical corporation to use the extraordinary investor privileges provided by U.S. 'trade' agreements as a tool to push for greater monopoly patent protections which increase the cost of medicines for consumers and governments."* (https://www.citizen.org/eli-lilly-investor-state-factsheet)

Eli Lilly is demanding $100 million in compensation. That same month, US-based Lone Pine Resources announced notice of its intention to seek USD 250 million in damages from the government of Quebec in response to its popular moratorium on gas shale extraction (fracking) under the St. Lawrence River. The fracking threat to water resources is well documented but Lone Pine contends the moratorium is "arbitrary, capricious and illegal" under Chapter 11.

The Ethyl Corporation MMT case shows how ISDS lawsuits can lead directly to changes in national or sub-national legislation. Tribunals can order "injunctive relief" in addition to compensation.

When the newly elected government of Slovakia in 2006 restricted the power of private health insurers to distribute or repatriate profits, several foreign health care providers sued for damages using the Netherlands-Slovakia BIT. The Dutch company Achmea was eventually awarded USD 25 million in damages and costs, and succeeded in enforcing the order through the Luxembourg courts, which have blocked EUR 29 million of the government's assets in its banks. The story doesn't stop there. In February 2013, Achmea initiated proceedings against the government of Slovakia to block draft legislation which would establish a single public health insurance scheme. The law is still in draft form and envisages various options to accomplish this goal. Achmea's claim for compensation for expropriation under a law which has not been adopted and under which it has therefore suffered no damages constitutes a pre-emptive strike to block future legislation. (http:// kluwerarbitrationblog.com/blog/2013/03/28/achmea-ii-seizing-arbitral-tribunals-to-prevent-likely-future-expropriations-is-it-an-option/)

The European Commission's October 2013 "Factsheet on Investor-State Dispute Settlement" (http://trade.ec.europa.eu/doclib/ docs/2013/october/tradoc_151791.pdf), part of the attempt to sell ISDS, asks: Will the ISDS mechanism limit the EU's right to regulate?, and answers: No. Including an ISDS mechanism in an investment agreement will not make it more difficult for the EU or its Member States to pass laws or regulations.

The mere threat of an expensive lawsuit hangs over virtually all regulatory measures, and can also be used as a bargaining chip. Lawsuits or the threat of ISDS under regional and bilateral agreements are being used to block legislation on mining-related water safety in El Salvador. In June 2012, the French services provider Veolia used the France-Egypt BIT to sue the Egyptian government for increasing minimum wages. In May 2012, the Swedish energy company Vattenfall launched a claim under the Energy Charter Act against Germany's phase-out of nuclear energy following the Fukushima nuclear catastrophe, although one of the two plants operated by the company in Germany has in fact been out of operation since 2007 due to numerous incidents.

Layer by layer, a powerful machine has been constructed to weaken the capacity of governments to regulate in the public interest. Many of the WTO treaties, like the TRIPS agreement on intellectual property, were built by first negotiating a series of wide-ranging bilaterals to neutralize opposition at the multilateral WTO. FTAs and BITs were in turn layered onto these treaties, which provide a floor. These have then become more expansive, more expensive and the corporations have become more litigious. The TPPA and TTIP would in turn set the new gold standard for corporate power. New adherents to the TPPA would have to join on a take-it-or- leave-it basis.

Can the treaties be limited?

The web of treaty obligations incorporated in the global investment regime already grants such enormous powers to transnational corporations that attempts to restrict the reach of new agreements with limiting clauses face substantial obstacles. The UNCTAD 2013 investment review advocates new, gentler and more "sustainability" friendly treaties, but concedes that "Renegotiation efforts aimed at reducing or rebalancing treaty obligations can be rendered futile by the MFN (Most Favored Nation) obligation, if the scope of the MFN obligation is not limited it can result in the unanticipated incorporation of stronger investor rights from IAs [investment agreements] with third countries." Treaties that define commitments to liberalize the service or other sectors through exclusions ("carve outs") leave no space for future regulation in response new and unanticipated social and environmental threats in the future and are otherwise susceptible to various forms of attack. Treaty language referencing the state right to regulate in a manner "otherwise consistent with this Agreement" (NAFTA Article 1114(1) on the environment) simply means that a treaty party may adopt any regulatory measure it wishes provided it is not discriminatory, is taken in the public interest and … compensation is paid. Achmea is using precisely this approach to attack a law which does not yet exist.

Language affirming commitments to refrain from undermining human rights or labour standards suffer the same weakness. These rights are already recognized in customary international law and add nothing to the treaties. The language merely encourages but is non-binding – governments "should" take no measure to undermine etc. No investment treaty sets out mechanisms by which the responsibilities of corporations to society can be effectively enforced. International human rights law is soft, investment law is hard. The United Nations Guiding Principles on Business and Human Rights reaffirm the state duty to protect, but set out no new legal obligations – that was one of their selling points.

Investment measures in trade agreements, for example, are consistently used to block states from banning or (limiting through labelling requirements) GMOs despite the Cartegena Protocol to the Biodiversity Convention, an international treaty which gives states that sovereign right. In the hierarchy of treaties, commercial law trumps human rights.

What purpose do these agreements serve?

There is no evidence to indicate that the absence of ISDS limits foreign investment. Brazil, Latin America's largest recipient of FDI has no investment agreements which contain ISDS. The United States has no ISDS with China, which continues to receive massive investment flows. As usual, jobs for hard-pressed workers is the promise used to sell these agreements to a skeptical public. Yet the

methodologically flawed impact assessment prepared for the European Commission predicts substantial job losses and prolonged dislocation for European workers without specifying the sources of new employment creation. NAFTA is now generally credited with destroying manufacturing jobs and fostering social inequality in North America, pushing Mexico far back in the development league, destroying Mexican agriculture and pushing millions of migrants north in search of work. The single market and the single currency in Europe were all sold in the name of jobs. There is no reason why this time things will be different. The path to recovery does not lead through more deregulation and the lowering of social and environmental standards.

The two decades of the WTO have brought huge increases in world trade and investment, but they have also brought recurrent crises, widening inequality and massive social and environmental destruction. The winners have been the corporations. The UNCTAD report previously cited in this report estimates that 80% of world trade now takes place within the value chains of transnational corporations.

We should not separate ISDS from the wider context or focus on it to the neglect of the other treaty provisions. Investor-to-state lawsuits are not the only mechanism for enforcing corporate power, though it is a powerful tool. Investment protection can be enforced through state-to-state mechanisms in FTAs/BITs and through contract provisions. The WTO treaties on Trade Related Investment Measures (TRIMS) and Government Procurement already severely restrict the use of local content and other performance requirements. A successful WTO complaint by Japan recently forced the Canadian province of Ontario to eliminate the provisions in its Green Energy legislation encouraging local renewable energy producers. The US is now similarly pressing India through the WTO to drop support for local solar power production. Corporations can simultaneously pursue WTO complaints as well as use bilateral ISDS. Philip Morris, for example, is challenging Australia's law on cigarette plain packaging through the WTO after failing to overturn it in the courts. The US-Australia FTA contains no ISDS, so the company is simultaneously claiming damages through the Hong Kong-Australia agreement, as well as suing Uruguay for its anti-smoking policies by claiming to be Swiss and making use of the Uruguay-Switzerland BIT! The government of New Zealand is awaiting the outcome of the WTO decision on Australia's cigarette plain packaging to determine whether it will implement similar legislation which is currently pending.

Where do we go from here?

The corporate web is dense, but opposition is growing. South Africa is letting its existing bilateral investor treaties lapse and will sign no new ones. Indonesia is exiting its investor treaties. (It should be noted that successor clauses in these treaties keep their terms in application generally for 10-15 years in the event of unilateral termination, so there is no instant relief.) Australia has refused to include ISDS in any trade agreement since 2011; there is none in the FTA just signed with Japan. Several Latin American countries have withdrawn from existing treaty commitments and there is growing discussion about regional schemes to foster cross-border investment on different foundations. Controversy around the TPPA and TTIP has generated unprecedented discussion about investment treaties and corporate power more broadly. Unions should seek to build on this momentum.

Rather than seeking exemptions or improved language, the goal should be to stop these treaties by making them a major national political issue, highlighting their domestic impact. Public opposition killed

the Multilateral Agreement on Investment (MAI) and the Free Trade Agreement of the Americas, both of which were attempts to bring NAFTA-style investor clauses into wider treaties. They have predictably returned again as the TPPA and TTIP, so the opportunity should be used to generate a deeper discussion about stopping all new agreements which exceed current WTO commitments and ultimately about rolling back the damage emanating from the WTO. All measures which constrain or potentially inhibit governments' authority and capacity for democratic regulation in the public interest should be stripped out of trade discussions. We need trade, and trade needs rules, but we don't need these rules. Proposals to tinker with the detailed language of these treaties ignore their fundamental purpose that of advancing investor rights over social needs.

Together with NGOs, social movements and public advocacy groups, we need to organize to defeat the negotiations on the TPPA and TTIP, but the struggle doesn't end there. It must be broadened to roll back transnational investor privileges enshrined in the current web of trade and investment treaties and reclaim democratic public policy space to strengthen the struggle for enforceable worker rights, sustainable livelihoods, quality public services and the tools and means to rebuild systems of food production in ways which conserve the world's resources and ensure the right to food.

8. Response to the EU Online Public Consultation on Investor-to-State-Dispute-Settlements (ISDS)

Vereinte Dienstleistungsgewerkschaft ver.di

An explanatory note by the editor:

Facing considerable civil society opposition to the inclusion of Investor-to-State-Dispute-Settlements (ISDS; see the contribution of Eberhardt in this volume), the European Commission General Directorate Trade came up with the idea of an online public consultation on the modalities of investment protection and ISDS in TTIP. The public consultation was launched on 27 March 2014 and was closed on 13 July 2014. Among the 149,399 online contributions to the consultation were 42 by trade unions. The Directorate Trade tried to pre-empt criticism by pointing out that its draft of an ISDS is addressing some of the deficits in previous investor protection clauses. Therefore, each question of the online survey was accompanied by an explanation of the issue, a brief summary of the approach in most investment agreements and the EU's objectives and approach to investor protection in the TTIP negotiations which mirrors the recently negotiated investment protection provisions in the EU-Canada agreement (CETA). For a better understanding of ver.di's response to the online questions, I have placed the EU's statement of objectives ahead of the response in italics. The EU's reference text of the protection provisions agreed upon in CETA can be found in the Annex.

Question 1: Scope of the substantive investment protection provisions

The EU wants to avoid abuse. This is achieved primarily by improving the definition of "investor", thus eliminating so –called "shell" or "mailbox" companies owned by nationals of third countries from the scope: in order to qualify as a legitimate investor of a Party, a juridical person must have substantial business activities in the territory of that Party.

At the same time, the EU wants to rely on past treaty practice with a proven track record. The reference to "investments made in accordance with the applicable law" is one such example. Another is the clarification that protection is only granted in situations where investors have already committed substantial resources in the host state - and not when they are simply at the stage where they are planning to do so.

Question*: What is your opinion of the objectives and approach taken in relation to the scope of the substantive investment protection provisions in TTIP?*

Under international law there are no general prerequisites on the presence of protected "investments". It always depends on the respective understanding of the term "investment" in the contractual context, which means on the concretely agreed understanding of "investment" in TTIP. The foreseen investment protection in TTIP is not unusual in existing bilateral contracts, but it is by no means imperative under international law. The EU's competences in trade policies encompass the conclusion of agreements on

Foreign Direct Investments, Art. 207 par. 1 p. 1 TFEU. The remaining competences of the member states for so-called portfolio-investments, however, need to be considered.

The terms "investor" and "investment" as used by the EU are very broadly conceived. The term "investment" in particular seems to have no limits, since it explicitly aims to cover "a wide range of assets, such as land, buildings, machinery, equipment, intellectual property rights, contracts, licences, shares, bonds, and various financial instruments", which are not explained in more detail. Moreover, the reference to BITs and CETA make it clear that direct and indirect capital investments, as well as stockholdings of minority shareholders without controlling influence ("portfolio-investments"), are included. Portfolio-investments are mainly transacted because of the associated expectations of return; aspects of taxation also play a role here. Independent from portfolio-investments, the term "investment" encompasses expectations of return or profit as well (cf. "expectation of gain or profit, CETA). Furthermore, the approach of the EU does not sufficiently strengthen the fundamental legal principles, especially the precautionary, preventive and the causative principle and basic rights such as the right to a high level of environmental and consumer protection as established in the EU-treaty and the EU Charter of Fundamental Rights. These principles and their implementation are dependent on interpretation, which is why enhanced democratic possibilities for participation and co-determination, also for civil society, need to be demanded dependent on the character of the concerned investment. Conceptual ambiguities and room for competing interpretations can be found equally in the CETA-text with regard to the definition of those investments and investors that are covered by such agreements. Formulations such as "the expectation of gain or profit", "any other kinds of interest in an enterprise" (what else is meant here, if not a catch-all clause), "substantial business activities" or "if the enterprise is owned or controlled" leave room for interpretation regarding the scope of the investment protection provisions. The proposal likewise implies a rather broad understanding of investment which includes portfolio-investments. For multilevel ownership structures, interesting options of influence are introduced if TTIP protects investments implemented by a corporation in the host country, which are only indirectly controlled by US-/EU- nationals. Also investors from third countries, who establish a corporation in the USA or the EU, could benefit from the contractual investment protection. In this manner, access to TTIP can be gained through corporate law constructions. A qualitative justification of the term "investment" or a limitation of investment protection to such investments which display a certain quality under international law is missing. This means that there is no limitation on capital investments, which meet the international standards on environmental protection, human rights and the standards on international labour law, particularly the eight core norms of the ILO. Equally, a link to UNCTAD's Investment Policy Framework for Sustainable Development, published in 2012, is absent.

Question 2: Non-discrimination

The EU considers that, as a matter of principle, established investors should not be discriminated against after they have established in the territory of the host country, while at the same recognises that in certain rare cases and in some very specific sectors, discrimination against already established investors may need to be envisaged. The situation is different with regard to the right of establishment, where the Parties may choose whether or not to open certain markets or sectors, as they see fit.

On the "importation of standards" issue, the EU seeks to clarify that MFN does not allow procedural or substantive provisions to be imported from other agreements.

The EU also includes exceptions allowing the Parties to take measures relating to the protection of health, the environment, consumers, etc. Additional carve-outs would apply to the audio-visual sector and the granting of subsidies. These are typically included in EU FTAs and also apply to the non-discrimination obligations relating to investment. Such exceptions allow differences in treatment between investors and investments where necessary to achieve public policy objectives.

***Question**: What is your opinion of the EU approach to non -discrimination in relation to the TTIP? Please explain.*

The assumption that foreign investors in the developed European or US-American legal systems are discriminated against or treated unfairly is not justified. It is not clear if the discrimination-protection also involves market access, which means national or EU legal regulations concerning the access of US-investors to the market of the respective member state (“pre-entry”-model) – and reciprocally the access of EU-investors to the US-market – or if the protection from discrimination only applies to already effected investments in the host country (“post-establishment”-model). This is regulated differently in different agreements. Also differently regulated is the question of whether or not foreign investors in the context of the most favoured nation principle (MFN) can benefit from other – already existing or prospectively concluded – agreements of host countries, which provide for more beneficial procedural or substantive protection measures. In these cases it is disputed whether an automatic “import of standards” occurs in favour of foreign investors, which would grant them a higher protection standard than the original bilateral agreement.

The protection of health or the environment is not to be defined as a derogation, whose justification is exercised by private tribunals, but is to be seen as a comprehensive constitutional principle, the scope of which is to be defined in a democratic manner or in the framework of constitutional legal systems, respectively. Furthermore, only a few single policy aims are listed as exceptions, and social or labour protection standards in particular do not belong to these. The latter would have to be included explicitly. The Commission's apparently pursued “post establishment”-approach remains unclear with regard to the question of discrimination-free market access (“pre-entry”). Even treaties, which provide discrimination-free market access, also allow for limitations of market opening for foreign investors in the form of an enumerative list of opened sectors/markets (“positive list”) or in the form of an enumeration of certain sectors/markets which are exempted from market access (“negative list”). The Commission does not clarify this point; a positive or negative list is missing. It remains likewise unclear if TTIP aims for an orientation towards the non-discrimination rules of chapter X within CETA (see annex, table 2). This would have wide-ranging consequences. Chapter X of CETA regulates the inclusion of Art. XX GATT 1994 and Art. XIV GATS within CETA. Both provisions of the WTO-law will be incorporated into the free trade agreement CETA (EU-Canada) and therefore become an integral part of the contract. The following legal consequences ensue: Art. XX GATT 1994 regulates a catalogue of exemptions with regard to measures that restrict trade such as the protection of life or the health of people, animals and plants (b) insofar as these are “necessary to [...]”. Additionally, a potential justification of trade restriction is under general reserve (“chapeau”) due to the exception provision “that such measures are not applied in

a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade".

Sensitive strategic sectors, which serve the interest of general wellbeing such as the water sector (public water supply and wastewater disposal) should not be accessible to foreign direct investments, precluding market access for foreign investors.

Question 3: Fair and equitable treatment

The main objective of the EU is to clarify the standard, in particular by incorporating key lessons learned from case-law. This would eliminate uncertainty for both states and investors.

Under this approach, a state could be held responsible for a breach of the fair and equitable treatment obligation only for breaches of a limited set of basic rights, namely: the denial of justice; the disregard of the fundamental principles of due process; manifest arbitrariness; targeted discrimination based on gender, race or religious belief; and abusive treatment, such as coercion, duress or harassment. This list may be extended only where the Parties (the EU and the US) specifically agree to add such elements to the content of the standard, for instance where there is evidence that new elements of the standard have emerged from international law.

The "legitimate expectations" of the investor may be taken into account in the interpretation of the standard. However, this is possible only where clear, specific representations have been made by a Party to the agreement in order to convince the investor to make or maintain the investment and upon which the investor relied, and that were subsequently not respected by that Party. The intention is to make it clear that an investor cannot legitimately expect that the general regulatory and legal regime will not change. Thus the EU intends to ensure that the standard is not understood to be a "stabilisation obligation", in other words a guarantee that the legislation of the host state will not change in a way that might negatively affect investors.

In line with the general objective of clarifying the content of the standard, the EU shall also strive, where necessary, to provide protection to foreign investors in situations in which the host state uses its sovereign powers to avoid contractual obligations towards foreign investors or their investments, without however covering ordinary contractual breaches like the non-payment of an invoice.

Question*: What is your opinion of the approach to fair and equitable treatment of investors and their investments in relation to the TTIP?*

No investor should be able to legitimately expect that the general law and administrative system of a host country remains unchanged in the long-term – that means there is no public obligation to "legal stability" in the form of a guarantee that the legal situation (legislation) in the host country does not change in a way which affects the investor negatively. It should be emphasized in this context that a relaxation of the "fair and equitable treatment" principle, especially on grounds of occupational safety and social minimum standards ("ILO"), of human rights and health and environmental protection, comes into consideration. Regarding the practice of decision making on this, it has turned out that tensions between investor interests and the general public interest arise regularly. The provisions of "arbitrary treatment", "targeted discrimination" or "legitimate expectations of investors" remain dependent on their interpretation and it

cannot be excluded that Investor-to-State tribunals interpret such facts generously in accordance with the wishes of investors and through the attribution of a quasi-international legal status put private interests of investors on the same level as democratic and sovereign interests of states or even above these. In this respect not only the recent excessive reference to the principle of "fair and equitable treatment" in arbitral procedures is problematic. Already the one-sided conception of investment protection agreements fosters the respective normative bias of the procedures' arbitrators. The explicit aim of the agreements is the protection of investment. Possible competing, democratically or constitutionally defined aims and principles are treated in the agreements as exemptions or restrictions - "in the spirit" of investment protection therefore as negatively. The principles of "fair" and "appropriate" conduct must not only be formulated with regard to states and governments, but also have to apply explicitly to the behaviour of investors and have to be enforceable. In recent reasoning on the reform of investment protection the UNCTAD for instance has considered the inclusion of "investors' duties". In so far as a need for such agreements exists in the first place, these must not be conceptualised as investment protection agreements but as investment agreements, in which the aim of protecting investments is qualified in the context of competing, partly superior aims or principles. The formulation of "carve-outs" or the reference to less binding or sanction-free OECD-guidelines for transnational companies is not sufficient in this regard. The concretisation of legitimate expectations concerning a stable development of the political conditions, often evoked in arbitral procedures, by referring to concrete stipulations in the context of investments might curb the excessive use of these provisions, but remains problematic. In democratically constituted societies investors also have to plan on changes in government or policies. If this has an impact on the contractual agreements between states and private investors, the proper legal course is open. Within developed legal systems with division of powers there is no reason to introduce an additional international privilege for investors.

Question 4: Expropriation

The objective of the EU is to clarify the provisions on expropriation and to provide interpretative guidance with regard to indirect expropriation in order to avoid claims against legitimate public policy measures. The EU wants to make it clear that non-discriminatory measures taken for legitimate public purposes, such as to protect health or the environment, cannot be considered equivalent to an expropriation, unless they are manifestly excessive in light of their purpose. The EU also wants to clarify that the simple fact that a measure has an impact on the economic value of the investment does not justify a claim that an indirect expropriation has occurred.

***Question**: What is your opinion of the approach to dealing with expropriation in relation to the TTIP? Please explain.*

The EU considers protection of property as fundamental to each investment agreement, also for TTIP. Under international law an expropriation of foreigners is permissible only if it serves a public purpose, has no discriminatory character and is linked to compensation. The compensation is mostly understood as complete compensation for the expropriation, which encompasses the current asset base and potential future profits. The new international contractual practice encompasses indirect expropriations alongside direct ones. This broad understanding of expropriations encompasses in addition to factual interventions, particularly regulatory measures, i.e. legislative and administrative instruments which eliminate the basis

for gains through changes in the framework conditions or otherwise intervene in the economic substance in a sensitive way. This can lead to a compensation duty for public measures. Especially with regard to public measures aiming for environmental protection or other public interests, the question arises whether this amounts to an expropriation-like measure which would cause a compensation duty towards foreign investors. The EU wants to clarify the term of measures with an expropriation-like effect and thereby provide the involved parties with an interpretation guideline to prevent potential compensation claims of investors which target public measures serving the general welfare. The aim is to guarantee that non-discriminatory measures, which serve the general welfare – e.g. environmental or health protection – cannot be perceived as expropriation-like measures, given that these are not disproportional. The circumstance alone that a measure has an effect of some sort on the economic value of an investment should not be sufficient. Questions with regard to the fact of an "indirect expropriation", the definition of exceptions and the evaluation of the 'damage' or an appropriate compensation are particularly problematic. The dispute between health or environmental measures and the opinion of investors that these amount to an indirect expropriation has been a regular subject of arbitral procedures recently. The formulation that non-discriminatory, 'legitimate' measures in the public interest should be excluded merely shifts the problem to assessments and considerations if such conditions are given or if the measures are appropriate. The experience from past arbitral procedures shows that the room for interpretation is being used and contributes to a rather inconsistent, partly contradictory "case law". Such assessments should reside with national courts or the European Court of Justice and provide possibilities for a public contention and, where necessary, participation. Dispute settlement procedures which are driven by commercial interests are not suitable in this context. This for example also applies when withdrawing granted concessions, licences or other commitments in the case of new scientific evidence or changed public assessments. Similar problems with regard to the weighting of differing interests and the appropriateness of measures or compensations arise likewise when evaluating the reduction of value of investments and the designation of an appropriate compensation. The evaluation of an investment's value or a reduction of value is mostly not objectively possible, since alternative developments are hypothetical and the future is tainted with uncertainty. Respective assessments and judgements therefore have to be independent and must not be influence by closely linked possibilities for profit.

Question 5: Ensuring the right to regulate and investment protection

The objective of the EU is to achieve a solid balance between the protection of investors and the Parties' right to regulate.

First of all, the EU wants to make sure that the Parties' right to regulate is confirmed as a basic underlying principle. This is important, as arbitral tribunals will have to take this principle into account when assessing any dispute settlement case.

Secondly, the EU will introduce clear and innovative provisions with regard to investment protection standards that have raised concern in the past (for instance, the standard of fair and equitable treatment is defined based on a closed list of basic rights; the annex on expropriation clarifies that non-discriminatory measures for legitimate public policy objectives do not constitute indirect expropriation). These improvements will ensure that investment protection standards cannot be interpreted by arbitral tribunals in a way that is detrimental to the right to regulate.

Third, the EU will ensure that all the necessary safeguards and exceptions are in place. For instance, foreign investors should be able to establish in the EU only under the terms and conditions defined by the EU. A list of horizontal exceptions will apply to non-discrimination obligations, in relation to measures such as those taken in the field of environmental protection, consumer protection or health (see question 2 for details). Additional carve-outs would apply to the audiovisual sector and the granting of subsidies. Decisions on competition matters will not be subject to investor-to-state dispute settlement (ISDS). Furthermore, in line with other EU agreements, nothing in the agreement would prevent a Party from taking measures for prudential reasons, including measures for the protection of depositors or measures to ensure the integrity and stability of its financial system. In addition, EU agreements contain general exceptions applying in situations of crisis, such as in circumstances of serious difficulties for the operation of the exchange rate policy or monetary policy, balance of payments or external financial difficulties, or threat thereof.

In terms of the procedural aspects relating to ISDS, the objective of the EU is to build a system capable of adapting to the states' right to regulate. Wherever greater clarity and precision proves necessary in order to protect the right to regulate, the Parties will have the possibility to adopt interpretations of the investment protection provisions which will be binding on arbitral tribunals. This will allow the Parties to oversee how the agreement is interpreted in practice and, where necessary, to influence the interpretation.

The procedural improvements proposed by the EU will also make it clear that an arbitral tribunal will not be able to order the repeal of a measure, but only compensation for the investor.

Furthermore, frivolous claims will be prevented and investors who bring claims unsuccessfully will pay the costs of the government concerned (see question 9).

***Question**: What is your opinion with regard to the way the right to regulate is dealt with in the EU's approach to TTIP?*

The right of democratic states to regulate is guaranteed through different regulations and principles of national and international law. Tension exists between public regulation oriented towards general welfare and the protection of foreign investments (see above answer to questions 2, 3 and 4). The EU pursues a balancing approach between the right of democratic states to regulate and investment protection. By clarifying rules of exception the aim is to make clear in favour of the involved parties, that non-discriminatory measures, e.g. for reasons of health protection, are permissible. The EU wants to establish the required rules for this purpose. This includes general rules of exception for times of crisis to guarantee the stability of the financial system (see below question 9). The involved parties can declare clarifying interpretations as binding and take these as a basis for arbitral procedures. A redemption of public measures should not be enforceable through arbitral procedures, only compensation payments to the investor. Moreover, frivolous claims should be filtered and the costs of unsuccessful claims imposed on the investor (see question 9).

The public right to regulation is self-evident. What is relevant are the indirect effects, which ensue from the assessment and interpretation of competing aims and pursued measures. The agency of states is not only compromised by potential compensation payments or the procedural costs of Investor-to-State-Dispute-Settlements, but also by the “chilling effect” that can be observed in consequence of threatened

claims in many cases. The reference to "legitimate public policy objectives" or "prudential reasons" still leaves room for interpretation. All the more important then becomes the question of to whom or to which authorities the respective interpretation is left and how these are guided. The assessment of whether or not a pursued policy aim is "legitimate", and primarily if and to what extent chosen measures are "necessary" or "expedient" and therefore justify an impairment of investors' interests is often dependent on the respective theoretical, interest-guided and not rarely ideological standpoint. This can be seen very markedly in the dispute about appropriate reforms and reactions to the financial crisis and the euro crisis. Positions and programmes of the International Monetary Fund and the EU-authorities are highly contested. Accordingly, the proposed exceptions regarding the regulations of financial markets and balance of payments in the draft CETA-agreement are also biased. Formulations that respective regulations have to be temporary, taken back as quickly as possible and should be evaluated on the basis of data and expertise of the International Monetary Fund, already mirror a specific – not uncontested – position, which has a priori influence on the assessment of corresponding "safeguard measures" as "appropriate" and "strictly necessary". Thereby, an ideologically guided prejudgement takes place, which (can) limit the opportunities for action of states to prevent crises or react adequately.

Decisions, for instance on the economic policy orientation, have to remain politically shapeable and must not be closed towards (future) societal and scientific contention. Moreover, definitions of single exceptions and the limitation of possibilities to regulate after the entry into force of the agreement, could be interpreted in a way that a negative list approach in the area of services and a so-called "ratchet effect" have been intended. Both would have to be refused.

Question 6: Transparency in ISDS

The EU's aim is to ensure transparency and openness in the ISDS system under TTIP. The EU will include provisions to guarantee that hearings are open and that all documents are available to the public. In ISDS cases brought under TTIP, all documents will be publicly available (subject only to the protection of confidential information and business secrets) and hearings will be open to the public. Interested parties from civil society will be able to file submissions to make their views and arguments known to the ISDS tribunal.

Question*: Please provide your views on whether this approach contributes to the objective of the EU to increase transparency and openness in the ISDS system for TTIP. Please indicate any additional suggestions you may have.*

The EU intends to incorporate the new UN transparency rules into TTIP in the context of the Investor-to-State-Dispute-Settlement. Consequently, all documents have to be published in principle. Civil society groups can furthermore file written inputs to the arbitral tribunal (so-called "amicus curiae briefs", cf. also WTO- dispute settlement). The actual interpretation and application of these, however, remains ambiguous so far. Given the existing relations between arbitrators, their chambers and investors (potentially) filing claims it must be feared that important questions among the parties will be discussed outside of the public procedures and will not be documented. In addition, there are various possibilities to circumvent transparency rules or to make them ineffective – starting from the interpretation of permissible exceptions in favour of confidentiality, the procedural organisation through to strategies of

issuing an overwhelming amount of hard to understand, but rather irrelevant information. It is doubtful if stricter transparency rules reduce the fundamental disadvantages of the Investor-to-State-Dispute-Settlement system compared to properly legitimated courts. On the contrary, it is to be feared that through rather marginal reforms without substantial improvements, mere acceptance shall be increased. New transparency rules neither justify a necessity nor an advantage of ISDS-arbitral procedures compared to proper courts.

Question 7: Multiple claims and relationship to domestic courts

As a matter of principle, the EU's approach favours domestic courts. The EU aims to provide incentives for investors to pursue claims in domestic courts or to seek amicable solutions – such as mediation. The EU will suggest different instruments to do this. One is to prolong the relevant time limits if an investor goes to domestic courts or mediation on the same matter, so as not to discourage an investor from pursuing these avenues. Another important element is to make sure that investors cannot bring claims on the same matter at the same time in front of an ISDS tribunal and domestic courts. The EU will also ensure that companies affiliated with the investor cannot bring claims in front of an ISDS tribunal and domestic courts on the same matter and at the same time. If there are other relevant or related cases, ISDS tribunals must take these into account. This is done to avoid any risk that the investor is over-compensated and helps to ensure consistency by excluding the possibility for parallel claims.

Question*:Please provide your views on the effectiveness of this approach for balancing access to ISDS with possible recourse to domestic courts and for avoiding conflicts between domestic remedies and ISDS in relation to the TTIP. Please indicate any further steps that can be taken. Please provide comments on the usefulness of mediation as a means to settle disputes*.

The EU intends to avoid investor ability to conduct procedures in front of a national court and the ISDS at the same time. Additionally, it shall be guaranteed that subsidiaries are not able to file a suit simultaneously in front of a national court and in the framework of the ISDS. The aim is to exclude an investor's overcompensation (due to two decisions in his favour). However, the relation between national jurisdiction and ISDS-procedures remains vague. An explicit exhaustion of all domestic legal remedies before the Investor-to-State-Dispute-Settlement can be accessed, is not envisaged. In principle, both legal processes are open to investors. If an investor initially takes legal action in the national jurisdiction, the way to the ISDS-procedure is subsequently further open to him. It also remains ambiguous if, when a foreign parent company brings an ISDS-procedure, a subsidiary located in the host country can simultaneously file a suit in front of the national court of the host country. Moreover it is not clear, why an additional ISDS-arbitral procedure alongside the public jurisdiction of the USA and the EU is necessary, since so far no evidence of systemic deficiencies in the two jurisdictions that could justify a basic mistrust is known. No investigations hint towards a discrimination of European companies by US-courts in favour of US-companies, but rather towards weaknesses in the ISDS-mechanisms. The prevention of (simultaneous) multiple claims is correct, but if the EU, as self-declared, prefers the domestic legal process, it would be more consequent to entirely waive the plans on ISDS-procedures, instead of merely agreeing on specific incentives and at the same time implicitly fuelling doubts regarding the reliability of proper courts.

Problematic: Only foreign investors have the possibility to additionally use the ISDS; domestic investors are excluded despite a comparable set of interests. This results in unequal treatment and discrimination of domestic investors.

Question 8: Arbitrator ethics, conduct and qualifications

The EU aims to establish clear rules to ensure that arbitrators are independent and act ethically. The EU will introduce specific requirements in the TTIP on the ethical conduct of arbitrators, including a code of conduct. This code of conduct will be binding on arbitrators in ISDS tribunals set up under TTIP. The code of conduct also establishes procedures to identify and deal with any conflicts of interest. Failure to abide by these ethical rules will result in the removal of the arbitrator from the tribunal. For example, if a responding state considers that the arbitrator chosen by the investor does not have the necessary qualifications or that he has a conflict of interest, the responding state can challenge the appointment. If the arbitrator is in breach of the Code of Conduct, he/she will be removed from the tribunal. In case the ISDS tribunal has already rendered its award and a breach of the code of conduct is found, the responding state or the investor can request a reversal of that ISDS finding.

In the text provided as reference (the draft EU-Canada Agreement), the Parties (i.e. the EU and Canada) have agreed for the first time in an investment agreement to include rules on the conduct of arbitrators, and have included the possibility to improve them further if necessary. In the context of TTIP these would be directly included in the agreement.

As regards the qualifications of ISDS arbitrators, the EU aims to set down detailed requirements for the arbitrators who act in ISDS tribunals under TTIP. They must be independent and impartial, with expertise in international law and international investment law and, if possible, experience in international trade law and international dispute resolution. Among those best qualified and who have undertaken such tasks will be retired judges, who generally have experience in ruling on issues that touch upon both trade and investment and on societal and public policy issues. The EU also aims to set up a roster, i.e. a list of qualified individuals from which the Chairperson for the ISDS tribunal is drawn, if the investor or the responding state cannot otherwise agree to a Chairperson. The purpose of such a roster is to ensure that the EU and the US have agreed to and vetted the arbitrators to ensure their abilities and independence. In this way the responding state chooses one arbitrator and has vetted the third arbitrator.

***Question**: Please provide your views on these procedures and in particular on the Code of Conduct and the requirements for the qualifications for arbitrators in relation to the TTIP agreement. Do they improve the existing system and can further improvements be envisaged?*

Unlike most investment protection agreements where the involved parties are allowed to freely choose the judges of the arbitral court without being bound to certain criteria, the EU intends to include clear rules in TTIP concerning the qualification, independence and ethically correct behaviour of arbitrators ("code of conduct"). Violations of these rules of conduct shall be punished by excluding the respective person from the arbitration. If the violation comes to be known only after the decision, the involved conflict parties can request the decision's repeal. Additionally, a register with suitable arbitrators is supposed to be established. Proven knowledge of international economic law (international investment law and, if possible, also international trade law and international dispute resolution law) are demanded as

qualifications. The introduction of rules of conduct and requirements with regard to the qualification and independence of arbitrators has to be understood as a (late and sheepish) reaction to criticism against the ISDS-mechanism. As long as such a code of conduct does not exist and no experiences have been made with the respective rules, their effectiveness is not assessable. However, as the experience with codes of conduct for companies shows, these are often weak or ineffective, are only insufficiently tested and frequently serve the purpose of warding off substantial rights of control and participation, e.g. of trade unions or civil society organisations. It remains equally doubtful if the problem of potential conflicts of interest and a lack of independence of the arbitrators can be removed through some procedural rules as long as the arbitrators and lawyers are recruited from a small and powerful network of specialised chambers. These chambers and their lawyers not only dispose of the necessary resources and various contacts, but also dominate the scientific discussion (and partly education) in this area of law, which is why one can suppose that they possess a certain degree of interpretational sovereignty concerning the formulation and interpretation of procedural standards. Also the interposition of a committee for preparing the list of persons and adopting the code of conduct as envisioned in Art. X-42 CETA, is not a solution since its composition takes place in accordance with the involved parties, can be steered by the parties, and therefore the independence of the committee is not guaranteed. The selection of personnel for the list is however an important pre-selection for a potential composition of the arbitral court. To qualify, the required legal knowledge has to cover the entire international public law, not only the international economic law. This is because the often decisive question of whether a host country can make use of legitimate exceptions for reasons of general welfare requires equally knowledge of international labour law, of international environmental and health protection law, and of the protection of human rights and social minimum standards. Likewise, knowledge on the law of the sued host country is a prerequisite.

Question 9: Reducing the risk of frivolous and unfounded cases

The EU will introduce several instruments in TTIP to quickly dismiss frivolous claims.

ISDS tribunals will be required to dismiss claims that are obviously without legal merit or legally unfounded. For example, this would be cases where the investor is not established in the US or the EU, or cases where the ISDS tribunal can quickly establish that there is in fact no discrimination between domestic and foreign investors. This provides an early and effective filtering mechanism for frivolous claims thereby avoiding a lengthy litigation process.

To further discourage unfounded claims, the EU is proposing that the losing party should bear all costs of the proceedings. So if investors take a chance at bringing certain claims and fail, they have to pay the full financial costs of this attempt.

***Question**: Please provide your views on these mechanisms for the avoidance of frivolous or unfounded claims and the removal of incentives in relation to the TTIP agreement. Please also indicate any other means to limit frivolous or unfounded claims.*

According to the EU's conceptions TTIP is supposed to include regulations to quickly filter and dismiss frivolous and unfounded claims. On top of that, regulations on costs are said to be incorporated, following which the defeated investor has to bear all costs of the proceedings. The question or decision whether claims are unfounded (noticeably without legal ground, unfounded on legal reasons) equally implies

questions of interpretation. Whether this will actually lead to a significant reduction in claims is as uncertain as the question whether this will decrease the pressure on political decision makers due to openly or covertly threatened claims. The justification of a claim has to be examined just as much as its chances of success, which again might provide those chambers with plenty of experience an advantage, especially towards public authorities with their limited resources. The assumption of the entire procedural costs by the defeated party might have a negative effect on economically weaker states. The rather high procedural costs, in particular of major international companies, are likely to pose a burden for such states and not the other way round (the state's procedural costs for these companies). The most effective and simplest way to reduce unfounded claims is to renounce the ISDS-mechanism in CETA and TTIP entirely.

Question 10: Allowing claims to proceed (filter)

The EU like many other states considers it important to protect the right to regulate in the financial sector and, more broadly, the overriding need to maintain the overall stability and integrity of the financial system, while also recognizing the speed needed for government action in case of financial crisis.

***Question**: Some investment agreements include filter mechanisms whereby the parties to the agreement (here the EU and the US) may intervene in ISDS cases where an investor seeks to challenge measures adopted pursuant to prudential rules for financial stability. In such cases the Parties may decide jointly that a claim should not proceed any further. Taking into account the above explanation and the text provided in annex as a reference, what are your views on the use and scope of such filter mechanisms in the TTIP agreement?*

It is planned to incorporate a TTIP-clause, following which the parties USA and EU are granted a collective procedural right to intervene in cases in which an investor's claim concerns the integrity of the public financial system, primarily or exclusively (as far as uncertain) in times of crisis ("financial crisis"). By the use of a collective intervention, the adversary proceedings will be stopped.

A collective intervention of the EU and the USA is assumed, thus constituting a consensus. This requirement can impede the termination of the adversary proceedings. The host countries are still exposed to the great risk of becoming involved in ISDS-proceedings due to measures of crisis management. This results in a virtual pressure on states and a not unrealistic self-limitation in favour of foreign investors and at the expense of financial wellbeing, even in times of crisis. In general, regulations which serve the stability and integrity of the financial sector must under no circumstances be negotiated in the framework of an Investor-to-State-Dispute-Settlement. To grant such possibilities to financial companies, whose business model partly consists of provoking and exploiting financial instability, is irresponsible. Past financial crises have impressively shown that a reliable protection in this regard is equally not to be expected from inter-governmental commissions. Firstly, international preferences concerning the stabilisation of specific financial markets are quite diverse; secondly, public regulation bodies also frequently possess insufficient information and knowledge on the financial sector and thirdly, a basic liberalisation bias still dominates with regard to the financial sector, which has significantly contributed

to the emergence of financial crises and is regularly limited (on a partial and temporary basis) only after the outbreak of a crisis.

Question 11: Guidance by the Parties (the EU and the US) on the interpretation of the agreement

The EU will make it possible for the non-disputing Party (i.e. the EU or the US) to intervene in ISDS proceedings between an investor and the other Party. This means that in each case, the Parties can explain to the arbitrators and to the Appellate Body how they would want the relevant provisions to be interpreted. Where both Parties agree on the interpretation, such interpretation is a very powerful statement, which ISDS tribunals would have to respect.

The EU would also provide for the Parties (i.e. the EU and the US) to adopt binding interpretations on issues of law, so as to correct or avoid interpretations by tribunals which might be considered to be against the common intentions of the EU and the US. Given the EU's intention to give clarity and precision to the investment protection obligations of the agreement, the scope for undesirable interpretations by ISDS tribunals is very limited. However, this provision is an additional safety-valve for the Parties.

***Question**: Please provide your views on this approach to ensure uniformity and predictability in the interpretation of the agreement to correct the balance. Are these elements desirable, and if so, do you consider them to be sufficient?*

The party involved in an ISDS-proceeding is supposed to be granted a right to intervene in order to introduce its interpretation of the decisive norm into the process. Moreover, binding interpretations of the involved parties shall limit the room for interpretation of the arbitral tribunal (see above).

The formulation of binding interpretations by public parties could potentially reduce the room for interpretation slightly, but it will not be removed. The arbitral tribunals still possess room for interpretation and are able to influence this through their "case law". One can perceive the belated formulation of interpretation guidelines as an attempt to split the criticism towards the ISDS-mechanism by firstly removing parts of the arrangement from public contestation to negotiate them afterwards with less attention. This strategy is not able to increase the acceptance of the Investor-to-State-Dispute-Settlement in CETA and TTIP since it amounts to a "blank-cheque". Such auxiliary constructs, moreover, reveal the questionable character of the ISDS-arbitral tribunals when public exertion of influence attempts to replace lacking judicial legitimation. Compared with this, proper courts liable to the principle of the division of powers are to be favoured.

Question 12: Appellate Mechanism and consistency of rulings

The EU aims to establish an appellate mechanism in TTIP so as to allow for review of ISDS rulings. It will help ensure consistency in the interpretation of TTIP and provide both the government and the investor with the opportunity to appeal against awards and to correct errors. This legal review is an additional check on the work of the arbitrators who have examined the case in the first place.

In agreements under negotiation by the EU, the possibility of creating an appellate mechanism in the future is envisaged. However, in TTIP the EU intends to go further and create a bilateral appellate mechanism immediately through the agreement.

***Question**: Taking into account the above explanation and the text provided in annex as a reference, please provide your views on the creation of an appellate mechanism in TTIP as a means to ensure uniformity and predictability in the interpretation of the agreement.*

Unlike other investment protection agreements, TTIP is supposed to be governed by a kind of "appellate instance" to enable a bilateral review of ISDS-decisions. Positive: An appellate instance serves legal certainty. Negative: The introduction of appellate mechanisms for single, specific agreement like TTIP or CETA rather additionally increases the inconsistency between various decisions of the arbitral tribunals.

Not only are the interpretations of single decisions then competing, but on top of that the decision and interpretation patterns on the basis of different and possibly competing agreements. If this leads to higher standards and increased legal certainty or to an intensified regime-shopping by multinational companies through exploiting the agreements' interpretational rivalry, is not identifiable.

Question 13: General assessment

***Question**: What is your overall assessment of the proposed approach on substantive standards of protection and ISDS as a basis for investment negotiations between the EU and US? Do you see other ways for the EU to improve the investment system? Are there any other issues related to the topics covered by the questionnaire that you would like to address?*

The question much more relevant in the civil society discussion, whether such a dispute settlement mechanism should not principally be precluded, has not been posed. There are no sufficient reasons to integrate an Investor-to-State-Dispute-Settlement mechanism into CETA and TTIP. Significant room for interpretation for the arbitral tribunals and the structural bias towards investment protection (foreign investors) including the thereby enabled potential to threaten other socially and democratically justified aims and rights to regulate (regulatory chill) remain. In the context of TTIP a considerable increase of claims has to be expected, whereby the financial burden and pressure against political regulation would grow. It is first of all an instrument of economic and political redistribution at the cost of the general public and democratic principles. Despite attempts to reform the ISDS-mechanism, the legal process via properly legitimated courts is to be widely favoured in developed democracies and constitutional states.

The character and 'spirit' of investment protection has to be reconsidered fundamentally – independent from the ISDS. Investment agreements should not be based exclusively on the protection of investors or investments. Other, partly superior societal aims or principles of protection (e.g. environmental and health protection, social, labour and political participation) have to be named as such - not merely as exceptions or restrictions – which would ensue duties for investors. International agreements shall serve the coordination of public and societal interests and not the private suability of individual interests. Most notably however, an interconnection between investment protection and fundamental international legal standards of international labour law (core norms of the ILO), human rights, environmental protection and social minimum standards is missing. A precondition for investment protection has to be an obligation by investors to respect and adhere to these fundamental standards of international law. If

private investors are able to sue (quasi)public contractual parties, who for their part as public authorities are bound to the above mentioned standards of international law, it would be consequent to oblige private actors through the TTIP-agreement to comply equally with these international legal standards, in order to benefit from TTIP's investment protection.

The fundamental question arises of whether a chapter on investment protection is required at all, since the USA as well as the EU have strongly enshrined the protection of property in their legal systems. Property rights are protected in the European Convention on Human Rights and the EU Charter of Fundamental Rights (the Charter). The Charter guarantees in Art. 17 the right to property and in case of deprivation a "fair compensation being paid in good time". The fundamental question moreover arises of why the ISDS-procedure alongside the US-jurisdiction, the EU-jurisdiction and the jurisdiction of the EU member states is necessary after all.

The ISDS-procedures present a form of privatised jurisdiction and the privatisation of judicature, which evolves next to public judicature and supplants the latter. There is no room for such private "auxiliary-jurisdiction" in democratic-constitutional states with a functioning, independent jurisdiction.

TTIP's system of legal protection results in a "two-class-system" for foreign investors who, along with the public jurisdiction, have access to the ISDS-procedure and domestic investors who are denied access to the ISDS-procedure, although their sets of interests do not differ.

ANNEX: Investment Protection in the Proposed EU-Canada Agreement (CETA)

An explanatory note by the editor:

The European Commission General Directorate Trade attached to its online public consultation on the modalities of investment protection and ISDS in TTIP (see previous chapter) an annex with a comparison of traditional protection provisions and those agreed upon in CETA. The CETA text is reprinted here.

A. Substantive Investment Protection Provisions

Question 1: Scope of the substantive investment protection provisions

'investment' means:

Every kind of asset that an investor owns or controls, directly or indirectly, which has the characteristics of an investment, such as the commitment of capital or other resources, the expectation of gain or profit, or the assumption of risk, and a certain duration. Forms that an investment may take include:

a) an enterprise;

b) shares, stocks and other forms of equity participation in an enterprise;

c) bonds, debentures and other debt instruments of an enterprise;

d) a loan to an enterprise;

e) any other kinds of interest in an enterprise;

f) an interest arising from:

i. a concession conferred pursuant to domestic law or under a contract, including to search for, cultivate, extract or exploit natural resources,

ii. a turnkey, construction, production, or revenue-sharing contract, or

iii. other similar contracts;

g) intellectual property rights;

h) any other moveable property, tangible or intangible, or immovable property and related rights;

i) claims to money or claims to performance under a contract;

For greater certainty, 'claims to money' does not include claims to money that arise solely from commercial contracts for the sale of goods or services by a natural person or enterprise in the territory of a Party to a natural person or enterprise in the territory of the other Party, domestic financing of such contracts, or any related order, judgment, or arbitral award.

Returns that are invested shall be treated as investments. Any alteration of the form in which assets are invested or reinvested does not affect their qualification as investment.

covered investment means, with respect to a Party, an investment:

a) in its territory;

b) made in accordance with the applicable law at that time;

c) directly or indirectly owned or controlled by an investor of the other Party; and

d) existing on the date of entry into force of this Agreement, as well as investments made or acquired thereafter.

investor means a Party, a natural person or an enterprise of a Party, that seeks to make, is making or has made an investment in the territory of the other Party.

But **"investor" does not mean:**

a) an enterprise of a Party, if the enterprise is owned or controlled by an investor of the other Party or of a non-Party and the enterprise has no substantial business activities in the territory of the Party under whose law it is constituted or organized; or,

b) a branch or representative office of an enterprise of a Party or a non-Party.

Question 2: Non-discriminatory treatment for investors

"Section X: Non-Discriminatory Treatment

Article X.1: National Treatment

1. Each Party shall accord to investors of the other Party and to covered investments, treatment no less favourable than the treatment it accords, in like situations, to its own investors and to their investments with respect to the establishment, acquisition, conduct, operation, management, maintenance, use, enjoyment and sale or disposal of their investments in its territory.

The treatment accorded by a Party under paragraph 1 means, with respect to measures adopted or maintained by a government in Canada other than at federal level, or by a government of or in an European Union Member State, treatment no less favourable than the most favourable treatment accorded by that government, in like situations, to investors of the other Party and to covered investments of Canada or of the European Union respectively, including jurisdictions of that government.

Article X.2: Most-Favoured-Nation Treatment

1. Each Party shall accord to investors of the other Party and to covered investments, treatment no less favourable than the treatment it accords, in like situations, to investors and to their investments of any third country with respect to the establishment, acquisition, conduct, the operation, management, maintenance, use, enjoyment and sale or disposal of their investments in its territory.

2. The treatment accorded by a Party under paragraph 1 means, with respect to measures adopted or maintained by a government in Canada other than at federal level, or by a government of or in an European Union Member State, treatment no less favourable than the most favourable treatment accorded by that government, in like situations, to investors and to covered investments of Canada or of the European Union respectively, including jurisdictions of that government.

3. Paragraph 1 shall not be construed to oblige a Party to extend to the investors of the other Party the benefit of any treatment resulting from existing or future measures providing for recognition.

4. For greater certainty, the "treatment" referred to in Paragraph 1:

a. does not include investor-to-state dispute settlement procedures provided for in other international investment treaties and other trade agreements, including compensation granted through such procedures, and

b. shall only apply with respect to treatment accorded by a Party through the adoption, maintenance or application of measures.

3. Paragraph 1 shall not be construed to oblige a Party to extend to the investors of the other Party the benefit of any treatment resulting from:

(a) treatment granted as a process of economic integration, which includes commitments to abolish substantially all barriers to investment, together with the approximation of legislation of the parties on a broad range of matters within the purview of this Agreement.

(b) any international agreement for the avoidance of double taxation or other international agreement or arrangement relating wholly or mainly to taxation.

Article Y: General exceptions

1. For the purposes of Chapters X through Y and Chapter Z (National Treatment and Market Access for Goods, Rules of Origin, Origin Procedures, Customs and Trade Facilitation), Section 2 (Establishment of Investments) and Section 3 (Non-discrimination of Investment), GATT 1994 Article XX is incorporated into and made part of this Agreement.

The Parties understand that the measures referred to in GATT 1994 Article XX (b) include environmental measures necessary to protect human, animal or plant life or health. The Parties further understand that GATT 1994 Article XX (g) applies to measures for the conservation of living and non-living exhaustible natural resources.

2. For the purposes of Chapters X, Y, and Z (Cross-Border Trade in Services, Telecommunications, and Temporary Entry and Stay of Natural Persons for Business Purposes), Section 2 (Establishment of Investments) and Section 3 (Non-discrimination of Investment)) GATS Article XIV (a), (b) and (c) is incorporated into this Agreement.

The Parties understand that the measures referred to in GATS Article XIV (b) include environmental measures necessary to protect human, animal or plant life or health.

Question 3: Fair and equitable treatment

Section X: Investment Protection

Article X.X.: Treatment of Investors and of Covered Investments

1. Each Party shall accord in its territory to covered investments of the other Party and to investors with respect to their covered investments fair and equitable treatment and full protection and security in accordance with paragraphs 2 to 7.

2. A Party breaches the obligation of fair and equitable treatment referenced in paragraph 1 where a measure or series of measures constitutes:

a. Denial of justice in criminal, civil or administrative proceedings;

b. Fundamental breach of due process, including a fundamental breach of transparency, in judicial and administrative proceedings.

c. Manifest arbitrariness;

d. Targeted discrimination on manifestly wrongful grounds, such as gender, race or religious belief;

e. Abusive treatment of investors, such as coercion, duress and harassment; or

f. A breach of any further elements of the fair and equitable treatment obligation adopted by the Parties in accordance with paragraph 3 of this Article.

3. The Parties shall regularly, or upon request of a Party, review the content of the obligation to provide fair and equitable treatment.

4. When applying the above fair and equitable treatment obligation, a tribunal may take into account whether a Party made a specific representation to an investor to induce a covered investment, that created a legitimate

expectation, and upon which the investor relied in deciding to make or maintain the covered investment, but that the Party subsequently frustrated.

5. For greater certainty, 'full protection and security' refers to the Party's obligations relating to physical security of investors and covered investments.

6. For greater certainty, a breach of another provision of this Agreement, or of a separate international Agreement, does not establish

Question 4: Expropriation

Article X: Expropriation

1. Neither Party may nationalize or expropriate a covered investment either directly, or indirectly through measures having an effect equivalent to nationalization or expropriation (hereinafter referred to as "expropriation"), except:

(a) for a public purpose;

(b) under due process of law;

(c) in a non-discriminatory manner; and

(d) against payment of prompt, adequate and effective compensation.

For greater certainty, this paragraph shall be interpreted in accordance with Annex X.9.1 on the clarification of expropriation.

2. Such compensation shall amount to the fair market value of the investment at the time immediately before the expropriation or the impending expropriation became known, whichever is earlier. Valuation

criteria shall include going concern value, asset value including the declared tax value of tangible property, and other criteria, as appropriate, to determine fair market value.

3. The compensation shall also include interest at a normal commercial rate from the date of expropriation until the date of payment and shall, in order to be effective for the investor, be paid and made transferable, without delay, to the country designated by the investor and in the currency of the country of which the investor is a national or in any freely convertible currency accepted by the investor.

4. The investor affected shall have a right, under the law of the expropriating Party, to prompt review of its claim and of the valuation of its investment, by a judicial or other independent authority of that Party, in accordance with the principles set out in this Article.

5. This Article does not apply to the issuance of compulsory licenses granted in relation to intellectual property rights, to the extent that such issuance is consistent with the Agreement on Trade-Related Aspects of Intellectual Property Rights in Annex 1C to the WTO Agreements ('TRIPS Agreement').

Annex: Expropriation

The Parties confirm their shared understanding that:

1. Expropriation may be either direct or indirect:

a) direct expropriation occurs when an investment is nationalised or otherwise directly expropriated through formal transfer of title or outright seizure; and

b) indirect expropriation occurs where a measure or series of measures by a Party has an effect equivalent to direct expropriation, in that it substantially deprives the investor of the fundamental attributes of property in its investment, including the right to use, enjoy and dispose of its investment, without formal transfer of title or outright seizure.

2. The determination of whether a measure or series of measures by a Party, in a specific fact situation, constitutes an indirect expropriation requires a case-by-case, fact-based inquiry that considers, among other factors:

a) the economic impact of the measure or series of measures, although the sole fact that a measure or series of measures of a Party has an adverse effect on the economic value of an investment does not establish that an indirect expropriation has occurred;

b) the duration of the measure or series of measures by a Party;

c) the extent to which the measure or series of measures interferes with distinct,

reasonable investment-backed

expectations; and

d) the character of the measure or series of measures, notably their object, context and intent.

3. For greater certainty, except in the rare circumstance where the impact of the measure or series of measures is so severe in light of its purpose that it appears manifestly excessive, non-discriminatory measures by a Party that are designed and applied to protect legitimate public welfare objectives, such as health, safety and the environment, do not constitute indirect expropriations.

Question 5: Ensuring the right to regulate and investment protection

Preamble [Extract]

"REAFFIRMING their commitment to sustainable development and convinced of the contribution of international trade and investment to sustainable development,

RECOGNISING the right of the Parties to take measures to achieve legitimate public policy objectives on the basis of the level of protection that they deem appropriate,

DETERMINED to strengthen their economic, trade, and investment relations in accordance with the objective of sustainable development, in its economic, social and environmental dimensions, and to promote trade and investment in a manner mindful of high levels of environmental and labour protection and relevant internationally recognised standards and agreements to which they are Parties,

DESIRING to encourage enterprises operating within their territory or subject to their jurisdiction to respect internationally recognized standards and principles of corporate social responsibility notably the OECD Guidelines for multinational enterprises and to pursue best practices of responsible business conduct,

SEEKING to establish clear and mutually advantageous rules governing their trade and investment and to reduce or eliminate the barriers to mutual trade and investment ,

BUILDING on their respective rights and obligations under the WTO Agreement and other multilateral, regional and bilateral agreements and arrangements to which they are party,".

Article X: Reservations and Exceptions

"1. Articles X- (National Treatment), X- (Most-Favoured-Nation Treatment), (…) do not apply to:

(a) an existing non-conforming measure that is maintained by a Party at the level of:

(i) the European Union, as set out in its Schedule to Annex I;

(ii) a national government, as set out in its Schedule to Annex I;

(iii) a provincial, territorial, or regional government, as set out in its Schedule to Annex I; or

(iv) a local government.

(b) the continuation or prompt renewal of any non-conforming measure referred to in subparagraph (a); or

(c) an amendment to any non-conforming measure referred to in subparagraph (a) to the extent that the amendment does not decrease the conformity of the measure, as it existed immediately before the amendment, with Articles X- (National Treatment), X- (Most-Favoured-Nation Treatment), (…).

2. Articles X- (National Treatment), X- (Most-Favoured-Nation Treatment), (…) do not apply to measures that a Party adopts or maintains with respect to sectors, subsectors or activities, as set out in its Schedule to Annex II.

3. Without prejudice to Article X [Expropriation] and Article X [Treatment of Investors and Covered Investments], no Party may adopt any measure or series of measures after the date of entry into force of this Agreement and covered by its schedule to Annex II, that require, directly or indirectly, an investor of

the other Party, by reason of nationality, to sell or otherwise dispose of an investment existing at the time the measure or series of measures becomes effective.

4. In respect of intellectual property rights, a Party may derogate from Article X.3 (National Treatment), Article X.4 (Most-Favoured-Nation Treatment) where permitted by the TRIPS Agreement, including any amendments to the TRIPS Agreement in force for both Parties, and waivers to the TRIPS Agreement adopted pursuant to Article IX of the WTO Agreement.

5. (…) Articles X.3 (National Treatment), X.4 (Most-Favoured-Nation Treatment) (..) do not apply to:

(a) procurement by a Party or a State Enterprise for goods and services purchased for governmental purposes and not with a view to commercial resale or with a view to use in the supply of goods and services for commercial sale, whether or not that procurement is "covered procurement" within the meaning of Article II of (Chapter XX - Public procurement); or

(b) subsidies or government support provided by a Party including direct or potential transfer of funds, the foregoing of government revenue (such as a tax credit), and the provision of goods or services."

Audiovisual:
"For the EU, the Section on Establishment and Section on Non-Discriminatory Treatment do not apply to measures with respect to Audiovisual services."

ARTICLE X: PRUDENTIAL CARVE-OUT
1. Nothing in this Agreement shall prevent a Party from adopting or maintaining measures for prudential reasons, including:

(a) the protection of investors, depositors, policy-holders or persons to whom a fiduciary duty is owed by a financial service supplier;

(b) ensuring the integrity and stability of a Party's financial system.

2. These measures shall not be more burdensome than necessary to achieve their aim.

3. Without prejudice to other means of prudential regulation of cross-border trade in financial services, a Party may require the registration of cross-border financial service suppliers of the other Party and of financial instruments.

4. Subject to Article X [National Treatment] and Article Y [Most Favoured Nation], a Party may, for prudential reasons, prohibit a particular financial service or activity. Such a prohibition may not apply to all financial services or to a complete financial services sub-sector, such as banking.

Article X: Safeguard measures
In exceptional circumstances of serious difficulties for the operation of monetary and exchange rate policy, in the case of Canada, or for the operation of the economic and monetary union, in the case of the European Union, or threat thereof, safeguard measures that are strictly necessary may be taken by the concerned Party with regard to capital movements or payments, including transfers, for a period not exceeding six months. The Party having adopted or maintained such measures shall inform the other Party forthwith and present, as soon as possible, a time schedule for their removal.

Article X Balance of Payments

1. Nothing in this Agreement shall be construed to prevent the Parties from adopting or maintaining safeguard measures with regard to capital movements or payments, including transfers, in case of serious balance-of-payments or external financial difficulties, or under threat thereof.

2. The measures referred to in paragraph 1 shall:

a) not discriminate among countries;

b) be consistent with the Articles of the Agreement of the International Monetary Fund, as applicable;

c) avoid unnecessary damage to the commercial, economic and financial interests of the other Party;

d) be temporary and phased out progressively as the situation specified in paragraph 1 improves.

3. In the case of trade in goods, nothing in this Agreement shall be construed to prevent a Party from adopting restrictive measures in order to safeguard its balance-of-payments or external financial position. Such measures shall be in accordance with the General Agreement on Tariffs and Trade (GATT) and the Understanding on Balance of Payment Provisions of the GATT 1994.

4. In the case of trade in services, nothing in this Agreement shall be construed to prevent a Party from adopting restrictive measures in order to safeguard its balance-of-payments or external financial position. Such measures shall be in accordance with the General Agreement on Trade in Services (GATS).

5. Any Party maintaining or having adopted measures referred to in paragraph 1 or 2 shall promptly notify the other Party of them and present, as soon as possible, a time schedule for their removal.

6. Where the restrictions are adopted or maintained under this Article, consultations shall be held promptly in the Trade Committee, if such consultations are not otherwise taking place outside of this Agreement. The consultations shall assess the balance-of-payments or external financial difficulty that led to the respective measures, taking into account, inter alia, such factors as:

(a) the nature and extent of the difficulties;

(b)the external economic and trading environment; or

(c) alternative corrective measures which may be available.

The consultations shall address the compliance of any restrictive measures with paragraphs 1 and 2. All findings of statistical and other facts presented by the IMF relating to foreign exchange, monetary reserves and balance-of-payments shall be accepted and conclusions shall be based on the assessment by the IMF of the balance-of-payments and the external financial situation of the Party concerned.

B. Investor-to-State Dispute Settlement (ISDS)

Question 6: Transparency in ISDS

Article x-33: Transparency of Proceedings

1. The UNCITRAL Transparency Rules shall apply to the disclosure of information to the public concerning disputes under this Section as modified by this Chapter.

2. The request for consultations, the request for a determination, the notice of determination, the agreement to mediate, the notice of intent to challenge, the decision on an arbitrator challenge and the request for consolidation shall be included in the list of documents referred to in Article 3(1) of the UNCITRAL Transparency Rules.

3. Exhibits shall be included in the list of documents mentioned in Article 3(2) of the UNCITRAL Transparency Rules.

4. Notwithstanding Article 2 of the UNCITRAL Transparency Rules, prior to the constitution of the tribunal, Canada or the European Union as the case may be shall make publicly available in a timely manner relevant documents pursuant to paragraph 2, subject to the redaction of confidential or protected information. Such documents may be made publicly available by communication to the repository.

5. Hearings shall be open to the public. The tribunal shall determine, in consultation with the disputing parties, the appropriate logistical arrangements to facilitate public access to such hearings. Where the tribunal determines that there is a need to protect confidential or protected information, it shall make the appropriate arrangements to hold in private that part of the hearing requiring such protection.

6. Nothing in this Chapter requires a respondent to withhold from the public information required to be disclosed by its laws. The respondent should endeavour to apply such laws in a manner sensitive to protecting from disclosure information that has been designated as confidential or protected information.

Question 7: Multiple claims and relationship to domestic courts

Article x-21: Procedural and Other Requirements for the Submission of a Claim to Arbitration

1. An investor may submit a claim to arbitration under Article x-22 (Submission of a Claim to Arbitration) only if the investor:

a) delivers to the respondent, with the submission of a claim to arbitration, its consent to arbitration in accordance with the procedures set out in this Chapter;

b) allows at least 180 days to elapse from the submission of the request for consultations and, where applicable, at least 90 days to elapse from the submission of the notice requesting a determination;

c) fulfils the requirements of the notice requesting a determination of the respondent;

d) fulfils the requirements related to the request for consultations;

e) does not identify measures in its claim to arbitration that were not identified in its request for consultations;

f) provides a declaration, where it has initiated a claim or proceeding, seeking compensation or damages before a tribunal or court under domestic or international law with respect to any measure alleged to constitute a breach referred to in its claim to arbitration, that:

i. a final award, judgment or

decision has been made; or

ii. it has withdrawn any such claim or proceeding;

The declaration shall contain, as applicable, proof that a final award, judgment or decision has been made or proof of the withdrawal of any such claim or proceeding; and

g) waives its right to initiate any claim or proceeding seeking compensation or damages before a tribunal or court under domestic or international law with respect to any measure alleged to constitute a breach referred to in its claim to arbitration.

2. Where the submission of a claim to arbitration is for loss or damage to a locally established enterprise or to an interest in a locally established enterprise that the investor owns or controls directly or indirectly, both the investor and the locally established enterprise shall provide a declaration pursuant to subparagraph 1(f) and a waiver pursuant to subparagraph 1(g).

3. The requirements of paragraphs 1(f), (g) and 2 do not apply in respect of a locally established enterprise where the respondent or the investor's host State has deprived an investor of control of the locally established enterprise, or has otherwise prevented the locally established enterprise from fulfilling the requirements in subparagraph 1(f), (g) or 2.

4. Upon request of the respondent, the Tribunal shall decline jurisdiction where the investor or, as applicable, the locally established enterprise fails to fulfil any of the requirements of paragraphs 1 and 2.

5. The waiver provided pursuant to subparagraph 1(g) or paragraph 2 as applicable shall cease to apply:

i. where the Tribunal rejects the claim on the basis of a failure to meet the requirements of paragraphs 1 or 2 or on any other procedural or jurisdictional grounds;

ii. where the Tribunal dismisses the claim pursuant to Article x-29 (Claim manifestly without legal merit) or Article x-30 (Claims Unfounded as a Matter of Law); or

where the investor withdraws its claim, in conformity with applicable arbitration rules, within 12 months of the constitution of the tribunal.

Article x-23: Proceedings under different international agreements

Where claims are brought both pursuant to this Section and another international agreement and:

a) there is a potential for overlapping compensation; or

b) the other international claim could have a significant impact on the resolution of the claim brought pursuant to this Section,

a Tribunal constituted under this Section shall, as soon as possible after hearing the disputing parties, stay its proceedings or otherwise ensure that proceedings pursuant to another international agreement are taken into account in its decision, order or award.

Article x-19: Mediation

1. The disputing parties may at any time agree to have recourse to mediation.

2. Recourse to mediation is without prejudice to the legal position or rights of either disputing party under this chapter and shall be governed by the rules agreed to by the disputing parties including, if available, the rules established by the Services and Investment Committee pursuant to Article x-42(5)(d).

3. The mediator is appointed by agreement of the disputing parties. Such appointment may include appointing a mediator from the roster established pursuant to Article x-25 (Constitution of the Tribunal) or requesting the Secretary General of ICSID to appoint a mediator from the list of chairpersons established pursuant to Article x-25 (Constitution of the Tribunal).

4. Disputing parties shall endeavour to reach a resolution to the dispute within 60 days from the appointment of the mediator.

5. If the disputing parties agree to have recourse to mediation, Articles x-18(5) and x-18(7) (Consultations) shall not apply from the date on which the disputing parties agreed to have recourse to mediation to the date on which either disputing party decides to terminate the mediation, by way of a letter to the mediator and the other disputing party.

Question 8: Arbitrator ethics, conduct and qualifications

Article x-25: Constitution of the Tribunal

1. Unless the disputing parties have agreed to appoint a sole arbitrator, the Tribunal shall comprise three arbitrators. One arbitrator shall be appointed by each of the disputing parties and the third, who will be the presiding arbitrator, shall be appointed by agreement of the disputing parties. If the disputing parties agree to appoint a sole arbitrator, the disputing parties shall seek to agree on the sole arbitrator.

2. If a Tribunal has not been constituted within 90 days from the date that a claim is submitted to arbitration, or where the disputing parties have agreed to appoint a sole arbitrator and have failed to do so within 90 days from the date the respondent agreed to submit the dispute to a sole arbitrator, a disputing party may request the Secretary-General of ICSID to appoint the arbitrator or arbitrators not yet appointed. The Secretary General of ICSID shall appoint the remaining arbitrators from the list established pursuant to paragraph 3. In the event that such list has not been established on the date a claim is submitted to arbitration, the Secretary-General of ICSID shall make the appointment at his or her own discretion taking into consideration nominations made by either Party and, to the extent practicable, in consultation with the disputing parties. The Secretary-General of ICSID may not appoint as presiding arbitrator a national of either Canada or a Member State of the European Union unless all disputing parties agree otherwise.

3. Pursuant to Article x-42(2), the Committee on Services and Investment shall establish, and thereafter maintain, a list of individuals who are willing and able to serve as arbitrators and who meet the

qualifications set out in paragraph 5. The Committee on Services and Investment shall ensure that the list includes at least 15 individuals.

4. The list established in paragraph 3 shall be composed of three sub-lists: one sub-list for each Party and one sub-list of individuals, who are neither nationals of Canada nor the Member States of the European Union, to act as presiding arbitrators. Each sub-list shall include at least five individuals. The Committee on Services and Investment may agree to increase the number of arbitrators for the list.

5. Arbitrators appointed pursuant to this Section shall have expertise or experience in public international law, in particular international investment law. It is desirable that they have expertise or experience in international trade law, and the resolution of disputes arising under international investment or international trade agreements.

6. Arbitrators shall be independent of, and not be affiliated with or take instructions from any disputing party or the government of a Party with regard to trade and investment matters. Arbitrators shall not take instructions from any organisation, government or disputing party with regard to matters related to the dispute. Arbitrators shall comply with the International Bar Association Guidelines on Conflicts of Interest in International Arbitration or any supplemental rules adopted pursuant to Article x-42 (Committee on Services and Investment). Arbitrators who serve on the list established pursuant to paragraph 3 shall not, for that reason alone, be deemed to be affiliated with the government of a Party.

7. If a disputing party considers that an arbitrator does not meet the requirements set out in paragraph 6, it shall send a notice of its intent to challenge the arbitrator within 15 days after:

a) the appointment of the arbitrator has been notified to the challenging party; or,

b) the disputing party became aware of the facts giving rise to the alleged failure to meet such requirements.

8. The notice of an intention to challenge shall be promptly communicated to the other disputing party, to the arbitrator or arbitrators, as applicable, and to the Secretary General of ICSID. The notice of challenge shall state the reasons for the challenge.

9. When an arbitrator has been challenged by a disputing party, the disputing parties may agree to the challenge, in which case the disputing parties may request the challenged arbitrator to resign.

The arbitrator may also, after the challenge, elect to resign. In neither case does this imply acceptance of the validity of the grounds for the challenge.

10. If, within 15 days from the date of the notice of challenge, the challenged arbitrator has elected not to resign, the Secretary-General of ICSID shall, after hearing the disputing parties and after providing the arbitrator an opportunity to submit any observations, issue a decision within 45 days of receipt of the notice of challenge and forthwith notify the disputing parties and other arbitrators, as applicable.

11. A vacancy resulting from the disqualification or resignation of an arbitrator shall be promptly filled pursuant to the procedure provided for in this Article.

Article x-42: Committee

The Committee shall, on agreement of the Parties, and after completion of the respective legal requirements and procedures of the Parties, decide to:

a) establish and maintain the list of arbitrators pursuant to Article x-25(3)(Constitution of the Tribunal);

b) adopt a code of conduct for arbitrators to be applied in disputes arising out of this chapter, which may replace or supplement the rules in application, and that may address topics including:

i. disclosure obligations;

ii. the independence and impartiality of arbitrators; and

iii. confidentiality.

The Parties shall make best efforts to ensure that the decisions referred to in (a) and (b) are adopted no later than the entry into force of the Agreement, and in any event no later than two years after the entry into force of the Agreement.

Question 9: Reducing the risk of frivolous and unfounded cases

Article x-29: Claims Manifestly Without Legal Merit

1. The respondent may, no later than 30 days after the constitution of the tribunal, and in any event before the first session of the Tribunal, file an objection that a claim is manifestly without legal merit.

2. An objection may not be submitted under paragraph 1 if the respondent has filed an objection pursuant to Article x-30 (Claims Unfounded as a Matter of Law).

3. The respondent shall specify as precisely as possible the basis for the objection.

4. On receipt of an objection pursuant to this article, the Tribunal shall suspend the proceedings on the merits and establish a schedule for considering any objections consistent with its schedule for considering any other preliminary question.

5. The Tribunal, after giving the disputing parties an opportunity to present their observations, shall at its first session or promptly thereafter, issue a decision or award, stating the grounds therefor. In doing so, the Tribunal shall assume the alleged facts to be true.

6. This article shall be without prejudice to the Tribunal's authority to address other objections as a preliminary question or to the right of the respondent to object, in the course of the proceeding, that a claim lacks legal merit.

Article x-30: Claims Unfounded as a Matter of Law

1. Without prejudice to a tribunal's authority to address other objections as a preliminary question or to a respondent's right to raise any such objections at any appropriate time, the Tribunal shall address and decide as a preliminary question any objection by the respondent that, as a matter of law, a claim, or any part thereof, submitted under this section is not a claim for which an award in favour of the claimant may be made under Article x-22 (Submission of a Claim to Arbitration), even if the facts alleged were assumed to be true.

2. An objection under paragraph 1 shall be submitted to the Tribunal no later than the date the Tribunal fixes for the respondent to submit its counter-memorial.

3. If an objection has been submitted pursuant to Article x-29 (Claim Manifestly Without Legal Merit), the Tribunal may, taking into account the circumstances of that objection, decline to

address an objection submitted pursuant to paragraph 1.

4. On receipt of an objection under paragraph 1, and subject to paragraph 3, the Tribunal shall suspend any proceedings on the merits, establish a schedule for considering the objection consistent with any schedule it has established for considering any other preliminary question, and issue a decision or award on the objection, stating the grounds therefor.

Reference text (on costs):
Text developed in EU-Canada agreement (CETA)

Article x-36: Final Award
5. A tribunal shall order that the costs of arbitration be borne by the unsuccessful disputing party. In exceptional circumstances, a tribunal may apportion costs between the disputing parties if it determines that apportionment is appropriate in the circumstances of the claim. Other reasonable costs, including costs of legal representation and assistance, shall be borne by the unsuccessful disputing party, unless the tribunal determines that such apportionment is unreasonable in the circumstances of the claim. Where only some parts of the claims have been successful the costs shall be adjusted, proportionately, to the number or extent of the successful parts of the claims.

Question 10: Allowing claims to proceed (filter)

1. The provisions of [Investor-to-State Dispute Settlement] apply, as modified by this Article and Annex XXX, to:

a. investment disputes pertaining to measures to which this Chapter applies in which an investor claims that a Party has breached Articles X.12 (Investment – Transfers), X.11 (Investment – Expropriation), X.10 (Investment - Compensation for Losses), X.9 (Investment – Treatment of Investors and of Covered Investments), X.15 (Investment – Denial of Benefits), X.3 (Financial Services - National Treatment) or X.4 (Financial Services - Most-Favoured Nation Treatment); or

b. investment disputes commenced pursuant to [Investor State Dispute Settlement] in which Article 15.1 (Prudential Carve-Out/Exceptions) has been invoked.

2. Unless the disputing parties agree otherwise, in the case of an investment dispute under sub-paragraph 1(a), or where the respondent invokes Article 15.1 (Prudential Carve-Out/Exceptions) within 60 days of the submission of a claim to arbitration under Article X-22 (Submission of a Claim to Arbitration), the Tribunal shall be constituted from the list established under Article X-19(Financial Services – Dispute Settlement). Where the respondent invokes Article 15.1 (Prudential Carve-Out/Exceptions) within 60 days of submission of a claim, with respect to a measure to which this Chapter does not apply, the time period applicable to the constitution of the Tribunal under Article X-25 (Constitution of the Tribunal) shall commence on the date the respondent invokes Article 15.1 (Prudential Carve-Out/Exceptions). In

the event that the disputing parties are unable to agree on the composition of the Tribunal within the time frame laid down in Article X-25 (Constitution of the Tribunal) either disputing party may request the Secretary-General of ICSID to select the arbitrators from the list established under Article X-19 (Financial Services – Dispute Settlement). In the event that disputing parties are unable to constitute the Tribunal from the list, or that the list has not been established under Article X-19 (Financial Services – Dispute Settlement) on the date the claim is submitted to arbitration, the Secretary-General of ICSID shall select the arbitrators from the individuals proposed by one or both of the Parties in accordance with Article Article X-19 (Financial Services – Dispute Settlement).

3. The respondent may refer the matter in writing to the Financial Services Committee for a decision as to whether and, if so, to what extent the exception under Article 15.1 (Prudential Carve-Out/Exceptions) is a valid defence to the claim. Such a referral cannot be made later than the date the Tribunal fixes for the respondent to submit its counter-memorial. Where the respondent refers the matter to the Financial Services Committee under paragraph 3 the time periods or proceedings specified in [Investor-to-State-Dispute Settlement] shall be suspended.

4. In a referral under paragraph 3, the Financial Services Committee or the CETA Trade Committee as the case may be, may make a joint determination on whether and to what extent Article 15.1 (Prudential Carve-Out/Exceptions) is a valid defence to the claim. The Financial Services Committee or the CETA Trade Committee as the case may be, shall transmit a copy of any joint determination to the investor and the Tribunal, if constituted. If such joint determination concludes that Article 15.1 (Prudential Carve-Out/Exceptions) is a valid defence to all parts of the claim in their entirety, the investor shall be deemed to have withdrawn its claim and proceedings shall be discontinued in accordance with Article X-32 (Discontinuance). If such joint determination concludes that Article 15.1 (Prudential Carve-Out/Exceptions) is a valid defence to only parts of the claim, the joint determination shall be binding on the Tribunal with respect to those parts of the claim, the suspension of the timelines or proceedings in paragraph 4 shall no longer apply, and the investor may proceed with any remaining parts of the claim.

5. If the CETA Trade Committee has not made a joint determination within 3 months of referral of the matter by the Financial Services Committee, the suspension of the time periods or proceedings referenced in paragraph 4 shall no longer apply and the investor may proceed with its claim.

6. At the request of the respondent, the Tribunal shall decide as a preliminary matter whether and to what extent Article 15.1 (Prudential Carve-Out/Exceptions) is a valid defence to the claim. Failure of the respondent to make such a request is without prejudice to the right of the respondent to assert Article 15.1 (Prudential Carve-Out/Exceptions) as a defence in a later phase of the arbitration. The Tribunal shall draw no adverse inference from the fact that the Financial Services Committee or the CETA Trade Committee has not agreed on a joint determination in accordance with Annex XXX.

Question 11: Guidance by the Parties (the EU and the US) on the interpretation of the agreement

Article x-27: Applicable Law and Rules of Interpretation

2. Where serious concerns arise as regards matters of interpretation that may affect investment, the Committee on Services and Investment may recommend to the CETA Trade Committee the adoption of interpretations of the Agreement. An interpretation adopted by the CETA Trade Committee shall be

binding on a Tribunal established under this chapter. The CETA Trade Committee may decide that an interpretation shall have binding effect from a specific date.

Article x-35: The non-disputing Party to the Agreement

1. The respondent shall, within 30 days after receipt or promptly after any dispute concerning confidential or protected information has been resolved, deliver to the non-disputing Party:

a) a request for consultations referred to in Article x-18 (Consultations), a notice requesting a determination referred to in Article x-20 (Determination of the respondent for disputes with the European Union or its Member States), a claim referred to in Article x-22 (Submission of a Claim to Arbitration) and any other documents that are appended to such documents;

b) on request:

i. pleadings, memorials, briefs, requests and other submissions made to the tribunal by a disputing party;

ii. written submissions made to the tribunal pursuant to Article 4 (Submission by a third person) of the UNCITRAL Transparency Rules;

iii. minutes or transcripts of hearings of the tribunal, where available; and

iv. orders, awards and decisions of the tribunal.

c) on request and at the cost of the non-disputing Party, all or part of the evidence that has been tendered to the Tribunal unless publicly available.

2. The Tribunal shall accept or, after consultation with the disputing parties, may invite, oral or written submissions from the non-disputing Party regarding the interpretation of the Agreement. The non-disputing Party may attend a hearing held under this Section.

3. The tribunal shall not draw any inference from the absence of a submission pursuant to paragraphs 1 or 2.

4. The tribunal shall ensure that the disputing parties are given a reasonable opportunity to present their observations on a submission by the non-disputing Party to the Agreement.

Question 12: Appellate Mechanism and consistency of rulings

The Committee on Services and Investment shall provide a forum for the Parties to consult on issues related to this Section, including:

a) difficulties which may arise in the implementation of this chapter;

b) possible improvements of this chapter, in particular in the light of experience and developments in other international fora; and,

c) whether, and if so, under what conditions, an appellate mechanism could be created under the Agreement to review, on points of law, awards rendered by a tribunal under this Section, or whether awards rendered under this Section could be subject to such an appellate mechanism developed pursuant to other institutional arrangements. Such consultations shall take into account the following issues, among others:

i. the nature and composition of an appellate mechanism;

ii. the applicable scope and standard of review;

iii. transparency of proceedings of an appellate mechanism;

iv. the effect of decisions by an appellate mechanism;

v. the relationship of review by an appellate mechanism to the arbitration rules that may be selected under Article x-22 (Submission of a Claim to Arbitration); and

vi. the relationship of review by an appellate mechanism to domestic laws and international law on the enforcement of arbitral awards.

Possible draft provisions establishing an appellate mechanism

Article xx (Award)
Either disputing party may appeal the award to the Appellate Body within 90 days of the issuance of the award. In such an event, if the Appellate Body modifies or reverses the award of the Tribunal then the Tribunal shall, after hearing the disputing parties if appropriate, revise its award to reflect the findings of the Appellate Body. The Tribunal shall seek to issue its revised award within 90 days of receiving the report of the Appellate Body.

Article xx (Appellate review)
A standing Appellate Body is hereby established. The Appellate Body shall hear appeals on issues of law covered in the Tribunal's decision or award and legal interpretations developed by the Tribunal.