Insight

Primer: The Trans Pacific Partnership

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Introduction

After years of negotiations and weeks of anticipation, the final text of the Trans-Pacific Partnership (TPP) has been released.[1] TPP is a trade agreement between the United States, Japan, and ten other Pacific nations. These countries represent 40 percent of the world's Gross Domestic Product and, combined, would form the largest free trade area ever created.[2]

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Source: Forbes[3]

The Trade Promotion Authority, passed earlier this year, established guidelines for the passage of trade deals like TPP. These guidelines stipulate that an up or down vote from Congress cannot occur for at least 90 days after the President notifies Congress of his intention to sign the agreement[4], which he did on November 5, 2015. This gives the public and Congress ample time to analyze its contents in detail and determine its implications for the American economy.

Tariffs and Non-Tariff Barriers

The primary purpose of TPP is to eliminate barriers to trade. One such barrier, tariffs, drives up the cost of foreign goods in order to encourage the sale of goods manufactured at home. These taxes on imports make foreign goods and services more expensive, reducing trade and limiting competition. Expanding competition, however, is generally thought to lower prices, incentivize innovation in manufacturing, and encourage the creation of higher quality goods.

TPP eliminates or reduces all tariffs on goods traded between partner countries. Currently, tariffs imposed on U.S. exports are as high as 100 percent on goods and 700 percent on agriculture products. The TPP agreement would abolish many of these tariffs, translating into approximately 18,000 tax cuts on U.S. goods sold abroad.[5]

TPP also aims to increase trade in services. Services make up a substantial portion of U.S. trade, accounting for $711 billion of exports in 2014.[6] TPP expands market access in this area by prohibiting quantity restrictions on imported services, outlawing discrimination against foreign service providers, and encouraging the open exchange of services in all sectors.[7]

Electronic Commerce

TPP is the first trade agreement to establish guidelines concerning electronic commerce.[8] Specifically, it bans forced data localization laws, which mandate that firms place physical servers in areas where they would like to do online business. These laws place undue burdens on businesses and make cross-border data flows more expensive, restricting electronic commerce and hurting consumers.[9] TPP also prohibits customs duties, another form of import taxes, on electronic transmissions and includes several provisions to facilitate paperless trading. These features all aim to encourage e-commerce as a growing method of international trade.

The agreement is also the first to specifically sets guidelines for the trade of digital products. Namely, it establishes a free market for digital goods by outlawing trade discrimination against them.[10] Digital goods include software, mobile apps, online games, or any other products that are shipped electronically.

Biologics

Biologics, a relatively new form of medicine made up of living cells, are among the fastest growing pharmaceuticals on the market. Some suggest that biologics will comprise 32 percent of major pharmaceutical sales by 2023.[11] While these drugs may be a life-saving breakthrough in medical science, they can also be very expensive: the yearly costs of commonly used biological drugs can range from over $20,000 to $200,000.[12]

TPP provides manufacturers of biologics in the Asian-Pacific region with at least five to eight years of data exclusivity before competitors can enter the market with their own non-innovator versions, called biosimilars. This would be the first time that some countries, like Mexico, have data protections for biologics. U.S. law, which currently guarantees 12 years of exclusivity, would not be changed. [13]

This provision has raised serious concerns among biologic manufacturers as to their ability to recover upfront investments before biosimilars enter the market. PhRMA, a representative of the pharmaceutical industry, issued a statement denouncing TPP for its lack of data protection. The group suggests that strong intellectual property laws are essential to freely encourage innovation.[14] Some, however, argue that without the market entrance of lower-priced biosimilars, the poorest consumers would be hurt most.[15] AAF research found that this is not necessarily the case: the complexity of biologics prevents biosimilars from achieving the same cost savings previously seen in the case of traditional small molecule generics.[16]

Agriculture

U.S. agriculture is likely to be a primary beneficiary of the agreement, as 85 percent of U.S. agricultural exports are currently sold to TPP nations.[17] The deal would boost agricultural trade even further by significantly lowering tariffs and opening up nations like Japan, New Zealand, and Malaysia to competition in agricultural trade. For instance, taxes would be immediately removed on over half of our agricultural exports to Japan and on over 90 percent of exports to Malaysia and New Zealand.[18] And for many agricultural products, tariff-rate quotas (TRQ) would be either newly established or increased, allowing more U.S. products to be imported tariff-free by our TPP partner countries.

Rice is a prime example. Currently, U.S. rice exports to Japan face significant market access barriers with tariffs as high as 800 percent.[19] TPP would immediately establish a new country-specific quota (CSQ) for tariff-free U.S. rice exports starting at 50,000 tons and rising to 70,000 tons over 13 years.[20] However, some U.S. rice growers are apprehensive about the consequences of eliminating tariffs, especially as it pertains to our trade with Mexico.[21] While low transportation costs have historically made Mexico our largest destination for rice exports, TPP could even the playing field for other rice-producing nations and lower Mexico's dependence on U.S. rice.

A more controversial consequence of TPP on agricultural trade involves the Canadian dairy supply management system. In order to stabilize dairy prices and prevent overproduction, Canadian farmers are limited in the amount of dairy they can produce. Similarly, to prevent foreign competition from bringing down dairy prices, Canada restricts dairy imports through a quota system. By giving exporters new access to 3.25 percent of the Canadian dairy market, TPP expands competition and may put downward pressure on Canadian dairy prices.[22]

Rules of Origin

Rules of origin dictate that goods manufactured within TPP nations can qualify for tariff benefits. With today's supply chains expanding across borders, these rules are made to incentivize domestic production. In addition to goods that are wholly produced or grown in TPP nations, the agreement also contains product-specific rules for goods requiring complex production processes. For example, 45 percent of vehicles and 35 to 45 percent of auto parts must be manufactured within TPP borders in order to be eligible for reduced tariffs.[23]

The Mexican auto industry has criticized TPP's rules of origin provisions for being weaker than in the North American Free Trade Agreement, which requires over 60 percent of automobiles and auto parts to be manufactured within the partner countries' borders.[24] Advocates instead suggest that these rules, combined with reduced trade barriers, will spur domestic manufacturing and benefit the auto industry.[25]

Labor

TPP includes the strongest labor and human rights protections of any trade agreement in history. For instance, it mandates that all TPP nations give workers the right to organize into unions and collectively bargain. It also completely eliminates forced and child labor and requires partner countries to have laws concerning minimum wages, hours of work, and occupational safety.[26] Furthermore, the U.S. made three separate agreements with countries that are especially lacking in labor standards: Malaysia agreed to implement significant reforms to combat human trafficking, and both Brunei and Communist Vietnam pledged to allow the full freedom of union activity.

TPP provides partner countries the right to institute trade sanctions against any nation that does not comply with these labor laws. Critics argue that these standards are unrealistic and fear TPP countries will continue to exploit labor to drive down the costs of manufacturing.[27] AFL-CIO, the largest federation of American unions, has come out against TPP, citing inadequate ways to enforce the standards.[28] Others criticize TPP's labor rules for the opposite reason: in countries that have never before implemented basic labor standards, drastically raising the cost of labor could harm their domestic economies and trade.[29]

Intellectual Property and Copyright Protections

TPP includes strong intellectual property (IP) standards to freely encourage innovation in production. It also extends copyright protections to cover the lifespan of a creator and 70 years after a creator's death. Penalties for breaking these provisions are severe: stealing trade secrets or pirating copyrighted goods is considered a criminal offense. Critics worry that these penalties carry dangerous implications for whistleblowers and online consumers.[30]

One of the more controversial aspects of TPP's IP protections concerns "fair use" exemptions to copyright law. These exemptions allow the limited use of copyrighted material, which is frequently utilized by online users who engage in research, commentary, and criticism.[31] Opponents condemn TPP for not including mandatory fair use exemptions, even though the deal does not explicitly outlaw them.[32] Others warn against exceptions and limitations to copyright protection. They suggest that mandating a one-size-fits-all fair use policy would be harmful to nations with different legal systems and in different stages of technological development.[33]

Network Neutrality

There is no true consensus on the definition of network neutrality or what it means in practice. Generally, it can refer to the notion that network providers should not restrict access or interfere with the speed of data as it travels to consumers.[34] TPP clearly promotes this concept by recognizing the benefits of open access to internet and telecommunication services across nations.[35] However, it does not mandate network neutrality among TPP nations.

Critics oppose TPP's weak language on neutrality. Instead of simply acknowledging the benefits, they demand that it be an obligation among trading partners. [36] While many support global network neutrality rules, they may be practically difficult to implement. Telecommunications officials caution that new regulations would negatively affect the quality of their service and discourage innovation.[37]

Investor-State Dispute Settlement

Investor-state dispute settlement (ISDS), as outlined in TPP, refers to a procedure by which private companies can sue foreign governments over discrimination, seizure of private property, or other wrongful acts. By utilizing ISDS, TPP participants can more quickly resolve their issues through mediation. However, some have asserted that ISDS is biased toward larger corporations at the expense of U.S. law: if the U.S. enacts a policy that is unfavorable to a foreign company's bottom line, ISDS would enable that company to take legal action against the U.S. outside of our court system.[38]

Others have voiced concerns that ISDS does not go far enough. TPP specifically excludes tobacco companies from participating in ISDS, which means that the tobacco industry would be prohibited from suing TPP nations that institute anti-smoking regulations. Several members of Congress have denounced this provision as harmful to U.S. tobacco growers. They also worry that the exemption may lead to other sectors being excluded from ISDS in the future.[39]

Currency Manipulation

Currency Manipulation occurs when a nation's central bank devalues its currency relative to the rest of the world by lowering the price of its goods and spurring export growth. Critics view this practice as an unfair scheme to boost exports and condemn TPP for not explicitly outlawing it.[40] Instead of including rules against manipulation in the agreement itself, TPP central bankers negotiated a side deal: a joint declaration in which all participating nations pledged to refrain from currency manipulation for competitive gain.[41]

This declaration aims to increase transparency in the crafting of monetary policy. It obligates TPP nations to publically report current and future exchange rates as well as quarterly reports on exports and imports. It also creates a group of "Macroeconomic Officials" from each TPP nation that will meet annually, giving TPP nations an opportunity to challenge any practices they deem unfair. However, the side deal does not outline any clear penalties against currency manipulation, which has been a major point of criticism.[42]

The auto industry has voiced strong objections to this point. U.S. auto manufacturing is the largest exporter in the country, with auto exports reaching record highs for each of the past three years.[43] Because of their dependence on exports, auto manufacturers are also disproportionately damaged by international currency manipulation. Ford motors recently slammed the trade deal for not including laws against devaluation.[44] Furthermore, the American Automotive Policy Council introduced its own proposal that would outlaw nations from manipulating their currencies and reverse the tariff benefits for any nations that do.[45]

Conclusion

TPP would radically transform U.S. trade in the Asian-Pacific. As a product of seven years of negotiations between 12 independent nations, the final deal is undoubtedly complex. While TPP may not have universal support in its current form, terms of the deal are not set in stone. TPP establishes a commission of senior officials who would regularly evaluate the agreement's economic impacts and meet to propose reforms.[46] It does, however, present a historic opportunity for the U.S. to join in free trade with some of the fastest growing economies in the world.[47]

It is now up to Congress to decide if the trade boost generated from TPP's tariff benefits outweigh its possible costs.

[1] https://ustr.gov/trade-agreements/free-trade-agreements/trans-pacific-partnership/tpp-full-text