Transatlantic trade and investment partnership – significance for the Baltic Sea region.

Author: Paweł Świeboda[1]

Transatlantic Trade and Investment Partnership will further improve conditions for US investment in Europe. It will bring better protection on the one hand and transparency on the other. The level-playing field across EU member states will translate into greater competition in attracting US investment. US investors will look for market size but also for niche competences which are a strong asset of the Baltic Sea region.

Transatlantic economies have hardly seen any economic growth since the beginning of the crisis in 2008 while China has grown 70 percent. This makes the economic case for the Transatlantic Trade and Investment Partnership (TTIP) overwhelming. The size of the EU economy is meant to be boosted by 120 bln euros, equal to 0.5 percent of GDP and the US economy will grow by 95 bln euros or 0.4 percent of GDP[2]. The objective of TTIP is to create 10 million of new jobs in an open transatlantic market by 2020. The trade part of the agreement is beyond everything which has recently been negotiated. The removal of tariff bariers alone is estimated to have the value of five times the US – South Korea agreement while the removal of non-tariff barriers is projected to bring three times as much for the US and the EU as the completion of the Doha Round[3].

Given the high level of interdependence of the US and the EU, all the low-hanging fruits have already been collected. For this reason, the intention is for TTIP to be more holistic and dynamic than traditional FTAs, covering trade in goods and services as well as investment provisions in a fashion which will make them amenable to up-dates in the future.

Expectations around the transatlantic partnership are enormous. A number of experts and officials have coined the term "economic NATO" to reflect the significance of the initiative. Commission officials stress that the nature of the agreement is commercial, rather than strategic. It is the balance in trade volumes that will decide the overall deal. The important context of the agreement is the growing integration of production and value chains. This means it will not be

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[1] Author is President of demosEUROPA – Centre for European Strategy (www.demoseuropa.eu) in Warsaw.
[2] "Transatlantic Trade and Investment Partnership. The Economic Analysis Explained.", European Commission, September 2013.
[3] Dan Hamilton and Tim Oliver, written evidence to the House of Commons.

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possible to use the TTIP agreement as a containment policy for the emerging powers, especially China. Brussels remains skeptical about the very idea of engaging in an exercise which could have protectionist undertones. Instead, TTIP is often seen as being about consolidating at home in order to reengage internationally.

TTIP is not the only trade agreement being pursued at the moment. The international context will have an important bearing on the pace and quality of the eventual package. This has to do with the slowly evolving multilateral framework, for which the autumn 2013 WTO deal in Dali is significant but does not compare in qualitative terms to what is envisaged as part of TTIP. Progress in Trans-Pacific Partnership (TPP) discussions as well as other agreements being pursued at the moment, such as the Alleanza Pacifico, will also feed into the dynamics of the transatlantic negotiations. The United States is likely to be open to the accession of China to TPP once the agreement is negotiated. This would run the risk of tipping the balance back in favour of the Pacific.

The level of ambition of TTIP

TTIP negotiations extend to the issues of:

a) market access and elimination of all duties on industrial and agricultural goods;
b) liberalisation of services where the agreement would both open the remaining services markets and create a better cooperation framework between regulators; barriers to competition which persist at the federal level would also be addressed both in the US and in Europe as protected service sectors on both sides of the Atlantic account for about 20 percent of the combined transatlantic GDP;
c) openning the public procurement market and getting as close as possible to national treatment at all levels of government;
d) regulatory cooperation where the agreement is envisaged to include a mechanism for addressing regulatory differences in order to reduce additional costs for companies;
e) establishing global rules in areas such as competition, labour, environment, trade facilitation and intellectual property.

The newly established methodology for analysing global value chains has shown strong interlinkages between trade in goods and trade in sevices. OECD analysis has revealed that tariffs on goods strongly affect also service suppliers. In 2009, over 30 percent of the total collected tarrifs were paid on service value. This means that service suppliers „appear to incur a substantive share of tariff costs in all manufacturing sectors and in countries at various levels of development“[4]. As a result, removing the remaining tariffs will have a broader significance.

[4] "S. Miroudot, D. Rouzet, F. Spinelli, "Trade Policy Implications of Global Value Chains", OECD Trade Policy Papers No. 161, 2013

TTIP will serve the transatlantic innovation economy by encouraging flows in research and development in sectors such as biotechnology and nanotechnology. Including energy in the agreement will be challenging. The international norms on the trade of energy resources and raw materials are limited and need developing. As a result of revolutionary changes in the production of unconventional gas, the US can reach energy independence by 2035. Inexpensive energy is spurring the onshoring of US industry - low energy prices lead to a degree of "re-industrialisation" in the chemical, steel, aluminium, tire and plastics industries. This will make the EU more interested in pressing for the inclusion of energy in the overall package.

Regulatory convergence will be about identifying and removing incompatibilities between systems as well as unintended discrepancies in areas where objectives on both sides of the Atlantic are the same. The idea is to agree the norms bilaterally and then export them multialterally.

When it comes to rules which will have an impact on third countries, the intention is to develop a global rule-book which, given the sheer weight of the transatlantic agreement, will be picked up by third countries. TTIP is about the transatlantic community creating a critical mass of norms and values to enable it to have a decisive say in how the global trade norms are being set. Issues of transparency, market access and export restrictions are areas to be developed in that context. In spite of the scepticism of some studies on the subject, economic benefits for third countries are expected to be significant. The expectation in Brussels is that this will encourage developing countries to re-engage in the multilateral framework.

Reaching agreement on TTIP will be challenging and many obstacles will need to be overcome. A number of interest groups in both the EU and the US will revert to their traditional skepticism about the deal. Questions of information-sharing as well positions of the various industrial sectors will be important, especially given that some sectors will gain and some will lose from TTIP. One example of a possible obstacle is that of the lactic acid which is used widely in the US as a decontaminant for beef carcasses while in the EU only water can be used for the purpose. The US has traditionally viewed the latter as a trade barrier. However, after evidence was presented by the US Department of Agriculture in December 2010 to the European Food Safety Authority, the EU agreed that lacid acid poses no threat to human health or the environment. The European Commission started to relax the relevant regulation but several member states, including France, have been opposed. This shows the scale of the difficulty in reaching any future transatlantic agreement in the field of agriculture.

The EU has viewed some US regulations as protectionist as well. This included the restriction placed by the Jones Act from 1920 on cargo services between US ports to be limited to ships registered and built in the US, owned by an American firm and manned by US nationals. Grounds for the Act are those of national security and the prerogative is that of protecting the military sealift capability of the US as well as maintaining a viable workforce of trained Americans for dealing with possible emergencies. Having said this the organised form of opposition to

TTIP can be found in Europe, rather than in the United States. The challenge on the US side will come primarily with the ratification of the agreement given the anti-trade sentiments which prevail in the Democratic Party.

It is by now clear that the initial objective of concluding TTIP within an ambitious time-frame will not materialise. The European Commission had hoped to complete the negotiations before elections to the European Parliament in May 2014 and the end of its current term. Similarly, Michael Froman, the US Trade Representative, had called for the agreement to be concluded "on one tank of gas". This is now clearly out of reach. Progress in the future will depend on the political dynamic in the capitals and the determination of the new European Commission to conclude the process. If the Comprehensive Economic and Trade Agreement between Canada and the EU is to be a point of reference, it took five years to negotiate before they were in principle concluded late last year.

Role of investment measures in TTIP

TTIP is about both trade and investment. The objective is to eliminate bilateral investment barriers, align bilateral investment competences and identify common approaches to restrictions on investment in third countries. Transatlantic economic relations are today driven more by investment flows than by trade which makes investment rules all the more significant. In fact, the dynamic between the two is such that companies often prefer to invest rather than trade if they have a clear choice.

The numbers show clearly that investment is to an equal extent the driver of the transatlantic economy. As Dan Hamilton points out, "there is more European investment in a single US state such as Indiana or Georgia than all US investment in China, Japan and India combined". Looking at the flow of investment from the US to Europe, the volume invested in the UK over the past 12 years was more than 11 times higher than the US investment in China. "Since 2000, US firms have invested more in the UK alone than in South and Central America, the Middle East, and Africa combined"[5]. This explains the inclusion of the investment-related provisions in the TTIP agreement which is in line with the international trend of integrating investment rules in FTAs.

The EU and the US have a shared objective of promoting open, transparent and non-discriminatory investment policies globally. The basis for that is the Shared Principles for International Investment agreed in April 2012. They include ensuring a level-playing field and open competition, non-discriminatory investment climates, fair and binding dispute settlement, robust transparency and public procurement rules or responsible buisness conduct. The transatlantic agreement on investment needs to take into account a number of global trends which include:

- the tenfold increase of the global stock of FDI since 1990,

[5] Dan Hamilton and Tim Oliver, written evidence to the House of Commons.

- dynamic growth of the FDI stock in China (thirty-five-fold since 1990) and an increasing inflow of Chinese investment into the EU and the US,
- multiplication of bilateral and regional investment agreements with guarantees for foreign investors' legal protections such as property protection, litigation possibility, fair competition.

Shared principles for investment are important also from the point of view of ensuring investor protection in dealings with third countries and edging towards harmonisation of rules globally. Given that both the EU and the US intend to negotiate bilateral investment treaties with China, the commonality of view worked out among them can help ensure eventual equal treatment of their companies on the Chinese market.

Negotiations on the issue will be more complex given the fact that the Treaty of Lisbon shifted competences on investment to the level of the European Union. The challenge this poses has to do with both managing the existing BITs and establishing a European investment policy which confirms the Union's openness to FDI inflows while protecting its economic interests. The European Parliament has demanded to be "adequately involved in the shaping of the future investment policy" and consulted on mandates for upcoming negotiations as well as briefed on the state of ongoing negotiations[6].

There has been much debate about the EU investment policy since the entry into force of the Treaty of Lisbon. In its 2011 report on the issue, the European Parliament has called for future investment agreements concluded by the EU to be based on the best practices from the member states and to extend to the following standards:

- non-discrimination (national treatment and most favoured nation), with the definition mentioning that foreign and national investors must operate "in like circumstances",
- fair and equitable treatment,
- protection against direct and indirect expropriation, with a definition establishing a "clear and fair balance between public welfare objectives and private interests"[7].

The European Parliament has already made clear that it would play an important role in the TTIP process. In a statement on 21 January 2014, the Socialists and Democrats in the European Parliament said that they want the Investor-State Dispute Settlement (ISDS) mechanism removed from the TTIP package. In their opinion, the ISDS "would mean opening the door for big corporations to enforce their interests against EU legislation" and "this would deprive states of crucial policy space in important fields such as health or environment"[8]. Some MEPs

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[6] Report on the future European international investment policy (2010/2203(INI), Committee on International Trade, European Parliament, 22 March 2011, page 5/22,

[7] *ibid*, page 7/22,

[8] Full text of the statement can be found on:

have also expressed a concern that such arrangements would make privatisations irreversible.

The new investment rules have been openly questioned by a number of European NGOs and MEPs. Their concern is that the governments' hands could be tied in the face of powerful US corporations. The particular concern, as in the case of some MEPs, has been voiced over TTIP's mechanism for legal disputes, the ISDS.

Ten European health, transparency and environment NGOs have written to the European Commission[9] expressing their concern about the lowering of the bar when a "level playing field" is created between the US and Europe. Their fear is that even the EU's "precautionary principle", which underpins significant parts of the EU regulatory regime, might be at risk. In other words, the EU could be forced to accept US standards which tend to be lower than in the US. However, the real concern is that American and multinational investors would have an opportunity to sue EU member states in cases when new environmental or health legislation is introduced. Precedence exists for this in other investment arrangements. Philip Morris was sued the Australian government over the packaging rules for cigarettes. The basis for the case was an ISDS contained in the Australia-Hong Kong bilateral investment treaty.

Additional concerns with respect to the ISDS mechanism have to do with the fact that member states may be afraid to work towards higher social and environmental standards should this upset trading partners. For the Baltic Sea region, this is of particular importance, given its much valued role as a standard-setter with respect to public policies on energy and climate, water, nature protection, food quality, chemicals. The operation of the arbitration panels in potential disputes is also likely to be costly to member states in case substantial fines are levied to compensate for loss of profit. The smaller among the Baltic states could be particularly unfavourably affected in a situation like this.

The need for an Investor State Dispute Settlement in TTIP is questioned in the context of the advanced judicial systems in Europe and in the United States. ISDS tribunals are criticised as unaccountable. The fall-back option could be for ISDS tribunals to become instances of last resort, used only when local judicial remedies are exhausted. This is what the European Parliament asked for in its 2011 report. The value added of the envisaged mechanism, as compared to the individual BITs, lies in improved transparency in the course of the arbitration process. In addition, independence of arbitrators can be guaranteed and a code

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http://www.socialistsanddemocrats.eu/newsroom/sds-want-investor-state-dispute-mechanism-out-eu-us-trade-and-investment-agreement-ttip

[9] Full text of the letter can be found on: http://www.euractiv.com/trade/ttip-puts-eus-environmental-soci-analysis-532724?utm_source=RSS_Feed&utm_medium=RSS&utm_campaign=EurActivRSS

of conduct drafted in the framework of the treaty. In the Comprehensive Economic and Trade Agreement (CETA) between the EU and Canada, decision was made as well to create a Committee on Services and Investment to oversee the arbitration process. Another significant innovation would be to create an appellate process.

In January 2014, the European Commission announced it would consult on the TTIP package to address the concerns that the level of social protection in Europe could be undermined. A three-month public consultation on the proposed investment rules for firms has been announced. The EU trade commissioner Karel de Gucht said "governments must always be free to regulate so they can protect people and the environment". "But they must also find the right balance and treat investors fairly, so they can attract investment... Some existing arrangements have caused problems in practice, allowing companies to exploit loopholes where the legal text has been vague."[10]

When the Treaty of Lisbon granted the European Union jurisdiction over foreign direct investment, it was hoped that this would create a window of opportunity for a more systemic approach to investment treaties in Europe, overcoming the complexity which results from the fact that member states are party to about 1200 bilateral investment treaties (BITs). The testing ground is the CETA agreement negotiated with Canada. Although initially conceived as a trade agreement, its scope was extended in September 2011 to include an investment chapter.

If we use the CETA language as the yardstick, it uses a broad definition of investment, covering assets of both existing and new enterprises in the host state, including in the pre-establishment phase when an investor is only seeking to invest. Enterprises without substantial buiness activities in the home state have been excluded to avoid misuse by „mailbox" investors. There are extensive market access commitments in CETA, prohibiting a range of measures which regulate entry. The use of a negative list with areas where market access is not granted is new for the EU. This approach has been criticised as more difficult to establish and less predictable.

One other issue which might be addressed in the context of TTIP is the prohibition of performance requirements. Included in NAFTA but absent from EU treaties so far, this provision can potentially have an effect on countries' ability to use economic policy tools. An obligation to provide national and most-favoured nation treatment will strengthen non-discriminatory treatment but also limit the ability of the EU and the US to regulate foreign investment in the entry and pre-entry phase.

There is an open question over the ability of investors to import provisions from other investment treaties. Should this be allowed, it would carry the risk of

[10] http://www.bbc.co.uk/news/world-europe-25829604

foregoing much of the comprehensive character that TTIP has promised to deliver.

As far as investment protection is concerned, TTIP can also be expected to contain a provision to accord fair and equitable treatment (FET) to investors. There are two possible approaches to FET – envisaging either an open or a closed list of situations which would amount to a breach of FET, such as targeted discrimination or manifest arbitrariness. In the context of CETA, another solution was taken up in which a closed list was the starting point but it was accompanied by a flexibility mechanism foreseeing regular discussions about the content of FET.

Further protection could be provided by inclusion of the so-called „umbrella clause“ which enables investors to claim a breach of contract to be a violation of the treaty. This could lead to the proliferation of arbitration claims.

As far as expropriations are concerned, the discussion is likely to be over the extent of exclusion of public welfare regulations from indirect expropriation. The tribunals' ability to interpret what amounts to expropriation depends on the treaty language to be eventually agreed. Discussion over the general exceptions clause will be about its future scope - in the narrow version it is likely to include protection of human, animal or plant life and conservation of natural resources while in the broader version it will have to do with protecting public security and public order.

US investment in the Baltic Sea region

The US has had a strong and relatively steady investment presence in the Baltic Sea region in the period since 2009. In terms of volume of investment, Germany is in a category of its own, with the US direct investment position standing at 121 bln USD in 2012, followed by Sweden with 24.5 bln USD, Denmark with 15 bln USD and Poland with 14 bln USD. Finland as well Lithuania, Latvia and Estonia have seen considerably less US investment.

The evolution of US investment in the region in the years 2009-2012 is presented in the table below:

	Denmark	Estonia	Germany	Finland	Latvia	Lithuania	Poland	Sweden
2009	13053	D	110149	1659	9	D	13412	36702
2010	11802	D	103319	1597	2	D	13152	23275
2011	15019	60	111088	2184	-3	D	13446	24827
2012	15092	58	121184	2013	13	D	14178	24532

D=supressed to avoid disclosure of data of individual companies
Direct investment position on a historical-cost basis 2009-2012

Source: US Department of Commerce

In the case of Germany, the nature of US investment is the most balanced with a relatively extensive spread across all categories[11] with 4.861 bln USD invested in chemicals by 2012, 2.354 bln USD in primary and fabricated metals, 5.005 bln USD in machinery, 8.375 bln USD in computers and electronic products, 4.623 bln USD in transportation equipment, 11.970 bln USD in wholesale trade, 19.474 bln USD in finance and insurance, 5.087 bln USD in professional, scientific and technical services and 30.479 bln USD in holding companies.

A similarly balanced spread, although at substantially lower volumes, can also be observed in the case of Denmark and Poland. When it comes to Denmark, holding companies take the largest chunk of US investment at 5.883 bln USD, followed by computers and electronic products at 1.484 bln USD, other manufacturing at 1.439 bln USD, wholesale trade at 1.433 bln USD and information at 1.310 bln USD.

In the case of Poland, food industry, transportation equipment, finance and insurance and wholesale trade tend to be especially prominent. US firms have invested 1.611 bln USD in the food industry, 0.711 bln USD in chemicals, 1.183 bln USD in transportation equipment, 2.138 bln USD in wholesale trade, 1.777 bln USD in finance and insurance as well as 0.322 in professional scientific and technical services.

Finance and insurance is the dominant field in the case of US investment in Sweden with 12.810 bln USD invested in the area. Wholesale trade takes second place with 1.692 bln USD, followed by food at 1.274 bln USD, information at 1.256 bln USD and holding companies at 1.079 bln USD.

In Finland, the largest individual segment is machinery at 0.463 bln USD, followed by professional, scientific and technical services at 0.419 bln USD and wholesale trade at 0.282 bln USD.

Investment in Lithuania is modest enough for data not to be available as it would concern individual companies. In Latvia, the figure of 0.013 bln USD invested is similarly insignificant while out of the 0.058 bln USD invested in Estonia, about half has been invested in mininig and the other half in electrical equipment, appliances and components.

Apart from divergent sectorial focus of US investment in the Baltic Sea region, there are also different incentives which are being used to attract new and maintain existing capital engagement. Apart from a traditional range of instruments, some countries in the region are successfully building on their unique strengths and characteristics such as advanced low carbon policies. An illustrative example is the flagship investment project is Facebook's data centre

[11] All data for the different categories of investment is for 2012; source: US Department of Commerce.

in Luleå, flagged as ten times the size of the largest pre-existing data centre in Sweden. Facebook's decision was said to be based on the fact that Luleå offered the best package of resources including a suitable climate for environmental cooling, clean power resources, available land, a talented regional workforce and a supportive business and corporate environment[12]. Access to renewable energy and the cold climate that is crucial for cooling the servers were seen as crucial factors. "It is our first data centre to draw its power primarily from renewables, and it features design evolutions like a 70% reduction in our reliance on backup generators.[13]"

This example shows that lowering companies' environmental footprint can be one of the new arguments in favour of investing in the Baltic Sea region.

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[12] http://www.government.se/sb/d/17748/nocache/true/a/222417/dictionary/true

[13] "Facebook builds "green" datacentre in Sweden", The Guardian, 27 October 2011