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The EU's new-generation trade agreements: the CETA treaty

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Against an international background of low tariff barriers, the EU's trade policy has shifted towards attaining bilateral trade agreements that promote the reduction both of non-tariff barriers and of those regulatory barriers that restrict the movement of goods, services, individuals and investment flows, in addition to including provisions relating to the environment, labour markets and intellectual property rights. An example of these "new-generation" agreements is the Comprehensive Economic and Trade Agreement (CETA) recently negotiated by the EU and Canada, which is in the process of being ratified by the national parliaments. The article describes the general characteristics of new-generation trade agreements, the difficulties posed by their regulatory and wide-ranging nature, and how the CETA has attempted to respond to some of the issues that have proven most controversial for public opinion. The significance of this agreement pertains not only to the economic impact it will have on the European and Canadian economies, but also to how it could act as a model for other agreements with developed countries, including that which the EU and the United Kingdom have to negotiate.

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Introduction

International trade has been a major source of economic growth in recent decades, both for the more developed economies and for emerging countries. Its dynamism was boosted by the multilateral trade negotiations that took place in the Uruguay Round (1986-93), under the aegis of the World Trade Organization (WTO). However, following the failure of the Doha Round, which began in 2001, progress towards multilateral integration was checked and, in the wake of the international financial crisis, an increase in protectionism has even become discernible [Global Trade Alert and WTO (2017)], which may also have contributed to the sluggishness of trade in recent years [Constantinescu, Mattoo and Ruta (2015)].[1]

Against this background, the European Union (EU) has pursued an active trade policy, negotiating "new-generation" bilateral and regional agreements which go beyond the reduction or elimination of conventional tariff barriers.[2] These include most notably the Transatlantic Trade and Investment Partnership (TTIP) with the United States which, after 15 rounds of negotiation, is currently at an impasse following the new US administration's change of tack. Greater headway has been made with the EU-Canada Comprehensive Economic and Trade Agreement (CETA), which stands as a reference point for this type of agreement, although it will have a lower economic impact given the lesser intensity of trade with Canada. Moreover, bilateral trade negotiations are being held with Japan, Vietnam, Singapore and Korea, and an investment agreement with China.

The CETA is an ambitious EU trade pact which, along with creating a free trade area for industrial and agricultural products, seeks to minimise non-tariff and regulatory barriers that hamper trade in goods and services and investment flows. The agreement also includes prescriptions relating to intellectual property rights, access to public procurement processes and a new investor-State dispute-settlement mechanism. In this respect, the CETA will be a benchmark with a view to future agreements with other developed countries and, in particular, in the context of the negotiation of the new legal framework for relations between the United Kingdom and the EU following Brexit.

The following section analyses the contents of the CETA and describes the complexity and most controversial elements of this and other "new-generation" agreements that the EU is currently negotiating with different economies. The last section discusses the possible implications of this agreement for the Spanish economy.

Main features of the CETA

LEGAL STATUS

The CETA was approved on 15 February 2017 by the European Parliament, along with the EU-Canada Strategic Partnership Agreement (SPA) which complements it and which extends bilateral cooperation between both regions to a broad range of non-trade matters

1 This rise in protectionism has come about against a backdrop of growing evidence on the inequality with which the gains associated with increased trade are being distributed. That points to the need to design measures that soften the possible effects globalisation may have exerted on specific groups [Autor, Dorn and Hanson (2013), OECD (2011) and European Commission (2017)].

2 The greater scope of trade agreements has been widespread, as attested to in the database compiled by the World Bank: http://data.worldbank.org/data-catalog/deep-trade-agreements.

(foreign and security policy, combating terrorism and organised crime, sustainable development, research and culture).

Its start-up requires the EU Member States to complete ratification in keeping with their respective constitutional rules (to date it has only been ratified by Spain, Latvia and Denmark). This is so because although the EU has been acknowledged to have the specific competence to negotiate trade and investment agreements on behalf of its members, treaties such as the CETA cover a broad spectrum of issues that comprise what are known as “mixed” or “shared competence” agreements whose approval requires they be signed both by the EU institutions and by the Member States. And in the case of decentralised economies, such as Canada or Belgium (where the treaty was on the point of being rejected in the Walloon region), the approval of the regional governments is also required, as aspects under their remit are negotiated.[3] In this respect, the lengthiness of the CETA negotiation process, the requirement of unanimity in the Council in relation to this type of international agreement (Art. 218.8 TFEU) and the particularities of the different national ratification processes may be indicative of the difficulties that defining the even more complex framework of relations between the EU and the United Kingdom will pose.

However, there would be potential scope for applying the agreement provisionally by means of a Decision by the EU Council, once approval by the Canadian judicial authorities is complete. In any event, any provisional application of the CETA would not cover the provisions of the agreement whereby a new dispute-settlement arrangement is laid down for States and investors in respect of investment, the implementation of which will not be effective until national ratification procedures have concluded.

From a legal standpoint, it should be stressed that the CETA does not amend EU legislation, so all imports from Canada must continue to comply with EU regulations and vice versa (e.g. technical standards and rules on products, health and phytosanitary regulations, rules on foodstuffs and transgenics, regulations on health and safety, environmental protection and consumer safeguards).[4] Along these same lines, the CETA retains the capacity of the EU, of its Member States and also of Canada to adopt and apply their own legislation and regulations on economic activity in the public interest.

CONTENTS

As earlier mentioned, the CETA is the most ambitious treaty signed by the EU to date, encompassing as it does a broad spectrum of measures relating to entry barriers to product markets, investment and public sector procurement and purchases usually not open to foreign companies, along with provisions on other aspects relating to intellectual property rights, labour mobility, etc.

More specifically, in relation to lifting customs duties, the CETA eliminates 99% of tariffs on trade in industrial products between the EU and Canada as from the treaty’s entry into force. Fish and agricultural products are subject to a gradual lowering of tariff barriers over a period of seven years; in the case of agriculture, the quotas on specific sensitive products are

3 For example, in the specific case of the CETA, it proved particularly complex to reach an agreement on access to regional government public procurement processes [Fafard and Leblond (2012)].

4 Although Canada is a country with high standards in respect of labour and environmental regulations and rights, concern over the possibility that such a wide-ranging treaty might affect European rights and legislation led both parties to sign an “interpretative instrument”, with the status of law, which provides guarantees on all these issues. Further, the principles governing the establishment of the dispute-settlement courts between investors and States are reiterated.

retained and, indeed, some are excluded from the liberalisation commitments.[5] Moreover, to ensure preferential tariff treatment, the rules of origin are simplified so that it will suffice for exporters to provide a document enabling the product of origin to be identified.

But the feature differentiating treaties such as the CETA from previous trade negotiations is that it is sought thereby to reduce not only conventional tariff barriers but also regulatory and administrative barriers, which at present place a much stronger brake on trade. It is precisely the regulatory nature of this type of agreement that makes the negotiation thereof more complex and raises controversy among certain economic agents. Generally, the elimination of such barriers is normally carried out through the mutual recognition of regulations establishing minimum quality standards and the technical, health and phytosanitary requirements that products must meet.

In this respect, it should be borne in mind that on many occasions the discernible differences in countries' regulations reflect different preferences in important areas such as food safety or the environment, and this can be seen in aspects ranging from labelling rules to the regulations covering vehicle CO_2 emissions. For example, in the case of Europe, the United States and Canada there are key differences in food safety arrangements which mean that in Europe it is necessary to demonstrate that a product is apt for consumption, whereas in the United States it is considered apt unless proven otherwise. Accordingly, the European Commission has undertaken to work with consumer associations so that no trade agreements should detract to any extent from consumer protection; in practice, the most sensitive products in respect of the general public, such as transgenics, are usually left out of negotiations [European Commission (2015)].

As regards the provision of services, the EU has for the first time adopted an approach under which, by default, all products not expressly excluded from an agreement (a "negative list") are liberalised, as was the case with the NAFTA negotiations, which in principle leads to greater liberalisation. Hence, sectors such as maritime transport, telecommunications and others related to the environment, both at the federal level and, for the first time, provincial level in the case of Canada, are being opened up. Moreover, the CETA provides a framework for the readier international provision of professional services since qualifications and training in such professions are mutually recognised. It also includes provisions making it easier for companies to temporarily assign staff from one side of the Atlantic to the other.

With regard to public procurement, the possibility of supplying goods and services is mutually opened up to the EU and Canadian governments, and, what is more significant, to any level of government, including for the first time the provincial/regional governments, which are responsible for a large share of public spending. Only certain State monopolies and rights to the supply of public services (such as waste management or public transport) are excluded, along with other specific services it is wished to retain in the public sphere, such as education, health care and water supply.

Investment is a very significant chapter, since Canada is among the advanced economies which, according to OECD indicators, still has the greatest restrictions on foreign direct investment. One of the biggest barriers here is the Investment Canada Act, which requires investments of a certain size to have prior authorisation. In this respect, the agreement reduces substantially the types of investment by EU companies that require authorisation.

5 The CETA restricts preferential access to fixed quotas on beef and pork and on sweet corn by the EU, and on milk products by Canada, while the market for poultry and eggs remains under the restrictions in place prior to the agreement.

Turning to intellectual property rights, the CETA raises the levels of protection relative to those agreed upon under the aegis of the WTO. The EU has, for example, managed to make Canada adopt greater levels of protection than it previously had in respect of industrial property in the pharmaceutical arena.[6] Canada has also agreed to reinforce border measures against counterfeit and pirated goods, although criminal provisions for non-compliance therewith have not been included. Also, the agreement acknowledges the protection of geographical indications under similar arrangements to those currently applied in the EU.

Finally, as in other free trade agreements, the CETA reproduces the commitment to sustainable development and, in this respect, includes comprehensive and binding obligations for Canada and the EU on workers' rights[7] and on climate and environmental protection.[8] As regards the elimination of administrative barriers, there is acknowledgement of the mutual acceptance of quality standards in specific productive sectors (electrical equipment, electronic and radio equipment, toys, machinery and measuring equipment), meaning that conformity assessment certificates issued by European regulators will be admitted in Canada, and vice versa.

THE INVESTMENT COURT SYSTEM

For investment dispute settlement, the CETA has established an innovative Investment Court System that seeks to overcome the shortcomings of previous systems. Specifically, the habitual practice of free trade agreements that include investment or bilateral investment treaties is to include dispute settlement arrangements for investors and States (hereafter, ISDSs - Investor State Dispute Settlements). These arrangements establish that when there is a dispute between an investor and a State, a specific arbitration court is set up for each case, with the power to impose fines or compensation. This court comprises three members, one designated by the defendant country, another by the plaintiff company and a third person by both, who acts as judge.

ISDSs seek to ensure some security for companies against possible expropriations or regulatory changes that may affect their interests. But in practice, the lack of transparency or of independence of arbitrators has given rise to highly controversial decisions potentially calling into question governments' right to regulate in the public interest, against the interests of certain companies.[9]

In this respect, the CETA – like the treaty negotiated with Vietnam – includes an innovative investment protection system in the form of an ICS (Investment Court System) made up of fifteen judges[10] – one-third of whom from the EU, another third from Canada and the remainder from third countries – with a five-year mandate renewable only once. An Appeals Court is also created (a possibility not available in ISDSs) with the power, under specific assumptions, to confirm, amend or repeal a ruling issued by the previous Court. In addition, the CETA ensures the full transparency of proceedings – with the publication of all the information on a website, with public hearings and the possibility for all parties to make submissions – and also has a code of conduct for the Court members that is conducive to their independence and impartiality.

6 The signing of the treaty involves Canada partly incorporating the European regulations that oblige it to extend the period covering the protection of and monopoly for patented drugs for an extra two years of market exclusivity. That has raised concern about its impact on the manufacture of lower-cost generic drugs.

7 Here the EU and Canada undertake to observe and apply the essential rules and conventions of the International Labour Organization. Each party's right to regulate on labour-related matters is safeguarded and ignoring or scaling back labour rights to boost trade is prevented.

8 The parties undertake to apply international environmental agreements, without expressly mentioning any of them in particular.

9 UNCTAD has detailed information on foreign investment disputes (http://investmentpolicyhub.unctad.org/ISDS).

10 Selected by the CETA Mixed Committee, made up of representatives from the EU and Canada, and co-chaired by the Canadian Minister of International Trade and the European Commission Member responsible for Trade.

Economic and financial relations between Spain and Canada

Current trade and financial relations between Spain and Canada are limited, although the agreement is a notable opportunity for those companies wishing to have an international presence or that are close to breaking into the Canadian market.

As regards trade, according to Customs data, goods exports to Canada in 2016 accounted for 0.6% of total Spanish exports (1.3% in the euro area),[11] which in terms of GDP is only 0.1% (see Chart 1). By product group, exports of energy intermediate goods (1% of the total) and of chemical industry intermediate products (1.3% of the total) were to the fore. In the case of goods imports, the weight is similar, at 0.5% of the total (0.9% in the euro area). Once again, in terms of GDP the relative weight is very low (0.1%). The salient heading was mineral purchases (1.2% of the total). In 2016 as a whole, the Spanish economy posted a trade surplus of €185 million with Canada.

Bilateral relations between both countries in the case of services are also limited. Canada represented 0.7% of total exports in 2016. It accounts for 1% of total tourism receipts[12] and for 0.5% of non-tourist services exports.[13] As in the case of goods, Spain runs a bilateral surplus with Canada on the services account.

As to financial relations, direct exposure is, in this case, also on a modest scale. Direct investment accounted in 2016 for 0.9% of total assets vis-à-vis the rest of the world and for 0.1% of liabilities, according to the International Investment Position (IIP) (1.9% and 0.4% of GDP, respectively) (see Chart 1). In terms of direct investment, Spain had a net creditor position with Canada in 2016 equivalent to 1.2% of GDP.

The Foreign Investment Register data offer more detailed information on direct investment between Spain and Canada. Spain has several significant investments in Canada.[14]

Foreseeably in Spain's case, and also in that of the euro area, the direct impact in the short term of the lowering of tariff barriers that the CETA will entail will be limited on trade flows, owing both to the current low level of tariffs and to the modest scale of existing trade between both areas. The weighted value of tariffs for exports from Canada to the EU stands at 3.6% in the case of agricultural products and at 0.8% for non-agricultural products, lower in both cases than that applied to exports from the United States (4.7% and 1.5%, respectively).[15] By contrast, the impact of the reduction in non-tariff barriers is expected to be somewhat greater, especially in services.[16]

Overall, the European Commission (2011) estimates that the long-term impact on EU GDP could amount to 0.02-0.03 pp, and be somewhat higher (between 0.18 and 0.36 pp) for Canada.[17] The lowering of the barriers to international trade in services contributes to explaining around 50% of this impact, while the reduction in tariffs would account for 25%

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11 The countries most benefiting would be Ireland and the United Kingdom, as both have closer trade relations with Canada.

12 According to EGATUR data, the main Balance of Payments source for Tourism and Travel.

13 According to data from INE's survey on international trade in services (ECIS) for 2015, the latest year published with a country-by-country breakdown.

14 Including most notably: the 407, A30 and Windsor-Essex motorways, a petrochemical complex in Quebec, a regasification plant in New Brunswick, a clothing store chain and several wind farms.

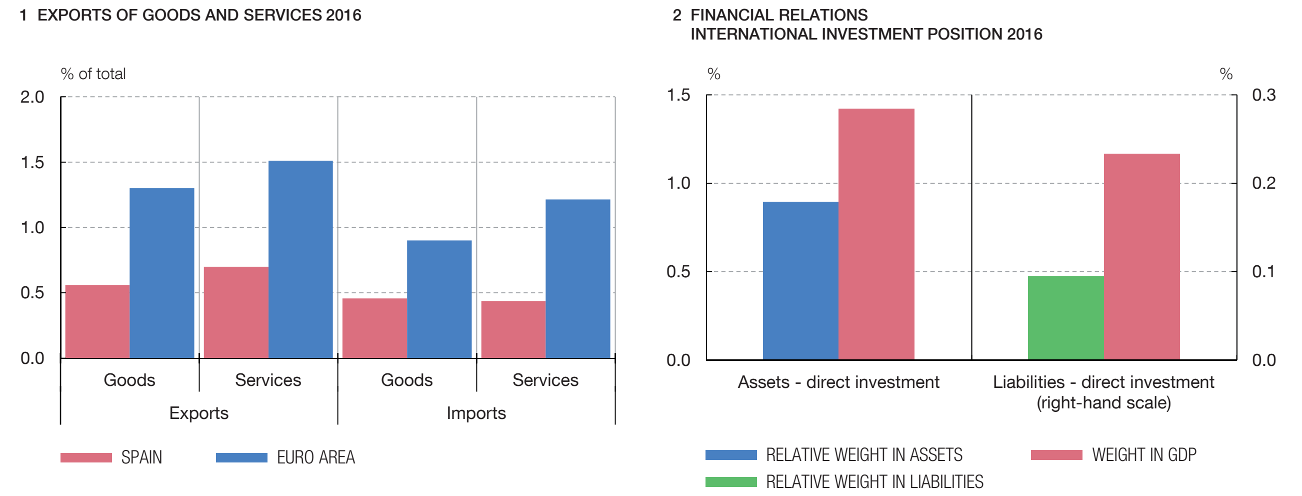
15 "World tariff profiles 2015", WTO, ITC and UNCTAD. The products considered correspond to the Harmonised System classification and the tariff is the weighted average of each based on the imports of each.

16 Francois, J. *et al.* (2007) estimate that Canadian market entry barriers entail additional costs of 25-50% for European firms, while EU entry barriers represent 18-42% for Canadian firms.

17 Unlike with the TTIP, there are not many studies that analyse the economic impact of the CETA and that allow the results of the papers by the European Commission to be tested. A recent paper by Raza, Troster and Arnim (2016) places the long-term effects at 0.02% of GDP for the EU and at 0.06% for Canada.

SPAIN'S EXPOSURE TO CANADA

CHART 1



SOURCES: Banco de España, INE and Eurostat.

of the impact in the EU and somewhat more than 30% in Canada. The sectors benefiting most in the EU would be food, chemicals, machinery and transport services, which currently face higher barriers and are of greater significance in the EU specialisation structure.

In the specific case of the Spanish economy, the reduction in non-tariff barriers is expected to exert a positive impact, in particular on those companies taking part in public procurement processes and in the regulated services sector, where entry barriers are going to be lowered for foreign companies (e.g. the telecommunications and energy sectors). In the case of public procurement, Spanish companies lead this market segment, with a share in the world total of over 10%, far above the weight of trade in goods and services in global markets (1.9% in 2015). Moreover, the lowering of non-tariff barriers would favour penetration by Spanish firms in a market where their presence is still limited (only 5% of total exporting firms sell their products in Canada, which is ranked 38th in respect of Spanish foreign direct investment, while Spain is ranked 15th as a recipient of direct investment from Canada). Given that the barriers in place to foreign direct investment in Canada are greater than those in Spain, the room for net gain in this area should be favourable to Spain.

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