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Trans-Pacific Partnership Agreement: Likely Impact on the U.S. Economy and on Specific Industry Sectors
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Thank you, Commissioners, for the opportunity to present the views of the Coalition of Services Industries (CSI) on the impact of the Trans-Pacific Partnership (TPP) on the U.S. services sector. CSI is the leading industry association devoted exclusively to promoting the international objectives of the U.S. service sector. Our members include the vast array of U.S. companies that provide services domestically and internationally, such as banking, express delivery and logistics, energy, insurance, media and entertainment, retail and wholesale services, technology, telecommunications, among others. We work globally to obtain solutions to significant international services issues, such as traditional market access restrictions (e.g., equity caps), a lack of national treatment, limitations on cross-border data flows, anti-competitive behavior from state-owned enterprises, domestic content and localization requirements, as well as a lack of transparency and due process in regulatory regimes. My testimony will analyze the TPP's provisions for the agreement's effectiveness in meeting these objectives. Overall, the TPP makes meaningful, positive progress in support of the services industry in many of these priority trade and investment areas. Issues remain to be resolved, most notably to include data localization prohibitions in financial services, but on balance the TPP makes positive steps toward strengthening the services industry's ability to compete in the Asia-Pacific region.

Two Revolutions

The global economy is experiencing two inextricably linked revolutions: the Digital Revolution and the Services Revolution. Services and digital communications are critical elements in the operation of global value chains, which are the principal phenomenon in international trade today. The United States is at the forefront of both movements. Our innovations in technology and in business models place us in the best position to define the course of both revolutions and---if we pursue the right policies, especially international trade policies---to benefit from them.

Services Revolution

The United States is the most competitive supplier of international services in the world. In 2014 U.S. companies exported services worth more than $700 billion, resulting in a services surplus of nearly a quarter trillion dollars. Services by far are the largest source of jobs, output, and economic growth. In addition, services are the enablers of all other sectors of the economy, including manufacturing, agriculture and energy. These sectors depend on banking, insurance, computer-related services, logistics, engineering, communications, etc. as critical elements to achieve their production and income goals.

Digital Revolution

At the center of the services revolution is a second revolution: "The Digital Revolution", of which the Internet is emblematic. This has enabled services to be delivered digitally across borders to a degree that was unimaginable twenty years ago. Keep in mind that Amazon.com was only founded in 1994, and Facebook was founded ten years later. Today all businesses depend on digital communication within their businesses, with their customers, and with their suppliers.

None of these advances were contemplated twenty years ago when governments negotiated the General Agreement on Trade in Services (GATS), the multilateral rules for trade in services that was part of the Uruguay Round in the World Trade Organization. The world has changed radically in the intervening years due to technological advances, global data flows, global value chains, innovative business practices, and the widespread use of the Internet by individuals, businesses, governments and other entities---in a word, everyone.

The international rules and provisions governing trade in services and digital trade have not kept up with these developments. These rules and provisions urgently need to be updated and brought into line with the realities of today's digitally-connected world. Ideally, WTO members would have taken the responsibility to negotiate such rules in the WTO, creating GATS 2.0. In the absence of prospects for a multilateral services agreement in the WTO, however, our best alternative is to obtain coherent and up-to-date rules and market access commitments across a range of agreements. If we can obtain coherent, updated, high ambition liberalization rules in the relevant chapters of negotiations such as the TPP, Trade in Services Agreement (TiSA) and the Transatlantic Trade and Investment Partnership (TTIP), we will have obtained de facto the standards for international trade in services in the coming years. And since the TPP will be open to additional countries joining, we will have gone a long way toward establishing the template for an eventual multilateral agreement.

In assessing the impact of the TPP on the U.S. services sector, one must look both "at the border" (i.e., permission to provide a service) and "behind the border" (the myriad regulations that set the rules in the importing markets).

The TPP, of course, is not the first services-liberalizing agreement with most of these countries. The U.S. already has free trade agreements with Australia, Canada, Chile, Mexico, Peru, and Singapore. So the new market access commitments essentially come from Brunei, Japan, Malaysia, New Zealand, and Vietnam.

Cross Border Trade in Services

While the United States is the world's leading services exporter, it still has tremendous scope to grow its services trade. Services account for almost 80 percent of the value added in the US economy, but only about 20 percent of its trade.[1] The TPP can help boost US services trade by expanding US services firms' access to markets with a collective population of over 480 million and GDP of almost $11 trillion.[2]

Chapter ten of the TPP provides binding disciplines for open and fair cross border trade in services, including national treatment, most favored nation treatment, prohibition on requiring specific types of legal entity on the part of the foreign service provider, and prohibition on requiring a local presence as a condition of the cross-border supply of a service. The market access provisions stipulate that the parties may not adopt or maintain measures that impose limits on the number of service suppliers, the total value of service transactions or assets, the total number of service operations, the total quantity of services output, or the total number of natural persons that

[1] World Bank, World Development Indicators and J. Bradford Jensen, *Global Trade in Services: Fear, Facts, and Offshoring,* 2011.
[2] Totals for the 11 countries other than the US in TPP, using IMF data (2014), as reported by CRS, *The Trans-Pacific Partnership: Negotiations and Issues for Congress* (2015).

may be employed in a particular service sector. The agreement also requires each party to permit all transfers and payments that relate to the cross-border supply of services to be made freely and without delay into and out of its territory in a freely usable currency at the market rate of exchange that prevails at the time of transfer.

E-Commerce

To an ever increasing extent, services are being provided digitally. One of the most important accomplishments of the TPP is its treatment of e-commerce. In this digital age, companies in international markets constantly need to move data digitally across the globe for their own internal operations and in serving their customers. While this may be obvious in the case of insurance firms processing claims or accounting firms verifying and reviewing audits, it is actually essential for any international business. For example, think of an airline company remotely monitoring its engines while the planes are in flight. Retailers have to manage their worldwide procurement and inventory.

The TPP includes a number of groundbreaking provisions vital for supporting services trade in the digital age. Importantly, the TPP assures that countries' market access commitments on services apply equally to services delivered or performed electronically as to those delivered conventionally. Furthermore, countries may not require services firms to establish a local presence as a condition for supplying services – vital for ensuring the ability to offer cloud computing and other Internet-based services. The TPP also ensures that digital products such as software and video remain duty free if transmitted online. In a first for a trade agreement, TPP calls for the member countries to cooperate on cybersecurity – an increasingly central priority for virtually every economy.

The negotiations have made important progress in advancing the objective of freedom for cross border data flows and prohibitions on localization requirements. Article 14.11:2 on Cross-Border Transfer of Information by Electronic Means provides that each Party shall allow the cross-border transfer of information by electronic means, including personal information, when this activity is for the conduct of the business of a covered person. It also provides for legitimate policy measures under certain constraints of non-discrimination, not disguised restriction on trade, and not greater than required to achieve the objective. In addition, Article 14.13:2 on the Location of Computing Facilities prohibits localization requirements and provides for legitimate policy measures under the same constraints as the cross border data flow provisions.

However, the TPP includes a very disturbing exception to the prohibition of localization requirements. As the Commissioners know, there are separate provisions in our FTAs and in the GATS that address financial services due to the sector's particular regulatory frameworks. The financial services chapter, which includes banking, securities, insurance, electronic payment service providers, and any other non-traditional financial services suppliers does not contain a provision on the prohibition on localization that is present for all other businesses in the e-commerce chapter. By this exclusion, financial services are denied the cost and efficiency benefits of the lowered trade barriers but will also be exposed to the considerable risks that derive from data localization laws to managing a secure, well-functioning global information system.

Most troubling is that this exception has occurred with the active support of the United States. This exception gives TPP countries and other trading partners the perfect political argument to impose such requirements on some of our most competitive businesses. Moreover, an insistence on the need for localization is particularly misplaced in that financial services companies are among the most highly regulated businesses in our economy, so any delays in providing data to financial regulatory agencies would jeopardize a recalcitrant company's very right to operate.

The financial services chapter also states that each party shall allow the cross-border supply of electronic payment services for payment card transactions, but it does not guarantee national treatment and the other market access provisions. This is a significant omission, and should not be repeated in future negotiations.

In order to maintain our competitiveness and leadership in the midst of the Services and Digital Revolutions, we need to stand firmly against localization requirements in all of our trade relations. The U.S. services industry is eager to work with the Congress and the Administration to ensure that the TPP and the negotiation of other agreements prevent the various forms of localization requirements in all sectors.

Media and Entertainment

The U.S. media and entertainment sectors are one of our core internationally competitive industries – with a trade surplus of over $13 billion, and trade surpluses with virtually every country in the world. Global markets are increasingly important to U.S. media and entertainment companies – for example, U.S. motion pictures receive about two-thirds of box office revenue from overseas markets. TPP is not as ambitious as ideal in terms of market access for the U.S. media and entertainment sector. In general, TPP provides good commitments for audio-visual products delivered online, even for countries with longstanding cultural protectionism. Online delivery of audio-visual content will be hugely important for the future, and in that way TPP makes important strides. TPP also, in general, includes good commitments for theatrical distribution of motion pictures. On the disappointing side, many countries retained the right to impose discriminatory policies in television, including pay television, which is an important export opportunity now and will remain so, particularly in countries with low broadband penetration. Additionally, many TPP countries took some type of "cultural" exception. While pre-existing FTAs blunt the importance of those exceptions with a number of the TPP countries, the number of such exceptions will make it more difficult to ensure high standard commitments from countries that join TPP in the future.

Another exclusion in the e-commerce world is the non-application to broadcasting of the non-discriminatory treatment of digital products, which also should be addressed in future negotiations.

Insurance

Gains in the TPP for the insurance industry include: a level playing field with strong disciplines on post office insurance entities owned by the government; market access provisions, including those that prohibit foreign equity limitations (with the exception of a Malaysian regulatory screen noted below); commitments on cross border data flows and e-commerce;

regulatory transparency (extending notice and comment); and the provisions of the chapter on state-owned enterprises (first time included in a trade agreement).

Over 70 percent of the global insurance market is concentrated in the U.S., Europe and Japan. However, driven largely by key demographic trends in emerging markets, including the rapidly emerging middle classes, future growth for the insurance industry will largely be derived from these developing markets. These markets tend to have more protectionist nontariff barriers and opaque regulatory regimes. High standard trade agreements are particularly crucial for this sector. In order to support quality professional jobs here in the U.S. in the future, access to these developing markets is critical.

Investment

The TPP includes investor protections vital for strengthening the rule of law throughout the TPP countries, including nondiscriminatory treatment and prohibition of expropriation without compensation. The inclusion of investment disciplines and investor-state dispute settlement (ISDS) are important elements for the services industries. The inclusion of these protections and the comprehensive prohibitions on performance requirements, such as local content rules and forced technology transfer, will be particularly important as other countries join the TPP.

Here again, however, financial services are carved out from an important protection. Financial services companies will not be able to bring a case under ISDS for a breach of the national treatment or MFN provision. The transition period for protection under the minimum standard of treatment is unfortunate since TPP parties should already abide by this important international law principle. There is no justification for denying any services sector full use of ISDS.

The non-conforming measures (NCMs) that countries have taken with respect to both Investment and cross-border trade in services are generally narrow enough to allow for expansion of market access across many industries. However, there are a few exceptions. In the case of Malaysia, for example, there is a highly discriminatory provision that permits Malaysia to apply a “best interest of Malaysia” test on any proposed investment or expansion of investment in the financial sector as well as for other situations where a financial services company seeks approval by the regulator. The absence of clear criteria for this test severely undermines the value of any Malaysian commitments on market access through investment for the financial services sector. Moreover, it is a serious negative precedent for future negotiations and for accessions to the TPP.

Domestic Regulation

Services are regulated to varying degrees, so the transparency and fairness of regulatory procedures (both development and implementation) are very important for services enterprises. Commitments in this area help strengthen the rule of law and are among the most important provisions in any trade agreement. The TPP includes important provisions to ensure that all measures of general application affecting trade in services are administered in a reasonable, objective and impartial manner. Among the safeguards are that measures are to be based on objective and transparent criteria, such as competence and the ability to supply the service. In cases in which a service provider requires authorization for the supply of a service, the competent authority must act within a reasonable period of time, establish an indicative timeframe for the processing of an application, inform the applicant of the decision concerning the application, and if an application is rejected, inform the applicant of the reasons for the rejection.

Government Procurement

The TPP parties have committed to applying transparent, predictable, and non-discriminatory rules for procurement of goods and services by their central government agencies. These commitments are especially important for Vietnam, Malaysia, and Brunei, which have not previously made such commitments. We are continuing to analyze the scope of their coverage.

Express Delivery Services

Annex 10-B prohibits a postal monopoly from cross-subsidizing its own or any other competitive supplier's express delivery services with revenues derived from monopoly postal services. In addition, chapter five on Customs and Trade Facilitation includes a number of improvements that will have operational benefits for commercial providers of express delivery services and their customers. These include: de minimis exclusions from customs duties on express shipments below a certain value (although unfortunately no specific value is set); expedited customs procedures for express shipments; risk management systems for assessment and targeting that enables customs administrations to focus their inspection activities on high-risk goods and that simplifies the clearance and movement of low-risk goods; and simplified customs procedures for the efficient release of goods, including the use of electronic systems accessible to customs users; and the use of international standards with respect to procedures for the release of goods.

Provisions in other sections of TPP will support the ability of U.S. express delivery services providers to provide seamless end-to-end service to customers. For example, Vietnam has removed foreign equity restrictions on freight agency, warehousing, and customs clearance, while Malaysia liberalized its customs clearance services. This new access is critical in markets where ancillary but key services continue to be restricted to joint ventures with local entities.

State-Owned Enterprises (SOEs)

Anti-competitive behavior from government subsidized, supported, or owned/controlled enterprises is a rapidly increasing barrier to the provision of services by commercial suppliers in many markets. The preferential treatment to these state-owned enterprises (SOEs) takes many forms, including:

- Exemptions, in whole or in part, from laws and regulations applicable to privately-owned enterprises.

- Subsidies granted to the SOE competing against the unsubsidized firms, or the SOE may be granted a monopoly on providing a given service.

- Foreign-owned firms may also face harsher financial and regulatory requirements and stricter supervisory enforcement than the SOEs with whom they compete.

An important innovation of the TPP is the inclusion of disciplines on such entities. The disciplines are confined to those SOEs (as defined by the TPP) that affect trade or investment among the TPP parties within the twelve TPP jurisdictions. This, obviously, is one of the limitations resulting from a purely plurilateral discipline, but it is an important first step. The significance of the disciplines also is limited by the rather narrow definition of an SOE. To qualify as an SOE in the TPP, the entity must be directly owned at least 50 percent by the government (or the government exercises more than 50 percent of the voting rights or the power to appoint a majority of the board of directors). This is an even more limited definition than applies in the U.S.-Singapore FTA, and should not become the model for defining SOEs in future agreements.

Within these limitations, TPP governments must ensure that their SOEs provide any commercial services in accordance with commercial considerations and non-discrimination in their sale or purchase of goods or services. In addition, TPP parties are enjoined from providing non-commercial assistance to their SOEs, subject to a finding of adverse effects or injury to the interests of another TPP party or that party's industry. The test for adverse effects is rather tightly drawn, so the burden of proof on the complaining party is substantial. Moreover, the agreement does not recognize that adverse effects can occur by an SOE's behavior in its own country---a rather inexplicable assumption. Frankly, the value of the SOE provisions lies less in their likely impact on the terms of competition in the market than in their providing a basis on which to build in future agreements.

Small and Medium Enterprises (SMEs)

The USITC's own research has shown that while few services SMEs export, those that do are leaders in growth of exports, revenues and employment.[3] The TPP's groundbreaking chapter on SMEs includes measures that should help more services SMEs to trade internationally, including a commitment for each TPP country to set up a web portal geared to helping SMEs take advantage of the agreement.

[3] USITC, *Small and Medium Enterprises: Characteristics and Performance,* November 2010.

Conclusion

On balance, the TPP will have a very positive impact on the majority of U.S. services industries. In addition to new market access commitments by those countries with whom the United States does not have FTAs, the most significant benefits will derive from the TPP's advances in addressing new issues stemming from the use of digital technologies. However, there are areas of the TPP that need improvement, as outlined in this testimony, which should be addressed as the TPP moves forward. The TPP's inclusion of disciplines on SOEs, even though very modest, is an important step in bringing those enterprises under international rules. The significance of the TPP in the long run will be the extent to which it proves to be a stepping stone to a multilateral adoption of provisions addressing the realities of international trade in services in the first quarter of the 21st century. That is why it is so important for the TPP to get it as close to right as possible in the areas of the Services and Digital Revolutions.