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## European Union trade policy

### Book section

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## **European Union Trade Policy**

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This contribution provides an overview of the evolution of EU policy, a summary of the EU's positions on key issues in international trade and a summary of the decision making procedures in EU external trade policy after the adoption of the Lisbon Treaty. The aim is of course to provide an overview and sufficient references for readers to follow up on the various aspects of the topic.

### *The evolution of EU trade policy*

The Treaty of Rome granted the European Economic Community (EEC) exclusive competence for Common Commercial Policy (CCP).<sup>1</sup> The creation of a customs union required the adoption of a common external tariff and thus a single EEC position on tariffs. The customs union also created a collective market power that exceeded that of the individual member states. As a result the EEC was able to achieve some important offensive interests during the Kennedy Round (1963-66) of the General Agreement on Tariffs and Trade (GATT), notably a reduction in US tariffs (Duer, 1998). A desire to show solidarity in building Europe and a decision making process that enabled member states to veto trade concessions also enabled the EEC to hold its defensive positions. These were to retain the preference margin for EEC producers the customs union would create and to protect the fledgling Common Agricultural Policy (CAP).

In the 1970s the US again led the charge in GATT. Facing a deteriorating balance of trade and what it saw as 'unfair' trade practices of the Japanese and Europeans in supporting their national industries the US pushed for multilateral controls for subsidies, an opening of government procurement markets and disciplines covering technical regulations and standards. The US had no active industrial policy, decentralised public purchasing and standards setting the US viewed the coordination of such instruments to favour national companies in other countries as unfair. But European Community (EC) member states pursued explicit (France and Britain) or implicit (Federal Republic of

Germany) national champion strategies. The implications for EC trade policy were however, the same, namely the defence of the policy space to enable these national policies to be continued.

There was some debate on EC level industrial policy but member state interests were too divergent for such an active policy. The only EC level intervention was in the form of coordinated adjustment or restructuring (in the face of competition from Japanese and Asian Newly Industrialising Countries) (Turner, et al, 1979). Towards the end of the 1970s there was some support for what was called pre-competitive cooperation between producers in different member states in more advanced technology sectors (McGuire S. 2006) . These were not significant except that they heralded a shift in private sector opinion away from reliance on national markets and towards greater market integration within Europe in order to compete with Japan and the USA.

The EC also entered the 1980s with a defensive position on international trade and resisted new initiatives on non-tariff barriers, services, investment and intellectual property rights (IPRs). But a paradigm shift within the EC towards more liberal, rule based policies facilitated both the Single European Market (SEM) initiative and thus support for a more proactive EC position on international trade (Young and Peterson, 2006). The SEM embodied a compromise between French dirigisme and rigorous reciprocity in trade negotiations and Anglo-Saxon liberalism. In fact the outcome was closer to a form of EC 'Ordnungspolitik' in other words a policy based on competition within the market and within an agreed framework of regulations guaranteeing key non-economic objectives and competition (Hodges, et al. 1991). The SEM and associated introduction of qualified majority voting with the Single European Act (SEA) resulted in common EC approaches to almost all the issues under discussion in the GATT Uruguay Round between 1986 and 94. There were effective EC level controls of subsidies, a comprehensive regime established for government procurement covering all forms of contract and levels of government. Technical regulations were addressed by the 'New Approach,' a combination of harmonisation of minimum essential requirements and mutual recognition. The SEM also liberalised some key service sectors, including

financial services and telecommunications, two sectors were seen as priorities for multilateral liberalisation.

The deepening and widening of the SEM enhanced EU market power (Holmes, 2006). The strengthened *acquis communautaire* gave the EU 'normative power,' as did consensus on the balance between market and regulation. Acceptance of a liberal, rules-based regime within the EU meant the EU was ready to support an equivalent regime at multilateral level provided it was consistent with the EU rules. Taken together these factors enabled the EU to play an active role in the Uruguay Round, and the EU together with the US (and other members of the quad) shaped the agenda and very largely the outcome of trade negotiations. On more traditional trade issues the EU further reduced its bound tariffs on manufactures to an average of [4.5%]. On agriculture the EU fought a rearguard action against liberalisation and in the end accepted the reestablishment of multilateral rules for agriculture but fairly little in terms of actual liberalisation.

From the mid 1990s the EU became the main proponent of a new multilateral round of trade negotiations. With the US reluctant to engage in further multilateral liberalisation due to domestic opposition and developing countries largely opposed to a comprehensive round, the EU assumed a kind of leadership role. The EU approach was shaped by the European Commission, which favoured a new comprehensive multilateral round ahead of preferential trade agreements (Lamy, 1995). By the time a multilateral round in the shape of the Doha Development Agenda (DDA) was launched however, some sources of EU relative strength had been weakened (Young and Peterson, 2006). The Lisbon agenda, a more intergovernmental follow up to the SEM, proved largely unsuccessful. As the 2000s progressed growth in relatively high tariff and otherwise protected markets such as China, India and Brazil burgeoned, eroding the EU's relative market power.

The negotiating leverage gained from holding out the prospect of concessions on agriculture in order to pursue offensive interests in NAMA, services and the Singapore issues proved insufficient and at the WTO Ministerial meeting in Cancun in 2003, the EU was obliged to drop investment, competition and transparency in government

procurement from the agenda. At the Hong Kong WTO ministerial in 2005 the EU made further concessions, such as agreeing to phase out export subsidies in agriculture, in order to keep the round alive. But with little support from the US and opposition from developing countries, the aim of an ambitious. Comprehensive round was lost and the DDA reverted to a modest conventional market access trade round focused on agriculture and non-agricultural market access (NAMA). By 2006 the EU recognised that success at the multilateral level was unlikely and switched to bilateral negotiations with major potential markets especially in Asia, as well as complete existing negotiations with African Caribbean and Pacific (ACP) states (Elsig, 2007; Heydon and Woolcock, 2009; Bartels, 2007). This policy was codified in the October 2006 Global Europe Strategy (European Commission, 2006; Evennet, 2007) and has been subsequently confirmed by the November 2010 policy statement on Trade, Growth and World Affairs (Commission, 2010). The 2010 policy statement also suggests a less liberal approach to reciprocity by hinting at the potential withdrawal of access to procurement markets for trading partners that do not offer reciprocal access.

#### *A summary of EU policy positions*

In addition to the kind of developments in European integration and the international trading system discussed above, EU trade policy is shaped by sector interests. Indeed, the general structure of EU preferences can be traced to the balance between offensive and defensive interests of sectors of the member state economies. Such sector interests are of course aggregated in EU level policies, so that the *acquis* itself reflects the balance of sector preferences.

The EU has generally favoured a formula approach to tariff reductions because the creation of the common external tariff (CET) appears to have smoothed the EU's tariff profile so that it has had rather higher average tariffs but fewer tariff peaks than for example the US. Consecutive multilateral rounds have reduced the average MFN tariff for manufactured goods to 3.9% with 100% tariff binding. The EU therefore has less to offer in NAMA compared to the large emerging markets such as China, Brazil and India (9%, 12% and 16% applied rates respectively) with higher bound rates in some cases.<sup>2</sup>

The EU policy position favours significant reductions in bound rates for major emerging markets. Such reductions in bound rates will not result in any significant reductions of applied rates, so what the EU seeks is discipline to prevent the emerging markets increasing rates on EU exports thanks 'water' in their tariffs or relatively high bound rates. For least developed countries the EU has offered tariff free quota free access to the EU market and urges other major WTO members to do the same (Faber and Orbie 2007). The EU also supports sector negotiations, there are such negotiations in 14 sectors and seeks some commitment from the large emerging markets to this process.

The average EU tariff is 15% in agriculture, compared to 10% in Brazil and China and 38% in India, but the EU of course provides significant agricultural subsidies. Since the initial limited McSharry reforms of 1992, the EU further reduced price support levels and 'decoupled' agricultural support from trade in the Agenda 2000 reform and especially the mid term review of the CAP in July 2003 (Daugberg and Swinbank, 2009). These provided some scope for the EU to make concessions so that it has accepted to tiered tariff and subsidy reductions in the chair's text of December 2008 in the DDA.<sup>3</sup> If finally agreed these could lead to further market opening by the EU, but much depends on the detail, including in particular what percentage of product lines are defined as sensitive and therefore excluded from tariff reductions. Anything more than 4% would limit liberalisation considerably. On subsidies the Chair's text would result in an 80% reduction in of the Overall Trade Distorting Support (OTDS) for EU agricultural, with some safeguards against shifting of subsidies between activities. This represents further liberalisation although is dependent of course on an agreed outcome of the DDA round as a whole. As part of a strategy of diversification out of commodity crops and into higher value added agricultural products, the EU is seeking greater protection for geographic indications, such as Parma ham and champagne.

The EU has pushed for the Singapore issues, so named because they were placed on the WTO work programme at the Singapore WTO ministerial meeting in 1996 (Van Dijk and Faber, 2006). On public procurement the EU, having adopted a comprehensive EU regime internally, would like other major economies that have not signed the WTO's

Government Purchasing Agreement (GPA) to at least adopt measures on transparency. The EU policy also believes greater transparency is beneficial for all countries because it promotes competition, more efficient use of public finance and fights corruption in the allocation of public contracts.

The EU supported negotiating investment in the WTO, in part to include investment in the rules-based regime of the WTO and in part because the main restrictions on investment were in developing countries. The US favoured the plurilateral OECD because it wanted high standards than could be expected in any WTO agreement. The collapse of the plurilateral 'Multilateral' Agreement on Investment (MAI) in 1998 effectively ended prospects for agreement within the WTO. The recent extension of EU exclusive competence to foreign direct investment with the Lisbon Treaty can be expected, in time, to result in a more common approach to investment by the EU (European Parliament, 2010). In the past the EU's policy has been hampered by the fact that competence for foreign direct investment was shared between the European Union and the member states, with the member states leading in negotiating investment protection in bilateral investment treaties (BITs). Exclusive competence implies the need to define a comprehensive, common EU position on investment. Given the importance of the EU for foreign direct investment a redefined, 'modern' approach to investment agreements by the EU could breathe the some life into the prospects of a genuine international agreement.

The rationale for EU support for the inclusion of competition as one of the Singapore issues was that there was a need to ensure that private restraints to trade do not replace public constraints following liberalisation. This was the same rationale used for EU-wide competition policy. Despite difficulties gathering information, there is evidence of damaging international cartel activity. The European Commission led in pushing for the inclusion of competition because it has exclusive powers in this policy area (Damro, 2006). But there was little strong support except among consumer groups within the EU. Internationally there was strong opposition from the USA, where the Department of

Justice opposed any substantive international rules on competition, and resistance from developing countries, which argued that they did not have the capacity for such policies.

In services the EU retains an offensive position given its comparative advantage in many service sectors, such as financial services, business services etc. Since the financial crisis of 2008 the mood has swung against further liberalisation of financial services. In the field of intellectual property rights the EU favours more effective enforcement of existing international conventions. Finally with regard to technical regulations and sanitary and phytosanitary measures the EU appears to have shifted from a policy of seeking mutual recognition agreements, because of the complexities involved in these, and now favours the promotion of full use of existing international standards.

### *The policy process*

EU policy making in trade functions reasonably well, despite the need to reconcile the positions of 27 member states, when there is a strong internal consensus as with the SEM and when there is a well established decision making regime in which the major stakeholders have confidence (De Bievre and Duer, 2005). The decision making regime for external trade has been established over a period of fifty years since the treaty of Rome and has provided the model for all external EU policy making used in the Treaty of Lisbon (Art 218 TFEU). In this regime the Commission provides the strategic orientation of policy thanks to its right of initiative on negotiating mandates. The EU's negotiating aims or mandate are adopted by the member states in the Foreign Affairs Council after work in the Trade Policy Committee (ex Art 133 Committee) that brings together member state and Commission senior trade officials (Art 207(3) and 218(2) TFEU). The TFEU confirmed that the consent of the EP, by a simple majority, is needed for all trade and investment agreement negotiated by the Commission. The EP would also like more say in setting EU objectives, because making its consent to any trade agreement conditional upon certain targets being met would strengthen the credibility of the veto power. The TFEU does not provide this.



During negotiations, whether at multilateral or bilateral levels, at a technical or political level, the European Commission is the sole voice of the EU (Young, 2006). This greatly facilitates coordination compared to other policy areas, where there are different negotiators at the technical and political levels, such as in the case of international environmental policy. There remain of course coordination problems both within the Commission between Directorates General and between the Commission and the member states (Kerremans, 2006; Meunier, S. and Nicolaidis, K. 2006). The well established regime of decision making in which the member states, through the TPC, assist the Commission during negotiations has generally facilitated this trust. Such close supervision of the Commission's approach to negotiations provides the assurance needed by the member state governments to allow the Commission to negotiate. The Council can also give the Commission directions during negotiations.

The adoption of the TFEU now requires the European Parliament must now be included in decision making including during negotiations. The EP (International Trade Committee (INTA)) now receives the same information on the progress of negotiations as the TPC. The Commission has for some time been working more closely with the EP in anticipation of the treaty changes and already provided a great deal of information (Woolcock, 2010). The Council and member states have a less easy relationship with the EP on trade policy and it will take some time before a *modus vivendi* can be developed between the two. Both Commission and Council, as well of course as interest groups and lobbies, will have to pay more attention to the EP, which has power to grant consent to all trade agreements. The EP also shares powers with the Council on trade legislation, such as the adoption of EU legislation implementing trade agreements or so called autonomous trade measures, such as the Generalised System of Preferences for developing countries. Prior to the TFEU the Council used to adopt legislation according to the coordination procedure in which the EP played virtually no role. After the TFEU the Ordinary Legislative Procedure (OLP) (formerly co-decision making) is to be used. This will be much slower than the previous arrangements, so it is likely that the Commission will be granted implementing powers to deal with the numerous detailed adjustments needed to

trade agreements and schedules, with OLP used only for the relatively few major pieces of trade legislation.

## **Conclusions**

EU trade policy has gone through various stages, some more defensive than others. During the 1980s and 1990s the EU moved to become more supportive of a liberal rules-based multilateral trading order. EU efforts to lead a comprehensive WTO round, in the shape of the DDA during the 2000s, has not had much success. As a result the EU has reverted to pursuing bilateral free trade agreements in order to pursue its aims.

The EU policy stance remains generally liberal, with the exception of agriculture where reform has been steady but slow, and there is unlikely to be support among a qualified majority of member states for any move towards the more aggressive use of reciprocity by threatening to close the EU market. But the EU lacks much leverage in negotiations, especially multilateral negotiations, due to the fact that it has an open market in most sectors, again with the exception of agriculture. The negotiation coinage that could be offered by way of opening the EU agricultural market did not prove sufficient to make progress on the EU's offensive interests in the DDA.

The decision making procedures of the EU have functioned tolerably well up to now thanks to member states having confidence and trust in the way decisions are made and the way the Commission, as agent, is controlled. The need to integrate the EP into the decision making procedures following the Lisbon (TFEU) Treaty is however, likely to result in a period of uncertainty.

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<sup>1</sup> The term EU trade policy will be used as it is the current usage. In actual fact Common Commercial Policy, the term used in the original Treaty of Rome more accurately reflects EU policy, which today extends well beyond what has been traditionally considered to be trade policy.

<sup>2</sup> The bound rate is the rate bound under GATT commitments. A higher bound rate than an applied rate means that a WTO member can increase tariffs up to the bound rate without infringing GATT rules and thus facing retaliation from other WTO members.

<sup>3</sup> The tiers as set out in the Chair's text of December 2008 are tariffs of more than 75% (70% reduction), 50-75% (64% reduction), 20-50% (57%) and less than 20% (54% reduction).