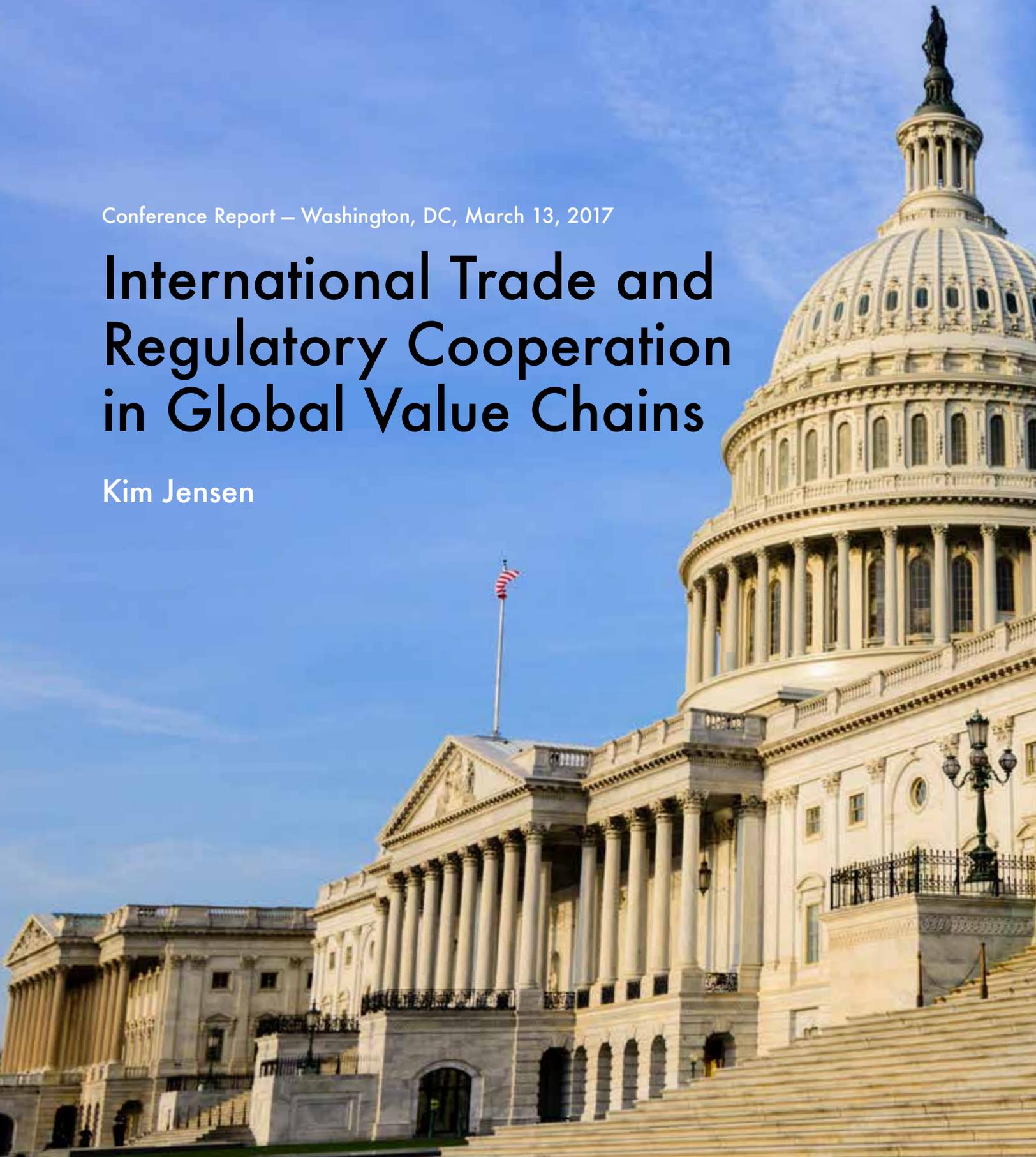

Centre for International
Governance Innovation

Conference Report – Washington, DC, March 13, 2017

International Trade and Regulatory Cooperation in Global Value Chains

Kim Jensen



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CIGI Masthead

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About CIGI

We are the Centre for International Governance Innovation: an independent, non-partisan think tank with an objective and uniquely global perspective. Our research, opinions and public voice make a difference in today's world by bringing clarity and innovative thinking to global policy making. By working across disciplines and in partnership with the best peers and experts, we are the benchmark for influential research and trusted analysis.

Our research programs focus on governance of the global economy, global security and politics, and international law in collaboration with a range of strategic partners and support from the Government of Canada, the Government of Ontario, as well as founder Jim Balsillie.

À propos du CIGI

Au Centre pour l'innovation dans la gouvernance internationale (CIGI), nous formons un groupe de réflexion indépendant et non partisan qui formule des points de vue objectifs dont la portée est notamment mondiale. Nos recherches, nos avis et l'opinion publique ont des effets réels sur le monde d'aujourd'hui en apportant autant de la clarté qu'une réflexion novatrice dans l'élaboration des politiques à l'échelle internationale. En raison des travaux accomplis en collaboration et en partenariat avec des pairs et des spécialistes interdisciplinaires des plus compétents, nous sommes devenus une référence grâce à l'influence de nos recherches et à la fiabilité de nos analyses.

Nos programmes de recherche ont trait à la gouvernance dans les domaines suivants : l'économie mondiale, la sécurité et les politiques mondiales, et le droit international, et nous les exécutons avec la collaboration de nombreux partenaires stratégiques et le soutien des gouvernements du Canada et de l'Ontario ainsi que du fondateur du CIGI, Jim Balsillie.

About the International Law Research Program

The International Law Research Program (ILRP) at CIGI is an integrated multidisciplinary research program that provides leading academics, government and private sector legal experts, as well as students from Canada and abroad, with the opportunity to contribute to advancements in international law.

The ILRP strives to be the world's leading international law research program, with recognized impact on how international law is brought to bear on significant global issues. The program's mission is to connect knowledge, policy and practice to build the international law framework — the globalized rule of law — to support international governance of the future. Its founding belief is that better international governance, including a strengthened international law framework, can improve the lives of people everywhere, increase prosperity, ensure global sustainability, address inequality, safeguard human rights and promote a more secure world.

The ILRP focuses on the areas of international law that are most important to global innovation, prosperity and sustainability: international economic law, international intellectual property law and international environmental law. In its research, the ILRP is attentive to the emerging interactions between international and transnational law, Indigenous law and constitutional law.

About the Author

Kim Jensen is an articling student at CIGI, providing assistance to in-house counsel on a range of legal matters and research support to the ILRP. Kim received her law degree from Thompson Rivers University in Kamloops, British Columbia, in April 2016. Prior to law school, Kim completed a bachelor of commerce with a major in international business management.

Executive Summary

A full-day round-table meeting organized by the Centre for International Governance Innovation (CIGI) and the World Bank Group brought together individuals representing industry, the public sector, think tanks and academia to discuss regulatory cooperation. Technical barriers have replaced tariffs as the most significant barriers to trade, and regulatory cooperation is a solution to some of these barriers, although this is a controversial topic. Participants offered a variety of ideas about how to solve problems associated with regulatory cooperation, and there was a rich dialogue between representatives from different interest areas.

Solving public concerns, building trust between regulators, increasing democratic legitimacy and providing incentives to regulators were highlighted as necessary preconditions to reducing controversy and achieving successful outcomes in this area. The appropriate mode and framework for implementing regulatory cooperation was discussed, as was the reduction of the costs of regulatory heterogeneity across countries, and the potential role of trade agreements to support regulatory cooperation and the achievement of national regulatory objectives. If the benefits of regulatory cooperation are appropriately leveraged, international trade will see enhanced economic competitiveness, while maintaining high levels of protection for consumers and the environment.

There is an urgency to identifying and implementing best practices for regulatory cooperation, and further research will facilitate this. Specific areas for research include undertaking a cost/benefit analysis of regulatory cooperation through case studies; addressing negative public opinion about regulatory cooperation through implementation in a manner respectful of national sovereignty and the right to regulate, as well as with better communication and complementary domestic policies; identification of industry characteristics where regulatory cooperation has been most successful; and examining mandates for regulators to identify how consideration for regulatory cooperation may be included. Connections between regulatory cooperation and development, democratic legitimacy, public safety and sovereignty were repeated throughout the round table, and some further research ideas were identified to resolve these persistent undercurrents.

Introduction

In a round-table meeting convened by CIGI and the World Bank Group, a group of experts came together on March 13, 2017, to discuss regulatory cooperation in international value chains. The entire event was held under the Chatham House Rule.¹ The purpose of the round table was to discuss lessons from recent experiences in regulatory cooperation alongside current research, with a view to developing a research agenda and policy recommendations. The goal was to achieve transnational sector-specific regulatory coordination in international trade in a way that bolsters, rather than depletes, the legitimacy and accountability of domestic democratic institutions.

The meeting was set against a backdrop of provocative current events, yet participants remained largely optimistic about the potential of regulatory cooperation. Current events that recurred in discussions included Brexit and the new direction of US trade policy, and whether these events were indicative of a definite trajectory toward nationalism. Some participants felt that although there is debate about the public understanding and political motivation for each event, it is difficult to dismiss the repercussions of both events for international trade and regulatory cooperation. Contrary to the indications given by Brexit and the evolving US trade policy, Canada is pursuing an agenda of internationalization and global partnerships. The benefits from this agenda are to be dispersed to all levels of society through domestic policy that is complemented by this internationalist approach. These distinct approaches from various countries illustrate how the uptake of regulatory cooperation will be contextual, and heavily shaped by the nation implementing it.

With strong signals of antiglobalization coming from many regions of the world, it would not be surprising if ambitious developments in international trade took a back seat; however, the participants of this round table agreed that the benefits of regulatory cooperation will be broad and worthwhile. New challenges resulting from the

¹ Under the Chatham House Rule, those present, including media, “are free to use the information received, but neither the identity nor the affiliation of the speaker(s), nor that of any other participant may be revealed.” For a full explanation of the Chatham House Rule, see: www.chathamhouse.org/about-us/chathamhouse-rule.

current events were acknowledged, but, despite this, there was an atmosphere of determination to dismantle barriers, one of the most important of which was regulatory divergence between trading partners. Some regulatory cooperation success stories were noted and, alongside the challenges posed by current events, these served to spur discussion of the theory underpinning the beneficial nature of international trade and of novel solutions to facilitate continued improvement.

The round-table participants discussed concrete examples of regulatory cooperation, such as the Common Electronic Submission Gateway developed by the Canada-United States Regulatory Cooperation Council.² The use of case studies directed the conversation to real concerns and benefits of regulatory cooperation, and participants responded with a variety of comments and questions. Some controversies animated the discussion, such as the questions of which mode of implementation was appropriate for regulatory cooperation, whether and how regulatory cooperation could benefit developing countries and how to demonstrate the broad benefits of increased regulatory cooperation to the public. The sections below develop these ideas further, and illustrate the potential of regulatory cooperation, if implemented judiciously.

Modality for Implementation of Regulatory Cooperation

One of the first issues raised in this session was whether it would be effective to advance regulatory cooperation through its inclusion in trade agreements, or whether there was a more appropriate mode for advancement. Participants mentioned that the benefits of attaching regulatory cooperation to trade agreements are enhanced visibility, centrality and political commitment to the issue. However, one major challenge raised about including regulatory cooperation in trade

agreements is having to overcome, or compensate for, the disconnect that arises because a trade agreement is meant to facilitate market access, whereas regulatory cooperation is about remedying a market failure. Other than trade agreements, regulatory cooperation could be advanced through international organizations or transgovernment processes outside of trade negotiations. Although these other options were raised, it seemed that attachment to trade agreements was accepted by some as somewhat of a norm. Obviously, any of the options raised have benefits and challenges, but not all options were canvassed as thoroughly as attachment to trade agreements.

Inclusion of regulatory cooperation in trade agreements may catalyze political commitment and make it less vulnerable to political whims than it might be if it remained solely in the policy realm. Negotiations for a trade agreement can result in losing substance, in favour of achieving agreement, and, if regulatory cooperation is subjected to this process, it may suffer fatal carve-outs of its substance. There is a chance of compromise and carve-outs in any negotiation, and this criticism of including regulatory cooperation in trade agreements could apply to any mode of implementation that includes negotiation between countries. Conversely, it was mentioned that inclusion in trade agreements adds efficiency by taking advantage of the existing framework; however, it also adds complexity to reaching consensus.

The Comprehensive Economic and Trade Agreement (CETA) between the European Union and Canada includes some provisions about regulatory cooperation. One such provision allows for the creation of a Regulatory Cooperation Forum, which will provide a place for engagement with this issue.³ Questions were raised regarding why regulatory cooperation was included in CETA and whether that was because the negotiation team believed the best mode of implementation for regulatory cooperation was as a chapter in a trade agreement. In response, it was suggested that the inclusion in CETA was not necessarily due to a decision that trade agreements are the best mode for implementation, but, instead, that it was an opportunistic inclusion, due

2 Government of Canada, "Canada-United States Regulatory Cooperation Council", online: <<https://www.canada.ca/en/health-canada/corporate/about-health-canada/legislation-guidelines/acts-regulations/canada-united-states-regulatory-cooperation-council.html>>.

3 EC, Commission, *Comprehensive Economic and Trade Agreement between Canada, of the one part, and the European Union [and its Member States...]*, 30 October 2016, art 26.2.1(h) (not yet entered into force), online: <<http://ec.europa.eu/trade/policy/in-focus/ceta/>>.

to the timely prominence of both the CETA negotiations and a mandate for advancement of regulatory cooperation. It will take time to observe how regulatory cooperation develops under CETA, and then there may be further insight into the question of modality.

Challenges to Regulatory Cooperation

There is public distrust about regulatory cooperation, and participants lamented this as a challenge that industry and governments need to overcome. Some of the widespread public beliefs about international trade and regulatory cooperation were seen to be misguided, and the changing of public perceptions was raised as a prerequisite to garnering support. Better communication, more effective public consultation and an effective regulatory cooperation framework were discussed as potential solutions. Overall public engagement should be built around the premise that regulatory cooperation helps meet goals that are not solely about free trade, but are about maximization of the benefits that flow from trade to all of society.

It was posited that regulatory cooperation should begin in non-controversial sectors that have little resistance, such as aviation safety. Successful forays into non-controversial sectors could allay concerns and develop a more positive perception of regulatory cooperation. If that occurs, then regulatory cooperation could be increased in value-laden, more controversial sectors, such as approving new pharmaceutical products or controlling environmental pollutants. As similarity of existing regulatory systems between partners is also thought to contribute to success, this should be considered when selecting sectors in which to increase regulatory cooperation.

Some participants mentioned that it is crucial to establish and maintain trust between regulators, in addition to having similar existing regulatory regimes. Regulators need to understand how their counterparts function, and they need to trust the standards and processes of the partner regulators. It may also be difficult to build trust with potential partners that have yet to develop and enforce an

effective domestic regulatory regime. Effective and transparent domestic regulatory systems were identified as a precondition to regulatory cooperation. Achieving this is complex and resource-intensive, which is beyond the current capabilities of some countries because regulators do not have infinite resources. The EU system provides an example of the difficulty in building trust as the regulator of each member state is obscured by the EU meta-regulators, which interface with other national regulators. This framework renders it difficult to develop relationships beyond those with the EU meta-regulators.

As important as trust is, it is not the sole precondition for developing regulatory coordination — an incentive is also required. Regulatory cooperation is a difficult task and will be most effective if it facilitates positive outcomes, such as more efficient markets, access to new markets, less market failure, diminishing costs and meeting the mandates of regulators. The discussion canvassed the difficult balancing that is required for regulators to cooperate and the level of investment of resources that is required for success, whether between different agencies in a single country, or between regulators from different countries. Even within one country, different agencies may have regulatory mandates that come into conflict. Further complications arise around trade in services, not least of all for regulators in the United States because each state and territory has authority in regulating services.

In some ways, EU regulators are already well positioned to have exchanges with other regulators because they have experience and processes in place for engagement between member states and EU meta-regulators. In comparison, many domestic national regulators are quite isolated. Culturally and constitutionally, the EU regulators have mandates that are distinct from those in the United States or Canada — some include “commercial purpose,” which means they have a broader scope of consideration when making regulations. Conversely, regulators in the United States generally have mandates that restrict their considerations to domestic interests. The divergence in mandates for regulators illustrates another factor that must be overcome prior to embarking on regulatory cooperation.

Trade Goals, Development and Regulatory Cooperation

Governments and regulators are fundamentally most interested in regulations that protect their domestic citizens and corporations. Government policies and mandates to regulators are indicative of this, and, thus, finding the balance between trade goals and development is complex. On the one hand, there are the conflicting interests of domestic citizens and corporations; and, on the other hand, there are the interests of citizens in developing countries. One theme of this session was how the concerns of the importing country may be successfully addressed so that, if they undertake regulatory cooperation, they will not be compromising opportunities or security for their citizens. Regulatory cooperation was also noted to be an opportunity to save resources, once an effective framework is in place, and to have access to other markets.

This discussion also touched on the possibility of an exporting country making a commitment to protect foreign consumers in exchange for the opportunity to engage in trade with that country. This is similar to programs already in existence in which importing countries inspect imports to ensure regulatory compliance. It may be cumbersome for exporters to meet a plethora of regulatory standards if they export to several countries, all with differing regulations. If a small or developing exporting country does decide to take foreign standards into account when regulating, at what point does it become infeasible for that exporter to adhere to the regulations of each individual importing country? Is it possible for an exporting country to regulate in a manner that facilitates market access with multiple trading partners?

In situations where there is a developed country negotiating with a small or developing country, leverage of the opportunity for market access may be used detrimentally or for short-term gains. The small country may make compromises and overcommit to bring its regulations into line to facilitate market access, without it ever being possible for the country to achieve the promises made. The desire to develop export markets may overshadow the reality of the domestic resource constraints for achieving the foreign regulatory standard.

The Interplay of Democracy, International Trade and Regulatory Cooperation

A few participants noted that democracy has been linked with development agendas because of the positive correlation between economic prosperity and political freedom. Despite this, during the discussion, it was acknowledged that trade rules may be intrinsically antidemocratic as they form carve-outs, albeit mutually agreed upon carve-outs, to national sovereignty. Democratic legitimacy around trading systems and international institutions should be strengthened to encourage positive public perceptions of international trade. Communication with the public is crucial, as it is ultimately those individuals that support, or not, the democratically elected governments that will be the institutions responsible for regulatory cooperation.

Although consumers may not have full confidence in the legitimacy of the international trade system, it is a system that has been developed through multilateral negotiations between democratically elected governments, and this lends a certain level of democratic legitimacy. The influence of the private sector on international trade was also mentioned as an antidemocratic force to be reckoned with. Likewise, this influence affects public awareness and consumer decision making. It was noted that services can touch on democratic values more substantially than goods can, and when issues such as consumer safety, the environment or education are involved, trade is pitted against democratic legitimacy and sovereignty.

If trade disputes were resolved in domestic courts, the usual systemic checks and balances would apply. However, the international trade dispute resolution mechanisms bypass state-level courts and use largely unfamiliar processes to resolve issues. The multilateral process that built the mechanism may be difficult for the public to understand, as the dispute resolution systems are not necessarily transparent and operate independently of national input once established. This means that the visible part of the dispute resolution system does not seem to be part of a democratic process with the same checks and balances as people are accustomed to seeing in domestic systems. It was suggested that inclusion of social and economic

representation in trade negotiations would strengthen the systems, increase public confidence and enhance the incorporation of democratic values.

The recent shift in the subject matter of trade disputes was highlighted. Regulatory subject matter that arises under agreements such as the Agreement on Technical Barriers to Trade⁴ or the Agreement on the Application of Sanitary and Phytosanitary Measures⁵ is distinct from tariff-related subject matter — it relates much more to morality and societal values. International trade dispute resolution mechanisms have tended to deal with tariffs, but now more commonly deal with value-laden issues, such as environmental concerns or consumer health and safety. The fact that international institutions make decisions about these subjects, traditionally reserved for a sovereign state, does justify some concern. Regulatory cooperation contributes to these concerns even more because it has potential to put those core values of society at risk by prioritizing homogeneous regulations over societal values. In the alternative, if implemented properly, regulatory cooperation could lead to an improvement in the way the domestic and foreign systems operate in terms of accountability and democratic legitimacy.

Consultation and public input were mentioned by participants as being other important elements in strengthening the democratic legitimacy of trade. It does take time and effort to understand the complex factors that interact in international trade systems and institutions, and this represents a “cost” of participation. This may explain why civil society and the public do not always engage at an early stage. Another issue with consultation is that only affected parties are likely to voluntarily engage when asked for input, and this generally means businesses. This natural selection of the parties that engage in the consultation limits the input; however, no clear solution to this issue was given. It was posited that the real challenge of legitimacy is in the social contract between people and their government, not between people and the international trading system. In trade-related circumstances, public discontent spills over to the entire trading system and trading institutions, and is not focused on that domestic social contract.

In terms of public support, the major benefit from trade is that consumers save money on imported products because the prices are lower, and they can then allocate some spending elsewhere. It was stated

that this benefit is currently invisible to consumers because today’s consumers have only ever known the low-price model that results from imports. It was jocosely suggested that we need a contraction of trade that would render imports unavailable, thus raising prices. The idea being that the resulting increase in prices of most products would provide evidence to consumers that trade is beneficial to entire societies through overall lower prices.

Fair trade is a concept that adds some costs related to environmental protection or human rights back into the price of an imported product. Some consumers are willing to pay more for fair trade products, and, in this situation, the benefits from trade are more difficult to illustrate because the lower prices of imports sometimes come at the expense of environmental protection or human rights. When costs are added back into prices, there is less difference between prices of imports and prices of domestic products. This is not a definitive rule for every product; however, the willingness of consumers to pay more for fair trade products is an important issue to recognize in a trade system.

One negative consequence of trade that was identified is that it creates very competitive markets. This can be detrimental for domestic producers who are not able to withstand the competition. Despite this competition, it is accepted by many economists that societies do grow richer overall as a result of international trade. If domestic businesses had confidence in their ability to compete, perhaps this issue would be resolved, although the competition might be considered unfair, due to the externalized costs in exporting countries that allow for lower prices on imported items, such as availability of cheap labour and externalization of environmental costs.

Well-planned redistribution and public programs that make the benefits of trade flow into a broader segment of society could ameliorate some public discontent with international trade. Industries that suffer as a result of international trade could have redistributive benefits in the form of retraining, or investment in developing new markets. It was broadly noted that it will be beneficial to address the larger issue of legitimacy in international trade as a whole. Procedural shifts such as incorporating more transparency may be a good practice for overcoming the real or perceived lack of democratic legitimacy. Further to this, impact analysis of trade was identified as an area where actual benefits, as opposed to planned benefits, could be measured, although this is very resource intensive and complex.

4 15 April 1994, 1868 UNTS 120 (entered into force 1 January 1995).

5 15 April 1994, 1867 UNTS 493 (entered into force 1 January 1995).

Potential Research Agendas and Partnerships

While not full case studies, some analysis related to regulatory impact assessment and the costs of regulatory divergence has been carried out on existing sectors in which regulators cooperate. Some predictors of when regulatory cooperation will be successful were suggested. These include the following: the number of players in the industry; the volume of output of the industry; and the level of complexity of the product. The lower the answer for each of these indicators, the more likely it is that regulatory cooperation will be successful. These predictors are tentative, and perhaps there are other, better, more specific indicators that could be identified through targeted research and case studies. A potential research agenda is to undertake case studies of the existing examples of cooperation and build best practices and a matrix to determine which industry characteristics contribute to the success or failure of regulatory cooperation.

A gap has developed between the traditional mandate of regulators — domestic consumer protection — and mandates requiring more complex goals to be considered, such as the impact of a regulation on international trade. Carrying out more complex mandates will require research into whether regulatory divergence has a cost, and, if so, how this cost can be quantified. Could greater coordination reduce the costs associated with divergent regulatory standards between countries? Studies of the cost of regulatory divergence would need to touch on costs to regulators, as well as costs to the private sector producers. The answer to this question may be determined by using a variety of cost-benefit analysis models, which means that the results will differ and may not provide any definitive answers. The difficulties associated with the quantification of benefits and costs that result from regulatory cooperation were mentioned, especially given the new and novel nature of this type of analysis. It may be necessary to develop a mechanism that could quantify the costs of regulatory divergence more accurately, prior to basing decisions on any existing model.

It was suggested that a potential research agenda would be around the modality and structure for implementation of regulatory cooperation. Are trade agreements the best place to prioritize regulatory

cooperation, or would international industry organizations be more effective? Would the regulatory cooperation bodies be set up sector by sector, and how would commercial interests be balanced with the consumer safety mandate? Where exactly would a democratic presence be incorporated so as to ensure the regulatory body does not become dominated by private commercial interests?

Another suggestion for further research was to map regulatory heterogeneity, which would facilitate formation of partnerships among countries that already have substantially similar regulations. The rationale is that the more similar the existing regulations are, the lower the barriers to cooperation will be. Similar regulations could be indicative of similar regulatory systems and similar societal values, which are factors that are expected to make regulatory cooperation more tenable.

Conclusion

Throughout the meeting, it was widely acknowledged that there are challenges that must be overcome to facilitate moving forward with regulatory cooperation. Despite this, there was a firm sentiment that regulatory cooperation can be designed in such a way that it leads to benefits for everyone. It must be approached cautiously, due to the existing public discontent, and with close alignment between domestic societal values and regulatory frameworks. Closer dialogue with regulators will be required, and regulators should be included in discussions such as the round table.

One particular challenge is negative public perception of international trade in general and, more specifically, of regulatory cooperation. Other challenges that were discussed included building a democratically legitimate system for implementation of regulatory cooperation, gaining public and private sector confidence and commitment to regulatory cooperation, and finding the most suitable sectors and partners for Canada to undertake regulatory cooperation with. Potential solutions to these challenges are communicating and consulting more effectively with the public, ensuring the framework used for regulatory cooperation does not compromise societal values for domestic or foreign partners, and cautiously selecting partners and sectors with which to cooperate.

Agenda

March 13, 2017

9:00 a.m. – 5:00 p.m.

The World Bank Group, 1818 H Street NW, Washington, DC, 20433

9:00–9:30 a.m.	Registration
9:30–10:15 a.m.	Welcome, introduction and participant expectations
10:15–11:15 a.m.	Presentation on trade and regulatory cooperation
11:15–11:30 a.m.	Health Break
11:30 a.m.–12:30 p.m.	Services trade and regulatory cooperation
12:30–1:30 p.m.	Working Lunch <i>Thematic discussion</i> — interplay of democracy, trade and development goals, regulatory interdependence
1:30–2:30 p.m.	<i>Thematic discussion</i> — lessons from trade negotiations and agreements
2:30–3:00 p.m.	Health Break
3:00–4:00 p.m.	<i>Thematic discussion</i> — constraints on regulatory cooperation; prospects for regulatory equivalence-based approaches
4:00–5:00 p.m.	Research gaps; potential partnerships; avenues for reform and wrap up

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