Fostering Growth in Digital Trade through Bilateral Cooperation in the Development of Trade Rules

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About the Author

Don Stephenson began his public service career in 1979, working in cultural policy for 10 years at the Department of Communications. He moved into economic policy, at Consumer and Corporate Affairs, Industry Canada and Western Economic Diversification, before returning to cultural policy, as director general of cultural industries, Heritage Canada, where he led the negotiations with the United States on the World Trade Organization (WTO) split-run magazine dispute. He was appointed director general of trade policy at the Department of Foreign Affairs and International Trade and served for two years as assistant secretary to the Cabinet, Economic and Regional Development Policy, Privy Council Office. In 2004, he was appointed ambassador to the WTO, serving as chair of the goods negotiations in the Doha Round until 2008. Don returned to become assistant deputy minister, trade policy and negotiations, until his retirement in late 2011, and continued to serve as chief negotiator for the Canada-India Comprehensive Economic Partnership Agreement until December 2018. Don lectures frequently on trade policy, trade negotiations and public policy development, and serves as trade and investment adviser to the Expert Deployment Mechanism for Trade and Development, a trade-related technical assistance program delivered under contract for Global Affairs Canada.

About the Project

The Canada-India Track 1.5 Dialogue on Innovation, Growth and Prosperity is a three-year initiative between CIGI and Gateway House: Indian Council on Global Relations to explore areas for closer cooperation. Experts, government officials and business leaders will convene annually to promote bilateral economic growth and innovation in today's digital economy.

Canada and India maintain strong bilateral relations built on the foundation of shared values and healthy economic ties. Economic exchanges between Canada and India are on an upward trajectory, but there continue to be unexplored areas for mutually beneficial growth, especially in light of rapid developments in technology that are changing every facet of the economy and society in both countries. To address these challenges, the partnership is helping to develop policy recommendations to promote innovation and navigate shared governance issues that are integral to the continued growth of Canada-India bilateral relations.

The Canada-India Track 1.5 Dialogue on Innovation, Growth and Prosperity strives to build closer ties between Canada and India and nurture the relationship to its full potential. Canada and India can be global leaders in innovation, and the Canada-India Track 1.5 Dialogue seeks opportunities to work jointly on multilateral issues and identify areas where improved cooperation could benefit both countries. In addition to its focus on innovation, the partnership examines topics such as collaboration on research and higher education, promotion of Canada-India trade and investment, energy cooperation and issues pertaining to global governance.

Through this partnership, Canada and India can be intellectual partners and cooperate in the design of their global governance frameworks.
Executive Summary

Trade is important for both Canada and India. For Canada, as an industrialized economy endowed with enormous resource gifts but a small domestic market, trade is essential. Trade represents a large share of the economy and makes an important contribution to Canadians’ high standard of living. For India, while it is less dependent on trade due to a much larger domestic market, expanding exports and attracting investment are essential to sustain rapid economic growth and to create jobs and economic prosperity for a large and growing labour force.

Trade is changing. Technology has been the principal driver of trade growth, through improvements in production, transportation and communications. Growth in communications capacity and decreases in the cost of computing have altered traditional economic development and, together with the internet, created the foundations for the most recent tectonic shift in the nature of business and trade, the emergence of an economy in which the most important resource is data.

In trade policy fora, the digital economy is most often viewed from the perspective of electronic commerce — goods and services purchased and sold over electronic networks. However, the digital economy — including digital trade — is much more than electronic commerce. The digital trade agenda is a subset of the broader digital governance universe, which spans issues of infrastructure, internet administration and myriad economic and social policy issues and involves innumerable stakeholders.

India and Canada have important commercial interests in digital trade, and both have counterbalancing social policy concerns, but they have important differences as well. The data-driven economy is expected to not only increase trade in services but also may reduce employment in manufacturing; it is also expected to shift the demand for services from business process outsourcing to higher-skill work. A resulting loss of tariff revenue is more meaningful for India, where it represents five percent of general government revenues, as compared with Canada, where it represents less than two percent. The potential loss of jobs and a shift in services exports will also have a greater impact on India due to its greater reliance on services exports and the massive growth of its domestic labour force.

Introduction

This paper, first presented as a backgrounder at Track 1.5 meetings in Mumbai, India, in November 2019, describes the digital trade agenda as viewed from the negotiating table. Its aim is to promote trade and, consistent with the objectives of the Track 1.5 Dialogue, calls on Canada and India to partner and lead in advancing the digital trade agenda.

Background

Few institutions can speak with more authority on the complexity of global cooperation on digital issues than Gateway House: Indian Council on Global Relations and the Centre for International Governance Innovation (CIGI). Gateway’s and CIGI’s research in this field makes clear the large number of inter-related policy questions posed by digital technology, among them:

→ infrastructure and data management standards;
→ personal and national security;
→ equitable access to services and distribution of economic benefits;
→ the ethical use of data;
→ the protection and promotion of cultural diversity; and
→ the balance between freedom of speech and promotion of hate.

Global digital governance involves many layers of technical, social and economic issues and interests. In a recent discussion on these questions in Ottawa, Canada, the participants were invited to “pick a layer.” Accordingly, this paper is focusing on the layer of commerce and, more precisely, the regulation of international trade in digital products and services.

There are two things on which India and Canada can agree, at the outset.
First, trade is important. In the case of Canada, trade is important because we have no choice — we are an industrialized economy endowed with enormous resource gifts but a small domestic market. Trade represents a large share of Canada’s economy and makes an important contribution to its high standard of living. In the case of India, while it is less dependent on trade due to a much larger domestic market, it must expand exports and attract investment to sustain rapid economic growth and create jobs and economic prosperity for a large and growing labour force.

Second, trade is changing. Technology has been the principal driver of trade growth, through improvements in production, transportation and communications. These changes have altered business models and patterns of trade, perhaps most dramatically by enabling task and service unbundling in “global value chains” (perhaps better described as “regional jobs networks”).

Explosive growth in communications capacity — the McKinsey Global Institute estimates that inter-regional bandwidth capacity rose 45 times between 2005 and 2014 (Manyika et al. 2016, 4) — and enormous decreases in the cost of computing — the consumer price index for personal computers declined 96 percent from 1997 to 2015, according to the US Bureau of Labor Statistics1 — have fundamentally altered traditional economic development (in keeping with Petty’s law, the theory that a country will progress from agrarian to industrialized to services- or knowledge-based economies).

Most important is the now ubiquitous internet (reaching half the world’s population — some four billion people — by smartphone, in 20192). Together, these changes created the conditions for the most recent seismic shift in the nature of business and trade, the emergence of an economy in which the most important resource is data.

In trade policy fora, the digital economy is most often viewed from the perspective of electronic commerce — goods and services purchased and sold over electronic networks. By that measure, global digital trade was assessed by the US International Trade Commission (2017, 13) at US$27.7 trillion in 2016, principally in business-to-business services. (Note here that all services’ trade data must be taken with a grain of salt: all that can be said with confidence is that it is large and growing faster than goods trade, and, importantly, that services trade has grown faster in developing countries than in the advanced economies.)

However, the digital economy — and digital trade — encompasses much more than electronic commerce. It is the mining and application of data in entirely new ways: artificial intelligence and machine learning; automation and 3D printing; internet-connected sensors and the Internet of Things; blockchain and automated document processing; internet-based communications and more. The World Trade Organization (WTO) estimates that data-based trade might increase global trade by two percent per year through 2030, through not only increased trade (in both goods and services) but also reduced transaction costs (reductions in customs processing time and the costs of finding suppliers or buyers) (WTO 2018).

The WTO notes, importantly, that the expansion of business-to-consumer digital commerce services will reduce barriers to entry into trade for micro, small and medium-sized businesses (ibid.), an important policy objective for both Canada and India. Internet platforms have enabled micro-multinational firms to reach global markets through novel business models — indeed, the new digital marketplace might be better described as consumer to business. Notwithstanding the enormous market dominance of early movers, the digital economy holds the potential to reduce the heavy concentration of trade in a few firms, and the heavy dependence on a few foreign markets — another shared policy objective.

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The Digital Trade Agenda

The digital trade agenda is a subset of the broader digital governance universe, which can be reasonably described as a “wicked problem.” Digital governance spans issues of infrastructure (telecommunications networks and internet servers), internet administration (domain names, Internet Protocol addresses and

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3 As defined by Rittel and Webber (1973).
so on), myriad economic and social policy issues (cultural policy, security, tax policy, industrial policy, intellectual property regimes, competition policy, development policy, trade policy and more) and involves innumerable stakeholders.

Within the trade agenda, there are two subsets of issues, one focused on the consumer (consumer protection) and the other on the supplier (promotion of commerce).

The consumer protection agenda includes provisions to:

- guarantee the protection of personal information;
- shield consumers from unsolicited commercial electronic messages; and
- ensure effective mechanisms for redress in the case of fraud or deceptive commercial activities.

The digital commerce agenda includes commitments to:

- not discriminate on the basis of the service provider’s nationality;
- expand market access (negotiated and codified in the services and investment agreements of the WTO, or the services and investment chapters of bilateral trade agreements, which endeavour to be technology-neutral);
- prohibit the application of customs duties on electronic transmissions (services delivered electronically);
- require the establishment of a domestic legal framework governing digital trade;
- adhere to international standards of electronic authentication, including the recognition of electronic signatures;
- promote paperless trading;
- ensure access to domestic internet infrastructure;
- provide legal liability and agency of internet service suppliers;
- prohibit requirements to locate computing facilities in the domestic market and limitations to the disclosure of the proprietary source code as conditions to do business; and
- enshrine the right to unfettered cross-border transmission of data (perhaps the most contentious provision).

The digital agenda is addressed in multiple WTO agreements, and in multiple chapters of bilateral trade agreements. There are relevant provisions on goods (for example, products purchased on the internet may still be delivered physically across borders, on which *de minimis* customs duty rules apply) and on product standards disciplines, telecommunications, information technology, customs procedures, intellectual property and government procurement rules.

WTO rules were conceived as cross-cutting and technology-neutral and continue to be elaborated, through the decisions of the dispute settlement system. However, there are gaps and weaknesses in the multilateral framework of rules for digital trade, including:

- definitional problems (unresolved questions regarding the treatment of products that can be delivered in physical or electronic form, and whether electronic services are consumed across borders or in the country of supply — separate “modes” of services delivery on which separate market access commitments are made in services schedules);
- classification issues (how to treat search engines, cloud-based services, internet platform services, mobile applications under the services disciplines of trade agreements);
- limited coverage of digital services in the market access commitment of individual members;
- an absence of explicit protections for cross-border data flows and consumer rights;
- limited provisions to promote trade facilitation; and
- no explicit rules of origin for digital products.

Bilateral trade agreements, particularly recent agreements, provide additional disciplines on digital trade. Of the 279 agreements inventoried by the WTO in 2016, some 75 included provisions specific to digital trade and this trend is increasing — fully 60 percent of agreements signed between 2014 and 2016 include such provisions. It is now widely accepted in trade policy
circles that a comprehensive trade agreement must include a chapter on digital trade.

Most of these agreements, including those of many developing countries and the European Union, take a cautious, soft law approach: they commit to non-discrimination of digital products, agree on a prohibition or moratorium on the application of customs duties to electronically delivered products, and commit best endeavours to strengthen confidence in electronic commerce through consumer protection, competition policy rules to prohibit fraudulent and deceptive practices, and protection against unsolicited commercial messages. They also typically provide for ongoing cooperation between trade and digital economy authorities to ensure continued dialogue on how trade rules should evolve to foster the growth of the digital economy.

Some agreements, including those of the United States and Asia-Pacific countries, seek to provide greater certainty to the digital trader, the evidence of which is the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), the high-water mark for legally binding disciplines to promote digital trade. These disciplines include a guarantee for the right to transmit data across borders and a prohibition against requirements to locate servers in the country or to disclose source codes as a condition of access to the market. The CPTPP allows legitimate public policy purposes to trump these obligations on the condition that such actions can be demonstrated not to be disguised barriers to trade and that they are the least trade-restrictive method to achieve the policy objective.

As in all trade, there are also competing interests at play among developing countries, and no greater agreement on how trade rules should be framed. It is important, however, to acknowledge the development dimension of digital trade and digital trade policy. Digital trade holds the potential to reduce the barriers to entry and expand market access for micro, small and medium-sized enterprises everywhere, and to allow developing economies to “leapfrog industrial age infrastructure” (Ciuriak and Ptashkina 2019, 1).

To realize that potential, however, both domestic and international policy must provide a marketplace framework that facilitates equitable access and sharing of the benefits. Equitable participation in digital trade must overcome an imbalanced competitive landscape through measures to facilitate access to technology and infrastructure, financing, and training in digital technology literacy and data-based business models.

Cogent arguments are made by some observers that a deeper understanding of the nature and implications of the data-driven economy is needed before trade rules can confidently be framed. Petty’s law, adapted for international trade disciplines, moves from shared understanding of the issues, to consensus on the need for and nature of marketplace framework law, to interest-based bargaining.

In the words of one trade academic, “law emerges in interaction...negotiators have to do a lot of ‘arguing’ before they understand a topic well enough for ‘bargaining’ or codification” (Wolfe 2017, slide 39). This is the utility of research and discussion in the Organisation for Economic Co-operation and Development and the Asia-Pacific Economic Cooperation (APEC), among others, and the motive behind the recent Group of Twenty proposal to integrate digital trade issues into the WTO Trade Policy Review Mechanism.

It is worth noting that the partnership between Canada and India in the Global Partnership on Artificial Intelligence (GPAI) was created “to support and guide the responsible development of artificial intelligence that is grounded in human rights, inclusion, diversity, innovation, and economic growth” (Innovation, Science and Economic Development Canada 2019). The GPAI was launched under the banner of the Group of Seven Digital

**Setting Imbalances Right**

There is no international consensus on how trade rules should be adapted to foster digital trade. Disagreements over how to proceed are sometimes portrayed as a North-South divide but, as noted above, there are important differences of approach even between the two richest markets in the world — one promoting the interests of firms that have built dominant positions in the data-driven economy through first-mover advantage, the other adopting a cautious stance in the face of the uncertainties of rapid technological change and still-evolving business models.
Ministers, at its May 2019 meeting, to collaborate on the theme of “Building Digital Trust Together.”

Trade policy cannot resolve domestic or international debates over social preferences, whether related to the promotion of cultural expression, environmental integrity, national or personal security and so forth. These issues must be resolved first, domestically and then in non-trade, international fora, before trade rules can be adapted to the public will. This resolution will take much discussion and time, notwithstanding businesses’ urgent need for certainty regarding their investments.

Disagreements on the broader trade agenda further complicate efforts to resolve digital trade issues at the multilateral level. Some hold the position that “legacy” issues in the multilateral trading system must be resolved before new issues are addressed, in particular the long-standing demand for reform of agricultural trade. Others have stepped back from multilateralism and trade liberalization to address complaints of economic inequality and dislocation by “rebalancing” (goods) trade and repatriating production. Calls for reform of the WTO will have to be answered before a new agenda can be agreed upon. In the meanwhile, regional groupings — APEC, the Association of South East Asian Nations, the European Union, the Canada-United States-Mexico Agreement (CUSMA) partners — have an important role to play in building the global consensus on digital trade rules.

Both India and Canada have important commercial interests in digital trade and both have counterbalancing social policy concerns, but they have important differences as well. The data-driven economy is expected to increase trade in services but may also reduce employment in manufacturing, and it may shift the demand for services from business process outsourcing to higher-skill work. A resulting loss of tariff revenue is more meaningful for India, where it represents five percent of general government revenues, as compared with Canada, where it represents less than two percent.

The potential loss of jobs and a shift in services exports will also have a greater impact on India due to its greater reliance on services exports and the massive growth of the domestic labour force. These differences in economic circumstance explain India’s reluctance to make permanent the moratorium on customs charges on electronic transmissions and its caution in making market access and other commitments that might weaken its competitive position in the services sector.

Geography and history have also made national security more challenging in India than in Canada. These reasons help explain India’s caution in moving forward on digital trade issues.

Canada’s greater reliance on trade and a rules-based trading system explain its relatively higher ambition in creating new trade disciplines, evident in the texts of the CUSMA and the CPTPP.

Logically, there are, or at least should be, some points of convergence in the Venn diagram of Canada’s and India’s national interests. For example, both countries should agree that there is cause for concern in the loss of consumer confidence in data-driven economy firms due to repeated, high-profile data breaches and cyber attacks, monetization and misuse of personal information, weaponization of social media, and so forth. Citizens are losing trust in the ability of firms and governments to protect personal privacy and shield them against fraud and deceptive commercial practices. According to a recent CIGI-Ipsos survey of 25 economies, 80 percent of citizens are concerned about privacy (CIGI-Ipsos 2019, 6); 25 percent do not trust the internet (ibid.), and 12 percent are making fewer online purchases (ibid., 55).

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This concern is the genesis of Canada’s modest ambition in WTO digital trade discussions, seeking disciplines to defend online consumers, ensure personal privacy, provide a shelter from unsolicited commercial electronic messages and foster ongoing cooperation between member countries on these issues. Strengthening public trust in digital products and services is clearly a shared interest.

Likewise, measures to ensure the interoperability of national legal frameworks for such things as authentication technologies or mutual recognition of paperless trading requirements are likely to benefit business in both countries, without need for harmonization, at this stage. In the longer term, of course, the aim is to agree on common rules, providing business with both certainty and reduced compliance costs. As one industry member put it: “I can deal with a set of bad rules; it’s conflicting sets of bad rules that can make doing business impossible.”

Even in respect of these modest goals for articulating common positions on which to build a broader consensus, it should be noted that soft commitments — without legal binding — can contribute to reducing uncertainty. Codifying rules to facilitate business will take time, but policy makers can build understanding and confidence through a step-by-step process.

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**What Track 1.5 Can Do: Recommendations**

**Create a bilateral process to identify common causes and a road map to advance the digital trade agenda.** The Track 1.5 Dialogue on Innovation, Growth and Prosperity was tasked to seek opportunities for Canada and India to work jointly on multilateral issues and identify areas where improved cooperation could benefit both countries. Creating a bilateral process to identify a common cause and a road map to advance the digital trade agenda represents just such an opportunity. At a maximum, joint proposals by India and Canada have the potential to rally broad engagement in the multilateral trade policy community at a time when leadership is badly needed. At a minimum, bilateral engagement between industry, academics and policy officials is likely to deepen their understanding of the issues and interests, building readiness to agree on rulemaking in the future.

**Spark greater bilateral cooperation by convening a business-to-business conversation and providing supporting research and analysis.** At arm’s-length from the negotiating stances of their governments, Gateway House and CIGI can spark greater bilateral cooperation by convening a business-to-business conversation and providing supporting research and analysis, designed to identify policy approaches that meet the minimum needs of both business constituencies. Consensus among industry leaders can be a powerful voice to persuade policy makers to take the next steps — to cooperate on proposals for regional and multilateral discussion. Gateway House and CIGI are well respected in the business community for the quality of their academic work, as well as for their balanced, independent discussion of the issues. With strong links to industry leaders in both countries, the two organizations are ideally placed to convene a discussion at a level likely to influence policy makers.

**Focus on the impact of digital technology, not just on electronic commerce but also on trade in traditional service sectors.** The work should focus on the impact of digital technology, in terms not just of electronic commerce but also of its impact on trade in traditional service sectors. Considering the broad range of industries captured under the 12 sectors and 55 subsectors of the Services Sectoral Classification List (WTO 1991), work should be narrowed to one or two industries of primary interest to India and Canada. Business services is a natural candidate for examination, comprising significant and varied commercial interests in both countries. Financial services seem like another — an enabling sector with global leaders and strong regulatory regimes on both sides.

By way of example and without limiting the scope of the discussion between industry leaders, the financial services sectors in both India and Canada are poised to be leaders in the emerging open banking services — the development of innovative applications and services, enabled by consumer-authorized third-party access to personal or corporate banking information.

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The growth of such services depends critically on the development of Application Protocol Interface (API) standards that allow for the secure transmission of financial data between financial institutions. Through bilateral cooperation, India and Canada can help avoid a “spaghetti bowl of rules,” threatened by the development of multiple national API standards, and shape the global standard, allowing their financial service providers to enter new markets without the heavy cost of new technology infrastructures. As principal stakeholders in this standard-setting process, leaders in the financial services sector need to make their needs clear to policy makers.

Governments can then take guidance from Mahatma Gandhi, who said (borrowing a phrase from Alexandre Auguste Ledru-Rollin): “There go the people; I must follow them, for I am their leader.”

Works Cited


About CIGI

The Centre for International Governance Innovation (CIGI) is an independent, non-partisan think tank whose peer-reviewed research and trusted analysis influence policy makers to innovate. Our global network of multidisciplinary researchers and strategic partnerships provide policy solutions for the digital era with one goal: to improve people’s lives everywhere. Headquartered in Waterloo, Canada, CIGI has received support from the Government of Canada, the Government of Ontario and founder Jim Balsillie.

À propos du CIGI

Le Centre pour l’innovation dans la gouvernance internationale (CIGI) est un groupe de réflexion indépendant et non partisan dont les recherches évaluées par des pairs et les analyses fiables incitent les décideurs à innover. Grâce à son réseau mondial de chercheurs pluridisciplinaires et de partenariats stratégiques, le CIGI offre des solutions politiques adaptées à l’ère numérique dans le seul but d’améliorer la vie des gens du monde entier. Le CIGI, dont le siège se trouve à Waterloo, au Canada, bénéficie du soutien du gouvernement du Canada, du gouvernement de l’Ontario et de son fondateur, Jim Balsillie.

About Gateway House

Gateway House: Indian Council on Global Relations is a foreign policy think tank in Mumbai, India, established to engage India’s leading corporations and individuals in debate and scholarship on India’s foreign policy and the nation’s role in global affairs. Gateway House is independent, non-partisan and membership-based.