



## COMMENTARY

BY STEPHEN KHO

# Beyond the Political: ECFA'S International Trade Implications

At the end of June, a unique moment unfolded in Chongqing, China. “Semi-official” representatives of China and Taiwan – two territories that do not formally recognize each other, and whose relationship is generally characterized by the slinging of rhetorical arrows – shook hands and committed themselves to an agreement aimed to reduce tariffs and commercial barriers between the two sides. However, the agreement, known as the Economic Cooperation Framework Agreement (ECFA), has since become mired in significant political acrimony in Taiwan.

Hailed by President Ma Ying-Jeou and members of the Kuomintang (KMT) as the key to breaking out of economic isolation, ECFA has been met with strong opposition by members of the Democratic Progressive Party (DPP), which characterizes the Agreement as a blow to Taiwan’s sovereignty and has called for a nationwide referendum on ECFA. Indeed, legislative approval of the Agreement has become so contentious that a meeting of the special legislative session called to consider the Agreement devolved into a brawl between members of the two parties, with two legislators requiring medical attention, one for broken ribs, the other for a contusion after he was hit by a clock.

However, putting aside the political dynamics surrounding this Agreement, it is important to consider the international trade implications of ECFA. Although not a free trade agreement in name, the intent of ECFA is essentially the same – that is, it is designed to liberalize the bilateral trading relationship between China and Taiwan. Based on the current Agreement, China will reduce tariffs on 539 Taiwanese goods worth \$13.8 billion within 6 months of ECFA coming in to force, with full elimination of tariffs to take place gradually over a span of two years. Also, China will open 11 service sectors to Taiwanese service providers, including banking, accounting, audiovisual, aircraft maintenance, and insurance. For its part, Taiwan will be reducing tariffs on 267 Chinese goods, including chemicals, textiles, tires, apparel-making machines, auto parts, and electronic parts, with a value of approximately US\$2.9 billion. As for services, Taiwan will open up nine sectors to Chinese service providers, including conventions, exhibitions, the film industry (10 film releases per year), sports and entertainment, banking, and research and development.

### “Substantially All the Trade”

While this is a good start towards a free trade agreement

between the two territories, it cannot be the end of negotiations. Under World Trade Organization (WTO) rules, as well as Article XXIV of the General Agreement on Tariffs and Trade (GATT) and Article V of the General Agreement on Trade in Services (GATS) in particular, a free trade agreement that affords the parties to the agreement better treatment than they afford to other WTO countries is only permissible if the agreement covers “substantially all the trade” between the parties. ECFA as it stands does not even come close to covering substantially all the trade between Taiwan and China. More goods and services must be covered, including those in the area of agriculture. China and Taiwan cannot stop at just a few hundred tariff lines of goods or a dozen service sectors.

Furthermore, China and Taiwan should consider addressing other measures that block the liberalization of trade, including non-tariff trade barriers such as technical and safety standards as well as other regulatory barriers. Only by eliminating the non-legitimate use of these barriers will there be no question that ECFA meets the GATT Article XXIV and GATS Article V requirements of eliminating “substantially all the trade” between China and Taiwan. Short of doing so may result in other countries challenging China and Taiwan in a dispute at the WTO because they also want the better than “most-favored nation” (MFN) treatment the two are providing each other under ECFA.

Indeed, ECFA explicitly recognizes this situation, as it commits both sides to negotiate further trade liberalization, specifically including the areas of non-tariff trade barriers, more service sectors, investments, and trade remedies. However, in the interim, between the time that ECFA goes into effect next year and when “substantially all the trade” is liberalized, China and Taiwan may very well be in violation of their WTO obligations due to the limited coverage of ECFA. Needless to say, further trade liberalization negotiations should be undertaken, agreed to and implemented as quickly as possible.

ECFA contains a dispute settlement provision, which states that issues arising out of ECFA may be resolved through this bilateral dispute mechanism, although the Agreement has yet to set forth the exact procedures for this mechanism (the text provides that China and Taiwan will agree to these procedures within six months of implementation).

This arrangement is an important component to the Agreement. In the past, China has been reluctant to bring WTO cases against Taiwan even though it was entitled to. One

example has been Taiwan's continued ban of about 2,000 products – including agricultural products – from China, despite WTO obligations on Taiwan to provide MFN treatment to all such products, including from China. But China has not challenged Taiwan in the WTO because of political reasons. For its part, Taiwan also appears to be unwilling to challenge China under the WTO for similar political reasons.

Having an ECFA dispute settlement mechanism in place will give the two parties a forum for resolving trade disputes, helping ease tension that may arise from unsettled disputes. Indeed, one of the main purposes of a dispute settlement mechanism in any trading relationship is to ensure that the relationship is not hurt by any disagreements – which are inevitable in such relationships, particularly one as robust as between China and Taiwan – and will continue to remain stable and perhaps even grow, even during those times of disagreements. Given China and Taiwan's reluctance to submit disputes between them to the WTO, this benefit will be especially true when substantially all of the trade between China and Taiwan is covered under ECFA, and so may incentivize the two parties to finalize full coverage under ECFA as soon as possible.

Included in ECFA is a separate agreement on intellectual property rights (IPR). In particular, this agreement requires that China and Taiwan grant priority rights to patent applications, essentially enabling Taiwanese manufacturers who file for patent or trademark applications in Taiwan to receive priority patent or trademark protection in China for up to one year, and for Chinese manufacturers to receive similar privileges in Taiwan. The IPR agreement also grants plant breeders variety rights in each other's territories for any new varieties they may develop. Moreover, the agreement commits both sides to coordinate enforcement efforts in the area of internet piracy and counterfeiting, well-known marks, and geographical indications, among other IPR issues.

It is worth noting that while there are MFN exceptions in the area of services and goods for free trade agreements, there is no MFN exception in the area of IPR. In other words, the benefits that China and Taiwan provide to each other under ECFA for IPR must also be provided to all other countries that are members of WTO, with very limited exceptions. In the area of enforcement, for instance, China therefore cannot provide better treatment for Taiwan intellectual property when enforcing these rights than that provided to other countries' intellectual property. It cannot enforce against internet piracy of Taiwan intellectual property and ignore internet piracy of other countries' intellectual property. The same is true for well-known marks from other countries, not just from Taiwan. In short, both territories must be prepared to provide the necessary resources to meet the IPR obligations under ECFA, not just for each other, but for the rest of the WTO countries.

One quick note of caution about trade remedy cases, particularly those in other countries. In recent years there has been an increase in anti-dumping and countervailing-duty cases brought against China and Chinese companies, as China continues to export all sorts of products in large quantities, and importing countries worry about illegal government subsidies and unfair pricing schemes. As trade barriers between

China and Taiwan are broken down by ECFA, one can expect more integrated manufacturing between the two territories. And with more integrated manufacturing, one can certainly expect more anti-dumping and countervailing-duty cases to be brought against both China and Taiwan together. Companies and governments on both sides of the Taiwan Strait will have to prepare for this eventuality. Better records will need to be kept, business and supply chain plans will have to be reevaluated, and more resources will need to be set aside to defend future investigations.

## Broader Policy Implications

Taiwan has been vocal about its goals for this ECFA, and its expectations for how ECFA will affect Taiwan's trading relationship around the world, and especially with the United States. It is first and foremost concerned about being marginalized in a region that is seeing integration among the South-east Asian countries, between these countries with China, and between China and Korea and Japan. Taiwan is being left out. If Taiwan does not make efforts to integrate itself into the region, it will suffer devastating economic consequences. And as it is no secret that the main reason for Taiwan's inability to integrate on a trading basis with the region (and around the world) is political tension with China, it only makes sense for Taiwan to first make efforts to integrate with China.

This strategy appears to be paying off, even in the short term. Indeed, many scholars believe that with ECFA in place, China will be much more willing to stand aside quietly as Taiwan seeks to negotiate free trade agreements with Singapore (which Taiwan has already announced it intends to pursue), Japan, Thailand, the Philippines, Malaysia, and perhaps even the United States. Some even speculate that China may be willing to stop blocking Taiwan's attempts to join international organizations such as the World Health Organization and the international standards setting bodies.

As for the United States, Taiwan is making it clear that it no longer needs to rely on the United States alone. It has long been perceived that the United States, believing that Taiwan has no alternatives but to lean heavily on U.S. support defensively and therefore economically as well, often tries to use Taiwan as an "example" of what it expects from the rest of the Asia region. For instance, the United States has pushed Taiwan hard in the area of IPR for many years, insisting that Taiwan show the region what changes must be made to national IPR regimes in order to meet U.S. standards. Although recently Taiwan has succeeded in resolving most of the outstanding IPR issues with the United States, to the point of being taken off the U.S. Special 301 Report, the United States continues to ignore Taiwan's request for further trade integration (this despite the United States' willingness to sign free trade agreements with countries that remain on the Special 301 Report).

Similarly, the United States for a period stopped all trade negotiations with Taiwan over the one issue of mad cow disease (or bovine spongiform encephalopathy). Considering that the United States had the same "problem" with most of the countries in the Asian region, it had hoped to use Taiwan to

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build momentum to reopen the other Asian markets to U.S. beef. However, these tactics backfired when Taiwan's Legislative Yuan wrote some import restrictions into law.

In light of the ongoing regional trade integration, Taiwan has been given no choice but to reach out to other major players in the area such as China and ASEAN. Such reaching out is a good thing, even if the United States begins to feel like "odd man out" as a regional trade alignment starts to coalesce without its involvement. With ECFA, Taiwan has the opportunity to become one of the main economic hubs in the region, avoiding isolation within Asia and increasing investment from abroad. With ECFA, the United States may now feel the need to reengage Taiwan commercially. With ECFA, Taiwan may now have the leverage to negotiate further integration with the world trading community on a level playing field.

For China, ECFA is part of its plan to become the center of international trade in Asia. Earlier this year China's free trade agreement with the 10-member Association of Southeast Asian Nations came into force, and it is now actively working on potential trade arrangements with Korea and Japan. China has the economic strength to command interest and desire with its regional trading partners to develop closer economic relations. Arguably the only really difficult negotiation was with Taiwan, due to political reasons. However, ECFA essentially bridges that gap.

Moreover, by bringing its regional partners together, China is lessening the commercial influence of the United States in Asia. Indeed, ECFA is further evidence of the degree to which the United States is being left behind in the region. U.S. eco-

nomics continue to erode as Asia draws tighter together around China without U.S. inclusion. If anything, the signing of ECFA should serve as the impetus for the United States to reengage Taiwan through the U.S.-Taiwan Trade and Investment Framework Agreement (TIFA), to implement the U.S.-Korea Free Trade Agreement, and to speed up negotiations on the Trans-Pacific Partnership Agreement.

Of course, if the United States does not reengage the region, that would probably be just fine with China. China's goal is to exert its influence in the Asian region, and decrease the United States' influence at the same time. To accomplish this goal, it was in China's best interest to sign ECFA, and it is in China's best interest to continue to negotiate as quickly as possible full coverage of all substantial trade – including reducing non-tariff barriers and erecting effective dispute settlement procedures – under ECFA.

Because of ECFA, the trading relationships around Asia are changing. Because of ECFA, China is continuing to exert its influence in the region. And because of ECFA, Taiwan may be able to engage the rest of the world trading community on a more level playing field. It is clear that the international trade implications of ECFA are enormous. ■

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