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WHAT DOES TTIP MEAN FOR FUTURE FTAs? HENNING VÖPEL AND JÖRN QUITZAU EXAMINE

BENJAMIN ZEEB ASKS WHAT FUTURE FOR EUROPE?

KENT HUGHES WRITES ABOUT NORTH AMERICA IN THE WORLD OF TRADE

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A question of trust

Europe's behaviour since the start of the financial crisis has not worked. Five years ago, the United States and Europe had approximately the same unemployment rate and level of public debt. But now, five years later, it's a different story: Unemployment has exploded here in Europe, while it has declined in the United States. Our economic output remains below the 2007 level. It has declined by up to 10 percent in Spain and Italy, and by 25 percent in Greece. The financial crisis has been transformed into a debt crisis. This has turned into a crisis of confidence across Europe.

Europe's establishment has not succeeded in demonstrating that the EU and the eurozone is serving the interests of the people. Voters don't seem overly keen to shift more power to Brussels. On the contrary, EU-sceptic parties are becoming popular everywhere. Political parties advocating or contemplating an exit have not reached the same audience in every European country, but they are on the rise. A euro exit, which was once only contemplated for 'periphery' countries as a consequence of high financial distress, comes to be seen as a political choice worth debating in 'core' countries. Syriza's election victory in Greece could serve as a shock therapy for those in power. What they've been doing isn't working, and a different approach is needed.

It's dangerous for the established parties to continue fuelling nationalist parties on the left and right. Five years of crisis, and counting, damaged Europe's social fabric and culminated in a Europe that has lost legitimacy with its own citizens and much of its credibility with the rest of the world. A Europe that is proclaiming greater union and consolidation in name while in practice its most acute problems are in fact being re-nationalised.

There is a problem with debt in Europe, and there is tremendous uncertainty about how the debt burden is to be resolved. This uncertainty has an economic cost, and the cost only grows over time. But because most policymakers stubbornly refuse to consider what seems to have become obvious to most Europeans, there is a very good chance that Europe is going to repeat the history of most debt crises. After many years of denying that they are insolvent, and many years of promises that reforms will be implemented that will set off enough growth to resolve the debt, policymakers in countries like Spain will be forced either to change their positions or they will be forced out by voters – simply because economic conditions will have deteriorated so drastically that a restructuring can no longer be put off.

Europe will not grow, the reforms will not 'work', and unemployment will not drop until the costs of the excessive debt burdens are addressed. The eurozone institutions need to demonstrate to the populace that they have plans for reforms that will work in reducing debt, unemployment and to increase growth.

Otherwise Europe's way of life will be under sustained and serious threat. ■

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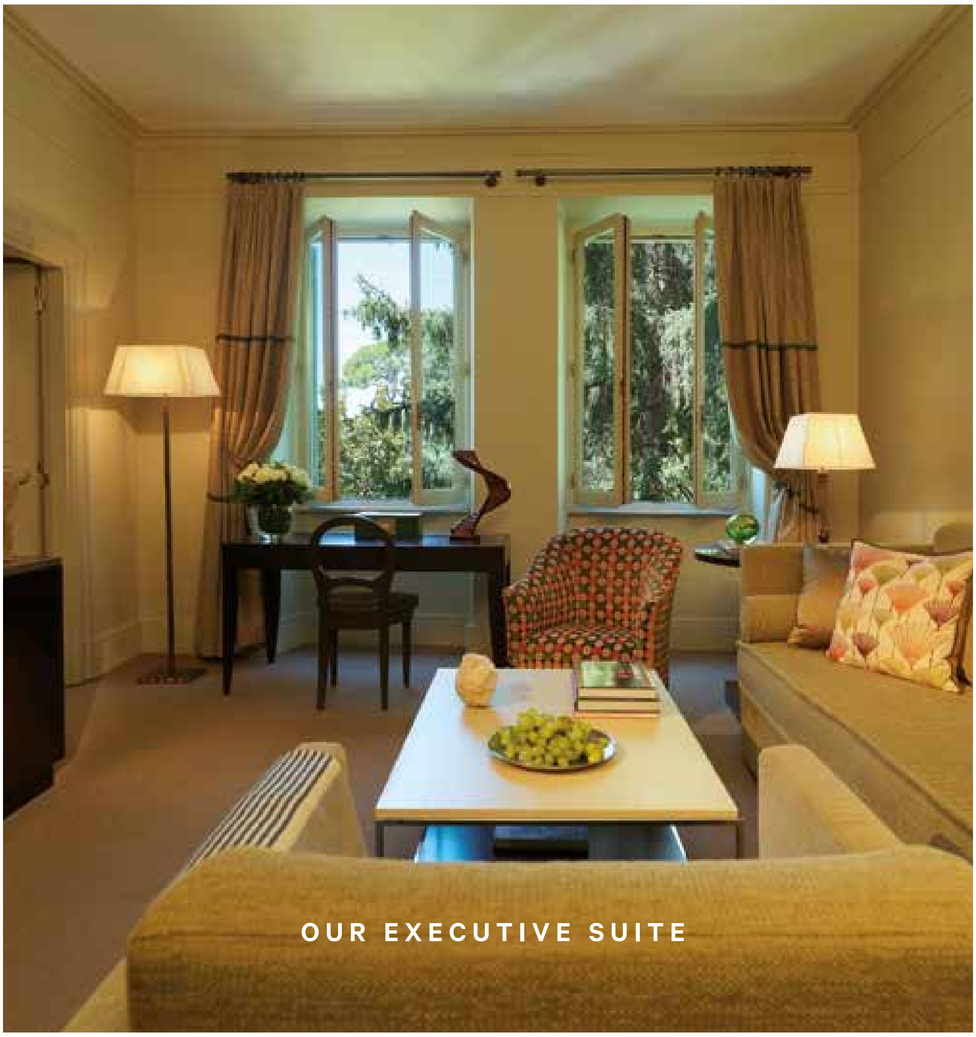

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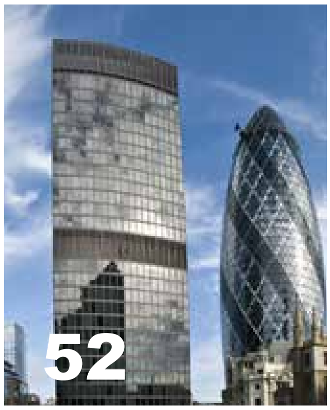

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Towards a new global economic order – what does TTIP mean?

Prof. Dr Henning Vöpel is Director of the Hamburg Institute of International Economics (HWWI), and Dr Jörn Quitzau is Head of Economic Trend Research at Berenberg

What is the Transatlantic Trade and Investment Partnership TTIP?

Through the TTIP the European Union and the United States of America intend to create the world's biggest free trade zone. The trade agreement would reduce tariffs and other barriers to trade, and harmonize technical regulations, standards, and permitting procedures on both sides of the Atlantic, with the overarching goal of creating additional prosperity and jobs. The TTIP is meant to strengthen the shared values of Europe and America, bolster their positions of economic dominance, and thus establish a counter-weight to dynamically emergent economies such as China, for example.

In some quarters, the TTIP is dismissed as a 'cheap economic stimulus program.' However, the effects of the agreement would go far beyond purely economic concerns. It has the potential to set worldwide standards. The successful conclusion of TTIP negotiations would be regarded as a benchmark for future free trade agreements.

The TTIP is not just a trade agreement, but also an investment agreement. Besides the extensive reduction of tariffs, the TTIP would also seek to lower non-tariff barriers to trade (such as technical requirements and standards, for example). This would make it easier for European and American companies to invest in the other economic zone, respectively.

Time plan

Concrete negotiations on the TTIP commenced on 16 July 2013. Originally, the negotiations were considered to be a no-brainer, and therefore ratification was initially expected in October 2014. However, resistance to the trade agreement has grown with every round of negotiations. At the present time, a ratifiable agreement is expected to be ready at the end of 2015, but even this date is now considered to be ambitious. German Finance Minister Wolfgang Schäuble (CDU) is only one of many who no longer believe that a final agreement can be reached by the end of 2015.

However, the negotiating parties are pushing for a speedier agreement, in view of the US Presidential elections in 2016, following shortly thereafter by the federal parliamentary elections in Germany, among others. No one wants to conduct negotiations against the backdrop of national elections because the sought-after agreement is too controversial politically. In the meantime, however, even this time plan is no longer considered to be realistic (as of early December 2014).

Criticisms

Many critics are particularly worried about the intended investment protection, as they believe that it would effectively circumvent democracy and the rule of law, because claims asserted by foreign companies against national governments

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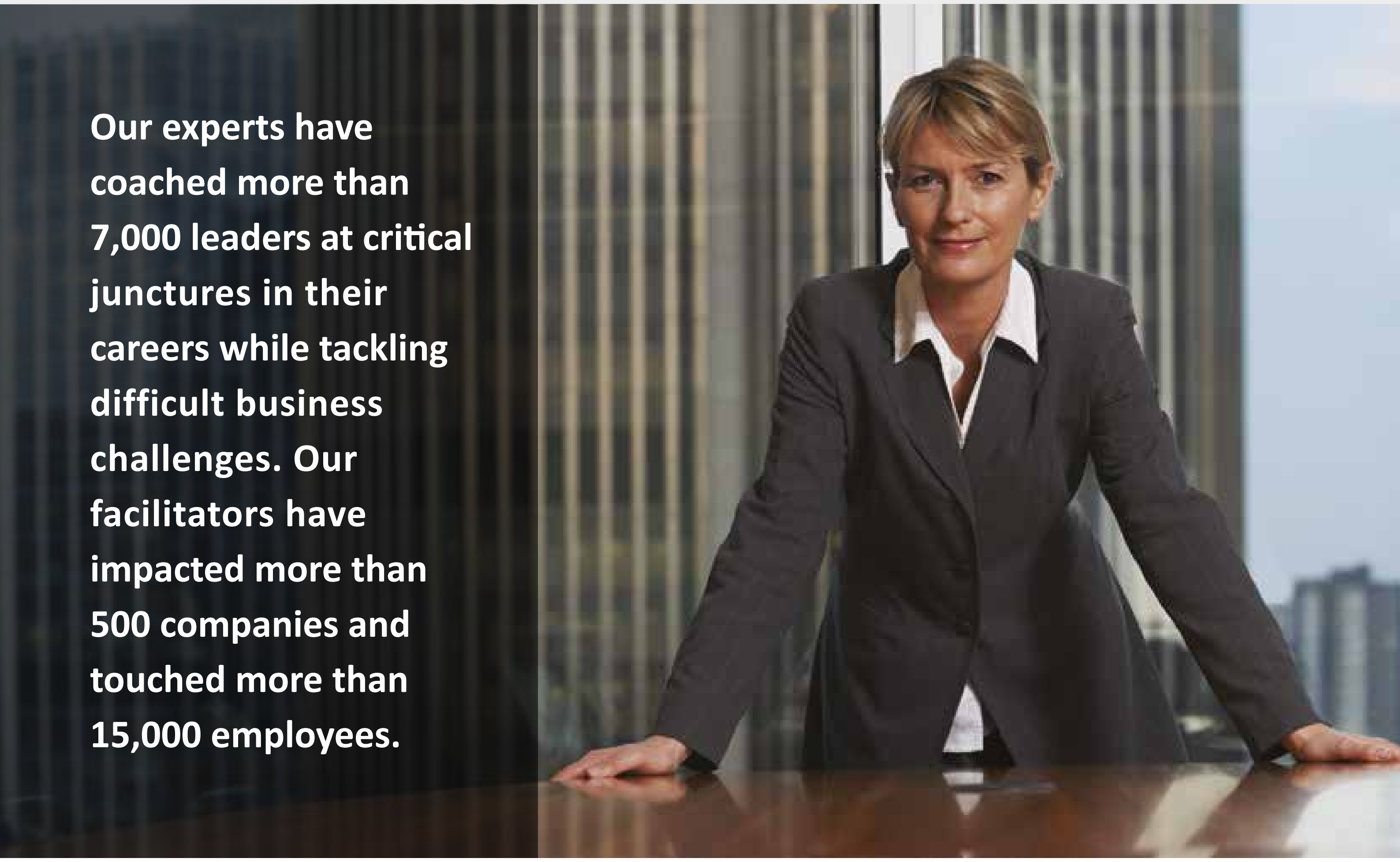

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"The successful conclusion of TTIP negotiations would be regarded as a benchmark for future free trade agreements"

would be settled by international arbitration tribunals, beyond the jurisdiction of European courts. As a result, so the critics claim, national governments would cede their sovereignty to industrial enterprises, at the expense of their citizens. If the agreement is found to have been breached, so they claim, the affected nation could be sentenced to pay high amounts of damages, which would be borne by taxpayers.

Another issue besides investment protection that provokes great anxiety is the food sector. Chlorinated chicken, genetically modified maize, and hormone-treated meat are only some of the sensitive topics that are invariably raised in press coverage of the TTIP. Such negative headlines have thrown some European and US citizens into a full-blown panic over the TTIP. Naturally, the highly sceptical nature of public debate has had the effect of slowing the negotiation process. The failure of this project would be a political disaster. Therefore, we will take a somewhat closer look at the various criticisms.

Another point of criticism involves the (insufficient) transparency of the negotiations. Critics feel that the exclusion of the public and the strict secrecy of the negotiation contents are undemocratic. In this regard, it certainly does not help that the EU Commission has praised the trade agreement as the most transparent in history.

Furthermore, critics take little comfort in the fact that a number of EU parliamentary delegates are allowed to view transcripts in reading rooms, or that position papers are published on the internet prior to each meeting of negotiating partners. Associations, companies, and NGOs have taken advantage of the opportunity to meet with the lead negotiators of both sides after each round of negotiations to learn more about the current status.

But critics are not placated by such arrangements. Although some details have leaked out in response to the growing public protest, the exact status of negotiations is supposed to be kept secret until ratification. However, the EU Commission has announced that the negotiating process will be made more transparent in the future, in that minutes of negotiation sessions will be made available to all EU parliament members and their aides.

On the subject of potentially weakened quality standards, the positions have hardened of late. The Europeans have no trust in the US food hygiene regulations, and the Americans do not trust the European standards for medical products. While it is true that the EU standards are stricter than the US standards in many respects, there are also areas in which the opposite is true.

Nonetheless, critics maintain that history has shown that the harmonisation that accompanies free trade agreements typically involves a weakening of standards. If the weakest or business-friendliest standard of any given country is adopted as the binding standard under the free trade agreement, that could unleash a downward spiral. The result would be cheaper, simpler, faster, but not necessarily better processes. Therefore, TTIP opponents are demanding the incorporation of a clause that guarantees the continued application of the highest standard in every case.

The so-called 'precautionary principle' is applicable in Europe. It states that no technology may be used if potentially harmful consequences cannot be ruled out with certainty. In the United States, the opposite principle applies: a product may be banned only if harmful consequences can be proven. Critics fear grave economic and environmental damage in Europe if this principle is weakened, because European consumer protection laws are naturally much more restrictive than those in the United States.

Trade between the European Union and the United States

In order to assess the significance and potential effects of a free trade agreement between the EU and the USA, the economic roles and current trade ties of these two regions should first be considered.

The EU and the USA are the two biggest economic regions in the world. Although their relative importance is diminishing somewhat as a consequence of the growing economic strength of other nations (such as China, for example), they still account for nearly half the world's economic output. Their proportional shares of global trade reflect the size of these economies. In 2013, the EU accounted for approximately 15%, and the USA for approximately 12.9% of total world trade. Furthermore, the EU is the most important trading partner of the USA, and vice versa.

In 2013, 16.8% of the foreign trade of the United States (including both exports and imports) was conducted with the EU, followed by Canada (16.4%) and China (14.6%). Conversely, trade with the USA accounted for 14% of the total extra-EU foreign trade of EU countries. The other important trading partners of the EU were likewise China, which accounted for 12.5% of extra-EU trade, followed by Russia and Switzerland (9.6% and 7.7%, respectively). In terms of absolute numbers, the EU exported goods and services worth about €447 billion to the USA in 2013, and imported goods and services worth about €342 billion from the United States. Thus, the EU generates a substantial trade surplus with the USA.[1]

The USA is also an important trading partner for Germany. Exports to the USA amounted to roughly € 90 billion in 2013, representing about 8% of the country's total exports. US imports to Germany amounted to nearly €49 billion.[2]

Structure of trade

In terms of sectors, industrial goods accounted for the lion's share of traded goods between the EU and the USA. In 2013, more than 80% of total exports amounting to €288 billion were industrial goods, leaving a relatively small share of agricultural goods. Exported services in the amount of approximately €159 billion were less than half as much as exported goods. Services are more important for the USA, accounting for €146 billion worth of exports to the EU, as compared to €196 billion worth of exported goods. Furthermore, the proportion of agricultural exports is somewhat higher for the USA.[3]

Considering the most important types of goods traded between the EU and the USA, one quickly notices that most trade is conducted in the same categories of products, which also represent similar proportions of the respective trade figures. Machinery and Transport Equipment are the biggest category by far, accounting for about 40% of the bilateral exports of the EU and USA in 2013.

The second-biggest category is chemical products, accounting for about 22% of bilateral exports in both cases, followed by other industrial goods and manufactured goods, and mineral fuels. The same ranking applies also to categories of goods traded between the USA and Germany, except that Machinery and Transport Equipment represent about 60% of German exports (USA slightly less than 50%). Chemicals represent 17% of the bilateral exports of both countries.

Openness of markets and barriers to trade

The currently high level of openness to trade is mainly reflected in the generally low tariff rates. In terms of sectors, both the EU and the USA levy the highest tariffs on agricultural products. The average tariff rate in the EU is 4.9% for agricultural products from the USA, while in the opposite direction the average tariff rate is 7.9%.

However, if one weights the average tariff rates by the volumes of traded goods, the tariff rate levied on agricultural products from the USA is only 3.9%, and the tariff rate levied on products from the EU is only 2.6%. The difference between the weighted and unweighted tariff rates can be seen at least partially as an indication of the trade-steering effects of tariffs. For industrial goods, the weighted average tariff rate is 2.8% for both the EU and the USA. The difference between the weighted and unweighted averages is less than in the agricultural sector. In this case, the tariff rates of around 3.5% are approximately the same.[4]

Higher tariff rates are levied on certain product categories, where they can have an even greater influence on trade. For example, the tariff rate for small trucks exported from the EU to the USA is very high, at 25%. In the opposite direction, the EU levies 22% on the same type of product. Furthermore, tariffs on specific agricultural products exported to the EU can range as high as 25%. The USA levies particularly high tariffs on clothing, textiles, and leather goods; these can be as high as 56%.[5] In such cases, a free trade agreement between the EU and the USA would make imported goods considerably cheaper. However, this particular detail could hardly be expected to appreciably stimulate trade, given the comparatively small quantities involved.

Non-tariff barriers to trade lead to higher costs, whether through the distortion of market prices or the necessity of maintaining duplicate organisations in manufacturing or permitting. However, it is difficult to estimate exactly what effects the elimination of some of these trade barriers and the related cost reductions would have on the overall volume of trade conducted between the EU and the USA. Furthermore, previous estimates related to the TTIP are often subject to criticism.

General assessment of the TTIP and conclusions

Abstracted from the technical and methodical details, therefore, the following statements can be made in relation to the economic assessment of the TTIP:

- The magnitude of macroeconomic effects will depend on the level of trade liberalization. Given the fact that trade is already highly liberalized, the marginal effect of further reductions of tariff-based and non-tariff barriers to trade would be minor, whereas the marginal costs in the form of modified standards that no longer completely satisfy specific social preferences can be expected to increase. Because trade between the USA and the European Union is already highly liberalized, the macroeconomic effects of the TTIP would be minor. The considerable openness of markets in both economic zones today already allows for the rapid transfer of technology advances. Thus, the dynamic growth effect would be somewhat weak.

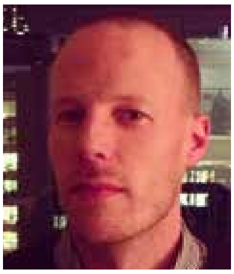
- The lower transaction costs that would result from the reduction of non-tariff barriers to trade would be equally advantageous for businesses and consumers, due to lowered market entry barriers, increased competition, and lower prices. A careful distinction must be drawn between the sensible reduction of genuine non-tariff trade barriers that represent a hidden form of protectionism, on the one hand, and the justifiable protection of consumer preferences by specific norms and standards, on the other hand.

- Rarely have the negotiations for a free trade agreement drawn as much public attention as in the case of the TTIP. That is good insofar as it has stimulated a broad public debate on the drafting of trade agreements and the negotiation process. The critical question involves the entity vested with the mandate to conduct the negotiations, and legitimacy of this decision. This question is particularly relevant within the EU, due to the perception that the legitimacy of decisions made in Brussels is very indirect, to say the least. After all, the transparency of the negotiations was enhanced and the influence of lobbyists was reduced only as a reaction to focused public attention.

- Besides the direct economic effects of the TTIP, proponents sometimes argue that the integration of these two economic zones to create a single trading block could strengthen the relative positions of the USA and Europe as the global economy evolves in the direction of a multipolar world order. In general, the creation of a single market encompassing the USA and Europe could play an important role in the development of norms and standards for the rest of the world, probably making it easier to enforce them, as opposed to weaker standards in a 'race-to-the- bottom' scenario. ■

This article is based on a new study: HWWI & Berenberg (ed.) (2015): Strategy 2030 – Free Trade. Download: http://www.hwwi.org/fileadmin/hwwi/Publikationen/Partnerpublikationen/Berenberg/HWWI_Freihandel_ANSICHT_ENG.pdf.

1. See European Commission (2014).
2. See Statistisches Bundesamt (2014).
3. See European Commission (2014).
4. See Gregosz/Walter (2013).
5. See Heinrich-Böll-Stiftung (2014).



TTIP and the digital economy

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The EU and the US are currently involved in negotiating the Transatlantic Trade and Investment Agreement, which would reduce trade barriers and hence facilitate trade between the two trading powers. This so-called mega-regional is at the outset an ambitious agreement that includes, besides custom duties, an extensive list that covers negotiating public procurement, market access in services and new rules and standards in energy, intellectual property, investments, plus regulatory cooperation.

These are just a few items with which negotiators on both sides of the Atlantic are dealing with. Since both trading parties cover large markets that represent around 60% of global GDP, TTIP could be marked as an important pact for the world economy. Especially as TTIP is proposed to go beyond the traditional trade barriers and large welfare gains are expected. Indeed, current costs of trading across the two trading entities are precisely to be found in the areas of regulation, rules and standards.

These beyond-the-border measures that affect trade are not new. Differences in regulatory procedures, standards and administrative requirements between countries have always existed. Yet, as a substantial part of traditional border barriers has declined worldwide over the years, the relative importance of these non-traditional trade costs, inducing regulations, has magnified. Research has in fact shown that the gains from alleviating these second-generation barriers can be manifold compared to goods.

This argument has also been put forward in a recent CEPR study commissioned by the European Commission. Especially if other countries would adhere to new transatlantic standards, benefits can 'spill-over' to the rest of the world prompting even greater welfare benefits. However, it remains to be seen whether this will truly be the case since negotiating these non-tariffs policies is a hard nut to crack due to many political economy considerations. And although a common transatlantic marketplace place will entail the largest market in the world, adhering to transatlantic technical standards also requires a political will.

Due to its proclaimed comprehensiveness, TTIP not only covers the regulations of traditional industries. It aims at setting global standards for new sectors, too. These newly emerging industries call for attention as novel regulations are put in place around the globe. One of these new areas of economic activity can crudely be called 'the digital economy'. The functioning of the digital economy stands or falls with the transfer and therefore by definition the trade of data.

This newly defined part of the economy covers various commercial sectors ranging from goods to services. For instance, it includes digital products such as ICT products and

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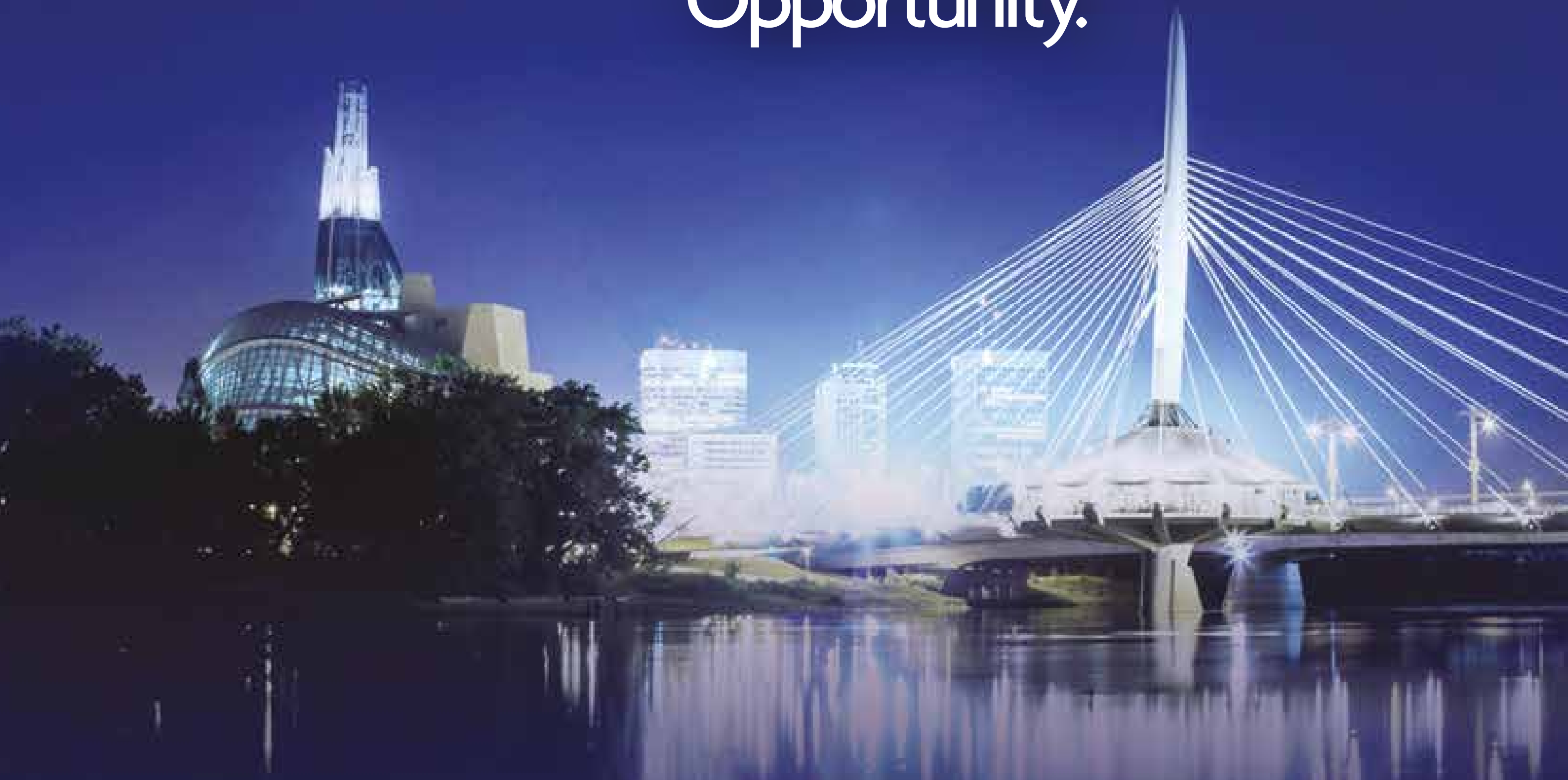

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"TTIP could be used as a good starting point for the new global digital economy"

semiconductors, pure cross-border data flows, online services such as the delivery of content over the internet, e-commerce, but also services sectors such as digital consultancy (eg. data processing, data storage or customer relationship management), software services, and traditional telecom services.

Most of these sectors are delivered through the use of a certain type of technology. And new regulations in this area is mostly focused on the utilization of this technology rather than in a sector. Consequently, when a regulation is put in place, the technological equipment cannot be employed and hence the data cannot be delivered, and therefore the service cannot be provided.

Due to the emergence of the digital economy the world economy has experienced a rapid and strong increase of flows in data, next to the existing flows in goods, capital and services. Many new companies in these sectors have production chains that are entirely based on data or have at least one essential element of their core business activity that is entirely dependent on the use of data. That in combination with the increased phenomenon of outsourcing and offshoring, trade in data is only to be expected to grow further.

Examples are manifold and include the transmission of employment data across departments for human resource purposes, the outsourcing of customer data for marketing campaigns, or the Internet banking activities outside the bank's country of origin for consumers and firms placed elsewhere.

In addition, there is a strong global trend towards intensified services production called servicification. This means that many new services are developed by goods firms as part of their manufacturing production process. Many of these companies utilize data as one of the core-elements in their business practises to deliver these services, which is also known as the internet-of-things (IoT). One famous example includes the automatic checking of large motors used by airplanes done by the producer. The data that is transmitted often flow across borders.

As one can see, the free flow of data plays a pivotal role in today's world economy. Very often data services affect indirectly the wider economy through their role as inputs into other sectors. It is therefore extremely important that these services markets become well regulated in an attempt to secure competition and to enable foreign suppliers to provide their services in an effective and efficient environment next to domestic suppliers.

Yet, regulation of data flows presents a relatively new feature in the broader spectrum of services regulation. It concerns rules on how data is utilised and processed by firms in the interaction between producers, but also between producers and consumers. Users can be exposed to the release of their (personal) data on numerous occasions, such as whilst executing financial transactions across firms, or during instances that can range from using social media to accessing healthcare services.

As in most other services sectors, regulation of the market is often required to prevent users from negative side effects caused by the ineffective organisation of the sector itself due to existing market failures. Various examples include asymmetrical information in financial services, as well as inefficient network systems in the telecom sector, or the existence of natural monopolies in the gas and electricity market. Although no formal type of market failure is yet described in data services, one major concern in the digital economy is said to be the potential failure of protecting the data of users that is stored and processed by producers. This might be seen as a form of asymmetrical information.

One regulatory policy that has proliferated around the globe is the legal requirement by governments for businesses to store data inside the country where the user is located, otherwise called data localization. It is a prominent example of a new sort of regulation that constrains the free flow of data across countries.

A number of countries are currently considering the implementation of new data localization laws (such as Brazil, the EU and India) whereas others have already implemented a variety of related regulatory policies (China, Russia and South Korea). Proponents of this law point out the fact that citizens are protected from illegitimate practises of the data by companies situated outside the host country.

Others state that with this law firms are not able to choose an appropriate location for the storage of the data, which ultimately results in higher costs for firms. Companies would like to send and locate data information there where countries can provide good conditions for storing such data. If this match cannot be made, higher trade costs are likely to be incurred by firms.

In the end, these costs negatively affect final consumers that use services and goods which are intensive in the usage of data. Besides, alternative types of regulations that aim to protect users are often put forward. One case in point is the consent requirement asking users permission to store and process user-specific data which one can give or refuse.

TTIP provides an opportunity to deal with these novel regulations in the digital economy. If both parties claim to negotiate an agreement that could set global standards and would include regulatory cooperation, it would be well-timed to deal with the secure yet efficient flow of data without needlessly exposing firms and consumers to any inefficiencies of excess regulation.

For most services, the challenge for policy makers is to find the right balance between developing necessary regulations that are linked to a particular social objective (stemming market failures) and implementing these regulations at a minimum cost in terms of economic welfare. By doing so regulators on both sides of the Atlantic must not create unnecessary costs for data users.

There are two additional reasons for TTIP to be a forerunner in setting sound data regulation standards. For one, no international organization currently deals with these matters. Since both the US and the EU currently hold one of the most important data producers in the world it would be logical if these two entities would start setting standards in this field. Furthermore, these regulations are often found in the realm of a country's domestic regulatory framework going beyond explicit trade barriers. Current FTAs in force are often precisely

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those which are used for dealing with non-traditional behind-the-border issues of which data localization is just one example. Hence, TTIP could further serve the interest of firms by including common measures on data regulations.

Traditionally, in the US lawmakers have relied on the concept of self-regulation for many business practises. In the EU, however, lawmakers have gradually implemented requirements regarding the processing and free movement of personal data. In many cases they prohibit the transfer of data based on the fact that other countries are unable to provide an equally secure level of data protection as defined by the EU. As far as flows between the EU and the US is concerned, a regulatory framework for dealing with transatlantic trade in data is currently in place, namely Safe Harbour.

Under Safe Harbour, the EU obliges US companies to fulfil a range of requirements that must be on an annual basis certificated by the US Department of Commerce. In practise this means that all companies based in the US have to provide strong administration and powerful IT systems which meet the various standards that the EU sets.

Further examples of rules that are included in Safe Harbour are the limitation of the use of personal data to a publicly announced purpose, or the exclusion of a third-party users that do not comply with the Safe Harbour criteria. Also, all affiliates must protect all data from losses, misuse and unauthorized access, disclosure, but also from data alterations and data destruction. Companies are furthermore required to fulfil extensive disclosure obligations concerning the practise of data and have to employ qualified staff for taking care of the handling of queries, complaints and data access requests.

In March 2014 the EU Parliament voted in favour of a comprehensive data protection law reform as a result of the Snowden releases. Thus, the future viability of Safe Harbour remains uncertain. As a result of this vote, the European Commission is currently drafting new rules with regard to the protection of data under the so-called General Data Protection Regulation (GPDR). This regulatory framework encompasses more than data localization alone, as it also deals with a battery of administrative hurdles such as the right for a consumer to have its data to be 'forgotten' or more extensive obligations for data controllers.

If put in place, these administrative measures could further increase the costs of doing business across borders. A study by ECIPE has indeed found that such measures decrease productivity thereby increasing prices in the wider economy. The reason is that many industries are dependent on services, which in turn are to a significant extent reliant on data as previously outlined.

It is still not clear what precisely the GDPR will entail. But, one strategy the EU could pursue is to regulate some of the trade-related data measures simultaneously in an EU and a transatlantic setting. This could provide a spring board for further data regulations across countries by setting a prudent and efficient precedent. This is also what the EU and the US are eventually striving for with the negotiations of TTIP: setting global standards. Today's trade patterns are marked by an ever slicing up of the value chain scattered around multiple countries.

As such, setting the smooth operation of services, data and technology across borders becomes essential so as to manage complex production-linkages at low costs, which can be passed on to consumers in terms of lower prices. What is needed therefore is an effective design and employment of regulations dealing with these data services inputs. TTIP could be used as a good starting point for the new global digital economy. ■

Why true free traders should push for a TTIP without investment protection

Sebastian Dullien is professor at HTW Berlin – University of Applied Sciences and Senior Policy Fellow at the European Council on Foreign Relations

Much has been written about the potential benefits of the transatlantic trade and investment partnership (TTIP) under negotiation at the moment. In Brussels circles, TTIP has long been hailed as a potential means to boost European growth in times of deep crisis and austerity without having to spend any additional euro from European or national budgets.

Opponents have rallied against TTIP. Civil society organisations have called the treaty a 'corporate power grab' and have started to mobilise resistance, which has resulted in more than 100,000 critical contributions to the public consultation process from citizens. According to some of the critics, TTIP will destroy jobs, lower incomes, and tie the hands of elected governments in regulate health, labour, and environmental standards – in fact, it will create a race-to-the bottom.

Upon closer examination, both positions are distorting the truth. Speakers from the European Commission often add up the potential benefits of TTIP over the 'working life of an


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"True free-traders should be able to see the political limitations of ISDS and, therefore, should aim for what is feasible – a limited TTIP with all tariffs removed and some harmonisation of standards, leaving open the potential for more in the future"

average household' in order to make the economic benefits look impressive. What is in effect quite a marginal increase in annual per capita GDP, 0.3 percent (in the case of the EU, this would amount to about €100 annually), can easily turn into a much more impressive €10,000 or greater, if one looks at a household of four and several decades of potential working history.

Civil society also overstates the anti-TTIP case. The rare studies that actually foresee a large number of jobs being destroyed or a drop in income rely on very specific assumptions and economic models and should be treated as outliers. Some safety regulations and standards from the United States are even superior to European standards. There is no indication that the harmonisation of standards would lead to a race-to-the bottom in European consumer protection.

However, the NGOs have a point when it comes to the hotly disputed investment protection provisions and the so-called investor-state-dispute settlement (ISDS) which is supposed to be included in the treaty. Some of the existing ISDS provisions in other treaties are so outrageous that it is easy to understand the claims of a 'corporate power grab'. ISDS usually allows companies to sue a government for compensation if they feel that they have been directly or indirectly expropriated. 'Indirect expropriation' can include all kinds of regulations that hurt a company's expected profits. Companies can usually sue without having to first go through the national court system.

Disputes are then decided by international arbitration panels. The dispute process is often criticised because panels are put together in an ad hoc fashion and it is possible for a panel member to have (quite recently) worked as a lawyer for the company concerned, or that s/he will represent the company shortly after the panel has ruled. And under many treaties, appeals are not allowed.

Also, ISDS provisions can create an uneven playing field between national and international corporations and can put small- and medium-sized companies at a disadvantage. Under ISDS provisions, international companies can resort to more advantageous international arbitration rules, while nationally owned companies have to go through the national court systems. Moreover, the legal cost of bringing a suit before international arbitration panels can easily run into millions of dollars, so they are not really an option for small- and medium-sized companies involved in a dispute about their (usually) small-scale investment.

Most ISDS provisions, while calling for 'fair and equitable treatment' for investors, do not define what a legitimate public interest is. Therefore, the panels are allowed a broad interpretation of when 'fair and equitable treatment' of an international investor is violated.

A number of recent cases have made headlines because they are seen as examples of a government's legitimate policy space to regulate being constrained. One prominent case is the suit brought by the tobacco company, Philip Morris, against the Australian government, which passed a law in 2011 banning the use of tobacco logos on cigarette packets. Philip Morris has also sued the Uruguayan government under a separate investment protection treaty after Uruguay increased the size of health warnings legally required on cigarette packaging.

Critics of the ISDS system claim that even if awards in favour of big corporations are not granted, policymakers' fear of them can lead to 'regulatory freeze'. As an example, they cite New Zealand, which ditched plans to follow Australia in limiting tobacco logos on cigarette packages after Philip Morris claimed damages against the Australian government.

It is often claimed that all these issues could be remedied by wording ISDS provisions carefully, by making procedures more transparent, and by changing the rules for panel appointments and proceedings. However, it is highly questionable whether such measures could really solve the problem.

The Canada-EU Comprehensive Economic and Trade Agreement (CETA), for example, is often referred to as a potential blueprint for TTIP rules. But CETA still defines investment very broadly, including bonds and bank deposits in the definition. Including these instruments risks severely limiting policy space in the future. For instance, if bonds were included in investment protection provisions, debt restructuring like that involving Greece in 2012 would be problematic, even if the agreement tries to carve out exceptions for orderly debt restructuring.

Even an agreement like CETA does not create firm and clearly defined rules that strike a balance between the interests of investors and the host country's legitimate interest in public regulation. Instead, CETA relies on a broad 'fair and equitable treatment' clause.

As compared to national law, provisions in recent treaties still tilt the balance of power away from governments and towards global corporations. For example, the German constitution includes a clause protecting private property. In cases of expropriation, the constitution calls for compensation. This compensation must take into account the private owner's interest as well as society's legitimate interests. The compensation principle in CETA is different: under the treaty, compensation is set based on the market value of lost profits – which constitutes an absolute investor protection without any concern for the public interest.

Of course, in principle, one could reform these rules further to make them closer to something that could be sold to the general population as being fair and compatible with democracy as they know it. The German minister of economics and chairman of the Social Democratic Party, Sigmar Gabriel, has introduced a proposal calling for setting up a formal 'investment court' with a permanent secretariat, professionalised judges, and the potential for appeal.

However, it is not clear whether these ideas can be implemented in practice and especially whether they could be realised in time to get TTIP through the US Congress before the start of the next presidential election campaign. First, what constitutes a justified regulatory step (one that would not warrant compensation even if an investor's profits were hit) would have to be defined in

detail. To date, this has never been done. Secondly, investment protection treaties are extremely complicated legal documents. It can easily happen (and it has often happened in the past) that wording slips through that later allows clever corporate lawyers to exploit a well-intentioned treaty. And unlike national law (in which things like this also happen regularly), a treaty cannot be easily changed by a vote of parliament.

At the same time, it would be a pity to see TTIP failing completely or being delayed indefinitely. While the overall effects of any conceivable transatlantic trade agreement are rather small, they might be substantial for single countries and single sectors. It is true that average tariffs in transatlantic trade are below 3 percent. Yet, due to their very different economic and export structures, some EU countries face very high tariffs on their top exports.

For example, while tariffs on Bulgaria's top exports to the US – mainly tobacco – average more than 10 percent, tariffs on Luxembourg's average a mere 0.28 percent. Even between countries with similar per capita incomes, existing rates of tariffs are quite different: while tariffs on France's exports average 0.69 percent, tariffs on Germany's average 1.65 percent; whereas tariffs on Portugal's exports (which include bed linen, on which there are tariffs of up to 20 percent) average 4.62 percent, tariffs on Slovenia's exports average only 0.66. Abandoning TTIP completely would mean preventing some of the crisis countries from gaining a much-needed export boost through higher sales to the US.

The logical solution would be to give in to the NGOs and ditch the ISDS provisions from the TTIP negotiations. It could always be revisited later by negotiating a bilateral – or even multilateral – investment protection agreement with sensible rules, setting up a standing international court for investor-state-disputes.

This strategy would also make sense because the actual economic effects from including ISDS into TTIP can be expected to be very close to zero. Economic literature struggles to find any significant effect of investment protection treaties on actual investment flows. In the case of transatlantic investment flows, the effects can also be expected to be extremely low to non-existent because of the fact that in both the EU and the US, the rule of law is strong and the judiciary is independent – so that most experts reckon that they really do not need investment protection between them.

One argument made by proponents of including ISDS in TTIP is that it would improve the bargaining position with regard to China, which so far has been very careful on the wording of investment protection treaties that it is prepared to sign. However, this argument is not entirely convincing. Why should China change its position of carefully protecting its own economic interest before signing an investment protection treaty just because the US and the EU have signed a bilateral deal?

Free-traders in Brussels are also voicing concern that giving in to NGOs' demands of scrapping ISDS in the transatlantic negotiations would hand them an easy victory and just give them an incentive to move on to fight against the next aspect of TTIP, until they have succeeded in dismantling the entire negotiation process. According to this narrative, it is better to hold the ground on ISDS and only budge as a final option.

This political economy argument seems questionable, though. There are real, not just perceived problems with ISDS. Simply trying to ignore the NGOs' concerns will not convince the public once it has been alarmed. Including ISDS in the treaty negotiation guarantees a permanent rallying point for NGOs. Already, the inclusion of ISDS in the TTIP negotiations has caused a public outcry never experienced in Europe before in the discussion of any trade agreement. It is safe to assume that, had TTIP been limited to the removal of tariffs and other conventional trade barriers, only a very small share of the population would even know what TTIP is.

To put it more bluntly: if you are against transatlantic free trade, the best way to prevent significant liberalisation is to insist on the inclusion of ISDS in a TTIP agreement as a sine-qua-non. True free-traders should be able to see the political limitations of ISDS and, therefore, should aim for what is feasible – a limited TTIP with all tariffs removed and some harmonisation of standards, leaving open the potential for more in the future. ■

Cents and sensibility: disputing the TTIP

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The Transatlantic Trade and Investment Partnership, a proposed trade, investment and regulatory deal between the European Union and the United States, has become emblematic of the increasingly polarised debate between proponents and critics of so-called globalisation. The size of the combined EU and USA economies - which together account for 45% of global GDP, or 40% in terms of purchasing power - makes the scale of the proposed agreement of major global significance. Furthermore, the scope of the proposed TTIP - covering multiple issues of market access, regulatory cooperation and rules - is notably broad. Therefore it is perhaps unsurprising that the proposed TTIP, drafts of which have been leaked to the public, has elicited considerable public debate. Such disagreements range from the potential economic value of the agreement to the way in which negotiations are being conducted.

One of the aspects of the TTIP that has elicited particular controversy is the proposed chapter on investment protection, which may include an Investor-State Dispute Mechanism (ISDS) for settling disputes through international arbitration. Under ISDS, qualifying international investors can commence international arbitration proceedings against the state hosting their investments for violations of substantive standards of protection, such as the uncompensated expropriation of their investment or unfair and inequitable treatment.

Between March and July 2014, the EU Commission held a public consultation on investment protection and ISDS in the TTIP, which culminated in its publication of a Report in January 2015. In its Report, the Commission highlighted the following areas for further development: (1) the protection of the right to regulate; (2) the establishment and functioning of arbitral tribunals; (3) the relationship between domestic judicial systems and ISDS; and (4) the review of ISDS decisions through an appellate mechanism.

At the macro level, the Commission reaffirmed in its Report its objective of achieving *"the right balance between protecting investors and safeguarding the EU's and member states' right and ability to regulate in the public interest."* This balancing act appears designed to meet some of the criticisms of ISDS and investment protection, while affirming the important role that ISDS can play in resolving investor-state disputes.

This article provides a brief overview of three issues: (1) the international framework for ISDS and investment protections; (2) the role of ISDS to resolve investor-state disputes; and (3) the fact that states, not investors, determine investment treaty standards.

Investment protection within international investment law

The large number of consultation submissions received by the EU Commission that were critical of ISDS and investment protection might be taken to suggest that they are novel innovations in international law. In fact, an investment chapter in the TTIP would sit within an established international framework of investment treaties and free trade agreements.

The era of modern investment treaties began with the signing of the first bilateral investment treaty (BIT) between Germany and Pakistan in 1959. Since then and alongside the increase in global trade and investment flows, investment agreements between states have proliferated. Indeed, there are now reported to be well over 3,000 international investment treaties between states. Whilst the majority of these agreements are bilateral, investment agreements have been included in a number of multilateral treaties, such as the Energy Charter Treaty (to which the EU is a party). Investment chapters have also been included in many free trade agreements (FTAs). For example, Chapter 11 of the North American Free Trade Agreement (NAFTA) between the USA, Canada and Mexico contains both investment protections and ISDS, in addition to trade provisions.

Investment treaties typically provide substantive standards of protection for qualifying foreign investors (such as a right to compensation in the event of expropriation of their investment). In addition, the vast majority of investment treaties provide qualifying foreign investors with a right to commence international arbitration against the host state of their investment for breaching those substantive standards. Accordingly, while an investment chapter in the TTIP along these lines would be a significant development, not least given the role of the EU, it would not be unique. Rather, it would take its place alongside the numerous other investment agreements currently in force in the international legal system.

ISDS to resolve investor-state disputes

The role of ISDS to resolve investor-state disputes is a different issue to the scope of investment protection standards in treaties. This section addresses the former issue and the following section addresses the latter.

The provenance of modern international arbitration as a means of resolving international disputes is frequently traced back to the Jay Treaty of 1794 between the United States and

Great Britain. Significantly, that treaty created mixed Anglo-American arbitration commissions to resolve both state-state disputes and disputes between individuals and states. As such, it was an important precursor to the ISDS provisions in modern investment treaties. Notably, ISDS is now a characteristic feature of the vast majority of investment treaties, with the OECD estimating that over 90% of existing BITs contain ISDS provisions.

While apparently proposing to maintain ISDS as a feature of the TTIP, the EU Commission has expressed its intention to refine it in certain respects, as compared with existing prevailing practice. For example, the EU Commission has stated its desire to enhance transparency in international arbitration under the TTIP. While arbitrations are generally confidential, the recently promulgated UNCITRAL Rules on Transparency in Treaty-based Investor State Arbitration of 2014 are a potentially significant milestone in enhancing transparency in ISDS that the EU Commission has endorsed. Canada is a leading proponent of transparency in ISDS and tries to ensure that key documents submitted to, or issued by, investor-state arbitral tribunals in disputes to which it is a party are made publicly available, as well as pressing for arbitral hearings to be made open to the public. The EU has made similar proposals regarding ISDS in the TTIP.

The EU Commission has also expressed its interest in the possibility of establishing an appellate mechanism for ISDS arbitral awards under the TTIP. In doing so, the EU is weighing in favour of enhancing the consistency of rulings, as compared with their finality.

In general, a party wishing to challenge an arbitral award is limited to a challenge in the national courts of the seat of arbitration or, in the case of ICSID (World Bank) arbitrations, by means of the ICSID annulment mechanism before an ICSID ad hoc annulment committee. One of the reasons behind the general lack of an appellate process in arbitration is to ensure finality of arbitral awards and facilitate the timely resolution of disputes. Nevertheless, the TTIP parties are free to agree on a different system for challenging arbitral awards and the EU Commission appears intent on doing so. Such an approach has been anticipated in other investment treaties. For example, the US-Chile FTA 2003 provides for the possibility of inserting an appellate mechanism for ISDS arbitral awards.

While addressing issues such as transparency and the question of appeals for ISDS arbitrations, the EU Commission appears to maintain its support for ISDS in the TTIP. This is notable since in the absence of ISDS, foreign investors may, for all practical purposes, be limited to seeking recourse against a host state in its own courts. This is seldom the preferred option for an aggrieved investor, not least since a sovereign state includes its judiciary (as well as its executive and legislature) as a matter of international law.

Absent ISDS rights, the investor could also seek (having previously exhausted local remedies) to persuade its home state to commence negotiations and proceedings if necessary against the host state of the investment. This is known as 'diplomatic protection'. One of the limitations of diplomatic protection is that it is within the home state's discretion whether or not to bring a claim on the investor's behalf. That can leave the investor beholden to an unpredictable political process beyond its control. Significantly, the home state of the investor may have no wish to engage in a dispute with another state for any number of geopolitical or economic reasons unrelated to the investor's claim.

"Notwithstanding some public suggestions that ISDS in the TTIP would only benefit US investors, it is notable that six of the top ten home states for investor claims are EU member states"

Some of the shortcomings of diplomatic protection were demonstrated in the *Barcelona Traction* case before the International Court of Justice (ICJ) between Belgium and Spain. This case concerned a Canadian corporation which operated light and power utilities in Spain and was based on the allegation that Spain had violated a number of its international obligations. Canada ultimately chose not to bring a claim at the ICJ, although Belgium agreed to do so as 88% of the company's shareholders were Belgian. However, the ICJ held in its 1970 Judgment that Belgium had no legal interest in the matter as it was the company's rights which had been infringed and the company was Canadian. Whatever the reason for the Canadian government's decision not to pursue the claim, this did not justify the exercise of diplomatic protection by another government. Notably, this decision and the limitations of diplomatic protection have been a key driver in the emergence of ISDS provisions in investment treaties. Furthermore, one of the benefits of ISDS as compared with diplomatic protection is that it can help to depoliticise disputes.

Accordingly, investors will generally prefer international arbitration to resolve disputes with host states as compared with recourse to the host state's courts or diplomatic protection. Among other benefits of arbitration, the investor and the host state can participate in the constitution of a non-affiliated arbitral tribunal which has experience of international investment law issues.

States determine investment treaty standards

Some of the criticism of ISDS appears to overlook the fact that it is states, not investors, who determine the scope of investment treaty standards. As a matter of international law, states can define protection standards as they wish within a treaty and create qualifications and carve-outs, for example related to public health and environmental measures. For example, Article 12 of the US Model BIT explicitly recognises the importance of environmental regulation and provides that *"The Parties recognize that it is inappropriate to encourage investment by weakening or reducing the protections afforded in domestic environmental laws."* The EU Commission is proposing to address the scope of application of the TTIP and the parameters of certain substantive standards in that agreement, such as the fair and equitable treatment standard and indirect expropriation. Notably, the recently negotiated EU-Canada Free Trade Agreement (CETA) provides greater specificity on the meaning of standards such as fair and equitable treatment and indirect expropriation in that agreement than is typically found in most BITs.

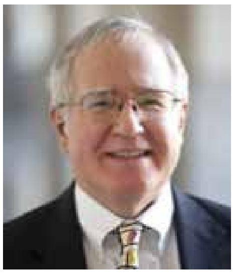
The key point here is that the TTIP negotiating parties can mould substantive provisions in the TTIP into the form they want. There is no restrictive formula of substantive standards that must necessarily be included in any investment treaty.

Conclusion

Notwithstanding the controversy surrounding ISDS in the TTIP, it is far from evident that proposed alternatives such as using local courts as the exclusive forum for investor claims against host states, and a return to diplomatic protection would be a panacea to replace arbitration of investment disputes. As regards substantive protection standards, it is notable that states, not investors, determine them in their treaties.

A frequently overlooked aspect of ISDS and investment protections is that they are reciprocal. As such, they apply to investors of both parties. Notwithstanding some public suggestions that ISDS in the TTIP would only benefit US investors, it is notable that six of the top ten home states for investor claims are EU member states. Furthermore, they are reported to have collectively brought more ISDS claims than US investors in the last 30 years.[2] The mutuality of ISDS and investment protections might therefore suggest that there is a role for both cents and sensibility as the EU Commission looks to open a new consultation on the TTIP in 2015. ■

1. This article does not reflect the views of Withers LLP or its clients.
2. Prof. Dr Christian Tietje and Prof. Dr Freya Baetens, "The Impact of Investor-State-Dispute Settlement (ISDS) in the Transatlantic Trade and Investment Partnership": Study prepared for the Ministry for Foreign Trade and Development Corporation, Ministry of Foreign Affairs of the Netherlands (24 June 2014), p. 26.



North America in the world of trade

Kent H Hughes is a Public Policy Scholar at the Woodrow Wilson International Center for Scholars

Building a competitive North America

What should North America do? Can three close neighbours with their own economies and traditions find a cooperative way to drive their collective competitiveness?

The simple answer is yes - but not in a way that ignores North America's deep ties to the global economy, other international agreements, or the reality of global businesses that cross multiple borders.

North America in economic terms

As an economy, North America is big, active, and growing. Together Canada, Mexico, and the United States have a combined population of some 474 million, 23% percent of global gross domestic product, and some 12.85% percent of world exports. Adding Central America and the Caribbean - both heavily integrated into the regional economy, would simply add to the totals.

In terms of innovation, the United States continues to stand out as world leader in terms of patents and in world changing innovations - think of the internet, Google, Apple, and a proliferating range of social media. Canada is also heavily committed to innovation, investing some 1.73 percent of GDP in research and development. At 0.43 percent of GDP (2011), Mexico currently lags behind its North American neighbours, but has a growing commitment to developing its own innovative capacity[1]. In the future, the world will see Mexico devoting more resources to research and development, increasing its emphasis on STEM (science, technology, engineering, and mathematics) degrees, and sending more Mexicans abroad to acquire a science or engineering education.

In terms of economic independence, North America has ample energy resources. Canada continues to innovate in the development of its oil sands - reducing the environmental impact and raising efficiency. Mexico has taken major steps to open it oil industry to greater competition and has potential reserves in the Gulf of Mexico and as yet unexploited shale oil and gas deposits in its North. The biggest surprise is the United States, which, through new technologies, has been able to develop major shale oil and gas deposits. Although recent development has slowed in response to the sharp drop in oil prices, the American outlook for hydrocarbon supplies is bright. At the same time, the United States is continuing to push for regulations to reduce carbon emissions - a force that is already driving innovations that range from the attempt to use carbon fibre panels in everyday automobiles to boosting the efficiency of solar panels.

In the manufacturing sector, there is already a good deal of interdependence. Cars and auto parts flow regularly across North American borders. US-based manufacturing companies are heavily invested in Canada and have increased their investments in Mexico. Service industries are also increasingly integrated with Canadian banks taking a more prominent role in the wake of the 2008 financial crisis.

How competitive is North America?

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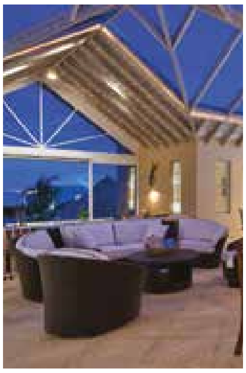

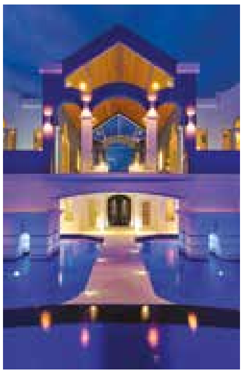

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"In taking a regional approach to investment and trade as well as education and innovation, Canada, Mexico, and the United States could set examples that other regions could pursue to their own economic and security advantage"

infrastructure, increase support for research and development, make the right choices on education, and support their respective manufacturing sectors, North America could develop into even more of a competitive force.

North America must keep its eye on the rest of the world. Competition has become a truly global game. Fluctuating exchange rates can affect import and export decisions as well where to put a new manufacturing plant. International competitors are not standing still. As an example, China is installing robots and moving up the value chain as rising wage rates put pressure on low wage, export-dependent industries. Around the world, countries are putting added emphasis on education and innovation.

Along with much strength, each of the North American economies faces its own set of challenges. In 2015, the United States is still experiencing the lingering effects of the Great Recession. While the unemployment rate has fallen below six percent, millions of Americans have simply left the workforce. Nor have wages risen. Gains from productivity have been concentrated in the upper 10 percent of the income scale. While the United States is home to many of the world's top research universities, it has mixed results in its K-12 schools. On average, Canada does considerably better but Mexico also lags in terms basic education. In addition to added pressures on the federal budget from an aging population, the United States has yet to deal with large and persistent trade deficits.

North America in the world economy

In a world of global supply chains, international trading rules, and proliferating bilateral free trade agreements, does it even make any sense to think of regional blocs? The short answer is yes, but not at the expense of ignoring forces that will continue to drive global, economic integration.

Science has long been a largely global phenomenon and technology is now following. Major countries that are historically based in the advanced industrial countries are increasingly global in their operations and their thinking. For example, the German company Siemens and the Dutch company Phillips both have major operations in the United States. IBM currently has more employees in India than in the United States. Global auto makers from Europe, Japan, Korean, and soon, China are deeply involved in North American manufacturing, sales, and even exports.

The world of trade is now an intricate web encompassing regional and bilateral free trade agreements that complement or, some would say, complicate the global trading system. Free trade agreements often contain different rules of origin, creating supply management challenges for global companies. North America is already party to a number of trade agreements. Canada, Mexico, and the United States share the North American Free Trade Agreement and are actively involved in the Trans Pacific Partnership trade negotiations, an effort that also includes countries from South America and Asia. Mexico has a free trade agreement with the European Union and Canada has made a similar agreement with the EU. The United States and the EU are in the process of negotiating the Trans-Atlantic Trade and Investment Partnership that promises to go well beyond existing free trade pacts.

China is an important trading partner of all the North American countries as is the European Union. As major commodity exporters, all three economies are tied to global markets. Asian supply chains are closely linked to North American manufacturers. The three economies look abroad for rare earth minerals and other critical supplies.

Why then talk about a North American economy at all?

There are three reasons. <u>First</u>, strengthening and rationalizing existing ties will foster <u>productivity growth and stimulate innovation</u>. At present, there is little cross border discussion about how improved infrastructure links could make the three economies more competitive. As Mexico works to make its economy more innovative, increased ties with American centres of innovation and America's tier-one research universities makes very good sense. Through innovation, cooperative regulations, and future oriented incentives, intra-North American cooperation can help build a bridge to a low carbon future, secure ocean resources, and preserve water supplies. Working with Canada and Mexico, America's capacity for innovation could be harnessed to develop solutions for shared economic, environmental, and resource-based challenges.

<u>Second</u>, the relative <u>independence</u> of North America in terms of <u>energy, commodities, and agriculture</u> has implications for <u>national security</u>. Memories of 1970s oil embargos and supply interruptions still influence US energy policy. Some oil exporters have used their oil and gas supplies for geopolitical as opposed to strictly economic purposes. Saudi Arabia used the oil weapon in the 1970s. Russia has sought to use its oil and gas resources to influence European powers and, most recently, Ukraine.

The sharp drop in oil prices in the 1980s reflected a Saudi Arabian strategy that may have targeted both the Soviet Union and America's Synfuels Corporation, an early effort to develop America's shale-based resources. Today's low oil prices reflect US production, but also Saudi interest in putting pressure on oil producing rivals and discouraging further shale oil and gas production in the United States as well as its determination to build market share in Asia.

<u>Third</u>, Canada, Mexico, and the United States have a <u>shared future</u>. They are <u>all democracies</u> that support similar values around the world. They are all working to respond to the risk of international terrorism. Despite efforts at border control, thousand mile long borders and extensive coastlines make cooperation in security essential. Economic ties can help build closer political cooperation.

North American competitiveness and the WTO

Will greater North American cooperation and integration undercut the WTO? No. Looking back at an older set of economic blocs that limited or distorted trade ignores the whole competitiveness approach. By Competing through investing, innovating, and educating, North America will drive progress not protectionism.

Jagdish Bhagwati, a prominent international economist, is a leading critic of the proliferation of free trade agreements. In his view, they are creating a spaghetti bowl of trade ties that complicates global economic relations and undercuts the World Trade Organization. As free trade agreements have spread to Asia, some economists have identified a second dish, a noodle bowel that adds further strands to an already complex web of trade relations.

There is another view. Started in 2011, the Doha Round of Multilateral Trade Negotiations has not yet been completed. Sadly, even selected pieces of the negotiations have not yet been made final. In addition to the intricacies of global trade negotiations, any final agreement must be agreed to by all of the 160 members of the World Trade Organization. Current tensions between Russia and the West coupled with East and South East Asian geographic rivalries make reaching a consensus on broad trade agreements even more difficult.

Outside of the multilateral negotiations, progress has been made. In contrast to the go-slow Doha Round, twenty-nine countries signed an Information Technology Agreement in 1997 covering a wide array of high-tech products. Over time, the agreement expanded to forty-six members. Current negotiations are intended to update the agreement and incorporate new members. Again there are signs of progress. In November of 2014, the United States and China reached an agreement on China's membership. The ITA agreement is overseen by the WTO.

In parallel negotiations, the Trade in Services Agreement (TISA) is designed to build on the 1995 General Agreement in Trade in Services (or GATS). It is another example of a sector specific initiative that could broaden international trade. Sectoral agreements do reduce pressures for multilateral negotiations, but they also create new rules that can inform a future global approach.

Toward a North American strategy

What should North America do? Can three close neighbours with their own economies and traditions find a cooperative way to drive their collective competitiveness?

In looking for common strengths, the North Americans cannot ignore either the diversity of the three countries and three economies or their common problems. The global shift toward inequality applies in different degrees to Canada, Mexico, and the United States. The Mexican south lags behind a rapidly growing Mexican north. The United States mixes a world leading set of universities with a K-12 system that ranges from outstanding to, at times, failing. History can always be a factor.

Canada and Mexico have some long standing questions about their American neighbour. If Americans ask their northern neighbours to define a Canadian, they are still likely to hear, 'we are not Americans.' In thinking about Mexico, it is still important for Americans to remember the much quoted phrase of the long-serving Mexican president, Porfirio Diaz. *"Poor Mexico"* he said, *"So far from God, so close to the United States."*

But the potential for building North American trade and competitiveness should not be held hostage to history. In fact, North America is already looking to a cooperative future. In 2014, the Council on Foreign Relations (CFR) released a report *North America: Time for a New Focus* that contained an ambitious agenda for North American cooperation on everything from cyber security to education.

The report calls for specific North American desks at the National Security Council and the Department of State to make sure that there was a clear eyed focus on North America when the United States is setting its global policy. To identify current or potential areas of cooperation, the CFR task force also proposes *"designating a senior US official as the North American 'champion' who will press for consistent policies across agencies and topics."* Sceptics will note the problems of past efforts in promoting cross-administration cooperation. President Obama's first term experiment with a series of in-the-White House czars has now faded. Coupling the high-level champion with a congressional requirement for an annual or even biennial report on how policies reflect that shared potential of North America would create periodic pressure for any administration to think in North American terms.

One measure of the scope of their visions is the call to develop a regional education and innovation strategy. The latter would include the creation of a 'North American network of laboratories for basic research. American, Canadian, and, in practice, researchers from around the world share developments in basic research.' In recent years, Mexico has been moving to further develop its own capacity for innovations. As an example, last year the Woodrow Wilson Center's Mexico Institute hosted a group of Mexican legislators who were looking at the current US innovation system for initiatives that could be adapted to the Mexican system[2].

In December of 2014, the Canadian Council of Chief Executives published *Made in North America: A new agenda to sharpen our competitive edge.* The report includes a list of 35 specific steps to improve North American competitiveness. The list ranged from infrastructure to improved customs procedures to cooperation in defining job skills.

In addition to the proposals of the Council on Foreign Relations and the Canadian Council of Chief Executives, the three countries could take on a shared effort to respond to specific regional problems that range from transportation blockages to water use to adopting on-line education. In a similar vein, they could explore regional aspects of global challenges such as possible flu pandemics or natural disasters.

Conclusions

America's size, dynamism, and global engagement have often led Americans to take their neighbours for granted. Yet shared interests and the potential for added growth make a compelling case for thoughtful cooperation. The three countries of North America have a clear shared interest in regional security, improved education, and an ambitious innovation agenda. In taking a regional approach to investment and trade as well as education and innovation, Canada, Mexico, and the United States could set examples that other regions could pursue to their own economic and security advantage. ■

1. Figures are from the World Bank, 2012
2. See Fostering Innovation in Mexico: Ideas from the High-Level Innovation Forum for Policymakers 2014

A tale of two worlds

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Latin America is splitting down the middle. Along its eastern coast, the Mercosur trading bloc and customs union, which comprises Argentina, Brazil, Paraguay, Uruguay and Venezuela, sports a fairly strong protectionist tilt. Along the western coast, the *Alianza del Pacífico*, which includes Chile, Colombia, Mexico, Peru and, soon, Costa Rica, goes for total openness. Which bloc shows the most promise?

Both blocs are the culmination of more than a century of efforts to foster economic regional integration. At first sight, Latin American nations should have several advantages over other areas, such as the European Union, that have eventually managed to overcome national instincts to form a common market: shared heritage, culture, the same dominant religion, and vast natural riches. Fruitful economic and political cooperation would appear all but assured.

Alas, it has not quite worked out that way. Ill-conceived economic policies, mutual distrust and the occasional strife have led to backwardness and a permanent trailing position for Latin America in the global development league.

The forerunners

To overcome this economic backwardness, Argentina, Brazil, Chile, Mexico, Paraguay, Peru and Uruguay launched the Latin American Association for Free Trade (ALALC, in its Spanish acronym) in 1960. Twenty years later it became the American Association for Integration (LAIA or ALADI), with the inclusion of Colombia, Ecuador, Bolivia and Venezuela. Panama and Cuba joined later on.

ALADI never lived up to its stated goal of *"…creating an area of economic preferences with the final objective of establishing a common market in Latin America."* But it has at least served as an instrument for the exchange of trade preferences between member countries under the framework of the so-called *Acuerdos de Complementación Económica* (Economic Complementation Agreements), most of which are currently in place.

A further effort was Andean (or *Comunidad Andina de Naciones*, CAN, in its Spanish acronym). Established in 1969 by Bolivia, Chile, Colombia, Ecuador, and Peru and later joined by Venezuela, its main objective was to create a single economic space where goods and services could flow freely amongst its members, while erecting a common external tariff to protect them against foreign competition. This meant that in practice it ended up replicating the industrial policies of individual members that still adhered to the tenets of import substitution.

Furthermore, the member countries pursued conflicting economic policies that included central planning for various industries, such as petrochemicals, steel, automobiles, and chemicals, among others. While it did manage to adopt one set of common rules, for the treatment of foreign direct investment (FDI), it unfortunately was of a markedly discriminatory nature.

Despite its commitment to erecting a protective common external tariff, innumerable negotiation rounds failed to bring agreement on the criteria for establishing it. And while it proclaimed many commitments to lowering inter-member tariffs towards the establishment of a free trade zone, these were systematically torpedoed by delays or went routinely unfulfilled. By the mid-1970s Chile, engaged in a general liberalization of its economy, voiced severe objections to its partners' views on tariff levels and the treatment of FDI. These objections ended with Chile leaving Andean in 1976.

The above notwithstanding, Andean has been able to survive as an institution, but has been vastly debilitated, particularly after Colombia and Peru started to adopt many liberalizing policies that adhered to the so-called 'Washington Consensus'. When these two countries announced that they intended to negotiate a free trade agreement with the United States, Venezuelan President Hugo Chávez was so enraged that he decided to pull Venezuela out of Andean in 2006; he later made it join Mercosur. Bolivia, in turn, despite its similar misgivings about Andean, decided to stay in, but also to pursue a membership in Mercosur, to which it is ideologically closer.

Surprisingly, in light of the above setbacks, Andean was able to put into effect a free trade zone (FTZ) of sorts in 2005, although ditching the idea of a customs union with a common external tariff. It also developed a vibrant and successful financial arm, the Andean Development Corporation (CAF).

Mercosur

The *Mercado Común del Sur*, Mercosur, came into being in 1985, with the signing of the Argentina-Brazil Integration and Economics Cooperation Program, and became formally established in 1991 by the Treaty of Asunción. Fairly ambitious on paper, it not only aimed at promoting free trade and the free movement of goods, people, and capital, but even posited a common currency and a common parliament. The currency never came around, but the other goals have been attained, at least in part.

The large domestic markets of Brazil and Argentina have allowed the five-member Mercosur, with a total population of 300 million and an aggregate GDP of approximately US$3.2 trillion, to build an important trading bloc, albeit relatively closed to the rest of the world. Its external tariff affords substantial protection against imports from non-member countries, but allows member countries waivers from applying

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the common external tariff schedule on a number of tariff lines corresponding to 'sensitive' products.

Most of the hurdles encountered by Mercosur are the same ones that thwarted Andean: the attempt to create a trading bloc conceived as a fortress against competing third-country imports, compounded by an inability to coordinate macroeconomic policies and by recurring periods of domestic economic crisis and external economic shock. In addition, over the years their various member countries have substantially altered their economic models.

For example, Argentina adopted for a decade a currency board, pegging its local currency to the dollar as a means of ending hyperinflation, and later hobbled its economy by ill-thought economic measures such as raiding the central bank reserves to finance budget deficits or the imposition of steep export levies on agricultural products. It has also doctored its inflation figures and alienated the international capital markets.

Venezuela, in turn, turned into an astonishingly incompetent state-run planned economy, with nationalization of industries and the imposition of price controls on many goods and several parallel exchange rates. Brazil undertook a vast monetary reform including the introduction of a new currency and the move from a fixed exchange rate regime to a floating one. Paraguay was suspended in 2012 for the violation of Mercosur's Democratic Clause, after its parliament impeached President Fernando Lugo. Not surprisingly, all these factors have often resulted in severe clashes between member countries.

The Mercosur partners, while engaging in trade negotiations with the US and Europe, have so far remained committed to protecting their large aggregate domestic market against external competition. It has not really helped: the share of intra-Mercosur exports fell from 19.5% a 15% of total exports between 1995 and 2012, and overall Mercosur growth has been tepid.

Not only economic factors have contrived against regional economic integration. Ideological and geopolitical elements have also played a crucial role. The initiative of President George W Bush to launch a Free Trade Area of the Americas (FTAA) was met with widely divergent reactions in Latin America. Countries like Chile, Colombia, and Peru as well as most of Central America view FTAA positively. Brazil, on the other hand, initially welcomed FTAA and participated in the negotiations, but later entered into conflict with the United States over such issues as US domestic agricultural support prices and export subsidies.

Other countries simply shunned the initiative. For Venezuela's Hugo Chávez, the FTAA was simply another form of neo-imperialism. He soon commanded the establishment of the Bolivarian Alternative for the Americas (which shortly thereafter changed its name to Bolivarian Association for the Americas, ALBA in its Spanish acronym). Formally established in 2004, in also includes Bolivia, Cuba, Ecuador, Nicaragua, Venezuela and several small Caribbean countries.

Thus, Latin America's efforts towards successful regional integration have been fraught with political instability, sharp swings in economic policies and the lack of a consistent vision to guide the design of industrial policies. It is no surprise that Latin America has not managed to set up value chains that make good use of its comparative advantages. Intraregional trade is low (20% in 2012), far lower than Asia (26%, same year) or the European Union (63%, also same year). Trade within the regional blocs is even lower than the overall regional average.

This is, hopefully, about to change.

The big divide

It is ironic that the swerve towards more enlightened economic policy was ushered in by highly unlikely champions of free trade, such as dictator Augusto Pinochet in Chile and authoritarian president Alberto Fujimori in Peru. Even more remarkably, Fujimori's liberalizing policies were continued by Alan García, whose illiberal economic policies had failed miserably during his first term, which preceded Fujimori's, as well as by García's successors. Peru, as a result, went from being a closed economy to the most open economy in Latin America, boasting the fastest growth in Latin America for many years.

The forerunner was Chile. Over the past 40 years, it has perhaps been the only country in the region consistently to adhere to the remarkably open trade and industrial policies first introduced in

Free-trade agreements of *Alianza del Pacífico* countries with AdP observers and other third countries

	Chile*		Colombia		Costa Rica		Mexico*		Peru*	
	Year of entry into force	Depth	Year of entry into force	Depth	Year of entry into force	Depth	Year of entry into force	Depth	Year of entry into force	Depth
Canada*	1996	(5)	2008	(6)	2002	(4)	1994	(7)	2008	(6)
United States*	2004	(6)	2012	(7)	2009	(6)	1994	(7)	2009	(7)
China	2006	(3)			2011				2010	(5)
India	2007	(1)								
Japan*	2007	(7)					2005	(6)	2012	
Singapore*	2006	(6)			2013				2009	(6)
South Korea	2004	(7)	2013						2011	
Australia*	2009	(7)								
New Zealand*	2006	(6)								
European Union	2003	(6)	2013		2013		2000	(3)	2013	
Switzerland	2004	(6)	2011	(7)			2001	(7)	2011	
Turkey	2011	(2)								
Israel			2013				2000	(4)		
Morocco										
Iceland	2004	(6)	2011	(7)			2001	(7)	2011	
Norway	2004	(6)	2011	(7)			2001	(7)	2011	
Brunei Darussalam*	2006	(6)								
Indonesia										
Malaysia*	2012									
Thailand									2011	(1)
Viet Nam*	2012									

*Source: Data from WTO RTA Gateway and Dür et al. (2014); visualization by Abusada-Salah et al. (2014). Depth is a measure of how profound each bilateral agreement is, with 1 very shallow and 7 very deep, ie. going beyond tariffs to include non-tariff barriers and regulations. * indicates parties to the negotiations of the Trans-Pacific Partnership TPP. Blue background indicates treaty under negotiation*

the early years of the Pinochet dictatorship. The most astounding proof of this commitment came when Pinochet stepped down in 1990 and the incoming democratic government decided to keep to such policies. This continuity was again put to the test during the first tenure of President Michelle Bachelet, when Brazil and Argentina tried to attract Chile to Mercosur. Chilean authorities pointed to the difficulties of joining a bloc relatively closed to foreign competition and where member countries still exhibited significant macroeconomic imbalances.

Chile went on to enhance trade relations with Latin America, NAFTA, the EU and Asia. Worryingly, however, the same President Bachelet, now in her second term, appears to be about to undo much of the good work with the introduction of modifications to the minimum wage rules and to the defined-contribution pension plan, as well as a seven-percentage-point hike in corporate taxation.

Mexico's trade policies have gained consistency since the coming into effect of the trilateral North America Free Trade Agreement (NAFTA) in 1994. The overwhelming importance for Mexico of economic relations within North America (almost 80% of its exports go to the US) has inevitably swayed the focus of Mexican trade relations away from the rest of Latin America. Nevertheless, Mexico has tried to increase its trade relations with Latin America and the Caribbean through the signing of many trade accords. Still, Mexico's trade with the countries to the south has remained limited, at around 7% of its total exports and less than 5% of its imports.

Colombia, in turn, despite its massive security problems (US Secretary of State John Kerry named Colombia in the same breath with the Central African Republic and the Democratic Republic of Congo as places where strife needs to be curbed, at the Security Conference in Munich this February), has made astonishing progress towards liberalizing its economy. It is now one of the world's fastest-growing economies.

Thus, by the end of the 2000s Latin American trade policies were clearly diverging into two separate paths. On the Atlantic side, the fairly protectionist and distrustful of globalization Mercosur bloc, intent on preserving its huge internal market. (Here, by the way, Uruguay is clearly the odd man out, with an economic and political stance that would fit beautifully with the Pacific countries; as it is, sandwiched between the two local mammoths, it didn't really have much of a choice.)

On the Pacific side, all countries (with the exception of Ecuador, which would fit ideologically well in Mercosur) had instead opted for what has been termed 'open regionalism,' which aims at deep integration at the regional level and an opening to the entire world. Each member country is free to enter into free-trade agreements with whomever they want. Even with Mercosur. The political will, clearly, was to give economics a chance.

Chile, Mexico and Peru have become members of the Trans-Pacific Partnership (TPP) and of the Asia-Pacific Cooperation (APEC) forum. Colombia later signed FTAs with the EU, Canada and South Korea. Furthermore, Chile and Mexico are members of the Organization for Economic Development and Cooperation (OECD); in 2013 Colombia launched its own accession process, and Peru has announced it will follow suit.

So, in light of the similarities in trade policies of these countries on the Latin American Pacific coast, Colombia proposed in 2006 the establishment of a forum for cooperation and coordination called *Arco del Pacifico* (Arc of the Pacific). The idea was endorsed by Chile, Mexico and Peru and in 2007 was formally established with the participation of Chile, Colombia, Costa Rica, Ecuador, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, Panama and Peru. It failed because of a lack of commitment and divergence of trade policy interests.

It was the formerly economically illiberal Peruvian President Alan García who, in 2010, suggested that Chile, Colombia and Peru should start a process to build what he called a 'profound integration' aimed at going beyond the usual disciplines or chapters included in FTAs to include a deeper coordination of public policies, building upon the already existing similarities of such policies in the three countries. García's proposal was met with immediate enthusiasm by the other two presidents. Later, the Mexican government requested to join the Group and in April 2011, finally, the Pacific Alliance (or *Alianza del Pacifico*, AdP) was officially created in Lima.

Its stated objectives are the construction of an area within which there will be free movement of goods, services, capital and persons, with the purpose of *"attaining greater welfare, overcoming socio-economic inequality and achieving greater social inclusion of their inhabitants"* and becoming *"…a platform for political articulation and economic and trade integration, and to project these strengths to the rest of the world, with a special focus on Asia-Pacific".*

Negotiations within the Alliance have proceeded at a vertiginous pace. Since its inception in April 2011, the member countries have celebrated nine leaders' summits and negotiated two important agreements. The first of them was the Framework Agreement of June 2012, which contains the legal basis that laid the foundations for the Pacific Alliance. The second was an Additional Protocol, signed in February 2014, which goes beyond tariff liberalization to include the harmonization of rules of origin, and covers non-tariff barriers, such as sanitary and phytosanitary and technical barriers to trade among its members. The Additional Protocol also contains clauses on government procurement, trade facilitation, investment, financial services, maritime services, e-trade, telecommunication, dispute resolution and transparency.

In terms of trade liberalization, the Pacific Alliance offers a small yet significant improvement vis-à-vis the agreements previously signed among its members. Bilateral FTAs among the Alliance members had already liberalized over 92% of the total trade. Once the liberalization schedule is completed, over 99% of trade will be free of tariffs and duties. Additional actions have already been taken in other areas, such as those regarding the merger of stock exchanges and the facilitation of movement of businessmen and people in general. There are no tourist and business visa requirements for Alliance citizens, and special programs are in place to make it easier for our students to study and travel.

Crucially, the Alliance opens the possibility for its members to collaborate in the areas of science, technology and the development of human capital, in order to enhance their competitiveness in global value chains with more diversified and technologically advanced products and services.

The open regionalism concept, as well as the political will that the leaders are wielding in its construction, has elicited worldwide interest, as witnessed by the 32 countries that now have observer status within the Alliance. In addition to Costa Rica, Panama is also an official candidate for membership. It is also significant that the Alliance can act with a single voice within the TPP and other trading bloc negotiations.

The current four member countries represent 214 million people, with a combined gross domestic product of US$2.1 trillion, and accounts for 37 percent of Latin America's total GDP. Over the past four years, their annual growth rate has averaged 5.1 percent. Alliance foreign trade adds up to more than US$1.13 trillion, and it is the recipient of 45 percent of total foreign investment flows in Latin America.

The member's stock exchanges are unified in the Latin American Integrated Market, listing more than 750 companies, with a market value of US$1.1 trillion. The members are busy establishing embassies and trade offices in shared facilities overseas.

Thus, in South America, the Andes mountains not only mark a mighty geographic division, but an economic policy one as well. You would do well to go west, young man. ■

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Creating a grand Africa-wide free trade area: overcoming challenges, taking opportunities

William Gumede is Associate Professor, School of Governance, University of the Witwatersrand, Johannesburg and Chairperson of the Democracy Works Foundation; and author of *South Africa in BRICS: Salvation or Ruination, Tafelberg*

Introduction

African states have set out an ambitious plan to create an Africa-wide free trade area, with duty- and quota-free movements of goods, services and business people by 2016, and an Africa-wide economic and monetary area by 2025.

So far 26 African nations have joined up, and the challenge is how to merge the three existing, the Common Market for East and Southern Africa (COMESA) the East African Community (EAC) and the Southern African Development Community (SADC), which are often overlapping, regional trade blocks[1]. Pooling African economies will bring larger economies of scale and markets, thus creating the potential to expand both production and demand.

Africa is too fragmented

On average, every African country belongs to four or five regional trading blocs, which are overlapping. All these regional groupings have different rules, regulations, membership criteria and are at different stages of integration. These factors could slow the building of a free trade area[2].

Ineffective institutions undermine integration

One of the key reasons for the failure of the African integration project so far is weak regional and continental institutions. In some cases the patronage systems at the level of national government have been transported to the regional bodies – undermining these too.

The institutional failures in African countries mean that many domestic and national institutions cannot support the complicated and ambitious regional integration commitments; and even if the capacity exists, there is no guarantee that the regional commitments will be honoured.

Lack of coherence in protocols, treaties, legal frameworks and policies

In terms of regional integration, policies adopted at the regional level to promote regional integration are often contradictory to individual countries' domestic policies. But continental policies are often also at variance with the policies adopted at the level of regional trade or political blocs. Often individual countries have ignored regional protocols, treaties and legal frameworks.

Unfair trade agreements with former colonial powers

Most African countries have trade agreements with former colonial powers that often undermine integration with other African countries. The Economic Partnership Agreements (EPAs) with former African, Caribbean and Pacific colonies proposed by the European Union to replace the preferential trade arrangements between the African, Caribbean and Pacific states, which had been operating for three decades before this, is one such example[3].

In terms of the EPAs, the EU has divided Africa into its own regions – which undermine African efforts at integration. The United States African Growth Opportunities Act (AGOA) signs trade arrangements with individual African countries, rather than with regional blocs – which undermines regional integration. US Secretary of State Hillary Clinton has acknowledged that *"regional integration has gotten too little attention within the AGOA framework"*[4].

Poor infrastructure

Poor physical infrastructure, with weak logistics and supply chains, poor power supply and transport networks and limited bank finance to fund infrastructure investment, undermines regional trade in Africa. Infrastructure across the region is either non-existent, inadequate, or not maintained or upgraded. This significantly increases the cost of business for African operators, making it difficult to access markets on the continent.

Lack of democracy hampers economic integration

Lack of democracy, poor governance and mismanagement is at the heart of all political instability in Africa. These and civil strife on the continent are a huge obstacle to establishing a grand free trade area across Africa. Many African countries have been destabilised by coups and political turmoil and misruled by autocratic governments. Better African leadership and greater democracy are crucial for creating an effective free trade area.

Non-trade barriers

Non-trade barriers, measures other than tariffs that restrict trade, such as import bans, quotas, technical regulations, permits and levies, export taxes, rules of origin, single-marketing channels, over-bureaucratic customs clearance procedures and travel restrictions, are undermining trade areas on the continent. Different regulations in different countries and red tape drive up the cost of business and undermine the idea of a free trade area.

The problems with customs unions thus far

In June 2009, COMESA[5] launched a customs union on paper[6], in the form of a trade bloc with a free trade area and common external tariffs. However, in real terms, the customs union is not

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functioning. Several have not even signed the COMESA free trade area protocols.

An EAC[7] customs union was supposed to come into force on 1 January 2010. Issa Sekito, from the Kampala City Traders Association, puts it succinctly: *"We are too many years into the customs union and a few miles into the practical application of the required protocols"*[8]. An SADC regional customs union that was supposed to be launched in 2010 is still some way off from being a reality.

How can the challenges be overcome?

Africa need political will to make free trade a reality

Lack of political will is undermining the establishment of the African free trade area. For a grand free trade area to work in Africa, African countries will need to cede some of their sovereignty. A big challenge is going to be to set out legally binding mechanisms – and penalties – to get signatories to the free trade area to stay the course.

An African free trade area will need effective dispute resolutions to deal with inevitable trade disputes between members. Independent tribunals will have to be set to rule impartially on disputes or disagreements on the interpretation or application of trade rules.

Regional industrialisation: diversify one-commodity economies

Continent-wide industrialisation should be the 'overarching objective' of an African grand free trade zone and the integration initiatives. Most African economies are based on one raw material or agricultural product, which on the face of it means that there is little to trade among themselves.

African countries could pool their mining and oil extractive industries – in similar ways that countries in the EU levered off their steel and coal industries – and build regional economies on the beneficiation of these primary products.

The challenge is for individual African countries within a grand free trade area to specialise: one country must produce what another country can't, but needs. To do so, each African country should be required to draft an industrial policy which at its heart should have diversifying from one agricultural product or commodity to value-added products. All the individual country industrial policies must feed into a regional industrial policy. This in turn should be connected to a continent-wide industrial policy for Africa.

Eliminate non-trade barriers

Non-trade barriers will have to be eliminated if a free trade area is going to work. Similar legislation, technical regulations and custom procedures across countries are vital. There should be penalties for countries that have signed on to the free trade deal but that persist with the implementation of non-tariff barriers.

Integrate infrastructure into broader economic development

African infrastructure development should be seen as a tool for long-term economic investment that is integral to a country's industrialisation. Infrastructure development must be linked to 'other regional economic stimulus measures [to] complement the infrastructure investment and generate synergistic effects'[9].

Regional and continental bodies have divided Africa into infrastructure corridors. However, these corridors are useless and ill-conceived, unless they are underpinned by industrial estates or zones that combine new infrastructure with establishing new firms and plants.

The current African regional trade blocs should be transformed into regional economic growth zones or regional zones of industrialisation. Infrastructure, which would include power, transport, telecommunication networks and so on, should be developed within each country, within and between the regional economic growth zones. A continental infrastructure grid should then connect these regional economic growth or industrialisation zones.

Bring in the informal sector or the second economy

Right now the bulk of regional trade across Africa is in the form of informal traders crossing the borders[10]. A free trade zone among Africans will be useless unless it includes small traders in the informal sectors, who often face formidable

bureaucratic barriers[11]. There will have to be uniform standards and specifications across the region to make it easier for the informal sector.

All members of African free trade zones must ramp up market support infrastructure for informal traders[12], in the form of facilities for storage, logistics and communication. African border posts must be made friendlier to informal traders.

Closer collaboration between Africa's development finance institutions and state-owned enterprises

African development finance institutions and state-owned enterprises, whether country, regional or continental, must work more closely and more collaboratively to facilitate regional integration.

Regional developmental finance institutions such as the African Development Bank, the Industrial Development Corporation (IDC) and the Development Bank of Southern Africa are well equipped to coordinate regional and continental infrastructure development and industrialisation on behalf of African states. African DFIs and SOEs must work more collaboratively.

Monetary union: only when strict criteria are met

All the three regions committed to a continental-wide Africa free trade area have set targets for setting up regional central banks and adopting a single currency. Not surprisingly, very little progress has been made, beyond setting such targets on paper. Before one can talk of monetary union, African countries will have to establish some semblance of fiscal and monetary discipline.

Unless the underlying poor political, economic and social governance in Africa is resolved, a continental common currency may end up with all the vulnerabilities of the worst weakest African currencies. Monetary union will have to be at the end phase of regional integration when the political, economic and non-trade obstacles have been smoothed out.

"Non-trade barriers... are undermining trade areas on the continent"

Bring in civil society, communities and citizens

African civil society will have to play multiple roles in the regional integration process: as partners providing capacity, representing the poor, and as critics. Given the lack of capacity in many African institutions, civil society has a strategic role to play in strengthened regional integration, through providing ideas, policy alternatives and even as alternative delivery agents. Civil society can also play a role in monitoring whether countries and regions are implementing integration commitments.

Currently there are no formal structural processes for civil society organisations to participate in policy formulation in regional and continental integration structures. This needs to be addressed, as it is essential that national civil groups cooperate with their peers at the regional and continental level.

Integrate regional and continental educational institutions

There will have to be closer cooperation between higher education institutions in the region, in order for the region to use its educational training capacity better. Higher education institutions can assist greatly in effective regional integration[13]. So far, cooperation between higher institutions within regional trade blocs has been weak, diffused and mostly at the level of rhetoric.

At present, there is little compatibility among higher education institutions in the regions – with differential levels of resources, different curricula, and different tradition. Research institutions, infrastructure and policies in the different trade regions have been fragmented and uncoordinated, resulting in inefficiencies. ■

1. The formal decision was taken by the three African regional organisations, the Common Market for East and Southern Africa (COMESA) the East African Community (EAC) and the Southern African Development Community (SADC) at a summit of heads of states in Johannesburg on 12 June 2011. The original idea for an African Free Trade Zone was mooted at a 2008 summit of these three African regional organisations.
2. These regional groupings were also formed for different and unique historical and political reasons – the SADC for example to oppose the hegemony of Apartheid South Africa; COMESA started from a preferential trade agreement for East and Southern African, initiated by UNECA and the OAU [See UN Economic Commission for Africa and African Union (2006) Assessing Regional Integration in Africa II: Rationalising Regional Economic Communities. Uneca Publications, Addis Ababa, p. 37].
3. In 2000 ACP countries and the EU signed the Cotonou Convention which wound up the 1975 Lome accords, which had formalised trade arrangements between the EU and its former colonies. The Cotonou Convention makes provisions for ACP countries to negotiate new trade agreements – the EU put the EPA on the table.
4. Quoted in John Page and Nelipher Moyo (2010) Supporting Deeper Regional Integration in Africa. Working Paper, Africa Growth Initiative at Brookings – Improving AGOA: Toward a New Framework for US-Africa Commercial Engagement. Brookings Institute, New York, p.8.
5. COMESA members are: Burundi, the Comores, Democratic Republic of the Congo, Djibouti, Egypt, Eritrea, Ethiopia, Kenya, Libya, Madagascar, Malawi, Mauritius, Rwanda, Seychelles, Sudan, Swaziland, Uganda, Zambia and Zimbabwe.
6. COMESA proposed a four-tariff band structure: 0 percent for raw materials, 10 percent for intermediate goods, and 25 percent for finished goods. To protect small economies, it includes a list of sensitive goods – towards which a flexible approach would be adopted and fully excluded some other products. [The East African (2010) Trade Disputes between COMESA countries and overlapping membership spell double trouble. October 18]
7. The EAC consists of: Kenya, Rwanda, Burundi, Tanzania and Uganda.
8. Faridah Kulabako (2011) Progress on EAC tariffs expected as leaders meet. The Monitor, April 19.
9. Tsuneaki Yoshida (2000) Japan's experience in infrastructure development and development cooperation. JIBC Review, December, 3: 62-92.
10. In many cases cross-border trade in the current regional trade groupings by informal traders is undervalued.
ECA/AUC/AfDB (2010) Assessing Regional Integration in Africa (ARIA IV): Enhancing Intra-Regional Trade [Chapter 5]. May; ECA/AUC/AfDB (2010) Assessing Regional Integration in Africa (ARIA IV): Enhancing Intra-Regional Trade [Chapter 5]. Addis Ababa, Ethiopia, May; Asareca (2009)
11. Informal cross-border and trade and trade facilitation reform in Sub-Saharan Africa. PAAP's Electronic Newsletter, Vol. 12 (8), April 24
12. UNECA (2010) Informal Trade in Africa. African Trade Policy Centre. Briefing 7. Addis Ababa.
13. Berlinguer, Luigi (2006) European views on the political future of universities: The Politics of European University Identity – Political and Academic Perspectives. In: J. Aviksoo et al. (eds) Proceedings of the Seminar of the Magna Charta Observatory, Bologna. Sept. 14, p.123

India-EU FTA: problems and future prospects

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Introduction

India-European Union relations started way back in the early 1960s, when India pursued diplomatic relations with the European Economic Community. The signing of a cooperation agreement in 1994[1] broadened the scope for bilateral relationship beyond trade and economic cooperation. Since then active cooperation has been witnessed in the form of political dialogue, enhanced cooperation in the field of security, agreement on R&D cooperation in the peaceful use of nuclear energy, consultations on foreign policy, strengthening of economic and commercial relations by increasing trade and investment, dialogue on financial services regulation, cooperation in the fields of science and technology, energy security, and various bilateral agreements.

Key bilateral agreements signed include the Science & Technology Agreement (2001, renewed in 2007), the Joint Vision Statement for promoting Cooperation in the field of Information and Communications Technology (ICT) (2001), the Customs Cooperation Agreement (2004), etc. The two sides adopted a Joint Action Plan in 2005 (reviewed in 2008) that provided for strengthening dialogue and consultation mechanisms in the political and economic spheres, enhancing trade and investment, and bringing people and cultures together.

In 2007, India and the EU began negotiating a broad-based bilateral trade and investment agreement. The recommendations of the India-EU High Level Trade Group were pondered over. Further, the removal of barriers to trade in goods and services and investment across all sectors of the economy has been a key concern. Both parties reiterated their belief in the primacy of the multilateral trading system and reaffirmed their commitment to the Doha Development Agenda (DDA) round of negotiations.

In the last couple of years the EU has reposed greater faith on the new growth order of the world economy – especially the Asian region. It concluded an FTA with Singapore on September 20, 2013, and FTA negotiations are at an advanced stage with India and in early stages with Indonesia and Philippines. The EU-India FTA is seen as the first of a new generation of FTAs between the EU and emerging economies.[2] This will also be India's first trade agreement with a large developed community of nations, which is also one of its largest trading and investment partners, and its impact will be significant due to large population group covered. India has extensively utilized its experience in negotiating FTAs, having earlier finalized FTAs with various economies such as Korea, Japan, Singapore, ASEAN, etc. Both the EU and India acknowledge the need for greater realization of their trade and investment potential. The finalization of India-EU FTA negotiations is expected to be a significant step towards bilateralism, and ultimately multilateralism. In this context, it is worth highlighting the recent trade and investment scenario between the two and pondering over the ongoing contentious issues in the negotiations.

India-EU trade and investment relations

Bilateral trade

The EU is India's largest trading partner accounting for approximately 13 percent of its total world trade. For the EU, however, trade with India (as a percentage of its total world trade), is less than one percent. Indeed, India's share of the EU's

Table 1: EU India Trade ($ Million)

Description	2011	2012	2013
EU's Trade with India	116,657	100,962	101,915
EU's Trade with World	12,269,795	11,603,582	11,978,630
India's Trade with EU	109,737	102,670	105,473
India's Trade with World	763,886	778,541	802,657
EU Trade with India (Share in EU's Total World Trade)	0.95	0.87	0.85
India's Trade with EU (Share in its total World Trade)	14.37	13.19	13.14

Source: Compiled from International Trade Centre

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total world trade has declined in recent years, as shown in Table 1. Further, India's imports from the EU which stood at 12 per cent in 2011, declined to 10.6 percent in 2013. Thus one can discern a growing asymmetry of interests between the two parties wherein India's importance to the EU continues to decline. This may also be attributed to the Euro zone's sovereign debt crisis which led to decreased trade with the world. In this scenario, there is scope of significant gain for India – as compared to the EU – if the India-EU FTA negotiations are finalized.

The EU's main exports to India are pearls and precious stones, machinery, nuclear reactors, electrical and electronics equipment, optical photo equipment, aircraft and spacecraft, iron and steel, etc. Interestingly, the top 10 among these account for three fourths of the EU's exports to India. It is apparent that India is not a large trade destination for the EU. However, India relies heavily on the EU for mainly machinery and nuclear reactors; optical and photo equipment; aircraft and spacecraft and vehicles other than trains. The EU may point to these sectors as showing potential for further growth during the FTA negotiations. Further, EU's top imports from India include mineral fuels, oil, distillation products, organic chemicals, articles of apparel, accessories, etc. The share of these sectors is very small in the EU's total imports, suggesting that the EU prefers to look toward other parts of the world to fulfil its domestic demand.

Investment

The EU's most attractive destinations in Asia are Hong Kong, Singapore and China. Together they accounted for almost half the EU-27's FDI investment in Asia at the end of 2012. However, there has been decline in investment volumes in China and Hong Kong – as well as in India – in 2013. The EU investment in India is about a third of what it invests in China. However, it is still India's leading source of FDI. The outward flows to India declined from €5.5 billion to €3.2 billion in 2013. Overall, the EU's outward investment is mainly focused on services, whereas in the cases of China and India, it is concentrated in the manufacturing sector. It held about 40 percent and 60 percent respectively of total EU FDI stocks in these economies at the end of 2011.[3]

The US, Brazil and Japan have been the most active players investing in the EU. India and Hong Kong have not shown any surge in outward flows to the EU. India received around one percent of the EU's extra outflows in 2009 which increased to almost three percent in 2011, but plummeted to less than one percent in 2013. Indian investments in the EU were €0.4 billion in 2013. The most important EU countries for FDI inflows into India in 2013 were the UK and Germany (with both investing €0.9 billion each), followed by Italy (€0.6 billion) and Belgium (€0.2 billion) (GOI, August 2014). Of the inflows into BRIC nations from the EU, India attracted about 10 percent, but the same has declined to 6.8 percent in 2013. Indian outflows to the EU have also been miniscule in the past two years.

India and the EU look favourably upon each other as investment destinations. The EU, for example, is the second largest investor in India and largest source of technology transfers. Between April 2000 and April 2013, total cumulative FDI inflows (goods and services) from the EU were valued at US$49 billion, which accounted for 25 per cent of the cumulative FDI inflows into India during this period.[4] Phenomenal growth has been noticed in FDI for both, India and the EU.

Table 2: FDI inward and outward flows (shares in % of extra EU, otherwise mentioned)

Partner	2009	2010	2011	2012	2013
FDI flows from EU					
Extra EU Values (€ Billion)	331.9	302.6	474.8	255.6	341.4
Extra EU	100	100	100	100	100
Brazil	3.79	14.81	6.39	8.70	10.43
Russia	2.64	9.16	1.74	6.33	-3.13
India	1.05	2.46	2.91	2.15	0.93
China (including Hong Kong), *of which*	3.54	6.03	5.69	11.94	5.42
Hong Kong	1.10	2.58	1.47	5.87	3.03
BRIC	11.03	32.46	16.74	29.11	13.65
FDI flows into EU					
Extra EU Values (€ Billion)	274.4	222.6	424.0	291.8	326.6
Extra EU	100	100	100	100	100
Brazil	0.43	4.47	3.07	0.76	6.58
Russia	4.55	3.42	0.74	2.89	2.49
India	0.44	0.22	0.54	-0.24	0.12
China (including Hong Kong) *of which*	0.55	6.36	2.73	2.24	2.83
Hong Kong	0.53	6.20	1.71	-0.38	2.50
BRIC	5.96	14.47	7.07	5.65	12.03

Source: Eurostat

India has a Bilateral Investment Promotion and Protection Agreement (BIPA) with 22 EU member states and Double Taxation Avoidance Agreements (DTAA) with 24 EU member states. The EU and its member states have actively supported various development programmes in India such as Operation Flood, the District Primary Education Programme (DPEP) and the Sarva Shiksha Abhiyan(SSA) programme, among others.

"As for the way forward, three things are needed: improvement in Indian manufacturing through domestic reforms, slashing of tariffs and proper government procurement processes"

Trade and investment barriers

Literature on the subject maintains Indian trade with the EU has been hampered by various issues such as SPS, TBT and NTBs (non-tariff barriers). The EU's SPS measures have affected the export of agricultural and food products, while the TBT has grossly affected the exports of industrial products. The pharmaceutical industry, where India has a significant stake, has experienced an increased demand by the EU for intellectual property protection standards over and above the World Trade Organization's (WTO) Trade-Related Aspects of Intellectual Property Rights (TRIPS) requirements.[5]

The European Commission has taken emergency measures by banning the import of five fruits and vegetables from India. This matter was highlighted in a recent EU member state experts' meeting at the Standing Committee on Plant Health on March 26, 2014. India has expressed its displeasure with the EU regarding this ban at the India-EU Sanitary and Phytosanitary and Technical Barriers to Trade working group in Brussels on April 1, 2014. Notably, the EU has imposed tough SPS and TBT measures on South Africa and Pakistan as well recently.[6] India has recognized the need for safe fruit and vegetable items and from April 1, 2014, has launched compulsory inspection, testing and labelling by trained personnel at agriculture produce and export development authority (APEDA) houses. Indian officials in the EU's SPS Committee have conveyed their country's compliance with the EU's strict requirements.

Regardless of the outcome, one can argue that the EU may have shown unnecessary haste in its actions. To elaborate, the SPS agreement states that a country may impose a ban upon products that could harm humans, plants or animals. But, at the same time, under Article 10 of the agreement, it provides leniency to developing countries (like India) by giving them a longer timeframe for the adoption of quality measures when there is no 'imminent' danger. Considering this, India intends to raise this issue arguing that the EU has flagrantly violated the World Trade Organization's SPS agreement.[7]

With regard to investment barriers, India is ranked the fifth most restrictive country in the *FDI Regulatory Restrictive Index 2013*, indicating the tough investment rules for foreign investment. At the sectoral level, business services and communications sectors exhibit the highest levels of regulation in terms of FDI. However, India is slowly addressing the regulatory norms by removing caps on foreign investment which recently came into force. The government is working towards further opening up of sectors with FDI caps.

The number of antidumping measures initiated by the EU against India, as well as those actually taken by it, far exceeds India's actions. Between 1995 and 2012, the EU initiated 50 anti-dumping measures and took 38 against India, while India initiated 34 measures and took 19 measures against the EU. Indian companies and industry associations have pointed out that non-tariff barriers in the EU have increased after the global slowdown and eurozone crisis. At the same time, there is a restrictive business environment in India for EU businesses, especially in financial, banking, transportation, and business services (European Parliament, October 2013). Moreover, the lack of a provision for government procurement and the complex multi-layered system for procurement are discouraging factors for EU companies. Other factors which affect the free flow of investment are the higher environment and labour standards in the EU.

It is pointed out that getting products passed through Indian Customs requires an additional check for certificates of conformity to specifications that are different from those recognized at the international level. This leads to additional checks, resulting in higher costs for the operator. In the World Economic Forum's *Global Competitiveness Report* for 2011-2012, India ranked 89th out of 142 countries on infrastructure. The report criticized India's transport, ICT and energy infrastructure as *"largely insufficient and ill-adapted to the needs of business."* The GAAR, which could lead to retrospective tax on cross border transactions, is also a cause for concern of foreign investors.

The low ranking of India in terms of Intellectual Property Right (IPR) protection environment, continued use of compulsory licences, patent revocations, and weak legislative and enforcement mechanisms raise serious concerns about India's commitment to promote innovation and protect creators. India's turning down of EU proposals to government procurement and market access for automobiles and wines and spirits is one of the major reasons for talks on the Bilateral Trade and Investment Agreement (BTIA)[8] getting stuck.

India EU-FTA negotiation: rationale, benefits and contentious issues

In the recent past, the EU considered the need to build strategic relationships with emerging economies in trade and investment in its vision document *Europe 2020: A European strategy for smart, sustainable and inclusive growth*. To realize this objective, it concluded FTAs with Singapore and Korea, and is currently negotiating FTAs with India, Canada, and Japan and the ASEAN group.

The India–EU FTA has been on the anvil for a long time, with no major breakthroughs in sight. A three days inter-governmental meeting in Delhi in May 2014 failed to iron out differences. India has a lot to gain from an FTA with the EU, particularly in regard to preferential and duty-free access to the European market. A Sustainability Impact Assessment, commissioned by the EU[9], indicates that an extended (broad) FTA (including further removal of non-tariff barriers to trade harmonization) would result in significant benefits to both parties in terms of welfare gains, production, international trade, wage and productivity increases. The welfare effects amount to an additional 0.3 per cent growth for the Indian economy in the short run and 1.6 per cent growth in the long run.

During the FTA negotiations, both sides have committed themselves to an ambitious agreement, with tariff elimination on more than 90 per cent of goods traded and a strong GATS (General Agreement on Trade and Services) - plus agreement in services. Most of agriculture will be exempted by mutual agreement. However, academicians maintain finalizing the India EU FTA will be a difficult journey because of the high trade-related regulatory and partial access to some services sectors such as professional services, financial services, retail and distribution.[10]

There is a serious doubt among Indian policymakers of any substantial gain through trade negotiations, as India levies an average tariff rate of 14.5 percent, whereas the EU's average tariff rates are only around 4.1 per cent. Moreover, India has a negative trade balance with the EU and there is a fear among industry and non-governmental organizations (NGOs) in India that this may further worsen after the tariff reductions. Trade negotiations are not easy for India given its track record of negotiations with Japan and Korea as the level of competitiveness differs vastly between emerging and advanced countries.

India-EU FTA development

The EU-India FTA negotiations were launched in June 2007, and so far there have been 11 full rounds the negotiations as well as smaller, more targeted clusters of meetings rather than full rounds – expert level inter-sessional meetings, chief negotiator meetings and meetings at higher levels. The issues related to labour standards, intellectual property rights, sanitary and phytosanitary standards, access to agricultural goods and animal origin, technical barriers, use of anti-dumping/anti-subsidy measures against Indian products, the complex system of quotas/tariffs, a single visa for Indian professionals on short-term contractual visits, data secure status and environmental issues were found to be key hurdles in expanding trade with the EU.

Even the EU had been inclined towards more protectionist measures in its trade policy (Upadhyay, 2012) India's high tariff rates[11] and non-tariff trade barriers[12] have been of great concern for foreign companies. India is unwilling to liberalize trade in services and on procurement there will be no deal at the state level (European Parliament, October 2013).

In FDI, there were substantial restrictions on acquisitions and the EU was seeking higher FDI limits in retail and insurance. Concerns have been voiced by some NGOs that the planned reduction of tariffs in the dairy sector (tariffs of up to 60 per cent) and poultry industry could have a serious impact on the cooperative, smallholder-dominated Indian dairy industry, mainly on employment.[13]

There were other contentious issues. The EU sought liberalization of the Indian banking and financial sector. It wanted various regulations pertaining to bank branches, numerical quotas, foreign ownership, equity ceilings, voting rights, and investments by state-owned companies in foreign banks in India removed, among other changes. High customs duties on European products such as automobiles and alcohol were key issues. The Indian automobile industry is apprehensive about its level of competitiveness due to high costs of inputs caused by inflation, the rupee's depreciation and the cascading effects of various taxes, apart from the economies of scale the EU auto industry enjoys.

The IPR provisions in India-EU draft FTA also raised concerns as they will limit the capacities of both India and the EU to use the public health safeguards and flexibilities allowed in the WTO's TRIPS Agreement.[14] It is pointed out that the provisions on IPR are problematic on various levels, particularly in the areas of expansion of copyright, inclusion of TRIPS plus provisions, cross border measures, liability of service providers and enforcement mechanisms.[15]

Another contentious area is India's demand for flexible regulations and easy visa requirement for Mode 4 services. Europe is cautious about allowing this fearing an increased unemployment problem due to its current fiscal crisis. Negotiations are also struck on the issue of Indian policy on government procurement. India is unwilling to make changes as it considers government procurement a sensitive issue from the development perspective.[16]

So far the negotiations have not produced the desired results. Most of the contentious issues have not been resolved. Recent negotiations have focused on market access for goods (to improve coverage of offers on both sides), the overall

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ambition of the services package and a meaningful chapter on government procurement and sustainable development.[17]

Still, some progress has been made in the FTA negotiations. These include suspending the implementation of some aspects of the preferential procurement policies for domestically manufactured electronic goods and telecom products. Regarding mandatory compliance of steel products, the date the mandatory certification requirements for certain steel products come into force has been delayed. India has also formally extended the grace period for the compulsory registration of 15 categories of IT and consumer electronics goods. India has also introduced some changes in investment rules and opened up higher investment possibilities in the telecom sector, defence manufacturing, insurance, and single and multi-brand retailing.[18]

The contentious issues seem to be the preferential agreements for the European automobile and auto-component sectors, and the heavy tariffs on wine and spirits. Under the Bilateral Trade and Investment Agreement (BTIA), key challenges are the exclusion of agriculture products from the negotiations. The reason is the huge subsidy agricultural products of the EU get, and the relatively less competitive Indian agriculture products. These cast doubts on the India-EU FTA being finalized.

Major challenges are non-tariff barriers such as the non-harmonized EU market, work permit and visa related barriers, the definition of who is a 'professional', the limited bilateral social security agreement, the limited access of FDI from the EU in the Indian service sector, in retail, insurance and banking, prohibition of FDI in atomic energy, railway transport, etc.

A host of contentious issues are yet to be resolved. India wants the EU to give it greater market access in the services and pharmaceuticals sectors, provide data secure nation status (beneficial to India's IT sector), and liberalize visa norms for Indian professionals. With over half its population under the age of 25, India's trade policy, driven by demographic considerations, focuses primarily upon job creation as opposed to maintaining an export-focused orientation. India's demographic advantages have provided it with a young, skilled, competitive, English-speaking workforce, of which Europe will be lacking in the near future.

Considering this, India places considerable importance on Mode 4 liberalization. This will enable the free movement of individual professionals and will entail measures such as relaxation of immigration norms. The EU, however, has been unable to take a unified position on the matter, being subject to the individual immigration policies of member states. Thus, regardless of the election results in the European Parliament, it is highly unlikely this issue will be resolved soon unless both sides can reach an amicable compromise.

On the other hand, the EU wants India to reform its banking and insurance sector, provide tax reductions for wines and spirits, create a stronger intellectual property regime, and allow duty cuts on automobiles. Whether India can summon the political will to make these changes, especially in the context of the recent leadership change, is difficult to ascertain.

Way forward

Studies carried out expect more gain for both India and the EU in trade and investment relations in the future. The EU can gain in two ways. Currently, India levies higher tariff rates on the EU (compared to, say, Korea) and reduction of such tariffs can add more value. Secondly, other trading partners of the EU have trade pacts with the US while India does not, though India and the US have a strategic partnership and the US is excited about the 're-energized strategic partnership.' For this, domestic reforms, regulatory certainty, transparency and effective data protection are the key issues to be addressed for fuller utilization of the proposed India EU BTIA.

As for the way forward, three things are needed: improvement in Indian manufacturing through domestic reforms, slashing of tariffs and proper government procurement processes. India's manufacturing sector is still struggling, and providing a more conducive environment to domestic manufacturers by carrying out long awaited economic reforms, and addressing regulatory and governance issues will certainly improve domestic productive capacities. Domestic firms can then take a firm stand if required against EU companies under the FTA.

Launching long awaited economic reforms in India can be an incentive for EU firms to enter the Indian market. This could offset the impact of the tapering off quantitative easing, both by the US Federal Reserve and the European Central Bank by injecting appropriate capital flows in India. The Chinese experience of concluding the investment agreement with the EU appears like strategic action, as China has allowed EU investment, well aware of its manufacturing competitiveness. Moreover, a large chunk of China's exports to the EU are by non-Chinese firms, particularly by EU companies in China.

China's agreement with the EU appears a concomitant of its export led policy with its investment promotion policy, thus making a complete package of trade and investment. India can learn from the EU-China investment agreement while utilizing its services potential in the EU market by concluding the FTA negotiations.

However, specific issues such as greater access of the EU to Indian service providers by removing Mode 4 services, understanding the development problems of developing countries and allowing procurement beyond the WTO plus treatment for investment and intellectual property rights – mainly on the grounds of the need to supply generic medicines to some African countries – along with some SPS and TBT measures, need to be addressed properly by the EU.

Alongside, India could fix lower tariffs on the automobile sector and gradually moving towards more stringent IPR regulation and promoting of innovations. This may result in the mutual confidence needed in concluding the EU-India FTA. Access to the Indian market for EU manufacturers of telecommunication products and electronic goods has improved in 2013.

The Indian government has suspended, for example, the preferential procurement policy in favour of domestically manufactured electronic goods and telecommunication products. It has also postponed the mandatory testing and certification requirements for telecom network elements and has introduced changes in its investment rules which open the possibility for 100 per cent foreign ownership in the telecom sector, along with raised cap for FDI in retail, insurance and the defence sector.[19] With these developments, albeit slow, the EU-India FTA is marching in the right direction.

Between 2001 and 2012, bilateral trade in goods increased fivefold between the two, while trade in services increased six fold. The EU had a positive trade balance in both goods and services. With the introduction of the Look East policy, Indian trade with the EU has declined gradually. In 2003-04, EU's share in India's merchandise trade was 20.84 per cent which declined to around 13 per cent in 2012-13. However, the increase in EU exports share to India suggests that the EU is looking for a larger market base in India. It increased from 1.6 percent in 2003 to 2.2 per cent in 2012 (European Parliament, October 2013). These figures show the scope for further trade between the two groups.

India has introduced some changes in investment rules and allowed 100 per cent foreign ownership in the telecom sector. There was also a positive development relating to single-brand retail investments. Following the opening of the sector, some European companies have already applied for and received licences. One European company has also applied for a multi-brand retail licence, the first for a foreign company in India. Also, India is going ahead with opening up of its defence and insurance sectors, which may add to the existing investment potential. Aiming to double Indian business activity in Nottingham, this European city is looking at focused business initiatives with Punjab, Haryana and Chandigarh in the next five years.

Also, the new government in India has attempted to introduce several reforms to deal with supply side constraints, particularly in energy and infrastructure in the recently announced Union budget in February 2015. It has stepped up funds to infrastructure sector by nearly Rs. 70,000 crores. Recently, the government has increased the FDI equity cap in defence sector to 49% and is taking steps to ameliorate bureaucratic and administrative hassles. Indian big ticket projects have mainly suffered from delay in clearances from ministries, complex procedures to start the business and land acquisition problems.

All these factors coupled with low savings and investment, have hampered the growth prospects of the country. However, the new leadership in its Union budget has also attempted to bring about tax reforms and assured to implement the Goods and Services Tax (GST) by April 2016 and also carry out amendments to the GAAR in due course. These initiatives will lead to a positive outlook for India and help it receive more foreign investment.

Despite the points of contention between India and the EU, it is clear that the potential gains of an FTA outweigh the costs. The last Trade Sustainability Impact assessment for the BTIA was conducted in 2009 by the EU. The study indicated that a broad FTA would be fairly beneficial for both parties. In the extended FTA, the report posited an expected gain of €4.9 billion in the short run and €17.7 billion in the long run. Further, it pointed to potentially significant gains for the automobile, apparel and leather, investment, transport, and insurance sectors.

Of course, the new government is currently focused on domestic politics, and the question of an FTA with Europe has so far received less attention than in the past. Additionally, unless certain key issues are resolved through some give and take by both sides, the BTIA negotiations may remain stalled in the foreseeable future. However, keeping the communications channel open through an improved investment environment may lead to more effective FTA negotiations between India and Europe. India's new foreign trade policy is expected to be announced by the end of March this year and once that happens, it is expected that India and EU will be able to sit down and resume negotiations. ■

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WCO Data Model: the bridgehead to connectivity in international trade

Satya Prasad Sahu is Commissioner (Single Window), Indian Customs, and Laure Tempier is from the World Customs Organization

Issues related to redundancies in documentation and data required by government agencies have been addressed extensively over the last two decades, and several recommendations and guidelines have been developed to reduce the trader's effort, cost and time in carrying out regulatory formalities. Principal among them is the use of international standards for data and documentation. In this domain, the WCO is promoting the use of its Data Model, a collection of international standards on data and information required not only by Customs, but also by government agencies, in relation to the regulation of cross-border trade.

Studies conducted with regard to the time and cost involved in carrying out activities related to international trade transactions have underscored the significant impact of tasks associated with 'document preparation' and procedural formalities. It is commonly acknowledged that considerable redundancy exists in the information that a trader is required to provide for carrying out commercial, transport and regulatory procedures.

The initiative by Australia in 2005 to develop a standardized data set for international trade illustrates the scale of the problem. With Customs as the lead agency, the Standardized Data Set (SDS) Project was a whole-of-government exercise to establish a common platform for the submission to government of import, export and transit data.

The SDS project team collected 7,649 data elements from 41 government agencies. This number was reduced to 3,993 with the elimination of 'same as' elements within agencies, and harmonized to 650 after a first quick review. To illustrate, 22 agencies collected the name of the exporter on 118 different forms. It was used 212 times on those 118 forms, described in 61 different ways, and required in 16 different formats, ranging from 20 to 300 characters in length. The SDS project team standardized this entry to one data element – 'Exporter Name', 70 characters in length.

Issues related to redundancies in documentation and data, complicated regulatory procedures and paper-based processes have been addressed extensively over the last two decades, and several recommendations and guidelines have been developed to reduce the trader's effort, cost and time in carrying out regulatory formalities. Principal among them is the use of international standards for data and documentation.

International data standards

When data is interchanged between trade partners by means other than paper documents, eg. by tele-transmission methods including direct exchange between computer systems, a common 'language' should be used with an agreed mode of expressing it, ie. common protocols, message identification, agreed abbreviations or codes for data representation, message and data element separators, etc.

If a universally accepted standard is not used, the 'language' has to be agreed bilaterally between each pair of interchange partners. Taking into account the large number of parties exchanging data for an international trade transaction and the ever increasing number of potential users of tele-transmission techniques, it is obvious that such a bilateral approach is not viable.

Currently, there are at least three 'data models' for international trade, that is to say, models which organize data elements and standardize how the data elements relate to one another. The oldest is the United Nations (UN) Trade Data Element Directory (TDED). The TDED has 1,083 elements and their definitions are available on the web pages of the UN Economic Commission for Europe (UNECE). The TDED is closely linked to paper-based forms and contains information about the location of each data element on a standard paper layout.

The TDED is just a list of data elements and does not explain how to combine data elements into meaningful information and arrange them on an electronic template. However, TDED continues to remain relevant even in the electronic environment as it provides the basis for the UN Electronic Data Interchange for Administration, Commerce and Transport (UN/EDIFACT).

UN/EDIFACT comprises a set of internationally agreed standards, directories and guidelines for the electronic interchange of structured data, and in particular, that related to trade in goods and services between independent, computerized information systems. TDED helps construct the UN/EDIFACT components which are commonly used in Electronic Data Interchange (EDI).

The Core Components Library (CCL), with over 6,000 elements, could be said to be a further development on the TDED. The CCL has a wider scope and, unlike TDED, includes the concepts of data modelling. By following a set of technical rules, one can build electronic business documents. Of the 6,000 or so elements defined in the CCL, not all TDED elements are explicitly included. This is probably due to a more systematic approach in the CCL, which can represent several TDED elements in a more generalized CCL definition.

The WCO Data Model draws heavily from the above standards. First, it is by and large cross-referenced to the TDED. The WCO Data Model is also expressed through a standard UN/EDIFACT GOVCBR (Government Cross-Border Regulatory) message. The modelling principles of the WCO Data Model are largely similar to the CCL, as both are based on the Core Component Technical Specifications.

The WCO Data Model has been assessed extensively for compliance with the generic international data standards developed not only by the UN, but also by the International Organization for Standardization (ISO), which form its building blocks. ISO codes include Country Code (ISO 3166), Currency Code (ISO 4217), Dates, times, periods of time (ISO 8601), and Trade Data Elements (UNTDED - ISO 7372).

It may be said that the WCO Data Model is a value-added product based on all these well-recognized data standards. It responded to the need for an international data dictionary for the Customs domain that would both harmonize and simplify Customs data requirements.

The WCO Data Model

The WCO Data Model is a collection of international standards on data and information required by government agencies in relation to the regulation of cross-border trade. This collection was developed by the WCO after careful examination of all relevant international instruments and guidelines, along with national and industry practice, with the objective of achieving a consensus on the manner in which data will be used in applying regulatory controls in global trade.

The Data Model contains data sets for different border procedures, including definitions of data elements, recommended data formats and suggested code lists. The data elements are logically grouped into units of meaningful information, called "information models". These information models serve as reusable building blocks with which one can build electronic document and data exchange templates.

The Data Model also includes Information Packages, which are standard electronic templates linked to business processes – goods declarations, cargo reports, conveyance reports, licences/permits, and certificates. It is a library of data components and electronic document templates that can be used to effectively exchange business data. The fact that the Data Model uses globally recognized standards as its building blocks provides assurance of worldwide acceptance and adherence.

Information Packages

As mentioned earlier, the concept of Information Packages is unique to the WCO Data Model. Information Packages describe the various profiles of the different ways in which the Data Model can be used. Starting with very generic templates of information exchange, called Base Information Packages, Derived Information Packages, reflecting the profiles of usage with well-defined legal contexts, have been developed.

Each type of business application of the Data Model may have its own Derived Information Package. For example, for the ship-port interface, there is the International Maritime Organization (IMO) FAL Derived Information Package. For import, export and transit goods declarations, there is the Single Administrative Document (SAD) Information Package.

"All these developments point to an environment where supply chain information will be available to be exploited in real-time for regulatory purposes"

The European Union (EU) has endeavoured to produce specifications for its new Union Customs Code Implementing Provisions based on the WCO Data Model. It is also understood to be considering the production of an EU Customs Information Package that reflects the interface requirements of all its member states.

User profiles

The WCO closely monitors the worldwide adoption and use of the Data Model. Since its launch, WCO members have pursued an approach to suit their unique national situations. A number of members have used the Data Model in national projects to upgrade national IT systems or to develop Single Window solutions. Under a SW, government agencies merge their respective goods declarations through a process of harmonization and standardization of data. The Data Model has been very helpful in harmonizing the documentary requirements of different government agencies. For example, Canada has produced an Integrated Import Declaration, which contains the requirements of all participating agencies.

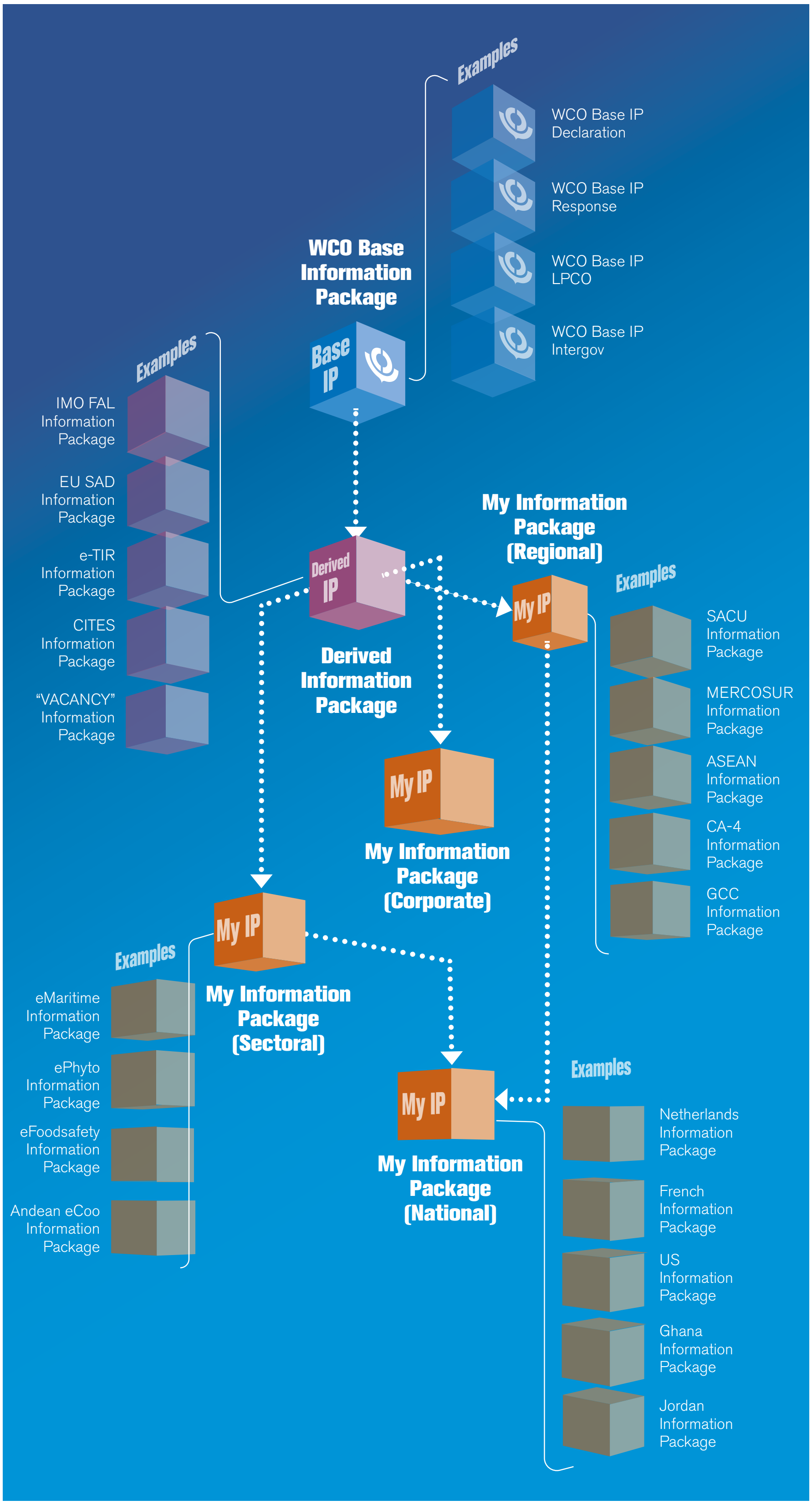
The implementation of border controls for certain groups of commodities usually involves licences, permits and certificates, which are issued by government agencies. These documents are interchanged by parties within and between countries. The Data Model Information Packages for Licences, Permits, Certificates and Other Authorizations (LPCO) have been developed precisely for this purpose.

The freight forwarders industry operates interfaces with Customs in order to provide crucial advance cargo information at various entry and exit points. Some of these interfaces may require pre-loading, pre-departure or pre-arrival cargo information, which calls for business agility and global data interoperability for interchange of information. Thus, in a transport contract requiring the provision of advance information to Japan and the EU for example, a freight forwarder can develop an interface based on the Data Model to successfully provide the required information.

Relying on data from export transactions from one country, a Customs broker can rapidly prepare the basic data for import in the country of import. To efficiently manage cross-border information flows, it is necessary to understand the requirements of different countries and legal regimes, using a global framework based on the Data Model and the associated local Information Packages.

Initiating adoption of the WCO Data Model

Whether it is a government agency or an entity in the private sector associated with international trade and transport, the decision to adopt or use the WCO Data Model involves a critical review of internal functional systems and software applications.



Since the exchange of information between organizations is involved, it is also necessary to develop an appropriate project concept and stakeholder engagement model. For Customs administrations, this means consulting national cross-border regulatory agencies in particular.

Each organization must review its existing business architecture and analyse its current information flows. Thereafter, the role played by the Data Model should be assessed. If a business model that ensures a favourable cost-benefit situation exists, then the organization should prepare a business plan involving the relevant functional, policy and information technology (IT) managers.

The Data Model is available free of charge to all government agencies and organizations, and to all other interested parties at a reasonable cost. Where an organization in the private sector is considering adopting or using the Data Model, it must develop an appropriate business model and contact the WCO in order to obtain the appropriate terms and conditions of use. The WCO offers the Data Model to all interested private sector entities on comparable terms of use on a non-exclusive basis.

One such entity in the private sector is GEFEG, which has a distribution agreement with the WCO. It is a company that has worked in the area of metadata development software for several years. Using its trademarked product 'GEFEG.FX', it currently markets the WCO Data Model in a structured reusable format, which offers efficient options for the rapid production of WCO Data Model implementation profiles, also referred to as Information Packages.

In order to produce conformant e-documents and messages, one must identify, tabulate, map and model the data contained in the prescribed forms with the Data Model. If this is done manually, it could take a considerable amount of time and effort. Using the GEFEG tool, this task is facilitated through a process of rapid customization.

The GEFEG tool is being used by Customs administrations, individual experts, governmental agencies, traders and other parties involved in cross-border processes. GEFEG, through its innovative solutions, has promoted the use of the Data Model by showing how it offers significant interoperability and conformance benefits to Customs administrations and partner governmental agencies by providing standardized cross-border data structures.

The future

The future of computing will be defined largely by ubiquitous, highly available computing facilities that will be used by mobile users to access applications on a variety of devices. These applications will depend upon, and result in, real-time information flows in step with progress in the execution of business processes. This is largely reflected in trends in the sphere of online commercial procurement, electronic invoicing, supply chain finance, the management of transport service requests, real-time inventory tracking and

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warehouse management solutions, fleet and load management, etc.

All these developments point to an environment where supply chain information will be available to be exploited in real-time for regulatory purposes. This concept is explored in projects that are testing 'data pipelines' that carry business data across the entire length of the logistical supply chain and can provide real-time, 'on-demand' data to Customs and other regulatory agencies.

This data is understood to be obtained first-hand from the source, uncontaminated by quality issues that creep in due to repeated transcription and interpretation by participating supply-chain actors. With minimal intervention, data entry and other costs, this approach is a win-win for both industry and government as it leaves fewer activities requiring intermediating efforts in data handling, allowing the industry and the Customs brokerage community to deploy its resources on crucial issues of local compliance.

This futuristic scenario is already a technological reality which is being exploited by an increasing number of business applications. Customs and regulatory agencies are still some distance away from realizing its benefits. The Data Model, with its Information Packages, promises to be just the right resource to capture and convey critical local knowledge to help build local interfaces based on global information flows that the 'plumbers' of the internet age can use to quickly help offer seamless flows of information, as envisaged in the 'data pipeline' concept. ■

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What future for Europe?

Europe is at a crossroads. Suffering from both internal failures and external pressure the intergovernmental model of the European Union has failed. What we decide to do next will determine European's quality of life, security and prosperity for generations to come, Benjamin Zeeb, the CEO of the Project for Democratic Union, writes

When I was asked to write an article about the future of the EU, the first question that came to mind was: which of the two possible scenarios? I understand that the reader has probably become accustomed to perceiving the future as an endlessly complex accumulation of possibilities and probabilities, largely incomputable due to countless contingencies and the unforeseen consequences of unforeseen actions. So collapsing all possible fates of Europe into two basic scenarios might not sound very convincing at first. But bear with me for a moment because where it counts, regarding the issues that truly determine the wellbeing of the continent and the security and prosperity of its inhabitants, the future of Europe has become a lot less complex than you might think. It has indeed become a binary problem.

Muddling through is over: it's make up or breakup time for the eurozone

If we haven't learned much from latest round of negotiations between the euro group and Greece, one lesson is very clear: for both parties sitting at the negotiation table, or more accurately, writing letters back and forth between Europe's capitals, the status quo has become unsustainable.

Nevertheless the fiction of actual agreement was upheld with Greece formally staying the course and Germany somewhat less formally allowing Greece some room for manoeuvre regarding its primary surplus. It is of course a deal that has no chance of lasting and in a few months' time we will be once again holding our breaths as the game begins anew. Meanwhile the stakes couldn't be higher: with Spain voting in December and Podemos polling highly there, the crushing uncertainty that has been with us for the past half- decade, chipping away at our spirits, keeping away foreign business and investment and emboldening our opponents to the East, will only increase.

"The eurozone in its current form has stopped working."

Given this situation it is now time for us Europeans to overcome our intellectual and cultural divides and to calmly assess our options. It is time to look for consensus even in the most unlikely of places. So instead of, for example, constantly reinforcing the differences in positions by the Anglo-American Keynesian camp and the central European ordoliberals, we would do well to take a look at what they actually agree upon.

We would do well to realize that both Paul Krugman and Hans-Werner Sinn, to take two of the most prominent representatives of either school, have repeatedly stated that under the current rule-set there is no credible way for Southern Europe to make its way back towards prosperity. While disagreeing on who's fault that is, whether Southern profligacy or German austerity is to blame, both have made very clear that under the current

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"... we Europeans need to push for a single act of debt consolidation and parliamentary fusion that would solve the current dilemma once and for all"

conditions large parts of the continent will remain immersed in high unemployment, deteriorating social conditions, and inner turmoil.

Furthermore, both have pointed out the inherent folly in Germany's ever-growing trade surplus. Again there are differences, with Krugman thinking of the problem in terms of a vile beggar thy neighbour policy through which Germany essentially crushes all countries trapped with her in the eurozone, while Sinn laments Germany essentially accepting IOUs for all the fine products it exports when there's virtually no chance of ever collecting on them. But the basic agreement is overwhelming: the eurozone in its current form has stopped working.

> *"Staying the course, muddling through, hoping and praying for confidence to magically return to save the day won't get us out of this mess. Neither will an ever more accommodating monetary policy."*

This shouldn't come as a huge surprise given all the scepticism that accompanied the euro's introduction in 1999. The very basic law according to which currency unions never work unless they are also political unions enabling automatic transfers, has prevailed. Mario Draghi once compared the common currency with a bumblebee, a miraculous creature that against all rational expectations and seemingly defying the laws of nature takes to the air to fly. Well, it turns out that just like in nature, where that bumblebee only flies under very favourable conditions, the euro too relied on such unlikely conditions to function. As soon as investors began to doubt Europe's cohesiveness and bond spreads began to widen, the game was up and Draghi's bumblebee faltered.

Staying the course, muddling through, hoping and praying for confidence to magically return to save the day won't get us out of this mess. Neither will an ever more accommodating monetary policy. The simple truth is that the days of the European Union, a hybrid construct that is held up by wishful thinking as much as endless legal procedure are numbered.

Now that this Union is really being tested by internal strife and challenges abroad it has revealed itself to be not much more than a reincarnation of the old Holy Roman Empire. With its emasculated emperor, over-mighty princes, weak parliament, and sclerotic courts the old Reich proved incapable of marshalling its vast resources for the common good of its inhabitants and ultimately broke apart. Even if we wanted to, we cannot and will not continue on the path we are currently on. This leads us to the above-mentioned fork in the road where Europe is left with but two alternatives.

Scenario I: the break-up

There are those among us who believe that in a situation like this it would be best to just throw in the towel and go back to the tried and true system of national states, each with their own currency controlled by their own central bank. Greece, Italy, Portugal and Spain could thus regain their competitiveness by devaluing their currencies and get back some of the sovereignty lost as a consequence of joining the eurozone. Real democratic legitimacy and popular rule could be re-established, they say, within the borders of Europe's national states and the painful path of internal devaluation abandoned.

> *"Europe has existed in this state before and could again"*

While this solution doesn't sound very optimistic from a European point of view, as it is opposed to the status quo of just continuing what we are doing now, it at least has the benefit of being remotely possible.

Of course most European countries are far too small for us to really speak of sovereignty in the true sense of the word as the dependencies on other European nations, let alone the US, Russia, and China would be immense. But Europe has existed in this state before and could again. We would not have to constantly worry about a carefully calibrated balance, always in danger of falling apart. While floating currencies would substantially hurt their bottom line, the Germans could pretend to themselves that they are not giving away anything to their neighbours; and governments in Southern Europe could once again return comfortably to their old ways of backscratching and nepotism without being scrutinized by any higher authority.

There are several game plans in circulation regarding this option. The most extreme versions, laced with a healthy dose of nationalistic fervour and animosity towards their respective European neighbours, are of course being peddled by the various right wing anti-European parties that have been gaining in influence since the inception of the crisis.

Marine Le Pen in France, Nigel Farage in the UK, Bernd Lucke in Germany all view some version of the breakup scenario as not only the inevitable outcome of the current crisis but also the logical end to the folly that was the European integration process. Their arguments highlight politics of culture, race and identity, decry immigration (an immigration that given current birth rates Europe desperately needs) and just generally show a lack of basic human compassion, solidarity and intelligence.

Concerning ourselves with these half-baked ideas is a waste of time. There are, however, other voices within the dissonant choir of eurosceptics calling for at least some controlled exits from the eurozone that we need to take more seriously.

The aforementioned Hans-Werner Sinn, for example, holds the view that given Greece's incapability to ever return to growth and full employment under the current conditions, calls for a temporary exit of the country from the eurozone. Writing off most of its debts and using the drachma to repress wage growth through inflation to once again become productive and regain its competitiveness Greece could then rejoin the common currency after a decade or so when it has reached a level where its simultaneous existence in the euro next to Germany could actually work out.

> *"Already the Greeks have played rapprochement with Russia as a card in the current negotiations and were they to leave the resulting geopolitical vacuum would present a welcome opportunity for foreign powers to exploit"*

The problem with this idea is not really a matter of economics; it's a matter of strategy. Ten years outside of the eurozone is a very long time. Already the Greeks have played rapprochement with Russia as a card in the current negotiations and were they to leave the resulting geopolitical vacuum would present a welcome opportunity for Russian but also Chinese and other foreign interests to exploit.

For many in Europe, especially in Germany, where concerns over foreign policy and security don't rank very highly anymore ever since the Eastern enlargement comfortably surrounded her with friendly nations, this threat doesn't really resonate.

But the facts remain: in Ukraine Russia's occupation of Crimea and the Donbass have created what Rebecca Harms, president of The Greens–European Free Alliance group in the European parliament, recently called a *"launch pad for distortion"* from where Mr Putin intends to constantly destabilize the country. It would be naïve to assume that similar problems and a similar campaign against Europe's interests wouldn't arise within a newly independent Greece.

In the current war on Europe's eastern border, Russia's aggression is not merely directed at NATO, it is directed the EU, and the model of civil society and rule of law that it represents. Timothy Synder, one of the most respected experts on the Ukraine issue, sees the conflict as a contest between those who wish to oppress civil society and those who wish to embody it.

As such it remains a central element of a larger historic struggle. In the context of this fight, a repeat of Poland's success story in Ukraine or any other of its former satellites presents the Russian government with problems that can only be called existential. Given this threat, there's little doubt that Russia would jump on any opportunity to weaken the EU to weaken the social model it stands for. Irrespective of this dilemma, it remains highly doubtful that Greece - or for that matter any other country leaving the common currency to rejoin it later - could by itself ever muster the strength to meet her European partners at eye level.

> *"For centuries the struggle over the central European lands, rich in resources and population, has haunted Europe."*

Most worrying of all, however, In the case of a European breakup, the 'German question' would once again return with full force. Over past centuries European politics was dominated by a never-ending struggle over Germany. Whether the Germans were too weak, as they were during the 30 years war, when foreign armies ravaged their territories, or too strong, as was the case from the second half of the nineteenth century, when they proceeded to set not only Europe but the entire world on fire, the struggle over the central European lands, rich in resources and population, has haunted Europe.

While the EU has managed to contain German power and the Germans themselves have changed through the experience of two devastating wars, the structural problem, potentially pitting Germany against its neighbours - most importantly France - if their close ties where to be loosened, remains.

A Europe divided, incapable of integrating Germany, to contain it when necessary but also to mobilize its recourses for the good of the continent, in short is not only a likely but also a deeply troubling perspective.

Scenario II: Europe forms a mighty democratic union

With muddling through out of the question and a breakup

undesirable, only one solution remains: the creation of a federal state based on the member countries of the eurozone.

For decades European federalism has been regarded as the project of dreamers. Old men mostly, some of them retired heads of state, who got a little too creative after they left office and dreamt up a Europe that according to realistic assessments sounded like a nice idea, the implementation of which, however, belonged somewhere in a more distant a future. Some young students and idealists might follow such a folly, but surely it wasn't a prospect any serious commentator would consider.

It is not without irony that we have now come to a point where this dream however grandiose it might appear holds up far better when confronted by the challenges of European realpolitik than any of the solutions still considered more likely by many analysts. Some of them are slowly waking up to the fact that when all other possibilities have been eliminated, what remains must be the only credible way forward.

> *"We cannot allow the continued existence of a power vacuum at the heart Europe."*

Loosely based on the Anglo-American model, first implemented in 1707 when Scots and Englishmen formed a union to better defend against foreign aggression, and later adopted by the United States of America, the new European Democratic Union would have to find its own way to deal with the necessary realignment. Crucial to the process however is the modus by which the change has to be made.

So far Europe has depended on a sequence of small steps on its path towards deeper integration. This modus operandi has failed. To avoid the fate of the Holy Roman Empire, where ideas about forging a more capable and lasting union were discussed over decades only to be forgotten or disregarded, we cannot allow the continued existence of a power vacuum at the heart Europe.

For the European Union, built to diffuse power, rather than to focus it in the hands of a legitimate representative, lacks the tools to bring about meaningful change in its internal makeup. Instead we Europeans need to push for a single act of debt consolidation and parliamentary fusion that would solve the current dilemma once and for all. The only way this can be made to happen is by referendum. A referendum of all citizens of the eurozone and those currently debating to join it.

> *"The Project for Democratic Union argues for the establishment of a Presidential system, in which the European Parliament would take on the role of a fully invested legislative chamber"*

To make the economics work, the new union would have to be a transfer union where transfers work through the union budget. Direct payments between members are obviously unsustainable for both practical and political reasons. This system of transfers already works well within many of the eurozone's member states, as well as elsewhere.

The state of New York, for example generates federal revenues of around $230 billion a year of which only around $135 billion are actually spent in NY. The rest of the taxes levied in the state is redistributed across the US through federal programs like Medicare, Medicaid, social security and infrastructure - and military expenditures. Florida on the other hand spends $284 billion a year and brings in only around $141 billion in taxes. That's a $143 billion each year that Florida receives from the US.

Despite all that is wrong and dysfunctional within the US federal system (mistakes Europe would not have to repeat) nobody in NY would seriously consider breaking away from the United States. Likewise Americans don't seriously consider expelling Florida. A union holds benefits beyond monetary concerns and all conflict aside the Americans understand as much.

Concretely, we at the Project for Democratic Union argue for the establishment of a presidential system, in which the European Parliament would take on the role of a fully invested legislative chamber. Non-union business would be left primarily to regional administrations, thus ensuring the most direct connection of the administration with its constituents. Nation states would continue to be represented in a senate made up of two delegates from each of the constituent states. Their bureaucracies and parliaments, meanwhile, would be stripped of much of their authority. The Union administration would command a single European army and be in sole control over the Union's finances.

> *"The old narrative is perfectly fine. What we need are new structures capable of turning this European promise of peace, prosperity, security and solidarity from a youthful and distant dream into a reality."*

But what about the people? Would they really go for it? Already scepticism against Europe is high and why would anybody be willing join such a project? The answer is twofold: first, we need to make absolutely clear that unification doesn't mean one has to give up one's national identity, culture or language. While Union business would be conducted in English, the use of the respective languages in their home territories should be preserved.

This is not a love marriage where we dream up some common narrative to gather everybody around the campfire to sing happy songs. It is grim necessity that brings us together, not unlike it brought together the Scots and the British 300 years ago, when they first forged a union that has allowed them to punch above their weight ever since. They may never have learned to love each other, but centuries later they still decided to renew that bond. It is to be hoped that maybe 300 years from now Europe will get chance to do the same.

The second reason lies within the realization that most European nations have already lost their sovereignty. So instead of an act to lessen their ability to decide their own fates, union actually re-empowers Europeans to make their voices heard and to have their interests looked after. Elected representatives, accountable to their own constituencies would make up a European Parliament that actually defines where we go as a Union.

Europe isn't lacking a common narrative or a common cause for us all to get behind, we don't need some new goal that we can all pursue together. The old narrative is perfectly fine. What we need instead are new structures capable of turning this European promise of peace, prosperity, security and solidarity from a youthful and distant dream into a reality. ■

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The EU is listening to business' cries for reform

Lucy Thomas is Campaign Director at Business for New Europe (BNE)

Whatever the outcome of the forthcoming general election, Britain's future relationship with the EU will be a major theme in the years ahead. Whether or not there is a referendum in the next five years, there needs to be a period of reform to make the EU more competitive and streamlined, with a focus on cutting red tape where possible.

The future of Britain's EU membership leapt fully into the public consciousness in January 2013, when David Cameron gave a speech at Bloomberg pledging to hold an in-out referendum. In that speech, he made some welcome comments on the reforms needed to make Europe fit to compete in the 'global race'. And this reform agenda has been led by the UK working with friends and allies across Europe to see where things can be done better in national capitals rather than Brussels.

Now momentum is growing both among other EU leaders and across the EU institutions to change the way things are done. Instead of focussing solely on what Europe can do to legislate, there is an appetite for things to be done at a member state level. As the new EU Commission Vice President for Better regulation put it, decision-making should be: *"national where possible, Europe where necessary"*.

Back in June 2012, Mr Cameron organised a joint letter with 11 other pro-reform EU leaders, including the prime ministers of Italy, Spain and Poland. The letter called on the EU to deliver reforms to make the EU more open and business-friendly: completing the Single Market in digital and services; an integrated European energy market; signing free trade agreements with other countries, in particular the United States; reducing the regulatory burden; and enforcing subsidiarity- the idea that powers should remain at a national level unless there is a compelling reason for them to be exercised by Brussels.

The Prime Minister re-emphasised many of these points in his Bloomberg speech. He particularly praised the single market, saying: *"When the Single Market remains incomplete in services, energy and digital - the very sectors that are the engines of a modern economy - it is only half the success it could be. It is nonsense that people shopping online in some parts of Europe are unable to access the best deals because of where they live. I want completing the Single Market to be our driving mission."*

It is worth setting out, briefly, what some of these reforms would mean in practice. First, the Single Market. Trade in goods across the EU is now almost completely free. But barriers to access in services remain in place. Breaking these down - for example, by opening up public procurement, creating cross-national telecoms networks and better enforcing the Services Directive - could create efficiency gains worth €235 billion a year across Europe. We in Britain would be especially well placed to take advantage of this, for services make up 78% of our economy, and we have a huge comparative advantage in financial, legal and professional services.

The Single Market came into force in 1993, when few could have imagined the way in which the internet was going to reorder our lives - and our ways of doing business. As David Cameron pointed out, it is far too difficult for online retailers to sell to other EU countries. Europe's digital sector is far too fragmented across national lines - surely part of the reason why the continent has not generated a tech company to match the American giants. Creating a Digital Single Market will require harmonisation of online purchasing, e-invoices and receipts, protection of intellectual property, and more besides. It is estimated that this could boost EU GDP by 4%, or €260 billion.

The EU's trade policy has featured prominently in the media recently, generally for the wrong reasons. The offending acronym is TTIP - the Transatlantic Trade and Investment Partnership - a free trade and investment deal with the United States that could be worth £10 billion a year to Britain's GDP. TTIP has provoked opposition, particularly among unions and NGOs, and the European Commission is working on improving the more controversial aspects of it. But there can be no denying the potential commercial benefit of a good deal between the EU and Britain's largest single trading partner and source of investment.

Political realities across the Atlantic can be protectionist - the Buy America Act is a good example - and so only by working with our EU partners can we get a far-reaching and balanced deal. Free trade deals negotiated by the EU have a very positive track record - after the 2011 agreement with South Korea, UK exports there rose by 82%, and we now run a trade surplus. The CETA with Canada, on which negotiations have recently concluded, will equally be very positive for the UK. And the EU is eyeing up further deals with India and Japan.

As a recent report by the Association of Financial Markets in Europe (AFME) showed, the EU's undersized capital markets are *"limiting growth in Europe."* The EU needs a single capital market, and it needs to break down barriers within states as well. The big prize here is funding to SMEs, the vast majority of which in Europe comes from banks. Britain's European Commissioner, Jonathan Hill, has been charged with developing a Capital

Markets Union in order to change this. It is estimated that this could unlock €60 billion a year for businesses, and the director of much of the money would be Europe's financial centre, the City of London.

The development of an Energy Union could save businesses and consumers across the EU €50 billion a year. Even more importantly, given the current situation in Ukraine, they could reduce the susceptibility of European nations to 'energy blackmail' by gas-rich states. This does not require some hugely expensive building of nuclear and renewable power generation. What is needed is a single European energy market, so countries with lots of generation capacity can simply sell power to those with less. This will require developing hubs and exchanges to let power flow across borders, and a single system of pricing and regulation on a continent-wide level.

The case against EU regulation is generally overstated. Firstly, in order to have a Single Market, you have to have standardisation of regulatory standards. Secondly, this standardisation more often than not makes businesses lives easier. In 2013, an Open Europe study of the 100 most onerous pieces of EU legislation found that the benefits to British business outweighed the costs by £30 billion. Thirdly, much of the regulation that irritates business is in fact UK government 'gold-plating' of European legislation - for example, going further than the Pregnant Workers Directive in allowing women to resign their posts on the day they return from maternity leave.

However, there are plenty of ways in which Brussels should improve its regulatory output. It must stick to the COMPLETE principles of better regulation, reducing the volume and complexity and introducing much better impact assessments. Also key to this is the principle of subsidiarity- unless there is a compelling reason for the EU to legislate, the matter in question should be left up to the member states. Fortunately, and thanks in part to continued British pressure, the new European Commission appears to be moving down this road.

The prospects in Brussels for progress on all of these fronts look very encouraging. The 2015 Work Programme, which outlines the Commission's agenda for the year, focuses on structural reforms, such as completing the Single Market, Energy Union and TTIP. Moreover, Brussels seems to understand the need for better quality and reduced regulation. The Work Programme withdrew 80 pieces of regulation, and proposed just 23- a fifth of that seen previously.

So the question on businesspeoples' lips is: so much for the talk, but will they walk the walk? Again, things seem to be looking up. Last month, a green paper on Capital Markets Union was unveiled by Jonathan Hill, Britain's European Commissioner. He aims to have it in place by the end of the Commission term in 2019- ambitious, but certainly doable. Frans Timmermans, formerly the Dutch Foreign Minister, has been appointed First Vice-President of the Commission, with responsibility for better regulation. The Dutch attitude to the EU can be summed up in the phrase 'Europe where necessary, national where possible,' and Timmermans has brought this state of mind with him to Brussels. All legislative proposals by Commissioners have to go through him, so the regulatory output will be smarter and more joined-up than was previously the case.

The line-up of the rest of the Commission also bodes well for reformers. Key economic portfolios are held by reformist politicians from states usually friendly to Britain: Sweden's Cecilia Malmström at Trade; Denmark's Margrethe Vestager at Competition; and Jyrki Katainen of Finland at Jobs, Growth, Investment and Competitiveness.

"Measures that have been part of the British agenda for years now form the centrepiece of the European Commission's agenda"

An example of the new pragmatism was seen in the attitude to genetically modified crops. For fifteen years, a common EU approach on this subject was made impossible by divisions between the member states. So the Commission simply decided to devolve decision-making to national capitals; those states (such as Britain) which want to grow GM will be free to do so, as will those who want to ban it.

The case for reform has not just been embraced in Brussels- it is now accepted across almost all the EU's national capitals. Take France. Elected in 2012 on a traditionally socialist platform, President Francois Hollande is now gunning for reform. In February, he forced a bill extending Sunday trading through the National Assembly. His new team - led by Prime Minister Manuel Valls and Economy Minister Emmanuel Macron - is much more business-friendly and open for reform that could have been hoped three years ago.

Italian Prime Minister Matteo Renzi is another lead in the mould of Valls and Macron - young, reformist and bold. Last year, he defied immense pressure from trades unions and his own party and passed an act making it easier for companies to dismiss workers; cut taxes for low-earners, and has made it easier to start infrastructure projects. In Berlin, Angela Merkel's government is fully committed to structural reform, and has insisted on linking reform to bailout packages for the countries like Spain and Greece.

The evidence suggests that this is beginning to work. Despite all the instability caused by the Greek saga, the eurozone's growth forecasts have been upgraded to 1.9% next year. Spain created 400,000 new jobs last year, and confidence indices for manufacturers and the service sector alike are positive. The eurozone has a very long way to go, but the political will seems to be there.

The most optimistic, some might say cynical, of British eurosceptics seem to believe that we can leave the EU, retain access to the Single Market and benefit from most these reforms anyway. They are selling a dream. On Capital Markets Union, for example, no city in Europe will benefit more than London; unless we leave. The EU is not going to allow its financial centre to be placed outside the bloc. Unable to fight for reform, we would be subject to EU legislation that we had no say whatsoever in making- regulation without representation. Moreover, without Britain's liberal and open voice at the table, it is likely that Brussels' regulatory output would increase if we left. And it is fantasy to think that Britain could, for example, break down American barriers to create a separate transatlantic trade deal without the weight of the rest of the EU behind us.

Member states, with Britain at the forefront, will need to keep pushing Brussels to carry out its promises. Protectionist and restrictive sentiment in other EU countries will need to be overcome. Measures that have been part of the British agenda for years now form the centrepiece of the European Commission's agenda. Eurozone states are finally grasping the nettle of structural reform. British trade with the rest of the EU has been pretty stagnant since the financial crisis, but the green shoots of recovery are now evident. In recent weeks, more and more businesses have come out to say that we should stay in - from banking giants like Standard Chartered, to the small businesses represented by the North East Chamber of Commerce. Britain has a history of leading in Europe - the Single Market, to take one example, was largely a UK creation - and the prize of implementing further economic reforms is immense. We shall only see them happen, and we shall only benefit from them, as an engaged player in the European Union. ■

Discerning Europe's fiscal situation

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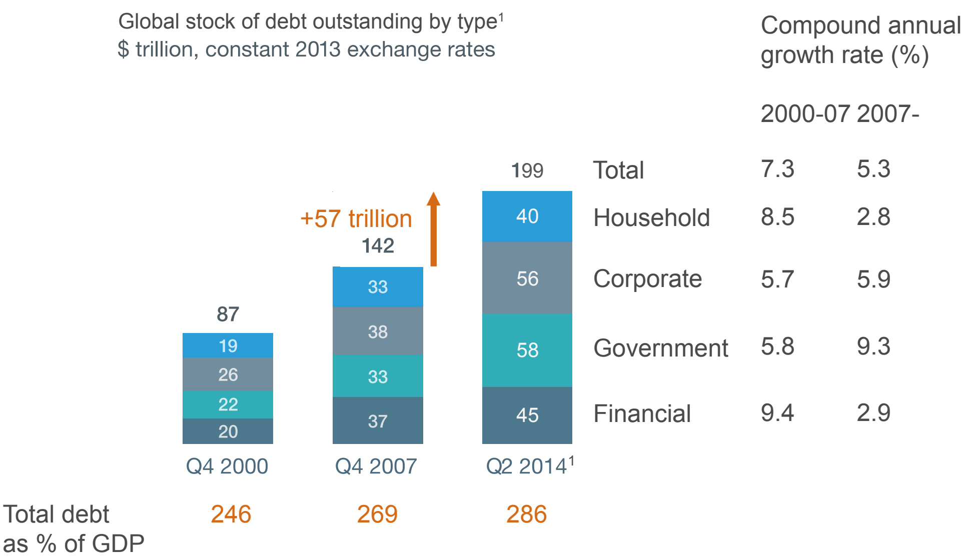
Since the Great Recession began in 2007-08, global debt and leverage have continued to grow. From 2007, through the second quarter of 2014, global debt grew by $57 trillion, raising the debt to GDP ratio by 17 percentage points. This is not as much as the 23 point increase in the seven years before the crisis, but enough to raise fresh concerns. Governments in advanced countries, including in the European Union, have borrowed heavily to fund bailouts in the crisis and offset falling demand in recession. See the figure given below.

The high debt situation in Europe, particularly, has been a cause of concern related to the slowdown in growth accounting numbers and a higher risk to financial crises (debt induced crises). Given the magnitude of the 2008 crisis, it has been quite surprising to see (Figure 2) that no major economies and only five of the developing countries have actually reduced their ratio of debt to GDP in the 'real economy' (households, non-financial corporations and governments excluding the financial sector). In contrast, Mackenzie Consulting in its latest report finds out that 14 countries have increased their total debt to GDP ratios by more than 50 percentage points. Figure 2 and 3 give us a good indication on this.

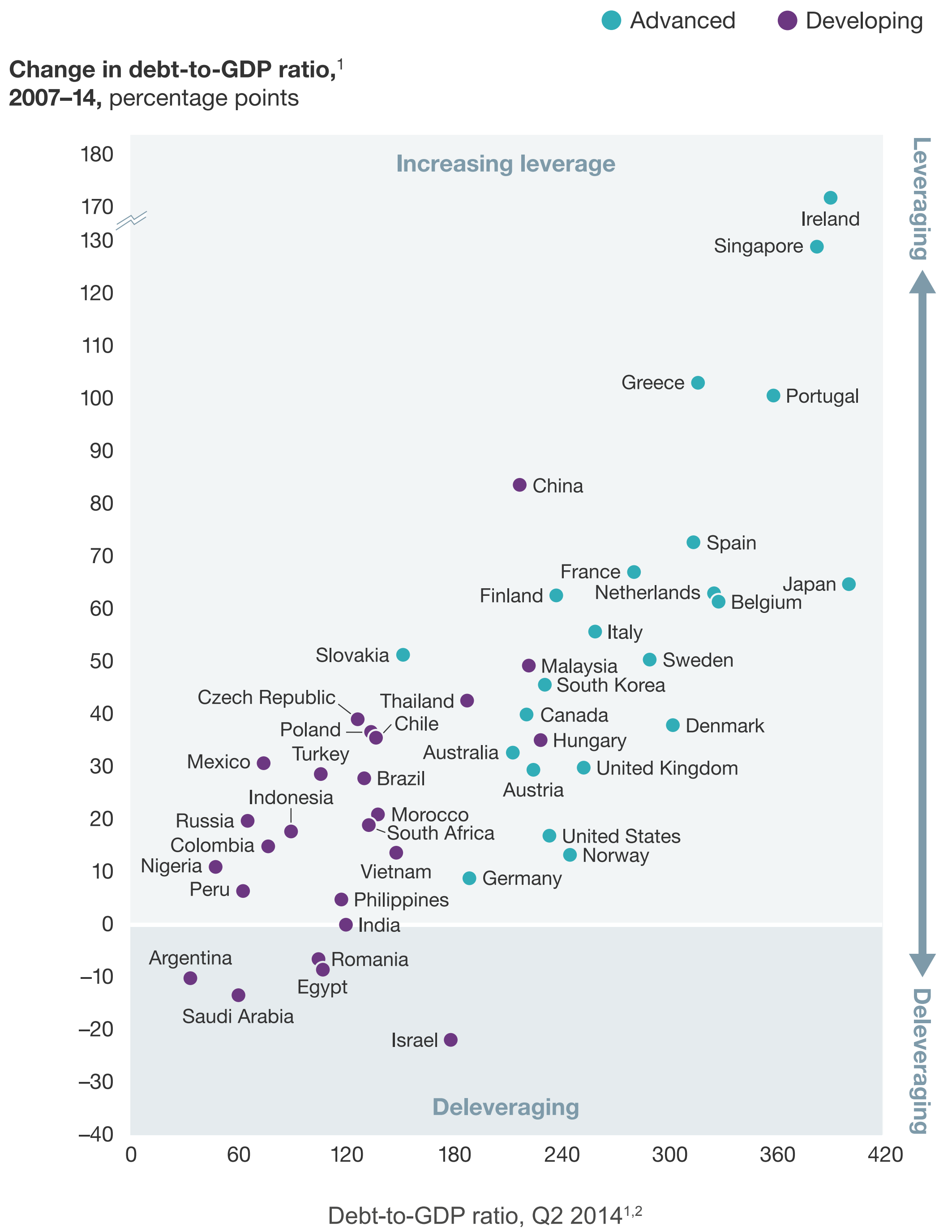
On 8th December 2011 Thomas J Sergent[1], in a Nobel Prize winning lecture, presented an interesting historical case study of the United States in reference to the large debts accumulated during the US War of Independence which led to a US fiscal

Figure 1. Global debt has increased by $57 trillion since 2007, outpacing world GDP growth



1. 2Q14 data for advanced economies and China; 4Q13 data for other developing economies. Note: Numbers may not sum due to rounding.
Source: Haver Analytics; national sources; World economic outlook, IMF; BIS; McKinsey Global Institute analysis

Figure 2. The ratio of debt to GDP has increased in all advanced economies since 2007



1. Debt owed by households, non-financial corporates, and governments.
2. 2Q14 data for advanced economies and China; 4Q13 data for other developing economies. SOURCE: Haver Analytics; national sources; McKinsey Global Institute analysis

crisis in the 1780s. The analogy of America's historical fiscal situation then, if given relevance, certainly seems to have a critical lesson and bears similarity with Europe's plight today. In a press release that jolted the markets a few days back, the ECB recently announced it will no longer accept Greek government debt as collateral. Though only time will tell how this is likely to impact the Greek economy and its fate in the Union. But Greece is not the main problem but just the tip of the iceberg if we look at the region as a whole.

History tells us that democracies have a tendency to balance conflicted interests. The case of America's constitution history in the late 18th century provide episodes on the government net of interest surplus process and therefore the value of government debt. Americans in the late 18th century tried two of them; first the Articles of Confederation that were ratified in 1781, and then the US Constitution that was ratified in 1788.

These constitutions pointed out by Sargent embraced two very different visions of a good federal union. The first constitution was designed to please people who preferred a central government that would find it difficult to tax, spend, borrow and regulate foreign trade. The second served opposite interests. Europe today is in a serious need of seeing such a transition to cater to contrary interests of the people across European nations today. The US framers abandoned a first constitution in

"Europe made a serious mistake... by not strictly keeping a check on the implementation guidelines of the Maastricht Treaty"

favour of a second because they wanted to break the prevailing statistical process for the net-of-interest government surplus and replace it with another one that could service a bigger government debt[2].

The issue here, thus, seems to be much more fundamental for Europe and its member nations that is distant from the monetary or financial woes of the region. The region once (and probably still in a lot of academic discourse) is cited as a benchmark example in the process of regionalization for economies to better engage in trade, commerce and address structural socio-economic problems collectively as a region. As a monetary union, the European region might have done well to have established the euro as a common currency and in gaining a uniform consensus amongst most member nations on that (with the exception of the UK as a big player). However, not safeguarding sustainable fiscal targets at the macro and micro level (within the member countries) is a major problem.

Re-echoing Sargent's arguments, confused monetary-fiscal coordination at a country or regional level creates costly uncertainties. Fiscal and monetary policies are always coordinated and are always sustainable, even though they may be obscure. For the US, they coordinated them by adopting a commodity money standard and restricting states and banks' ability to create fiduciary monies. Europe made a serious mistake, especially the European Central Bank, by not strictly keeping a check on the implementation guidelines of the Maastricht Treaty (under the Stability and Growth Pact) in 1992 with reference to keeping a 3% of the Government Debt to GDP ratio target for all member nations. A pertinent fact worth mentioning here is that the first country to break this 3% fiscal target was Germany and not Italy, Portugal, Greece nor Spain (PIGS). The PIGS nations just followed Germany's suit but situation got worse for them vis-à-vis Germany[3].

In terms of fiscal arrangements, the EU today has features reminiscent of the US under the Articles of Confederation. The power to tax and other fiscal instruments lie with the member states. Unanimous consent by member states is required for many important EU-side fiscal actions. As Sargent says:

"Reformers in Europe today seek to redesign these aspects of European institutions, but so far the temporal order in which they have sought to rearrange institutions has evidently differed from early US experience in key respects. The US nationalized fiscal policy first and for the US framers, monetary policy did not mean managing a common fiat currency, or maybe even having a common currency at all. The EU has first sought to centralize arrangements for managing a common fiat currency and until now has not wanted a fiscal union. And to begin its fiscal union, the US carried out a comprehensive bailout of the government debts of the individual states. So far, at least, the EU does not have a fiscal union, and dew statesmen now openly call for a comprehensive bailout by the EU of the debts owed by governments of the member states."

The policymakers need to identify the eurozone as one single country, like the US or the UK if they have to ultimately solve EU's problems. The US until quite recently was also undertaking significant austerity measures, even though there was no significant market pressure to do so. The main argument for doing so is that the government debt has been too high. The common fiscal policy needs to be countercyclical and not pro-cyclical and Keynes today would have said exactly this. However, the political considerations and situation would need an 18th century US-like transformation to cater for Europe's stability and existence in the future. ■

1. Link to the complete lecture and paper: http://ec.europa.eu/economy_finance/economic_governance/sgp/index_en.htm
2. The term 'framers' used by Sargent In his lecture instead of 'founders' or 'founding fathers' is more descriptive of how they thought of themselves, namely as creators of an institutional framework within which their successors would act. See Rakove (1997).
3. One of the reasons why Germany was able to keep a check on its debt levels was by keeping a large reserve base of foreign currency reserves and also by containing inflation over time.

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Corporate taxation in Europe: let's get it together!

Willem Pieter de Groen is a Research Fellow in the Financial Markets Unit at the Centre for European Policy Studies (CEPS)

Lux leaks has placed the issue of corporate tax avoidance and evasion once again on the political agenda. In November 2014, the International Consortium of Investigative Journalists[1] unveiled the secret tax deals struck by about 350 multinational companies with the Luxembourg authorities, which allowed them to reduce their corporate income tax (CIT) bill. The companies used mismatches in the tax systems as well as deals with the authorities to reduce both the effective tax rate and the base.

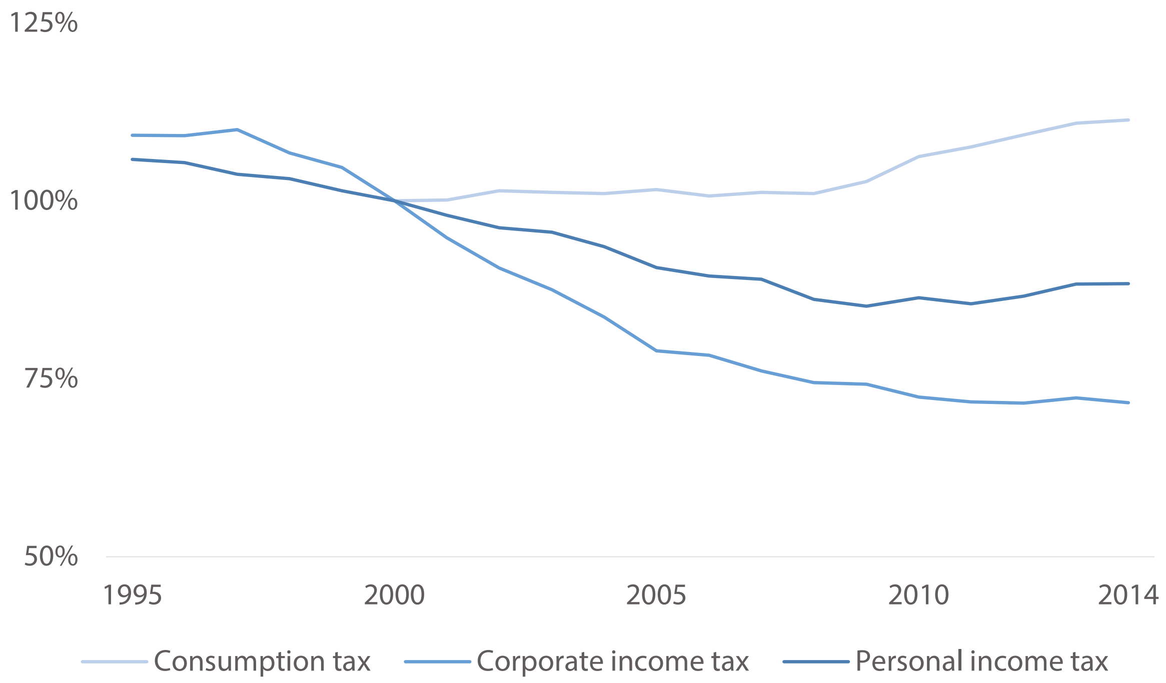
Lux leaks is not the first and is unlikely to be the last tax-avoidance scandal. It followed the public outrage provoked two years earlier in the United Kingdom over reports that the US coffee shop chain Starbucks had substantially reduced its tax bill by paying royalties to its regional headquarters in the Netherlands, which has a regime with low rates on royalties. In turn in the Netherlands, the government-owned national railways attracted public attention when media disclosed that it transferred profits to Ireland to benefit from the lower corporate income tax rate.

But Ireland (with 12.5% CIT and attractive intellectual property (IP) regime), Luxembourg (advance agreements) and the Netherlands (IP regime and tax treaties) are definitely not the only EU countries with tax regimes that facilitate tax avoidance. Hence, also Belgium (notional interest deduction and IP regime), Cyprus (12.5% CIT and tax treaties), Estonia (deferral of CIT), Malta (low CIT) and Spain (tax credits and IP regime) are known for having schemes that allow multinationals to lower their tax bill.

The corporate tax evasion is a side effect of the tax schemes that mostly aim to make a country more attractive as a location for (high-growth) foreign companies or to facilitate business-service industries. This in itself is already distorting, since investments are not necessarily taking place at the locations where they are most efficient. In addition, the competition based on tax schemes presses other member states to make their tax system more attractive for international companies to preserve their competitive position. In fact, in the past two decades, the average top CIT rate has declined almost one-third from 35% in 1995 to 23% in 2014. The variance between the top and bottom rate has further narrowed in the same period by 25-28 percentage points.

In order to make up for the lower CIT-rates, member states need to shift the tax burden to other less-footloose companies or to charge more on rates that are harder to avoid (see Figure 1 for

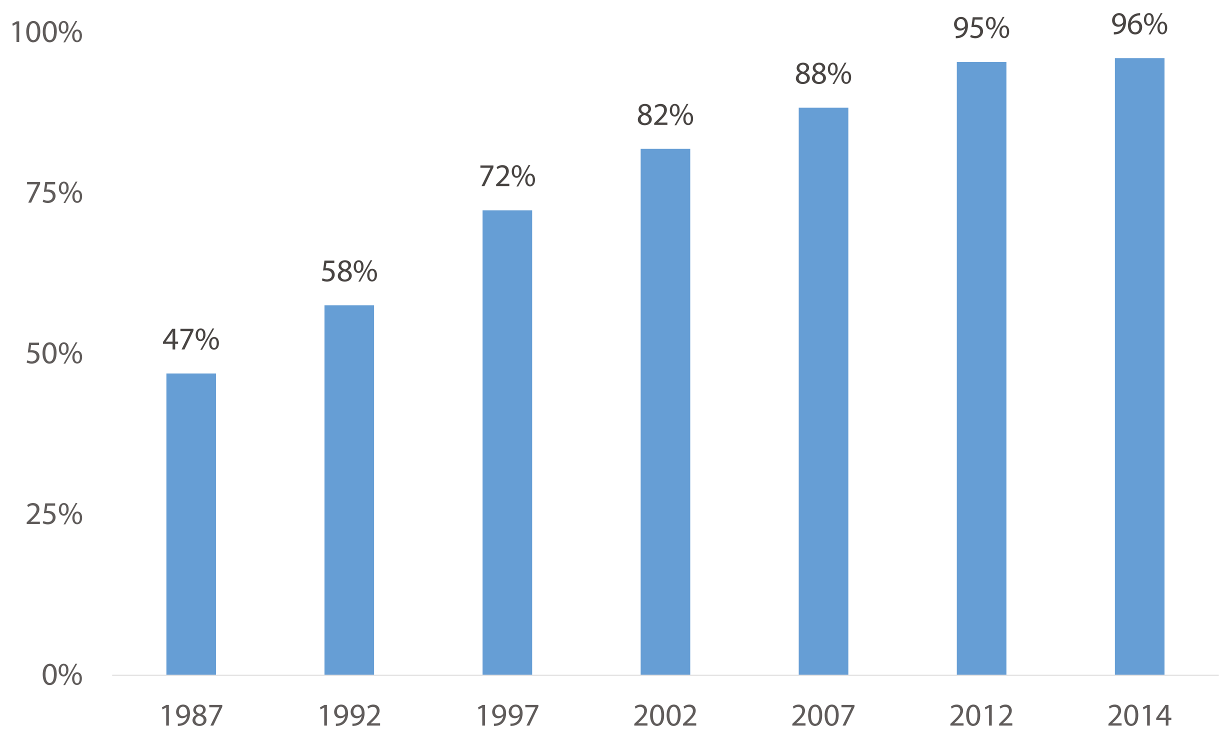
Figure 1. Relative development of tax rates in the EU28 (2000=100), 1995-2014



Note: The figure shows the index of the EU28 average (base year=2000) for three different types of tax: consumption tax: standard value added tax (VAT); personal income tax: top personal income tax rate; and corporate income tax: adjusted top statutory tax rate on corporate income.

Source: Author's own calculations based on data from Eurostat (2014).

Figure 2. Coverage of double taxation conventions in the EU (changing composition), 1987-2014



Note: The share of total double taxation conventions (DTCs) in the EU is calculated using the number of bilateral DTCs in force in the EU as a share of the maximum possible number of bilateral DTCs between EU member states. Hence, if all 28 member states in the EU in 2014 would have had DTCs with the 27 other member states (ie. 378 DTCs,) this would be presented as 100% in the figure.

Source: Author's own calculations based on OECD (2015) and Bulgarian National Revenue Agency (2015).

"More coordination at the international level is thus required to make sure that all corporate profits are taxed only once and undertaking cross-border activities in the EU becomes less burdensome"

the relative development of various tax rates). These rates are often also more harmful for the economy. The consumption of European citizens, for example, has been hampered in recent years by the increase of the average rate of value added tax (VAT). The top personal income tax rates decreased, but less than would have been possible if a higher (or more effective) CIT could be charged. The higher than necessary labour costs made it less attractive or more difficult for employers to hire new personnel, raise net salaries or improve profitability.

The corporate tax avoidance today is primarily the consequence of how taxation been addressed in the European Union in the past. Although a national competence, taxation plays a pivotal role in the correct functioning of the internal market. In the earlier days, however, rather than tax avoidance, it was double taxation that formed the main obstacle.

Member states chose to address the double taxation of cross-border activities through bilateral double taxation agreements, which in general prescribe that companies are only taxed in the host-country. Later on, the Parent-Subsidiary Directive further restricted the maximum CIT rate on a subsidiary's income to the higher of the CIT rate charged in the parent and subsidiary country. The double-taxation agreements and implementation of the Parent-Subsidiary Directive, which requires companies only to pay corporate tax in the subsidiary's country, allow for some (aggressive) tax planning.

In the latter case, the primarily larger internationally active companies are able to exploit the mismatches between tax systems to reduce both the effective tax rate and base. Figure 2 shows that the coverage of double taxation agreements has gradually increased from 58% in the year of the creation of the Single Market (1992), to almost complete coverage today.

In response to the recent cases of excessive tax avoidance and the global G20-decisions as well as OECD initiatives, the Council has recently adopted two measures. In the meeting on 9 December 2014, it agreed on including a common anti-abuse clause in the Parent-Subsidiary Directive, aimed at preventing the directive from being used purely to facilitate arrangements to avoid paying taxes. However, since member states are left the option to apply it and the clause is primarily targeting the excesses, it is unlikely to change much. The Council also agreed to strengthen the mandatory automatic exchange of information to prevent taxpayers from hiding taxable capital or assets for the authorities, which is critical in the fight against tax evasion.[2]

But the fundamental flaw in the design, namely the fragmentation in EU tax systems, is still not addressed. Besides facilitating tax avoidance, it also makes cross-border activities more expensive than necessary. Companies need to declare their tax in all member states where they are active instead of only their home country. This administrative burden weighs in particular on companies with smaller foreign activities. In fact, the taxation requirements might even restrain smaller businesses from conducting cross-border activities at all.

More coordination at the international level is thus required to make sure that all corporate profits are taxed only once and undertaking cross-border activities in the EU becomes less burdensome. The initiatives taken at global level have so far proved to be unsuccessful, but this should not discourage the EU from deepening the tax cooperation within its own borders. The European Commission's proposals to enhance the coordination have failed in the recent decades.

Nevertheless, the most recent proposal for a Common Consolidated Corporate Tax Base (CCCTB) could be brought forward again. The 2011 European Commission proposal foresees a single set of rules to determine the tax base covering all EU member states, which would allow companies to declare CIT at consolidated level. In turn, the member states can still set their own rates for their share of the profits. Nevertheless, the CCCTB should become obligatory for all companies (with cross-border activities) and not optional, as currently proposed, to eliminate the arbitrage possibilities. Moreover, further action will still be required to avoid the usage of third-countries for tax avoidance and evasion as well as to address the differences in accounting standards between companies using IFRS and the various local GAAPs.[3]

The European Parliament might prepare the ground for challenging the status quo in corporate taxation discussions. It has recently taken a more active role in this dossier by setting up a special committee on tax avoidance.[4] Although less resolute than the committees of inquiry demanded by a large minority in the Parliament, the committee could still broaden general awareness of the harmfulness of corporate tax avoidance and evasion as well as create a sense of urgency of the need for Europe to move towards a consolidated corporate tax.

In the meantime the European Parliament could broaden its earlier demands for public disclosure of the country-by-country corporate tax bill, which would provide better insights into the frequency and magnitude of tax avoidance and allow customers to hold companies accountable for the morality of their tax behaviour. ■

1. See www.icij.org/project/luxembourg-leaks/lux-leaks-revelations-bring-swift-response-around-world
2. See www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ecofin/146136.pdf
3. See MP Devereux and C Fuest (2009), "Corporate income tax coordination in the European Union", Transfer: European Review of Labour and Research, 16(1), 23-28 http://www.sbs.ox.ac.uk/sites/default/files/Business_Taxation/Docs/Publications/Policy_Papers/TransferPolicydocumentVersion0311Website.pdf.
4. See www.europarl.europa.eu/news/en/news-room/content/20150206IPR21203/html/Parliament-sets-up-a-special-committee-on-tax-rulings

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Dual-learning contributes to the competitiveness of industry

Markus J Beyrer is Director General of BUSINESSEUROPE

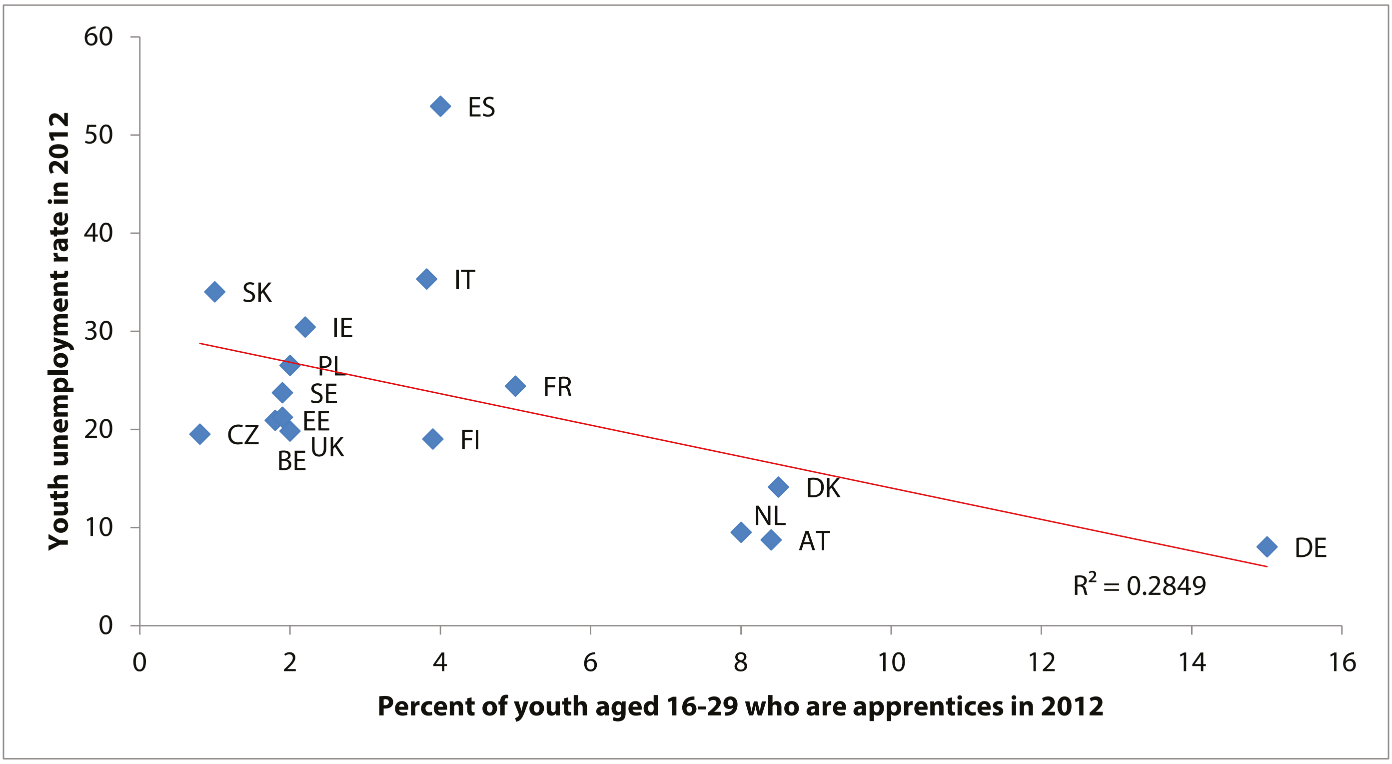
A key structural weakness in Europe is the difficulty to integrate new entrants into the labour market. Employment, particularly of young people, is hindered not only by (sometimes) too rigid employment regulations; the structural weaknesses are also caused by a mismatch between the skills provided by education and training and those needed on the labour market. This happens at a time when we know that Europe's ability to compete globally will depend on developing innovative ideas and bringing them to the market more quickly. This requires the rapid conclusion of the labour market reforms and having a skilled and productive workforce in Europe.

In one of its medium-term skills forecast the European Centre for the Development of Vocational Training (Cedefop) looked ahead to 2020 and has found that Europe is on its way to an economy where services, knowledge and skill-intensive occupations will prevail. Projections also show that about 15% of jobs in 2020 will be low skilled in nature, while 50% will be medium skilled and around 35% highly skilled.

To ensure that available skills will meet future labour market needs BUSINESSEUROPE advocates the principles of work-based learning and the strengthening of dual-learning systems in member states. Young people's transition from education to employment can be made easier and smoother by expanding access to dual-learning systems, such as apprenticeships.

The involvement of enterprises in apprenticeship schemes is seen both as a way of identifying and meeting skills needs on the labour markets. Engagement in apprenticeship schemes brings a number of advantages for enterprises, including better matching of skills as a result of in-house training, increased production, new knowledge and perspectives from apprentices. They also can expect an enhanced standing and recognition of the company as a good employer, and more broadly among its main stakeholders, customers, suppliers.

The facts speak for themselves: there is a close correlation of apprenticeship schemes with lower youth unemployment. Countries with high percentages of students enrolled in work-based vocational apprenticeship programmes at upper secondary level usually have the lowest youth unemployment rates. This is the case in Denmark; Germany; Austria; and the Netherlands. These countries have a well-established tradition for dual-learning apprenticeship schemes.



Source: OECD, Eurostat, BUSINESSEUROPE

In countries like Slovakia, the Netherlands or Germany more than half of the students choose the vocational path. In other EU member states, the proportion is between 40-50%, like in Denmark, Poland, France or Spain. We also see 33% participation rate in Estonia and 30.5% in the UK.

In some of the EU member states company-based training represents the largest share of total training hours: between 66-70% in Denmark, Estonia, France, Germany, the Netherlands, and the UK. These apprenticeship systems are led by the demand: they originate from employer willingness to offer places to young people. By contrast, in other countries, apprenticeships are mainly school-based. In Poland for example, in-company training represents a relatively low share of total training with apprentices spending as little as 1 day per week in a company, depending on the agreement between the enterprise and the school.

Funding arrangements of apprenticeship systems vary a lot between the EU member states. Sometimes they are financed exclusively by employers, sometimes supported by public authorities. The fact that employers in some countries are willing to pay the entire bill shows that the benefits they enjoy from this system are higher than the price they pay. Public authorities might provide incentives for employers to offer apprenticeships, but it is important that the apprenticeships do not become a means to achieve the integration of disadvantaged youths.

This may have a negative impact on their overall image and attractiveness to well educated people that might prefer a vocational pathway to an academic one. Equally, part of the challenge of increasing the attractiveness of apprenticeships is improving the permeability with higher education and to foster an entrepreneurial mind-set.

Though the main reason why employers in some countries may be reluctant to engage in apprenticeship schemes is the costs of engaging in training activities. The adaptation of work stations, possible mistakes made by apprentices, the administrative paperwork and the time company trainers and employees spend with monitoring apprentices don't come free. The high costs involved may be an even stronger obstacle to the engagement of small and medium size enterprises (SMEs). A number of cooperative solutions have been taken at national level to mutualise the costs of training between SMEs in a given sector; for example by providing training opportunities in more than one company for the same apprentice.

A precondition for well-functioning apprenticeships is, of course, that employers need to be able to rely on the skills acquired. In this respect the cooperation between employers, the providers of vocational education and training, as well as craft and commerce chambers is key. They are expected to ensure that qualifications reflect the skills needed on the labour market and certify the skills acquired appropriately. For example, many EU member states organise a universal examination at the end of the studies to ensure transparency and reliability of skills acquired. Another issue is the perception of the quality of these skills.

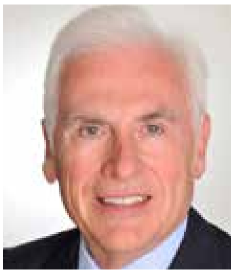
There is no doubt that apprenticeships appear to be a good way to ease the headache and shorten time young people spend with finding proper jobs on the labour market. In 2009, for example, German, companies retained 57% of their apprentices and signed regular employment contracts with them. The same year in France 64.2% of the population, having finished an apprenticeship, was in employment within a few months. In Estonia, only 17.0% of apprenticeship graduates had not found a job six months after graduating in 2009 while in Spain, 78%

"... apprenticeships appear to be a good way to ease the headache and shorten time young people spend with finding proper jobs on the labour market"

of initial vocational training graduates were able to find a job in less than one year (2010).

In a project under the European Alliance for Apprenticeships (EAfA), to which BUSINESSEUROPE and the other European social partners are signatories, BUSINESSEUROPE is exploring issues around the attractiveness of apprenticeship schemes for employers from the perspective of their cost-effectiveness. The diversity of national apprenticeship systems across Europe allows us to learn from each other without adopting a copy-paste approach. Drawing on this, we can help to identify the core elements in different countries which motivate employers to step up their role in apprenticeship schemes. By focusing on the engineering, ICT and commerce sectors we also hope to address the attractiveness of apprenticeships beyond the traditional perception that they are only meant for blue-collar sectors and occupations. For example, the availability of e-apprenticeships demonstrate the changing nature of apprenticeship schemes and the skills that companies require. In case of e-apprenticeships this is digital skills.

We know really well, of course, that having more and better apprenticeship systems in place is not the silver bullet to solve all Europe's competitiveness problems overnight. But if we really want to put Europe's competitiveness first and create a better future for young generations they must and will play an invaluable role. ■



What globalisation needs: world-class business education

As business becomes more global, so too must professional education. International Chamber of Commerce Secretary General, John Danilovich, discusses the need for professional education that is relevant, reputable and accessible worldwide

Economic growth in the emerging markets means that business is now thriving in all corners of the globe. Not only are the emerging markets building their own multi-national giants, they are also taking advantage of the increase in 'south-south' trade (trade between emerging markets) – giving rise to scores of business opportunities and partnerships worldwide.

As business globalises, so too must professional education. Certainly, there is a vital need for global standards of excellence in professional and business education. Professional certification must be global while educational programmes should be accessible to anyone, anywhere, at any time.

Through the launch of the ICC Academy, the International Chamber of Commerce (ICC) aims to provide just such a global educational structure – a dynamic digital platform for delivering rigorous, relevant and applicable business education. Our aim is to encourage individuals to reach their highest potential with respect to professional competency and ethical conduct – allowing global partnerships to flourish.

As part of the world's largest business organisation, the ICC Academy will take full advantage of ICC's extensive business reach in over 130 countries. It will also utilise our roster of experts and practitioners as well as incorporate insight, where appropriate, from external senior business leaders and policy-makers.

Digital platform

Yet it is the delivery of the courses that really sets the ICC Academy apart. Utilising a dynamic digital platform that combines distance learning with group-based project work, our goal is to enable equal access to professional education for the largest number of potential participants around the world.

Distance learning – facilitated by digital platforms – removes geographical barriers to education. The result is that anyone – no matter where they are in the world – can follow a distance learning course, as long as they have access to the Internet. And the same class can be attended simultaneously by multiple students around the world, or be accessed later on an individual basis.

Of course, this also allows both a standardisation in quality and a raising of the bar in terms of the achievable standards – something only an organisation of ICC's breadth and reach can instigate.

The ICC Academy will be launched, and based, in Singapore, a global hub of business, finance and trading excellence. To this end, the Singapore government has been highly supportive and members of the government will attend the launch.

Singapore is also fitting due to the Academy's initial courses being focused on banking and trade finance. Indeed, the opening offering includes almost 70 online courses and global certifications in trade finance, although will broaden over time to cover all of ICC's business-related areas of operation.

Educating the emerging markets

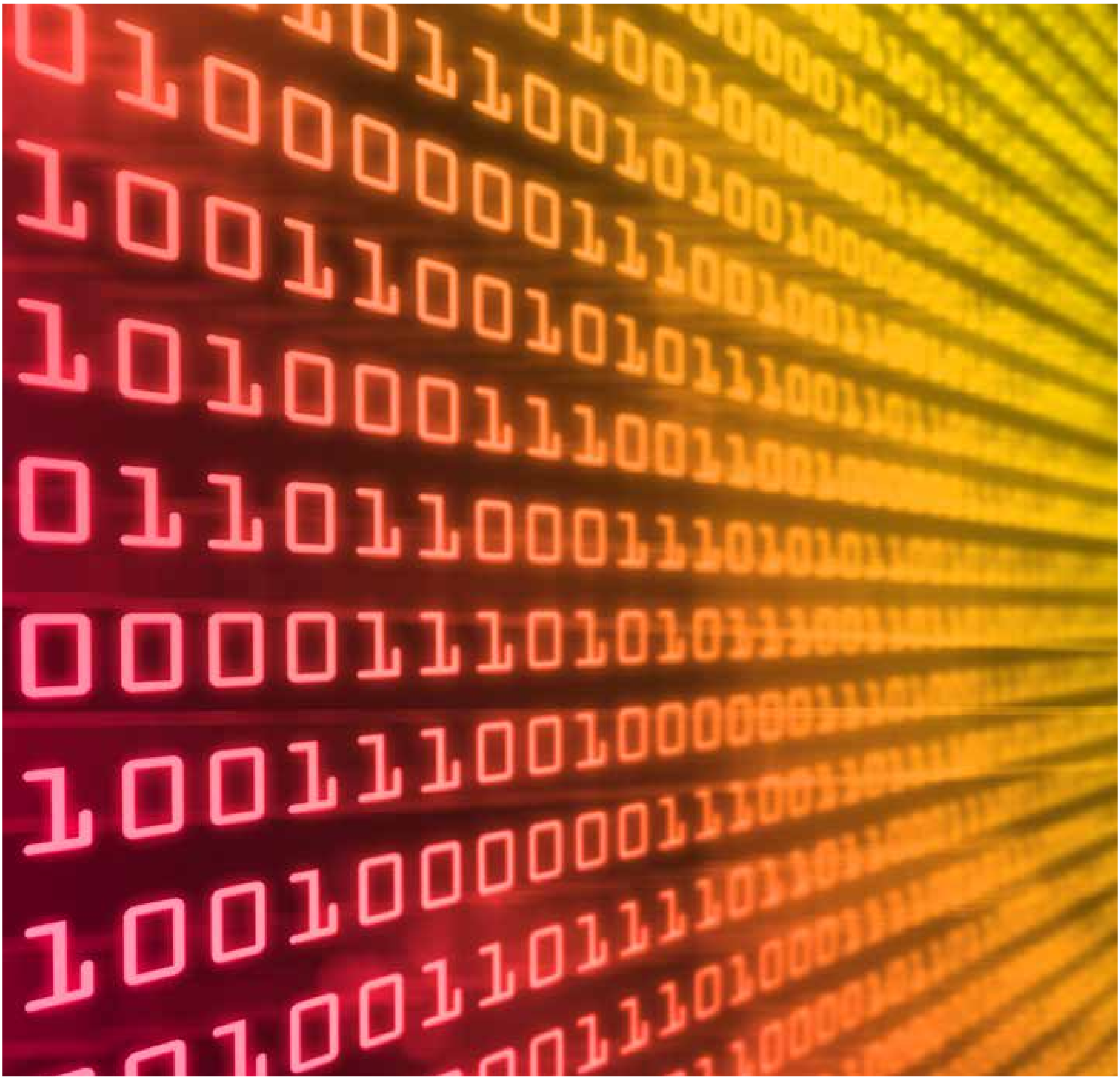
While undoubtedly valuable for developed markets, the biggest impact of an online professional education initiative such as the ICC Academy will be felt in the emerging markets. Certainly, e-learning opens education to millions that would previously have been shut out entirely.

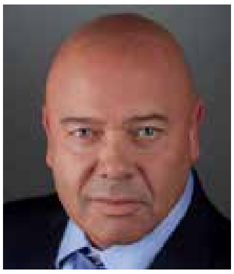
The benefits of broadening the availability of globally standardised business education to emerging markets are, however, universal. By 2020, a third of global trade – and nearly all of the growth in trade – is likely to be south-south, a phenomenon that requires professional standardisation and certification.

Certainly, the ICC Academy should not be a static institution. It is committed to continual evolution – keeping up with the latest changes in the business world and adapting to meet changing demands with new courses, new technology and new educational approaches. In fact, it is an ideal model for building partnerships with corporates and multilateral institutions, since the Academy can help them drive their competitive advantage through their employees.

"The benefits of broadening the availability of globally standardised business education to emerging markets are universal"

But it is not just for large companies and their employees – or for any defined group. The ICC Academy makes world-class and globally-respected professional education available to everyone, no matter whom or where they are. ■





Enterprise leadership evolving towards a five dimensional orientation

Govert Doedijns is a Talent Management Consultant and Executive Coach. He also serves as the EMEA Regional Leader and member of the Advisory Board at Executive Core

Effective leadership is viewed as a central driving force towards organisational success. In the 1990s, leadership developers often had to explain, demonstrate and convince top management of the benefits and ROI of leadership development. Today that is no longer the case; organisations no longer ask the question 'why?', but 'how?'

In recent years, we have witnessed the emergence of the concept of the enterprise leader. Academics, talent management consultants and corporations on the forefront of leadership and talent development have embraced the concept and there is now data – in the form of improved leadership effectiveness metrics - to prove it.

In 1997, Dr Martin Chemers (of the University of California at Santa Cruz) described leadership as *"a process of social influence in which a person can enlist the aid and support of others in the accomplishment of a common task"*. This is a powerful definition of leadership, as it permits and encourages us to consider a number of factors simultaneously. Let us begin by considering five key elements of this definition.

'Leadership is a *process*' – leadership is not some innate, invisible magical quality people are born with. If leadership is a process, then it is a systematic, planned, intentional set of behaviours and capabilities that can be broken down into sequential steps and learned, practised and refined.

'Social influence' – this underlines the fact that leadership is largely about interaction between human beings, and actually has little to do with position, rank, title, salary or education. If success in your job requires influencing others to provide help, support, commitment, or information, then you have a leadership role – regardless of relative positions within the enterprise.

Interaction means interpersonal dynamics, and by extension the importance of influencing capabilities. The leader needs to be effective and maximise personal impact in a variety of very different contexts; the leader needs to be able to influence, persuade and engage at all levels and across all functions - upward, downward and laterally. Influence is consensual, situational, and is a bilateral process rather than a singular event.

'Is able to' - Dr Chemers reminds us that there are no guarantees, and that we shouldn't consider leadership success in terms of a linear cause/effect equation, but rather as a perpetual dynamic of learning that takes place in small sequential steps. Leadership success is not about getting what you want every single time: rather it is about improving one's batting average over the course of a thousand leadership interactions, a program/project, or a career trajectory.

'Aid and support of others' – the notion of aid and support implies an exchange or a transaction. *"Who has what I need?"; "What does this person have that I need?"; "What can I do to maximise the chances of them giving me what I need?"* This could mean information, resources, commitment, support or any one of a range of enterprise assets or political capital.

Successfully securing the aid and support of others requires a sophisticated understanding of the objectives and needs of the other party. Leaders need to be able to encode their needs and objectives in the language and context most meaningful to others and help them decode the world in similar terms. This relates directly to the next point.

'Common task' – leadership involves positioning and describing tasks in terms of mutual interest, demonstrating how a course of action is in the shared interest of the contributor, the leader, the team, the function, the division and the enterprise as a whole.

> *"Leaders must establish a relationship with followers that guides, develops, and inspires them to make meaningful contributions to group goals and the organisational mission. Such relationships must match the needs and expectations of followers, which leaders discern trough nondefense judgements.*
>
> *Leaders must mobilize and deploy the collective resources of self and team to the organisational mission by matching operational strategy to the characteristics of the environment."* (*An Integrative Theory of Leadership*, Martin M Chemers, 1997)

Leaders therefore need to be highly capable translators, interpreting effectively between levels, functions and even generations within organizations – each of which will have their own interested, objectives, agendas, and perception of consequence. The most important leaders within an organization are those who manage the communication loop between the disciplines of strategy formulation and strategy execution – each of those two activities needs to receive and manage feedback from the other to ensure appropriate adaptation for success.

Leaders also need to be able to view and analyse human performance systems in multiple dimensions, decoding and encoding information in order to provide feedback in meaningful for recipients, process feedback when received, necessitating learning the language of multiple functions and hierarchical levels.

Effective modern leadership in other words necessitates the ability to interpret and understand large and dynamic integrative multidimensional layers of information. That is a far stretch from the starting point of management science.

Is this a structural, linear process…? Let's look back in time… I will explore how we got here. Is this a recent and trending topic or an evolution of a spectrum of competencies and if so can we establish a process so as to, not only verify its current validity, but also predict and thus anticipate where we need to be 2020 and beyond. In order to do that lets look at how this evolved.

Henri Fayol, one of the founding fathers of today's management science wrote in the early 19th century *"to manage is to forecast and to plan, to organise, to command, to co-ordinate and to control."* His work illustrates an early recognition of management competencies. The boss or manager obtains his or her position because of skills and meritocracy rather than as a result of wealth, birth, seniority, or nepotism. Fayol's general theory of business administration is widely acknowledged as amongst the founding theories of modern management methods. He proposed five primary functions of management of which the fifth; the control function, is used in the sense that a manager must receive feedback and analyse the deviations of a process in order to make necessary adjustments. My reason for singling out the control function is the notion of receiving worker feedback and adjusting accordingly. In doing so we go from a linear command towards a bilateral communication structure between boss and workers.

Management science continued to evolve at a rapid pace and in the US we saw the birth of the MBA. As the country became more industrialised, companies began to seek out new, more scientific approaches towards business management. Automated machines began to replace manual labour, which led to a demand for educated supervisors to oversee machines, labour and automation. Harvard established the first MBA program in 1908 and soon, more colleges began to offer these programs. By the 1950s, the first MBA degrees outside the United States were awarded.

With the growing popularity of the MBA, we witnessed the birth of a new generation of future managers with a scientific approach to management and broad rather than a singular functional expertise skill set such as accounting, controlling or engineering from which people were promoted in the past. The MBA created a generation of highly skilled analytic and successful strategic managers. As these managers rose to senior roles during the 70s and 80s it became apparent that their 'soft', or people skills, often left a lot to be desired for and that in many cases these future leaders and subsequently the organisations they worked for would benefit from the integration of more interpersonal skill, training into the MBA curriculum.

During the 90s we subsequently witnessed the conversion of management training towards broader leadership training and simultaneously we witnessed exponential growth of leadership development and consulting firms growing to what is now a $10 billion industry. The manager was out and the leader was in, and leadership now encompassed a whole array of inter- and intrapersonal skills.

The international perspective; leadership going global

What happens when we do not see or understand context and take a singular subject matter expertise without the interpretation or encoding and decoding of all the elements surrounding and influencing it? Living and working in Europe there is one large international survey that comes to mind that illustrates the results of professionals who predominately use one singular skillset; translators.

The European Union counts 28 member states; expand the region to EMEA than it encompasses about 150 countries. The EU counts 23 official languages and employs some 2,500 translators at a cost of about €1.5 billion.

A 2003 and 2010 translation quality survey indicated that only 16 and 17% of the respondents obtained a satisfactory test score on a test verifying the accuracy of a 300-word translation. Only about one out of 15 translators obtained a 'very good' grade. Does this imply that the vast majority of these translators are incompetent; surely not? Their translations were mostly grammatically correct and most words were accurately translated according to their most common linguistic equivalent. Where it went wrong in over 4 out of 5 cases was that the translation was inaccurate because the translators had little or no contextual understanding or knowledge of the subject matter.

Europe itself has the greatest linguistic and cultural diversity of the Western world. It is therefore of crucial importance to analyse the cultural dimensions and aspects of the corporation the leader works for, as well as his or her personal cultural make up and that of their team. Having specialized in work with European and EMEA leaders of European and or American firms for the past 13 years, the majority of my leadership development and coaching work has carried English as it's the official language.

In addition to having worked with leaders across the globe, I have previously worked and lived in five European countries as well as the United States, which has allowed for me to personally experience many of the business challenges and cultural dynamics the leaders and teams I work with encounter on a daily basis. Many of my assignments have been trilingual and thanks to my contextual understanding, I have acquired a significant amount of insight, which has been crucial in helping the leaders, and teams I worked with throughout the past 13 years.

In 1993 I took on the challenge of acquiring an almost bankrupt industrial company in France through an MBO. Within 100 days of the takeover, I rebuilt the company and steered it out of its crisis. One year later, the company and I were now ready to tackle our mid- and long-term strategy of becoming an innovating and trendsetting leader in French industry.

One of my primary personal goals for this challenge being a successful immersion into the French society in order to steer away from the 'expat' stereotype, I did my best to embrace the French lifestyle and mindset by tackling each new day of this (work-enriching) experience from the point of view of a typical Parisian. I was to address every morning with the finesse of a Parisian by sipping on a thick espresso at the local brasserie with a copy of *Le Monde* in hand while balancing a lean Gaulois cigarette, à *la francaise*. I had officially debuted my mission towards the transformation of this French company and I was ready to conquer any upcoming challenge.

As a manager and leader, I realised that my experience, upbringing and academic background had instilled a very Anglo-Saxon, Nordic view of management and leadership. At the time, I believed in the participative management style upholding a very low power distance. I was very ethnocentric in regards to this and believed that my French employees would come to embrace such a leadership style once they became sufficiently exposed to it. But unfortunately for me, I was to quickly discover that the equalitarian mind-set I had hoped to be a universal was far from the truth.

The company that I worked with had amongst its parking facilities four prime parking spots: two exclusively reserved for the VIP customers, and two that were allocated for the MD, who for his convenience preferred to park in the middle of two. Upon purchasing the company, I changed the two MD spots to serve as employee spots on a first-come-first-serve basis. To me, this was a conscientious and respectful move on my behalf and I could not imagine how employees could possibly perceive this any other way. By both downgrading my parking spot while upgrading theirs, I was establishing a just field of equality which I believed to be the perfect platform to build on when trying to make a name for oneself in a foreign company.

But despite my aspirations, I learned shortly thereafter that what I had thought to have been an act of compassion and kindness did not conform to the power and distance dynamic to which the French were previously habituated, and that despite my motives my actions had been perceived as being weak, giving me the embarrassing prejudice of the 'boss who was incapable of assuming his leadership role, being conflict aversive and fragile'. But this episode wasn't the last in the series of mistakes I was to make before finally coming to the realisation that I was far from being an expert in the field of cultural disparity and the different dynamics that this field encompasses. I eventually started to study and read about culture in order to broaden my spectrum and understanding of it and I bought Geert Hofstede's book *Culture's Consequences*.

Cultural dynamics

Geert Hofstede is seen as one of the key writers and proponents of cultural theory. His research, which originated in the late 1970's and early 1980's, was conducted amongst IBM employees and covered over 116,000 responses and 76 national subsidiaries. The research identified systematic differences in national cultures on four primary dimensions to which he later added two more.

Hofstede's observations help us in understanding the cultural differences and dynamics that come into play amongst the leaders, stakeholders and team. We already observed that languages can form an obstacle towards accurate communication. We subsequently need to realise that interpreting communication within their appropriate culture setting is equally important. There is a plethora of research to support this notion and confront us with our dismal capacity of doing so effectively. According to one survey of senior executives:

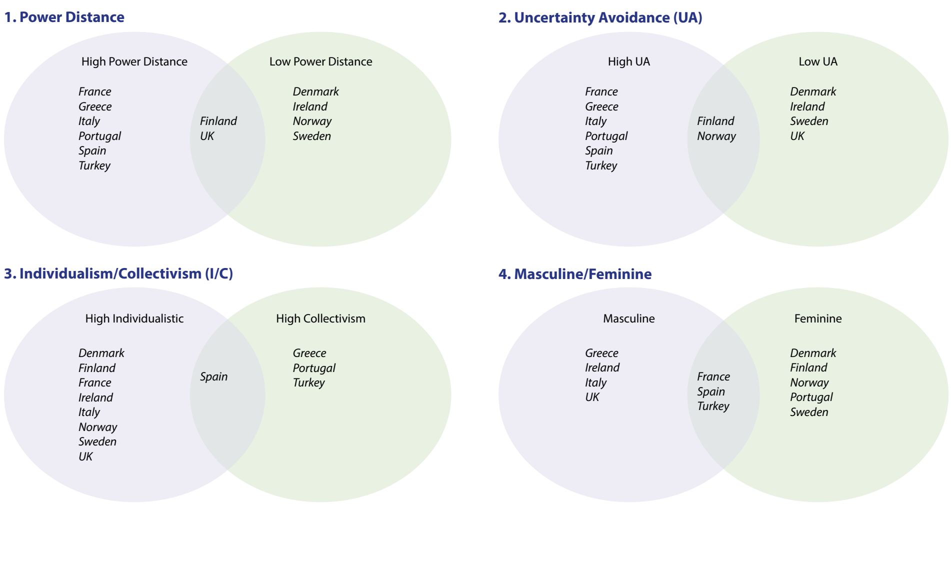
- 76% believe their organizations need to develop global-leadership capabilities.
- 7% think they are currently doing so very effectively.
- 30% of US companies admit that they have failed to exploit fully their international business opportunities because of insufficient internationally competent personnel.

Shirley Daniel and Ben L Kedia, US Business Needs for Employees with International Expertise

Exploring the hypothesis that the pre-management science period was a mono dimensional perspective and that during the last century we gradually added a two, and subsequently, a third dimension, then integrating additional layers of depth and context to the equation such as cultural dynamics provides us with a fourth dimensional view. Leadership has, however evolved beyond these four-dimensional layers and today comprises an even more integrative approach across the enterprise through enterprise leadership.

Enterprise leadership is a holistic approach to value creation in the enterprise, recognizing and integrating the challenges of the 21st century global executive. Today's leaders have to manage and influence multicultural teams across large regions and often throughout a complex structure of corporate brands, divisions and companies. Their impact and success no longer depends on their individual control and command skills but rather on how effective they are at steering and navigating their teams in adjusting and anticipating the dynamics and challenges they are faced with.

The enterprise leader is a translator who translates, articulates, manages and enacts communications across the enterprise. He needs to translate strategy formulation to execution and code and decode feedback from and towards the organisation



Hofstede (1994) Cultures and Organizations - The Four Cultural Dimensions

No one leader can 'manage' the entire enterprise, and therefore leadership needs to be distributed. The shifts a function head must make when first becoming an enterprise leader involve learning new skills and cultivating new mind-sets. Michael Watkins in his article; *how managers become leaders* (*HBR* 2012) described the following seven seismic shifts:

- Specialist to generalist
- Analyst to integrator
- Tactician to strategist
- Bricklayer to architect
- Warrior to diplomat
- Problem solver to agenda setter
- Supporting cast member to lead role

Reflecting the changes in the environment, the competencies that will be most valuable to the future leader are evolving. Leaders need to be agile critical thinkers that solve problems while leading by influence and collaborating across networks using complex and adaptive thinking abilities. They need to have an entrepreneurial mind-set and be able to interpret large amounts of data while being eloquent and effective communicators. Many of these leaders will have to be groomed through vertical development within the enterprise.

If we try to view or conceptualize leadership development and our understanding of effective leadership in a five dimensional model where each dimension and layer provides us additional context and interconnectivity, then we should take all external influences into perspective as they have a significant impact or influence the effectiveness of the leader.

In doing so the analogy of the evolution of medical imaging came to mind to show the increasingly sophisticated insights we have into leadership behaviours and the decisions those insights enable.

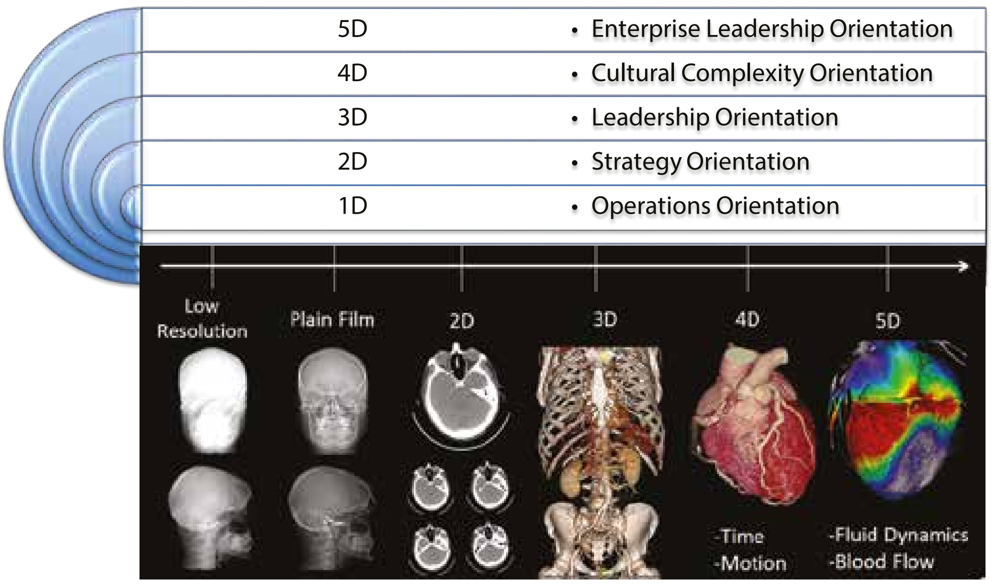
> *"Leaders need to be agile critical thinkers that solve problems while leading by influence and collaborating across networks using complex and adaptive thinking abilities"*

Nick Petrie 2014 in his article; *Future Trends in Leadership Development*, CCL 2014, described four trends for the future of leadership development:

1. More focus on vertical development
2. Transfer of greater developmental ownership to the individual
3. Greater focus on collective rather than individual leadership
4. Much greater focus on innovation in leadership development methods

Once we accept that the ideal goal for leaders is to achieve a true enterprise leadership orientation, the key question becomes 'how can leaders accelerate this development?' A critical accelerant on this journey is the sourcing of advice and counsel from selected thought partners with complementary experience and perspectives; these thought partners may be within the enterprise, or often external to it. Our experience at Executive Core shows that a combination of both is usually necessary: in order to seek, partner with and obtain counsel and support from key advisers internally, leadership skills are necessary for securing mentoring relationships (answering the question 'how can I get from this person what I need, and how can I solicit their help in terms which will be relevant to them?) - which very often requires the advice and help of an external coach or adviser. ■

Evolving towards a 5 Dimensional Enterprise Leadership Orientation



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AMBA Careers Fair

MBA global employment landscape has never looked better – Microsoft, Oracle, HSBC, Bloomberg and L'Oreal look for fresh MBA talent

There has been a significant growth in MBA demand in all sectors; consulting, energy and technology in particular.

Over 600 MBA students of 90 nationalities from AMBA accredited schools in UK, France, Italy, Germany, Belgium, Spain, Greece, Portugal and the Netherlands gathered in London on 20 February at the biggest MBA recruitment event in Europe.

Current MBA students and recent MBA graduates from top business schools, such as Hult International Business School, HEC Paris, IE Business School, Imperial College Business School, SDA Bocconi, ESADE, Vlerick Business School and others met with 16 multinational organisations looking to recruit MBAs for positions within their Consulting, Marketing, Sales, Technology, Executive and Research and Finance business units.

The MBA job-seekers were 33 years old on average, had 8.5 years of work experience and 35% of them were women. Qualified candidates from diverse backgrounds, including sectors such as Industry/Manufacturing (22%), Financial Services/Banking (17%), Energy (17%), Information/Communications/Technology (17%), Service/Consumer/Retail (16%) and Public Sector/ Health (11%) met with talent scouts from Bloomberg, HSBC, L'Oreal, Microsoft, Oracle, Gartner, Pirelli, Curzon, TalentHawk, Cognizant and others to discuss the global employment opportunities.

Doug Gray, Managing Director of TalentHawk, an international IT and Professional resourcing consultancy thinks that MBA global employment landscape has never looked better: *"There has been a significant growth in MBA demand in all sectors; consulting, energy and technology in particular. Employers are driven to employ more MBAs as they typically demonstrate a higher level of business acumen."*

Ioana Tanase, Global MBA Staffing Consultant from Microsoft agrees: *"MBA hires are definitely worth the investment. They bring a lot of value, new skills and strategic thinking which drives our business to the next level"*, she said.

"They are typical all round star performers; they are good in people management, finance and they have clear decision making ability", Koen D'Hoore, IT Innovation consultant from Oracle said.

Also, more and more MBAs are willing to work globally, demonstrating the global nature of an MBA degree and their adaptability, one of the most critical competencies for executives in today's ever-changing market. *"We are seeing a more global approach in terms of where MBAs want to work. They are more than ever considering different locations, outside of the continent and original location"*, said Ioana Tanase from Microsoft.

Andrew Main Wilson, AMBA Chief Executive added: *"Employers clearly recognise the unique mix of intelligence, general management skills training and sheer dedication an MBA can bring to their organisations (an MBA typically invests over 2,000 hours of learning time in their MBA). MBAs do need to prepare meticulously before interviews with employers however, if they are to do themselves full justice and obtain the very best career roles, in such a highly competitive global marketplace."* ■

One of [Peter Drucker's] skills was his ability to spot the clouds of change in society while they were still far off on the horizon, long before the thunderstorm broke. I try to emulate his skill in my own work so that people can better prepare themselves for new futures

CLOUDS OF CHANGE

Charles Handy, like Peter Drucker, has always sought to identify the clouds of change threatening society. Here he identifies one such possible threat – the dysfunctional behaviour of our large corporations

Peter Drucker has been a big influence in my life and work. I valued hugely my occasional meetings with him and my bookshelves groan under the weight of his many books.

One of his skills was his ability to spot the clouds of change in society while they were still far off on the horizon, long before the thunderstorm broke. I try to emulate his skill in my own work so that people can better prepare themselves for new futures.

One of the clouds on the horizon that currently worries me is the behaviour and the future of large corporations. Much though I admire and encourage the entrepreneurs of all sorts who are our futures and much though I enjoy my contacts with small organisations and family businesses, the fact is that the public corporations are the great elephants of our economies.

We ride on their backs. They provide the greater part of the new wealth of society as well as the bulk of the jobs, directly or indirectly. If they falter or do not live up to their responsibilities, we all suffer.

So when I see these great beasts getting fewer in number, particularly in America, as well as older, fatter and greedier I start to worry. They have served us well over the last 70 years but success can be the enemy of progress, blinding one to the need to change.

The Greeks of old called it hubris, which I was taught to translate as overweening pride, that which comes before a fall, the arrogance that infuriates the gods and brings down their wrath.

The basic facts suggest that the corporate fall may be nearer than we know. A recent Brookings Institute research report found that firms aged 16 or older now represented 34% of all economic activity in the US, up 50% in 20 years. They are also lasting less long with fewer new entrants coming along, which bodes ill for the future. There are now 50% fewer publicly listed companies in America than there were 15 years ago; nor is it very different in the rest of the world. Business, the Brookings Report concludes, is getting old and fat.

Commenting on the report, the journalist Simon Caulkin says that *"the quoted company, the engine of capitalism for the last 150 years is beginning to look like an endangered species"*. That should give us all cause for concern. There are more worries.

Those elderly elephants may be increasingly in danger of falling foul of what St Augustine called the great sin, that of being so *"turned in on oneself"* that you forget your greater purpose. This charge could be levelled against many of the boards of those companies who have been indulging in an orgy of share buybacks.

William Lazonik, writing in the *Harvard Business Review* of September 2014, points out that the 449 companies in the S&P 500 index that were publicly listed from 2003 to 2012 used 54% of their earnings, a total of a colossal $2.4 trillion, to buy back their own stock in the open market. With dividends taking up a further 37% only a paltry 9% of earnings were left for reinvestment.

There are sometimes technical reasons to buy back stock, to compensate, for instance, for any temporary lowering of the share price when stock options are exercised. But the main reason has to be either that the board members have run out of ideas of how to spend their earnings on new projects or, quite simply, need to boost the value of their own stocks or options. Why, one might ask, would they need to do that given that the average annual take-home pay of the chief executives of those companies was $30 million?

It is only when you realise that 83% per cent of that pay is in the form of stock grants or options that the reason becomes clear, the buybacks are needed to preserve the underlying value of their pay packets. To put it bluntly, those directors are pocketing the seed corn of future generations and nobody is noticing or, if they are, nobody is caring. Am I not right to be worried?

Of course there are exceptions. Not all boards are so self-interested, but the exceptions are just that, exceptions. We need many more of them to set a new tone. Lazonick, who is professor of economics at the University of Massachusetts Lowell and co-director of its Center for Industrial Competitiveness, comments that from the end of the Second World War until the late 1970s the prevailing orthodoxy in the boardrooms of the world was to *retain and reinvest* ones earnings. Now it is *downsize and distribute*, to ourselves and our supportive shareholders. We have moved from value creation to value extraction. He is right.

When I started work in 1956 in the Royal Dutch Shell Group I remember only too well the opening briefing that we fledgling executives received from one of the managing directors in our first week of training: *"We are,"* he said, *"an important part of the energy supply system of the world. Our job is to supply our customers with their needs and to secure the long-term future of the business. We need to make substantial profit in order to finance that future. We also pay a rent to our shareholders, in the form of dividends, for the use of their money, a rent that includes a risk premium, although in our case that premium is low and we want to keep it that way."*

There were no stock options or bonuses on offer then. We were all paid a rate for the job. You got more if you were promoted. The top management was well paid but not excessively so. The shareholders were bystanders, seen more as an indicator of public approval or disapproval, our business thermometer if you like, than as real investors since all new money had to come from our own earnings. So what was it that changed in the 1970s?

In 1970 Milton Friedman declared that the purpose of a business was the maximising of shareholder value, *"the business of business is business"*.

This was developed by two ex-colleagues, Michael Jensen and William Meckling, into Agency Theory, which argued that the directors and managers were in no way the owners of the

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16

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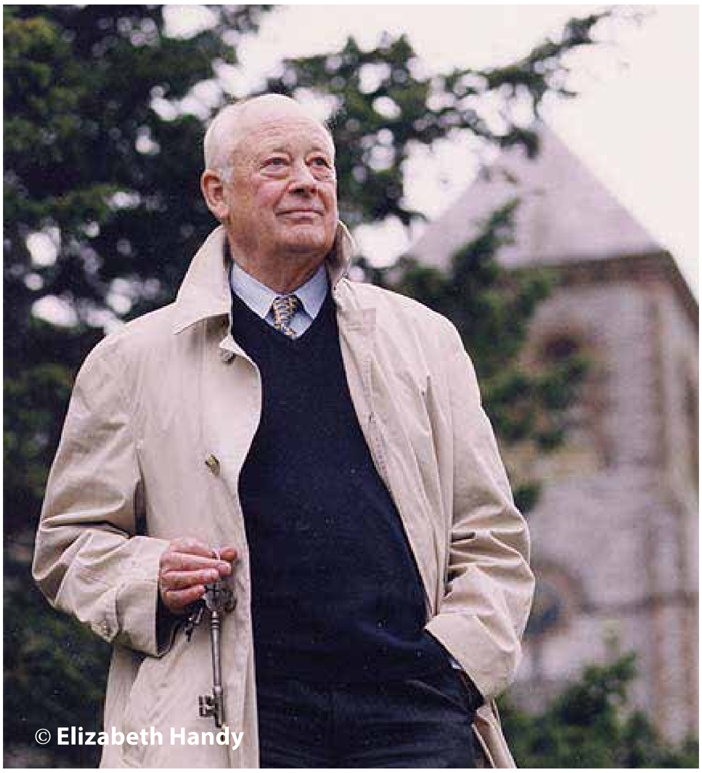

business, they were only the agents of the real owners, the shareholders.

It was well intended; it gave the business a clear objective and it implied that if the business made its owners rich this would in due course enrich society. All would be well for all. As it turned out all would only be well for some.

Directors and senior managers were quick to claim that if they were working for the shareholders, it was only sensible that their rewards should tie in with those of the shareholders, creating a community of interest. The world of stock options and bonuses tied to share prices came into being, and a new story began.

Perhaps John Maynard Keynes was right when he said that *"Madmen in authority, who hear voices in the air, are distilling their frenzy from some academic scribbler of some years past."*

Whatever the cause, the whole culture and *raison d'etre* of business changed from then on. The money men were in charge, supported, I am sorry to say, by enthusiastic business schools who now had one simple yardstick for success which they could pass on to their eager students.

Forty years later it is clear that the new formula has not worked for most. Not for society as a whole, which has had to live through two recessions and a financial crash; not for most individuals given that the median salary in both America and the UK has remained constant in real terms for the last 30 years; and, intriguingly, not even for the shareholders, the focus of the new philosophy. The rate of return on US capital in 2011 was one-quarter of what it was in 1965 and Roger Martin, former Dean of the Rotman School of Management at the University of Toronto, has calculated that the overall returns to shareholders in the 40 years before 1970 was larger than in the 40 years after.

It is odd, in hindsight, that nobody challenged the idea that a business should be seen as a piece of property to be owned by its financiers. That might have made sense to the Victorian mill owner in his mansion looking down at the mill he had built and then hired labour to work the machinery. But now the machinery and the buildings serve the workers not the other way round.

A company is more truthfully a community, a community of companions with a common purpose and no one can legally or even metaphorically own the people of a community. That would be slavery. In any case those shareholders are very seldom the original contributors of finance, who long ago passed on their right to the hoped for stream of dividends to a succession of others who can now be only passive onlookers, betting on their chosen stocks.

Their only rights are to elect the directors or to vote if the directors want to sell the company to another. Even if they

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were allowed to challenge the strategy of the company they are unlikely to have the competence to do so. Responsible owners they cannot be.

The shareholder value doctrine, as it came to be labelled, is even wrong in law. As the leading legal expert Professor Lynn Stout, the Distinguished Professor of Corporate & Business Law at the Cornell Law School in the US, has shown, a company is an independent entity, it belongs to no one. The directors of a company have no reason to give preference to the shareholders. They are instead responsible to the company as a whole for its longer-term survival. They cannot, in law, give priority to any one group of stakeholders, be they shareholders or managers or workers. This is not peculiar to America.

Company Law in most other countries is similar. In Germany, the requirement that a business has a social as well as a financial purpose is written into their constitution, at the instigation, as it happened, of the Allied occupying powers who neglected to do likewise back home.

I see further worries looming. Some of those elephants are growing so large and so global that they are becoming beyond the scope of governments to control, since they can choose to domicile themselves wherever the tax regime is most favourable.

Nor are some of them subject to the usual disciplines of the regulators. How do anti-trust regulations apply when the dominant firm has no competitors because in the internet businesses the winner takes all and leaves everyone else stranded? Even the normal market constraints will not work in these situations. How does one compete with a business like Amazon that seeks to be the largest shop on the planet and feels no need to make a profit en route?

So, I ask, can we safely trust these huge, ageing, bloated and selfish organisations with our futures? Is it not time to return to the idea of a business as a responsible community that pays due heed to all its constituents, one whose core purpose must be to seek immortality through continuous self-improvement and investment?

I have concentrated on America where market capitalism has been most developed but the same trend is discernible in other economies. Continental Europe is protected to a degree by its more rigorous governance structures and its greater reliance on the banks as the longer-term financiers but even here the temptations and pressures of the shareholder value model can be felt. Capitalism is a wonderful social invention, but like all inventions it can turn on its creators if it is not used with care.

I have no easy or immediate solutions. I am not sure that any fiddling with the legal structures of a company will work. What we need is what the Drucker Forum in Vienna is calling for: *"A Great Transformation"*, particularly in the attitudes and examples of those at the top of our great businesses. They need to be reminded that their responsibilities go way beyond themselves and their financial friends, that they cannot rely on the market to keep them fair and honest, and that their people are more than human resources, they are their community and not their property.

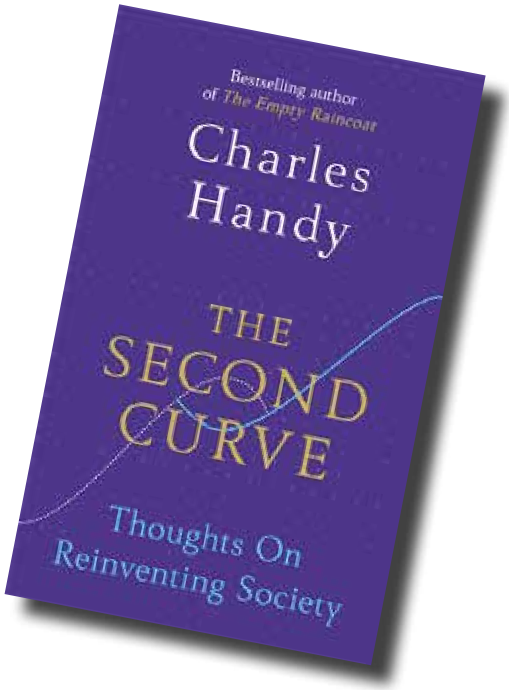
$2.4 trillion

The Harvard Business Review in 2014 noted that 449 companies in the S&P 500 index used 54% of their earnings, a total of a colossal $2.4 trillion, to buy back their own stock in the open market

It is vital, in short, to all our futures that our business leaders remember St Augustine's warning that to be lost in oneself, to focus on means rather than greater ends, is a misuse of your talents, a waste and a sin, and that it applies to organisations just as much as it does to individuals. ■

ABOUT THE AUTHOR

Charles Handy has moved through careers as an oil executive, a business school professor and BBC broadcasting and is widely acknowledged as a world leader in management thinking. His prolific authorship includes books which are standard works on bookshelves worldwide, including his memoir, Myself and Other More Important Matters, as well as The Elephant and the Flea, and The Empty Raincoat. His new book, The Second Curve is published in March 2015. His concern for society and individuals as the world faces the changes that technology, demography and economics bring, has been awarded with a dozen doctorates or fellowships, numerous prizes, and a CBE.



Above
In *The Second Curve*, Handy builds on a life's work to glimpse into the future and what challenges and opportunities lie ahead. Provocative and thoughtful as ever, he sets out the questions we all need to ask ourselves – and points us in the direction of some of the answers.

This article is an edited version of a presentation by Professor Charles Handy to the European Forum Alpbach in August 2014., and was published in EFMD Global Focus, Volume 9 Issue 01, 2015. www.efmd.org

From the top of the boot to the toe, the Italian hotel scene is booming. Here, our favourite places, whether urban style setters or idyllic country retreats, are revealed

LUCULLAN ITALIANO

Like Rome, the best hotels in Italy weren't built in a day. *World Commerce Review* takes the time to check in on our timeless favourites

With its sweeping vineyards, pantheon of historical sites, and beloved cuisine, Italy offers something for everyone. Not surprisingly, its urban retreats and coastal resorts are just as diverse as the guests who visit.

You might sample award-winning gelato in a Byzantine tower in Florence, or take an afternoon swim in a terraced saltwater pool on a secreted corner of the Amalfi Coast. Gratify your inner chef as Nonna teaches you the art of hand-cut pastas, or get pampered like Roman royalty with a massage using rosemary and olive oil from groves at your Tuscan hideaway. In Italy's best hotels, every detail is bellissimo.

Whether conjuring visions of Venetian opulence or rolling-hill retreats and dips in the clear-blue Mediterranean, Italy is an eternal fixture on our list of must-do Europe as well as yours. Uncover the cobbled paths and meandering canals to the best hotels in Italy.

No. 1 Hotel de Russie, Rome

Situated between the Spanish Steps and Piazza del Popolo, Hotel de Russie is a fascinating mix of old and new, with modern design that respects the classical architecture of the building. Since its opening, aristocratic travellers, Russian royalty and renowned artists have all passed through the elegant lobby. With its Secret Garden, Hotel De Russie is a green oasis in the centre of the city. Everything that's great about Rome is within reach. From the splendour of St Peter's to the drama of the Colosseum, Rome is a feast for the senses. The neighbouring Piazza del Popolo and Piazza di Spagna make a good starting point. Throw a coin in the Trevi Fountain before an aperitif in the Centro Historico. The lively Piazza Navona is also within easy reach. Explore the famous fashion boutiques of Via Condotti, Via Borgognona and Via del Babuino. Take a tour of the galleries on Via Margutta or admire the contemporary artworks in the MAXXI museum.

No. 2 Castello di Casole - A Timbers Resort, Casole d'Elsa

A cypress-lined road leads to the rolling 4,200-acre Tuscan estate with a castle that dates back to the 10th century. Now owned by Timber Resorts, it was formerly the home of film director Luchino Visconti and an entertainment centre for countless Hollywood luminaries. The 41 rustic-luxe suites incorporate oil paintings, local antiques, wood-beamed ceilings, and reclaimed terracotta. And Essere Spa, originally the estate's wine cellar, features seven treatment rooms and massages incorporating orange and basil essential oils.

No. 3 Hotel Santa Caterina, Amalfi

Now in its fourth generation of Gambardella family management, this 1904 looker still reigns in Belle Époque splendor. Rooms are spread across the main building, two villas, and a triplet of honeymoon cottages and decorated with local antiques. An elevator descends to a private beach, saltwater pool, fitness center, and thatched-roof pizzeria and fish grill. As you stroll through the secluded terraced gardens and citrus orchards, it's obvious why Liz Taylor and Richard Burton chose to hide out here.

No. 4 Il San Pietro di Positano, Positano

One mile outside town seems to be just far enough from Positano's crowds to attract a constellation of stars (George Clooney, Julia Roberts, Franco Zeffirelli) to the coast's most famous cliff-top hideaway, which spills down the sides of a rocky promontory, its terraced rooms discreetly hidden amid a profusion of flowering plants. The elegant guest quarters - decorated in a singularly odd mix of gilded 18th-century-style elegance and 1970s fab - all come with sea views from private balconies (and, in some cases, from the showers). Tiled benches scattered around the grounds are ideal for sunset cocktails. Though there is a small pool, most guests opt for the private sunbathing patio and sandy beach - a coup for any hotel along this rocky coastline - reached via a dramatic elevator ride down through the cliff.

No. 5 Le Sirenuse, Positano

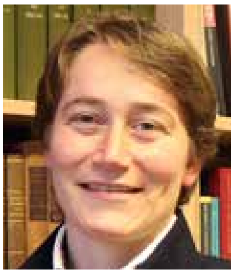
The San Pietro may be flashier, but nothing beats archrival Le Sirenuse for traditional, dignified luxury. In 1953, two years after it opened, John Steinbeck described it as *"an old family house converted into a first-class hotel."* More than half a century of overexposure later, that impression remains at this storied hotel, now in its second generation of Sersale family management. Nearly all the rooms in the poppy-red, 18th-century villa, with museum-quality antiques and hand-painted ceramic-tile floors, have a private balcony or patio overlooking the bay. Diversions include an alfresco champagne-and-oyster bar, a pool and Aveda spa, and a vintage wooden boat for tooling up and down the coast in 1960s-starlet style. The Neapolitan menu at the restaurant, La Sponda, was devised by chef Matteo Temperini.

No. 6 Hotel Savoy, Florence

Situated on Piazza della Repubblica, Hotel Savoy puts you right at the heart of things. Everything that's great about Florence is within its reach. Hotel Savoy is next to the Duomo and within walking distance of the River Arno, Ponte Vecchio, Boboli Gardens and Pitti Palace, as well as the finest designer boutiques of Via Roma and Via Tornabuoni. Hotel Savoy is built on the site where the Mercato Vecchio and church of San Tommaso once stood. Work on the hotel started in 1893 and, once completed, it was praised for its modern and luxurious touches — including central heating, an elevator and even electric lights. Centuries of craftsmanship continue nearby with the city's best shoemakers and bag-makers. Discover more about the legendary Florentine shoe designer at the Salvatore Ferragamo Museum, with its wooden casts of famous customers' feet. Culture lovers can unearth classic treasures at the Uffizi and Accademia Galleries, Davanzati Palace, and the Leonardo Da Vinci and Galileo Museums. Florence is alive with contemporary culture too, with a feast of modern music and cuisine, as well as the Gallery of Modern Art.the front. Have the concierge arrange a roundtrip shuttle to the Mall, where you'll find some of the region's best high-end outlets, including Gucci, Armani, Fendi, and Valentino.

No. 7 Palazzo Avino, Ravello

From the gym to the underwater window in the heated pool, sea views abound at this ornate 12th-century palazzo along the Amalfi Coast (formerly known as Palazzo Sasso). Guestrooms are layered in 17th- through 19th-century antiques, Vietri tile floors, and Frette and Bulgari appointments. Chef Michele Deleo's Italian cuisine has garnered a Michelin star for Rossellinis Restaurant (open April–October).



On the separation of church and state

Discussions on neutrality in the Netherlands

Fleur de Beaufort is a researcher at the Telders Foundation, the Dutch liberal think tank affiliated to the liberal political party VVD

"Yes, religion will fare far better if the civil government does not interfere with it whatsoever, given that all such interference is only bound to have a negative effect on religion."

Boudewijn van Rees

Teylers Godgeleerd Genootschap – founded in Haarlem by Pieter Teyler van der Hulst in 1778 – organised its traditional annual competition in November 1795. The Theological Society endeavours to ensure that this competition always remains topical, which is why the separation of church and state was selected as the theme in 1795. This issue came under discussion that year following the establishment of the Batavian Republic (between the French Revolution and the rule of Napoleon). Participants had to pen an essay that answered the following question: 'May and should a civil government exert any influence over matters relating to religion?'[1]

The Theological Society received twelve entries for this competition, four of which eventually won a prize. The jury awarded a gold medal for the essay written by the Remonstrant clergyman and city secretary Boudewijn van Rees (1753-1825) from the city of Leiden.[2] The work was praised due to its comprehensive reflection on the topic as well as the fact that the winning author was responsive to new insights as the study progressed. In his essay Van Rees advocated the complete separation of church and state.

Although the other prize-winners were also in favour of separation, their arguments were in no way as far-reaching as his. As a Remonstrant[3] clergyman, Van Rees knew better than anyone else what it was like to constantly stand in the shadow of the public church. His essay not only demonstrated that freedom was a *conditio sine qua non* for the purity of the perception of religion, but that a lack of protection, even persecution, was also far more preferable to the status of a privileged church. He believed that the government could only promote religion as such. All financial relations between church and state also had to be separated.[4] Today, the proposal put forward by Van Rees would be regarded as very close to *laïcité.*

Realising that the ideas of Van Rees could have far-reaching consequences, the director of Teylers Godgeleerd Genootschap opposed the jury's majority decision and allowed his feelings to be placed on record in no uncertain terms. This caused a commotion in Haarlem.[5] The desirability of the separation of church and state was a topic that caused great dissension at the end of the 18th century and still does today.

The principle of separation of church and state

When is a separation between church and state realised?[6] If churches are free to develop without any interference by the state, in exactly the same way that any other non-religious organisation in the Netherlands has been able to do so since the liberal constitution of 1848 by virtue of the right of association. And if the state is in turn free of ecclesiastical influence and observes neutrality. In other words, if it does not show any preference whatsoever for one of the religious denominations, nor for the phenomenon of religion or religiosity. The state is therefore not only obliged to observe neutrality towards worshippers of various gods in all denominations (or worshippers of 'something'), but also towards all of those worshippers together on the one hand as well as atheists and agnostics on the other hand.

Although liberals consider religion a private matter, the above does not imply that the existence of confessional parties – such as those that exist in the Netherlands nowadays in the form of the large Christen-Democratisch Appèl (CDA) and the two small orthodox Protestant parties, namely the ChristenUnie (CU) and the theocratic Staatkundig Gereformeerde Partij (SGP) – already violates the principle of the separation of church and state. Whatever inspires politicians from these parties is a matter that concerns only them, as long as they do not act according to obligatory instructions from spiritual leaders.[7]

However, the principle is violated the moment confessional politicians draw up laws or other binding provisions based purely on religious views or writings. If this is indeed the case, a private organisation will 'hijack' the public domain. Religious inspiration must only find its way into the political arena in the form of sound and reasonable arguments.

The desire to make the state and public life neutral is usually viewed by confessional parties as a desire to outlaw religion. But a neutral state is not anti-religious. A neutral state regards religion as a private matter from which it must distance itself, precisely because religion for individual citizens can be so important. Liberals will be quick to concur, but the following question that arises is how far does the order for non-interference extend? Does this also imply that subsidies are absolutely forbidden whatever the circumstances?

Opinions within liberal circles in the Netherlands also differ greatly in this regard. Some people do indeed oppose any form of interference, including subsidy relationships, while others believe that subsidies must be possible provided the state uses objective criteria that organisations from any denomination can also comply with. If a subsidy relationship for liberals is to be reconcilable with the separation of church and state, this can only be the case if that subsidy is equally available to non-religious organisations.

A concrete example: if a subsidy is provided for the renovation of church buildings, this must occur on the basis of their monumental value. And in that case, other monuments without a religious function must be entitled to such a subsidy subject to similar terms and conditions and to the same degree. For liberals, a church or any religious organisation also falls under the standard principle of freedom of association: they enjoy complete freedom of association within the limits of the law, but a church does not have greater freedom, additional privileges or fewer obligations in relation to another private association.

"... how far does the order for non-interference extend? Does this also imply that subsidies are absolutely forbidden whatever the circumstances?"

With regard to neutrality the Dutch professor Wibren van den Burg distinguishes between 'exclusive neutrality', 'inclusive neutrality' and 'compensatory neutrality'.[8] 'Exclusive neutrality' is based on the French principle of *laïcité* and completely excludes religion (as a private matter) from public life. 'Inclusive neutrality' requires the state to be impartial in the sense that all (recognised) religions and beliefs are treated equally, while 'compensatory neutrality' is based on the notion that exceptional circumstances can be involved – such as historical or structural inequalities or social arrears of certain religions

or ideologies – that may make the state provide additional support to groups lagging behind.

Although 'exclusive neutrality' dovetails with the liberal principle of separation of church and state, 'inclusive neutrality' – which can only be characterised as liberal if the neutrality also encompasses non-religious organisations as it will otherwise encroach on the separation of church and state – in fact fits the current situation in the Netherlands best. Whereas 'compensatory neutrality' in my opinion is a veiled term for granting privileges to certain religions and must therefore be condemned as a gross violation of the separation between church and state.

Contemporary discussion on the neutrality in the Netherlands

The last years several political, juridical and legislative decisions showed a growing movement towards more exclusive neutrality. But still there are a lot of violations of the separation between church and state, where religions or religious citizens are treated different in a favourable way.

A recent example of growing neutrality towards religions is the fact that since 2013 blasphemy is no longer a punishable offence in the Netherlands. Ever since a confessional parliamentary majority reintroduced the prohibition of blasphemy in 1932 liberal politicians tried to abolish this particular article in the Dutch Penal Code as it causes legal inequality and is alien to the separation of church and state. Until 2013 the discussion on blasphemy from time to time flared up again, for example after the murder of film director Theo van Gogh, who was stabbed to death by a radical Muslim for his comments on Islam. Of course the recent terrorist attacks in Paris and Copenhagen renewed the discussions on the desirability of legislation on blasphemy, but with the liberals in government there is little chance that this legal inequality will be revived.

Another issue where the discussion slowly tends to more neutrality during the last decade concerns the Sunday rest. Until 2013 most stores in the Netherlands remained closed on Sunday and were not allowed to open. Traditionally in a country with Christian roots, Sunday was regarded as a collective day of rest. Although the liberal party was in support of extending the shopping hours and leave it up to the shop keepers themselves to decide whether they would open their business or not. Since 2013 it is up to the local authorities to decide whether shops in their municipalities are allowed to open at Sunday and how many days a year this allowance will be granted.

Municipalities with confessional majorities still don't allow Sunday openings for shops and in some very orthodox areas also sport facilities remain closed on Sundays. In fact the public domain in these areas is controlled on the basis of religious views, which for liberals contradicts with the separation of church and state.

In a constitutional state every citizen is equal before the law; no one should be above the law or be excused to disobey the law. The Netherlands nevertheless has a number of laws that do not apply to believers with 'conscientious objections'. Some of these privileges are already conferred to certain believers by law, while in other cases the believer can submit a request to be relieved of a statutory duty. For example a small number of strict members of the Dutch Reformed Church object to vaccinations against and even to health insurance policies. From time to time this leads to outburst of for instance small pox or polio among communities with orthodox majorities, always resulting in public debates on the fact that parents are allowed to risk the lives of their children because of their own 'conscientious objections'.

Conclusion

As early as 1795, contestants in Teylers Godgeleerd Genootschap competition argued for a separation of church and state that was certainly far-reaching in those days. The winner even wanted the separation to go further than the present-day situation in the Netherlands. To this very day Teylers Godgeleerd Genootschap holds a completion nearly every year that often features a topical subject in relation to religion. Perhaps a following completion could focus once again on the separation of church and state by asking participants to identify those areas in which this separation has not yet been completed in the Netherlands and how this can be accomplished as quickly as possible. ■

This article is based on a contribution Fleur wrote together with Patrick van Schie, which was published in the book Separation of Church and State in Europe. With views on Sweden, Norway, United Kingdom & Ireland, the Netherlands, France, Portugal, Italy and Slovenia.[9]

1. S Vuyk, 'Pleidooi voor de scheiding van kerk en staat. Teylers Godgeleerd Genootschap en de prijsvraag van 1795' in: E van der Wall and L Wessels (Ed.), Een veelzijdige verstandhouding. Religie en Verlichting in Nederland 1650-1850, Nijmegen 2007, pp. 348-349.
2. Silver medals were awarded to essays submitted by the writer and poet Rhijnvis Feith (1753-1824) from Zwolle, the Mennonite professor Gerrit Hesselink (1755-1811), and Cornelius Rogge (1761-1806), a Remonstrant minister from Leiden.
3. Remonstrants form a small minority within the Christian community in the Netherlands and originate in the resistance against dogmatism and religious constraint during religious upheavals in the Dutch Republic in the beginning of the seventeenth century. In the Remonstrant tradition the freedom of faith has always been the key issue.
4. Vuyk, 'Pleidooi voor de scheiding van kerk en staat', pp. 350-351.
5. Ibidem, p. 349.
6. When referring in general to the relationship between (and the separation of) 'church' and state, we mean all religious organisations that focus on religious perception, and therefore also Jews in synagogues, Muslims in mosques, etc. For the sake of the legibility of our article, the various organisational relationships geared to the perception of religion will not be mentioned separately in the text each time.
7. In the event they do, they are not yet violating the separation of church and state, but are infringing their independence as representatives of the people. This, incidentally, is no different to when a politician follows binding instructions from trade unions, environmental organisations, etc.
8. W van den Burg, Het ideaal van de neutrale staat. Inclusieve, exclusieve en compenserende visies op godsdienst en cultuur, inaugurale rede gehouden op 24 april 2009, p. 29. This distinction between certain forms of neutrality is not exclusively made by Van den Burg, but has also been made by different other researcher.
9. The book is digital available via:
http://www.liberalforum.eu/en/publications.html?file=tl_files%2Fuserdata%2Fdownloads%2Fpublications%2F2012%2FSeparation2012.pdf

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Fixing the broken region of the Caucasus

Jos Boonstra is head of the Eastern Europe, Caucasus and Central Asia programme at FRIDE. Laure Delcour is scientific coordinator and research fellow of the EU FP7 CASCADE project at the Fondation Maison des Sciences de l'Homme

The Caucasus is a broken region, characterised by local tensions and conflicting influences of large regional actors. Armenia, Azerbaijan and Georgia have chosen different paths for political and economic development, while Turkey and Russia – which can also be considered part of the Caucasus – have very different relations with these three states. The Caucasus is also divided between its southern part of three independent republics and a northern Caucasus, which is part of Russia. The Caucasus borders have increasingly emerged as obstacles to cooperation, movement of people and trade.

For the European Union, this landscape is challenging. The EU prefers to deal with well-defined regions, where regional cooperation leads to integration. Unlike in the Balkans (which was another broken region), where the EU did foster regional cooperation as part of the terms for accession, in the South Caucasus the Union is not the only game in town and has to compete with a Russia that aggressively seeks to maintain its influence.

Over the past few years the simultaneous deployment of two mutually exclusive projects – the Deep and Comprehensive Free-Trade Areas (DCFTAs) offered by the EU as part of its Eastern Partnership (EaP) and the Russian-led Eurasian Economic Union (EEU) – has only exacerbated differences in the South Caucasus. In 2014, Georgia (like Moldova and Ukraine) signed an Association Agreement (AA) and a DCFTA with the EU. Neither of the other two South Caucasus countries is likely to conclude similar agreements in the near future. Armenia has become a member of the EEU, which entered into effect in January 2015, while Azerbaijan has so far dodged any hard-law commitments.

Behind a broken region

Armenia, Azerbaijan and Georgia have diverse foreign policy priorities and domestic reform processes. They have thus different expectations vis-à-vis the EU. Moreover, their engagement in either EU- or Russia-driven regional projects is not clear-cut or irreversible, but fraught with multiple tensions.

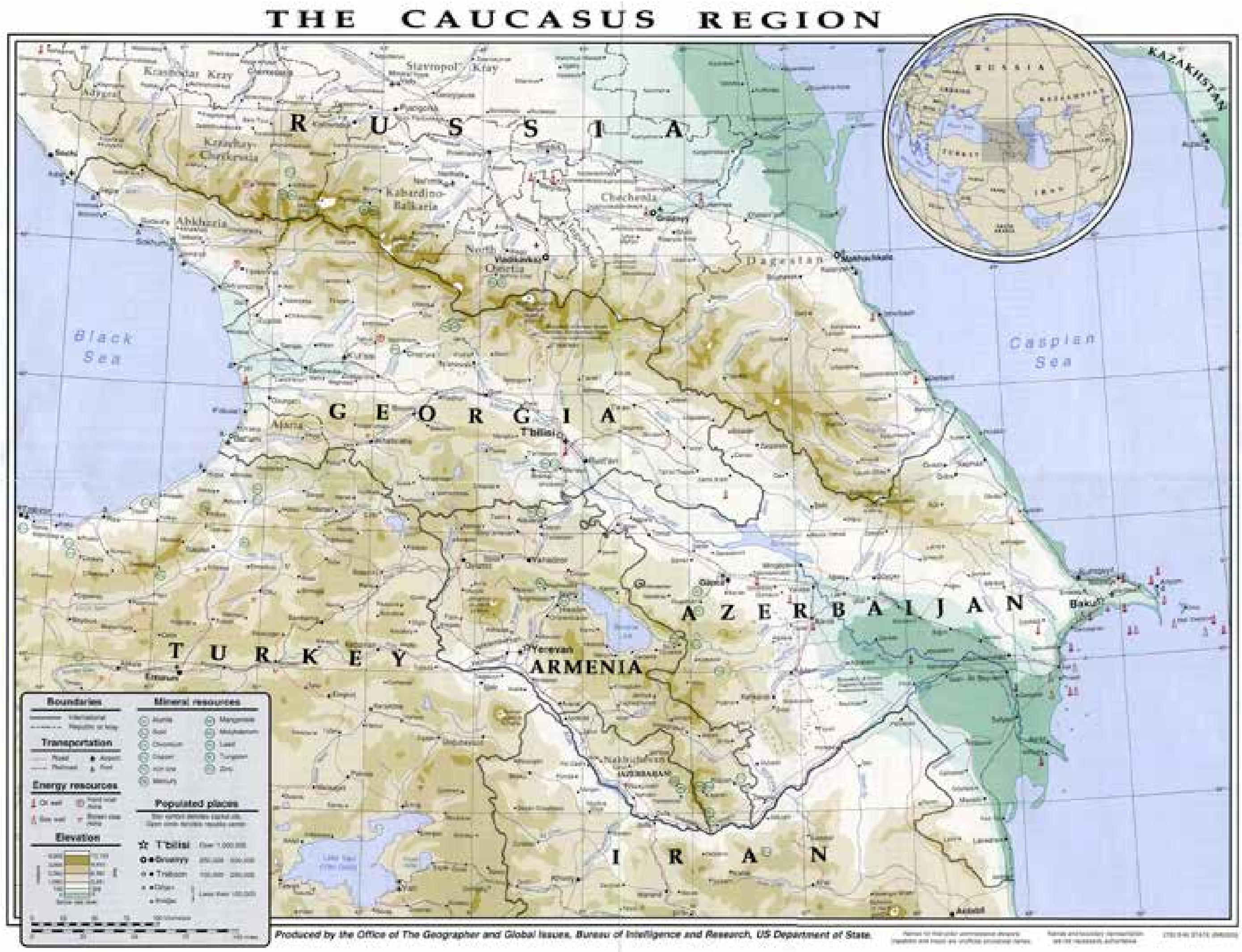
Over the past few years, Georgian attitudes towards the EU have shifted as a result of both regional and domestic developments. The 2008 conflict with Russia – which resulted in the de facto loss of Abkhazia and South Ossetia while also putting an end to the hopes of NATO accession in the short run – marked a turning point. Building on the progress made under the Saakashvili presidency (he was in power from 2004-2013), the current government seems to be speeding up its regulatory alignment with EU acquis (rules and practices).

However, in Georgian eyes, EU policy (or specifically the EaP), has two major flaws. First, it does not offer any membership prospects and the recognition of Georgia as an 'Eastern European country' in the 2014 Association Agreement is of little consolation. Second, it does not help address Georgia's immediate security concerns. For example, as a response to the November 2014 'Treaty on Alliance and Strategic Partnership' between Russia and Abkhazia, the EU could do nothing more than reiterate its support for Georgia's territorial integrity. The newly tabled treaty with South Ossetia goes a step further in granting Russia full control over that Georgian territory. And Tbilisi is aware of the EU's inability to counter Moscow's stronghold over both areas, or any further attempts by Russia to encroach upon Georgian territory.

Initially, Armenia had welcomed the EU's enhanced offer under the EaP; in fact, Yerevan adopted EU trade-related standards and even completed negotiations for a DCFTA. But Armenia's engagement with the EU is complicated by the simmering Nagorno-Karabakh conflict with Azerbaijan, since Yerevan depends on Russian support to deter Turkish-backed Baku. During 2013, Russia started increasing its pressure on Armenia to join the Eurasian Customs Union (the EEU's forerunner) – an option initially ruled out by Yerevan.

As a result, Armenia accommodated Russian requirements at the expense of EU-inspired reforms and joined the EEU. Nonetheless, Armenian authorities seek to preserve links with the EU to the greatest extent possible and Armenia is keen to conclude an agreement that would reflect improved relations with the EU. However, this is unlikely to be easily accepted by Brussels, since Armenia's 2013 U-turn generated disappointment and mistrust and tailor-made bilateral arrangements would take time to develop within the current rather stringent EaP format.

For its part, for the moment Azerbaijan can afford the luxury of not aligning with the EU – or listening to prescriptions on human rights and democracy – or submitting to Moscow's will. The country's vast wealth of oil and gas has resulted in the firm establishment of an authoritarian regime that maintains an iron rule at home and advertises its economic progress abroad. As the country's economic growth skyrocketed, Baku's ruling elite has tightened control over society. In the past few years, the political opposition has been marginalised, independent



Source: CIA, 'Map of the Caucasus region in 1994', University of Texas Library, available at: http://commons.wikimedia.org/wiki/File:Caucasus_region_1994.jpg

journalists repressed, and there has been a purge against independent non-governmental-organisations (NGOs) and think tanks.

However, in contrast to its sanctions on Belarus, for example, the EU is not prepared to consider sanctions against Azerbaijan, unless mass violations of human rights take place. First, the EU is less concerned about developments in a country that is not a direct neighbour and has no desire for membership. Second, the EU views Azerbaijan as a future alternative to Russia for gas supplies (especially if the Trans-Anatolian Natural Gas Pipeline is built). And last but not least, the country is an interesting partner to the EU (and the US) from a geostrategic perspective. Like neighbouring Iran, Azerbaijan is Shiite, yet moderate and secular, and is ethnically and linguistically close to (NATO member) Turkey.

The way ahead

It is in the EU's interest that the Caucasus becomes a stable and democratic region. This will require the EU to prioritise bilateral approaches to the region. Relations should be increasingly country-tailored, taking into account the needs of both the EU and its partners.

The Russian authoritarian model will keep traction as it pretends to solve the short-term worries of some of these states and to safeguard the incumbent regimes. The EU should be ready to fully support those countries that do opt for in-depth political and economic reforms. All three countries are aiming for (albeit at different speeds) visa liberalisation, which requires substantial reforms in key areas such as migration management or the fight against corruption. Georgia may get a visa-free regime this year, while Armenia may progress toward a visa liberalisation action plan. Azerbaijan is further behind, but visa facilitation and readmission agreements signed with the EU are in force.

As such, the EU could be an agent for domestic change in the South Caucasus. It will be essential for the EU to engage increasingly with the region's societies, and not only the incumbent governments. Visa liberalisation, trade, educational exchanges and civil society cooperation are essential in this sense. Europe's attractiveness remains high – also in Armenia and Azerbaijan – and in the long run will be more influential than short-sighted Russian propaganda.

Security-wise, neither a harder security posture from the EU, nor success in settling protracted conflicts in the South

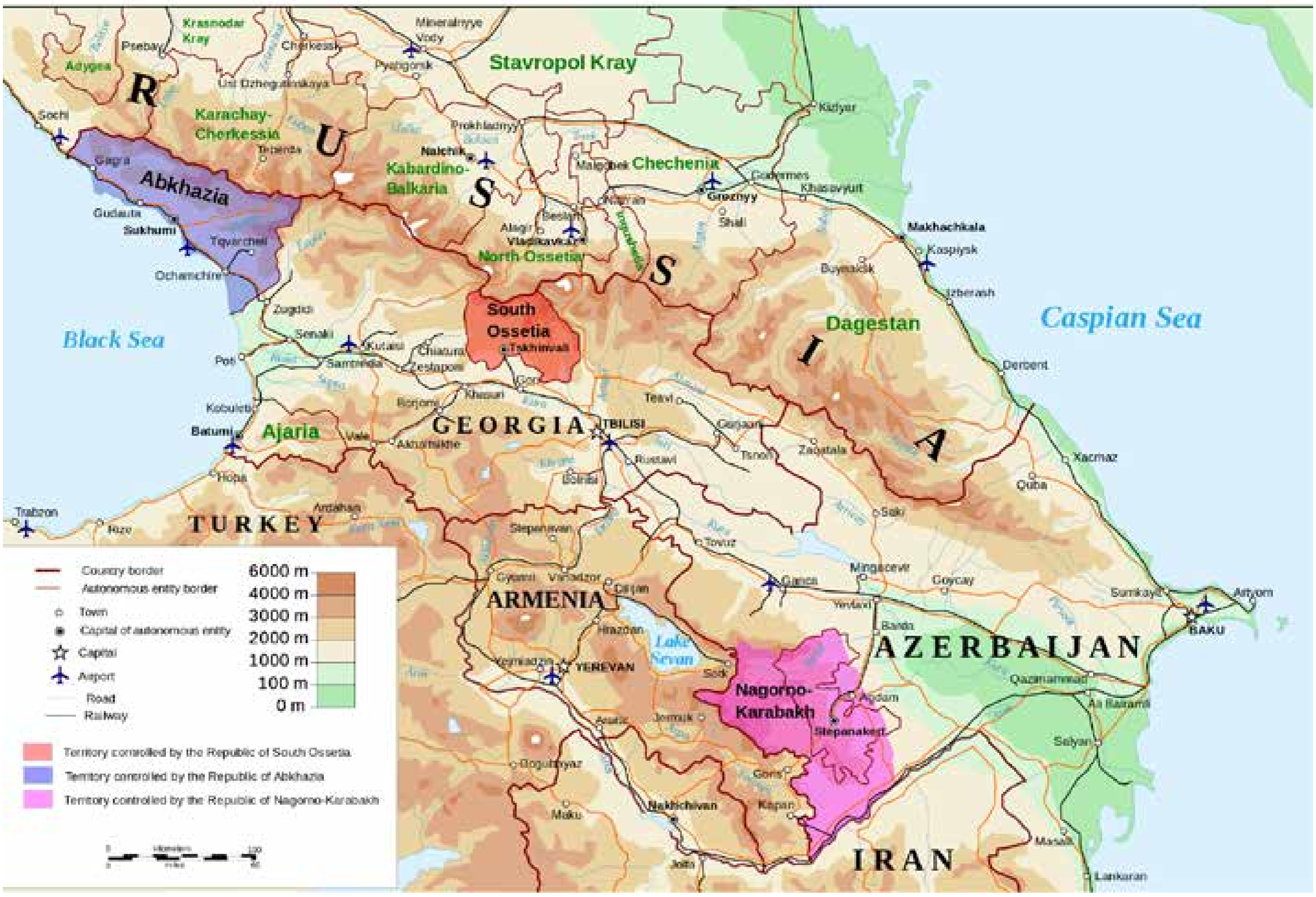
“The EU should seek to play a responsible and more active security role in the South Caucasus by being prepared for further problematic relations with Russia, and being ready to cope with a shifting, complex, and uncertain domestic and regional environment”

Caucasus (without Russian involvement and agreement), are on the table. The current EU engagement in security matters is largely confined to the Common Security and Defence Policy (CSDP) border monitoring mission in Georgia (EUMM) and the participation of an EU Special Representative in the Geneva talks between Georgia and Russia. Besides stepping up EU engagement through NATO and the Organisation for Security Cooperation in Europe (OSCE) at the Minsk talks concerning Nagorno-Karabakh, there is little more the EU can do.

However, the EU could more strongly support the reform of the security sectors of those countries willing to engage, for instance by assisting in reforming partners’ police, border guards, judicial systems, and democratic oversight mechanisms. Furthermore, there are elements of security sector reform (SSR) in the EU’s visa liberalisation policies with Caucasus countries as these affect some aspects of the police, border guards and judicial systems; this can potentially be an entry point for broader SSR engagement.

The ongoing fragility and fragmentation of the South Caucasus will not be fixed anytime soon as the region is prone to domestic instability, inflammable protracted conflicts, and Russia’s heavy influence. The EU will not (and cannot) fix the Caucasus region, but it can have a positive bearing on its development. The EU should seek to play a responsible and more active security role in the South Caucasus by being prepared for further problematic relations with Russia, and being ready to cope with a shifting, complex, and uncertain domestic and regional environment. ■

The breakaway republics of Abkhazia, South Ossetia and Nagorno-Karabakh within the Caucasus region (after August 2008)



Source: Andrei nacu, ‘The breakaway republics of Abkhazia, South Ossetia and Nagorno-Karabakh within the Caucasus region, after the South Ossetia war in August 2008’, English Wikipedia, available at: http://commons.wikimedia.org/wiki/File:Caucasus_breakaway_regions_2008.svg

This article is based on a longer FRIDE document “A broken region: evaluating EU policies in the South Caucasus” (FRIDE Policy Brief 193, January 2015, www.fride.org), published under the CASCADE Project (www.cascade-caucasus.eu)

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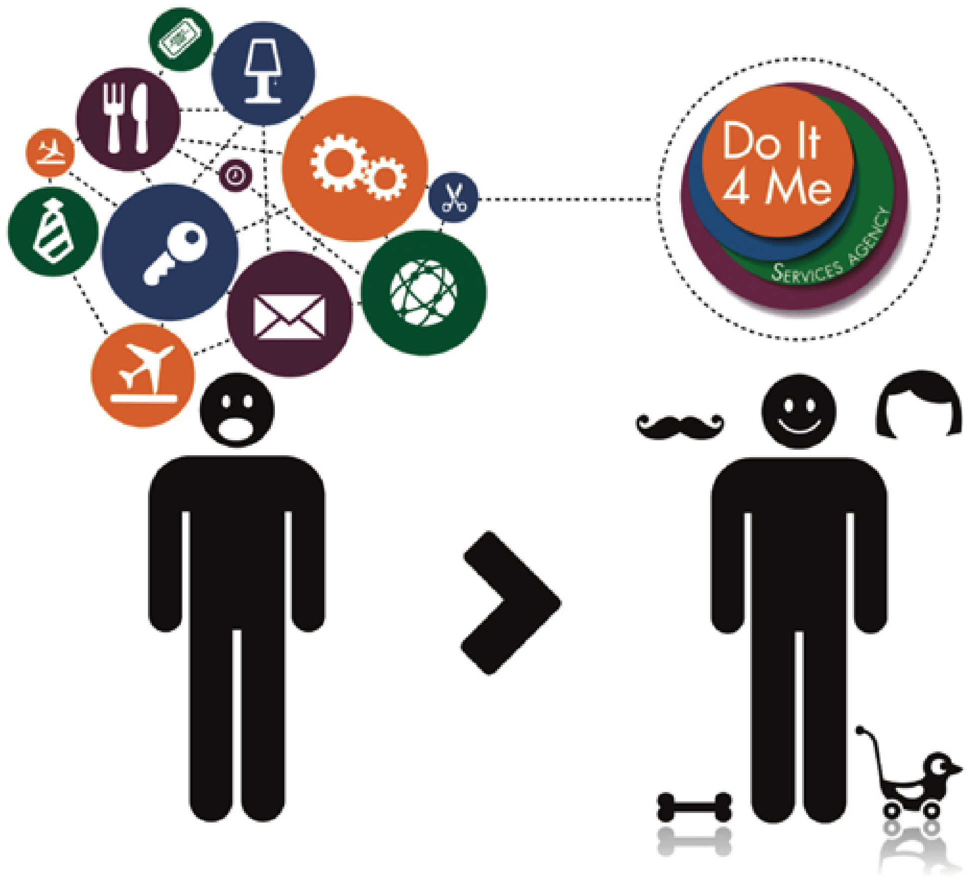

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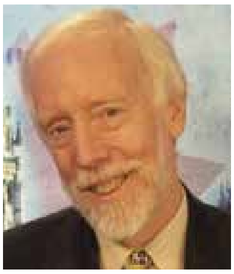

Reconsidering climate change

Tom Harris is Executive Director of the Ottawa, Canada-based International Climate Science Coalition (www.ClimateScienceInternational.org).

Climate sceptics include many of the world's most qualified scientists - ignoring them is causing disaster for the world's most vulnerable people

If you believe environmental activists, only unqualified, right-wing scientists funded by the hydrocarbon fuel sector contest the hypothesis that anthropogenic carbon dioxide (CO_2) emissions will cause dangerous climate change. Climate sceptics, at times mislabelled 'deniers', are frequently portrayed as a small, monolithic band of ignorant troglodytes who don't care about future generations or the environment.

This mistaken idea was perhaps best summed up by Lord Robert May, former president of the Royal Society, who famously described the climate science debate by saying, *"On one hand, you have the entire scientific community and on the other you have a handful of people, half of them crackpots."*

Main stream media amplify this message, portraying the science as 'settled' and dissenters misguided or corrupt and so not worth listening to. The *Los Angeles Times* even announced its editorial policy to not publish letters to the editor questioning political correctness on the issue. With only rare exceptions, politicians of all persuasions follow suit. 'Scientists agree; the time for action is now,' is the clarion call.

US Secretary of State John Kerry is a prime example of this overconfidence. After telling Indonesian students, civic leaders, and government officials on February 16, 2014[1] that climate change represents *"the greatest threat that the planet has ever seen,"* Kerry claimed that climate science is *"simple"*, and *"not really a complicated equation."* The secretary concluded, *"…the science is absolutely certain. It's something that we understand with absolute assurance of the veracity of that science."*

In reality, trying to unravel the causes and consequences of climate change is arguably the most complex science ever tackled. Professors Chris Essex (University of Western Ontario) and Ross McKitrick (University of Guelph) write in their book *Taken by Storm*[2], *"Climate is one of the most challenging open problems in modern science. Some knowledgeable scientists believe that the climate problem can never be solved."*

It is therefore not surprising that many of the world's leading experts either question or refute the claim that CO_2 from the combustion of coal, oil, and natural gas will cause serious climate problems.

The most important evidence of the intense debate raging in the scientific community about climate change is found in the reports of the Nongovernmental International Panel on Climate Change (NIPCC)[3] published between 2008 and 2014. Citing thousands of peer-reviewed references published in the world's leading science journals, NIPCC reports demonstrate that today's climate is not unusual and the evidence for future climate calamity is weak. The NIPCC lays out how the United Nations Intergovernmental Panel on Climate Change (IPCC) has ignored much of the available scientific literature that does not conform to their position on climate change and so often comes to conclusions that do not match the facts.

Surprisingly, there *is* agreement between the NIPCC and IPCC on at least one issue - the lack of extreme weather increase with global warming.

In 2012 the IPCC asserted that a relationship between global warming and wildfires, rainfall, storms, hurricanes, and other extreme weather events has not been demonstrated. In their latest assessment report released on September 27, 2013, IPCC scientists concluded that they had only *"low confidence"* that *"damaging increases will occur in either drought or tropical cyclone activity"* as a result of global warming.

The NIPCC report released on September 17, 2013 concluded the same, asserting that *"In no case has a convincing relationship been established between warming over the past 100 years and increases in any of these extreme events."*

Even here, however, fearing angry backlash from climate campaigners and alternative energy, insurance, banking, and foreign aid spokespeople, politicians continue to claim that a rise in the incidence and severity of extreme weather events will result if we don't 'stop global warming.' That even the IPCC agree that there has been no statistically significant global warming in the past 17 years is simply ignored.

It is not as if sceptical scientists have not tried to bring their views to the attention of political leaders and the public. Literally thousands of scientifically qualified individuals have endorsed open letters and other declarations opposing, either directly or indirectly, the CO_2/dangerous anthropogenic global warming

(DAGW) hypothesis. Among the sceptics signing public documents were Dr Antonio Zichichi, President of the World Federation of Scientists; Freeman J Dyson of Princeton Institute for Advanced Studies; Dr Zbigniew Jaworowski, professor of natural sciences, Warsaw; and Dr Richard S Lindzen, Professor of Meteorology, Massachusetts Institute of Technology. Here are some of the open letters, all linked to their web pages:

2012: 134 climate experts endorsed an open letter to UN Secretary General Ban Ki-moon[4] during the UN Climate Change Conference in Doha, Qatar in which they stated, *"The hypothesis that our emissions of CO_2 have caused, or will cause, dangerous warming is not supported by the evidence."* Mr Ban did not respond to the letter.

2012: 50 former NASA scientists and astronauts signed an open letter to NASA Administrator Charles Bolden[5] in which they asserted, *"We believe the claims by NASA and GISS, that man-made CO_2 is having a catastrophic impact on global climate change are not substantiated."*

2010: 142 climate experts from 22 countries endorsed the Climate Scientists' Register[6] which stated, *"…having assessed the relevant scientific evidence, [we] do not find convincing support for the hypothesis that human emissions of CO_2 are causing, or will in the foreseeable future cause, dangerous global warming."*

2010: 35 climate and related experts signed an open letter to the US Environmental Protection Agency Administrator Lisa P Jackson[7], which claimed, *"…we can demonstrate that rising CO_2 levels have had little impact on the Earth's climate so far, and at this point, there is little theoretical reason to believe they will ever have a significant impact."*

2009: 166 science and technology experts from 15 countries well qualified in climate science[8] endorsed the Copenhagen Climate Challenge[9], sent to Mr Ban during the UN Climate Change Conference in Copenhagen, which challenged the UN *"to produce convincing OBSERVATIONAL EVIDENCE for their claims of dangerous human-caused global warming and other changes in climate."* Mr Ban did not respond.

2009: 61 experts signed the Open Letter to the Council of the American Physical Society[10] which stated, *"While substantial concern has been expressed that emissions may cause significant climate change, measured or reconstructed temperature records indicate that 20th and 21st century changes are neither exceptional nor persistent, and the historical and geological records show many periods warmer than today."*

2009: 115 scientist endorsed an open letter to President Barack Obama[11] which stated, *"Mr President, your characterization of the scientific facts regarding climate change and the degree of certainty informing the scientific debate is simply incorrect."*

2008: 206 climate science specialists or scientists in closely related fields agreed to the Manhattan Declaration on Climate Change[12], in which they agreed, *"That there is no convincing evidence that CO_2 emissions from modern industrial activity has in the past, is now, or will in the future cause catastrophic climate change."*

"The real tragedy in the climate debate is that most climate funding is devoted to trying to prevent events that might someday happen, not to what is actually happening today"

2007: 100 scientist signed an open letter to Mr Ban[13] to coincide with the UN Climate Change Conference in Bali, Indonesia in which they stated, *"…it is not established that it is possible to significantly alter global climate through cuts in human greenhouse gas emissions."* Mr Ban did not respond.

2006: 60 climate experts signed 'Open Kyoto to Debate - An open letter to Stephen Harper, Prime Minister of Canada'[14], which stated *"Global climate changes all the time due to natural causes and the human impact still remains impossible to distinguish from this natural 'noise.'"*

2003: 46 leading scientists endorsed 'Protocol lacks 'credible science' - Open letter to Canadian PM Paul Martin,'[15] calling on the Government of Canada to conduct *"wide ranging consultations with non-governmental climate scientists as soon as possible in order to properly consider the range of informed opinion pertaining to the science of Kyoto."* Mr Martin did not respond.

2002: 30 scientists[16] signed an open letter to Canadian PM Jean Chretien[17], asserting, *"Many climate science experts from Canada and around the world, while still strongly supporting environmental protection, equally strongly disagree with the scientific rationale for the Kyoto Accord."* Mr Chretien did not respond.

1997 and later: 31,487 American scientists (including 9,029 with PhDs), thousands of whom are qualified in climate science, allowed their names to be listed as supporting the Global Warming Petition Project[18] which asserted, *"There is no convincing evidence that human release of CO_2, methane, or other greenhouse gases is causing or will, in the foreseeable future, cause catastrophic heating of the Earth's atmosphere and disruption of the Earth's climate."*

1995: 80 scientists endorsed the *Leipzig Declaration on Global Climate Change* which stated, *"…we consider the scientific basis of the 1992 Global Climate Treaty to be flawed and its goal to be unrealistic. The policies to implement the Treaty are, as of now, based solely on unproven scientific theories [and] imperfect computer models…"*

1992: 46 scientists[19] agreed to the 'Statement by Atmospheric Scientists on Greenhouse Warming[20],' which warned, *"Such policy initiatives [the Earth Summit] derive from highly uncertain scientific theories. They are based on the unsupported assumption that catastrophic global warming follows from the burning of fossil fuels…"*

While none of this proves that the majority of climate scientists support the sceptics' position, it demonstrates that Lord May's 'crackpot' label is unsubstantiated - sceptics include some of the most highly qualified climate experts on the planet.

Despite claims by activists and politicians that the vast majority of climate scientists agree with the DAGW hypothesis, this has never been demonstrated by a reputable worldwide poll. Australia-based climate data analyst John McLean has shown that, even among the thousands of scientists who worked on the IPCC assessment reports, only a few dozen of them actually commented on the issue, and some of those disagreed with the view that activists attribute to all of them.

Statements by national science academies are generally meaningless. Not a single one that officially supports the DAGW view has demonstrated that a majority of its scientist members actually agree with their academy's position. Their statements are simply the politically expedient opinions of the groups' executives, or small committees appointed by the executives.

The popular view that sceptics all march to the same tune is also mistaken. In preparing this article I asked dozens of climate experts who oppose the DAGW hypothesis, *"What kind of climate sceptic are you?"* The answers I received demonstrate a wide variety of opinion:

- A few said that, all other things being equal, some, but not very much, greenhouse warming is to be expected. Christopher Monckton, The Viscount Monckton of Brenchley, fell into this category. Dr Will Happer, Professor of Physics at Princeton University had a similar view. *"CO_2 emissions will probably cause modest warming, although the exact amount is uncertain,"* said Happer. *"Regardless, the additional CO_2 will be a very good thing because of its major benefits to photosynthesis and agriculture."*

- Other sceptics asserted that that our emissions of CO_2 are causing *calculable* warming but that it is lost in the noise of natural variability and so not currently detectable. Dr Howard Hayden, Professor Emeritus of Physics at the University of Connecticut was in this group.

- Many scientists said that our CO_2 emissions may, or may not, be causing measureable warming but, regardless, it will not be significant. Generally falling into this category are Dr Albrecht Glatzle, Agro-Biologist from Paraguay; American meteorologist Joe Bastardi; Australian geologist

Aert Driessen; Dr S Jeevananda Reddy, Formerly of the UN World Meteorological Organization, India; Professor Bob Carter, former Head of the Department of Earth Sciences, James Cook University, Australia; Dr Bruce Borders, Professor, Forest Biometrics, University of Georgia; and Oregon-based 'carbon' sequestration expert Dr Bob Zybach who concluded, *"I believe that human-related CO_2 emissions probably do not affect global temperatures one way or the other."*

- Experts who maintain that our CO_2 emissions are definitely not causing measureable warming included Dr Ian Clark, Professor of Earth Sciences, University of Ottawa; Dr Brian Pratt, Professor of Geology, University of Saskatchewan; Dr Don Easterbrook, Emeritus Professor of Geology, Western Washington University; and Dr S Fred Singer, Professor Emeritus (Environmental Sciences), University of Virginia. Easterbrook explained, *"It's very clear that climate and the oceans drive atmospheric CO_2, not the other way around."*

- Asserting that our CO_2 emissions are not causing temperature changes, or any other sort of climate change at all, are scientists Dr Arthur Rorsch, Emeritus Professor, Leiden University, The Netherlands; Norwegian biologist and climate expert Per Engene; and Dr David Kear, former Director-General of New Zealand Department of Scientific & Industrial Research. Driessen also had considerable sympathy with this position explaining, *"I see no evidence whatsoever that CO_2 has ever been a cause of climate change in the entire geological record."*

- Some sceptics, such as Dr Tim Ball[21], maintain that our CO_2 emissions are causing cooling. Regardless of his stance on the impact of CO_2, solar expert Dr Habibullo Abdussamatov of Russia's Pulkovo Observatory agrees that cooling is most likely. *"From approximately 2014, we can expect the start of the next bicentennial cycle of deep cooling with a Little Ice Age in 2055 plus or minus 11 years,"* concluded Abdussamatov.

Many of the experts contacted refused to have their scepticism categorized. Any thoughts that sceptics are even remotely monolithic are clearly wrong. They are practicing real science where concerns about consensus are irrelevant.

The real tragedy in the climate debate is that, largely because of the mistaken idea that we know the future of climate change and humanity controls it, most climate funding is devoted to trying to prevent events that might someday happen, not to what is actually happening today.

According to the San Francisco-based *Climate Policy Initiative* (CPI) report (October 2013), of the approximately US$357 billion (almost $1 billion per day) that was spent on climate finance across the world in 2012, only 6% of it went to helping people in today's world prepare for and adapt to climate change.

CPI's 2011 report demonstrated that, even within developing countries, only 5% of climate finance went into adaptation, an approach that costs many lives each year in countries such as The Philippines which are subject to severe, periodic natural disasters. The rest of the money was directed to 'mitigation', trying vainly to stop climate change in the distant future. This is essentially giving more value to the lives of people yet to be born than those suffering today due to climate variability. This is clearly immoral.

John Kerry was right to tell Indonesians that climate change is a serious danger to humanity if not addressed appropriately. And scientists explained to the UN Secretary General in the 2009 Copenhagen Climate Challenge exactly what that appropriate approach is: *"Climate policies need to focus on preparation for, and adaptation to, all dangerous climatic events however caused."*

Assisting countries adapt to present day climate change should be a foreign aid issue driven only by humanitarian concerns and our financial capabilities. Accepting responsibility for causing what are almost certainly natural climatic events is irrational and, ultimately, hurts the world's most vulnerable people. ■

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7. http://sppiblog.org/news/many-leading-scientists-tell-the-epa-to-think-again
8. https://web.archive.org/web/20120722125346/http://www.copenhagenclimatechallenge.org/index.php?option=com_content&view=article&id=64&Itemid=1
9. https://web.archive.org/web/20130403061013/http://www.copenhagenclimatechallenge.org/index.php?option=com_content&view=frontpage&Itemid=1
10. http://scienceandpublicpolicy.org/images/stories/papers/commentaries/american_physical_society.pdf
11. http://object.cato.org/sites/cato.org/files/pubs/pdf/cato_climate.pdf
12. http://www.climatescienceinternational.org/index.php?option=com_content&task=view&id=66&Itemid=1
13. http://climatescienceinternational.org/index.php?option=com_content&view=article&id=445
14. http://www.lavoisier.com.au/articles/greenhouse-science/climate-change/openletter2006-3.php
15. http://www.john-daly.com/guests/openletter.htm
16. http://www.eecg.utoronto.ca/~prall/climate/ca02_orig.html
17. http://www.parl.gc.ca/HousePublications/Publication.aspx?DocId=605426&Language=E&Mode=1&Parl=37&Ses=2%20-%20T1350
18. http://www.petitionproject.org/
19. http://www.tpromo2.com/gko/sep00/092200f.htm
20. http://www.tpromo2.com/gko/sep00/092200e.htm
21. http://drtimball.com/

Soaring to new heights

PH Richard Smith MBE FRAeS, is Director General of Civil Aviation at the Civil Aviation Authority of the Cayman Islands

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For more information on The Cayman Islands Aircraft Register, please visit www.caacayman.com

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Tachymeter-display with double second hand

The dial also reflects technical refinement and motor sports excitement:

A double seconds hand makes it possible to shift the tachymeter index at the 120-km marker precisely to 12 o'clock. The upper, straight-cut part of the seconds hand is used for the chronograph function. The lower, wedge-shaped part of the seconds hand indicates the average speed measured for a distance of one kilometre (tachymeter function). The tachometer-style seconds hand prevents confusion and assures correct readings for each measurement.

Our professional timepieces are characterized by their unique design concepts and the movements integrated in their cases.

Future-oriented

The accuracy of quartz movements developed in the 1970s can hardly be further enhanced. Mechanical movements, true wonders of technology that established the reputation of Swiss watches, can be improved only at the detail level. This is why, looking to the future, we are on a permanent quest for new technical solutions. Currently, we are developing a new, mechanically inspired ecological drive system whose accuracy can be compared with that of a quartz movement.

Formex Watch SA is the brainchild of watch designer and CEO Hans Peter Grädel.

"It has always been my ambition to create a watch with motor sports appeal. Everything began with the patented suspension system that we developed in-house. Quite simply, it is part of every Formex 4SPEED watch. Features like these and superior technology combined with sporty styling characterize our collections. I am sure that our timepieces are more than just extraordinary. They are literally ahead of their time."

Having a FORMEX watch on your wrist means having a reliable technical expert with you as a friend both for sport and in life. It is a technologically advanced instrument and integrated with a Swiss Made movement. You are not simply wearing just a 'Watch'! A FORMEX watch on your wrist is a philosophy FOR SPEED in life! ■

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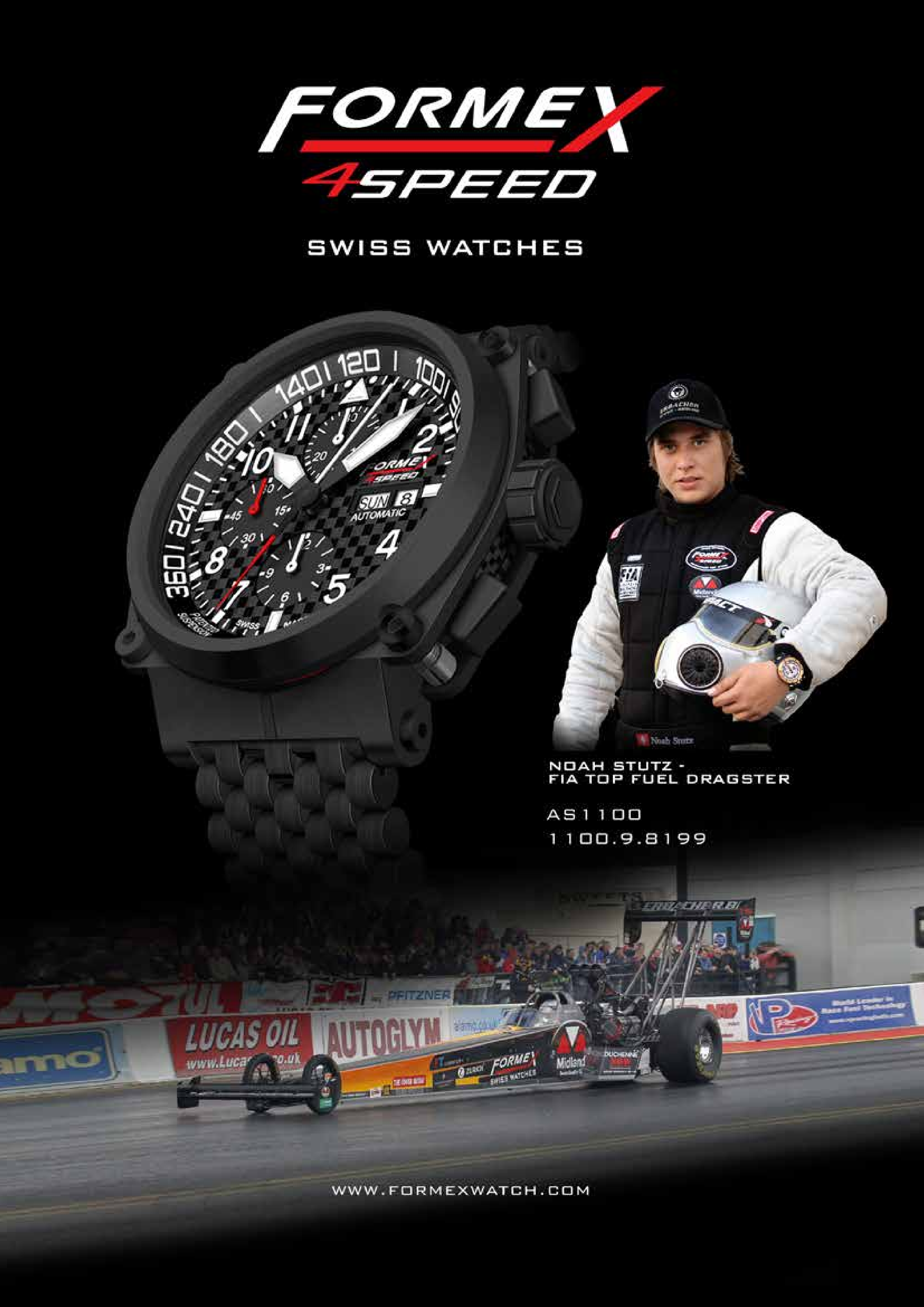
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Flying high

Stanley Bugeja is President of the Malta Business Aviation Association (MBAA)

It has been now one hundred years since the first sea plane landed in Malta. As Malta celebrates its hundred years of aviation, the Malta Business Aviation Association is proud of the success the country has achieved in the past five years within the business aviation industry.

Since Malta enacted the Malta Aircraft Register Act in 2010, and soon after became a signatory of the Cape Town convention, business aviation companies from across Europe and the world came to Malta in the scores. With close to thirty EASA Air Operating Certificate licensed business jet operators and close to a hundred business jets on the Maltese aircraft register, despite its tiny size Malta is punching well above its weight.

Within the European Union and not just, Malta is one of the fastest growing reputable business aviation jurisdictions. Despite the economic downturn and uncertain recovery Malta has proven to be not only resilient but also innovative, providing serious business aviation aircraft management companies operators with a sound legal framework which is efficient and cost effective.

The Maltese jurisdiction provides the operating and managing companies with the confidence that in the ever changing EASA legislative framework the Maltese Civil Aviation Directorate will not only regulate but does so safely and efficiently. As a signatory of the Cape Town convention, business jet owners and financiers alike have the comfort that their asset and their investment is protected and recognised through a well-oiled and efficient mechanism, which has proved its clout and substance, time and again in the past five years.

As a small island in the Mediterranean, Malta has always acknowledged the importance of aviation for its survival. Hardly any businessmen or government official is indifferent to the aviation industry. The aviation sector provides the island with connectivity it requires to exist and prosper. Scheduled and charter airlines connect Malta to world 365 days a year. Having one of the longest runways in Europe, Malta International Airport can handle any type of aircraft. The aviation industry in Malta has found a jurisdiction which does not give it lip service, but instead the support it requires for a sustained growth.

The aviation economic activity on the island is testament to this. The island hosts some of the most renowned and largest Maintenance Repair Organisations in Europe, whether a scheduled airline or a business jet operator, the island has it covered. Government and private schools provide a myriad of aviation courses, not only to serve its own demand, but in view of the expertise available on the island, the country is also experiencing a growth of foreign individuals and organisation who undertake their aviation training requirements in Malta.

The MBAA recognises the fact that to remain at the forefront of this industry the Maltese private and public sector need to continue to work together to improve the framework and sustain the growth. To this end one of the most ambitious programs of the association is that amongst other activities, the Malta Business Aviation Association together with Malta Enterprise, a government agency, have embarked on a project to create an aviation cluster with the participation of both the private and public sector. The objective of the cluster is to collectively work together to increase the productivity, services offered and gain a competitive edge.

For the fifth year the MBAA, Malta Enterprise and Transport Malta will be participating in Europe's largest business aviation conventions and exhibitions. It provides not only a platform for the local service providers but also for future customers of the jurisdiction the opportunity to meet and discuss why Malta with the authorities but also members of the aviation community who experience it first-hand. See you in Geneva. ■

The Malta Business Aviation Association (MBAA) aims to promote excellence and professionalism amongst our Members to enable them to deliver best-in-class safety and operational efficiency, whilst representing their interests at all levels in Malta and consequently Europe. The MBAA will strive to ensure recognition of business aviation as a vital part of the aviation infrastructure and the Maltese economy.

MBAA
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