

Moving the Bar

How the US and UK Can Help
Create a New Level Playing Field
for Digital Trade



BritishAmericanBusiness



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Introduction

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Given the UK's imminent departure from the EU, the international trade context, and the historically strong relationship between the UK and the US, it is critical and timely to examine the current state of digital trade and the way in which the two global leaders can enable its development.

First, the growth and scope of the global digital economy, in which both the US and UK are leading players, is enormous and ever-growing. The digital transformation has helped to reduce costs, facilitated the coordination of global value chains, spread innovation, and connected businesses and consumers. The momentum needs to be captured and harnessed.

Second, digital trade has largely been neglected in global trade agreements, with some notable exceptions in the United States-Mexico-Canada Agreement (USMCA) and the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP). There is a clear opportunity to build on these recent agreements to further strengthen digital trade in the US-UK context.

Third, two of the economies most active in digital trade, the US and the UK, have expressed the ambition to agree on a comprehensive trade agreement, with a focus on services.

This paper explores the breadth, importance, and challenges of digital trade, as well as how the US and the UK can consolidate forward-looking principles and provisions in upcoming free trade negotiations, in order to help create a level playing field which enables digital trade across the Atlantic and worldwide. The paper at hand should be a basis for future discussions around digital trade and the US-UK relationship.

Digital Trade: More Than Just ICT

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The digital transformation of the economy and society is well underway, with industries and whole ecosystems realigning and consolidating around digital innovation. The distinction between the offline and online world is no longer meaningful, as digitization and data transfers have long ceased to be relevant to the Information and Communications Technology (ICT) sector; in fact, **a full 60% of global GDP is expected to be digitized by 2022.**¹

While difficult to correlate data traffic with commercial links, the sheer volume and increase in data flows is indicative of the current state of digitalization: the volume of data crossing borders has risen by 64 times during the course of this decade. Between 2015 and 2017 alone, the data deployed on international networks doubled, rising to 684 terabits per second.²

Additionally, the highly anticipated 5G will increase the volume of mobile data to 131 exabytes per month by the end of 2024. The 5G-enabled Internet of Things (IoT) is expected to add \$1.1 trillion in value by 2025 and will continue to expand the size of the global digital services market.⁵

In this context, digital trade – defined by the OECD as digitally-enabled transactions of trade in goods and services that can be delivered either digitally or physically – is one of the fastest growing areas in international trade. It includes digitally delivered software, e-books, data or database services, as well as digitally-enabled but physically delivered goods and services, such as purchasing a good or using a matching service to book a taxi or hotel room.⁶



- **3.5 billion people are connected to the internet**
- **\$27.7 trillion global e-commerce market**
- **\$90 billion digital content revenue**
- **5G will increase the volume of mobile data to 131 exabytes per month by 2025**
- **IoT expected to add \$1.1 trillion in value to global digital services market**

Global digital trade is booming. The total internet-connected population reached 3.5 billion people in 2018 – almost half of the entire world's population.⁷ Global e-commerce grew to over \$27.7 trillion in 2016; in the same year, global digital content revenue nearly reached \$90 billion and spending on public cloud services reached nearly \$63 billion in the US and \$19 billion in the EU (the two largest markets).⁸

Overall, half of all global trade in services now depend on access to cross-border data flows.

Therefore, it is imperative that 21st century trade policies encompass these developments and continue to enable growth.

Digital Trade in a US-UK Context



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Nowhere is the digitalization of the world more clearly noticeable than in the transatlantic corridor, where the US and Europe together generate roughly three quarters of the global digital content. In 2017, the US registered a \$172.6 billion trade surplus in digitally-enabled services with the world. Its main commercial partner was Europe, to which it exported \$204.2 billion in digitally-enabled services and from which it imported \$123.7 billion.⁹

Within that, the US and the UK make up the largest part of the digital trading flows. Most of the trade between the two countries consists of services, all of which is being digitized. In 2018, for example, total US trade in services with the UK (exports and imports) amounted to an estimated \$134.8 billion.¹⁰

The UK is the third largest e-commerce market in the world – worth £560 billion in 2017.¹¹ The UK is the US' biggest digitally-enabled services trading partner, accounting for 23% of US exports and 29% of US imports of digitally deliverable services from the EU.¹²

In 2017, US exports of ICT goods were \$146 billion, while ICT services exports amounted to \$71 billion. In addition, exports of potential digitally-enabled services were \$439 billion, comprising over half of US services exports that year.¹³

As such, the US and the UK, consistently ranked as two of the most innovative economies in the world,¹⁴ find themselves in an excellent position to lead by example, promoting global rules and principles that continue to enable growth in digital trade.

Challenges and Barriers to Digital Trade

Formulating and implementing digital trade policy in a way that maximizes its growth, however, is not a simple task. At the international level, there are often disagreements between countries and trading blocs over what policy priorities should be. This is often because of issues at the domestic level, where there are competing interests between different stakeholder groups, as well as regulations which may create barriers for digital trade.

For instance, trade negotiators, together with companies and individuals seeking to do business abroad, focus on opening or maintaining market access, which may include cross-border data flows, while others may try to block or restrict these data flows in order to limit foreign competition. Privacy advocates often focus on protecting personal information, while law enforcement and defense advisors may seek the ability to access or limit information flows on national security grounds.

In practice, these interactions between different stakeholders may result in several types of barriers to digital trade, such as the imposition of tariffs and duties, regulatory barriers, or uncertainty due to security risks and Intellectual Property Rights (IPR) infringement.¹⁵

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- **High tariffs:** tariffs at the border raise the prices of products for producers or end customers, thus reducing market access for exporters. Both Free Trade Agreements (FTAs) and the World Trade Organisation's (WTO) Information Technology Agreement currently ensure that tariffs are not levied on many digital products.
- **Cross-border data flow limitations**
 - **Localization requirements** increase costs by compelling companies to maintain physical infrastructure within a country's borders for digital services conducted there. Data localization raises data hosting costs by 30%-60%, while, according to studies, it also impacts free speech, social mobility, and civic engagement by restricting information availability.¹⁶
 - **Filtering or blocking:** governments often seek strict control over digital data within their borders, such as what information people can access online and how information is shared inside and outside its borders. Governments that filter or block websites, or otherwise impede access, form another type of non-tariff barrier.¹⁷
 - **Differing legal requirements for the protection of personal data** can act as a barrier to the movement of data and therefore digital trade between jurisdictions. In the case of jurisdictions that do not have an agreement that allows for the movement of personal data between companies operating across borders, various legal mechanisms must be put in place by the company, adding cost and complexity.

- **Cybersecurity risks:** Cyberattacks are deliberate attempts by unauthorized persons to access ICT systems, usually with the goal of theft, disruption, damage, or other unlawful actions. Cybersecurity risks can disrupt business operations and supply chains and create uncertainty for businesses. Specialist analyses have estimated that cybercrime has a direct GDP cost of \$275 billion to \$6.6 trillion globally, and total GDP costs (direct and systemic) of \$799 billion to \$22.5 trillion (representing 1.1 to 32.4% of global GDP).¹⁸
- **Intellectual Property Rights infringement:** one of the downsides of the digital revolution is the ease with which trademarks and copyright can be copied and infringed. It is estimated that the value of digitally pirated music, movies, and software was over \$200 billion in 2013 and would grow to as much as \$384-856 billion in 2022.¹⁹ The annual cost to the US economy alone from counterfeit goods, pirated software, and theft of trade secrets has surpassed \$225 billion (not including patent infringement).²⁰
- **Discriminatory standards or burdensome testing:** where national or local standards diverge widely from international standards, costs for businesses rise as they must ensure compliance. If it is unable to comply, a firm's ability to serve a market is severely limited.
- **Opaque and anti-competitive telecommunications regulations:** Modern trade flows cannot exist without communications services. These services allow businesses to reach new markets and provide the flows of goods and services that trade agreements are intended to facilitate. Lack of clarity around regulations and restricting access to networks create anti-competitive business environments.
- **Governments requiring the handover of source code and algorithms as a prerequisite for market access.** This leads to higher costs, lower access to products and content, uncertainty and distrust concerning the use of products and services, and, in some cases, human rights violations.
- **Low *de minimis* thresholds:** Most countries' *de minimis* levels – which exempt low value imports from tariffs and consumption taxes – have not kept up with the proliferation of online shopping. *De minimis* thresholds enable faster customs clearance for low-value goods. Most current thresholds are not high enough to facilitate trade and avoid customs clearance delays.²¹



The USMCA - The US' Gold Standard for Digital Trade

As digital trade has grown in importance over the past decades, it has also slowly climbed up the US' and other countries' trade policy agendas. The majority of existing trade agreements, however, have not fully kept pace with the digitization of the economy and society. The first time the US included an e-commerce chapter in its FTAs was its 2003 agreement with Singapore. More recently, the US-South Korea FTA contains the most robust provisions in a US FTA currently in force, including on access and use of the internet to ensure consumer choice and market competition, and explicitly refers to cross-border information flows.

The recent successor to the North American Free Trade Agreement (NAFTA), the USMCA takes FTAs a step closer to the digital age by acknowledging and addressing a much broader category than just goods that are sold online: goods and services that are enabled by internet connectivity but can be delivered either online or offline. It is one of the first trade agreements containing a chapter specifically devoted to digital trade.²²

More importantly, the USMCA directly addresses several of the aforementioned barriers to digital trade. These measures can form the basis of discussion for future FTAs' digital trade provisions, as it:²³

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- **Prohibits the imposition of customs duties** on digital products and electronic transmissions.
- **Facilitates cross-border data transfers** by enshrining the principle that free data flows are the norm, with any exceptions needing to be clearly justified. It also recommends that signatories use OECD and APEC norms, as well as APEC's Cross-Border Privacy Rules, which aims to increase interoperability between national privacy regimes as well as predictability for both consumers and businesses.
- **Prohibits data localization measures** for financial services, and any other unjustified purposes.
- **Strengthens IP protection** by extending the prohibition of forced transfer or disclosure beyond source code, to include algorithms.
- **Promotes access to open government data**, providing a boost to data analytics and artificial intelligence.
- **Recognizes that threats to cybersecurity undermine confidence in digital trade** and promotes a risk-based approach based on common standards and best practices.

These provisions represent a solid liberalization agenda on which to build a competitive global market for digitally-enabled goods and services and is balanced by welcome provisions on security and privacy. In that context, the USMCA is the US gold standard for digital trade and a likely model for future US trade agreements.

The UK: A Liberal Force in a European Framework

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The UK's trade policy has historically been determined by its EU membership. Trade with non-EU countries is an EU-level prerogative, as the European Commission formulates policy and conducts negotiations, with input and signoff from Member States and the European Parliament. In this framework, the UK has long been considered a liberal champion; shaping discussions and policies from within.

As the UK prepares to leave the EU, the country will face an interesting, albeit challenging task of balancing the opportunities afforded by leaving a slow and often cumbersome decision-making process with the need to maintain a level of regulatory alignment that ensures it maintains access to the EU's Single Market, and does not jeopardize a future trade agreement with the world's largest trading bloc.

In other words, the UK will most likely want to balance liberalizing, pro-competition principles and provisions with maintaining close alignment with key elements of the European framework, such as the General Data Protection Regulation (GDPR). In pursuing this balance, the UK is likely to embrace certain fundamental principles and provisions which it has itself helped to shape as a Member State.

The latter could be particularly around provisions that safeguard individual privacy and empowering individuals to have access to their personal data and control over how it is used. While at times restrictive, the GDPR includes provisions which businesses across the world that collect and process data on EU citizens have welcomed and are complying with; in return, they maintain access to one of the world's largest markets.

With the GDPR likely to inform global standard setting on privacy in years to come, and the known business need to reach continued alignment between the UK and the EU on data and privacy, the UK can use its experience as a EU Member State to inform future discussions with the US, reflecting the aforementioned principles. **A US-UK trade agreement could set the global standard for digital trade and privacy.**

Recommendations

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With a double-pronged objective of removing barriers to digital trade and maintaining close regulatory alignment with the EU in pursuit of continued access, the future US-UK trade agreement should strike a balance between liberalizing principles on the one hand and safeguarding privacy and cybersecurity on the other. The section below outlines several key digital trade recommendations of the transatlantic business community to inform the discussion towards a successful and forward-looking future agreement:

1. The US and UK governments should use the current window of opportunity to **acknowledge and enshrine the magnitude and volume of global digital trade**, and of transatlantic trade in particular.
2. **Discussions surrounding digital trade should avoid considering it in a vacuum.** Instead, governments must acknowledge the growing digitalization of economy and society, which will help define and develop better policies across all sectors.
3. In formulating positions and drafting the agreement, **policymakers can rely on existing, top-of-the-line agreements such as the USMCA**, which have taken important steps towards bringing trade agreements into the digital age.
4. **The US and the UK should work towards measures aimed at minimizing trade barriers** for digital and digitally-enabled goods and services. As two of the most important liberal forces in the world, both countries should take a leadership role in digital trade by developing the freest possible flow of digital and digitally-enabled goods and services. In particular, the two sides should:
 - a. **Avoid imposing customs duties on electronic transmissions.**
 - b. **Avoid imposing tariffs on digital products.**
 - c. **When considering digital taxation, consider a global, multilateral solution under OECD auspices**, rather than country-by-country solutions which increase fragmentation and regulatory compliance burdens.
 - d. **Facilitate cross-border data transfers**, for example by recognizing OECD Cross-Border Privacy Rules (CBPRs), increasing interoperability and predictability.
 - e. **Avoid forced data localization measures which are highly detrimental to all digitally-enabled services**, and to the financial services industries on both sides of the Atlantic in particular. This should include data transfer/access agreements between financial services regulators.
 - f. **Remove market access barriers for telecommunications services**, which underpin the digital economy, and ensure consistent, pro-competitive regimes. Strong commitments in a US-UK agreement should provide a platform that helps sustain a competitive transatlantic



telecommunications market. Commitments should include:

- **Transparent regulatory frameworks** monitored by independent regulators and data-driven decisions.
 - **Consistent, pro-competitive regulation of business grade wholesale access to telecommunications networks** that prevents discrimination by major suppliers, whether in favor of their own downstream businesses or others’.
- g. **Strengthen Intellectual Property (IP) protection, including for source code and algorithms.** The US and the UK need to make the case for the importance of IP for innovation and cooperation on global challenges.
- h. **Build upon the WTO’s Trade Facilitation Agreement** to further simplify and expedite the clearance of e-commerce shipments. Maintaining high *de minimis* thresholds would be a welcome step forward.
5. Given the close relationship between the US and UK governments on security, the two should also **take the lead on global cybersecurity standards and practices by promoting a risk-based approach** and developing a common vision and commitment to risk management.
6. **Maintain a careful balance which does not put the UK at odds with the EU’s regulatory regime regarding data and privacy.** The EU will remain a critically important trade partner for the UK, while the many US companies which have chosen the UK as their European home will seek to maintain access to the EU’s market. As such, the future US-UK trade agreement should ensure that it does not endanger the free flow of data across the three parties. The UK government’s experience with the EU decision making process should be an important asset in achieving this balance.
7. **Work to improve the volume and quality of data.** In particular, promoting open government data will give access to more highly valuable resources to industries and sectors which employ Artificial Intelligence (AI) and data analytics, in turn improving goods and services.
8. Work towards reducing protectionist sentiment by committing to programs which explain **how the public benefits from data and AI.**

Conclusion



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Digital trade is one of the fastest growing areas in international trade. The digitalization of trade flows therefore needs to be embraced by the global framework, recognizing that the distinction between the offline and online economic world is increasingly losing its meaning.

In context of the UK preparing to leave the EU, both the US and the UK, two of the world's most innovative economies, have a unique opportunity to work together to set a global standard for digital trade.

The way forward in advancing digital trade is by building on the forward-thinking provisions of the USMCA – such as prohibiting or minimizing customs duties, keeping data flows open, adopting a risk-based cybersecurity approach, and strengthening IP protection. This will strengthen the overall relevance and representation of digital trade in the global trading framework.

The US and UK should take advantage of the opportunity to bring together the American and European approaches to digital trade, ensuring that a new transatlantic model will not endanger the trading relationship the UK enjoys with the EU. In addition, we are hopeful that the momentum carried by US-UK discussions on digital trade can create a level playing field for others across the globe to follow.

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