

Background

No. 2061
August 15, 2007



Published by The Heritage Foundation

Free Trade with Taiwan Is Long Overdue

John J. Tkacik, Jr., and Daniella Markheim

Although Congress has allowed trade promotion authority (TPA) to expire, this paradoxically presents Congress with an opportunity to consider a country-specific initiative that both the majority and minority should find attractive—a free trade agreement (FTA) with Taiwan. Among other things, a U.S.–Taiwan FTA would increase U.S. auto, rice, poultry, and livestock exports and open a significant new market for new research medicines.

At the same time, a U.S.–Taiwan FTA would signal Congress's displeasure with Beijing's trade misbehavior and demonstrate U.S. resolve in shoring up the eroding geopolitical position of a major American ally in East Asia.¹

What's Not to Like?

A Taiwan FTA has a lot to offer for everyone and promises to be more beneficial to U.S. exports than to Taiwan's exports. Automobiles, machinery, and agriculture are some of the main trade concerns on Capitol Hill, and annual U.S. exports in these sectors would surge under an FTA with Taiwan. Furthermore, Taiwan has a developed economy on par with Europe,² with labor and environmental standards that are world-class and intellectual property protections that have earned the praise of U.S. businesses.

While many Members of Congress oppose free trade agreements and are reluctant to authorize full trade promotion authority, there should be room for a broad bipartisan consensus on an FTA with Taiwan. For its part, Taiwan seems willing both to meet the

Talking Points

- Taiwan has been a top U.S. trade partner for the past three decades and is willing and able to meet the USTR's "gold standard" FTA template on trade and investment issues and address Congress's concern about labor and environmental issues.
- Congress should act now to give the Administration the authority to begin fast-track negotiations for a U.S.–Taiwan FTA.
- A U.S.–Taiwan FTA not only would prove a significant boon to American farmers, manufacturers, and service providers, but also would provide geopolitical relief to a democratic Taiwan under threat from communist China.
- China would angrily oppose a U.S.–Taiwan FTA, but there is no legal or diplomatic bar to such an agreement, and the United States should not permit China to dictate the form or substance of U.S. trade relations with Taiwan or to isolate Taiwan further in the international economic community.

This paper, in its entirety, can be found at:
www.heritage.org/Research/TradeandForeignAid/bg2061.cfm

Produced by the Asian Studies Center

Published by The Heritage Foundation
214 Massachusetts Avenue, NE
Washington, DC 20002–4999
(202) 546-4400 • heritage.org

Nothing written here is to be construed as necessarily reflecting the views of The Heritage Foundation or as an attempt to aid or hinder the passage of any bill before Congress.

high bar of the U.S. Trade Representative's "gold standard" FTA template on trade and investment issues and to address Congress's concern about labor and environmental issues. Congress should seriously consider a country-specific mandate to begin FTA negotiations with Taiwan along with instructions on how to structure the FTA.³

Taiwan stands out as an FTA partner that even free-trade skeptics can love. A U.S.–Taiwan FTA has the potential to boost American jobs in key manufacturing industries, with autos and business equipment topping the list. Taiwan has developed-country levels of trade, high labor and environmental standards, and solid health and intellectual property protections. Its market for U.S. goods still has considerable room for expansion, particularly for automobiles, agricultural products, and high-tech goods.

A Major U.S. Trading Partner

Taiwan is an important global power in its own right. It is now the world's 16th largest economy,⁴ the 10th largest trading power, and the third largest holder of foreign exchange reserves after China and Japan.⁵ It has a larger population than Australia and a larger gross domestic product than any member of the Association of Southeast Asian Nations (ASEAN). For the past two decades, Taiwan has consistently ranked

as one of America's top 10 export markets, and it already gives fairly free access to imported U.S. goods and services, which totaled \$23 billion in 2006. With its successful accession to the World Trade Organization (WTO), Taiwan has reached a level of economic and trade maturity that would enable it to open its still-restricted agricultural, automobile, manufacturing, and pharmaceutical markets to American business.

Because of the size of the Taiwan market, an FTA with Taiwan would be an important trade accomplishment and a highly significant addition to America's existing pool of FTAs.⁶ However, many of these FTAs are notable primarily for their political and security significance rather than for their economic impact.

An FTA would have a rather muted effect on Taiwan's trade posture. For example, Taiwan's information technology sector, Taiwan's biggest export sector, already enjoys relatively free access to U.S. markets under the WTO's Information Technology Agreement (ITA),⁷ which gives duty-free access to information technology products.

Nevertheless, geopolitical and security considerations have led Taipei to seek an unrestricted trade and investment regime with the United States, despite domestic political resistance.

1. Taiwan is treated legislatively as though it were designated a major non-NATO ally for arms-transfer purposes. However, Taiwan can also be considered a key ally in the sense that the United States engages in ongoing security and intelligence cooperation with Taiwan. The expressed U.S. policy toward Taiwan is "to consider any effort to determine the future of Taiwan by other than peaceful means, including by boycotts or embargoes, a threat to the peace and security of the Western Pacific area and of grave concern to the United States" and "to maintain the capacity of the United States to resist any resort to force or other forms of coercion that would jeopardize the security, or the social or economic system, of the people on Taiwan." 22 U.S. Code § 3301(b)(4) and (6).
2. Taiwan's per capita GDP of \$29,500 (ranked 36th) in purchasing power parity terms is comparable to the European Union average of \$29,900 (34th). Central Intelligence Agency, "Rank Order—GDP—Per Capita (PPP)," *The World Factbook*, updated July 19, 2007, at www.cia.gov/library/publications/the-world-factbook/rankorder/2001rank.html (August 3, 2007).
3. The Heritage Foundation first recommended exploring a U.S.–Taiwan FTA in 1990. Andrew B. Brick, "For America, Taipei Offers an Example of Chinese Democracy," *Heritage Foundation Asian Studies Backgrounder* No. 102, April 12, 1990, at www.heritage.org/Research/AsiaandthePacific/asb102.cfm.
4. Some rankings put Taiwan as the world's 16th largest national economy in purchasing power parity terms, just ahead of Australia. Central Intelligence Agency, "Rank Order." *The Economist* lists Taiwan as the world's 20th largest economy on an exchange rate basis. *The Economist, Pocket World in Figures 2007* (London: Profile Books, 2006), p. 26.
5. China Economic News Service, "Taiwan's Forex Reserves Down Slightly to \$267.5 B (NT\$8.86 T) in March," April 11, 2007.
6. U.S. FTAs in force are Israel; NAFTA (North American Free Trade Agreement: Canada and Mexico); Jordan; Chile; Singapore; Australia; Morocco; Bahrain; Oman; and CAFTA–DR (Central America Free Trade–Dominican Republic Agreement: El Salvador, Nicaragua, Honduras, Guatemala, and the Dominican Republic). FTAs with Peru, Colombia, Panama, and South Korea (KORUS FTA) are pending congressional approval. Office of the U.S. Trade Representative, "Bilateral Trade Agreements," at www.ustr.gov/Trade_Agreements/Bilateral/Section_Index.html (August 6, 2007).

Taiwan's Commitment to Free Trade

Taipei fears relentless geopolitical isolation at Beijing's hands and hopes to expand its participation in the international community to counter China's pressure. Taiwan recognizes that the strategic benefits of establishing closer ties with the United States go beyond free trade. Taiwan is literally begging the United States for an FTA. Taiwan's political leaders tell American counterparts—Republicans and Democrats—that they will agree to virtually anything the United States wants to secure a trade agreement that they quite reasonably deem vital to preserving Taiwan's economic independence from communist China.

Recent conversations with Taiwanese politicians from across the political spectrum suggest that there is a broad consensus of support in Taiwan for a truly comprehensive FTA regime encompassing autos, office equipment, agricultural products, financial and telecommunications services, pharmaceuticals, and government procurement.⁸

Taiwan's domestic labor and environmental standards are unlikely to spark debate. Taiwan adheres to all International Labor Organization (ILO) standards, despite China's continued efforts to block Taiwan's membership in the ILO. Moreover, Taiwan's intellectual property protections, legislation, enforcement, and judicial sentencing have improved dramatically over the past four years, making it one of the best environments for protecting intellectual property rights (IPR) in Asia, exceeded only by Japan, Singapore, and Hong Kong.⁹

Benefits for U.S. Auto, Manufacturing, and Pharmaceutical Sectors

Taiwan exports no automobiles, but import duties on foreign-made autos now stand at about 30

percent and will decrease to 25 percent by 2012. Under a U.S.–Taiwan FTA, American-made autos and other motor vehicles could enter Taiwan's market duty-free and without quotas, giving U.S. autos a hefty edge over Japanese, Korean, and European motorcars in this 400,000–500,000 units-per-year market. U.S. automobile, motor vehicle, and auto parts exports to Taiwan would jump about 400 percent (an additional \$629 million per year or roughly 12,000 new U.S. jobs) according to a 2004 meta-analysis by the Institute for International Economics.¹⁰ This would equal a 1 percent jump in total U.S. automobile exports.

U.S. manufacturers of other machinery and equipment (e.g., office equipment, engines, turbines, communications equipment, appliances, and an array of industrial control computers) would enjoy similar increases in exports. Taiwan would buy an additional \$868 million worth of these U.S. products annually, an increase of about 17 percent.¹¹

Although Taiwan's financial services markets have opened substantially since its WTO accession, further relaxing restrictions on foreign banking, insurance, and capital firms would be useful. The market potential for U.S. financial institutions in capital management is in the hundreds of millions of dollars annually.

American pharmaceutical companies would also gain, given Taiwan officials' openness in discussing National Health Insurance (NHI) pharmaceutical reimbursements. The current pricing structures permit Taiwan hospitals to bill the NHI for far higher reimbursements for off-patent generic drugs that are manufactured locally (a practice known as the "black hole") than for new pharmaceutical imports. U.S. exporters want the non-tariff barriers in this sector,

7. The ITA provides for WTO participants to eliminate completely duties on information technology products covered by the agreement. Developing country participants have been granted extended periods for some products. See World Trade Organization, "Information Technology Agreement," at www.wto.org/English/tratop_e/inftec_e/inftec_e.htm (August 3, 2007).
8. Interviews held on May 14–19, 2007. Taiwan's negotiators are uncomfortable discussing FTA terms outside of negotiating chambers, but their willingness to undertake comprehensive, across-the-board removal of trade barriers in all sectors including agriculture, financial services, and government procurement is well known to U.S. trade officials.
9. U.S. Trade Representative, "2006 Special 301 Report," at www.ustr.gov/assets/Document_Library/Reports_Publications/2006/2006_Special_301_Review/asset_upload_file473_9336.pdf (August 8, 2007).
10. Nicholas R. Lardy and Daniel H. Rosen, *Prospects for a U.S.–Taiwan Free Trade Agreement*, Institute for International Economics, Washington, D.C., December 2004, pp. 15–17. All other estimates of trade changes are from this volume unless otherwise specified.

especially this barrier, to be eliminated. An FTA should require equitable pricing regulation and rational market access policies.¹² American pharmaceutical companies also want less cumbersome validation data requirements for new research medicines that do not include repeating certification tests conducted by the U.S. Food and Drug Administration.

However, political pressures in managing the NHI's prescription burdens have failed to address the widespread sale of contraband pharmaceuticals by registered pharmacies. FTA negotiations would be a powerful lever to induce law enforcement action, which Taiwan urgently needs to protect Taiwanese patients from potentially harmful counterfeit generic drugs.

An FTA would also bolster Taiwan's nascent biotech industry by making Taiwan more attractive to international companies looking for research and development partnership opportunities. Taiwan could learn from Singapore's experience in luring global pharmaceutical firms.

Benefits for U.S. Farmers

Taiwan, which imported over \$2.4 billion in U.S. farm products in 2006, is America's seventh largest export market for agricultural goods. In fact, it ranks as one of the top three consumers of U.S. corn, feed grains, peaches, plums, celery, apples, cherries, broccoli, and hides.¹³ Taiwan was also one of America's few Asian trading partners to recertify U.S. beef for importation in 2005 after the "mad cow" disease scare of 2004. Taiwan now imports twice as much American beef as it did before the scare.¹⁴

Under an FTA, U.S. farm exports could grow dramatically. If Taiwan lifted all of its barriers to trade with the United States, total U.S. global exports of rice, fish, pork, beef, vegetables, fruits, and nuts

would increase by 2 percent. To enter the WTO, Taiwan lowered its duties on imported agricultural products from an average of about 20 percent to 14.5 percent. These duties will fall to 12.86 percent by 2010. Yet American rice, poultry, and pork remain under Taiwan's tariff rate quotas (TRQs), which means that imports above the quotas face tariffs of up to 300 percent. With these tariffs, U.S. agricultural products simply cannot compete against homegrown Taiwan farm goods. An FTA with Taiwan should eliminate TRQs for U.S. goods, such as American rice, pork, chicken, and beef.

If Taiwan can ever get around Beijing's obstruction and participate in the WTO's Government Procurement Agreement (GPA)¹⁵ or reach a bilateral agreement with the United States, American rice will receive preferential treatment from Taiwan's official buyers over rice from non-GPA members. This is because Taiwan's government purchases 65 percent of all quota rice on a first-come, lowest-price basis.

Under an FTA, all U.S. farm products would gain direct tariff-free and quota-free access to Taiwan's consumers, with or without WTO and GPA adherence.

U.S. negotiators should pay special attention to Taiwan's restricted rice market. This is understandably a politically sensitive issue in Taipei. Taiwan's government estimates that Taiwan's overall domestic farm production will drop \$1.5 billion under an FTA with the United States. In 2001, to cushion the blow to farmers from WTO accession, the Taipei government announced a \$330 million support budget for rice farmers. In 1999, Taipei purchased 415,000 metric tons of locally grown rice for \$275 million. Since then, domestic paddy rice production has dropped from 1.56 million tons to 1.16 million tons in 2004,¹⁶ but since 2003, U.S. rice exports to Taiwan have also declined.¹⁷ Under an

11. *Ibid.*

12. American Chamber of Commerce in Taipei, "Pharmaceutical," at www.amcham.com.tw/dl/PHARMACEUTICAL.pdf (August 6, 2007).

13. Nora Brooks, "Top 15 U.S. Export Destinations," U.S. Department of Agriculture, Economic Research Service, updated November 27, 2006, at www.ers.usda.gov/Data/FATUS/DATA/xfytop15.xls (August 3, 2007).

14. U.S. Census Bureau, "U.S. International Trade Statistics; Value of Exports, General Imports, and Imports by Country; by 3-digit Commodity Groupings; Taiwan (5830)," at <http://censtats.census.gov/sitc/sitc.shtml>.

15. China, which is blocking Taiwan's participation in the GPA, has demonstrated no intention of adhering to the GPA.

FTA, virtually all of that market would face competition with high-quality, competitively priced American rice. Across the board, American farmers stand to gain \$500 million per year in new income from exports to Taiwan once an FTA is signed.¹⁸

Intellectual Property Rights

Taiwan has made tremendous progress in intellectual property rights enforcement and sentencing over the past three years. According to the American Chamber of Commerce in Taiwan, "Overall, during the past year [2006], Taiwan has been recognized globally for improved intellectual property protection."¹⁹ This was the result of vigorous enforcement action, arrests, convictions, and heavy penalties. Taiwan's judiciary has fast-tracked IPR cases.

In 2002, the International Intellectual Property Alliance (IIPA) estimated that piracy in Taiwan cost U.S. companies \$847.9 million, mainly in the game software and motion picture industries. That figure dropped to \$376.9 million in 2005²⁰ and \$124.2 million in 2006.²¹ In 2005, Taiwan was removed from the U.S. Trade Representative's "Special 301 Priority Watch List," and while Taiwan remains on the regular watch list, the trend is rapidly moving in the right direction.

The China Factor

Regrettably, the Administration is paralyzed by a diplomatic version of "approach-avoidance conflict" with China that prevents it from even contemplating a Taiwan FTA. The clear benefits of a Taiwan FTA are eclipsed by anticipated anger from China,

which builds up stress in the foreign policy bureaucracy, paralyzing its ability to make a rational cost-benefit decision.

However, a clear look at the costs and benefits suggests that the costs would be transitory and psychological, while the benefits would be enduring and substantial. Beijing will, of course, complain. It always does. But such complaints would be groundless.

There is no legal or diplomatic bar to a U.S. trade agreement with Taiwan. China acquiesced to Washington's stated intention to continue the U.S.–Taiwan trade relationship as a condition of normalization of U.S.–China relations. In the document establishing U.S.–China diplomatic relations on January 1, 1979, the United States stated that it intended to "maintain cultural, commercial, and other unofficial relations with the people of Taiwan."²² Maintenance of America's complex trade relationship with Taiwan via continued negotiation of bilateral agreements was an implicit condition of America's normalization with China, which was made explicit when Congress passed and President Jimmy Carter signed the Taiwan Relations Act (TRA). As of December 27, 2000, the U.S. had concluded at least 98 international agreements with Taiwan within the TRA framework.²³

China will undoubtedly say that a free trade agreement that must be approved by Congress is qualitatively different from previous executive agreements. This assertion is easily rebutted by pointing out that the TRA contemplated such an agreement and that the United States has never committed not

16. Republic of China, Council of Agriculture, *Agricultural Statistics Yearbook 2004*, pp. 24–25, at http://eng.coa.gov.tw/htmlarea_file/web_articles/5846/024.pdf (August 3, 2007).

17. U.S. rice exports to Taiwan totaled \$21.7 million in 2002, \$33.9 million in 2003, \$28.0 million in 2004, \$17.4 million in 2005, and \$19.9 million in 2006. See U.S. Census Bureau, "U.S. Exports to Taiwan from 2002 to 2006," modified March 15, 2007, at www.census.gov/foreign-trade/statistics/product/enduse/exports/c5830.html (August 3, 2007).

18. Lardy and Rosen, *Prospects for a U.S.–Taiwan Free Trade Agreement*, pp. 28–29.

19. American Chamber of Commerce in Taipei, "2007 Taiwan White Paper," p. 37.

20. Charles Snyder, "Taiwan Set to Stay on Piracy List," *Taipei Times*, February 15, 2006, p. 1, at www.taipeitimes.com/News/front/archives/2006/02/15/2003293068 (August 3, 2007).

21. Press release, "The Copyright Industries in the International Intellectual Property Alliance (IIPA) Submit to USTR Their 2007 Report on Piracy in 60 Countries/Territories," International Intellectual Property Alliance, February 12, 2007, at www.iipa.com/pdf/IIPA2007301PRESSRELEASEFINALwithchart021107.pdf (August 3, 2007).

22. U.S. Department of State, Joint Communique of the United States of America and the People's Republic of China, December 16, 1978, at http://usinfo.state.gov/eap/Archive_Index/joint_communique_1979.html (August 3, 2007).

to negotiate congressionally approved trade agreements with Taiwan as a condition of normalization or anything else. Moreover, it is a diplomatic imperative that the United States not allow China to dictate either the form or substance of U.S. trade relations with Taiwan.

Furthermore, perceived congressional pressure to move ahead with a U.S.–Taiwan FTA would be useful diplomatically as another reason for Administration to proceed with an agreement.

U.S. Business Support for a Taiwan FTA

While the U.S. government might not retreat in the face of a Chinese rhetorical onslaught, few other entities are so brave. Generally, U.S. businesses are quietly supportive of a Taiwan FTA, but they cannot say so publicly. Indeed, under Chinese pressure, most U.S. businesses argue that a U.S.–Taiwan FTA must be conditioned on Taiwan's opening of air-transport links between Taiwan and China that would be classified as "domestic air service." Indeed, there are indications that the Administration has adopted the Chinese position that a U.S.–Taiwan FTA must be conditioned on Taipei's dropping all barriers to Chinese trade and transportation.²⁴ With the Washington bureaucracy seemingly amenable to Chinese pressures, few U.S. companies want to challenge China on this issue.

Many well-intentioned analysts and business people make the case that Taiwan alone is not compelling enough a partner without improved economic links with the mainland. First, while such links would make Taiwan a more attractive environment from a business perspective, a U.S.–Taiwan FTA would be about more than business

and economics. Second, even without formal economic integration with the mainland, Taiwan is at least as attractive an FTA partner as any current U.S. partners. Integration with the mainland, economic or otherwise, is something that should be left to the Taiwanese democracy to decide. Standing U.S. policy, which has been stated explicitly since the Reagan Administration, has been not to pressure democratic Taiwan to come to an accommodation with communist China.

China has threatened many commercial business firms and a number of countries, including the United States, with unspecified punishment if they seek to enhance their trade relationships with Taiwan.²⁵ In fact, despite potentially significant increases in their exports to Asia, most—if not all—major U.S. firms are afraid to support an FTA with Taiwan openly for fear of Chinese retaliation. The US–Taiwan Business Council is the only business group that openly supports the FTA without reference to economic integration with the mainland, but even it does not do so in the names of specific council members.

How U.S. FTAs Are Isolating Taiwan

Washington's trade policies have the unintended consequence of placing Taiwan at a disadvantage as it seeks to open free trade with other major American trading partners in East Asia.

In general, U.S. imports from Singapore and Australia do not compete directly with Taiwan exports in the U.S. market. However, the new U.S.–Korean FTA would place Taiwan at a disadvantage, even though it is at least as committed to free trade with the U.S. as South Korea is. Under the FTA,

23. The TRA specifies that "Whenever the President or any agency of the United States Government is authorized or required by or pursuant to the laws of the United States to enter into, perform, enforce, or have in force an agreement or transaction relative to Taiwan, such agreement or transaction shall be entered into, performed, and enforced, in the manner and to the extent directed by the President, by or through the Institute." 22 U.S. Code § 3305(b) (emphasis added). For a list of U.S.–Taiwan agreements as of December 31, 1999, see *Federal Register*, Vol. 65, No. 249 (December 27, 2000), pp. 81898–81901.

24. Karan K. Bhatia, Deputy U.S. Trade Representative, in hearing, *Asian Free Trade Agreements: Are They Good for the USA?* Committee on International Relations, U.S. House of Representatives, 109th Cong., 2nd Sess., July 20, 2006, at http://commdocs.house.gov/committees/intlrel/hfa28788.000/hfa28788_0.HTM#6 (August 13, 2007).

25. Monique Chu, "WTO Won't Guarantee Better Foreign Relations," *Taipei Times*, January 6, 2002, p. 3, at www.taipeitimes.com/news/2002/01/06/story/0000118792 (August 3, 2007). See also China Economic News Service, "Beijing Opposes Free Trade Pacts Involving Taiwan," May 31, 2002; Associated Press, "Chinese Minister Warns Countries Not to Sign Free Trade Agreements with Taiwan," June 21, 2002; and Yu Guoxin, "wo tuidong qianshu FTA, Zhonggong Zunao" (PRC obstructs FTAs urged by Taiwan), *Zhongguo Shibao* (Taipei), June 22, 2002.

nine of Taiwan's top 10 exports to the United States would compete (with an average tariff of about 5 percent) directly with nine of South Korea's top 10 exports, which would enter the U.S. duty-free.²⁶ In other words, the FTA will give South Korean products an unfair price edge over Taiwan's products (e.g., flat panel displays, televisions, and electrical appliances).

Strategic Benefits vs. Economic Benefits

An FTA with the United States would not be painless for Taiwan. It would adversely affect Taiwan's farmers, who account for 5.5 percent of the workforce, albeit while producing only 1.5 percent of GDP.²⁷ It would also affect Taiwan's banking and other services. However, Taiwan considered similar costs when it entered the WTO in 2002, and Taiwan President Chen Shui-bian has undoubtedly considered the additional social pressures that signing a U.S.–Taiwan FTA would cause and has decided that they are worth the shock.

For the United States, an FTA is a nearly perfect trade proposition. The only wild card is the Administration's anxieties about China's reaction. If Washington is seen by Asia as backing away from a traditional ally²⁸ and top trading partner in response to Beijing's vituperation, America's allies and friends among the community of Asian democracies will perceive that the United States is pulling back from the Pacific and yielding the role of preeminent Pacific power to China.

An FTA could also give Washington a diplomatic advantage. The United States can signal that China's poor performance as a responsible trading partner (e.g., lack of intellectual property protections, massive state subsidies of domestic exporters, state industrial policies that distort trade competitiveness of imports, disregard for product safety, below-cost

export dumping, and mercantilistic attempts to monopolize raw materials production overseas²⁹) has made it politically unpopular to appease China's territorial claims on Taiwan by colluding in Beijing's campaign to isolate the democratic island.

Moreover, the closer U.S.–Taiwan economic ties are seen to be in Beijing, the less likely Beijing will assume that it can take military action against Taiwan without involving America. Beijing may then see the benefits of resolving frictions with Taipei through enticements, concessions, and general goodwill rather than with threats of military force. If a U.S.–Taiwan FTA had this effect alone, it would be worth giving it priority attention in Washington.

In a broader sense, the geostrategic benefits from tying Taiwan closer to the United States argue for moving ahead quickly with an FTA in Washington.

What the U.S. Should Do

With the U.S. Trade Representative no longer occupied with negotiating FTAs under the President's now expired trade promotion authority, Congress should grant country-specific trade promotion authority to allow the USTR to negotiate an FTA with Taiwan on a fast-track basis. A successful FTA with Taiwan would include the following:

- **Rice.** Taipei is under pressure to protect Taiwan's rice farmers, but excluding any major trade sector would diminish the value of the free trade agreement.
- **The fullest possible liberalization of Taiwan's auto market.** U.S. negotiators should give top priority to removing all tariffs and quotas on U.S.-manufactured autos.
- **A remedy for the prescription pharmaceutical "black hole."** The black hole constitutes a non-tariff barrier to new U.S. pharmaceutical drugs

26. Taipei Economic and Cultural Representative Office, Washington, D.C.

27. See Central Intelligence Agency, *The World Factbook*, s.v. "Taiwan," updated July 19, 2007, at www.cia.gov/library/publications/the-world-factbook/geos/tw.html (August 3, 2007).

28. Congress made Taiwan's security a matter of U.S. law in 1979. 22 U.S. Code § 3301(b)(6).

29. Former Deputy Secretary of State Robert Zoellick noted with deep disapproval that "China is acting as if it can somehow 'lock up' energy supplies around the world," a policy he described as "mercantilistic" and "not a sensible path to achieving energy security." Robert B. Zoellick, "Whither China—From Membership to Responsibility?" remarks to National Committee on U.S.–China Relations, New York, September 21, 2005, at www.state.gov/s/d/former/zoellick/rem/53682.htm (August 3, 2007).

that induces hospitals to resist prescribing them because the reimbursement margins are low and often negative.

On the diplomatic side, the Administration should not give China a veto over U.S.–Taiwan trade relations. Specifically, the Administration and Congress should:

- **Reject any Beijing complaints that a Taiwan FTA violates the “one China policy.”** Beijing will complain that a U.S.–Taiwan FTA would be a quantum jump in relations and would therefore violate U.S. “one China” commitments. In fact, an FTA would be wholly consistent with the U.S.–China Normalization Communiqué of 1978, and the Taiwan Relations Act specifically envisions such a trade agreement via the two “instrumentalities” of bilateral relations: the American Institute in Taiwan for the American side and the Taipei Economic and Cultural Representative’s Office (and the Coordination Council for North American Affairs office in Taipei) for the Taiwan side.
- **Prevent U.S. negotiators from pressuring Taiwan for trade or transportation concessions to China.** A U.S.–Taiwan FTA need have nothing to do with China. A major purpose of a U.S.–Taiwan FTA is to prevent Taiwan from becoming an economic dependency of China’s. Taiwan is already China’s third largest source of imports.³⁰ It could hardly open itself more to China without seriously compromising its own economic security. In the past, Administration officials have used Taiwan’s unwillingness to drop trade, immigration, aviation, and investment restrictions (including Taiwan investments to develop China’s advanced computer and semiconductor technologies) against China as an excuse to avoid discussing an FTA. Congress should insist that FTA talks with Taiwan avoid obliging Taiwan to grant any trade or transportation advantages to China. This is a matter best left to Taiwan to decide.

- **Use enhanced U.S.–Taiwan trade ties to dramatize congressional displeasure with China’s trade practices.** While the Administration and Congress wrestle with China’s bad behavior on intellectual property, non-tariff barriers, product safety, and consumer safety, among other issues, a bill mandating a U.S.–Taiwan FTA would serve notice that China has lost credibility on Capitol Hill.
- **Pressure China.** Congress should recognize that pursuing an FTA with Taiwan would put meaningful and painful diplomatic and political pressure on China in a way that avoids firing the first shot in what could be a disastrous trade war.

Conclusion

Now that trade promotion authority has lapsed, a specific, congressionally mandated FTA negotiation round with Taiwan would eliminate excuses to avoid Taiwan because the USTR’s “negotiation inbox is full.”

A U.S.–Taiwan FTA not only would prove a significant boon to American automobile, agricultural, pharmaceutical, and financial services exporters, but also would give geopolitical relief to a beleaguered Asian democracy under threat from Asia’s most powerful dictatorship and signal to Beijing U.S. displeasure with China’s trade misbehavior.

Indeed, most Members of Congress could find a lot to like in an FTA with Taiwan, a country that has world-class labor and environmental standards already in place.

Additionally, the U.S. is in an ideal negotiation position with Taiwan. USTR negotiators have great leverage in a deal with Taiwan because Taiwan seeks the FTA for political as much as economic reasons.

—John J. Tkacik, Jr., is Senior Research Fellow in China, Taiwan, and Mongolia Policy in the Asian Studies Center and Daniella Markheim is Jay Van Andel Senior Trade Policy Analyst in the Center for International Trade and Economics at The Heritage Foundation.

30. Specifically, Taiwan accounts for about 10.2 percent of Chinese imports, behind Japan with almost 14 percent and South Korea at about 11.5 percent. See “Taiwan Third Largest Source of Imports into China for Jan.–Feb. Period,” Taipei Central News Agency, April 10, 2007.