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EXECUTIVE SUMMARY OF THE IMPACT ASSESSMENT

Accompanying the document

Recommendation for a Council Decision

authorising the opening of negotiations with Turkey on an Agreement on the extension of the scope of the bilateral preferential trade relationship and on the modernisation of the Customs Union

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Executive Summary Sheet

Impact assessment on a Recommendation for a Council Decision authorising the opening of negotiations with Turkey on an Agreement on the extension of the scope of the bilateral preferential trade relationship and on the modernisation of the Customs Union

A. Need for action

Why? What is the problem being addressed?

Based on a nearly 20-year old EU-Turkey Customs Union, which enhanced two-way trade, economic integration and investment flows, the EU-Turkey trade relationship has been overtaken by a more ambitious trade policy of the enlarged EU and the negotiation and conclusion of a number of deeper and more comprehensive trade agreements with key economic partners. The scope of the EU-Turkey bilateral preferential trade framework however remains limited to goods, without deeper liberalisation in agriculture. It does not cover services and public procurement neither the rules on major aspects related to an economic environment. That leads to unfulfilled trade potential and insufficiently predictable and stable legal and economic environment. In addition, certain deficiencies in the design of the Customs Union have become evident, i.e. Turkey's difficulties in negotiating preferential trade agreements with the third countries with which the EU concludes such agreements as well as in meeting its obligation on legislative alignment to EU law, and the lack of an effective dispute settlement mechanism. Largely due to these deficiencies, the two sides have been unable to find appropriate ways to solve the increasing number of trade barriers which Turkey has created over the past few years, in breach of the Customs Union rules. In view of the above shortcomings which are all inter-related, both sides reached consensus that the current BPTF was no longer sufficient to frame and foster a modern and ambitious preferential trade relationship between the EU and Turkey, and that a comprehensive approach was needed to address all of the above interlinked problems at the same time.

What is this initiative expected to achieve?

In respect of future EU-Turkey economic and trade relations, the objectives can be grouped into two categories::
1) Modernise the functioning (or design) of the customs union: (i) address the problems related to the difficulty of parallel conclusion of FTAs by the EU and Turkey; (ii) address Turkey's difficulties in complying with its obligation on legislative alignment to EU law; (iii) introduce an effective dispute settlement mechanism;
2) Extend the scope of trade preferences: (i) mutually enhance market access for trade in agriculture; (ii) improve market access for trade in services; (iii) enhance access to each other's public procurement market, (iv) agree on rules to enhance the environment for trade and investment (e.g. trade and sustainable development, energy/raw materials, sanitary-phytosanitary measures, geographical indications, SMEs, transparency, etc).

What is the value added of action at the EU level?

The main objective of policy intervention in this case is to create more favourable conditions for further increasing trade and investment between the EU and Turkey. According to Article 5(3) of the Treaty on European Union (TEU), the subsidiarity principle does not apply in areas of exclusive EU competence. The common commercial policy is listed among the areas of exclusive competence of the Union in Article 3 of the Treaty on the Functioning of the European Union (TFEU). This policy includes the negotiation of trade agreements pursuant to Article 207 TFEU.

B. Solutions

What legislative and non-legislative policy options have been considered? Is there a preferred choice or not? Why?

Three policy options were analysed. Option A ('baseline scenario') means continuing with the current framework; but this risks leading to a deterioration of the bilateral trade relationship while not achieving the objectives. The other two policy options entail a new trade agreement with Turkey. Option B entails on the one hand the modernisation of the customs union by addressing its deficiencies, and on the other hand the extension of trade preferences to new areas notably in services, agriculture and public procurement. Option C envisages on the one hand the replacement of the existing customs union with an FTA relationship for industrial goods (currently covered by the customs union), and on the other hand also the extension of trade preferences to new areas. Option B is the preferred policy option. Firstly, as the Customs Union is viewed as a stepping stone towards Turkey's EU accession, doing away with it may be perceived politically as a setback. Secondly, Option B is economically more beneficial for both sides, as it maintains the free circulation for industrial goods, while Option C entails increased trade costs to prove compliance with the rules of origin that would be reinstated under this option. Moreover, given the above political aspect, Option C may imply less commitment by the parties to trade liberalisation (to be undertaken in the new areas of trade preferences). Indeed as mentioned above, the shortcomings of the bilateral preferential trade framework are inter-linked, therefore comprehensive approach is

needed to address all of them at the same time. This policy option was endorsed already by the report of the EU-Turkey Senior Officials Working Group (of April 2015) which constituted the result of a scoping exercise.

Who supports which option?

Both the European Commission and Turkish authorities support Option B, as this is the most beneficial for both sides, in both economic and political terms. Both sides agree that Option A may be difficult to sustain in the longer term, in view of the changing global trade environment (including the several bilateral FTAs concluded and under negotiation). Businesses are in favour of a new EU-Turkey trade agreement to further enhance economic ties; for them, both Options B and C may be interesting, although in view of the different economic impacts Option B would be more beneficial. As Option B entails larger welfare gains for both sides, it would be more beneficial also for consumers.

C. Impacts of the preferred option

What are the benefits of the preferred option?

The preferred policy option – i.e. Option B – has a positive overall economic impact on both the EU and Turkey. According to the economic analysis, the EU's real GDP would increase by close to 0.01%, its economic welfare would rise by EUR 5.4 billion, and EU exports to Turkey would increase by EUR 27.1 billion. (It should be noted that the effects of services liberalisation are underestimated due to limitations in the modelling, and the effects of increased access to the public procurement market are not included as those are difficult to quantify.) Turkey's real GDP would rise by 1,44%, and its welfare by EUR 12.5 billion, while its exports to the EU would grow by EUR 5.0 billion. Both EU and Turkish consumers and businesses would benefit from this option.

Social impacts (notably wages and employment) are likely to be slightly positive in the EU and in particular in Turkey. Overall effects on economic and social human rights (adequate standard of living, right to work, social protection) as well as other rights derived from welfare gains (health, education) would be positive in Turkey.

What are the costs of the preferred option?

As a usual consequence of reduction in trade barriers, increased economic activity would result in slightly higher greenhouse gas emission (increase in Turkey by 2.1 million MT CO₂ equivalent, but only marginally in the EU, and decrease in the rest of the world, leading to a marginal increase globally) – unless Turkey mitigates this by specific measures. The EU envisages the inclusion of provisions in the agreement on principles of environmental protection in a trade and sustainable development chapter.

Trade liberalisation could lead to some transitional unemployment in a few sectors. In particular, increased market access in primary agriculture may negatively affect rural employment of small farmers in Turkey, especially in the rice and cereals sectors.

How will businesses, SMEs and micro-enterprises be affected?

Option B features relatively deep across-the-board lowering of barriers to goods and services imports in Turkey, with especially large reductions from tariff elimination in primary agriculture.

Besides, provisions that simplify customs procedures and administration, which can disproportionately impact small exporters, are very important for SMEs. In addition, provisions on bilateral cooperation to enhance SMEs' access to information would improve transparency for SMEs.

Will there be significant impacts on national budgets and administrations?

No significant impacts are expected from the new trade agreement on national budgets and administrations. (Impacts on EU budget would likely be overall positive under both Options B and C. Option B would entail closer administrative cooperation between the EU and Turkey.)

Will there be other significant impacts?

No.

D. Follow up

When will the policy be reviewed?

The new trade agreement, after its conclusion and entry into force, would be implemented and its implementation would be monitored, including by way of monitoring indicators. Regular consultations with stakeholders would ensure an effective follow up on its implementation. There would be an evaluation of the new agreement after it will have been in force for sufficient time to ensure availability of meaningful data.