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Communications

While the Internet provides remarkable potential for global wealth creation, the multilateral trade system as it exists today is woefully inadequate to address the myriad issues arising from digital trade in goods and services, according to Duane W. Layton, a partner with Mayer Brown, Washington, D.C., and Kelsey M. Rule, an associate with the firm. In this Bloomberg BNA analysis piece, Layton and Rule discuss cross border digital trade barriers, which include localization requirements, data security, and intellectual property protection. The two largest trade agreements currently under negotiation, the Trans-Pacific Partnership and Transatlantic Trade & Investment Partnership, will address digital trade issues for the first time, and they are likely to set the standard for global rules of digital trade for decades to come, the attorneys say.

Debugging Digital Trade: Challenges for the Global Trade Regime

BY DUANE W. LAYTON AND KELSEY M. RULE

The Internet has completely transformed the global economy in the last two decades, facilitating new business models that connect producers and consumers of all levels as never before. There are more than 2 billion people connected to the Internet, and nearly 200 million more are added each year. According to a study by McKinsey Global Institute, the Internet accounted for nearly 21 percent of GDP growth in developed countries over the last five years. The study also found that 75 percent of Internet impact arises from traditional industries' use of web technology.

While the Internet provides remarkable potential for global wealth creation, the multilateral trade system as it exists today is woefully inadequate to address the myriad issues arising from digital trade in goods and services. The WTO multilateral agreements, which were used as models for most regional trade agreements, were drafted in 1994—before the Internet was fully commercialized. Two decades later the global economy has gone digital, and trade negotiators need to catch up.

What is digital trade? At its most fundamental level, digital trade is the cross-border transmission of goods and services via electronic means. The universe of digi-

tal goods and services can be roughly divided into the following categories:

Digital content	<i>e.g., ebooks, streamed music and videos, news media, images</i>
Social media	<i>e.g., social and professional networking sites, online dating, user-created content platforms</i>
Search engines	<i>e.g., web search engines, database search engines</i>
Digital services	<i>e.g., software and web</i>

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Data storage

development, communication services, traditional services delivered electronically
e.g., cloud computing, hosted servers, managed servers

The two largest trade agreements currently under negotiation, the Trans-Pacific Partnership (TPP) and Transatlantic Trade & Investment Partnership (TTIP), will address digital trade issues for the first time. The enormity of the agreements combined with the novelty of digital trade rules suggest these agreements are likely to set the standard for global rules of digital trade for decades to come. These new rules will impact not only large multinational entities, but also the increasing number of small players with virtual global presence.

Localization requirements. Localization is the most direct barrier to digital trade across borders. Within the context of digital trade, localization refers to any measure that requires a domestic nexus of the supply-side of digital transactions. For example, regulations that compel companies to use local (i.e., domestic) data servers or locally sourced software and programming services are localization measures.

Several EU members, most notably Germany and France, are contemplating local server requirements for data storage services. Such measures would require cloud computing and web hosting servers to be physically located within the territory of the enacting state, thus precluding robust global competition for those digital services.

Additionally, the EU's 2007 Audiovisual Media Services Directive expanded the scope of previous local content quotas for television and radio programming to include on-demand and streaming media.

Some countries, such as Brazil, have established government procurement rules that favor local providers of digital goods and services.

The most prominent user of localization requirements is China, which has implemented such measures in a number of key industries, including banking, energy, and telecommunications. These programs aim to protect networks related to essential infrastructure; the level of importance of a particular industry to national security, social order, and economic interests corresponds to the level of localization required for its digital services.

Data privacy and Security. There are three main categories of data that may raise privacy and security concerns: payment data, personal data, and controlled data. Traditionally, personal data was comprised of so-called "census information"—name, address, telephone number, and email address. However, the universe of personal data is expanding rapidly with the proliferation of programs that capture behavioral information such as pages viewed, duration of visit, "likes," and "shares." Personal biometric data is captured by applications that track steps, calories, and even mental acuity. Presumably, the majority of this information is captured for legitimate marketing purposes. However, the potential for abuse and gross invasion of privacy

brought on by mass data collection cannot be overstated.

Data privacy is perhaps the biggest obstacle to achieving a unified approach to global trade of digital goods and services. The two biggest players in the digital economy—the U.S. and the EU—have diametrically opposing views on data privacy. The U.S. takes the position that personal information provided to a business may be used, stored, and even sold with minimal restrictions. In a recent Senate hearing on data privacy, FTC Chairwoman Ramirez explained that the agency's authority to regulate unfair or deceptive data practices only extends to holding companies accountable for the privacy policies they establish for themselves, even if those policies provide substandard protection to consumers.

The EU, on the other hand, requires that data collection and distribution activities be fully disclosed to consumers up front and subject to various limitations. Companies operating in the EU, unlike in the U.S., do not have discretion whether to establish or maintain stringent data privacy policies. To facilitate data flows, the EU has enacted a Safe Harbor provision that requires U.S. companies to certify compliance with EU data privacy regulations. However, it is not always easy to break data collection habits, as Google recently discovered when it ran afoul of the data privacy regulations of several EU members. Achieving harmonization of divergent data privacy regimes will be a major challenge in developing cross border digital trade standards.

Intellectual property Intellectual property protection has been an ongoing challenge for global trade partners since the mid-1990s. Global copyright, trademark, patent and trade secret regimes have not been harmonized. While the Trade-Related Aspects of Intellectual Property ("TRIPs") Agreement requires WTO members to provide a basic level of intellectual property protection, the lack of a unified set of intellectual property rules presents a variety of problems for digital trade.

First, software and digital content producers feel the impact of intellectual property infringement in real time. An illegal download or bootlegged file can be transmitted around the world with the click of a mouse, but unattributed content usage and unauthorized peer-to-peer (P2P) sharing is not uniformly prohibited on an international level.

Second, the lack of uniformity of intellectual property protections creates chilling uncertainty for many companies without the resources to keep abreast of multiple regulatory regimes. For example, sites that rely on user-created content (e.g., YouTube and Tumblr) may be subject to liability for intellectual property infringement in certain jurisdictions, but not others based on their user-posted content. Argentina, Brazil, Indonesia, Russia, Thailand, and Vietnam reportedly do not have adequate laws governing intermediary liability for copyright-infringing content.

Finally, many countries (including Brazil, Canada, India, Indonesia, Mexico, Russia, Thailand and Vietnam) do not have adequate notice and takedown regimes to govern the removal of infringing online content upon notification by rights holders.

The U.S. has implemented the World Intellectual Property Organization (WIPO) Copyright and Performances and Phonograms Treaties (collectively, the "In-

ternet Treaties”), and promotes the treaties as a solution to the problem of divergent online intellectual property protection regimes. The U.S. Trade Representative actively encourages U.S. trading partners to ratify and implement the treaties.

Censorship Censorship of Internet content and platforms is a frequent occurrence. Countries such as China, Iran, and Saudi Arabia engage in systematic and pervasive censorship. While these measures seem to be primarily used to block the free flow of information and maintain government control over public discourse, censorship measures also disrupt the operations of foreign digital providers that offer fully compliant services and content.

In countries that conduct broad censorship activities, foreign providers are subjected to heightened levels of blocking and filtering of Internet content. For example, foreign providers in China and Vietnam are routed through gateways that domestic providers avoid altogether. Such impediments greatly inhibit the quality and speed of delivery of foreign-sourced content. At the same time, lax intellectual property protections often allow pirated content to freely circulate in these markets.

Border measures Digital trade brings small businesses to the global marketplace on a scale that would have been unimaginable fifteen years ago. Online retail sales from small business (including many self-employed “hobbyists” through sales platforms like Etsy) have increased dramatically in recent years. It is

no coincidence that low-value or “micro” exports from the U.S. increased by 103 percent between 2005 and 2010, which is more than twice the increase for all U.S. exports.

While digital sales platforms make these transactions possible, many micro exports remain prohibitively costly to countries with low *de minimis* import tariffs. A recent study demonstrated that increasing the U.S. *de minimis* level to \$800 would increase the value of transactions handled by express delivery firms by over 8 percent for 48 different types of merchandise. Raising *de minimis* import levels for tariff applicability has been discussed within the context of the TTIP negotiations, as there is huge potential for digitally-enabled micro export across the Atlantic.

The next generation of international trade rules The time is ripe for nations to take up the issues facing global trade of digital goods and services. The ongoing TPP and TTIP negotiations represent two of the largest regional trade agreements by trade volume ever attempted, which could serve as a model for future multilateral agreements on digital trade through the WTO. The Trade Facilitation Agreement concluded in Bali last year signaled that the WTO is shaking off a decade of stagnant Doha Round talks and moving forward with a new agenda. If the U.S. and the EU can resolve their differences regarding privacy protection and draft a strong regional agreement on digital trade, they will set the standard for digital trade rules for the rest of the world.