

**Testimony Before the Committee on Ways and Means
House of Representatives**

**Hearing on “The Future of U.S. Taiwan Trade”
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Chairman Neal, Ranking Member Brady, distinguished members of the House Committee on Ways and Means, thank you for the opportunity to testify before you at this hearing on “The Future of U.S.-Taiwan Trade.”

Taiwan is the world’s 21st largest economy¹ and a beacon of democracy in Asia. Strong trade linkages are critical for Taiwan’s security, as exports account for almost 70 percent of Taiwan’s gross domestic product (GDP). Taiwan is also an important economic and security partner of the United States. Especially for high-tech and electronic sectors, Taiwan is a critical part of the global supply chain for U.S. firms, given its competitiveness in crucial sectors such as semiconductors. These linkages have important spillover effects for U.S. defense and security.

Finding ways to strengthen trade and investment linkages between the United States and Taiwan is therefore critical to America’s economic and national security in the Indo-Pacific region. My testimony today will focus on elements that the United States should bear in mind as it seeks to do so. After a brief review of Taiwan’s economic status and U.S.-Taiwan trade, I will discuss opportunities and challenges facing the United States overall in deepening trade ties with Taiwan and with respect to specific sectors and issue areas.

Background Facts on Taiwan’s Economy and Trade Ties

Taiwan’s economy has two faces. Taiwan is a global leader in leading-edge semiconductors, and Taiwanese firms are important players in the information and communications technology (ICT) sectors. In 2019, the World Economic Forum ranked Taiwan as the 12th most competitive economy in the world and 4th in terms of innovation capacity.² Another set of competitiveness rankings, compiled by the IMD Business School in Switzerland, placed Taiwan as 7th in the world, ahead of the United States.³

However, Taiwan’s economy has shown signs of structural weakness. Taiwan has not succeeded in diversifying its economy and faces declining economic competitiveness outside of the high-tech sectors. As is true of other advanced economies, Taiwan is grappling with problems of wage stagnation, an aging population, inequality, and talent shortages.

¹ Taiwan ranks 17th if the European Union is counted as a single economy.

² World Economic Forum, *Global Competitiveness Report 2019* (2019), pp. 538-541.

³ IMD World Competitiveness Center, *IMD World Competitiveness Booklet 2022* (2022), p. 33.

Taiwan loosened restrictions on contacts with mainland China in the 1990s, leading to a large outflow of Taiwanese capital, manufacturing, and talent to the People's Republic of China (PRC). Between 1991 and May 2021, Taiwan approved 44,577 cases of outbound foreign investment to the PRC, totaling \$193.5 billion.⁴ Between 2000 and 2010, cross-Straits trade grew ten-fold.⁵ However, closer economic ties have not contributed to a calming of cross-Straits tensions. Instead, they have simply led to an overdependence of the Taiwanese economy on the PRC and contributed to Taiwan's growing economic and security vulnerability.

Taiwan's government has sought to shift its trade and investment relationship away from the PRC toward Southeast Asia. However, despite the incentives provided, these efforts have not succeeded. Taiwanese firms continue to find the PRC to be an attractive location for manufacturing and sourcing of inputs due to its talent pool, developed infrastructure, supply chain ecosystem, macroeconomic stability, cultural and linguistic proximity, etc. In 2021, over 42% of Taiwan's exports went to the PRC, including Hong Kong.⁶ This was larger than the combined volume to the U.S., Japan, Australia, Canada, the United Kingdom (UK), and the European Union (EU).⁷ Similarly, in 2021, the PRC, including Hong Kong, accounted for 22% of Taiwan's imports, more than double those of the United States.⁸

Taiwan has been a member of the World Trade Organization (WTO) since 2002. However, due to its precarious diplomatic status, it has few formal preferential trade agreements with its trading partners, either in the form of a free trade agreement (FTA) or a regional trade agreement (RTA). Most notably, Taiwan has no such agreements with any of the world's top 30 economies, except for the Cross-Strait Economic Framework Agreement (ECFA) with the PRC.⁹ This stands in stark contrast with other WTO members of similar economic size and importance. Taiwan has FTAs in force only with several Central American countries (El Salvador, Guatemala, Honduras, Nicaragua, and Panama). In Asia, Taiwan has concluded Economic Cooperation Agreements (ECAs) only with New Zealand and Singapore. Despite the rapid proliferation of FTAs and RTAs in the past decade, Taiwan has not signed any other preferential trade agreements with an advanced economy since 2013.¹⁰

In light of Taiwan's expressed desire to reduce to economic interdependence with the PRC and to strengthen its economic relationship with like-minded democracies, Taiwan views concrete steps by the United States to deepen economic relations as an important demonstration of U.S. engagement and commitment to supporting Taiwan. The creation of the U.S.-Taiwan Economic

⁴ Government Portal of the Republic of China – Taiwan, Cross-Straits Relation, https://www.taiwan.gov.tw/content_6.php (last accessed Sept. 12, 2022).

⁵ Ibid.

⁶ Analysis based on statistics provided by Taiwan's CPT Single Window, Statistics Database Query, <https://portal.sw.nat.gov.tw/APGA/GA35E> (last accessed Sept. 12, 2022).

⁷ Ibid.

⁸ Ibid.

⁹ Note that the follow-up agreements to the ECFA have yet to be concluded and were the source of much domestic political tension in Taiwan under the prior government; therefore, the ECFA has yet to be formally notified to the WTO Committee on RTAs.

¹⁰ Taiwan has signed ECAs with a few other smaller economies (Eswatini, the Marshall Islands, and Paraguay).

Prosperity Partnership dialogue in 2020 and the resumption of regular talks held under the 1994 Trade and Investment Framework Agreement (TIFA) have been important signals to this effect.

Strengthening U.S.-Taiwan Trade Ties Will Have Some Geopolitical Ripple Effects

Deepening U.S. economic engagement with Taiwan provides an important signal to like-minded allies, including Australia, the EU, Japan, and the UK. They will find security in moving together with the United States, given the negative reaction that such moves may engender from the PRC.

However, there are also countries in the Indo-Pacific region that are averse to inclusion of Taiwan in any regional or multi-party framework absent the PRC. This includes the Indo-Pacific Economic Framework. Stronger U.S. engagement is unlikely to have an impact on this second group of countries, which includes several countries in Southeast Asia for which the PRC is their most important economic trading partner and which do not wish to be seen as too closely aligned to either the U.S. or PRC.

In September 2021, Taiwan applied to join the Comprehensive and Progressive Trans-Pacific Partnership (CPTPP); that application is under review. It is unlikely that the CPTPP Secretariat will choose to proceed on Taiwan's accession on a timeline that is significantly faster than that of the PRC, which has also applied to join the CPTPP. Consequently, it is highly unlikely that Taiwan will be invited to join the CPTPP anytime soon, if ever.

Therefore, for the foreseeable future, deepening economic engagement with Taiwan is likely to take the form of bilateral or sectoral arrangements. Besides the U.S., the EU has also taken steps to further its economic engagement, including through the recent EU-Taiwan Trade and Investment Dialogue in June 2022. Further U.S. engagement may well embolden a few others to take such steps. However, this is likely to be limited to like-minded democratic allies that have already sided squarely with the U.S.

Boosting U.S. Exports to Taiwan Requires a “Market Access-Plus” Strategy

In 2021, Taiwan was the United States' 10th largest export market, if one considers the EU as a single trading partner. Overall U.S. exports of goods totaled \$36.9 billion, with agricultural goods totaling \$3.9 billion. Other key categories of U.S. goods exports include machinery (including electrical machinery), mineral fuels, and optimal and medical equipment. Because of the impact of the COVID-19 pandemic, year-on-year comparisons are not especially valuable. However, even absent any trade agreement, U.S. exports to Taiwan have grown steadily over the past decade.

An analysis of Taiwan's applied tariff rates, for trading partners with most-favored-nation (MFN) status, highlights two important facts:

First, opportunities for greater market access exist, particularly for U.S. agricultural exports. The average MFN applied tariff rate for agricultural products was 15.06% in 2021, as compared to

4.14% for industrial products.¹¹ At the HS-2 level, the highest MFN applied tariff rates are the categories encompassing agricultural products, including live animals, vegetable products, fats & oils, and prepared foods.¹²

Second, tariff-related market access concessions obtained through further negotiations are likely to benefit only a select number of industries, rather than generate across-the-board benefits for U.S. exporters broadly. Stated differently, for a number of key U.S. export sectors, the most important trade barriers to resolve through negotiations are outside of the traditional market access domain – not the lowering of tariffs.

In preparing this testimony, I analyzed Taiwan’s MFN applied tariff rates for the top 250 U.S. worldwide exports at the HS-6 level.¹³ Slightly less than half of the top U.S. export products face no tariffs in Taiwan whatsoever (i.e., the MFN applied tariff rate is zero). An additional one-sixth of these products are subject to a MFN applied tariff rate of less than 3%. Only approximately one-fifth of the most competitive U.S. export products face a MFN applied tariff rate greater than 5% in Taiwan today.

Besides agriculture, the other major U.S. export sector that is impacted by existing high tariffs in Taiwan today is the automotive sector and related parts of the automotive supply chain. However, this sector is complicated, as a number of other factors such as consumer preferences, shipping costs, standards (particularly with regards to automotive safety), dealerships, etc., all play in role in impacting local demand for U.S. exports. In particular, given the structural similarities, Congress may wish to undertake a deeper analysis of the continued difficulties facing the U.S. automotive sector in South Korea over the past decade since the U.S.-Korea Free Trade Agreement went into effect, in order to understand better what is needed with regards to further generating opportunities in Taiwan.

Addressing Regulatory and Other Trade Barriers Is Absolutely Critical

Rather than focusing simply a traditional market access strategy, a smarter and more impactful way to move forward on deepening trade relations with Taiwan requires focusing in tandem on other trade barriers, particularly in the regulatory space. This is the essence of what I deem the “plus” component of the strategy. Below I highlight a number of issues that should be addressed in trade negotiations.

Sanitary and Phytosanitary Standards

¹¹ Office of the United States Trade Representative, 2022 *National Trade Estimate Report on Foreign Trade Barriers* (2022), p. 467.

¹² World Trade Organization, Trade Policy Review of the Separate Customs Territory of Taiwan, Penghu, Kinmen, and Matsu, WT/TPR/S/377/rev.1 (March 6, 2019), p. 48.

¹³ This analysis was based on information provided by the WTO Tariff Download Facility and the UN Comtrade database.

Even though Taiwan has relaxed some of its restrictions on U.S. beef and pork products, as the December 2021 referendum demonstrated, public sentiment remains charged. The negative attention generated has been detrimental to U.S. exporters. In addition, Taiwan has not yet aligned with the maximum residue levels (MRLs) allowed under Codex Alimentarius for certain products (e.g., offal) and continues to restrict importation for certain bovine blood products. Steps should be taken to lower these barriers and to ensure that recent gains cannot be rolled back by a future government without cost.

Overall, the two sides should explore efforts to better align cooperation between their regulatory authorities and align standards related to MRLs in a variety of agricultural areas, so as to lower the trade tensions that have consistently arisen from this area.

Intellectual Property (IP)

Taiwan and the U.S. have taken steps in recent years with regards to strengthening Taiwan's IP regulations for protection and enforcement. Nevertheless, long-standing points of contention remain, particularly with respect to digital infringement and counterfeit products (e.g., drugs). Most critically, given the importance of the innovation economy to both sides, steps should be taken to further strengthen cooperation with respect to theft of high-tech trade secrets. Both sides need to ensure that stronger deterrence exists to prevent a repeat of the theft of U.S. trade secrets by employees of Taiwanese companies to further the development of high-tech sectors, such as semiconductors, in mainland China. One immediate step that could be taken by Taiwan is to further amend its National Security Act to enhance criminal penalties for economic espionage.

Services Barriers

Although Taiwan is a net importer of services, barriers remain that negatively impact U.S. service providers. Roughly one-quarter of Taiwan's services sub-sectors are not covered by its commitments under the General Agreement on Trade in Services (GATS), and therefore, opportunities exist for further liberalization.¹⁴ U.S. firms have expressed long-standing concerns over restrictions that exist in sectors such as financial services, telecommunications, and some professional services (e.g., legal services, accounting, etc.). Given the importance of the services sector for employment as well as for the emerging internet-of-Things, steps taken to further integrate U.S. and Taiwan services sectors would serve both sides favorably.

Currency Manipulation

Intervention by Taiwan's central bank in its currency markets to weaken the value of the New Taiwan Dollar has garnered repeat concern by the U.S. Treasury. Strengthened rules to enforce against currency manipulation is important, in order to ensure that U.S. workers and firms are able

¹⁴ WTO Trade Policy Review, *supra* note 12, p. 121.

to compete fairly. Because of the impact of currency movements on trade, such discussions need to occur in parallel with trade discussions, rather than left on its own separate track.

Strengthened Trade Integration Should Be Viewed as a Component of a Multi-Prong Integrated Strategy to Deepen Economic Ties Across-the-Board

Efforts to deepen economic ties with Taiwan through trade must be integrated with other instruments of economic statecraft. As this hearing is focused on trade, I will simply list some of these other components:

- Investment screening
- Restrictions / government approval for outflows of critical technologies
- Supply chain resiliency for key high-tech sectors
- Joint standards development for emerging technologies
- Joint infrastructure projects, including provision of services, in third countries
- Research & development for next-generation technologies for critical infrastructure and dual-use goods

Discussions to strengthen trade ties must take place in parallel with efforts to strengthen ties on these other key elements, particularly with respect to semiconductors and other key supply chains that flow through Taiwan.

Tight Rules of Origin Are Absolutely Required

Given Taiwan's continued economic interdependence on the PRC, tight rules of origin (ROOs) are an absolute must to ensure that these do not serve as an unintended backdoor for PRC entities to enjoy its benefits. Any new trade arrangements with Taiwan that liberalizes goods trade should include ROOs that well exceed that found in any other U.S. trade agreement with other trading partners in the Indo-Pacific region. While the ROOs in the U.S.-Canada-Mexico Agreement (USMCA) may offer a starting point for consideration, the two sides may also wish to consider delineating a list of inputs that, if sourced from non-market economies, would bar a product from eligibility. Such a list should be subject to regular review and updating.

In addition, given Taiwan's ECFA with the PRC and the possibility that this framework agreement may lead to further concessions by future governments on both sides of the Taiwan Straits, any new trade arrangements with Taiwan should include a provision similar to Article 32.10 of the USMCA that allows the United States to scale back or terminate its commitments unilaterally, if it views further liberalization under ECFA as detrimental to U.S. national interests.

Conclusion

Taiwan is a key U.S. strategic and economic partner. Deepening trade ties between the United States and Taiwan is vital on many different fronts. Such efforts ought to move beyond traditional

forms of trade negotiations, which have concentrated on market access, and instead focus on a broader approach examining the lowering of regulatory barriers and strengthened coordination on trade as well as other elements of economic statecraft. As a vibrant democracy with a commitment to liberal values, deepened bilateral trade ties with Taiwan can present a template for further global cooperation on supply chain resiliency, environmental / climate change resiliency, and development of next-generation technologies. Such efforts must remain mindful of the difficulties posed by Taiwan's past, including its continued economic ties to the PRC.