

IRAN-TURKEY PREFERENTIAL TRADE AGREEMENT

Gist of the news

According to *Tehrantimes.com* on December 31, 2014:

TEHRAN – The preferential trade agreement, which was signed last year between Iran and Turkey, goes into force on January 1, 2015....

In January 2014, Iran and Turkey signed the agreement with the goal of boosting bilateral trade. The agreement was signed during Turkish Prime Minister Recep Tayyip Erdogan's visit to Iran.

According to the agreement, 125 items of Iranian goods and 140 items of Turkish goods will be traded based on preferential tariffs as of January 1, 2015.

Irna.ir also reported on January 2, 2015 that:

The Iran-turkey preferential trade agreement, which was earlier approved by the Iranian government was confirmed by the Turkish Parliament and put in effect bilaterally as of Thursday, January 1, 2015.

According to this agreement, the tariffs of 125 items of Iranian goods are decreased in Turkey's favor and those of 140 Turkish goods in favor of Iran.

Signing preferential trade agreement with different countries is one of the measures that can pave the path for Iran to join the World Trade Organization (WTO).

Iran has so far signed nine such agreements with different countries.

In this News & Analysis report we analyze and discuss the following issues:

- 1) What is the significance of Preferential Trade Arrangements (PTAs) in the global context?
- 2) What are the economic and legal impacts of the PTA signed with Turkey?
- 3) Is Iran-Turkey PTA beneficial for Iran or not?
- 4) How would it be possible to manage a PTA to maximize its benefits and minimize its negative repercussions?

Preferential trade arrangements in the global context

According to T.N. Srinivasan in his article titled Preferential Trade Agreements with Special Reference to Asia:

Preferential Trade Agreements (PTAs) are agreements among a set of countries involving preferential treatment of bilateral trade between any two parties to the agreement relative to their trade with the rest of the world. Preferences, however, need not extend to all trade between the two, and the coverage could depend on the type of PTAs.

The definition provided by the *Businessdictionary.com* is more detailed:

Preferential trade agreement. A trade pact between countries that reduces tariffs for certain products to the countries who sign the agreement. While the tariffs are not necessarily eliminated, they are lower than countries not party to the agreement.

To understand the above definition, it is indispensable to understand the exact meaning of two terms: tariff, and reduction of tariffs.

Tariff – According to *investmentanswers.com*: “A tariff is a tax on imports or exports. Money collected under a tariff is called a duty or customs duty. Tariffs are used by governments to generate revenue or to protect domestic industries from competition.”

Tariff reduction – The website of *WTO.org* explains that: “Traditionally, the tariff reductions that resulted from trade negotiations came from bilateral product-by-product bargaining, or they were based on formulas that applied over a broad range of products, or combinations of the two.”

Economic and legal impacts of the PTA signed with Turkey

According to *yarnsandfibres.com* on January 3, 2015, the PTA signed between Iran and Turkey will result in the following concrete consequences:

A. Tariff-related consequences

- 1) The customs taxes imposed on 265 products will be lowered by a great degree with some of the customs taxes imposed on certain products to almost zero percent.
- 2) 140 products from Turkey and 125 products from Iran customs taxes have been decreased and are currently working for more. Iran and Turkey will also strive to increase the number of product types from 265 to 290, even to 300 for which low or zero customs taxes are applied.

B. Structural consequences

- 3) Two technical committees will be established, consisting of experts from both countries with the committees set to hold monthly meetings in order to supervise the progress of the agreement and to offer solutions for any possible problems that may occur during the implementation thereof.

4) The technical committees are scheduled to hold their first meeting in January and a large Turkish committee will be organizing a business forum at the beginning of February.

5) Turkey is currently in the process of establishing two institutions in Iran. First of all, Turkey's under-secretariat of Commerce will be reinforced, evolving into a center with eight to 10 employees. Further, Turkey will establish a center that hosts various Turkish firms and their offices that will receive support from their ministry. As a result, companies will get the opportunity to establish branches in Iran will be able to come as a part of group and engage in activities.

The main benefit of the PTA for both sides, without any doubt, is the structural changes that will take place in the coming months. Turkish companies and firms will have a more efficient and more beneficial presence in Iran. They will certainly need more administrative and legal support in Iran too. Both the public and the private sector of the Iranian economy shall be involved in providing this support. Iranian legal firms will be a main player in assisting and helping the Turkish companies and firms. A new market is opening for these firms in the near future.

Is Iran-Turkey PTA beneficial for Iran or not?

Two main arguments in favor of signing the PTA with Turkey are raised. First, it will open the way for Iranian products to enter the EU market, and secondly, it will pave the way for Iran to join the WTO.

Impact on trading with the EU – According to Article 3(2) of the Decision No 1/95 of the EC-Turkey Association Council of 22 (96/142/EC):

Products from third countries shall be considered to be in **free circulation** in the Community or in Turkey if the import formalities have been complied with and any customs duties or charges having equivalent effect which are payable have been levied in the Community or in Turkey, and if they have not benefited from a total or partial reimbursement of such duties or charges.

It must also be noted that under the Preamble of the Council Regulation (EC) No 519/94 of 7 March 1994:

Whereas, in the case of other products, the Commission must examine import terms and conditions, import trends, the various aspects of the economic and commercial situation, and the measures, if any, to be taken;

Whereas for those products, it may become apparent that there should be Community surveillance over certain of these imports;

Whereas it, is for the Commission and the Council to adopt the safeguard measures called for by the interests of the Community with due regard for existing international obligations....

Two terms used in the above text call for attention: “Community surveillance” and “existing international obligations”. The international sanctions imposed on Iran result in making Iranian products subject to the EU surveillance under the existing international obligations of its member countries. We have analyzed some of these sanctions in our previous News & Analysis reports but they need to be reconsidered in the light of this new PTA signed with Turkey.

Impact on joining the WTO – Signing preferential trade agreements with different countries can pave the way for Iran to join the World Trade Organization (WTO), according to Financial Tribune on January 6, 2015. The question is that whether this claim is true or not? The answer is not always on the positive side. *Europesworld.org* in its report on June 15, 2014 elaborates upon this issue in a sophisticated way:

Is it threatening to split the world economy into sets of trade blocs that exclude developing countries that constitute the majority of WTO members? My own answer is no. While there is clearly some disconnect between the PTAs and the WTO-based trading regime, the TTP and TTIP will not doom the WTO.

The same analysis then continues to argue that all depends on management of the WTO rules and regulations and their interactions with the PTAs:

There is much more that can be done through the WTO to pursue cooperation in areas that currently are not subject to multilateral disciplines. Dealing with regulatory trade barriers is complex, with much to be learned from the way different PTAs have reduced regulatory trade costs. We need to identify areas where multilateralization of a PTA-based initiative is appropriate (as was done for trade facilitation, with agreement on a common set of good practices that were largely developed by the World Customs Organization), and to use the avenues where the WTO offers subsets and its members can cooperate on new policy areas.

Management of PTAs

According to the WTO Staff Working Paper ERSD-2011-10 dated June 16, 2011, PTAs are complicated texts composed of diverse elements. As explained above, the expected consequences of the PTA signed between Turkey and Iran depend heavily on the ways and means of understanding, analyzing and managing these elements:

1) *Objects of PTAs* - Main objects of the PTAs, as explained at page 6 of the Paper are:

“To lock-in domestic reforms, strengthen their position in multilateral negotiations, pursue import-substitution policies at the regional level, address security concerns, or sign PTAs as a reaction to other agreements”.

In the current circumstances, one of the main objectives of Iran is to strengthen its position in multilateral negotiations.

2) *Market access* – Iran is subject to heavy sanctions that have curbed its access to international markets. To establish such access, Iran needs to take the following elements explained in pages 14 and 15 of the Paper into consideration:

First, tariff schedules, degree of concessions, tariff peaks, exemptions, speed and depth; whether states work with the Harmonized System (HS) or a national system, which particular HS references are used (as these have been regularly updated; HS 1988/92 - very similar and therefore usually combined, HS 1996, HS 2002 and HS 2007) and at which digit level concessions are listed.

Second, the coding differentiates whether the parties agree on a uniform (basket) approach or whether there are areas that have a specific treatment (e.g., agriculture, fishery products, textiles, etc).

Under the PTA, 140 products from Turkey and 125 products from Iran customs taxes have been decreased. To understand the real impacts of the PTA, it is necessary to classify the products on both sides of the border to find out which areas of the economy they fall into. The available information that needs to be verified shows that on the Turkish side, these products fall into at least eight categories: cloths, electric appliances, hygiene products, steel products, car pieces, furniture, house appliances, and plastic products. On the Iranian side, the categories include fruit, vegetable, food products, etc. It is open to question whether the parties could strike a reasonable balance in including these products in their lists of preferential treatment or not.

3) *Public procurement* – One of the main questions that can be raised is that whether this PTA has any influence on the public procurement process on both sides of the Iran-Turkey border or not. In other words, it would be interesting to know whether the PTA is also an agreement on regulation of procurement policies including a national treatment clause, a transparency clause, and a reference to the GATT/WTO rules on public procurement. The last question is that whether the scope of the procurement provisions (if any) in terms of entities (government, sub-national governments, state-owned enterprises) and type of purchase (goods and/or services) is covered by the PTA or not. As discussed in page 23 of the above Paper, these are major issues of concern for the private firms and companies that are affected by public procurement activities, both in Iran and in Turkey.

4) *Dispute settlement* – In every trade arrangement, there must be some space for future dispute settlement mechanisms. The Paper also advises to take the following elements into account at the time of including means and ways of dispute settlement in a PTA:

Existence of provisions, degree of delegation, choice of dispute settlement forum, implementation (bindingness and sanctions), and exemptions... the extent to which parties allow delegation to occur (consultation, mediation, arbitration, creation of a standing body, or use of external dispute settlement forms). As to the choice of forum, ... parties can choose from different dispute settlement mechanisms and what rules apply (in particular restrictions to forum choice).

Conclusion

Preferential trade agreements are one of the main vehicles that may help a country to come of its isolated position and enter into reasonable and productive relationship with its neighbors and trade partners. Turkey is one of the major regional economic forces whose influence in the region has increased substantially in recent years. Entering into a PTA with Turkey is a major step ahead that needs to be followed by other positive actions such as real privatization of the Iranian economy, opening the Iranian market towards foreign companies and firms, removing all trade barriers that stop the private sector of Iran from increasing its presence inside and outside Iran, etc. The first step for moving towards meeting all of these objectives is to increase the level of information-sharing about the commercial and legal matters. This action, in its turn, paves the way for analyzing, understanding and helping to understand the best possible options open to the Iranian public and private sector. After that, all will depend on a firm intention and an informed decision to move towards progress and development.

All rights reserved for International Law Office Dr. Behrooz Akhlaghi & Associates ("ILO") and Mr. Farhad Emam (the Co-Writers). No part of this News & Analysis may be reproduced or transmitted, in any form or by any means, without written permission of the Co-Writers to be obtained from and through the ILO.