
4 Recent developments in trade policy

Australia has traditionally reduced its barriers to international trade mainly through domestic industry assistance reform initiatives, subsequently reinforced by participation in multilateral trade agreements under the GATT and the WTO. The latest round of multilateral trade negotiations (the Doha round) has been underway for over six years, but progress has been limited. This reflects a number of influences, the most fundamental being the political and policy-making environments within WTO member countries. In part reflecting the difficulties of achieving improved access for Australian exports through multilateral negotiations, Australia has recently negotiated bilateral trade agreements with several countries, most notably the United States of America, and more are in prospect. This chapter reports on these and other developments in Australia's international trade policy.

4.1 Impasse in multilateral trade negotiations

For more than 50 years, the World Trade Organization (WTO) and its predecessor, the General Agreement on Tariffs and Trade (GATT), have provided a stable rules-based system for international trade (box 4.1). They have also provided a forum for governments to negotiate agreements to liberalise trade. Successive rounds of multilateral trade negotiations have facilitated substantial reductions in many trade barriers and underpinned the strong expansion of international trade and growth in living standards (PC 2000b, 2006a).

Despite eight rounds of multilateral trade negotiations, many of the world's major economies continue to retain high trade barriers in areas such as textiles, clothing, services and agriculture — the latter two being largely excluded from GATT deals prior to the Uruguay Round.

Progress in the Doha negotiations has stalled

The Doha round of WTO trade negotiations was launched at the Fourth WTO Ministerial Conference, held in Doha in November 2001, with WTO member governments agreeing to negotiate on a broader and more complex range of issues than in previous GATT rounds (JSFADT 2003) (table 4.1). For example, the member governments agreed to negotiations covering intellectual property and

public health, phasing out agricultural export subsidies, e-commerce, environment and the so-called ‘Singapore’ issues — including investment rules, competition policy, transparency in government procurement and trade facilitation (WTO 2001). However, given the broadened scope of the agenda and uncertainties surrounding some of the language in the declaration, the nature of the final outcome, including which elements would be included, was not established at the outset of the negotiating round (PC 2001a).

Member governments also made an ambitious undertaking to complete the wide ranging and complex agenda by January 2005; that is, some four years less than was required to complete the Uruguay round (WTO 2001, 2005).

Box 4.1 The WTO: a global, rules-based trading system

The WTO provides a framework of rules for international trade. This ‘multilateral’ framework was established in 1947 with the signing by 23 countries of the GATT. Currently, there are 150 members, with Vietnam joining in January 2007. Almost 30 more countries are negotiating membership.

The key trade rules

WTO provisions require members to apply their trade rules in a transparent and non-discriminatory manner. The key elements of the system are:

- the *most-favoured-nation* rule, which bars a member country from discriminating between ‘like’ products of other members or from favouring non-WTO members over members (except, for example, within the ambit of free trade agreements).
- the *national treatment* rule, which (with some exceptions) prevents foreign products, having satisfied quarantine and customs requirements, from being treated less favourably than domestically produced goods.
- rules to discipline protective measures (eg. tariffs, subsidies and other non-tariff barriers) and to discipline trade-distorting subsidies at the export level.

Consensual decision making

Agreements are negotiated through consensus, limiting the extent to which large trading nations can exploit their economic power and, in turn, providing opportunities and legal protections for small- and medium-sized trading nations, such as Australia.

Dispute resolution

Where a trade dispute occurs, WTO members are committed *not* to take unilateral action against perceived violations of their rights. If conciliation is unsuccessful, the parties in dispute must instead argue their case before an independent panel, with appeals to a separate body possible. The outcome is then confirmed by the WTO Dispute Settlement Body, constituted by all the member governments.

Sources: WTO (2005, 2007).

Table 4.1 Coverage of multilateral trade rounds

Year	Place/Round name	Subjects covered ^a	No of countries
1947	Geneva	Tariffs	23
1949	Annecey	Tariffs	13
1951	Torquay	Tariffs	38
1956	Geneva	Tariffs	26
1960–61	Dillon Round	Tariffs	26
1964–67	Kennedy Round	Tariffs & anti-dumping measures	62
1973–79	Tokyo Round	Tariffs and non-tariff measures, ‘framework agreements’	102
1986–94	Uruguay Round	Tariffs and non-tariff measures (for services as well as agriculture and non-agricultural products), anti-dumping measures, services, intellectual property, dispute settlement, textiles, agriculture, creation of WTO	123
2001–	Doha Round	Tariff and non-tariff measures (for services as well as agriculture and non-agricultural products), intellectual property, investment rules, competition policy, transparency in government procurement, trade facilitation, anti-dumping, regional trade agreements, dispute settlement understanding, environment, e-commerce, small economies, debt & finance, technology transfer, capacity building, least-developed countries, special & different treatment	150

^a Not all subjects covered are necessarily included in the final agreement.

Sources: WTO (2001, 2005, 2007).

While there has been some progress in the Doha Round, member governments have failed to come to agreement on key issues. In earlier editions of *Trade & Assistance Review*, the Commission reported that:

- At the Fifth WTO Ministerial Conference, held in Cancún in September 2003, members were unable to agree on the scope and pace of reform — particularly in relation to agriculture and the Singapore issues. Underlying this disagreement was a concern among developing countries that their interests were not being given sufficient weight. The meeting ended in deadlock (PC 2003).
- In July 2004, the WTO General Council meeting in Geneva removed some of the stumbling blocks of Cancún by limiting the scope of the negotiations (the Singapore issues open to negotiation were reduced to just one: trade facilitation) in what is known as the ‘framework package’ (PC 2004a).
- The Sixth WTO Ministerial Conference, convened in Hong Kong in December 2005, could not resolve a number of the more difficult agricultural reform issues, such as the size of tariff reductions on agricultural goods (PC 2006a).

The December 2005 Hong Kong Ministerial Conference set a number of new timing objectives for progressing the negotiations. However, despite intensive

negotiations over the seven months to July 2006, no agreement was reached on agriculture and non-agricultural tariff reductions, and agricultural subsidy reductions. When a meeting of ministers from six key trading nations — the G6 (US, EU, Japan, Australia, India and Brazil) — came to an impasse on the question of, how much to cut farm subsidies and agricultural tariffs on 24 July 2006, the negotiations were suspended.

As reported by the ICTSD (2006), unblocking the negotiations would require parallel progress on a ‘triangle’ of issues, two sides of which relate to agricultural trade liberalisation:

- the EU would have to agree to increased agricultural market access through greater tariff cuts in agricultural products;
- the US would have to agree to deeper cuts to its domestic farm support; and
- developing countries, such as Brazil and India, would have to agree to lower tariffs on non-agricultural products.

Trade negotiations recommenced informally in November 2006 after signs that member countries’ requests to resume negotiations were ‘widespread and genuine’ (WTO 2006). After two months of informal meetings, including discussions by trade ministers from 30 WTO members at the World Economic Forum in January 2007, across-the-board negotiations formally recommenced in February 2007.

At this stage, however, there is still no agreement on the areas of difference that caused the suspension in negotiations in July 2006.

Why have multilateral trade negotiations become so difficult?

Protracted differences among negotiating parties and an apparent lack of progress is not an unusual occurrence for multilateral trade negotiations. For example, the Uruguay Round, which commenced in 1986, took almost eight years to complete, and still did not attain its objectives in a number of areas (Young 1994).

One reason suggested for the apparent difficulties and slowness in reaching agreement is the strategic behaviour of member countries, who typically seek to conceal the ‘concessions’ they are willing to make until the final stages of multilateral trade negotiations. The presence of such strategic behaviour can also make it difficult to judge the real gap that exists between different members’ negotiating positions during the course of a negotiating round.

Nevertheless, delays in achieving agreement in multilateral trade negotiations and difficulties in assessing actual progress cannot be solely attributed to strategic behaviour of member countries. After five years of negotiations, a number of other factors have been canvassed to explain the slow progress of the Doha Round.

Increased complexity of negotiations

As multilateral trade agreements generally require a consensus among members, it is widely acknowledged that the substantial increase in membership of the WTO in recent years has increased the difficulty of achieving agreement on further liberalisation (JSFADT 2003, PC 2004a). The first GATT agreement, for example, comprised just 23 countries, most having similar levels of economic development, in contrast to the 150 members that are currently participating in the Doha Round (WTO 2005, 2007).

This much larger membership has been associated with a greater diversity of objectives and interests of member countries, and a greater role played by the newer member countries in the negotiating process. For example, the G20 is a group of developing countries, led by Brazil and India, seeking to achieve greater liberalisation of agriculture by *developed* countries (Gifford 2006). However, the G20 is divided about certain reform issues in relation to developing country agricultural products. Some G20 members (including Brazil) have a strong interest in achieving market access into other developing countries, while other members of this group (such as India and Indonesia) are also members of the G33, that has differing objectives and priorities.

Added to this is the progressive expansion of negotiating areas. Tariffs on manufactures were the ‘bread and butter’ of most GATT trade rounds, and were relatively simple to negotiate. Increasingly, more attention has been paid to politically ‘sensitive’ agriculture, as well as services and ‘behind the border’ issues such as standards and intellectual property, which tend to be seen primarily as domestic matters. At the same time, WTO member countries have come under pressure to include labour and environmental standards in trade agreements.

The rise of preferential trading agreements

The relationship between preferential trading agreements (PTAs) and multilateral trade agreements is contentious. WTO rules do not prevent member countries from participating in PTAs. However, they do require that such arrangements meet certain criteria, such as that they remove or reduce barriers on ‘substantially all’ goods within the region. While some claim that the outcomes of PTAs can be ‘building blocks’ for trade liberalisation, others see them as ‘stumbling blocks’. For instance, the OECD (2003, p. 5) has cautioned that:

... the patchwork of regional initiatives may also give rise to systemic frictions because of divergence among [PTAs] and with WTO agreements.

Apart from issues relating to the impact of PTAs on trade (see below), it has been suggested that negotiating bilateral and regional agreements deflects resources and attention away from multilateral trade agreements. For example, it was suggested that not as much ‘groundwork’ had been undertaken in the Doha round as the Uruguay Round for this reason (Garnaut 2003). However, as noted in Australia’s case, the rise in PTAs itself has in part reflected frustration at the difficulty and slow pace of multilateral negotiations.

Domestic political obstacles remain strong

The difficulties faced by multilateral negotiations can also be attributed to more fundamental political influences operating within WTO member countries. Compared to most PTAs, multilateral liberalisation generally places greater competitive pressure on domestic industries of participating countries. The political calculus favouring protectionist interests within democratic societies is well known and has long posed major obstacles to trade reform in agriculture and for other exports of interest to Australia. The key elements have been described previously and are summarised as follows:

- The beneficiaries of protection tend to be concentrated in specific industries and sometimes in particular regions. They have strong incentives to form associations to lobby politicians to maintain or increase their protection (and to change their vote if they don’t). They also have incentives to rally public support by drawing attention in the media to the risks to their livelihoods from removing protection — witness protests by French farmers.
- By contrast, the costs of protection are generally dispersed widely but thinly throughout the community — for example, through higher prices for farm produce and other protected items. Individual consumers have little incentive to lobby to have the protection removed (or to change their votes if it isn’t). In fact, many consumers may not even be aware of the existence of a tariff or other trade barrier on a particular item and its adverse effect on their spending power and product choice, let alone the broader adverse effects on productivity and resource allocation.
- This skewing of public awareness and political incentives is exacerbated because the costs of trade liberalisation are more immediate and visible than the benefits. For example, the potential loss of existing jobs in a protected industry is visible, tangible and a cause of immediate angst, and thus particularly amenable to media coverage. However, the jobs that would be brought into existence in other industries consequent upon reform are scattered throughout the economy and may not eventuate until some time after the reform takes place.
- These uneven political pressures are compounded by government administrative structures which tend to be aligned with particular groups or sectors, leading to a

focus on their welfare, and making it harder for governments to assess the economy-wide effects of trade reform.

- More broadly, there is often confusion about the source of the gains from trade liberalisation. It is widely recognised among economists that major benefits for a country from trade and its liberalisation come from having access to lower cost imported goods and services, and the stimulus to domestic industry performance and restructuring flowing from the increased competition it provides. However, much public debate continues to reflect mercantilist notions that exports are good for a country's prosperity while imports are bad.

Why isn't 'reciprocity' working?

The exchange of concessions in reciprocal fashion among member governments was an intentional design feature of the GATT (and now WTO) aimed at counteracting the skewed domestic politics that impedes trade reform (Dam 1970; Roessler 1989). Reciprocal agreements can potentially ameliorate the political difficulties confronting reform by:

- harnessing interests of exporting industries in gaining access to foreign markets to support domestic liberalisation (*quid pro quo*);
- setting foreign producers interested in export expansion against domestic protectionist interests; and
- reducing transitory adjustment losses from liberalisation.

Such influences no doubt contributed to the considerable success of the GATT in reducing manufacturing tariffs across most areas of merchandise trade in the decades following World War II. But they have proven much less effective in the most 'sensitive' sectors, like agriculture and TCF, and in a number of areas of services trade which are now encompassed within the negotiations.

Experience has shown that exporters are not likely to lobby their government for trade liberalisation policies as intensively as import competing industries are likely to lobby for the retention of protection. Further, the pressure from foreign exporters to improve market access has minimal influence on the domestic debate due to their lack of political representation and support within the community.

In fact, the reciprocity approach used in multilateral trade negotiations can reinforce the general lack of domestic willingness to liberalise trade, because the agreement to reduce protection levels can be treated as a 'concession' to other WTO members, rather than as a source of benefit to members. This mode of thinking may then be both reflected in, and reinforced by, governments 'selling' the benefits of trade agreements they enter by emphasising the improved market access for their

country's exports, rather than the favourable effects of lower priced imports on national welfare (PC 2001b). This can further add to the tendency for the community to view an increase in exports as a good outcome for the economy, while increased import competition is not. In this way, trade negotiations can themselves become an impediment to domestic reform.

In relation to multilateral negotiations themselves, undue emphasis on reciprocity can stall progress, as member governments may be concerned about being seen to offer too many 'concessions' (such as reductions in their tariffs) relative to the concessions offered by others. This mutually self-defeating process was evident in the recent Doha Round negotiations, with claims that each country or region had requested that other countries 'offer' more before they give up more 'concessions' (ICTSD 2006). For example, EU Trade Commissioner Peter Mandelson made the comment that:

The United States was unwilling to accept, or indeed to acknowledge, the flexibility being shown by others in the room and, as a result, felt unable to show any flexibility on the issue of farm subsidies (ICTSD 2006, p.1).

In response, US Trade Representative released a statement claiming:

During the recent G-6 meeting the US made clear that it was ready and willing to demonstrate greater flexibility in the area of domestic supports if the EU and advanced developing economies demonstrated greater flexibility in market access. (Office of the US Trade Representative 2006, p.1).

Domestic mechanisms to promote trade liberalisation?

The sticking point in the Doha Round — the divisions between the EU, US and developing countries regarding the adequacy of current concessions — relates to perceptions within those countries regarding the source of the benefits of trade liberalisation and how this translates to the multilateral negotiating arena. Resolution of these differences will not be straight-forward, and there is currently no process within the WTO trade negotiation process that can solve the underlying problem.

What is needed are processes and institutions within member countries that can promote a better understanding of the domestic tradeoffs in trade liberalisation, and help counter the political influence of protected industries by demonstrating which sections of the economy and community bear the costs of trade protection and which sections benefit.

This of course is not a new idea. Indeed it is an approach which Australia itself has followed in its approach to industry assistance. This has been favourably remarked

on by international agencies such as the OECD (2003), as well as the WTO (2007) and has attracted some interest within APEC.

The notion of using GATT/WTO processes to establish ‘domestic transparency’ mechanisms within member countries was advocated two decades ago by two eminent international study groups reporting on ways to overcome the then impasse in progressing multilateral trade negotiations (Leutwiler 1985, Long 1987). The Long Report, headed by a former Director-General of the GATT and including W. B. Carmichael, a former Chairman of the Industries Assistance Commission, set out the broad features that a transparency mechanism would need to contain (see box 4.2).

Box 4.2 The Long Report’s model for domestic transparency

The Long Report suggested that the following elements might be suitable for a domestic transparency mechanism:

Institutional vehicle: The designation of an independent, and preferably statutory, body within each country to prepare regular reports ... to their governments on public assistance to industries.

Charter: Its reports should cover all forms of public assistance, including measures under laws on ‘unfair trade’ practices, to all industries. The reports should be made public so that they are a vehicle for public scrutiny, within the domestic economy, of industry support.

Focus of guidelines: The standard code of objectives negotiated to provide a reference framework for such bodies should be related to domestic economic efficiency and the general public interest rather than any international commitments (although these are clearly compatible).

Status in domestic institutional arrangements: While it is essential that the independence and industry-neutrality of these bodies should be guaranteed by statute, they should have only an informational role in the domestic policy environment. They should have no judicial, executive or direct policy role and they should be accountable solely to their respective governments or legislatures.

Status in international negotiations: The public informational output of each such body would assist its national government to determine what approach to international relations would be most rewarding nationally but they would have no mandatory or pre-emptive effects on the course of any [multilateral trade] negotiations.

Source: Long (1987).

Methods of establishing greater domestic transparency were under consideration in the first stages of the Uruguay Round in the negotiating group on the Functioning of the GATT System (Rattigan, Carmichael and Banks 1989). Despite widespread recognition of the need for greater domestic transparency of industry assistance, finalising the institutional arrangements was placed on the ‘backburner’ with

priority given to establishing the Trade Policy Review Mechanism (PC 2000b). This vehicle for international surveillance of member countries' trade policies has generally been regarded as a useful advance. Nevertheless, it remains a mechanism that is largely *external* to the policy debate within member countries.

The idea of promoting greater transparency in trade policy development within WTO member countries continues to have support.

The Tasman Transparency Group, a collective of Australian and New Zealand agriculture and business organisations, released a paper, in July 2006, proposing that a unit be established within the WTO to assist countries to build a local institutional capacity in trade policy formulation (see box 4.3).

Box 4.3 The Tasman Transparency Group's proposal

The 'Tasman Transparency Group' recently proposed that a special facility, a 'transparency agency', be created within the WTO. This agency would be at arms length from the negotiating process. Its role would be to assist individual governments introduce domestic processes that would enable governments to secure better outcomes from multilateral negotiations — that is, greater trade liberalisation. Member countries would have the option to make use of this facility, but there would be no obligation to do so.

The Group proposed that the transparency agency would have no power of enforcement. The aim of the agency would be to raise awareness of the source of domestic gains from reform including trade liberalisation. The Group recognised that, given the consensus nature of decision-making in the WTO, considerable effort and debate would be required to gain the necessary support.

The Tasman Group suggested that the Australian and New Zealand Governments advocate their proposal to APEC, the World Bank, the IMF, the OECD and UNCTAD (United Nations Conference on Trade and Development).

Source: Tasman Transparency Group (2006).

Australia's Prime Minister, John Howard, has acknowledged the benefits of a domestic transparency mechanism in assisting trade reform:

...supporting trade liberalisation in democracies will only succeed if communities in each country believe that it is in their interest to liberalise. In the Australian context, the work of the Productivity Commission and its predecessors ... has been fundamental to building and maintaining Australian public understanding of the benefits of greater openness to international competition. ... If other countries could adopt similar transparent institutional responses, public opinion would be better informed on the cost of trade barriers... (Howard 2003a, p.2).

The particular institutional arrangements to achieve this would need to reflect each member country's social and political environment. Developing and implementing such arrangements is not something that is likely to be achieved quickly or easily. Nevertheless, the longer term benefits could be substantial and warrant renewed attention within the WTO forum.

4.2 Developments in preferential trade agreements

Worldwide, the number of preferential trade agreements (PTAs) is increasing rapidly. More than half of all PTAs notified to the GATT/WTO since 1948 have been finalised in the last decade — 186 PTAs had been notified as of November 2005 (PC 2006a). More recently, the WTO has estimated that the number of PTAs could rise to 400 by 2010 (Lamy 2007).

The effects of PTAs are significantly more complex and uncertain than the effects of multilateral reform. The recent surge in PTAs, while affording possible benefits, also carries some risk (PC 2004a).

An eminent panel of trade policy experts (WTO 2004) noted that PTAs can provide an avenue for small groups of nations to further liberalise trading arrangements beyond what is currently achievable in a multilateral arena, and that any progress in regional trade liberalisation could be multilateralised through WTO negotiations in the future. It is also argued that the negotiation of PTAs may also help challenge some well-established protectionist interests within a country, and assist developing countries to adjust gradually to the opening of their markets.

However, the panel suggested that the proliferation of PTAs could undermine the key 'most favoured nation' principle of the WTO rules and global trade liberalisation. The panel cautioned that PTAs can divert trade from the most efficient countries, entrench support for less ambitious multilateral reform from the beneficiaries of PTA discrimination; divert skilled and experienced negotiating resources; and facilitate the emergence of 'non-trade' objectives in trade agreements (WTO 2004). PTAs can also introduce other costs for businesses, associated with different preferential rates and 'rules of origin'.¹

¹ Rules of origin specify the conditions under which a good is deemed to have originated from one of the countries that are party to a PTA, and thus be eligible for concessional treatment. For example, rules of origin might specify that, to be eligible for concessions, at least 50 per cent of the value added of the good must have been added in the countries party to the PTA. Without such rules, there could be an incentive to import goods from a third party country into the PTA region (through the member with the lowest tariffs) and hence take advantage of the concessions *within* the region. Circumventing higher tariffs in this way reduces the value of the preference given to some exporters.

Much of the analysis of PTAs has been undertaken at a conceptual level, or has involved modelling the potential impacts on trade and production in advance of the implementation of a PTA. Key influences on the trade and economic outcomes from a PTA include: the scope for trade diversion relative to trade creation, the nature of rules of origin, the coverage of trade under the agreement, and the number of exemptions and escape clause provisions. How these will play out in practice is often hard to predict.²

One of the few empirical studies to assess the effects of PTAs *in place* was conducted a few years ago by Productivity Commission staff (Adams et al. 2003). This analysis, while not definitive, suggested that a number of longer-standing PTAs may have diverted more trade than they created, potentially reducing welfare in the countries where this had occurred. However, the study also found evidence that some non-trade provisions could enhance international investment flows, particularly where the provisions were non-preferential in nature.

While the Australian Government has indicated that its 'highest trade priority is to free up global trade through the Doha Round' (Vaile 2006a), Australia has also followed the current trend of developing more PTAs, in part reflecting views about the pace and scope of likely outcomes from multilateral negotiations under the WTO. According to the (then) Minister for Trade:

In addition to our multilateral trade efforts, Australia is also looking for trade results through bilateral and regional agreements. These can often get faster commercial results than the multilateral process. They can also address non-tariff barriers like government procurement, competition, intellectual property and investment controls (Vaile 2006b).

Prior to 2003, Australia was party to three agreements, with Papua New Guinea, South Pacific countries and New Zealand, of which only the latter was a reciprocal agreement.³ Since then, Australia has concluded bilateral agreements with Singapore, Thailand and the United States.

² The Australian Department of Foreign Affairs and Trade has indicated that, in recognition of these points, Australian trade negotiators are pushing for strengthened disciplines on PTAs as part of the Doha negotiations. It has stated that "Subjecting [regional trade agreements] to review and effective disciplines in the WTO is important to Australia's broader trade objectives by ensuring the comprehensive [free trade agreements] are concluded that can serve as building blocks to broader trade liberalisation" (DFAT 2006c, p. 82).

³ The PTAs are the Papua New Guinea-Australia Trade and Commercial Relations Agreement, the South Pacific Regional Trade and Economic Cooperation Agreement and the Australia-New Zealand Closer Economic Relations Trade Agreement (ANZCERTA). However, only the ANZCERTA is a reciprocal agreement; the others are essentially mechanisms by which Australia unilaterally grants preferential entry to its market for aid reasons.

The Australian Government is currently negotiating further bilateral agreements with China, Malaysia, Japan, Chile and the Gulf Cooperation Council (GCC). It is also pursuing a joint agreement encompassing the Association of South East Asian Nations (ASEAN) and New Zealand. The Australian Government is undertaking a feasibility study of the benefits of a PTA with the Republic of Korea. The details of these negotiations are summarised below.

The Australian Government has also recently implemented changes to the rules of origin in the Australia-New Zealand Closer Economic Relations Trade Agreement. These changes are also outlined and discussed in this section.

On-going negotiations

China

A joint feasibility study on a PTA between Australia and China, released in April 2005, suggested that it could provide significant economic benefits. Following the release of the study, the Prime Minister of Australia and the Premier of China agreed to enter into negotiations.

Eight rounds of negotiations have been held thus far, with the market access negotiations for goods and services starting at the 7th round held in December 2006. While the exact details of country goods offers are confidential, Australia's offer did not include any acceleration of the current tariff reduction in existing industry plans for textile, clothing and footwear and passenger motor vehicles sectors (DFAT 2006a). Following this initial round of offers, Australia has requested that China provide a broader goods offer, particularly in the area of agriculture. Matters subject to forthcoming negotiations include the methodology for the rules of origin and import licensing.

Despite China acknowledging that negotiations with Australia were complex, reflecting a level of ambition in the PTA that is unprecedented for China, it has committed to significant progress in negotiations by mid-2008 (Chinese Government 2006, DFAT 2006b).

Malaysia

In April 2005, following the release of scoping studies, the Prime Ministers of Australia and Malaysia agreed to begin negotiations on a PTA.

There have been four full rounds of negotiations since May 2005. Initial tariff offers on goods were tabled in July 2006, which began the process of each country identifying areas for improved offers. Agreement has been reached on the approach

to rules of origin, and negotiations have significantly advanced agreement on intellectual property. A number of issues remain to be resolved. Australia has raised concerns that Malaysia's import licensing system may impede realisation of the market access benefits brought about by tariff reductions. Negotiations are also continuing in relation to government procurement, services and investment.

ASEAN-New Zealand

Regional trade negotiations commenced in early 2005 on an Australia–ASEAN–New Zealand Free Trade Area.

Tariff negotiations are proceeding using a two-track ('normal' and 'sensitive') approach. Tariffs on goods covered by the normal track, covering 90 per cent of tariff lines, will be eliminated over an agreed timeframe (still subject to negotiation). Tariff commitments on the remaining tariff lines are still being discussed, but will involve a combination of tariff elimination for some products and commitments such as tariff caps for others. Indicative lists of sensitive goods have been exchanged by ASEAN countries, Australia and New Zealand. Initial tariff offers are expected to be exchanged in the middle of 2007, to be followed by detailed market access negotiations.

Negotiations relating to rules of origin are underway. All parties have agreed to establish a rule of origin regime under which exporters will be able to use either a Change in Tariff Classification approach or a value added approach.

Discussions have begun on the broader services agenda, including provisions regarding the movement of persons, telecommunications, electronic commerce and financial services. Initial services offers are to be exchanged by mid-2007. Negotiations have also been held on investment regimes, although a number of issues are still to be resolved (DFAT 2007).

Recent announcements

In December 2006, the Australian Government announced that it would seek to commence bilateral negotiations, with a view to developing comprehensive and ambitious PTAs, with:

- Japan;
- the Gulf Cooperation Council (GCC⁴); and
- Chile.

⁴ The GCC comprises Bahrain, Kuwait, Oman, Qatar, Saudi Arabia and the United Arab Emirates.

Bilateral negotiations are expected to commence during 2007 (Truss 2006a, 2006b, 2006c).

Previous bilateral negotiations with the United Arab Emirates have been incorporated into the GCC negotiations following the decision by the Supreme Council of the GCC that member countries could only negotiate trade agreements collectively, with the exception of those with the United States.

In addition to the announcement of a number of bilateral trade negotiations, Australia and the Republic of Korea agreed to conduct a joint study on a possible PTA in December 2006. The feasibility study will be undertaken by private research institutions in both countries. The study is expected to report to both governments towards the end of 2007 (Truss 2006d).

Changes to the Australian New Zealand CER rules of origin

In 1983, Australia signed the Australian New Zealand Closer Economic Relations Trade Agreement (ANZCERTA). Like most PTAs, ANZCERTA has specific rules of origin which determine whether goods are classified as being manufactured in either Australia or New Zealand, thus qualifying for concessional entry. The rules are relevant only where concessional entry applies under ANZCERTA — that is, for items with non-zero tariffs in Australia or New Zealand.

In 2004, the Commission was asked to report on the suitability of these rules of origin. It found that, although there were some problems, generally the ANZCERTA rules of origin were not overly restrictive (compared to rules of origin in other agreements) and, in any case, were becoming of less importance as both Australia and New Zealand continue to lower their trade barriers. Accordingly, the Commission recommended against changing the framework of ANZCERTA rules of origin. It found that the most prudent approach would be to make minor changes to reduce operational problems, and to liberalise the current rules by applying a waiver to provide duty free entry for CER goods manufactured in Australia or New Zealand which face trans-Tasman tariff differences of 5 percentage points or less (PC 2004b).

Subsequently, a new framework for ANZCERTA rules of origin was agreed at the annual meeting of Australian and New Zealand Trade and Economic Ministers, December 2004. The Ministers agreed to adopt a ‘change of tariff classification’ (CTC) approach to determining origin in ANZCERTA, and committed to ‘the liberalisation of all tariff lines over time’ (CERMF 2004). The new rules of origin were finalised in 2006, taking effect on 1 January 2007.

The new rules of origin will operate concurrently with the existing ‘factory cost’ rules until the end of December 2011, when the factory cost rules will cease. Under this transition arrangement, producers of goods not currently qualifying for preferential treatment under the outgoing ‘factory cost’ rules would be able to apply under the 2006 rules. Similarly, producers failing to qualify under the 2006 rules would be able to apply under the factory cost rules. From 1 January 2012, origin for the purpose of obtaining ANZCERTA tariff preferences would be determined only by the 2006 rules.

The 2006 rules differ significantly from the outgoing rules. The latter are relatively free from deliberately restrictive and product-specific provisions (PC 2004b). While the 2006 are based on a CTC approach, they also contain a variety of product-specific provisions, sector-specific technical tests and regional value-of-content provisions (see box 4.4), settled after a significant period of negotiation involving exporters, industry associations and government officials. Such additional provisions apply to nearly 20 per cent of the line items to which tariffs apply, including many ‘sensitive’ items which attract relatively high tariffs.

The Commission has found that product-specific rules (typically associated with the CTC model) are fraught with problems including: inconsistent treatment of industries; differences between PTAs for individual items of trade; openness to manipulation to provide sectoral assistance with limited transparency; and multiple criteria for individual items (PC 2004b). These problems tend to reduce efficiency and raise compliance and administrative costs.

However, the ultimate impact of the new ANZCERTA rules of origin will depend on the relative tariffs in Australia and New Zealand and the margin of preference these differences afford Australian and New Zealand producers — the lower the tariffs and differences in tariffs between PTA partners, the lower the potential efficiency costs of product-specific rules of origin. The Commission found that further scheduled tariff reductions in Australia and New Zealand could render ANZCERTA rules of origin ‘virtually irrelevant in 5 to 10 years time’ (that is, before 2015).

It noted that there would be gains to both Australia and New Zealand from closer alignment of their trade regimes, such that there would be little or no need for rules of origin and the economic and administrative costs associated with them. Accordingly, among other things, the Commission recommended that:

Before 2010, consideration should be given to advancing the goals of the CER Agreement by: ... alignment of remaining non-zero MFN rates in the Australian and New Zealand tariff schedules, so that ultimately merchandise trade from all sources enters each jurisdiction on a common basis. (PC 2004b, p. 178)

Box 4.4 Selected examples from the 2006 CER rules of origin

While the majority of the new rules of origin are based on the CTC approach alone, a significant minority also include applications of product-specific regional value content and technical tests for determining origin.⁵ Three examples of such rules follow.

Example 1: Men or boy's coats and jackets (HS 6101 & 6103)

The rule requires that there is a change to heading 6101 or 6103 from any other chapter:

- provided that the good is both cut (or knit to shape) and sewn or otherwise assembled in the territory of one or both of the Parties; and
- there is a regional value content of not less than 50 percent based on the factory cost method.

Example 2: Blankets and travelling rugs (HS 6301)

The rule requires that there is a change to heading 6301 from any other heading:

- except from headings 5007, 5111 through 5113, 5208 through 5212, 5309 through 5311, 5407 through 5408, 5512 through 5516, 5602 through 5603, 5801 through 5802, 5809 through 5811, 5903, 5906 through 5907 or 6001 through 6002; or
- provided there is a regional value content of not less than 55 percent based on the build down method.

Example 3: Insecticides, rodenticides, fungicides, herbicides etc (HS 380850)

The rule requires that there is a change to heading 380850 from any other subheading:

- provided that 50 per cent, by weight of the active ingredient or ingredient, is originating.

Source: Customs (New Zealand Rules of Origin) Regulations 2006.

⁵ The CTC approach requires that each of the non-originating materials used in the final goods must undergo the applicable classification change. Generally, this means that the non-originating materials are classified under one tariff provision before processing and under another once processing is complete. The regional value content approach requires that a certain proportion of the value of the final good must originate in the preferential trade area (that is, Australia or New Zealand). The product specific rules adopt a number of methods for defining origin. Technical or specific process tests require certain industrial processes to be undertaken to confer origin in the country in which the processes are carried out.