
10 Other possible economic effects of BRTAs

Bilateral and regional trade agreements (BRTAs) can have broader impacts on the economies of partners apart from those that directly result from changes in trade and investment flows. In particular, some BRTAs contain provisions that extend past trade related matters and deal with domestically focused regulations. BRTAs can also have an influence on barriers between markets and the potential for economic integration.

Section 10.1 examines the potential impacts of behind-the-border reforms, while some of the impacts from greater economic integration embodied in BRTAs are discussed in section 10.2.

10.1 BRTAs and domestically focused regulation

There is the potential for BRTAs to influence domestically focused policies in a number of ways. First, BRTAs may result in partner countries directly negotiating changes to domestic regulations aimed at local markets but which may inhibit trade — for example, registration requirements for service professionals to operate in their field of expertise. Alternatively, BRTAs may place pressure on inefficient and production distorting domestic policies by subjecting industries to increased competition that would otherwise be unattainable. Such increases in competition may then contribute to broader reforms within a domestic economy.

Direct influences on domestically focused regulations

BRTAs sometimes have a direct influence on behind-the-border regulations. In some instances, such influences are likely to create additional rigidities in domestic regulations. For example, the Music Council of Australia believes that provisions drawn in from BRTAs, such as the ANZCERTA and AUSFTA agreements, have hindered Australia's ability to regulate to protect its cultural industries:

The Closer Economic Relations (CER) agreement with New Zealand resulted in a curious – and unexpected – outcome: Australian television productions must now be defined as being both Australian and New Zealand programs for the purposes of the

Australian Content Standard with which Australia's free-to-air commercial television broadcasters must comply. ...

Notwithstanding the openness of the Australian market and whilst already subject to considerable cultural domination by the United States, Australia was nonetheless forced to compromise its capacity to regulate to protect its own cultural industries. Existing measures in respect of regulating content on Australian analogue television and radio services have been frozen and subjected to ratchet provisions. The extent to which Australia is able to regulate these services in the digital environment is severely constrained and in respect of its capacity to regulate new media is subject to tests that must secure US agreement that there is a demonstrable lack of access to Australian content. (sub. 35, p. 4)

Other examples of rigidities include the intellectual property (IP) rights provisions within AUSFTA. Further, some provisions can potentially create negative impacts for an economy, for example as was perceived with the Pharmaceutical Benefits Scheme (PBS) during the AUSFTA negotiations during the AUSFTA negotiations. These issues are discussed below.

IP rights under AUSFTA

All of Australia's more recent agreements include a chapter on IP provisions. However, in most cases these agreements are high level principles-based undertakings that codify existing commitments. For instance, provisions in agreements often simply reaffirm commitments in the WTO Trade-Related aspects of Intellectual Property Rights agreement. One exception to this is the agreement with the United States which included a number of additional provisions and, as noted by IP Australia (sub. 24), was the only agreement that involved legislative changes. (The recent agreement with Chile also includes some of the provisions of the United States agreement, such as the copyright extension — both Australia and Chile having pre-existing agreements with the United States.) As detailed by DFAT (2010c), these include:

- protection for copyright owners, including:
 - agreement to implement the World Intellectual Property Organization (WIPO) Internet Treaties; and
 - an expeditious process that allows for copyright owners to engage with internet service providers (ISPs) and subscribers to deal with allegedly infringing copyright material on the Internet;
- tighter controls on circumventing technological protection of copyright material together with a mechanism for examining and, as necessary, introducing public interest exceptions in relation to technological protection measures, along with a transition period to provide the opportunity for public submissions in this area;

-
- agreement on standards of copyright protection;
 - an increased term of protection for copyright material;
 - enhanced intellectual property enforcement, including:
 - increased criminal and civil protection against the unlawful decoding of encrypted program carrying satellite TV signals;
 - agreed criminal standards for copyright infringement and on remedies and penalties; and
 - reinforcement of Australia’s existing framework for industrial property protection.

The extension to copyright terms was the most contentious of these and subject to a number of investigations (for example, the Senate Inquiry — SCFTAAUSA 2004). Some of the broader economic effects of this extension are discussed below, along with some of the other IP related provisions.

Extension of copyright provisions

IP rights can encourage innovation and the production of certain goods by conferring monopoly property rights to an individual or business so that the additional benefits gained compensate for the costs borne in developing the good. In this way, an environment where innovation can occur is created, generating significant benefits to the economy.

Despite this, there is uncertainty over the time period required for such monopoly rights to exist, such that there is sufficient incentive for the production of these goods. If too short, there is a risk that a socially desirable level of production of these goods will not exist. If too long, there is a risk that consumers will pay too much for these goods, and the owners of these goods will receive what are termed ‘economic rents’.

Prior to the AUSFTA, Australia and the United States had different durations of protection for copyright material. However, as part of the agreement, Australia agreed to extend the duration of protection from life of an author plus 50 years to the longer US duration of life of an author plus 70 years, despite previously rejecting calls for such an extension (SCFTAAUSA 2004). Subsequently, there has been debate as to whether these changes to Australia’s domestic regulation have been beneficial.

Participants in this study have expressed differing views on the changes under

AUSFTA. On one hand, the Copyright Agency Limited (CAL) stated:

As far as CAL is aware, trade agreements have resulted in an improved environment for the production of, and legitimate access to, copyright content. Outcomes from trade agreements that have contributed to this improved environment include obligations to accede to multilateral treaties such as the Agreement on Trade Related Aspects of Intellectual Property (TRIPS), standards or obligations that exceed those required by multilateral treaties, such as border controls, and assistance with capacity building. (sub. 34, p. 3)

However, Telstra expressed caution as to the operation of IP chapters and suggested ‘... Australia’s trade agreements should not include matters which are not settled under Australian law.’ (sub. 49, p. 2)

John Ravenhill also suggests that such provisions, while being spread by the United States through BRTAs, may not be welfare enhancing:

The US now has agreements with Australia, Canada, Chile, Mexico, Peru and Singapore: it has signed but not ratified an agreement with Korea, and has been negotiating with Malaysia. These are the most comprehensive agreements in the region and could provide a foundation and framework for multilateralization (although they contain provisions that arguably are not welfare-enhancing, including some on intellectual property rights and the exceptions granted to US agricultural production). (sub. 36, p. 4)

In terms of AUSFTA, Dee provided some estimates of the effects suggesting that the copyright provisions could result in an annual net cost to Australia of up to \$88 million:

The DFAT/CIE report made some simplifying assumptions in order to quantify the benefits of extending the term of copyright protection. While the report was not able to make the same assumptions to quantify the costs, this has been done in Box 2. The net effect is that Australia could eventually pay 25 per cent more per year in net royalty payments, not just to US copyright holders, but to all copyright holders, since this provision is not preferential. This could amount to up to \$88 million per year, or up to \$700 million in net present value terms. And this is a pure transfer overseas, and hence pure cost to Australia. (Dee 2004, p. 31)

Other IP provisions

The AUSFTA also required Australia to make a number of other changes to aspects of its copyright system. While some of the commitments in the agreement to join the WIPO ‘internet treaties’¹ may yield benefits in terms of creating a unified international system to deal with piracy issues, as the Senate observed, other

¹ The WIPO Copyright Treaty and WIPO Performances and Phonograms Treaty.

measures are more likely to have created net costs. In this regard, a number of concerns have been expressed about the copyright provisions in the AUSFTA, both then and since, including the:

- enshrining in domestic regulation business activities that would otherwise be anti-competitive (such as permitting the use of region codes on DVD players), and making circumvention of such technology an infringement;
- failure to adopt a definition of ‘fair use’ that more closely aligned with the broader US approach; and
- extending ‘safe-harbour’ regimes for ISPs, which removes potential liability for secondary-infringement if ISPs ‘act expeditiously’ to remove infringing content once notified by rights holders, without a requirement for rights holders to prove in a court that such material is infringing.

At the time of the agreement, a Senate Inquiry questioned a number of these provisions, and in regard to the technological protection measures (TPMs) or anti-circumvention devices, the committee concluded:

... the Committee remains concerned that the AUSFTA goes too far. TPM circumvention may be done for legitimate, non-infringing purposes, not simply piracy. A ban on TPM circumvention, while possibly assisting to curb some piracy, may also prevent many legitimate purposes. This severely interferes with the rights of consumers to do as they wish with property that they have legally purchased. It is important to ensure that certain classes of copyrighted work be exempt from the normal TPM circumvention prohibitions where the circumvention is for a noninfringing use. (SCFTAAUSA 2004, p. 90)

Reflecting on Australia’s overall experience following AUSFTA, the Australian Digital Alliance and the Australian Libraries Copyright Committee submitted that the:

...net impact of implementing AUSFTA in Australia was to set a level of copyright protection that is, in practice, even higher than that in the United States. This is because we matched their higher level of copyright protection, but have maintained our lower level of copyright users’ rights. Thus, the balance of interests favours copyright owners to a greater extent in Australia than in the United States. (sub. DR79, p. 6)

As with the term of protection, IP provisions regarding the scope of rights, anti-competitive activities and non-infringing uses by consumers should foster access to knowledge and innovation while protecting against unnecessary and excessive rents accruing to producers. In the Commission’s view, the changes following the AUSFTA have make it less likely that an appropriate balance between supplier and user interests prevails in Australia’s intellectual property system.

PBS scheme and AUSFTA

At the time of negotiating AUSFTA, there was considerable contention over the impact on the operation of Australia's PBS scheme. For example, it was argued by some in the medical professions that:

Provisions in the Australia-United States Free Trade Agreement (AUSFTA) may threaten the Australian Pharmaceutical Benefits Scheme (PBS), the "gold standard" of such programs worldwide. (Outterson 2004, p. 1)

The provisions within the agreement were aimed at procedural changes which provided drug manufactures more opportunities to have drugs listed on the PBS. Burton and Varghese (2004) provided a summary of the changes, noting that only applications for new listings rejected by the Pharmaceutical Benefits Advisory Committee (PBAC) are eligible for an independent review. It was feared that the changes would undermine Australia's control over the PBS through the addition of a review process.

Despite this, as argued by Burton and Varghese (2004), and detailed in SCFTAAUSA (2004), much of the public debate at the time of the AUSFTA deal was incorrect. Burton and Varghese (2004) found that the AUSFTA provisions did not require the review findings to be binding on the PBAC decision, and thus were unlikely to influence Australia's control. Further they stated:

... AUSFTA does not change the Committee's legislative requirement to make decisions on the basis of therapeutic effectiveness and cost-effectiveness. So whatever form the review process takes, the Committee remains bound to these criteria. If new drugs are listed on the PBS as a result, it could be argued that consumers will be better off because they will pay less for these medicines and have access to more effective drugs. (Burton and Varghese 2004, p. 1)

At the same time, the AUSFTA negotiations were used to achieve greater transparency in the process.

Despite this, the Commission was informed during consultations that the potential for an adverse outcome was real, and that vigilance was required to ensure this did not arise. The Senate inquiry into the AUSFTA reached a similar conclusion:

This committee appreciates that Australia's negotiating team has negotiated long and hard in the face of considerable pressure to ensure that Australia's commitments in this area have much less impact on our existing law and policy than US negotiators would no doubt have liked. (SCFTAAUSA 2004, p. 140)

But the Senate inquiry also questioned the inclusion of these provisions in the first

instance on wider public interest grounds:

By allowing the PBS to enter a trade negotiation in the first place, the government has opened the door to forces that it ultimately may not be able to control. (SCFTAAUSA 2004, p. 140)

Given these concerns, and those put to the Commission during consultations, bringing domestically focused regulation aimed at public-good outcomes, such as the PBS, under the umbrella of trade agreements risks incurring substantial and potentially unforeseen costs.

Indirect influences on behind-the-border regulations

The influence that BRTAs have indirectly on behind-the-border reforms is difficult to assess. For example, if reform-minded governments are more likely to be involved in BRTAs, then the existence of a BRTA, or the provisions embodied may not directly influence the reform path that occurs subsequently as governments would have otherwise taken that path. Alternatively, governments may use BRTAs as a means of driving behind-the-border reforms by reducing domestic concern over reform by making it a *quid pro quo* for improved market access in partner countries. For example, the United States-Vietnam bilateral trade agreement in 2001 led to many changes in border and behind-the-border regulations in Vietnam in return for a normalisation in trade relations between the two countries (Parker, Quang and Anh 2002). Vietnam adopted a number of investment, services and intellectual property reforms, and agreed to reduce tariffs on a number of products on a most-favoured-nation basis under the agreement.

It may also be the case that the impacts from a BRTA may play a role in domestic reform, but not be the sole driver. For example, the Australian Dairy Industry Council suggested that the ANZCERTA was a key driver of the reforms to domestic dairy industry regulation during the 1980s, which has had subsequent effects on industry rationalisation and investment:

The introduction of this agreement was a key factor in the rationalisation of commercial and policy arrangements with the Australian dairy industry from the mid 1980s.

Prior to the introduction of CER two-way dairy trade between Australia and New Zealand was minimal with both countries maintaining barriers to trade. In more recent years exports from Australia to New Zealand have exceeded \$100 million per annum while imports into Australia from NZ regularly exceed \$300 million. There has been significant investment in Australian dairy by the New Zealand dairy company Fonterra over the past decade. (sub. 38, p. 9)

Nevertheless, the Council recognised that:

Given Fonterra's activities in other countries around the world it is reasonable to speculate that this investment would have occurred even in the absence of the CER Trade Agreement. (sub. 38, p. 9)

Despite the varying influence BRTAs may have on domestic reform, it remains the case that these reforms do not necessarily rely on trade agreements to progress. A number of submissions have highlighted this point. For example, as put by the Business Council of Australia (BCA):

Policy options which support trade reform enhance the prospect for delivery of long term growth in the Asia-Pacific region. FTAs are not a substitute for properly designed strategies for economic reform. However, they are limited in the policy changes they can drive to encourage and stimulate programs to address 'behind the border' barrier to facilitate a more open and transparent business environment. (sub. 41, Attachment 1, p. 9)

Further, arguments have been put forward suggesting the use of BRTAs to gain such reform is not the best way forward. The Joint Submission by Nineteen Australian and New Zealand Business Leaders and Economists (sub. 5) suggests that to gain meaningful behind-the-border (and at-the-border) reform, while allowing domestic governments to maintain sovereignty and control over policy, transparency in domestic policy effects and policy making needs to be improved. For this to occur, governments should be encouraged to develop institutions which highlight the economy-wide impacts of policy decisions.

10.2 Economic integration impacts from BRTAs

Economic integration has been variously defined (box 10.1). Integration occurs as a result of barriers between members of a particular area being reduced allowing the freer flow of goods, services, people and investment across borders within the integrated area, and is seen by some as reflecting the dynamic gains that can result when increased trade openness leads to increased competition in merchandise, services and investment markets. In this way, the processes which determine the prices of these goods, services and capital become common between the economies involved.

Integration in this sense goes beyond the commitments to reduce trade barriers within BRTAs. Some participants believe that BRTAs are differentiated by the degree of economic integration embodied. For example, as put by Lloyd:

... one should distinguish between agreements that pursue the objective of "trade liberalisation", as mentioned in the Terms of Reference, and those that pursue the objective of "economic integration". The Closer Economic Relations (CER) agreement between Australia and New Zealand is distinct from the other five actual agreements in

that it has evolved into an agreement that can be regarded as pursuing the objective of economic integration. (sub. 3, p. 1)

Box 10.1 Economic integration and trade openness

Economic integration is believed to occur along a continuum which extends from trade openness between economies, to common monetary and fiscal policy settings which exist within the European Union. While broadly consistent, a number of definitions of economic integration exist. Lloyd (2005) defines economic integration in relation to BRTAs as:

... the process of removing government measures which discriminate against foreign suppliers of goods and providers of services and suppliers of factors. In the regional context, the relevant “foreign” suppliers are those located in the other countries which are members of some regional agreement.

Two or more national economies in a region will be completely integrated if all measures that discriminate against regional suppliers are removed. The concept of complete integration provides a standard by which we can assess the extent of economic integration at any one time in any RTA. ...

Three sets of policies are involved in the achievement of a completely integrated market: the elimination of *border* barriers to cross-border trade; the elimination of *beyond-the-border* laws and regulations that inhibit cross-border trade or delivery of services; harmonisation of measures *across-borders* ... (pp. 3–4)

Corbett observes that economic integration occurs when prices in the integrating economies are established by a common process (Corbett 2010). Others suggest that economic integration can be associated with the reduction of trade barriers. For example, as put by the BCA in their submission in relation to ASEAN:

Over the past decade, ASEAN nations have sought to deepen economic integration amongst themselves and with other trading partners in the Asian region. Trade and investment liberalisation in both bilateral and regional trade agreements are core to this. (sub. 41, Attachment 1, p. 8)

Another important element is the freer movement of labour. For example, Elek (sub. 54, attachment 1) points out that impediments to the freer movement of factors of production (including labour) are significant impediments to economic integration.

A common element in all definitions is trade openness, that is, reduced trade and investment barriers promote economic integration. However, while increased trade openness can provide scope for economic integration to occur, it does not mean it will occur. Instead, in order to reach a point where price formation processes are common, actual improvements in competition and conditions which allow the freer movement of factors of production need to be observed.

There are a range of potential benefits which flow from economic integration. In financial markets, for example, potential gains include (Corbett 2010):

- the larger pool of capital available for one party once barriers are removed increases investment and promotes the efficient use of capital through greater competition for funds; and

-
- improvements in productivity through a greater degree of knowledge transfer between economies.

In a similar vein, the BCA claimed that economic integration was important for business profitability:

Business has a commercial interest in furthering economic integration through the Asian Pacific region which optimizes opportunities for Australian companies to operate easily and profitably in other markets. It is important that integration frameworks in the region are based on open and competitive markets for trade and investment and promote economic growth in the longer term. (sub. 41, Attachment 1, p. 21)

Benefits from economic integration are also seen as arising in the form of dynamic productivity gains, and deriving from the freer movement of labour within the integrated area. These aspects are discussed below.

Dynamic productivity gains

The CIE (2004a) identified four sources of dynamic productivity gains in an integration context.

- Dynamic investment: a reduction in tariffs on investment goods improves the return to capital of these goods, and therefore productivity.
- Pro-competitive effects and scale economies: increasing competition can discipline domestic businesses, encouraging them to be more efficient. Further, the potential to increase market size through exports promotes specialisation, increasing productivity.
- Endogenous productivity: foreign firms with relative production efficiencies are most likely to expand into a domestic market once trade barriers are reduced, bringing with them new technologies, better practices and innovations which can be absorbed by domestic competitors.
- Endogenous capital flows: foreign direct investment (FDI) may bring with it new technologies which could have a flow on impact on productivity in the rest of the economy.

Examining past research, the CIE (2004a) also found that the impact of these dynamic effects was significant. On average, it was found that a 1 per cent unilateral reduction in tariffs for a sector led to a 0.3 per cent increase in the productivity of that sector.

A number of other studies, including by the Commission, have also found links between protection and productivity. For example, a 1998 study by Commission staff found that general decreases in industry tariff protection were found to

increase output growth. However, the result was not uniform across each of the manufacturing sectors consolidated, suggesting that industry structure also plays a role (Chand, McCalman and Gretton 1998). The Commission has also found that reductions in assistance have contributed to productivity improvements in particular Australian industries through its inquiry program (for example, PC 2002, 2003, 2009). More generally, the Commission has found that Australia's program of tariff reductions and domestic economic reform contributed to the high productivity growth experienced in the 1990s (PC 2005).

Applying these general conclusions to the particular case of bilateral agreements, the CIE (2004a), as part of the study into the AUSFTA, modelled some of the potential benefits from such dynamic productivity improvements (through an assumption of induced productivity improvements). Overall, dynamic productivity benefits were estimated to account for somewhere between 5 to 10 per cent of the net gain from the agreement.

However, the emergence of *dynamic* productivity gains is not universally accepted. For example, in a critique of the CIE approach, Quiggin observed:

The first assumption relates to the so-called 'dynamic productivity gains', supposed to arise from trade liberalization. Belief in these dynamic gains is something of an article of faith for Australian supporters of microeconomic reform. They are undeterred by the fact their position is inconsistent with mainstream economic theory, and unsupported by empirical evidence. (Quiggin 2004, p. 70)

Others have adopted a more cautious view. In reviewing submissions and modelling commissioned for the Senate *Select Committee on the Free Trade Agreement between Australia and the United States of America*, the committee in its findings suggested that given the uncertainties involved, such benefits should not be considered when making policy decisions:

It is clear to the Committee that the CIE's estimates of the dynamic benefits of the AUSFTA should, at the very least, be treated with a great deal of caution and scepticism. Instead, the Committee should follow the approach recommended by Dr Dee and Dr Brain, and indeed by Treasury in previous inquiries. The Committee recognises that dynamic effects may result, and may have substantial benefits. However, as Professor Garnaut points out, they may not. Policy decisions in relation to the FTA should therefore be made principally on the basis of the direct effects, with the recognition that dynamic effects may eventuate. (SCFTAAUSA 2004, p. 205)

Some commentators have also been sceptical of the potential for trade-related productivity gains to arise from preferential agreements. For example, Sally (2010) states that, to date, preferential agreements within Asia have had limited success:

In short, with few exceptions, Asian FTAs are not strong enough to change existing national practice in a liberalising or trade-facilitating direction. (p. 7)

Despite the debate over the nature of the benefits, there has been little empirical research that sheds light on the economic integration actually achieved under BRTAs, and to what extent agreements are likely to yield benefits, such as the dynamic productivity gains often associated with trade liberalisation.

A couple of examples exist in assessments of US agreements — the United States-Canada Free Trade Agreement and NAFTA. Trefler (1999) examined, amongst other effects, the influence on productivity of the United States-Canada Free Trade Agreement. The tariff cuts associated with the agreement were found to increase labour productivity in the manufacturing sector by 0.6 per cent per year for the sector as a whole. Polaski (2006) also suggested that NAFTA played a role productivity improvements in Mexico, due to the extent of the tariff reductions involved. On this matter, Hornbeck (2004) cited research which suggested Mexico's productivity levels would be 4 to 5 per cent lower in 2002 were it not for its involvement in NAFTA.

However, in the Canadian Government's *NAFTA@10* review, Harris (2006) cautioned:

The productivity effects of the FTA have been the most controversial of the ex post FTA results after employment. (p. 25)

Reviewing a number of studies, Harris (2006) examined the productivity changes related to increased specialisation and scale, and those related to variety and the price of goods and services. On the former, Harris observed that a number of studies provided evidence that suggested that NAFTA had increased the specialisation of firms, and thus was likely to have also increased productivity. On the latter, Harris found that the evidence was not as strong.

The *NAFTA@10* study also included the work of Gu and Rennison (2006), who examined the impact NAFTA had on export and import industries. The authors found that NAFTA had increased productivity in these sectors relative to previous growth paths and other sectors. Overall, total factor productivity improvements in the NAFTA period were 1.8 and 1.9 per cent greater annually for export and import industries respectively.

In this study, the Commission used the GTAP model to investigate the potential gains from FDI led productivity improvements. FDI is often thought to embody technical change, which is likely to improve the productivity of the industry in which it occurs. Following the investment scenario presented in chapter 9, a productivity scenario was modelled through a 5 per cent productivity improvement accruing to industries in Australia and the United States in proportion to their use of FDI from

Australia and the United States in the preferential case. In the non-preferential case, the improvement was applied to all industries using FDI from any source.

The addition of a productivity improvement embodied in FDI flows would increase the potential for gain from lowering barriers to FDI, from levels otherwise achievable (table 10.1). For Australia, a hypothetical 5 per cent improvement in productivity by FDI activities is projected to raise the potential benefit of non-preferential investment liberalisation (by US\$103 million in the scenario considered). A similar productivity improvement, but associated with preferential liberalisation, is projected to deliver a lesser benefit (US\$72 million). The net effect of preferential liberalisation is, however, potentially negative for Australia in this hypothetical example, because Australia is a net importer of capital from the United States — the trade agreement partner (see chapter 9).

Table 10.1 Potential gains from productivity improvements due to increased FDI

US\$ million

	<i>Australia</i>		<i>United States</i>	
	<i>GDP</i>	<i>GNP</i>	<i>GDP</i>	<i>GNP</i>
Incremental impact of an FDI-induced 5 per cent increase in productivity ^a				
Preferential	82	72	20	23
Non-preferential	115	103	407	382
Net impact of reduced barriers FDI and 5 per cent rise in productivity				
Preferential	140	-97	66	413
Non-preferential	507	424	6383	5390

^a Productivity shocks were applied at the industry level in proportion to each sector's FDI content. The FDI intensity is higher in Australia than in the United States.

Source: Commission estimates.

Freer movement of labour

Closer integration between economies can also arise through policies that provide for the freer movement of labour. Such policies can have a variety of impacts, for the employees relocating, their country of origin (the donor country) and the receiving (or host) country.

As noted in chapter 3, the GATS defines international services trade into four modes, where mode 4 involves a business supplying a service in another country through the presence of a natural person overseas. Mode 4 is generally seen as covering:

-
- a business in one country sending employees to another country in order to provide a service directly;
 - independent service providers selling a service to a company or individual in another country; and
 - a person employed overseas by a foreign business established in the host country.

While not strictly a form of mode 4 trade, people may also travel overseas to work for a domestic firm in a host country, such as under a temporary skilled or unskilled migration program. Such movement of people can be distinguished from permanent migration on the basis that those employees will eventually return to their country of origin. However, there is no formal definition of ‘temporary’ migration, and therefore such arrangements may in practice be for many years.

As noted in chapter 4, Australia has a visa system that enables Australian businesses to temporarily bring labour into Australia (through the 457 visa program), subject to meeting certain conditions, and it is not uncommon for other countries to operate similar systems. In addition to domestic policy settings and preferences, partner countries can include provisions that recognise these conditions and relax them on a preferential basis through BRTAs. Most of Australia’s BRTAs contain concessions by the partners regarding the movement of business people (including managers, executives, specialists or other technically-skilled personnel) into their countries and can also contain specific concessions. For example, Australia agreed to specific concessions for the entry of Thai chefs as part of TAFTA.

As well as provisions agreed in BRTAs, countries can liberalise restrictions on labour movement unilaterally or in coordination with other countries. For example, APEC has developed provisions to ease the movement of business personnel between member nations. The APEC Business Travel Card Scheme allows accredited business people to obtain multiple short-term business visitor visas to participating nations. Further, card holders can access streamlined process lanes when travelling through immigration arrival or departure (Department of Immigration and Citizenship 2010). Similarly, while the AUSFTA does not contain any commitments by the United States on the movement of natural persons, the United States separately agreed to introduce a special visa category — the ‘E3’ — for Australians temporarily engaging in certain forms of work in the United States.

The economic literature suggests that relaxing restrictions on the movement of labour between countries can have a range of benefits. They can enable eligible workers, particularly from less developed countries, to earn higher wages in other countries (some of which may be remitted home). Working abroad can enable

workers to acquire new skills and technological know-how that on return can improve productivity in the donor country. And the prospect of better employment opportunities abroad may result in greater numbers of people pursuing education, again improving productivity in the donor country. That said, in some cases, such as where a highly-skilled employee temporarily transfers from one developed country to work in another, the benefits for the employee and the host country will be largely offset by the loss of employment resource and associated output in the donor country. Nevertheless, at a global level, measures to facilitate the movement of people may improve efficiency through the better use of labour resources, including allowing better matching of employee skills with labour needs in different markets and overcoming labour bottlenecks or shortages in particular countries at particular times (Winters 2002).

Indeed, the trans-Tasman labour movement provisions in the CER agreement are often seen as having helped address short-term imbalances in both the Australian and New Zealand labour markets, particularly at times when the countries have been at different points in the business cycle. The BCA said that Australian businesses had seen ‘deliverable and practical benefits’ from such provisions in BRTAs, although it noted that the extent of liberalisation varied between agreements:

... CER, through the Trans-Tasman Travel Arrangement has achieved almost complete labour mobility between Australia and New Zealand. Provisions for the cross border movement of business persons in AANZFTA, SAFTA, TAFTA and CAFTA tend to improve on commitments made under the WTO, but they remain linked to immigration requirements and are restricted to business personnel, investors and certain categories of workers such as service professionals. (sub. 41, Attachment 1, p. 18)

The BCA also indicated that benefits had arisen from increased labour mobility as a result of the visa initiatives agreed with the United States (sub. 41, p. 2). Indeed, at a policy forum on the Draft Report, one business participant estimated that the E-3 program could result in as much as \$6 billion per annum of business in the United States.² However, while the E-3 program has undoubtedly delivered benefits for some Australians, it is unlikely that there have been major benefits to Australia in net terms from the program to date. This is because the take-up of E-3 visas has to date been limited, and may have involved some substitution away from other means of servicing the United States market.³ And to the extent that there has been a net

² ‘E-3’ visas are valid for up to 2 years for an Australian working for a US business, and are subject to an annual quota of 10 500. The estimate was based on an assumption that there were 12 000 E-3 visa holders, earning on average half a million dollars each per year in the United States. Data is not available, however, on the incomes earned by E-3 visa holders while in the United States, nor on what proportion of those incomes might be repatriated to Australia.

³ Determining the extent of any increase in Australian’s supplying the United State market, consequent upon the E-3 program, is difficult. Australians may enter the United States for work

increase in Australians supplying the US market, this will have entailed a transfer of Australian labour resources (and associated output) to the United States market from the domestic or other export markets.

While measures that facilitate the cross-border movement of labour can generate benefits for some workers and, potentially, for the donor and/or host country, some participants submitted that the inclusion of such matters in a BRTA is inappropriate. For example, the CPSU stated that:

Our position on labour mobility begins with the principle that people are not commodities and cannot be traded. There is no place for agreements about movement of natural persons... (sub 22, p. 4)

Others suggest that such provisions can have a negative impact on Australia's domestic labour market, through the greater use of foreign skilled workers in place of domestic employees. For example, the CFMEU argued that because Australia's commitments under some of its BRTAs preclude the use of labour market testing, they amount to:

...a significant downgrading of the rights of Australian workers to jobs within Australia, ahead of foreign nationals,... [a development that] is proceeding with little or no public debate. (sub. DR90, p. 9)

More broadly, the CFMEU acknowledged in its submission that while there had been changes to the 457 visa program (sub. DR90, p. 9), it still considered that the movement of labour was an issue for immigration policy, stating:

The Commonwealth government has given top priority to employer-sponsored PR [permanent residency] visas in its skilled migration program, and over one half of all 457 visa holders now seek PR. (sub. DR90, pp. 9–10)

Overall, some of Australia's BRTAs to date have relaxed the conditions on the movement of labour and business personnel, with the CER agreement providing the least restrictive conditions. The freer movement of labour and business personnel can afford advantages to Australia, including providing opportunities for

purposes under a number of different visa classes, depending on the type of work and duration of stay. The general H1-B work visa offers similar conditions to Australia-specific E-3 visa, and there may have been some substitution away from the H1-B after the E-3 visa was created. For example, in 2004, approximately 1600 Australians were granted H1-B visas. In 2009, this had fallen to 442, while 2191 E-3 visas were issued (US DHS, 2009). In addition, Australians may travel on the short-term B1/2 visa, and intra-corporate transferees may work in the US under the L-1 visa system. That said, determining the extent of substitution between different visa classes is confounded by other factors, such as changes in economic conditions in different countries, that may affect the propensity of Australians to pursue work in the United States. It is also possible that any increase in Australians supplying the United States market in person might be at the expense of other modes of supply, such as cross-border supply.

Australians wanting to work abroad and providing means of obtaining additional labour in Australia to provide specialist skills and address bottlenecks. However, the net benefits arising from such provisions can be overstated, and there are concerns relating to the general system of labour mobility, its relationship to immigration policy and its extension on an ad hoc basis through BRTAs. Chapter 14 considers in further detail the need for greater analysis of such matters before they are included in a BRTA.

The possible contribution of BRTAs to regional integration

While there is a range of potential benefits from economic integration between partners to a BRTA, given that at least for preferential bilateral agreements, the direct impact on overall trade flows and GNP is small (see chapters 8 and 9), the integration effects of agreements are also likely to be small. Even where an agreement has strong integration potential, such as ANZCERTA, stimulus to bilateral trade flows and hence integration between partner economies is likely to have been at the expense of some reduced flows to global trading partners.

Against this background, debate exists over the role that BRTAs can play in respect to broader regional integration — that is, with a range of trading partners, both members and non-members to a particular BRTA. Where BRTAs contain discriminatory provisions that exclude regional parties, such as those of preferential bilateral agreements, they necessarily work against regional integration. However, a regional trade agreement could potentially be used to further regional integration (as inferred by changes in trade flows). On this, empirical evidence suggests that larger regional and non-preferential agreements have had a greater trade creating impact (both for members and non-members) and thus have a greater potential to contribute to broader regional integration.

The ASEAN agreement, and the recent AANZFTA along with the APEC agreement, are generally regarded as more open than other BRTAs seen worldwide. Given the less or non-preferential nature of these agreements, the scope for economic integration to occur at a regional level also increases. For example, some see potential for future BRTAs to contribute to regional integration. The BCA argued in the context of ASEAN that:

It is important that Australia is part of a regional trade and investment architecture which involves ASEAN. That should be supported by FTAs which deepen economic integration and foster policy reform to reduce regulatory barriers in ASEAN economies. (sub. 41, Attachment 1, p. 8)

Further, the BCA felt that BRTAs would be able to facilitate the achievement of these benefits in future:

FTAs will continue to be the driving force for economic integration in the Asia-Pacific region for some time. ... there is an opportunity for Australia and like minded economies to lead in the standard setting of FTAs and to highlight the importance of US engagement in the region. The TPP — involving Chile, New Zealand, Brunei, Singapore and now Australia, Peru, Vietnam and the US — will be important for doing so. (sub. 41, Attachment 1, p. 21)

Others, however, were sceptical of the role of BRTAs. Malcolm Bosworth and Ray Trewin, for example, put that:

... trade policy in Asia is currently very unbalanced, relying too much on weak and partial FTAs which will not liberalise where it matters and thus not be a driving force for regional or global integration. (sub. 32, Attachment 2, p. 54)

In a similar vein, Sally (2010) states that to date, BRTAs have had limited success:

... with few exceptions, Asian FTAs are not strong enough to change existing national practice in a liberalising or trade-facilitating direction. Clearly, they have not proved to be a force for regional integration — at least not so far. Nevertheless, FTA proponents argue that they are stepping-stones to wider regional-integration initiatives. (p. 7)

Further, the barriers that exist today, and the treatment of sensitive sectors, will continue to prove a stumbling block for BRTAs to yield regional integration:

Therefore it is pie-in-the-sky — psychedelic cloud-nine politics — to expect very large group cooperation to produce a strong, clean, comprehensive FTA in Asia — not for a long time to come. It will take Herculean policy-making to iron out wide differences in tariff rates, treatment of quantitative restrictions, sectoral exemptions, ROOs and other provisions spread across so many bilateral and plurilateral FTAs, and fold them into a sensible regional FTA. Rather the result is likely to be a very low common denominator — another trade-light FTA with complicated ROOs, adding to (not subtracting from) an expanding noodle bowl. Finally, such FTA activity distracts attention from further unilateral liberalisation and domestic reforms ... That will probably hinder, not help, the cause of regional economic integration. (Sally 2010, p. 12)

Notwithstanding these comments, there has been considerable progress reaching convergence in areas such as rules of origin (RoO) within the East Asia region. For example, the ASEAN Trade in Goods Agreement and the ASEAN agreements with Australia and New Zealand, Japan and Korea all involve a co-equal approach of a 40 per cent regional value content or 4-digit change in tariff classification based RoO. The Commission also notes that further work is being undertaken in this area:

... a work program is just beginning which involves the countries of ASEAN, and the six countries (Australia, China, India, Japan, New Zealand and South Korea) with which ASEAN has regional FTAs [which] ... is looking at the ROOs in these FTAs with a view to improve their complementarity and coherence in promoting regional economic integration. (DFAT, sub. DR98, p. 9)

As for economic integration, little literature exists examining the actual outcomes of BRTAs in this area. However, the econometric modelling work conducted by the Commission, set out in chapter 8, provides some evaluation of the potential for BRTAs to contribute to regional integration.

As discussed above, trade openness provides an opportunity for economic integration to occur. If trade openness as a result of a BRTA occurs to goods, services and investment suppliers from both member and non-member countries, then it is possible that agreements will foster *regional* integration (and not just economic integration between partners as would be possible from improved member trade flows). By examining the openness of agreements and how much trade creation occurs between members and non-members, an insight into whether or not BRTAs contribute, through increased trade, to regional integration outside the member base can be gained. While not a direct measure of regional integration, if a significant proportion of trade is created with non-members due to a BRTA, then it is likely that such agreements at least do not create barriers to regional integration.

Examining the estimated ratio of extra-bloc to intra-bloc trade creation from the gravity model presented in chapter 8 and the coverage of agreements, for a range of agreements, reveals a general trend — as the share of intra-bloc to total trade decreases, the ratio of extra-group trade creation to intra-bloc trade creation increases (table 10.2). That is, agreements that cover a greater amount of trade for partners are generally more inward focused, with those covering a lesser amount being more outward focused.

However, the APEC and ASEAN agreements do not fit the general trend. While the share of intra-bloc trade in the APEC group of countries total trade is the largest of the agreements examined, extra-bloc trade creation is estimated to be one third greater than intra-bloc trade creation — compared to the EEC (with a share of intra-group imports of 45 per cent) where extra-group trade creation is one fifth of the estimated intra-group trade creation.

Similarly, while the share of intra-group trade in the ASEAN group of countries' total trade is 13 per cent (in between the share of intra-group imports of United States–Canada at 18 per cent and MERCOSUR at 10 per cent), the estimated extra-group trade creation is more than three times that of the intra-group trade creation (in comparison with approximately nine tenths and one to one for the United States–Canada and MERCOSUR agreements respectively).

Table 10.2 Ratio of extra-bloc to intra-bloc trade creation and agreement coverage, 2008

11 selected agreements

<i>Agreement</i>	<i>Ratio of extra-bloc trade creation to intra-bloc trade creation in 2008</i>	<i>Share of intra-bloc trade in total trade (average)</i>
	Ratio	Per cent
EEC	0.18 : 1	45
NAFTA ^a	0.34 : 1	28
United States–Canada	0.92 : 1	18
MERCOSUR ^a	0.98 : 1	10
APEC	1.37 : 1	50
Andean	2.20 : 1	4
ASEAN	3.48 : 1	13
LAIA	4.44 : 1	8
CEFTA	9.10 : 1	6
CACM	36.25 : 1	8
EFTA	62.48 : 1	2

^a NAFTA and MERCOSUR are also estimated to have a trade diversionary effect; the ratio of extra-bloc to intra-bloc trade creation excludes this trade diversionary effect.

Source: Commission estimates.

These results suggest that open regional agreements, such as APEC and to a lesser extent ASEAN, have the potential to promote regional integration. In comparison, while a large agreement, NAFTA is not an open one, and while its inward focus is by design, it is not likely to foster broader regional integration outside its member base, and may even inhibit it through its trade diversionary effects (see chapter 8).

The impact that a trade openness focus can have on promoting trade flows with non-members, and thus a greater scope for regional integration is further evidenced by examining the Central American Common Market (CACM) in its two incarnations. Initially launched in 1960, the agreement was formulated to foster import substituting industrialisation or closed regionalism. Following a regional crisis in the mid-80s, it was relaunched in the early 1990s as a model of open regionalism (Bulmer-Thomas 1998). The estimated ratio of extra-bloc trade creation to intra-bloc trade creation for the agreement following its relaunch in 1993 is significant at 36:1. For the precursor incarnation, the estimated ratio of extra-bloc to intra-bloc trade creation for the agreement modelled from 1960 to 1985 is significantly lower at 3:1.

Despite the paucity of evidence, it is likely that, overall, the degree of regional integration achieved will depend on the scope of these agreements to non-

discriminatorily reduce barriers and open trade. Available evidence suggests that both APEC and ASEAN have at least been partly successful in doing this in the trade-in-merchandise-goods area. However, as cautioned by a number of commentators above, this scope is limited by both the exclusion of sensitive sectors and the continued proliferation of bilateral preferential agreements.

10.3 Summing up

This chapter examined two broader impacts from BRTAs — those related to direct and indirect reforms to domestic regulation, and those related to economic and regional integration.

For Australia, those domestic regulations that have been incorporated in BRTAs, in particular AUSFTA, have resulted in mixed outcomes. While the extension of copyright provisions (in particular, for existing works) has clearly imposed a net cost on the Australian economy, the relative costs and benefits of other provisions are less clear. Despite this, as seen in the case of the PBS, there are significant potential risks to incorporating certain domestic regulations in trade agreements. For those with a domestic public good focus (such as the PBS), the inclusion in trade agreements has the potential to impose costs beyond the benefits that can be obtained and reduce economic welfare (even though, in the PBS case, the outcome appears to be reasonably benign and even positive).

In terms of integration, possible outcomes are mixed. On the one hand, economic integration can occur between members to an agreement. Additionally, bilateral agreements may evolve into larger agreements and, over time, become a means to achieve wider economic integration. For example, the Canada-US bilateral agreement can be seen as a predecessor to the broader NAFTA agreement. On the other hand, as discussed in chapter 13, little use has been made of accession clauses to expand existing agreements. Further, the extent of broader regional integration (as observed in trade flows) and the economic benefits that arise depend on the openness of the agreement in question. In particular, the Commission's econometric analysis suggests that, insofar as they focus trade towards a partner country, preferential agreements can detract from broader regional integration, while agreements based on open regionalism, such as APEC and to a lesser extent the previous ASEAN-CEPT agreement in the Asia-Pacific, appear to foster economic and regional integration.