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## 12 Future approaches to trade liberalisation and the role of BRTAs

The terms of reference request the Commission to analyse the role of bilateral and regional trade agreements (BRTAs) in reducing trade and investment barriers both in Australia and other countries, and in promoting regional integration. In this context, as noted in the previous chapter, BRTAs are one of several options available to governments to achieve these goals. Based on the analysis in part C and chapter 11, this chapter considers what form of trade liberalisation mechanism (or mix of mechanisms) potentially provides the greatest net benefits to the community. Section 12.1 looks at unilateral reform, section 12.2 at multilateral reform and 12.3 at the role for bilateral and regional agreements.

### 12.1 Unilateral reform

Over the last three or so decades, Australia has gained significant economic benefits as a result of programs of unilateral reform, which entailed reducing domestic trade barriers without the need for any specific international engagement (Banks 2010). The Commission considers that continued unilateral reform is the most productive option for achieving the objective of lower domestic barriers to trade and investment as it provides the most direct means of delivering the benefits of trade to Australian consumers, businesses and the economy more broadly.

As the Commission has stated previously, domestic liberalisation also secures the majority of benefits available from trade liberalisation, regardless of existing trade and investment barriers abroad (see, for example, PC 2001). Of course, the proportion of a country's gains that arise from domestic liberalisation will depend on the level of existing barriers. That is, the lower the domestic barriers, the larger the relative gains from foreign, rather than domestic, reductions.

While Australia's previous unilateral reform efforts have reduced tariffs substantially, even at current tariff levels the preliminary modelling conducted as part of this study (chapter 8) suggests that the majority (approximately 60 per cent in the simulations undertaken (table 12.1)) of the gains in GDP available to Australia from tariff reductions are likely to arise from unilateral reform. The modelled gains from further unilateral reform are substantially larger than the

estimated gains possible from the full bilateral tariff reductions modelled in relation to Thailand and the United States — countries with which Australia has recently entered bilateral trade agreements.

**Table 12.1 Simulated aggregate effects of reducing tariffs to zero**

<i>Simulation</i>	<i>GDP-Australia</i>	<i>Share of potential world gain</i>
	Per cent change	Per cent
T1. Australia-small country <sup>a</sup>	0.05	5.7
T2. Australia-large country	0.12	12.4
<b>T3. Australia unilateral</b>	<b>0.56</b>	<b>59.5</b>
T4. Stylised APEC	0.86	91.7
T5. World	0.94	100

<sup>a</sup> Simulations are representations of the effects of the removal of barriers to trade. T1 Represents zero tariffs on all trade between Australia and a small country, T2 on trade between Australia and a large country. T3 simulates unilateral liberalisation as the removal of tariffs on all imports into Australia. T4 simulates zero tariffs on imports into all APEC countries and T5 simulates zero tariffs worldwide.

*Source:* Simulation results.

Australia also stands to gain if barriers in other countries are reduced, an objective that domestic reform is unable to (directly) affect. As such, while unilateral reform affords the greatest potential benefits in terms of reducing domestic barriers, in terms of an overall approach to trade policy, multilateral agreements or BRTAs can yield additional benefits by providing frameworks for trade and investment between countries and for coordinated reductions in trade and investment barriers. It is the interaction of unilateral reform with these other agreements that raises a potential policy issue, discussed below.

### **‘Bargaining coin’ issues**

Where there exists further scope for the pursuit of trade agreements, the issue arises as to whether Australia should delay or withhold otherwise beneficial domestic reforms in order to retain ‘negotiating coin’ to offer in future trade agreements.<sup>1</sup> The issue arises from the perception that, while Australia gained significant domestic benefits from the unilateral reform already undertaken, as a result, it has little negotiating coin left.

<sup>1</sup> In addition to BRTA negotiations, this argument also applies to WTO negotiations that are normally undertaken on the basis of ‘bound’ restrictions rather than applied levels. As the Commission has previously noted, ‘[w]here “negotiation coin” can come from the binding of liberalisation already undertaken, there is no benefit in delaying liberalisation.’ (PC 2001, p. 5)

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However, given Australia's relative size in international trade, there is some scepticism about the ability of any remaining negotiating coin to 'buy' valuable concessions from partner countries:

... Australia already has low applied tariff rates, which indicates that it's not the economic benefits of greater market access that attract countries to form PTAs with Australia. (RIRDC, sub. 10, p. 12)

Australia is a small player in international trade and its economy is already among the most open in the world, leaving our trade negotiators little to offer by way of 'concessions' to lure potential negotiating partners to the table and to induce them to make good offers. (Capling and Ravenhill 2008, p. 2)

Further, some contend that unilateral reform does not necessarily impede the pursuit of reduced barriers in other countries through the use of trade agreements:

Australia's ability to pursue the reduction of barriers to our exports has been heightened when Australia has itself pursued an ambitious economic reform agenda domestically. This is for two reasons. First, such reform enables the economy to be more competitive and thereby enables economic actors to be able to compete in global markets. Second, it provides a valuable demonstration effect. Domestic reforms give Australia credibility in trade negotiations. Agreeing to bind such reforms provides useful negotiating coin. (DFAT, sub. 53, p. 3)

Where a demonstration effect and the binding of existing reforms can be used in negotiations, there may not even be a 'trade off' between further unilateral reform and further bilateral, regional, or multilateral reform.

Indeed, an important consequence of Australia's approach to unilateral reform is that reductions in tariff rates have not always been 'bound' to the same extent in Australia's WTO schedule; meaning that, in effect, this form of bargaining coin has been preserved. For example, while the current applied tariff rate for imported motor vehicles is five per cent, Australia's bound rate for vehicles is 40 per cent.

Regardless of the effectiveness of various forms of negotiating coin, unilateral reform has a number of features that commend it over reliance on retaining existing impediments to trade as negotiating coin for trade agreements. First, the ability to undertake unilateral reform is a decision solely for the Australian government, and thus is more certain (and can be implemented sooner) than reforms that may come out of a negotiation process with one or more partner countries. Second, it is possible that countries may agree to an outcome under a trade agreement, only for the effective gains to be diminished by later domestic actions from partner countries. Third, the negotiation process itself comes at a cost (chapter 7).

Moreover, there are still pockets of protection and unnecessary regulation in the Australian economy where domestic reform can offer considerable gains (for

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example, in relation to the Foreign Investment Review Board). The case for delaying reform of such policies in the name of retained bargaining coin is particularly weak.

Overall, the Commission's assessment is that beneficial unilateral reforms should be identified and pursued as part of normal Australian policy processes, and not delayed on account of bargaining coin considerations that may be claimed for possible future negotiations.

In this context, the Commission notes that as part of the last *Review of Australia's General Tariff Arrangements*, conducted in 2000, the Commission recommended that existing general tariffs (those at 5 per cent or lower) should be removed as soon as possible (PC 2000). The Commission in subsequent studies has reaffirmed the benefit of this course of action (PC 2003, 2005 and 2009c). In light of the time that has elapsed and the estimated gains available, the Commission's assessment is that there would be merit in the government revisiting this issue.

Similarly, the Commission notes the modeling conducted in chapter 9 of this study indicated that moving from preferential to non-preferential reductions in barriers to investment under the Foreign Investment Review Board (FIRB) processes could afford benefits to Australia. Previous work by the CIE (2004a) and others also reported significant benefits (though there was contention over the magnitude). Given that it was deemed to be appropriate to extend these reductions to investors from the United States, the question arises as to why it is not appropriate to extend them to others, and why such further reform should be delayed. In this context, the Commission notes that Australia is currently negotiating with New Zealand to conclude an ANZCERTA Investment Protocol, which will include lifting the screening thresholds to \$953 million (in 2009) for New Zealand investors (Rudd and Key 2009). As such, the Commission's assessment is that the issue of extending these reductions on a non-preferential basis also merits examination by the government.

#### RECOMMENDATION 8

***The Australian Government should examine the potential to further reduce existing Australian barriers to trade and investment through unilateral action as a priority over pursuing liberalisation in the context of bilateral and regional trade agreements. The Government should not delay beneficial domestic trade liberalisation and reform in order to retain 'negotiating coin'.***

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## 12.2 Multilateral reform

As illustrated in table 12.1 (above), the largest potential gains to Australia come as a result of multilateral trade reform. To date, efforts at multilateral liberalisation have been pursued through the GATT and WTO institutions (chapter 4).

### The current state of WTO negotiations

As discussed in chapter 4, the WTO's Doha Round of negotiations, which commenced in 2001, is yet to be concluded. Participants in this study put forward several reasons for this, for example:

[W]ith 153 members, progress on more far-reaching trade liberalisation through the WTO, Doha Round has been frustratingly slow. By attempting to overload the WTO with non-trade issues that are not directly relevant to its objectives (e.g. environmental, animal welfare and labour standards, landscape management, food security and the socioeconomic viability of rural areas), some members are not helping this situation. These elements only act to distract the WTO mandate and weaken its capacity to deliver on trade reform. (National Farmers' Federation, sub. 13, p. 8)

The negotiations collapsed over issues of agricultural trade between the United States, India and China, in particular, disagreement between India and [the] United States over the agricultural special safeguard mechanism. (Government of South Australia, sub. 56, p. 7)

In light of the current situation, there are differing views on the prospects for conclusion (with meaningful gains) on the topics under negotiation in the Doha Round being reached in the short term. The WTO itself acknowledges that progress has been slow, but is still committed to working towards a conclusion for the Doha Round, as Director-General Pascal Lamy recently stated:

... although we have made some progress since 2008, there is no denying the fact that we are not where we wanted to be by now. ... Everyone agrees that no miracle solution is available to us at this point in time.

[However] ... Everyone is still very much committed to the mandate of the Round and to its successful conclusion. ... While there is certainly disappointment that we are not closer to our goal, I have not detected any defeatism. (WTO 2010c, p. 1)

Some participants in this study were also optimistic about the conclusion of the Doha Round:

Multilateral liberalisation under the auspices of the Doha Round will likely be realised; but at this point in time it is hard to say what the scope and pace of liberalisation will be. However, RIRDC sees the issue as not so much whether multilateral liberalisation will be realised, but when. (RIRDC, sub. 10, p. 4)

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Others were less confident about the prospects of multilateral reform:

The Doha Round has failed, and what we are left with is to decide whether to have its funeral or push on to finalise an agreement that is already so badly compromised through negotiations that it is worth very little, and certainly no recipe for trade liberalisation and transparency. While inherent weaknesses in the WTO system, including a far too wide an agenda and diverse membership, have no doubt contributed to this situation, there is little doubt that governments' growing pre-occupation with DTAs has been a major factor. (Malcolm Bosworth and Ray Trewin, sub. 32, p. 2)

The outcome of the WTO Doha Round is unclear. It is unlikely it will be concluded this year. Maintaining the integrity of the WTO is crucial for the future of the multilateral trading system. While concluding the Round would give an important boost to that, it is equally imperative that developments in the trade architecture do not undermine further efforts to continued trade and investment liberalisation. (Business Council of Australia, sub. 41, Attachment 1, p. 9)

Though some momentum was re-built through the WTO's Seventh Ministerial Conference held in Geneva in December 2009 where all members committed to the common objective of concluding the Doha Round in 2010, substantive progress has been slow and the prospects of an expeditious breakthrough in the near future are not particularly bright. (Government of South Australia, sub. 56, p. 7)

Based on the views expressed to date, it is apparent that the Doha Round has, for the present, stalled. While this means that some other actions may be necessary if trade liberalisation is to be pursued in the short term, it does not mean that the Doha Round is 'dead'. Indeed, efforts to conclude the round should be maintained in order to build on work done so far, particularly given the potential gains at stake:

... successful conclusion to the Doha Round, involving as it does 153 WTO members, has the potential to deliver an outcome which is more commercially significant than is possible via any FTA. (DFAT, sub. 53, p. 46)

The Commission notes that DFAT has stated that the conclusion of the Doha Round negotiations 'remains the Australian Government's highest trade policy priority' (sub. 53, p. 3) and supports the continuation of this approach.

Further, it is important that any actions taken in the interim serve to bolster, rather than undermine, the multilateral trading system. While BRTAs are one option that can be pursued at the same time as ongoing WTO negotiations, their effect on the multilateral trading system is the subject of some debate (chapter 6). As such, actions that can be pursued that would more clearly support the prospects for multilateral liberalisation should also be considered.

In the course of this study, the Commission has examined courses of action that could be pursued to support the multilateral trading system under the WTO.

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## **Strengthening WTO requirements for trade agreements**

As discussed in chapter 4 (box 4.2), trade agreements that would otherwise breach the ‘most-favoured-nation’ requirements of the WTO are permissible under GATT Article XXIV provided that (among other things) they apply to ‘substantially all trade’. The WTO also aims to add transparency to the formation of trade agreements by requiring that they are examined by the Committee on Regional Trade Agreements (CRTA). Given the recent proliferation of trade agreements, rules governing their interaction with the multilateral system take on a heightened importance. However, the present rules appear to be having little effect, as ‘substantially all trade’ remains undefined and the CRTA has yet to finalise an examination report since it was established in 1996. Following the Draft Report, some participants called for a greater focus on disciplines within the WTO:

... Australian policy makers should be implored to redouble their efforts to bring PTA’s under multilateral surveillance and discipline in the WTO. Article XXIV of GATT, The WTO Understanding on Interpretation of Article XXIV and GATS Article V all need elaboration ... (Graeme Thomson, sub. DR82, p. 2)

The Commission understands that Australia is already taking action in this area (box 12.1). It is clear that there are difficulties involved in this process, such as the number of parties and interests involved and Australia’s ability to influence change in multilateral settings. Further, as has been the experience with multilateral reform generally, it is likely that real outcomes would only be reached over a longer time frame.

Nonetheless, given the potential benefits to the multilateral system, and in line with recommendation 6.1 of the Mortimer review, the Commission endorses the action already taken and believes that the Australian Government should continue in its efforts to improve the RTA transparency mechanism at the WTO.

## **Domestic transparency measures**

It is widely acknowledged that a fundamental obstacle to international trade reform is political resistance within each trading country. The GATT (and WTO) was originally conceived as a means of creating explicit export winners from domestic liberalisation through the reciprocal concessions provided by trading partners, thus helping to balance the political opposition of perceived ‘losing’ industries on the import side. This logic also extends to reciprocal concessions within bilateral trade and regional agreements, where the potential exporting beneficiaries can also sometimes be more clearly identifiable. But the experience over a long period has been that the domestic import-competing interests remain the dominant influence.

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This is largely because there is more at stake for them than the relatively dispersed or uncertain ‘winners’ from domestic liberalisation, who typically also lack information about the gains, to them and the wider economy, from trade reforms. The upshot is that countries generally approach international trade negotiations as exercises in obtaining maximum concessions in foreign markets, while at the same time minimising their own. This is not conducive to rapid agreement or sustainable progress. Thus, as noted, the Doha Round has now been going for over nine years, with no conclusion in sight, while Australia’s negotiations with China are five years old.

**Box 12.1 Australian advocacy of improved WTO scrutiny of RTAs**

Australia has been active in advocating improvements in the WTO processes for trade agreements under GATT Article XXIV. In regard to adding transparency to the formation of agreements, DFAT submitted that:

Australia has played a central role in this area of the Doha Round as it sees greater clarity with respect to the rules as helping to guard against low quality agreements, which would ultimately be to the detriment of the WTO.

... The [negotiations to enhance transparency have] produced a positive result, with an RTA transparency mechanism having been agreed (and applied) provisionally in late 2006. Australia seeks to ensure that the mechanism, under which WTO members have agreed to subject all FTAs (including those agreements notified under the enabling clause) to a standardised notification, reporting and review process, will be permanently adopted as part of a final Doha Round package. Australia is a leading advocate on RTA standards and transparency in the WTO. (sub. 53, pp. 47–48)

Australia has also been active in working towards a definition of ‘substantially all trade’, although this issue:

... has been much more contentious and little progress has been made. Australia has been one of the most active participants in these negotiations submitting a number of formal detailed proposals on the question of substantially all trade. At the core of Australia’s submissions was a quantitative benchmark, which would require an RTA to eliminate tariffs on at least 95 per cent of tariff lines in order to meet the substantially all trade requirement.

In the absence of any real prospect of agreement to a rigorous definition of substantially all trade, the current focus in the Doha Round negotiating group on rules is shifting to a possible forward work program on RTAs. Australia is considering such a work program as a means of building on the success of the transparency mechanism and informing future consideration of the substantially all trade issue. (sub. 53, p. 48)

These essentially political obstacles to reform are not easily overcome, but could be ameliorated through the use of more transparent policy processes within each country to shed light on the economy-wide effects of reform. As the Commission has previously noted:

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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. (PC 2007, p. 4.8)

These insights are of course not new, and have been raised in international forums since the mid-1980s. For example, institutional requirements to this end were considered in some detail by a study group chaired by Olivier Long, former Director-General of the GATT (Long, 1987). The Long Report concluded that the fragmented administrative arrangements found in most government bureaucracies had compounded the undue influence of industry groups resisting reform:

The achievement of an economy-wide, long-term perspective in trade policy requires that influences wider than those associated with claimant industries should be brought to bear on the policy-making process. This will not occur on its own. It depends on having procedures that provide for public scrutiny of protective action and that promote domestic understanding of its effects. We call this ‘domestic transparency’ – open, informed policy-making. (Long 1987, p. 21)

The report proposed that an agreement be negotiated within the then Uruguay Round on a code which would establish some broad design principles for domestic ‘transparency institutions’(citing the then Industries Assistance Commission in Australia as one example). This was carried forward within the negotiating group on the ‘Functioning of the GATT System’, but was ultimately displaced by efforts to create the Trade Policy Review Mechanism. While this constructive initiative has enhanced awareness and scrutiny internationally of WTO members’ trade policies, its effectiveness in shaping those policies is inherently limited by the fact that it is external to the domestic policy-making environment.

In the context of the present review, a group of prominent Australian and New Zealand businessmen and economists have reasserted the arguments for domestic transparency mechanisms:

Protectionism results from decisions taken by governments at home, for domestic reasons. Any response to protectionism must therefore begin at home, and bring into public view the domestic consequences of those decisions. G20 leaders should sponsor domestic transparency arrangements in individual countries, to provide public advice about the economy-wide costs of domestic protection. The resulting increase in public

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awareness of these costs is needed to counter the powerful influence protected domestic interests exercise over national trade policies. (sub. 5, Attachment 2, p. 1)

It is recognised that transparency mechanisms in themselves could not guarantee significant gains in the short term. Indeed, in the Australian experience, momentum for reform was only achieved over a long period:

Building a pro-reform constituency in government and the wider community is a gradual process. It took Australia four decades to get tariffs down and more than a decade tackling sources of underperformance in economic infrastructure services. And neither reform program is yet complete. That said, reforms once made in Australia have tended to stick, having stronger foundations of support or acceptance within the community precisely because the basis for reform *was* transparent. (Banks 2010, p. 279)

Thus, the introduction of such mechanisms would not see a speedy resolution to the Doha Round. However, the very difficulties in successfully concluding the Doha Round (as well as some current BRTA negotiations) underline the need to have a better basis for the progress into the future.

In order to pursue this and other possible options to reinforce the multilateral system, the formation of a new international study group has been proposed:

... with membership drawn from private policy institutes in Australia, New Zealand, the US and the EU. ... It will not focus on the Doha Round, but will concentrate on the longer-term options available to improve outcomes from future Rounds of multilateral trade negotiations and to counter the on-going threat of protectionism. (Saul Eslake and Peter Corish, sub. 59, Attachment 1, p. 1)

The Commission was informed that, in response to this suggestion the then Minister for Trade, in March 2010, indicated that he was happy to lend support to a study group of senior business and think-tank representatives ‘... to build on broader efforts to increase the domestic transparency on the cost of protectionism and promote the benefits of trade liberalisation’. (sub. 59, Attachment 2, p. 1)

The Australian Government is well-placed to lend support to such initiatives. The Productivity Commission, the descendant of the Industries Assistance Commission, continues to be cited internationally as one such institutional mechanism to assist structural and trade reform:

The [Productivity Commission] has been an important part of the institutional architecture for regulatory reform in Australia and it provides a model with many features that could usefully be emulated outside Australia in other OECD countries. (OECD 2010b, pp. 99–100)

The New Zealand Government has recently taken steps to establish its own New Zealand Productivity Commission, with the new body scheduled to commence

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operations in early 2011 (English and Hide, 2010). Some other countries have also demonstrated an interest in such institutional arrangements, including developing countries in the Asia-Pacific. At the 2008 APEC Meeting in Melbourne, Ministers agreed to a new ‘structural reform initiative’, noting that:

... robust institutional arrangements and processes are key to driving and achieving structural reforms on an ongoing basis, and that these arrangements and processes require strong support from government. (APEC 2008)

Since 2008, the G20 has assumed a larger role, and has itself promoted the need for increased transparency in some policy areas (G20 2009; 2010).

In sum, the Commission accepts that the cause of international trade liberalisation, whether conducted multilaterally, regionally or bilaterally, would be well served by nations giving greater attention to the domestic institutional requirements for identifying what is at stake domestically from their own liberalisation. Initiatives directed at this end could yield a significant pay off in the longer term and deserve support.

### **Other possibilities for furthering broadly based trade reform**

While it would appear that negotiations to conclude the Doha Round have, at present, stagnated, the potential benefits at stake suggest that efforts to conclude the round should be sustained. Further, it will be important to ensure that trade policy actions contemplated in the interim and in the post-Doha environment serve to support, rather than undermine, the multilateral system.

In this context, there may be merit in the Government weighing up with like minded countries the costs and benefits of a critical mass agreements (CMAs – box 12.2), or other broadly-based mechanisms, to push for reform. CMAs may be one effective mechanism for achieving broad plurilateral agreement in a number of areas. However, the Mortimer review — reporting in 2008 — questioned whether they would be widely subscribed. Of course, it may be difficult to effectively advance a CMA agenda without leadership from nations with significant trading power. This crucial role could be played by leading groups of nations, such as the G20, which could drive substantial progress through CMAs if none were forthcoming through the Doha Round.

Were the use of CMAs to gain momentum, Australia should not necessarily take part in every agreement. As with any sort of agreement, it would be necessary to first analyse any CMA to ensure that acceding to it is in Australia’s benefit.

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### Box 12.2 Critical Mass Agreements

One suggestion for regaining momentum at the international level has been the use of plurilateral agreements (involving a sub-set of WTO members) such as critical mass agreements (CMAs). These agreements (such as the Information Technology Agreement mentioned in chapter 4) come into effect once the signatories account for a designated percentage (90 per cent in the ITA) of world trade in the product in question. Once in effect, they impose obligations on signatories, with the resulting concessions typically offered on a MFN basis by signatories. When a large percentage of world trade has been covered, there can also be a secondary sign-up effect as remaining countries can be reluctant to be 'left behind' in the eyes of markets and investors.

As part of its report on WTO reform, the 2007 Warwick Commission recommended that:

... consideration be given to the circumstances in which a "critical mass" approach to decision-making might apply. The key implication of this approach is that not all [WTO] Members would necessarily be expected to make commitments in the policy area concerned. ... Among the criteria for considering a critical mass approach to defining the agenda are the need to identify a positive global welfare benefit, to protect the principle of non-discrimination, and to accommodate explicitly the income distribution effects of rule-making. (University of Warwick 2007, p. 3)

In commenting on this matter, the 2008 Mortimer review argued:

The Review believes that there are a number of factors that would need to be considered before such an initiative was launched. In particular, the prospect of success is far from secure. At present, many developing countries see very limited commercial interest in services exports and are, as a result, generally disinclined to give market access undertakings without reciprocal access in areas of high priority to them, such as agriculture and textiles. Without the scope for cross-issue trade-offs, it is unclear whether a services-only negotiating process could generate sufficient critical mass. We consider that more work is required to develop the proposal and Australia should include this issue as part of its post-Doha agenda. (Mortimer 2008, p. 82)

## Summing-up

The Commission's assessment is that work can be done to improve the prospects of multilateral (and other forms of) reform. While Australia is already supporting reform within the WTO regarding the transparency of trade agreement formation, the Commission's assessment is that more should be done to advocate domestic reforms in other countries, and investigate the possibility of pursuing reform with groups of like-minded countries.

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*The Australian Government should support worthwhile efforts to achieve multilateral liberalisation. Should meaningful progress within the WTO prove elusive, the Government should weigh up with like-minded countries the feasibility of appropriate broadly based agreements to advance reform.*

*The Australian Government should lend support to initiatives directed at the establishment of domestic institutions in key trading countries to provide transparent information and advice on the community-wide impacts of trade, investment and associated policies .*

### **12.3 Bilateral and regional agreements**

While Australia has already undertaken substantial liberalisation of its own trade barriers and should continue to do so, there are still benefits that could accrue to Australia from the reduction in barriers to trade and investment in the economies of our trading partners.

Reductions in barriers in other countries would ideally be achieved through unilateral reforms or the multilateral processes of the WTO, but other trade policy options should also be considered in order to achieve the potential gains.

Notwithstanding the increasing interest in CMAs in academic circles, presently the most prominent tool directed at this objective is the use of BRTAs. As noted in chapter 11, the Commission's assessment is that there is a legitimate policy rationale for bilateral and regional agreements to reduce barriers in partner countries, and that such agreements can also promote economic cooperation and integration. However, the extent of potential benefits that Australia can gain in pursuing these objectives through such agreements depends critically on the nature and design of those agreements.

#### **Frameworks for trade**

One area in which bilateral and regional agreements can play a positive role is in setting the institutional frameworks and rules for trade between nations. Agreements between governments should aim to establish clear and consistent systems that would have several benefits for businesses, including easing entry into new markets,

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reducing compliance costs and increasing certainty of operating in a given market. Such systems include:

- like systems for contracting between parties;
- clear allocation and definition of property rights;
- transparent regulatory frameworks;
- transparent and objective criteria and processes for dispute resolution; and
- mutual recognition (or harmonisation) of standards and accreditation for goods and services.

The Commission recognises that much work has already been done in multilateral forums to establish the broad frameworks for trade. Nevertheless, there remains a substantial role for bilateral and regional agreement on many, more detailed, matters. Typically, these include domestic regulation where simple differences in regulatory settings can act as behind-the-border barriers (such as mutual recognition of professional qualifications and standards). Effective cooperation on such matters hinges on the development of regulatory trust between partner countries. Therefore, such topics naturally lend themselves to building bilateral agreements (as initial steps in expanding recognition to progressively wider groupings).

While such areas of cooperation are not traditionally considered as the ‘core’ area of trade agreements — which tend to focus on reducing more visible at-the-border barriers — their importance (along with trade facilitation measures discussed in chapter 13) for modern trading economies is increasing:

Today, we must find [ways] to deal with:

- problems of communications and logistics, often linked to security concerns;
- lack of efficiency, transparency, needless divergence and sometimes arbitrary implementation of economic policies in different economies.

These are the dimensions of cooperation where the marginal benefits of cooperation are now greatest. Research, including by the OECD, the World Bank and the ADB, tells us that the potential gains from reducing transactions costs other than traditional border barriers are enormous. (Elek, sub. 54, pp. 3–4)

It is important to note that while such cooperation can occur under the umbrella of a BRTA, it can also take place through a number of different forms of agreement (examples of such agreements are discussed in box 12.3). Indeed, the use of such alternative agreements could be beneficial where they serve to meet the objectives at hand more cost effectively, without entailing the negotiations and complications involved with achieving a single undertaking to a wider trade agreement involving trade-offs between various provisions.

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### Box 12.3 **Alternative types of agreement**

While the pursuit of BTRAs has been prominent in recent years, they are not the only option available to governments seeking to influence the trade policy of other countries. In addition to the unilateral and multilateral options noted earlier in the chapter, there are a range of different sorts of agreements.

For example, as noted by DFAT:

Other non-binding bilateral arrangements such as Trade and Investment [Framework] Agreements (TIFAs) and MOUs [Memoranda of Understanding] are routinely utilised by the Department on behalf of Government to achieve narrower trade, investment and economic objectives which can promote productivity improving reform in partner countries. (sub. 53, p. 67)

MoUs and TIFAs are potential options for focusing on particular topics for agreement between countries, and fostering broader cooperation between governments and agencies. For example, the Commission notes that, while negotiations for a trade agreement have yet to be finalised, ten new agreements with China were recently announced, including several MoUs. While many of the agreements involve private businesses, some were also concluded between governments, including an MoU between the Australian Department of Resources, Energy and Tourism and the National Energy Administration of the People's Republic of China on cooperation in the field of energy, and a protocol of Phytosanitary Requirements for the Export of Apples from Tasmania to China (Rudd 2010).

Further, standards and accreditation agreements or mutual recognition agreements (MRAs) can reduce behind-the-border barriers for businesses, allowing a wider range of goods and service providers into countries, while satisfying regulatory standards for a number of objectives such as health and safety.

These can be sector-specific agreements that focus on a particular range of products (such as the APEC MRA for Conformity Assessment of Telecommunications Equipment, or the Australia-EC MRA on standards and conformity assessment, which covers eight particular sectors). Wider MRAs typically exist between trade agreement partners, such as the Trans-Tasman MRA between Australia and New Zealand.

Another alternative form of agreement that can be used to further cooperation in particular areas are CMAs, discussed in box 12.2.

## **Reducing barriers to trade**

As well as establishing general frameworks for trade, bilateral and regional agreements can play a positive role in reducing specific barriers to trade and investment.

Based on the evidence and analysis in this study, greater gains would be available to all parties from trade liberalisation where it is possible to devise agreements that could be implemented on a non-preferential basis. This suggests that Australia

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should give weight, in prioritising and negotiating agreements, to non-preferential agreements (such as open regionalism agreements like APEC) or ‘preference-light’ agreements (such as the original ASEAN CEPT agreement).

However, the process of reaching agreements necessarily involves other, sovereign, parties. These parties may not be willing to negotiate with Australia on a non-preferential basis. Thus, although the potential gains from preferential agreements are smaller than those from non-preferential ones, they are nonetheless likely to be positive. Rather than forfeit any potential gains by refusing to negotiate preferences where partner countries insist upon them, the Commission’s assessment is that Australian negotiators should not be precluded from accepting such conditions.

### **Broader considerations**

While there is a potential role for BRTAs in establishing frameworks for trade and the reduction of existing barriers to trade and investment, earlier chapters have shown that particular provisions (and as such, agreements as a whole) can vary in the extent of the benefits and costs that they provide, depending on design. Further, given the major trading partners with which Australia already has negotiated agreements or is currently at some stage of negotiation, it is likely that the additional benefits attainable through future agreements may be relatively small, although the risks associated with adverse trade diversion from preferential arrangements also diminish as the scope of Australia’s agreements expands. With smaller impacts in prospect, the value of such agreements to Australia is likely to become increasingly more marginal.

In the Commission’s view, to ensure that any future agreements are in the public interest, it is important that agreements are subject to more transparent assessments of their economic benefits and costs before they are entered into and that they compare favourably with other trade liberalisation options (chapter 15). In this context, as with any policy instrument, the relationship between BRTAs and other mechanisms is also important, particularly if they can act as complements or must be prioritised as alternatives. It is important that any assessment of a potential BRTA identifies not only that it would be likely to yield net benefits, but also that it is part of the most cost-effective package of actions to achieve trade liberalisation objectives.

As discussed in chapter 11, some agreements may have impacts on strategic or security objectives. However, as detailed in that chapter, given the availability of more appropriate options for achieving those objectives, the Commission considers

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that such considerations should not be part of the analysis used to inform the decision of whether to pursue a trade agreement.

RECOMMENDATION 1

***The Australian Government should only pursue bilateral and regional trade agreements where they are likely to:***

- ***afford significant net economic benefits; and***
- ***be more cost-effective than other options for reducing trade and investment barriers, including alternative forms of bilateral and regional action.***

Where a trade agreement is pursued, there are a number of framework considerations that can be adopted to maximise the potential gains. In particular, as noted in chapter 8, the use of non-preferential (or preference ‘light’) tariff provisions can enhance the potential for economic benefit. Likewise, as noted in chapter 9, the nature of most barriers to services trade means that non-discriminatory reforms are likely to provide the most benefit. Further, as discussed in chapter 13, there are several other areas where non-discriminatory reforms have been identified as more beneficial than preferential treatment, including government procurement, competition policy, technical barriers to trade, capacity building and trade facilitation measures. The pursuit of bilateral or regional agreements also should avoid impeding the expansion of agreed conditions to (larger) regional or multilateral groupings, or the pursuit of beneficial unilateral reforms.

RECOMMENDATION 2

***The Australian Government should ensure that any bilateral and regional trade agreement it negotiates:***

- ***as far as practicable, avoids discriminatory terms and conditions in favour of arrangements based on non-discriminatory (most-favoured-nation) provisions;***
- ***does not preclude or prejudice similar arrangements with other trading partners; and***
- ***does not establish treaty obligations that could inhibit or delay unilateral, plurilateral or multilateral reform.***

In addition to these general guidelines, the extent of potential benefits that Australia can gain through future agreements also depends on the nature, scope and design of those agreements. It is therefore important that any future agreements follow good design principles (chapter 13) and have appropriate limits to their scope (chapter 14). The processes surrounding the initiation, negotiation and implementation are also important in improving the potential gains from them. Such process matters are discussed in chapter 15.