

# Chapter 6

## The Australia-US Free Trade Agreement

### What is a free trade agreement?

6.1 A free trade agreement (FTA) is typically a bilateral, preferential<sup>1</sup> agreement between two countries aimed at securing maximum access to each other's domestic markets in order to facilitate trade in goods and services. It commits the parties to policies of non-intervention by the state in trade between their nations. Such an agreement usually entails:

- removing or lowering explicit trade barriers, including import taxes (tariffs) and import quotas.
- softening or eliminating non-tariff or 'hidden' trade barriers – for example, quarantine laws, production and export subsidies, local content requirements, foreign ownership limits, and domestic monopolies.

6.2 Free Trade Agreements necessarily involve an exception to the Most Favoured Nation (MFN) principle, the fundamental rule guiding trade in goods among members of the World Trade Organisation. Under the MFN rule, members of the WTO must give fellow WTO members no less favourable treatment in terms of tariff rates and other trade measures than they afford to any other country. However, WTO rules allow individual countries to afford preferential treatment to partners in an FTA, provided that the FTA conforms to certain strict conditions.

6.3 The rationale for allowing this exception is set out in Article XXIV of the General Agreement on Tariffs and Trade (GATT) of 1947, which recognises the desirability of increasing freedom of trade by the development of closer integration between member countries through agreements establishing free-trade areas. At the same time, strict conditions apply to FTAs to ensure that they serve a liberalising purpose in international trade and do not encourage the establishment of new barriers. Nor should FTAs provide an occasion to introduce new measures discriminating between trading partners.

6.4 The crucial test of an FTA is that it must eliminate all tariffs and other restrictions on substantially all trade in goods between its member countries. Although WTO members have differed over how precisely to define 'substantially all trade', few would disagree that this means, at the very least, that a high proportion of trade between the parties - whether measured by trade volumes or tariff lines - should be

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1 Some economists contend that a 'preferential' agreement is, by its very nature, also 'discriminatory' – that is, discriminatory against all those countries that are not included in the FTA.

covered by the elimination of tariffs and other restrictive trade regulations. Australia considers that this must be a very high percentage, and that no major sector should be excluded from tariff elimination.<sup>2</sup>

6.5 The WTO also provides for bilateral or regional agreements liberalising trade in services. While an FTA as defined under the WTO does not have to include trade in services, most contemporary agreements that are labelled 'Free Trade Agreements' cover both goods and services, reflecting the growing importance of the services in the global economy.

6.6 In addition to trade in goods and services, Free Trade Agreements frequently cover such issues as investment protection and promotion, government procurement and competition policy, which are either not yet encompassed by WTO rules or only partially covered.

6.7 FTAs often also contain practical provisions in areas such as harmonisation or mutual recognition of technical standards, customs cooperation, application of subsidies or anti-dumping policies, electronic commerce, and protection of intellectual property rights.

### **Australia's economic relationship with the United States<sup>3</sup>**

6.8 The United States is Australia's most significant economic partner when measured in terms of combined trade and investment activity. However, of all its trading partners, Australia carries the largest trade deficit with the US, which distorts the economic relationship.

6.9 The US is Australia's second most important destination for merchandise exports after Japan, and our most important market for services and investment. Two way trade in goods and services in 2002 was valued at over A\$45 billion, accounting for nearly 15% of Australia's total trade. The United States was the single most important destination for Australian services exports in 2002, accounting for nearly 15% of total services exports and has grown by A\$363 million over the last five years to A\$4.6 billion. Overall, however, Australia only ranks 28 on America's list of import sources. In 2002, for example, America drew only 0.6 per cent of its global imports from Australia.<sup>4</sup>

6.10 Australia is currently the United States' 24<sup>th</sup> largest trading partner (total trade) and 15<sup>th</sup> largest export market. The United States is among Australia's highest growth export markets, with 5-year trend growth at 16 per cent. Australia's merchandise exports to the United States represent nearly 10 per cent of total

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2 Department of Foreign Affairs and Trade at [http://www.dfat.gov.au/trade/negotiations/us\\_bkg.html](http://www.dfat.gov.au/trade/negotiations/us_bkg.html)

3 Information supplied by the Department of Foreign Affairs and Trade, *Submission 54*

4 DFAT *Fact Sheet: United States of America* available at <http://www.dfat.gov.au/geo/fs/usa.pdf>

Australian exports. However given the firming of the Australian dollar against the US currency, this trend can be expected to plateau.

6.11 Principal exports to the United States in 2002 included beef - where Australia filled its US tariff rate quota for the first time in late 2001 and again in 2002 - crude petroleum, alcoholic beverages, aircraft and parts, and motor vehicles. Exports of elaborately transformed manufactures (ETMs) are one of the strongest performers increasing by 63 per cent over the last five years – albeit from a relatively small base. The United States is now Australia's largest market for exports of ETMs.

6.12 The United States remains the largest source of Australian merchandise and services imports. Merchandise imports accounted for 18 per cent of total imports - major items being aircraft and parts, computers and parts, telecommunications equipment and measuring instruments. In 2002, services imports from the United States accounted for 20 per cent of total Australian services imports.

6.13 As is clear from the above, Australia continues to carry a substantial merchandise trade deficit with the United States - the largest of any trading partner. Whilst the deficit doubled over 1990-95, the bilateral balance on merchandise trade then stabilised, remaining within an A\$11-A\$13 billion range in favour of the US. The trade deficit with the US was A\$12.8 billion in 2002. The merchandise trade deficit is in large part the result of Australia's manufactured and high tech import requirements being sourced from competitive US suppliers. This should all be seen in the context of Australia's overall trade deficit, which in September 2003 was running at \$2.3 billion – the fourth highest deficit on record, and the 22<sup>nd</sup> consecutive month in which imports outstripped exports.

6.14 As at 30 June 2001, the United States was the largest recipient of Australian investment (A\$177 billion) and Australia's largest source of investment (A\$235 billion, or around 30% share of total level of foreign investment in Australia). Flows of Australian investment in the United States over the last five years have been increasing from around \$18 billion in 1995 to around \$97 billion in 2001, although dropping off in 2002 to \$75 billion. In 2001-2002, the US share of foreign investment in Australia was 28.7 per cent.

6.15 Australia's economy is small in comparison to the US, being about 4 per cent the size of the US economy. Both economies are already relatively open, Australia being one of the most open economies in the world. The US maintains a protectionist regime in agriculture – an area in which Australia's highly efficient rural producers have a comparative advantage.

## **History of the Australia-US Free Trade Agreement (US FTA)**

6.16 The government's wish to pursue a free trade agreement with the United States came to public attention around the middle of 2001, as Prime Minister Howard was preparing to visit Washington for celebrations surrounding the 50<sup>th</sup> Anniversary of the ANZUS Treaty. The Prime Minister expressed the government's position in the following terms during radio interviews in August and September 2001:

It won't be easy getting a start on negotiating a free trade agreement with the United States but it is worth looking at. I won't sign any agreement ... that damages Australia's interests. But the United States market is a very big market and if we are able to get greater access to that market on reasonable terms then we'd be foolish to give up that opportunity, absolutely stupid... [I]f we were able to get a toehold into that huge American market that would be tremendously important to Australia.<sup>5</sup>

I don't expect to get... an in principle commitment to start negotiations for that. The reason is that right at the moment, in fact, almost while I'm in Washington there's an exchange going on between the administration and congress for the administration to get a trade promotion authority and they, for domestic, political reasons, which I fully understand, they don't want issues relating to in-principle commitment to negotiate free trade agreements to other countries to be around at the time they're having that exchange with congress.<sup>6</sup>

6.17 Unlike the Australian situation, the US government requires an Authority from Congress before it can proceed with a trade agreement. This so-called 'Trade Promotion Authority' specifies the framework, goals and conditions which are to inform the development of the agreement.

6.18 Some informal discussions at officials' level took place during the ensuing 12 month period,<sup>7</sup> and in November 2002, the United States announced formally its intention to enter into negotiations with Australia.<sup>8</sup> Australia's designated lead negotiator, Mr Stephen Deady, outlined the sequence of events that flowed from the formal announcement

There was a 90-day period required under the US Trade Promotion Authority whereby consultations with the Congress were required before formal negotiations could commence. The first negotiating round was held here in Canberra, back in March of this year. We have now had three full negotiating rounds—the one in March in Canberra and then two subsequent rounds in May and in July in Hawaii. We are now in the process of preparing for the fourth round of talks, which will be back here in Canberra running through the week beginning 27 October. At this stage we have also planned a further full negotiating round for the first week in December, in Washington.<sup>9</sup>

6.19 The main focus of the negotiations in the first three rounds was on:

- a) developing the broad framework,

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5 John Howard MP, Transcript of Radio 4BC interview with John Miller, 9 August 2001

6 John Howard MP, Transcript of Radio 3LO interview with Jon Faine, 4 September 2001

7 *Committee Hansard*, 2 October 2003, p. 482 (Deady, DFAT)

8 *Committee Hansard*, 2 October 2003, p. 460 (Deady, DFAT)

9 *Committee Hansard*, 2 October 2003, p. 460 (Deady, DFAT)

- b) the legal text that would cover the agreement, and
- c) agreeing on the chapters that would be covered by a comprehensive agreement between Australia and the United States.<sup>10</sup>

6.20 In May 2003, Prime Minister Howard met with US President Bush at Crawford, Texas, and both leaders confirmed that they wished to pursue a target date of December 2003 for the conclusion of negotiations. DFAT officials advised the Committee that negotiations were being conducted assiduously in order to meet the tight deadlines.

It was only in the third round that we were able to sit down with the United States and begin negotiations on the specific market access aspects of the negotiations. These market access commitments are really the core of free trade agreements. Again, a requirement of US law was that the United States was not able to commence formal negotiations on market access until the International Trade Commission in the United States had completed an economic assessment of the impact of the Australia-US free trade agreement on US industry...

We are seeking a truly comprehensive and liberalising free trade agreement that is fully consistent with the rules of the WTO, both the rules of the GATT which deal with free trade agreements and the rules under the GATS which talk about the economic integration of economies. We are looking at a very big agreement. The agreement itself will run to probably 23 or 24 different chapters, covering the full range of economic activity.<sup>11</sup>

6.21 Once negotiations have been completed, and a proposed Free Trade Agreement settled, the US Trade Promotion Authority requires that Agreement to be considered by Congress. There are no provisions for Congress to amend the Agreement – it will either accept or reject it.

## Why a Free Trade Agreement?

6.22 The Howard Government has consistently regarded bilateral agreements as an important supplement to its multilateral trading efforts. Following the Seattle WTO ministerial, the government announced that it was:

intending to explore the prospect of bilateral free trade agreements where these would deliver benefits to Australian exporters in a deeper way and in a quicker fashion than perhaps may have been possible through the multilateral negotiations.<sup>12</sup>

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10 *Committee Hansard*, 2 October 2003, p. 460 (Deady, DFAT)

11 *Committee Hansard*, 2 October 2003, p. 460 (Deady, DFAT)

12 *Committee Hansard*, 2 October 2003, p. 481 (Deady, DFAT)

6.23 On 3 March 2003, the Minister for Trade, Mr Vaile, announced the Australian Government's objectives for the Australia-US FTA (Appendix 3). Key points from those objectives supporting the government's decision to negotiate an Australia-US Free Trade Agreement were summarised in DFAT's submission to the Committee:

- This is an unprecedented opportunity to negotiate an agreement with the largest economy in the world, and a major trade and investment partner for Australia.
- Improved market access to this major market and expanded two way trade would stimulate economic growth, which will mean more jobs, income and improved well-being for Australians:
  - by addressing existing market access problems in the US market for Australian exporters of farm products, manufactures and services, including beef, dairy, sugar, canned fruit, fast ferries, magnesium, telecoms and electronic commerce, the movement of people, intellectual property rights, and government procurement.
- An FTA would rebalance our competitive position vis a vis the exports of other countries that already enjoy lower barriers to trade in the US – or may do so as a result of future FTAs
- An FTA would help build momentum towards multilateral liberalisation and help Australian exporters compete in an environment where the popularity and number of FTAs are growing.
- A high standard FTA with the US would add momentum to the objectives we are pursuing through the WTO aimed at strengthening the multilateral trading system and advancing the cause of global trade liberalisation.
- The Government has stated its intention to ensure that the FTA will not impair Australia's ability to deliver key public policy objectives in areas including health care, education, consumer protection, environment and Australian culture and identity.<sup>13</sup>

6.24 The government commissioned from the Centre for International Economics a study on the economic impacts on Australia of a USFTA. The study suggested that liberalisation of bilateral trade and investment could boost Australia's GDP by 0.3-0.4 per cent per annum within 10 years. The modelling assumed the removal of all tariffs and other barriers for which it was possible to estimate the quantifiable impact of their removal. If the final agreement were not to eliminate all barriers immediately upon entry into force, the impact would be proportionately less and spread over a longer time frame.

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13 *Submission 54*, pp. 37-38 (Department of Foreign Affairs and Trade)

6.25 The CIE report became the subject of some debate during the Committee's inquiry, especially following the release of a report from another consulting group (ACIL) that drew notably less favourable conclusions about the proposed FTA. This controversy will be examined in a little more detail below. Government officials have consistently endorsed the CIE report, and have argued that ACIL's analysis is flawed.

6.26 The financial benefits identified in the CIE report were outlined by DFAT on several occasions, and summarized by Australia's lead negotiator, Stephen Deady, in the following terms:

The study does a number of things: it produces a run of what GDP would be over the course of the next 20 years with an FTA between Australia and the United States with full liberalisation. So it makes GDP projections for 20 years. It produces a run on what GDP would be without an FTA. There are several things it does but, of the numbers that have been quoted, the purpose of one was to say: 'Let's take a snapshot. In 2010, 10 years after it came into effect, GDP in Australia would be \$US2 billion higher than it would otherwise be.' So, in that year, GDP is higher by that amount... GDP over five or 10 years would be \$10 billion—

The... modelling is driven by the removal of all barriers to trade—tariffs, quantitative restrictions—at the border, but there are a number of additional barriers, restrictions, that the modelling work cannot measure. To that extent it is an underestimate, if you like, of the gains. For example, we have had this debate with the modellers just in the last couple of weeks: it does not take into account the restrictions on Australia selling to the government procurement market in the United States. It looks at the tariffs, non-tariff barriers, quantitative restrictions but not at some of those other instruments of policy in the United States which clearly impact on Australian exports. To that extent, it would underestimate the gains. In services and investment, again it is argued that it would underestimate. The modellers tell us that is a very hard thing to model. To that extent, the dynamic gains that might emerge from the investment services aspects of the agreement again are not fully reflected. With that caveat on your description, as a modelling exercise it models the things it can measure—removal of all those barriers, elimination of all the quantitative restrictions, all the tariffs on goods—and those things are fully reflected.

The study identified a number of additional barriers that Australia faces in the US market. It also talked about some of the barriers in Australia. It talked about the procurement barriers in relation to the United States—the Buy America Act and the fact that we were not a member of the GPA of the WTO. It talked about some of the difficulties in modelling things like procurement, but it did not actually model those restrictions on Australia's exports into the United States or the removal of those restrictions in relation to procurement.<sup>14</sup>

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14 *Committee Hansard*, 2 October 2003, pp. 484, 485, 486. (Deady, DFAT)

6.27 The Committee does not question the professional competence of CIE – nor indeed that of ACIL. But the Committee is mindful of the limitations of economic models in predicting actual outcomes. Significant factors in the results produced by such models include the accuracy and comprehensiveness of the data entered, the consistency or otherwise of trendlines, and the range and accuracy of the assumptions that are built in to (or excluded from) the models used. For this reason, the Committee does not dwell too deeply on the dollar figures thrown into the FTA debate, preferring to concentrate on the *principles* of global free trade, the *process* by which free trade agreements are developed, and the *mechanisms* by which such agreements are legitimized.

### Adequacy of the economic analysis

For the US, an FTA is thus a much less significant national economic decision than for Australia.<sup>15</sup>

[I]mpacts have been at best only partially considered; impact analysis is inadequate... [W]e do not seem to have estimated in any satisfactory way potential gains and losses under alternative regimes; so regime analysis is inadequate. ... [O]ur goals, strategies and processes appear confused; negotiations are then likely to be less effective than they might be. Indeed, we could actually achieve outcomes which are disadvantageous to the interests of Australia and Australians.<sup>16</sup>

6.28 Several witnesses commented upon the fact that Australia was the initiator of the recent moves towards an FTA with America, and that there was no immediate or obvious significant benefit to be had by the US in entering such an arrangement. It also appears that the Australian move did not emerge from any prior detailed assessment of the economic benefits that might be realised. Professor Ross Garnaut told the Committee that:

From what I hear, no real economic analysis was done even in the closed circles of the Public Service prior to the initial commitment to seek a free trade agreement with the United States in December 2000.<sup>17</sup>

6.29 Professor Garnaut presented his concerns in considerably more detail in a paper delivered in February 2003 to the Sydney meeting of the Australian Business Economists group.<sup>18</sup>

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15 Australian APEC Study Centre *An Australia-US Free Trade Agreement: Issues and Implications*, Monash University, August 2001, p.48

16 *Committee Hansard*, 24 July 2003, p. 408 (McGovern, Queensland University of Technology)

17 *Committee Hansard*, 22 July 2003, p. 200 (Garnaut)

18 Garnaut, R 'Australian security and Free Trade with America'. Paper presented at the Australian Business Economists meeting on *US and Australia Free Trade Agreement: National interest or Vested interest?* Sydney, 27 February 2003

6.30 During its inquiry, the Committee noted the emergence of a common thread of concern among public witnesses (both in relation to GATS and the US FTA) about the perceived shortcomings of DFAT in the coverage and balance of its published information and advice. The perceived lack of serious attention to any negative impacts of these agreements seems to have made many people suspicious. They sense that they are not being told the full story - that the government is being insufficiently frank, that it seems only to present information that is favourable to its case, and that the government is exaggerating the benefits.

6.31 The Committee was told by one witness that, when he sought from DFAT any material outlining what he called the ‘disbenefits’ of free trade and investment, the emailed responses from DFAT stated, among other things:

Regarding the “disbenefits” of trade liberalisation, I suggest you search your university library for alternative viewpoints. It is the government’s belief that trade liberalisation is, on the whole, beneficial to the Australian and world economies...

... For your purposes, the Productivity Commission may be a more useful source of information on trade liberalisation and domestic market reform than DFAT. Unlike government departments, the Productivity Commission is an independent Commonwealth Agency, which does not report directly to a Minister.<sup>19</sup>

6.32 Another witness expressed serious reservations about DFAT’s willingness and capacity to make a judicious assessment of the merits of various arguments within the trade debate. He spoke of his personal dealings with DFAT officials as part of the consultation process engaged in by the Department.

One particular session I attended was about the importance of trade. It was by the Trade Advocacy and Outreach Section. They were very concerned that the general public had not cottoned on to their way of seeing things and those they needed to educate the public to the correct view.... In answering questions, the presenter of this particular talk was talking of this big marketing push and of bringing the public along. I took some verbatim quotes while I was there. He said, ‘It is ideological, political, and I am comfortable to acknowledge this.’ He also said, ‘We look for information that bolsters our own view.’ I think the Senate needs to be aware that this attitude is within that department and that these people are not capable of giving balanced, open, fair and fearless advice.<sup>20</sup>

6.33 The point was frequently made to the Committee that the material provided publicly by DFAT – especially the documentation available on its website – lacked balance in that there was little, if any, consideration of potential downsides to a US FTA.

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19 *Submission 53*, pp. 23-24 (Edwards)

20 *Committee Hansard*, 24 July 2003, p. 392 (Sanders)

The materials that the Department of Foreign Affairs and Trade has published to advance the Government's agenda of globalisation of trade and investment argue only one side of the case, as if 'there is no alternative'... Simply repeating a false statement over and over does not make it true. If there is one message which I would like to leave for the Committee, it is the shallowness of so much of what is presented as argument in favour of free trade and the absence of critical, multi-disciplinary analysis.<sup>21</sup>

The economic impacts of trade liberalisation are being consistently overstated and environmental and regional impacts in particular are being understated. There is an imbalance in the way we have reported on trade liberalisation and understood it... I suggest... that some of the official Commonwealth documentation provides evidence of confusion and misrepresentation. I think there are some issues here in terms of the way the whole trade story is being discussed.<sup>22</sup>

6.34 The Committee appreciates that DFAT's task is to communicate, promote and implement government policy. However, it is problematic if that communication is perceived by many to be at best insufficiently nuanced, or at worst, brute propaganda.

6.35 The Committee has noted earlier the controversy generated by the studies that had been commissioned to assess the potential of the Australia-US Free Trade Agreement. DFAT commissioned two main studies concerning the US FTA. They are available on its website.

- a) *An Australia-US Free Trade Agreement: Issues and Implications*, produced by the Australian APEC Study Centre, Monash University published in August 2001, and
- b) *Economic Impacts of an Australia-United States Free Trade Area*, produced by the Centre for International Economics, published in June 2001

6.36 The US government requested a report from its own International Trade Commission (ITC) on the impact of the FTA on the American economy. The Committee sought advice from the ITC about the status and availability of that report and was advised that 'the report was sent to the United States Trade Representative's office in early June 2003' and that it is 'a confidential report for internal U.S. Government use only'.<sup>23</sup>

6.37 A third report by ACIL Consulting was commissioned, not by DFAT, but by the government's Rural Industries Research and Development Corporation. Entitled *A Bridge Too Far? An Australian Agricultural Perspective on the Australia/United*

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21 *Submission 53*, p. 1 (Edwards)

22 *Committee Hansard*, 24 July 2003, p. 407 (McGovern)

23 Correspondence between Mr David Lundy (ITC) and the Committee Secretariat, 25 November 2003

*States Free Trade Area Idea*, this report was at odds with the findings of the DFAT-commissioned studies. It proved to be the catalyst for some academic and political disputation. In March 2003, the Centre for International Economics published a critical rejoinder to the ACIL Report.

6.38 The Committee does not intend to pursue its own critique of these reports – it merely notes the differences between them. However, economists, trade officials and financial commentators have made a variety of claims about the validity of the reports, and the Committee has had several of these drawn to its attention in hearings and submissions.

6.39 DFAT and the CIE have both criticised the ACIL report (*A Bridge Too Far ?*) in some detail – CIE in the published paper mentioned above, and DFAT in the verbal evidence to the Committee given by its lead negotiator Stephen Deady:

I had serious problems with a number of the assertions and claims made in that [ACIL] study when I was a referee on the study going right back through the process. I really tried to explain to the author why I thought what I did about some of those claims about what happened in the Uruguay Round and subsequently in trade policy in the United States and in this country. But, anyway, that is their report. They have put their name to it and they stand by it. I have no problem with that. But, as we have said, we believe that the report is flawed, and I certainly stand by that.<sup>24</sup>

6.40 In turn, perhaps the most detailed critique of the DFAT-commissioned CIE Report (*Economic Impacts of an AUSFTA*) has been made by Professor Ross Garnaut in articles produced during 2002 and 2003. In these, he argues that the CIE report should be regarded ‘not as an attempt at realistic assessment of the effects of an Australia-United States Free Trade Agreement, but rather as an assessment based on assumptions that are generally favourable to a free trade agreement.’<sup>25</sup>

6.41 In his evidence to the Committee, Professor Garnaut observed:

Some ex post facto economic work was done but by consultancies under quite specific and narrow terms of reference, which did not ask the question, ‘Would this free trade agreement be good for Australian economic welfare?’ Those terms of reference specified a lot of assumptions and then asked, ‘What are the implications of these assumptions?’ That negates transparent, independent analysis, which was the key to Australia becoming a more open, productive economy in the last decades of the 20th century.<sup>26</sup>

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24 *Committee Hansard*, 2 October 2003, p. 491 (Deady, DFAT)

25 Garnaut, R ‘Australian security and Free Trade with America’. Paper presented at the Australian Business Economists meeting on *Us and Australia Free Trade Agreement: National interest or Vested interest?* Sydney, 27 February 2003, p. 6

26 *Committee Hansard*, 22 July 2003, p. 200 (Garnaut)

6.42 Professor Garnaut also presented to the Committee five important issues relating to the US FTA that, in his view, were not ‘amenable to modelling.’<sup>27</sup> These issues are as follows:

- the negotiation of a bilateral FTA would accelerate the weakening of the multilateral system;
- there will be resulting trade diversion from Australia’s most important export region, East Asia;
- the rules of origin associated with a US FTA would raise transaction costs in international trade and lower productivity in the process;
- the exclusion of US agricultural subsidies from the FTA would corrode the position of free trade agricultural exporters in the international system and could negate any benefits from increased market access to the US;
- the processes of policy making in developing this agreement, relying on commissioning consulting reports with limited terms of reference, have been very damaging to trade policy processes.<sup>28</sup>

6.43 According to Professor Garnaut:

Every one of those [five] points was excluded by assumption when DFAT commissioned the Centre for International Economics to do their study... Those five points are the big ones. If you exclude those points and say, ‘Let’s forget about those but what would a free trade agreement that does not consider any of those things do?’ there is still a debate.<sup>29</sup>

6.44 With respect to the APEC Study Centre report, it was of significance for some witnesses that the director of the Centre that produced *Issues and Implications* is Mr Alan Oxley. Mr Oxley is also the managing consultant of the firm International Trade Strategies, and the business director for AUSTA, the ‘Australian Business coalition established to promote conclusion of a Free Trade Agreement between Australia and the United States.’<sup>30</sup> It was also claimed that Mr Oxley’s colleagues in the APEC Centre research team were prominent advocates of business interests and one of them also an employee of his firm International Trade Strategies.<sup>31</sup>

6.45 The Committee does not question the professional competence of any of the agencies that produced the various reports. However, it understands how perceptions have arisen among some members of the public that DFAT attends almost exclusively to those reports and assessments that are favourable to its policy objectives; that those

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27 *Committee Hansard*, 22 July 2003, p. 205 (Garnaut)

28 *Committee Hansard*, 22 July 2003, pp. 196, 197, 198, 199, 100 (Garnaut)

29 *Committee Hansard*, 22 July 2003, p. 205 (Garnaut)

30 *Submission 47*, p. 1 (Oxley for AUSTA)

31 *Submission 160*, p. 22 (Australian Manufacturing Workers Union)

reports are too closely aligned with vested interests; and that DFAT either disregards or denigrates alternative assessments.

6.46 In the Committee's view, it is vital that policy analysis and development not only be transparent but be seen to be so. This is especially the case where such high-profile agreements are concerned. To do otherwise is to invite criticism of the FTA on process grounds alone.

It is disturbing that transparent and disinterested analysis has played such a small role, and business vested interests such a large one, in policy making so far on the free trade agreement. The debate suffers from the absence of a report from the Productivity Commission, attempting to measure objectively and independently the extent and distribution of benefits. The papers commissioned by DFAT came after the policy decision to seek a free trade agreement...<sup>32</sup>

6.47 The Committee notes that the government's decision to pursue a free trade agreement with America represented a significant turnaround from its previous position, and something of a 'historic departure in Australian trade policy'.<sup>33</sup> Like its Labor predecessors, 'through the 1990s the Howard government... remained deeply wary of proposals for bilateral trade deals'.<sup>34</sup>

6.48 When President Bill Clinton approached Australia about the possibility of a free trade agreement he was rebuffed. Rob O'Donovan was Australian Senior Trade Commissioner in Los Angeles until 1998, and was a contributor to the DFAT *Review of Australian US Trade relations - A Partnership in Transition*. In a February 2002 article for the Brisbane Institute he wrote:

The Howard government ... in 1997... still firmly rejected the overtures from the Clinton Administration for a bilateral free trade agreement as the Hawke government had done so in the late 80's. It did so for much the same reasons - any success we had was achieved multilaterally and we were unlikely to get any joy in those US agricultural markets where we were competitive but our competitors had friends in Congress... The last consideration hasn't changed so it is worth asking what has?<sup>35</sup>

6.49 The Committee has been unable to elucidate a satisfactory account of the process by which the Australian government's views on this matter were modified to the extent of shifting from a consistent rejection of a US free trade agreement to a

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32 Garnaut, R 'Australian security and Free Trade with America'. Paper presented at the Australian Business Economists meeting on *Us and Australia Free Trade Agreement: National interest or Vested interest?* Sydney, 27 February 2003, p. 20

33 Capling, A 'Trade, the USA and Down Under's Tyranny of Size' *The Sydney Papers* Autumn 2001, p. 180

34 Capling, A 'Trade, the USA and Down Under's Tyranny of Size' *The Sydney Papers* Autumn 2001, p. 177

35 Available at [http://www.brisinst.org.au/resources/brisbane\\_institute\\_fta.html](http://www.brisinst.org.au/resources/brisbane_institute_fta.html)

forthright and energetic pursuit of one. Some commentators have discerned the shift to be purely a political choice.

Although the public debate will be about economics, the real agenda of the FTA is political. Prime Minister Howard has strategic reasons to support the agreement. An FTA would consolidate the emerging US-Australia axis.<sup>36</sup>

6.50 Occasional reference was made during the Committee's inquiry to the potential role of the Productivity Commission in assisting the Commonwealth government to assess the economic impacts of a free trade agreement. The Howard government has not sought such advice from the Productivity Commission in relation to the US FTA. However, a Productivity Commission Staff Working Paper was published in May 2003 entitled *The Trade and Investment Effects of Preferential Trading Arrangements – Old and New Evidence*.<sup>37</sup>

6.51 The Working Paper examined 18 existing preferential trade agreements (PTAs), and not those in prospect. Findings relevant to the Committee's present inquiry include the following:

- The 'bulk of the existing literature seems to point to PTAs being stumbling blocks rather than building blocks to multilateral liberalisation'. (p22)
- Nearly all PTAs are found 'to have caused net trade diversion' and overall have created 'negative net trade effects.' (p77)
- The findings on investment are 'more positive than with trade, but not without qualifications'. (p98) It is 'possible for PTAs to have more adverse effects on investment flows than trade flows.' (p97)
- Some of the 'apparently quite liberal PTAs... have failed to create significant additional trade among members' (p100)
- The findings 'on the effects of the non-trade provisions of PTAs are more positive than those on the trade provisions'. (p101)

6.52 The Committee believes that it would be highly desirable if the services of the Productivity Commission were drawn upon by the government to provide analysis and advice concerning proposed trading agreements. Not only would this add significantly to the pool of information available to government for decision-making and policy development, but it would also militate strongly against the perception that the government was relying on advice that was highly coloured by a particular view.

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36 Hamilton, C 'Free trade deal won't produce the goods' *Australian Chief Executive* (CEDA) April 2003, p. 29

37 Adams, R (et al) *The Trade and Investment Effects of Preferential Trading Arrangements – Old and New Evidence*, Productivity Commission Staff Working Paper, Canberra, May 2003

## Recommendation 11

**6.53 The Committee recommends that the government – prior to embarking on the pursuit of any bilateral trading or investment agreement – request the Productivity Commission to examine and report upon the proposed agreement. Such a report should deliver a detailed econometric assessment of its impacts on Australia’s economic well-being, identifying any structural or institutional adjustments that might be required by such an agreement, as well as an assessment of the social, regulatory, cultural and environmental impacts of the agreement. A clear summary of potential costs and benefits should be included in the advice.**

## Key issues of concern with the US FTA

6.54 In both submissions to the Committee, and in oral evidence given at public hearings, certain key issues were repeatedly highlighted. The following provides a brief summary of the matters raised.

### Do bilateral agreements undermine multilateral arrangements?

6.55 There has been a long-standing debate about the extent to which WTO based multilateral trade negotiations might be undermined by countries entering bilateral agreements that are by their nature preferential. The Committee explored the issue on several occasions by posing the question as to whether burgeoning bilateral agreements had ‘sucked the oxygen out of’ multilateral efforts.

One of the reasons for it lacking oxygen is that the energy of major players—including Australia, the United States and Japan—has been focused on small-group and bilateral free trade agreements rather than multilateral negotiations. To get a pretty good feel for the nature of the problem, one only has to compare the effort that the Australian government put into organising support amongst Western Pacific countries during the Uruguay Round with the focus of attention on trade policy discussion at the moment.<sup>38</sup>

6.56 Both in oral evidence before the Committee, and in its submission, the government argued strongly that there was no conflict arising from the pursuit of both bilateral and multilateral arrangements.

Some commentators have suggested that negotiation of an FTA with the US will undermine the multilateral trading system founded on the WTO, or signal a lessening of Australia’s commitment to the WTO and multilateral liberalisation.

This observation appears to ignore the following:

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38 *Committee Hansard*, 22 July 2003, p. 197 (Garnaut)

- FTAs are sanctioned by the WTO – good FTAs are accepted as consistent with the WTO if they are comprehensive and trade creating...
- FTAs can help the WTO system to generate momentum by liberalising difficult sectors among a few countries – and help with the adjustments necessary under global liberalisation negotiations
- in circumstances where the pace of the Doha Round is slowing ... and in particular the difficulty of securing commitments from WTO members to significant agriculture reform, governments will wish to take the opportunity to secure WTO-consistent market opening elsewhere;
- suggestions that bilateral FTA negotiations somehow conflict with Australia's efforts in the WTO reflect a flawed understanding of trade negotiations
- there is no conflict between the objectives Australia is pursuing in the WTO and our FTA negotiations.
- we *continue to press the United States* in Geneva on access for sugar, dairy and other products
- the bilateral FTA negotiations give us a further opportunity to secure our Doha Round objectives on agricultural market access more deeply and rapidly than would be possible through the WTO Doha Round.<sup>39</sup>

6.57 The Committee notes the rather more cautious statement by the Centre for International Economics – author of the government-commissioned report favourable to a US FTA – in its rejoinder to the (less FTA-favourable) ACIL Report.

It would have to be admitted, however, that a competitive scramble to form as many bilateral FTAs between pairs of countries around the world distracts attention from the main game – the multilateral reduction of barriers. FTAs do suffer from the problem that they are discriminatory and weaken the principle of non-discrimination that underpins the GATT.<sup>40</sup>

6.58 Agricultural interests have consistently regarded multilateral negotiations as the most effective path to liberalisation of their sector. The Committee notes, however, that the US FTA has received broad support from agricultural industries.

We certainly do not resile from the fact that the main game is the WTO. ... [S]ome of the oxygen is going out as a result of people looking at bilateral arrangements or preferential deals. That could partly be because of frustration with the process, but I believe also that the process has pretty much slowed up because one of the major parties, the EU, cannot get

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39 *Submission 54*, p. 40 (DFAT)

40 Centre for International Economics *Australia-United States Free Trade Agreement: Comments on the ACIL Report* (Sydney) March 2003, p. 12

themselves sorted out on agriculture. That has meant that everything else has drifted. We are waiting for the Europeans to pull themselves together and work out what they want internally before we can get on with the multilateral round.<sup>41</sup>

### **The broader foreign policy and security framework**

6.59 In the Committee's view, Australia's pursuit of a free trade agreement with America has as much, if not more, to do with Australia's broader foreign policy objectives as it does with pure trade and investment goals. Certainly for the United States administration, free trade agreements can only be situated within a particular foreign policy setting. This was made clear in a widely-reported speech (May 2003) to the Institute for International Economics by USTR Zoellick:

U.S. Trade Representative Robert Zoellick late last week said countries that seek free-trade agreements with the United States must pass muster on more than trade and economic criteria in order to be eligible. At a minimum, these countries must cooperate with the United States on its foreign policy and national security goals... The U.S. seeks "cooperation -or better- on foreign policy and security issues," Zoellick said... Given that the U.S. has international interests beyond trade, "why not try to urge people to support our overall policies?" he asked.

Zoellick said that he uses a set of 13 criteria to evaluate potential negotiating partners, but he insisted that there are no formal rules for the selection or any guarantees. "It's not automatic," Zoellick said. Negotiating an FTA with the U.S. "is not something one has a right to. It's a privilege."<sup>42</sup>

6.60 Some witnesses regarded these sorts of remarks as signalling America's desire to 'cement a network of countries into a pact which will bind them to comply with US foreign policy ambitions.'<sup>43</sup> Others expressed concern that Australia's national interests may be compromised by being seen as inextricably bound to the US.

Australia has built up positive trade and cultural relationships with many countries in our region. This is in part because we are not seen as an economic or cultural appendage of the US, but as an independent country with its own trade and foreign policy, which has in the past differed with the US on some key issues. Australia's role within the Cairns Group could be compromised if a US-Australia FTA goes ahead.<sup>44</sup>

6.61 Other witnesses regarded a US FTA as an appropriate and important complement to Australia's existing alliance with the United States. The government has been unequivocal in this respect. In particular, its views are declared strongly in Australia's latest foreign policy White Paper *Advancing the National Interest*.

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41 *Committee Hansard*, 9 May 2003, pp.139, 140 (Lavery, Australian Dairy Industry Council)

42 Quoted in *Inside US Trade*, 16 May 2003.

43 *Submission 53*, p. 20 (Edwards)

44 *Submission 42*, p. 34 (Australian Fair Trade and Investment Network - AFTINET)

Australia's links with the United States are fundamental for our security and prosperity... Australia has a vital interest in supporting long-term US strategic engagement in East Asia, because of its fundamental contribution to regional stability and prosperity. The government's pursuit of a free trade agreement with the United States is a powerful opportunity to put our economic relationship on a parallel footing with our political relationship, which is manifested so clearly in the US alliance.<sup>45</sup>

6.62 The Committee agrees that Australia's relationship with the United States is its most vital strategic and political alliance. However, several witnesses argued that the linking of trade and investment agreements so closely to issues of security and strategic political interest is not without its tensions.

As a trade economist, I get very nervous about links between trade and security or trade and defence or other things which are not closely related to trade, because they can distort the kind of agreement that comes out of it.<sup>46</sup>

Never before has Australia compromised our foreign policy independence for trade favours. Our Government might deny such but US trade negotiator Mr Zoellick himself linked the issue of trade and foreign policy. This is a dangerous precedent for our independence as a nation.<sup>47</sup>

6.63 The linking of trade and security relationships is clearly regarded as desirable and appropriate by both the American and Australian governments, but the Committee notes that the role of the US Congress in trade matters introduces a distinctive dynamic into that linkage.

The United States trade policy is not made by the administration; it is made in the Congress. There is a long tradition—and not a very elegant tradition—of United States trade policy being bought and sold in the US Congress, and administration views on security priorities do not always hold sway in the US Congress. So people who give high priority to a good political relationship and to the ANZUS alliance have always taken pains to separate the alliance relationship from the trade relationship<sup>48</sup>.

6.64 In the Committee's view, the harmonizing of trade and security relationships is something that must be approached with considerable caution. There have been instances in the past where discriminatory trade action by the US – especially in connection with agriculture – has led to strong domestic calls for retaliatory action on the security front, such as withdrawal of permission for American access to satellite tracking stations and communications facilities. Such controversies are best avoided.

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45 Australian Foreign and Trade Policy White Paper *Advancing the National Interest* Canberra (2003) p.(xvi)

46 *Committee Hansard*, 9 May 2003, p. 161 (Lloyd)

47 *Submission* 125, p. 2 (ACTU)

48 *Committee Hansard*, 22 July 2003, p. 203 (Garnaut)

6.65 As Australia becomes more deeply engaged in trade with its regional neighbours, and especially with emerging economic powers like China, any tensions between, say, the US and China, could place Australia in an invidious position if the Australia-US relationship is predicated on closely entwined security and trade interests that verge on the symbiotic.

### **Prospects of trade diversion from existing markets**

6.66 Australia's trade arrangements have historically been strongly multilateral, and since the 1950s have been oriented strongly towards the Asia-Pacific region. In recent decades, the focus has intensified with respect to South-East and East Asia. China, Japan and Korea are among Australia's most important export markets.

6.67 Professor Ross Garnaut has been one of the more prominent economists arguing that a US FTA would divert trade from Australia's regional trading partners.

[T]he negotiation of such an agreement would weaken Australian trading performance in its most important export region, East Asia, including by encouraging the emergence of free trade areas in East Asia that discriminate against Australia.

Trade discrimination within East Asia with Australia being excluded—for example, giving Thai and Philippine preferences in the Chinese, Korean and Japanese markets—would be devastating for Australia, and discussions are now under way to do precisely those things. Any potential gains in the United States market from the bilateral agreement would, on analysis, be trivial compared with the potential losses of our main markets and main growth markets in East Asia. I am not saying that we would lose all of those markets, but we now are at risk of discriminatory arrangements being developed in East Asia that will exclude us, which will be very damaging.<sup>49</sup>

6.68 The Committee pursued this argument at some length during its inquiry, especially with Australia's lead FTA negotiator, Mr Stephen Deady. Mr Deady argued strongly that the trade diversion argument did not square with the reality of what was happening between Australia and its Asian neighbours.

What we are looking at are the barriers that Australian exports face in the United States market. Some of those barriers are particularly significant, coincidentally, in areas where we are perhaps the world's most efficient producer—or, if we are not the most efficient, we are in the top two—namely, the areas of sugar, dairy and beef. Any access that Australia gains to the United States market in those commodities is, in my view, unequivocally trade creating. There is no diversion of product. ... We are not displacing a third country which is an inefficient producer in the US market; we are replacing inefficient US production.<sup>50</sup>

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49 *Committee Hansard*, 22 July 2003, pp. 197, 198 (Garnaut)

50 *Committee Hansard*, 2 October 2003, p. 494 (Deady, DFAT)

All of this discussion of trade creation and trade diversion has to take into account the level of the external tariff. If you looked at these studies 10 or 15 years ago, the external tariffs were significantly higher and so the threat of trade diversion was potentially again significantly much higher. The fact is that the average Australian tariff is now very low and a very large percentage of imports into this country are duty-free, so there is no negative impact whatsoever from preferential arrangements within the United States where existing multilateral tariffs are zero.<sup>51</sup>

6.69 The DFAT submission to the Committee addressed the argument in some detail, but at the broader level of Australia's relations with East Asia.

Some observers appear to be concerned that the opening of negotiations between Australia and the US will damage Australia's relations with or interests in the East Asian region because of the signal it would send about Australia's attachment to the region. This observation appears to ignore evidence that Australia's ongoing commitment to and engagement with East Asia remains strong:

- the recent signing of our FTA with Singapore;
- negotiations on a Closer Economic Relations Free Trade Agreement with Thailand, launched in May 2002;<sup>52</sup>
- the ongoing high priority we attach to a strong and progressive APEC agenda which brings together all the key economies of our region;
- our pursuit of a new trade and economic agreement with our largest export market, Japan, and Australia's willingness to undertake an FTA with Japan;
- our pursuit of a new framework agreement with China to enhance trade, investment and economic cooperation, announced in May 2002;<sup>53</sup>
- the AFTA-CER Closer Economic Partnership framework agreement between the Association of South-East Asian Nations (ASEAN) governments and Australia and New Zealand, signed in 2001, which stemmed from Australia's initiative in 2000 to explore a possible FTA between AFTA and CER.

Moreover, other countries in the region are not only interested in pursuing FTAs with each other, and with others outside the region, but with the US as

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51 *Committee Hansard*, 2 October 2003, p. 495 (Deady, DFAT)

52 And brought to a successful conclusion in October 2003.

53 The visit of China's President Hu Jintao in October 2003 provided an occasion to confirm that Australia and China would undertake studies to examine the possibility of a free trade agreement.

well – which hardly suggests that the countries of the region have a philosophical objection to FTAs in general, or with the US in particular:

- most East Asian countries are already involved in FTA discussions or negotiations or have concluded FTAs both within and outside the region (Japan-Mexico, Korea-Chile, ASEAN - China, ASEAN-Japan, Singapore with the US, Canada and Japan, New Zealand with Singapore and Hong Kong);
- the US announced in October 2002 the Enterprise for ASEAN Initiative under which the US and individual ASEAN countries will jointly determine if and when they are ready to launch FTA negotiations;
- in these circumstances it would appear odd if those countries were to single out Australia for negative reaction to the announcement of the opening of negotiations for an Australia-US Free Trade Agreement;

DFAT has encountered no such negative reaction from our regional trading partners.

Pursuing trade links with Asia and the US is not a zero-sum game: the US is an important economic partner for most Asian countries, and a stronger and more prosperous Australia will be a better partner for them.<sup>54</sup>

6.70 The Committee acknowledges the merits of these arguments. There remains, however, the findings of the research mentioned earlier that was carried out by the Productivity Commission. This research examined ‘both theoretically and empirically, the effects of the trade and non-trade provisions of PTAs on the trade and foreign direct investment flows of member and non-member countries’.<sup>55</sup> This research concluded, among other things, that ‘of the 18 recent PTAs examined in detail, 12 have diverted more trade from non-members than they have created among members.’<sup>56</sup>

6.71 The Committee considers that the question of trade diversion is not the same as the broader question of damaged relations through a perception that Australia’s focus is beyond the region. The former is more amenable to objective measurement than the latter. The Committee reiterates its view that, when it comes to making assessments of the merits of a proposed new trading arrangement, it is important that governments seek comprehensive, independent advice that draws on detailed analysis of potential costs as well as potential benefits.

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54 *Submission 54*, p. 39 (DFAT)

55 Adams, R (et al) *The Trade and Investment Effects of Preferential Trading Arrangements – Old and New Evidence*, Productivity Commission Staff Working Paper, Canberra, May 2003, p(xi)

56 Adams, R (et al) *The Trade and Investment Effects of Preferential Trading Arrangements – Old and New Evidence*, Productivity Commission Staff Working Paper, Canberra, May 2003, p(xii)

## Retention of governments' policy flexibility and right to regulate

There is a significant lack of detail at the moment in terms of the sorts of regulatory changes that the Americans might be seeking under the free trade agreement process. We are very concerned about the time frame that is being advanced, which is moving very rapidly—at least on some of the recent comments last week—to a conclusion of a free trade agreement between Australia and the United States, for there to be full public discussion about the consequences of regulatory changes that the government may commit to in making those treaties. Without having the details, it is difficult for us to comment, but we do raise our very significant concern that there has to be a capacity for consideration and discussion before there are any binding consequences on Australian control of public policy.<sup>57</sup>

6.72 A prominent public concern with respect to both GATS and the US FTA was whether such agreements militated too strongly against the capacity of governments to regulate effectively and to prescribe domestic policies without them being challenged as breaches of agreements or impediments to trade. Such concerns relate particularly to environmental, investment and quarantine controls, cultural protections, and the provision of core public services. It is a particular issue in the context of the US FTA which uses a 'negative list' approach. Such an approach automatically binds all trade in goods and services to the liberalising commitments of the agreement unless specific exemptions from the agreement are identified. The negative list approach is discussed in more detail in the next section of this chapter.

6.73 The Committee notes the DFAT's strong reassurance concerning the retention by government of its right to regulate:

Some commentators have questioned the value of an Australia-US Free Trade Agreement because they argue that pressure from the US will force changes to important domestic public policy programs. These observations do not take account of the following important points:

- the Government, in the statement of Australian negotiating objectives released on 3 March 2003, explicitly committed itself to ensuring that outcomes from the FTA negotiations do not impair Australia's ability to deliver fundamental objectives in health care, education, consumer protection and supporting Australian culture and identity;
- it will, of course, listen carefully to any issues that the US Government wishes to raise in the course of the negotiations. No government entering such negotiations would rule out areas for discussions before the negotiations start.<sup>58</sup>

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57 *Committee Hansard*, 8 May 2003, pp. 14, 15 (Waters, Community and Public Sector Union)

58 *Submission 54*, p. 41 (DFAT)

USTR Zoellick's letter to Congress set[s] out US Objectives for the negotiations ... While these proposals are broad-ranging in scope the Australian Government's objectives statement makes clear it remains committed to the underlying objectives of current policy settings (see also discussion of goals and strategy). The Government has committed itself to ensuring that outcomes from the FTA negotiations do not impair Australia's ability to deliver fundamental objectives in health care, education, consumer protection and supporting Australian culture and identity<sup>59</sup>.

6.74 Notwithstanding these reassurances, many witnesses emphasised the risks to which domestic policies and regulations might be exposed as the FTA negotiations approached their difficult stages. Such anxiety has been compounded by the perceived relative weakness of Australia's bargaining position, captured in the statement of the APEC Centre study *Issues and Implications* that 'one way of viewing the economic association from the US perspective is to see it as the addition of another medium sized state roughly equivalent in GDP to that of Pennsylvania.'<sup>60</sup>

6.75 The following excerpts from submissions and evidence convey the general range and tenor of the public's concerns:

The DRS [Doctors Reform Society] believes that public services such as health care and water services will be targeted that could result in a compromise of public policy. It is concerning that DFAT has stated that aims of an FTA with the USA "will be to liberalise trade in goods and services, to facilitate trade and investment and to address government-level impediments to increased commercial exchanges". US Trade Ambassador Robert Zoellick has also stated that they seek "enhanced access for US services firms to telecommunications and any other appropriate services sectors" (USTR Robert B. Zoellick, 2002). As US services firms already have access to commercial services in Australia the targets would be public services such as health care.<sup>61</sup>

The AMWU does not support the type of investor/state compliance mechanism that has been so infamous in the NAFTA [North American Free Trade Area] agreement. Despite earlier assurances to the contrary the mechanism in the NAFTA agreement has been used to allow companies to sue governments for compensation where governments have merely enacted legislation to protect the environment or health of the communities that they represent.<sup>62</sup>

I believe the department should be put under an onus to prepare what I call social and regulatory impact assessments of proposed commitments under ... free trade agreements... so that it is possible—for the public and the

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59 *Submission 54*, p. 45 (DFAT)

60 The Australia APEC Study Centre, Monash University, *An Australia-USA Free Trade Agreement Issues and Implications*, August 2001, p. 48.

61 *Submission 148*, p. 19 (Doctors Reform Society)

62 *Submission 68*, p 27 (AMWU)

Joint Standing Committee on Treaties, the parliament and for non-government organisations that have an interest in this—to engage on a transparent basis with what commitments we are negotiating.<sup>63</sup>

6.76 Questions of governments' right to regulate are particularly relevant to controls over environmental and health matters. Food labelling issues and broader environmental concerns associated with the proposed US FTA were a significant consideration for many contributors to the Committee's inquiry.

The US is the largest producer of food containing GMOs. Lobbying by agribusiness companies has ensured that there are no US rules for labelling to show GMO content in food. Australia has labelling requirements and a regulatory regime for GMO crops because consumers want to know whether food contains GMOs, so that they can make an informed choice. This attempt to remove the democratic right of informed choice from consumers should be rejected.<sup>64</sup>

6.77 The Committee notes that, whereas the government has commissioned studies into the economic impacts of the US FTA, it has not sought an assessment of the FTA's environmental impacts. Such an assessment, however, has reportedly been completed by OzProspect, a think-tank funded by the Myer Foundation, the Foundation for Young Australians and the Vizard Foundation. The findings are not encouraging.

The study concludes that if the US market for primary products is opened up for Australian farmers, the resultant expansion in agricultural production would increase Australian water use by up to 1.3 trillion litres a year – almost as much as the entire national domestic water use.... [Michael Cebon, the report's author] calculates that Australia's annual energy-related greenhouse gas emissions from agricultural production would rise by two million tonnes, or by more than 25 per cent.<sup>65</sup>

6.78 Unlike Australia, the US Congress has passed legislation requiring that trade agreements must be accompanied by a review of their environmental impacts. These reviews must include 'significant opportunities for public involvement'.<sup>66</sup> Given that Australia is experiencing what has been described as a national water crisis, the Committee is concerned that the Commonwealth environment Minister and the State Premiers may not have given adequate consideration to the potential environmental impacts of the proposed US FTA.

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63 *Committee Hansard*, 8 May 2003, p. 28 (Murphy, National Tertiary Education Union)

64 *Submission 86* (Rainforest Information Centre/Friends of the Earth)

65 Davidson, K 'A free trade pact will hurt our environment' *The Age* 3 November 2003, p. 11.

66 Davidson, K 'A free trade pact will hurt our environment' *The Age* 3 November 2003, p. 11.

## Negative list approach

6.79 Several witnesses raised with the Committee their concern that, unlike the approach to liberalisation of services under GATS where the government makes commitments to liberalise certain services by specifically nominating them (a ‘positive’ list), the US FTA utilises a ‘negative list’ approach to trade in services and investment. Under such an agreement, all trade in services and investment is regarded as automatically ‘free’, apart from any items that are specifically excluded from liberalization (a ‘negative’ list). Governments normally achieve this exclusion by taking out ‘reservations’ with respect to certain services, thereby retaining their right to regulate or amend policies regarding those services into the future. These reservations are normally spelled out in annexes to the main agreement.

6.80 Australia had been a very strong advocate of a ‘negative list’ approach to its FTA with Singapore – an approach which took many months of negotiation to settle as a *modus operandi*. Negotiations with the US settled on a negative list approach from day one.

We saw the inherent greater liberalising thrust of that approach and the transparency that comes with a negative listing as being pluses for our objectives to be best met in negotiations with Singapore.

With the United States, a very similar approach occurs. They adopt a negative list approach in their NAFTA agreements. That is the approach we both stepped off from. We believe that approach certainly is appropriate to achieving very much a GATS-plus outcome on services as part of these negotiations. It is more transparent, it is inherently more liberalising but at the same time—in getting to some of the comments and criticisms perhaps of the negative list approach—it still provides government with the flexibility to take reservations to ensure that, where it has measures in place not in conformance with the obligations taken in terms of national treatment or market access, we can fully reserve those and commit to a standstill provision, and that is annex 1.

Essentially annex 1 is a standstill where we have a measure that is inconsistent with the obligations but where effectively we agree to be bound. In Singapore—and we would do the same in the United States—we agree not to make that measure any more inconsistent and have it become any more trade restrictive than at the date of entry into force of the negotiations. That is the value of a binding. As I have said, the GATS-plus element is reflected very much in the liberalisation that has happened in Singapore over recent years. That standstill commitment from Singapore was locked in and was a key part of the outcome. That is very much one of the pluses we see in these processes.

Annex 2, the second annex to this negative list, allows us to carve out whole sectors from the obligations in those two chapters of services and investment. That means the government maintains full flexibility to introduce new and more restrictive measures in relation to those sectors. The negative list approach—even though to my mind it is inherently more liberalising—has the capacity still to maintain flexibility, where necessary,

and for the government to take whatever reservations it considers necessary in order to ensure there is that flexibility in the future. That is how we have approached it<sup>67</sup>.

6.81 The Committee agrees that a negative list approach is ‘inherently more liberalising’, and acknowledges the use of annexes to reserve or ‘carve out’ certain specific services from the universal coverage of the agreement. However it is the very universality of the agreement -covering present and yet-to-emerge services, and binding governments into the future - that is problematic.

The primary problem with a negative list approach is that all future services that have not been created—have not been developed, have not evolved—are automatically liberalised with a negative list approach...

We find it difficult to understand the logic of precluding the regulatory options of future governments for future services whose dynamics and needs are not known. At least with a positive list approach, whilst there may well be arguments... about what should and should not be included on the list, you are not foreclosing the future for future regulatory needs...

The other problem with a negative list approach is that with your existing service sector you have one opportunity to get it right—the first time—in deciding what provisions need to go on that annex that retains the ability to introduce new trade restrictive measures and what sectors go on that annex that only allows you to maintain your existing trade restrictive measures. They are the two concerns we have with that structure.<sup>68</sup>

6.82 In the Committee’s view, the negative list approach raises several issues of accountability and responsibility that must be weighed against the argument for the inherently liberalising effect of the negative list. Parliamentarians have a special duty of care under these circumstances. They have a responsibility to the citizens that they currently represent to ensure that any commitments undertaken serve their constituents’ economic and social interests. They also owe a duty of care to future generations who may have to live with adverse consequences flowing from commitments made.

6.83 For example, an agreement struck some years ago without foreknowledge of the advent of the internet, may have led to commitments in electronic communications that prevented later governments regulating to control pornographic content or email spam.

6.84 Parliamentarians of the future, too, will have to grapple with any issues that may arise if undertakings implied by the negative list approach deny them the capacity to regulate for desired social policy outcomes. Parliamentarians and ministers cannot

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67 *Committee Hansard*, 2 October 2003, pp505-506 (Deady, DFAT)

68 *Committee Hansard* 22 July 2003, p241 (Murphy, ACTU)

see into the future. The Committee therefore believes that a negative list approach militates against prudent and responsible decision-making.

6.85 Witnesses highlighted the difference in the approaches between the GATS and the US FTA, noting in passing that Australia's arguments in the WTO Uruguay Round for a negative list approach in GATS were 'not persuasive in terms of the final outcome'.<sup>69</sup>

The government has tried to reassure us about GATS by emphasising that it is a positive list agreement—that is, that it only includes what each government actively decides to list in the agreement...

The US free trade agreement negative list for services brings back the whole GATS agenda in a worse form because of the negative list. For example, if the government succeeded in its proposals to deregulate doctors' fees and university fees and the US free trade agreement was then signed, a future government could be challenged if it tried to reintroduce regulation to ensure more equitable access to these essential services.<sup>70</sup>

6.86 Given the agreement from day one that both Australia and the US wished to proceed with negotiations on a 'negative list' basis, the Committee acknowledges that such an approach would be enormously difficult to wind back. It is therefore extremely important that any reservations taken by the Australian government are carefully worded and thoroughly thought through.

6.87 In the Committee's view, a negative list approach is a highly risky strategy that appears not to be justified by the efficiency argument that it is 'inherently more liberalising'. Services and investment matters are becoming increasingly significant in the economies of developed nations that are engaged in global markets. A small error in the wording of a reservation, or an unanticipated technological development, or the devising of an entirely new service of major significance, could easily result in a country being deprived of the right, and a future government of its responsibility, to make policies about, and to regulate, that service in the national interest. The Committee does not relish the prospect of a future significant opportunity or benefit being 'spoilt for a half-penny's worth of tar.'

6.88 It is difficult to over-emphasise the importance of adequate parliamentary scrutiny of a process which involves automatic, binding commitments unless specific exemptions are identified. For all the reasons outlined above – attention to the national interest, accountability to citizens, intergenerational responsibility and incomplete knowledge of future developments – the Committee believes that the negative list approach should be avoided. The Committee notes that agreements such as the GATS eschew negative list in favour of a positive list approach.

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69 *Committee Hansard* 22 July 2003, p241 (Murphy, ACTU)

70 *Committee Hansard*, 23 July 2003, p. 275 (Ranald, AFTINET)

## Recommendation 12

6.89 **The Committee recommends that future bilateral trade agreements be pursued without recourse to a negative list approach.**

### Specific issues arising from FTA negotiations

#### Pharmaceuticals

6.90 Concerns about the possible impact of a US FTA on Australia’s regulations concerning the advertising of prescription drugs, and on the Pharmaceutical Benefits Scheme have agitated the public mind throughout the trade negotiation process.

The PBS is widely reported to be a preoccupation of the USA, notwithstanding its omission from the USTR letter. This scheme is essential to the affordability of prescription drugs and hence critical to the maintenance of public health in this country. The ACTU would also strongly oppose any US suggestion that the Australian prohibition on advertising prescription drugs to consumers be replaced by the American model of setting standards for such advertising. There is enough evidence to suggest that advertisements promoting prescription drugs to doctors can have cost-escalation effects because of the displacement of generics from medical prescriptions. Allowing direct advertising to consumers would compound the problem. No commitments should be given that would undermine the PBS.<sup>71</sup>

6.91 The Committee probed DFAT officials concerning the threat to the PBS and related matters, and was assured that resistance to any such threat would be robust.

At this point [2 October 2003] no specific proposal has been put to us by the United States on the PBS. We are open to continuing to explain the operation of the scheme to them, very much on the basis—and this is a very clearly stated objective of the government in this area—that we are not in any way negotiating in the FTA an outcome that would limit the ability of the government to provide a sustainable PBS and affordable medicines. That is very much the vision that has been articulated and that we have put very clearly to the United States.<sup>72</sup>

6.92 DFAT’s submission to the Committee also spoke in similar terms:

The Australian Government remains committed to providing Australians with access to quality and affordable medicines through a sustainable Pharmaceutical Benefits Scheme (PBS).

- in this respect it should be noted that the Chief US Negotiator has stated publicly that the US is “not going after” the PBS (See *The Australian* and the *Sydney Morning Herald*, 22/3/03)

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71 *Submission* 125, pp. 7-8 (ACTU)

72 *Committee Hansard*, 2 October 2003, pp. 510, 511 (Deady, DFAT)

- US pharmaceutical companies in Australia have expressed support for the integrity of the PBS in relation to the Australia-US FTA negotiations.<sup>73</sup>

6.93 Barely three weeks after Stephen Deady's assurances to the Committee on the PBS, the press reported the Australian Medical Association as claiming that Australians could face paying twice as much for prescription drugs if the PBS was included in the FTA.<sup>74</sup> Health Minister Tony Abbott was quick to respond, declaring:

The Pharmaceutical Benefits Scheme will not be a bargaining chip in these negotiations and frankly, it shouldn't be, because the [PBS] does not discriminate between overseas and locally produced drugs. It is not a trade instrument... it is an instrument for ensuring Australians get reasonable access to affordable drugs.<sup>75</sup>

6.94 *The Canberra Times* on 1 November 2003 reported that 'Australia and the United States have postponed free trade negotiations on key issues such as agriculture and pharmaceuticals until early next month'. It also stated that the US team 'had not yet provided a proposal on the ticklish issue of pharmaceuticals access to Australian markets.'

6.95 US negotiator, Ralph Ives, was reported as saying that the Australian government had been 'very clear on the sensitivity of this [PBS] issue and the fact that the fundamental nature of the program will not be changed' adding that the US is 'looking at some of Australia's own reports and commissions to see ways that the Australian government has identified that the system could be improved.'<sup>76</sup>

6.96 For the Committee, the US negotiator's remarks are code for 'We are not letting go of our aspirations for more favourable PBS arrangements'. AAP news service has also reported that the US 'has signalled [that] it plans to bring its most contentious demands, such as changes to the PBS, up at [the final round of talks set down for early December in Washington].'<sup>77</sup>

6.97 The Committee concurs strongly with the views of Health Minister Tony Abbott that the PBS should not be a 'bargaining chip'. In the Committee's view, any US proposal that undermines the fundamental integrity of the PBS, or leads to dramatic price increases, should not be entertained.

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73 *Submission 54*, pp. 41-42 (DFAT)

74 General news: 'A striking deal on balance in trade' *Daily Telegraph* 25 October 2003, p17.

75 Hon Tony Abbott MP quoted in 'Drugs threaten US trade deal' *The Australian* 27 October 2003.

76 Ralph Ives quoted in 'Aust, US postpone talks on free trade' *Canberra Times* 1 November 2003, p. 4.

77 'Doubts grow on US trade deal' *The Canberra Times* 3 November 2003, p. 6.

### Recommendation 13

**6.98 The Committee recommends that the government declare that it will not entertain any further proposals from the United States that go to the structure or operation of the Pharmaceutical Benefits Scheme, or that in any way undermine the effectiveness of the PBS as a price capping mechanism. Accordingly, the government should exempt the PBS from the proposed Australia-US Free Trade Agreement.**

### Quarantine

6.99 Australia, as a largely disease free island continent, has always maintained a strict quarantine regime and has insisted that all its quarantine decisions are determined on a scientific basis. Trading partners have sometimes criticised Australia's quarantine rules as a disguised trade barrier. The EU has been a recent notable critic of Australia's position, claiming that many of the prohibitions have no scientific basis.<sup>78</sup>

6.100 Several witnesses believed that negotiations on the US FTA would produce a watering down of quarantine standards. One industry representative was quite explicit about the US's motives.

Having failed over the years to break down Australia's quarantine regime on chicken meat, and having declined to contest Australia's decisions in the WTO, United States officials appear to be using the opportunity of this FTA negotiation to attack Australia's quarantine protection of its chicken meat industry, and to obtain results which could not be achieved in WTO processes.<sup>79</sup>

6.101 DFAT, however, has insisted that quarantine matters are of utmost importance:

The Government will not enter into any arrangement that would compromise the scientific integrity of Australia's quarantine regime, nor the broader objective of protecting human, animal and plant health.<sup>80</sup>

6.102 Such assurances are still not sufficient to quell the fears of those agricultural and horticultural industries that have a strong interest in keeping diseases at bay:

Australia's FTA negotiating objectives were announced on 3 March (MVT13/2003). This confirmed that quarantine will be "in play" in the negotiations in response to the US negotiating agenda. It is also relevant that reportedly extensive and detailed prior discussions on quarantine

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78 European Union Delegation of the European Commission in Australia, *EU News* No.4, October/November 2003, p. 5

79 *Submission* 31, p. 3 (Australian Chicken Meat Federation)

80 *Submission* 54, p. 42 (DFAT)

between Australia and the United States have been held throughout the last year (Zoellick 2002).<sup>81</sup>

6.103 The Committee believes it would be irresponsible in the extreme for Australian negotiators to make concessions on quarantine rules in response to demands from US agricultural export interests. It is confident that the government will adhere to its promise to retain the scientific integrity of Australia's quarantine regime.

#### **Recommendation 14**

**6.104 The Committee recommends that in view of the risks associated with the negative list approach, the government exempt Australia's quarantine laws from negotiations for the proposed Australia-US Free Trade Agreement.**

#### **Genetic modifications and food**

6.105 Consumer advocacy and environmental groups pressed upon the Committee their concerns about the differences between the US and Australia with respect to genetically modified foods and their labelling. Australia's gene technology labelling requirements are contained in FSANZ food standard 1.5.2. These were introduced in response to strong public concern about the risks posed to human health and safety by GM foods and a variety of objections relating to GMO production processes.

6.106 Referring to USTR Zoellick's letter to Congress seeking a Trade Promotion Authority, the Australian Conservation Foundation stated in its submission that:

The U.S government has indicated that through the FTA negotiations it will seek to have Australia reaffirm its WTO Technical Barrier to Trade Commitments (TBT), including those relating to labelling requirements on U.S food and agriculture products produced through biotechnology, and eliminate any unjustified TBT measures. Although it is not yet entirely clear, this objective indicates that the U.S will seek the Australian government's commitment to remove or weaken Australia's food labelling laws relating to GMOs.<sup>82</sup>

6.107 This reading of the Zoellick letter was questioned by a trade consultant in the following terms:

I have not seen that. It was run up early and a lot of the civil society groups are saying that it is an issue. When the Zoellick letter, the first letter of notification to congress, went in, right at the top it had biotech related to the food issue. A couple of groups thought that meant GMOs. I was over there and I asked the American negotiators what the issue was and they were

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81 *Submission 31*, p. 6 (Australian Chicken Meat Federation)

82 *Submission 24*, p. 5 (Australian Conservation Foundation)

surprised to be told that it was GMOs. They do not have a GMO agenda. Somebody has jumped the gun on that one.<sup>83</sup>

6.108 The Committee is aware that the preamble to the WTO's Technical Barrier To Trade Agreement states that 'no country should be prevented from taking measures necessary to ensure the quality of its exports, or for the protection of human, animal, and plant life or health, of the environment, or for the prevention of deceptive practices, at the levels it considers appropriate'. However, Members' regulatory flexibility is limited by the requirement that technical regulations 'are not prepared, adopted or applied with a view to, or with the effect of, creating unnecessary obstacles to trade'. (Article 2.2)

6.109 The Committee agrees with Greenpeace that 'the requirement for labelling of genetically engineered food products in Australia is not a technical barrier to trade. Rather it fulfils a legitimate objective in protecting human health and safety, and as such is a justifiable TBT measure under the WTO/TBT Agreement'. The Committee notes that Australian labelling requirements for products from the United States are no less favourable than those accorded to national products or products from other countries.

Labelling of genetically engineered food products is justifiable as the method of production of genetically engineered food, that is using genetically engineered organisms, is fundamentally different to the production of non-GE food products, and *could well result in altered product performance*. Long term scientific information about the health impacts of genetically engineered foods is limited, and therefore product information for GE food should be available in the form of labelling.<sup>84</sup>

6.110 In the Committee's view, it is important that Australia does not make any concessions to reduce labelling laws or standards for genetically engineered foods, and also that Australia ensures that future improvements in or extensions to labelling standards are not precluded by any undertakings in the US FTA.

### **Recommendation 15**

**6.111 The Committee recommends that in view of the risks associated with the negative list approach, the government exempt Australia's genetic engineering regulatory regime (including that dealing with labelling and GE free zones) from negotiations for the Australia-US Free Trade Agreement.**

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83 *Committee Hansard*, 9 May 2003 (Oxley, AUSTA)

84 *Submission 159*, p. 3 (Greenpeace)

## Local content rules in media

A red flag for Australians is that according to all reports the US has ambitious services liberalisation objectives for the AUSFTA negotiations. It has long sought the abolition of our local content requirements for audiovisual services such as free to air television programmes, advertising, and radio music content. The... audiovisual services sector is highlighted by the USTR as one of the liberalisation gains from the recent FTA with Chile... Australia should reject any US overtures for the abolition of local content requirements. Australia should also refrain from agreeing in AUSFTA to reduce the various percentage content requirements for audiovisual sub-sectors. Whether the existing quotas are maintained or varied should be a matter for successive Australian governments to decide.<sup>85</sup>

6.112 The Committee encountered vigorous advocacy from screen writers, producers, artists and media workers in favour of strong protection for cultural policies such as quotas of Australian production in television and interests related to audio-visual services, copyright and the development and delivery of the so-called ‘creative industries.’

6.113 The President of the Australian Writers’ Guild, Ian David, expressed the core concern in the following terms:

This is a vital issue for every Australian, because it is about whether we will have a distinctive voice with which to express ourselves in the future. To some this may just be about trade, commerce and access to markets. To us it's about our heritage, our identity, our livelihood.<sup>86</sup>

6.114 The Guild also drew to the Committee’s attention the Government’s position in respect of the audiovisual sub-sector as articulated in the Australian Intervention on GATS made in Geneva in 2001:

Australia has long recognised the essential role of creative artists and cultural organisations in reflecting the intrinsic values and characteristics of our society, and is committed to sustaining our cultural policy objectives within the context of multilateral trade negotiations...It is essential that Australia’s media reflects Australian identity, character and cultural diversity and provides an Australian perspective on local and international events.

Australia remains committed to preserving our right to regulate audiovisual media to achieve cultural and social objectives and to maintain the broad matrix of support measures for the audiovisual sector that underpin our cultural policy; including retaining the flexibility to introduce new measures in response to the rapidly changing nature of the sector.<sup>87</sup>

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85 *Submission 125*, p. 6 (ACTU)

86 *Submission 40*, p. 5 (Australian Writers’ Guild)

87 Australian Intervention on Negotiating Proposal on Audiovisual Services, CTS Special Session, Geneva, July 2001. Cited in *Submission 40*, p5 (Australian Writers’ Guild)

6.115 Notwithstanding such unequivocal commitments, reported statements by Prime Minister Howard and Trade Minister Vaile around the time of US President Bush's visit to Australia indicate that, while they retain support for existing quotas, the Prime Minister said that 'in looking at future or new media, we are prepared to be fairly flexible there'.<sup>88</sup> The US has been pushing hard to make further inroads into the Australian film and TV market, even though American programs already account for 69 per cent of the overseas fare shown on Australian televisions, and around two thirds of the films shown in Australian cinemas.

[Y]ou may be aware of the 'soothing' comments... made by the US... about how they could go forward and live with and accept the regime that we presently have in place as far as our local content is concerned. That position in the parlance used in the trade areas is described as 'standstill'. We believe that the arguments about a standstill position are completely unacceptable...

It is unacceptable because we are working in an area of very fast and dramatic changes in terms of technology and production, delivery and distribution of audiovisual services. It is impossible to predict the systems that will evolve to distribute and deliver audiovisual programming cultural product in the coming years—within five years, let alone 10 or 15 years. To agree to standstill now would be perhaps the equivalent—as I often like to say to people—of having an inquiry about radio in 1950, agreeing to lock off on certain conditions concerning radio and not being aware of a thing called television, which was about to burst on to the scene<sup>89</sup>.

6.116 The problems with 'standstill' positions came to the fore in the late 1990s when New Zealand, having made full commitments to market access in GATS Modes 1, 2 and 3 for production, distribution, exhibition and broadcasting of audiovisual works, found itself unable to re-introduce local quotas in free-to-air television in accordance with the new government's cultural policy. The Committee shares the concern expressed by witnesses about these and associated threats to governments' abilities to meet their preferred cultural objectives.

It is imperative that cultural industries are not part of the same discussions that encompass wheat, lamb, sugar and steel. Culture is not transferable, nor is it replaceable. Australians must maintain their ability to tell their own stories to their own people, on film, television, interactive media and radio, through music, dance, Indigenous expression design, crafts and the spoken and written word.<sup>90</sup>

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88 John Howard MP quoted in 'Fears grow over free-trade deal concessions' *Sydney Morning Herald* 24 October 2003, p. 6.

89 *Committee Hansard*, 23 July 2003, pp. 258, 259 (Dalton, Australian Film Commission)

90 Brown, G 'Protecting our cultural diversity' *Australian Chief Executive*(CEDA) April 2003, p. 27

6.117 The US is pressing for much greater regulatory freedoms in products that are delivered digitally, but it is precisely in this form that, in future, most cultural product will be produced, stored and delivered. It was suggested to the Committee that, for the US, success in this area as part of the Australia-US FTA, would be a valuable precedent for its attempts to secure better access to other major markets – notably the European Union.

We believe that this treaty is terribly important to the Americans. It is not important in terms of market access, because they have that—they have everything they want out of Australia really—it is important to the Americans because they are slowly building a series of bilateral agreements, and this is the first bilateral agreement they are negotiating with a developed country in this particular round they are pushing into at the moment and they do not want to have on that treaty in any way something which undermines their fundamental position.<sup>91</sup>

6.118 In its submission to the Committee, DFAT stated that the Government ‘will take into account Australia’s cultural policy objectives, and the need to maintain our capacity to support Australian culture and national identity. The Government recognises the need for appropriate regulations and support measures to achieve these objectives in areas such as audiovisual media.’<sup>92</sup> On 2 October 2003, Australia's negotiator Stephen Deady told the Committee:

As I say, we are talking to industry about this, but the government’s commitment in terms of its objectives here is very clear, and that is that we will be ensuring that our cultural objectives can continue to be met. Ralph Ives has said publicly that the US are comfortable with the current arrangements—the local content requirements on broadcast television and the other aspects of the existing arrangements. He went further in fact and said that the subsidies that are provided for those cultural activities in Australia are also not a concern to the United States. Those are significant statements. We are continuing to talk to the industry about precisely what that means and what the reservation, if any, would look like in relation to that sector.<sup>93</sup>

6.119 But barely a month later US negotiator, Ralph Ives, was reported as saying, with respect to arrangements for the future, that ‘the proposal by Australia is too broad and we need to work on narrowing that.’<sup>94</sup>

6.120 The Committee is aware that Australia has a Free Trade Agreement with Singapore ‘which many in the arts industry see as the optimum model to secure indigenous culture because it builds in protection for the local industry in

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91 *Committee Hansard*, 23 July 2003, pp. 265, 266. (Dalton, Australian Film Commission)

92 *Submission 54*, p. 42 (DFAT)

93 *Committee Hansard*, 2 October 2003, p. 511 (Deady, DFAT)

94 Quoted in Davis, M ‘FTA progress on local content’ *Australian Financial Review* 1 November 2003

perpetuity.’<sup>95</sup> This contrasts with the FTA that the US struck with Chile, whereby the Chilean government ‘gave up its right to give preferential treatment to Chilean producers of any computer programs, text, video images, sound recordings and other products that are digitally encoded and transmitted electronically.’<sup>96</sup> The Australian government’s recently declared willingness to be ‘flexible’ with regard to local content and similar rules for future media forms has prompted considerable alarm within domestic media production and other cultural industries.

6.121 The Committee believes that cultural protection is a critically important responsibility for government, and that any specified protections related to it must be technologically neutral. If e-commerce is defined as ‘all digital products’ this is a clear back door way to include cultural industries in a trade agreement. In the Australia-Singapore FTA a narrow definition of e-commerce was used that excluded Australia’s cultural industries.

The Australian Singapore Free Trade Agreement chapter on e-commerce is limited to dealing with trade transactions that use e-mail or electronic data exchange. Both countries agreed to base their domestic legal framework for electronic transactions on the United Nations Commission on International Trade Law (UNCITRAL) Model Law on Electronic Commerce. ... None of [the wording of] this suggests that e-commerce is being defined as widely as it is by the notion of ‘digital products’.... Cultural goods and services such as books, video, DVD, music and downloadable films are also now traded via e-commerce with few, if any, barriers. However, these goods and services do not lose their cultural characteristics because of the means by which they are traded.<sup>97</sup>

## Recommendation 16

6.122 **The Committee recommends that:**

- a) **the narrow definition for e-commerce used in the Singapore-Australia FTA be the definition for e-commerce in the Australia-US Free Trade Agreement; and**
- b) **the government ensure that Australia’s cultural objectives will not be compromised by avoiding any concessions or undertakings that would enable future technologies or content delivery platforms to undermine or circumvent existing or future cultural protection policies.**

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95 Hackforth-Jones, P ‘A Mickey Mouse trade agreement?’ *Australian Financial Review* 18 October 2003, p. 30.

96 Letts, D (Music Council of Australia) in a Letter to the Editor, *The Australian* 27 October 2003, p. 10.

97 *Submission* 155, para 6.2 (Australian Film Commission)

**Accordingly, the Committee recommends that the government exempt Australia's cultural industries from the proposed Australia-US Free Trade Agreement.**

6.123 Perhaps the most pertinent observation on the state of play has been provided by Tim Colebatch, the economics editor at *The Age* newspaper:

Ultimately, this will be a deal between politicians, to decide what they can afford to give away and what they cannot. Taking on the film industry is the big risk for Howard, when Vaile has repeatedly told the industry and the public that “we will ensure our capacity to support Australian culture and national identity including audiovisual media is not watered down in the negotiations.” Now the Government proposes to do the exact reverse. Time will show whether it is worth it.<sup>98</sup>

## Investment

6.124 In the opinion of some commentators, the US FTA ‘is not about trade at all. It is about investment flows’<sup>99</sup>, and the Committee received an array of comments about perceived dangers in the closer Australia-US financial integration that an FTA would entail.

6.125 USTR Zoellick, in his letter to the US Congress, listed the following as the US’s objectives on investment

- Seek to establish rules that reduce or eliminate artificial or trade-distorting barriers to U.S. investment in Australia, including investment screening by the Australian Government, while ensuring that Australian investors in the United States are not accorded greater substantive rights with respect to investment protections than U.S. investors in the United States, and to secure for U.S. investors in Australia important rights comparable to those that would be available under U.S. legal principles and practice.
- Seek to ensure that U.S. investors receive treatment as favorable as that accorded to domestic or other foreign investors in Australia and to address unjustified barriers to the establishment and operation of U.S. investments.
- Provide procedures to resolve disputes between U.S. and Australian investors that are in keeping with the goals of making such procedures expeditious, fair and transparent.

6.126 The model for investment provisions ‘comparable to those that would be available under U.S. legal principles and practice’ is the North American Free Trade

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98 Colebatch, T ‘New-look trade map a work in progress’ *The Age* 25 October 2003

99 Hamilton, C ‘Free trade deal won’t produce the goods’ *Australian Chief Executive* (CEDA) April 2003, p. 53.

Area agreement (NAFTA). In particular, Chapter 11 of the NAFTA agreement has drawn extensive criticism, with opponents alleging that it gives corporations too much power to bend to their will the governments of those countries in which they invest and operate. The concerns of such opponents are captured in the submission to the Committee from the Australian Fair Trade and Investment Network:

NAFTA itself has been characterised as more an investment treaty than a trade treaty because of the significance of its investor rights regime. Investor rights in NAFTA have been enforced against governments by powerful multinational corporations, particularly in the past seven years. If an Australia-US Free Trade Agreement is to include provisions similar to those of NAFTA, the almost inevitable outcome will be a reduction in the capacity of all levels of Australian government to regulate.

The US is seeking the abolition of the Foreign Investment Review Board ... The Foreign Investment Review Board has the power to review other foreign investment in the national interest. Its discretion is very seldom exercised, but it is a power which the Australian government should retain. The US is also seeking a complaints mechanism for investors which is likely to be modelled on the NAFTA disputes procedure. This would enable US corporations to take legal action to force changes in Australian law if they could argue that the law was not consistent with the agreement. They could also sue the Australian government for damages...

Chapter 11 of NAFTA defines ‘investors’ widely and grants them broad rights. Only the parties - that is, the governments - to NAFTA may be sued, but they may be sued by investors, that is, corporations. The government ‘measures’ which can be challenged as infringing on investors’ rights include ‘any law, regulation, procedure, requirement or practice’ at all levels of government. Disputes are decided in one of two international arbitration panels originally set up for the resolution of disputes between private, rather than public, bodies. These bodies – UNCITRAL and ICSID – do not provide the levels of openness of national courts. While investors sue governments seeking public money and seeking rulings on the appropriateness of public policy decisions, members of the public are not informed of the disputes or afforded the opportunity to be heard.<sup>100</sup>

6.127 The Committee is aware that the rules of procedure for ICSID and UNCITRAL dispute settlement bodies all derive from a commercial arbitral model. They are ‘ad hoc tribunals without the fundamental principles of transparency in procedure or open hearings, they do not have to notify the public in the event of registration of a claim, nor is there any public interests requirements as found in domestic administrative law.’

These may not be pertinent issues when two international private actors are in arbitration over commercial matters, however, when one party is a state party, which is essentially a representative of a collectivity, of the people,

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100 *Submission 42*, pp. 37-38 (AFTINET)

“the policy goals of the state become implicated in the dispute” . Therefore... it is imperative that any dispute resolution process follow the principles underlying our domestic courts, the process must be open, transparent and accountable, and ...amicus briefs from persons or sectors, whether industry, agricultural, human rights or labour, whose rights or interests may be affected must be allowed. A further [concern] ... is the relationship between a private ad hoc dispute settlement mechanism and Australia's domestic courts, developing jurisprudence under NAFTA suggests the potential for conflict between the two legal systems.<sup>101</sup>

6.128 The Committee explored with Australia's lead negotiator Stephen Deady the extent of the investment issues being proposed for the FTA. Particular attention was given to whether NAFTA-style provisions were likely to be included in a US FTA, and, if so, the extent of any amelioration of the Chapter 11 problems. Mr Deady advised that:

... there have been adjustments to the investor state dispute settlement mechanisms since NAFTA. There has been some refinement, certainly, in the US approach to these... Those clarifications or interpretations of the NAFTA articles, in terms of direct or indirect expropriation that it talks about, have themselves been reflected in trade promotion authority. They are also reflected in the US-Singapore and US-Chile agreements.<sup>102</sup>

So there is greater certainty, I think, and greater clarity about precisely what these articles mean. There have been changes made to the chapter 11 type procedures and language in the subsequent US agreements, reflecting some of these interpretations. That is now the basis on which this discussion will take place between ourselves and the United States—if, in fact, we do get to discuss an investor state dispute process.<sup>103</sup>

Neither [the US nor Australia] has yet introduced language on an investor state clause into the chapter on investment.<sup>104</sup>

With respect to the third category—and I would say at the moment that this is where this investor state dispute settlement is—we have talked about it, we have explained our approach in Singapore, we have asked questions of the Americans and their experience with NAFTA, what they did with Singapore and what they have done with Chile. We have asked the question: with two developed countries, these are some of the issues this throws up; do we really need this sort of article? Both countries have reflected on that and gone back and had internal discussions, and they are still going on. It is certainly very much a possibility as part of the agreement, but neither

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101 *Submission 14*, pp 4-5 (Liberty Victoria)

102 *Committee Hansard*, 2 October 2003, p. 501 (Deady, DFAT)

103 *Committee Hansard*, 2 October 2003, p. 509 (Deady, DFAT)

104 *Committee Hansard*, 2 October 2003, p. 503 (Deady, DFAT)

country as yet has come forward and specifically put down language saying, 'Yes, we want one and this is what we think it should look like.'<sup>105</sup>

6.129 The Committee notes that while Australia has investor-state clauses in a range of agreements, until recently these have always been with developing countries. They have been used to protect Australian investments from expropriation by governments in those countries where the rule of law is weak. The Australia-Singapore FTA is the first agreement with a *developed* country<sup>106</sup> that has included investor-state provisions.

The investment chapter of the Singapore free trade agreement enables an investor to challenge laws or regulation and to sue governments for damages if such laws breach the terms of the agreement in a way which causes loss or damage to the investor. There are similar clauses in the US-Chile and US-Singapore agreements, and this is clearly part of a template and a beachhead about investor state complaints mechanisms that the US wants to establish in terms of the global trade scene.<sup>107</sup>

6.130 The Committee remains concerned that an FTA modelled on NAFTA would grant US corporations inappropriate powers to challenge government regulation at local, State and Commonwealth levels. If, as seems likely, the United States regards US-Singapore and US-Chile FTAs as 'a template and a beachhead about investor state complaints mechanisms', Australia should not be surprised if the US negotiators seek to introduce them into the Australia-US FTA even at a very late stage in proceedings.

6.131 Witnesses frequently drew attention to various examples of where corporations, using NAFTA Chapter 11 provisions, had sued governments.

US corporations have aggressively challenged laws and sued governments on the grounds that their investments have been damaged... The US company, United Parcel Service... is suing the publicly owned Canada Post... arguing that Canada Post's monopoly on standard letter delivery is in violation of provisions on competition policy, monopolies and state-run enterprises...

The US Metalclad Corporation was awarded \$15.6 million because it was refused permission by a Mexican local municipality to build a hazardous waste facility on land already so contaminated by toxic waste that local groundwater was compromised. It won that suit. Ethyl Corporation, a US chemical company that produces a fuel additive called MMT which contains manganese and is hazardous to human health, successfully sued the Canadian government when it tried to ban MMT on health and safety grounds...

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105 *Committee Hansard*, 2 October 2003, p. 503 (Deady, DFAT)

106 Singapore is categorised by the IMF as an 'advanced economy' – a category that includes countries like Australia, Sweden, Belgium, Taiwan.

107 *Committee Hansard*, 23 July 2003, p276 (Ranald, AFTINET)

I should also indicate that ... the US Council of State Governments, the National League of Cities—which represents local government—plus the National Labor Advisory Committee to the US Trade Representative have all, in their reports to the US Trade Representative on the Chile and Singapore US free trade agreements, objected to the investor dispute process in those agreements. Although it is slightly different from NAFTA, they do not consider it is different enough to protect against these sorts of suits and to protect against the unreasonable restriction on the right of governments to regulate.<sup>108</sup>

6.132 To the Committee, it appears that the proposals listed in the USTR's statement of objectives are similar to key aspects of the ill-fated OECD Multilateral Agreement on Investment that drew broad, hostile and effective community criticism during the late 1990s. In the Committee's view, any threat to government's capacity to regulate foreign investment matters should be strongly resisted. The Committee also believes it is vital that dispute settling mechanisms built into any trade agreements, bilateral or multilateral, are transparent and provide an opportunity for bona fide NGOs and to express their views as part of any tribunal processes.

6.133 According to the evidence cited above (put by Australia's lead negotiator Stephen Deady) both the Australian and US negotiators have asked the question: 'Do we really need an investor-state provision?' and neither country had at that stage (October 2003) come forward with a specific proposal. The US FTA Briefing No.4 published by DFAT states: '...both Australia and the US have strong, robust and independent legal systems, which provide an effective avenue for our investors to pursue issues of concern to them. In that light, the need to create an alternative ISDS mechanism in an FTA... appears to be less compelling than it might be in other agreements.' The Committee concurs with the government's view, and regards such a provision as unnecessary.

### **Recommendation 17**

6.134 **The Committee recommends that:**

- a) **the Australian government retain its capacity to regulate foreign investment, including the retention of the Foreign Investment Review Board; and**
- b) **no investor-state provisions be included in the Australia-US Free Trade Agreement.**

### **Agriculture**

6.135 There is little doubt that agricultural issues have been a prominent aspect of negotiations for an Australia-US Free Trade Agreement, with broad general support

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108 *Committee Hansard*, 23 July 2003, p. 276 (Ranald, AFTINET)

for an FTA coming from highly efficient Australian producers all very keen to export. Unsurprisingly, farm issues are also the issues that have proven most difficult to resolve, and at the end of the fourth round of officials-level talks in October 2003, agriculture continued to test the wit and try the patience of the negotiators.

6.136 The Committee sought to determine a clear sense of the position of Australia's major agricultural interests with respect to the US FTA. The following is typical of the quite categorical views that were expressed:

The National Farmers Federation... will support the negotiation of a US FTA, on the condition that agriculture is at the heart of the negotiations and the final agreement. What does 'at the heart' mean; what are we seeking? ...[T]he US is an important market, but we do face several restrictions into the US for several of our commodities. The NFF seeks the elimination of tariffs and tariff rate quotas on agricultural exports to the United States. We seek this elimination upfront when the agreement is signed—not subject to long time lines.<sup>109</sup>

6.137 The Committee notes that such views were entirely congruent with the government position stated by Australia's lead negotiator, Stephen Deady, in evidence to the Committee:

[T]he government's position on the market access package in relation to agriculture and the United States has... been very clearly stated. We need a substantial market access outcome in negotiations with the United States. We need a significant, immediate improvement in access into that market and we need to be looking at the elimination of all border protections, tariffs and quotas on Australian exports of agricultural exports into the United States. That package... has to include those elements: significant and immediate improvements in the transparent process leading to the full elimination of tariffs and other quotas on agricultural products into the US market.<sup>110</sup>

6.138 At the close of the October 2003 round of negotiations, however, it appeared that the Australian negotiators were being confronted with a serious challenge to at least some aspects of that position. The original US farm trade offer had been described by Australian officials in mid-2003 as 'the big problem, too little, across the board'. In October 2003, Trade Minister Vaile described the revised US offer as only an 'incremental improvement'.<sup>111</sup>

6.139 The Prime Minister was quoted as saying to US President Bush that he would:

..understand if those benefits [for agriculture] build up over time, but there has to be an agreement that builds those benefits in. What [President Bush]

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109 *Committee Hansard*, 22 July 2003, p. 245 (Fargher, National Farmers Federation)

110 *Committee Hansard*, 2 October 2003, pp. 477, 478, 479 (Deady, DFAT)

111 Quoted in Wallace, C. 'Pack could cut a deal' *Weekend Australian* 25 October 2003, p. 26.

had in mind there was what the US had done in a number of other agreements. You can stagger how you do things if that helps to facilitate getting them through.<sup>112</sup>

6.140 The Committee is aware that US agreements with Canada, Mexico and Chile included timetables for the removal of barriers that extended to 15 years. According to the National Farmers Federation, these ‘exceptionally slow’ timetables had ‘undone the effectiveness’ of these deals.<sup>113</sup> This is of some concern to the Committee given that, in the recent free trade agreement struck between Australia and Thailand, the producers of Australia’s main agricultural goods will not achieve open access until 2020 – and 2025 in the case of the dairy sector.<sup>114</sup>

6.141 Following the Prime Minister’s comments on a ‘staggered’ approach, Peter Corish, President of the National Farmers Federation, was reported as saying that Australian farmers are seeking ‘significant improvements in market access up front... over very short transition times... For us, one to five years is probably an acceptable time.’<sup>115</sup>

6.142 Several witnesses pointed out that, even if tariff barriers to Australian goods were dropped, the US domestic farm subsidies would still place Australian producers at a competitive disadvantage – although at least one witness declared that this was not an insurmountable problem:

It might not be a completely level playing field but it levels it a hell of a lot. We believe that we can compete against subsidised product when there is open access. We at the moment ship product to both Korea and Japan. Both those countries subsidise their domestic producers. Domestic subsidies—and at some other stage I can show you evidence of this—tend to inflate cost structures in an industry.<sup>116</sup>

6.143 DFAT stressed to the Committee that the key element of the FTA as far as agriculture was concerned was that of market access and not US domestic subsidies.

The focus of FTAs, I have to say, is very much on... improving access for Australian agricultural exports into the US market...

I certainly am very prepared to indicate today that the negotiations with the United States as part of the FTA are not about seeking reductions in Farm Bill domestic subsidies. That is beyond the scope of the negotiations. The

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112 John Howard MP quoted in Allard, T ‘Fears grow over free-trade deal concessions’ *Sydney Morning Herald* 24 October 2003, p 6.

113 NFF President Peter Corish quoted in Allard, T ‘Fears grow over free-trade deal concessions’ *Sydney Morning Herald* 24 October 2003, p. 6.

114 Wright, S ‘Trade hurdles as US jumps at its chances’ *The Canberra Times* 1 November 2003.

115 Quoted in McKenzie, D ‘Access is vital to any deal’ *Weekly Times* (Vic) 29 October 2003, p. 13.

116 *Committee Hansard*, 23 July 2003, p. 296. (Barnard, Meat and Livestock Australia)

wording does reflect the objective that we took into the negotiations, and I do believe—looking at the language now—it is still broadly consistent with what we are trying to do. There are clearly some ambitions on export subsidies but not on overall reductions or the elimination of export subsidies as part of the FTA. Again, that is a bridge too far. That is for the multilateral processes..<sup>117</sup>

6.144 Other witnesses took a far less sanguine view of the subsidies issue, regarding them as problematic in themselves as well as setting unfortunate precedents for other trade agreements if changes to domestic subsidies were not included in a deal.

The fourth element of the economic case is that the acceptance that agricultural subsidies will be outside a bilateral free trade agreement—as is likely—would be WTO-minus, a development that would corrode the position of free trade agricultural exporters in the international system and negate any benefits from increased market access to the United States. In some discussions of the Australia-US FTA it has been said that subsidies will not be included. That is a big step back from the principles of trade agreements that have already been established in the WTO. On the issue in the international trading system that is more important for Australia than any other, this would be a WTO-minus agreement if it did not control subsidies and it would be a dreadful precedent for other negotiations. I have heard from continental European and Japanese trade policy people that they are delighted by what they hear about the US-Australia FTA because it will not lead to constraints on subsidies.<sup>118</sup>

The precedent unfortunately is already there in other arrangements that the United States has negotiated. But I think that because Australia is such a high profile supporter of agricultural trade liberalisation, Australia entering these arrangements with the United States would be more influential than Chile or Mexico entering these arrangements. So its demonstration effect would be costly, but even more important would be the demonstration effect of our accepting a trade agreement that did not provide a good model for subsidies.<sup>119</sup>

6.145 The Committee remains concerned about the levels of US domestic subsidies both in terms of making Australian products uncompetitive on the American domestic market, and also because they play such a huge part in American domestic political affairs – especially around election times. The Committee heard evidence of quite staggering levels of subsidy support in certain areas of US agriculture.

The world price for peanuts is about \$US250 a tonne. That is for farmer stock, not for the edible peanut component. US farmers are paid about \$US550 a tonne ... It is partly a farming subsidy. The government guarantees in the market loan \$US355 a short tonne, and they get that

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117 *Committee Hansard*, 2 October 2003, pp. 477, 478, 479 (Deady, DFAT)

118 *Committee Hansard*, 22 July 2003, pp. 198, 199 (Garnaut)

119 *Committee Hansard*, 22 July 2003, pp. 208, 209, 210 (Garnaut)

topped up to \$495 – to the target price – per short tonne. They have a special phrase like ‘loan deficiency payment’ ... and therefore is not considered a production subsidy.... They also then support the breeding program totally. Between the US government and US universities, they pay nearly \$US30 million into breeding programs. Total agricultural research in the US is somewhere between \$US60 million and \$US100 million on peanuts per annum.<sup>120</sup>

6.146 Counterpointing Australian producers’ views are the strong protectionist positions that have consistently been taken by American farmers and their representatives. As well, many American producers are unhappy about what they regard as unfair barriers (mostly quarantine-based) to their access to Australia’s market for US chicken, pork, stone fruit, corn and coarse grains. Australia’s monopoly wheat exporter, AWB Ltd, is also seen as a major impediment, with US wheat growers urging President Bush to ‘walk away from an FTA if AWB... is not opened up to competition’.<sup>121</sup>

6.147 It has not been lost among many observers that the farm lobby is a powerful influence on Congress, that President Bush comes from a farming state, as does his brother Governor Jeb Bush, and that the farm vote is crucial in any American election. Congressional rejection of an FTA that does not please American farmers is a distinct possibility.

### **Recommendation 18**

**6.148 The Committee recommends that the government retain the ‘single desk’ arrangements for wheat exports and that these arrangements be exempt from the proposed Australia-US Free Trade Agreement.**

6.149 The consistently reinforced commitment of President Bush and Prime Minister Howard to settle a deal before Christmas 2003 has put enormous pressure on negotiators to resolve the differences over agriculture. The Committee is concerned that political urgency or expediency could result in poor decisions about this notoriously complex and sensitive sector, or worse, that an FTA could be settled which goes nowhere near addressing the needs of Australia’s agricultural exporters.

6.150 The timeframe and dynamics of the whole negotiating process have been keenly observed by a number of journalists and commentators. One of them has opined that:

The US had set up a classic negotiating ambush. First, leave the biggest, most critical element of the deal to the last moment. Remember, there are just eight weeks to cut this deal if it is to get congressional approval before the election year makes its passage a practical impossibility. Second, make such a derisory offer that one’s (much smaller) negotiating partner squirms

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120 *Committee Hansard*, 24 July 2003, p. 349 (Hansen, Peanut Company of Australia)

121 AAP ‘Doubts grow on US trade deal’ *The Canberra Times* 3 November 2003, p. 6.

in desperation at what it's going to take to get a decent offer. The unkind might call it negotiating in bad faith.<sup>122</sup>

## Rules of origin

6.151 The Committee was advised by DFAT that a chapter of the proposed US FTA will be devoted to 'rules of origin' issues. Australia's objectives here are :

- Agree on a set of rules of origin that ensure that the benefits of preferential tariff treatment under the FTA apply only to Australian and US goods eligible for such treatment while avoiding unnecessary obstacles to trade.
- Agree on conditions to maintain the integrity of the rules and seek to ensure they are not unnecessarily burdensome to administer from the points of view of business and government.<sup>123</sup>

6.152 The US objectives were simply stated as : 'Seek rules of origin, procedures for applying these rules, and provisions to address circumvention matters that will ensure that preferential duty rates under the FTA with Australia apply only to goods eligible to receive such treatment, without creating unnecessary obstacles to trade.'<sup>124</sup>

6.153 Behind these seemingly straightforward propositions the Committee found a vigorous debate being conducted among economists about the extent to which the administrative and compliance requirements of rules of origin were burdensome and costly.

I do not think you can have a free trade agreement without any rules of origin. That is one of the problems of a preferential or discriminatory free trade agreement. Genuine free trade does not have this problem at all. When we reduced most of our protection from very high levels to something between nought and five per cent we did it across the board so that we did not have to have the industry department and the trade department checking on whether businesses were deciding to purchase too large an amount of some supply from particular countries. That issue just does not arise if you trade on a most favoured nation basis. It only arises when you have some preferential arrangement and the rules of origin are necessary to confine the privileges that you are giving out to the people you intend them to go to. So rules of origin are inevitable if you have these discriminatory free trade agreements. It is one of the problems of free trade agreements, perhaps the biggest problem. It is why this is not the way to go. It is why leading

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122 Wallace, C 'Pack could cut a deal' *Weekend Australian* 25 October 2003, p. 26.

123 *Submission* 54, Appendix C (DFAT)

124 *Submission* 54, Appendix D (DFAT)

economists all around the world emphasise that free trade should be multilateral free trade, to maximise everyone's welfare.<sup>125</sup>

6.154 Australian negotiators were adamant that such criticism was ill-founded:

I think there is an exaggerated concern about the rules of origin. I think it is based on an assumption from an earlier period when the external tariffs were very high and perhaps this was the result... Very clearly, only the preferential trade is impacted by the rules of origin. In a very large proportion of that trade the rules of origin are largely irrelevant, because clearly the product is from Australia or from the United States. There are no transaction costs in establishing that, particularly if you use the model that the United States pursues in these matters, which is that it is purely a change of tariff classification.

If you import an engine and you export that engine in a motor vehicle, there is no bookwork required, and that qualifies as the rules of origin... Rules of origin are crucial. It is important that we get them right. They are very important, as I have said, in relation to textiles in this country. The approach of the United States certainly gives the Australian textile industry cause for concern. But I do not think that the claim that somehow it will lead to a significant rise in transaction costs is supported by the facts. That has certainly not been the reaction that we have had from Australian industry when we have explained the US approach to the rules of origin.

We are still talking to the Americans. More importantly, we are still talking to Australian industry and explaining the US approach—whether it would be appropriate for Australia in the context of the FTA with the United States.<sup>126</sup>

6.155 The Committee notes Mr Deady's remarks that the approach of the United States 'certainly gives the Australian textile industry cause for concern'. The Committee understands that under current US rules of origin arrangement, the so-called 'yarn forward' rule would have huge implications for Australian textile, clothing and footwear (TCF) access to the American market.

6.156 The 'yarn forward' rule that currently applies to the American TCF sector allows for the make-up of goods in overseas countries *as long as US made fabric or yarn is used*. In the Australian TCF sector, manufacturers make extensive use of imported fabric or yarn, so if the 'yarn forward' rule is applied in the Australia-US FTA, very few goods currently made-up in Australia will qualify for tariff-free market access.

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125 *Committee Hansard*, 22 July 2003, p.208, p.209, p.210. (Garnaut)

126 *Committee Hansard* 2 October 2003, pp. 498-499 (Deady, DFAT)

## Recommendation 19

**6.157 The Committee recommends that any rules of origin applied in the Textile, Clothing and Footwear sector provide for goods made-up in Australia to access the US market without tariffs, irrespective of the source of the original yarn or fabric.**

## Consultation and transparency

6.158 A major issue for the Committee, both with respect to negotiations related to the GATS and the Australia-US Free Trade Agreement, is the extent to which the government has consulted with relevant interest groups and has facilitated transparency of the dialogue and decision-making between the respective negotiating teams.

From November, we [DFAT] have asked and called for public submissions. There has been a very high level of interest in these negotiations and we have conducted, I believe, a very detailed series of consultations with Australian industry and other stakeholder's right through the process. It has been a very fast moving process that has required, I believe, even more consultations and negotiations than perhaps would be the norm. We have attempted to complement those consultations with the publication of a regular newsletter. We have put out three of those, reporting on the outcome of the three rounds that we have conducted.<sup>127</sup>

6.159 The Committee was pleased to discover that, broadly speaking, people were happy with the level of consultation undertaken by DFAT officials both in the lead-up to the US FTA negotiations and during the negotiating phase itself.

Speaking on behalf of the Australian Film Commission, I think that the degree of consultation with the government at all levels has been entirely adequate, and we have gone on the public record regularly to make that statement.<sup>128</sup>

I think that DFAT have made a conscious effort to try to draw the broader community in on some of these trade issues ... I know that at the [consultation] that I attended in Sydney there were pretty wide ranging views expressed at the seminar there.<sup>129</sup>

We have had opportunities at several different levels to consult and be consulted. We have participated in the regular industry forums that DFAT has organised... We have also had private consultations going back to November last year with DFAT and with DCITA... Those consultations

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127 *Committee Hansard*, 2 October 2003, p.462 (Deady, DFAT)

128 *Committee Hansard*, 23 July 2003, p. 264 (Dalton, Australian Film Commission)

129 *Committee Hansard*, 23 July 2003, p. 299 (Barnard, Meat and Livestock Australia)

have covered general issues and specific issues such as intellectual property rights, government procurement and so on.<sup>130</sup>

6.160 Community and union groups were somewhat less positive in their assessment of DFAT's consultative efforts. These groups conveyed a sense that the consultations were sometimes tokenistic, that DFAT often seemed unable to understand their concerns, and that feedback on negotiations was inadequate. It was frequently a case of 'access, yes; substantive detail, no.'<sup>131</sup>

6.161 The Committee has commented earlier on the problems that arise when citizens feel that the government is not apprising them of the matters being placed on the negotiating table, or when they sense that a veil of secrecy is being drawn over agreements that may have far-reaching consequences for their economic, social, environmental or cultural futures.

6.162 While the Committee appreciates that negotiating tough trade deals requires the parties to observe a considerable degree of discretion, and that to reveal one's hand is rarely an appropriate strategy, the Committee is also strongly of the view that the process by which major trade deals are initiated, developed and prosecuted must be as transparent as possible.

The Australian people need to understand what it is that is being asked of them, and who is asking it in the case of multilateral talks because that will vary the impact from country to country. In the case of bilateral talks, they need to understand what is being asked of them and what we are putting on the table.<sup>132</sup>

6.163 A representative of the Local Government Association captured the sense of the attitude required of governments in trade negotiations when he declared:

The collective commitment of Australian governments to advance the wellbeing of all Australians relies to a considerable degree on trust and confidence. I cannot be 100 per cent emphatic in a statement here that all that we desire and all that we understand as a consequence of our discussions with the Commonwealth will come to pass, but to the extent that a sphere of government can rely on the undertakings given to it by another sphere of government we believe that the Commonwealth will at the very least, if it runs into a roadblock directly relevant to the issues of concern to local government, come back and engage us in consultations again before a bottom line is agreed.<sup>133</sup>

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130 *Committee Hansard* 22 July 2003, p. 176 (Australian Information Industry Association)

131 *Committee Hansard* 22 July 2003, p. 240 (Burrow, ACTU)

132 *Committee Hansard* 22 July 2003, p. 240 (Burrow, ACTU)

133 *Committee Hansard* 22 July 2003, p. 189 (Chalmers, Australian Local Government Association)

6.164 The Committee is persuaded that the translation of that sentiment and principle into a standard practice by which Australia progressed its trade deals would overcome much of the public anxiety and suspicion. It would also encourage the public to engage more fully in the debate, enable citizens to be better informed, and most importantly assist the government towards a full appreciation of the views of its electors. In short, the public interest would be served.

In talking about the public interest, we are really talking about two major themes. One is the provision by government of public benefits to the community; the second is the demonstrable operation of transparent public governance arrangements. With ‘public benefit’ it is the capacity of ...[government]... to provide services and to make regulations and by-laws which ensure the community good. With ‘public governance’ it is the processes of government which are open, consultative, transparent and accountable.<sup>134</sup>

6.165 During its current inquiry, the Committee has been compelled to consider the US FTA without the benefit of knowing exactly what the final agreement will look like. While the Committee is satisfied that the analysis and assessments it has made thus far are consistent with the facts of the case as they are so far known, any final judgment on the US FTA can only be made once the detail of the agreement has been made public.

### **Recommendation 20**

**6.166 The Committee recommends that the Senate refer the final text of the *Australia-US Free Trade Agreement* to the Senate Foreign Affairs, Defence and Trade References Committee for examination and report.**

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134 *Committee Hansard* 22 July 2003, p. 194 (Chalmers, Australian Local Government Association)