Committee Secretary
Joint Standing Committee on Treaties
The Parliament of the Commonwealth of Australia
PO Box 6021
Parliament House
CANBERRA ACT 2600

Freight & Trade Alliance and Hunt & Hunt Lawyers – Submission in respect of the China Australian Free Trade Agreement

We refer to the review being undertaken by the Joint Standing Committee on Treaties (**JSCOT**). We are pleased to provide JSCOT with the attached joint submission in respect of the proposed China Australia Free Trade Agreement (**ChAFTA**). This submission primarily focuses on issues associated with trade in goods.

SUMMARY

We note the general support in the trade community for ChAFTA but bring to the JSCOT's attention, the following issues:

- The impact of ChAFTA could be undermined by provisions which may see Chinese goods shipped via Hong Kong losing their status as being of Chinese origin.
- The "preferential" customs duty rates for most clothing is set at a rate higher than the general rate that applies for goods not covered by ChAFTA.
- In implementing ChAFTA Australia should give thought to dispensing with the need for origin certification so as reduce the administrative burden of ChAFTA.
- Requirements relating to the use of declarations of origin need to be administered in a trade facilitative manner.
- Australia should strive in future years for relaxation of the origin certification rules so that there is consistency with other free trade agreements (FTAs) entered into by Australia.
- Utilisation of the ChAFTA is likely to be higher than for other FTAs as use of alternative concessions is becoming more difficult.
- Australian licensed customs brokers will play a significant role in the implementation of ChAFTA. The crucial role of customs brokers should be recognised and supported.

Each of these issues is discussed below.

ABOUT FREIGHT & TRADE ALLIANCE

Formed in September 2012, Freight & Trade Alliance is in a unique position being representative of a cross-section of Australia's international trade sector with diverse subscriber base of 197 international freight logistics and import / export trade entities (refer to the online directory at www.FTAlliance.com.au). Freight & Trade Alliance provides a range of support and advocacy services to industry dealing with increasing border security requirements, evolving global trade agreements, variations in international shipping practices and numerous domestic landside logistics issues.

ABOUT HUNT & HUNT

Hunt & Hunt Lawyers are a national law firm that has a long history of acting on behalf of customs brokers, freight forwarders, importers and exporters and industry bodies associated with international trade. Hunt & Hunt regularly advises clients on the application of free trade agreements, the availability of customs duty refunds, liability to pay customs duty and concessions available to reduce customs duty payable.

GENERAL SUPPORT FOR CHAFTA

It is generally submitted that ChAFTA is an important step in liberalising trade with Australia's largest trading partner.

International trade in agricultural goods and services remains highly distorted due to a number of protective measures. For Australian exporters ChAFTA aims to lessen these barriers and in doing so enables these areas of the economy to experience significant growth. This opportunity is made more significant due to the fact that most of Australia's international competitors will not enjoy the same level of Chinese market access.

From an import perspective, the removal of tariff barriers will provide importers, and ultimately consumers, with lower priced Chinese goods. However, the extent to which these benefits will be obtained will depend on the utilisation of ChAFTA. We do hold concerns that the administrative origin requirements of ChAFTA will prevent high levels of utilisation. Below we address issues which we believe will increase the utilisation of ChAFTA.

CONSIGNMENT RULES

Article 3.13 of chapter 3 of ChAFTA is entitled "Direct Consignment" and sets out when an originating good can be transported through one or more non-originating countries and maintain its originating status. Under paragraph 2 of article 3.13 a good can be transported through a non-party and not lose its originating status provided that the goods remain under "customs control" in the non-parties.

This is particularly relevant under ChAFTA as it is not unusual for goods of Chinese origin to be shipped to, and warehoused in, Hong Kong prior to shipments to third countries, including Australia.

Hong Kong is an independent customs state from the People's Republic of China. It is treated as a non-party under ChAFTA. As such, if Chinese originating goods are transhipped via Hong Kong they will only retain their status as originating goods if the goods remain under "customs control" in Hong Kong.

Customs control generally refers to a period from the arrival of the goods at a port until their clearance into home consumption (general commerce) by the relevant customs authority. If goods are under customs control they generally must not be altered and must remain in customs controlled areas such as ports or licensed bonded warehouses.

The difficulty is that Hong Kong is essentially a free port and does not exercise customs control over most goods. This makes it difficult, if not impossible, for goods shipped via Hong Kong to remain under customs control. To this end, we are aware of informal advice from the previous Australian Customs and Border Protection Service in respect of other FTAs that goods warehoused in Hong Kong will not be treated as being under customs control and will lose their preferential status.

It is expected that most goods shipped via Hong Kong will not technically be able to maintain their Chinese originating status under ChAFTA. This will greatly reduce the effectiveness of ChAFTA in reducing duty on Chinese goods.

We recommend the following:

- Research be undertaken into how much China/Australia trade in goods is potentially affected by this issue;
- Australia consider unilaterally waiving the restriction in paragraph 2(a) of article 3.13 in respect of goods transhipped via Hong Kong (the requirements in 2(b) and (c) will still apply and prevent further processing of the goods in Hong Kong);
- The Australian Border Force release guidance to the trade community on how it will treat goods transhipped via Hong Kong;
- The Committee on Trade in Goods to be established under article 2.15 of chapter 2 of ChAFTA consider this issue early in the operation of ChAFTA.

RATES APPLYING TO CLOTHING

The most tangible way that ChAFTA liberalises trade is to reduce customs tariffs applying to goods of Chinese or Australia origin. Clothing and textiles are the Chinese product exported to Australia in the greatest volume.

From 1 January 2015 the general duty rate for clothing has been 5%. This rate can be obtained regardless of the origin of the goods. When ChAFTA negotiations were concluded (November 2014) the general for clothing was 10%. Because of this the tariff reduction schedule under ChAFTA has 10% as its starting point with that rate being progressively reduced over 3-5 years.

Where the reduction schedule timeframe is 3 years the "preferential" rate for Chinese origin clothing on implementation of ChAFTA is 6.6%. Where the reduction schedule is 5 years, the "preferential" rate for Chinese origin clothing on implementation of ChAFTA is 8%.

In each case, the rate applying under ChAFTA in year one will be higher than the general rate. That is, an importer would be worse of applying the "preferential" rate under ChAFTA.

It is assumed that this outcome was an oversight and a different reduction schedule would have been agreed if the negotiators had appreciated that the general rate for clothing would be 5% when ChAFTA commenced.

This unusual outcome will have a big impact on the utilisation of ChAFTA in its initial years given that clothing constitutes Australia's largest value imported good of Chinese origin.

It is submitted that ChAFTA's utilisation will be greatly improved by Australia applying to Chinese originating clothing a reduction schedule with a base rate of 5% instead of 10%. This would mean the following:

Reduction schedule	Year 1	Year 2	Year 3	Year 4	Year 5
5 years	4%	3%	2%	1%	0%
3 years	3.3%	1.7%	0%	0%	0%

The above highlights that it is crucial that our trade negotiators are aware of future planned reductions in general duty rates. Given the importance of clothing exports to Australia, offering the above lower rates may have been a valuable negotiating tool. In the end, what was negotiated offers no immediate benefit to Chinese exporters and Australian consumers.

CERTIFICATE OF ORIGIN

The paperwork associated with satisfying origin requirements is one of the main reasons that FTAs are underutilised. Traditionally, FTAs have set out that origin will only be established if a certificate of origin is obtained from an authorised body.

In more recent times (see the FTAs with Japan and Korea) FTAs concluded by Australia have included self-certification provisions. These provisions allow producers, exporters, and in some cases, the importer, to self-produce an origin certification document.

Under ChAFTA, a certificate of origin issued by an authorised body or a declaration of origin must be held to claim preferential duty rates.

It is submitted that the utilisation of ChAFTA will be greatly increased in respect of imports into Australia if Australia waived the requirement for certificates of origin. Paragraph 1 of Article 3.18 of Chapter 3 of ChAFTA allows a party to waive the requirement for the provision of a certificate of origin.

The waiver of the requirement to produce a certificate of origin does not remove the requirement that the goods actually be of Chinese origin. It merely means that obtaining a certificate of origin is not necessary to prove origin.

In this respect we note that New Zealand does not require certificates of origin in respect of its FTA with China and that Australia does not require origin documentation for importers to claim preferential status in respect of imports from developing countries and the US.

It is our view that compliance with origin requirements is more likely to be obtained by the Australian Border Force regularly auditing claims of origin rather than requiring certificates of origin. To this end we note that certificates of origin are usually issued by registered bodies based on information provided by the supplier. While the process may identify where origin has been incorrectly claimed due to a lack of understanding of the rules, it is unlikely to identify deliberate false claims of origin.

Reliance on certificates of origin creates a false sense of compliance and adds to the administrative burden of all importers wishing to use ChAFTA.

If the requirements for certificates of origin are not completely waived, we recommend that the requirement be waived for importers that are accredited as Trusted Traders under the Australian Trusted Trader Programme.

DECLARATIONS OF ORIGIN

While the recent FTAs with Japan and Korea included a requirement for origin certification, the provision of this documentation was made easier by liberal self-certification provisions. In respect of the FTA with Korea, self-certification can be by the producer or exporter. Under the FTA with Japan self-certification can be by the producer, exporter or importer.

Under ChAFTA, a declaration of origin will be accepted where the goods are covered by a Government issued origin ruling. Specifically, ChAFTA provides that a declaration of origin can be used in place of a certificate of origin for any consignment of goods covered by an advance ruling issued by the importing party that deems the goods to qualify as originating, so long as the facts and circumstances remain unchanged and the ruling remains valid.

Essentially this means that before a Chinese exporter can issue a declaration of origin for goods produced in China, the Department of Immigration and Border Protection (Department) must have issued an origin ruling in respect of those goods.

We make the following comments about this approach:

- Declarations of origin will rarely be used as producers/exporters in one country will be disinclined to make an application for a ruling from a foreign customs authority.
- Linking declarations of origins to origin rulings is only practical for commodity type products where there is a large volume of identical goods. For manufactured products a single exporter will have such variety in the type of good, inputs and methods of manufacture that 100s, if not 1000s, of origin rulings would be required to enable the exporter to widely use declarations of origin.
- A origin ruling is only valid so long as the facts on which the ruling is based remain the same. This means that if a manufacturer changes an element in the manufacture of the goods a previously obtained ruling will not be valid and a declaration of origin cannot be used.
- Unless it undertakes onsite reviews in China, it is unclear how the Department would assess the origin of goods manufactured in China, other than by relying on information provided by the manufacturer. If origin assessment is based purely on information provided by the manufacturer, it is difficult to see what additional benefit the granting of an origin ruling provides. The origin ruling requirement would give the declaration or origin system more veracity if the ruling was issued by

the customs authority in the exporting country. We say this because that customs authority would have the ability to independently review the information provided by the manufacturer/exporter.

- Linking declarations of origin with origin rulings will place a significant resourcing strain on the Department. It has been the experience of customs brokers that the length of time it takes to receive a ruling has been increasing over recent years. While the Department's goal timeframe is 28 days, the average time is closer to 60 days. Given the influx in requests for rulings likely to be occasioned by linking self-certification to origin rulings, it is important that the Department be sufficiently resourced.
- The Department should issue clear guidance on what level of change in product or manufacturing will require a new origin ruling. For instance, if the manufacturer's supplier of an input changes, but the input is still of Chinese origin, will a new ruling be required. Alternatively, if the product is modified but the classification of the good and origin of its inputs remain the same, is a new ruling required.
- Australian producers and exporters will require an origin ruling from Chinese Customs in order to use a declaration of origin. We recommend that DFAT, the Department and Austrade work with their Chinse counterparts to make obtaining origin rulings as simple as possible. As a starting point, a guide on obtaining a Chinese Customs origin ruling should be produced.

As the likely utilisation of ChAFTA will be impacted by the ability of traders to self-certify origin, the administration of the declaration of origin provisions needs to be made as trade facilitative as possible.

ALIGNMENT OF ORIGIN CERTIFICATION RULES WITH OTHER FTAS

The point has been made on many occasions that the lack of consistency in origin rules across FTAs makes FTA use difficult for Australian traders. We agree with this position and note our experience that the difficulty of applying rules of origin is one of the main reason for FTA underutilisation. It also stands to reason that greater uniformity in rules of origin across FTAs would reduce the difficulty and cost of complying with those rules.

By way of example, the origin certification requirements under each of FTAs with China, Korea and Japan are set out below. Remembering that these FTAs were concluded by the same Australian Government in a short period of time.

	Korea	Japan	China
Who can self-certify origin	Producer or exporter	Producer, exporter or importer	Producer or exporter
Is an origin ruling required to self-certify	No	No	Yes
Can an origin document be used for multiple consignment	Yes	No	No
Regional value content rule	Widely used	Widely used	Rarely used

We assume that the Department of Foreign Affairs and Trade (DFAT) has a view as to its desired outcome regarding origin provisions. While we do not advocate amendments to ChAFTA prior to it commencing, at the various review stages of the agreement DFAT should advocate for relaxation of the origin rules to reflect its desired position. This should occur across all FTA to which Australia is a party.

If this approach is taken, over time the differences between the origin provisions of the various FTAs will be decreased, reducing the compliance costs incurred by business.

USE OF OTHER CONCESSIONS MAY DECREASE

One of the reasons for the historic underutilisation of FTAs is the alternative of other concessions. In the Australian context a significant alternative concession is tariff concession orders (TCOs). TCOs are made on application where an importer can demonstrate that there is no producer in Australia of substitutable goods. Where a TCO applies the duty payable is reduced to zero.

Over the past 2 years a significantly stricter approach has been taken by the Australian Customs and Border Protection Service, and now Australian Border Force, to the application of TCOs. A key feature of this approach has been to deny the application of TCOs to goods that fundamentally meet the terms of the TCO but include an additional good or feature that is not specified in the TCO wording.

This approach has created uncertainty regarding the application of TCOs and in some cases, a preference to use other concessions, such as FTAs.

If the trend towards strictly interpreting the wording of TCOs continues, it can be expected that the use of alternative FTAs will increase with a corresponding decrease in the use of TCOs.

Given the uncertainty regarding the application of TCOs, having an alternative concession, such as ChAFTA, is welcomed.

ROLE OF CUSTOMS BROKERS

For the reasons set out below, it is considered that customs brokers will have a greater than usual role in facilitating the use of ChAFTA. It is crucial that Government recognise and support this important role.

As has been reported elsewhere, FTAs are traditionally underutilised. A major reason for this is the difficulty in understanding and applying rules of origin. Rules of origin are relatively easy where the good is the product of Australia (grown here, or Australian minerals) or produced entirely from Australian originating goods.

The difficulty arises where goods have inputs that are not entirely of Australian origin. Very few manufactured goods will be entirely of Australian origin. In these circumstances, ChAFTA generally requires that the non-Australia/Chinese input undergo a change in tariff classification when compared to the exported finished good (CTC Rule). The degree of change will depend on the particular good.

In most FTAs Australia has negotiated alternative origin rules to be used where goods are not entirely of Australian origin. These rules are the CTC Rule and rules which are based origin on a minimum level of Australian content (usually 40-45%) (RVC Rule). It is notable that ChAFTA rarely allows the use of the RVC Rule.

The RVC Rule is primarily an accounting based rule and can be more easily applied by traders or their accountants. The CTC Rule is directly linked to tariff classification. It is our experience that only customs professionals, such as customs brokers, are trained in tariff classification.

The primary use of the CTC Rule under ChAFTA will mean that the technical skills of brokers will be called on to help determine whether goods qualify for preferential treatment. We recommend the following:

- The Department provide training to customs brokers on the rule of origin provisions under ChAFTA. In respect of recent FTAs with Korea and Japan 1-2 hour seminars were provided by the Australian Customs and Border Protection Service. Such seminars should be again provided together with webinars and more detailed workshops.
- When promoting FTAs to traders, DFAT and Austrade should highlight the CTC Rules and inform traders of the role customs brokers can play in determining origin.

- Consideration should be given to allowing the cost of assessing origin under ChAFTA, or other FTAs, (including fees paid to a customs broker or other advisors) to be eligible for the Export Markets Development Grant. We say this as eligibility for preferential status under an FTA is an extremely valuable marketing tool.

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We are happy to discuss these issues with you at your convenience.

Yours faithfully

Hunt & Hunt

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