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Senator Alex Gallacher
Chair of the References Committee
Standing Committee on Foreign Affairs, Defence and Trade
Parliament House
Canberra

SUBMISSION TO THE INQUIRY INTO THE COMMONWEALTH'S TREATY-MAKING PROCESS

Dear Senator Gallacher

The Australian Industry Group (Ai Group) thanks the Standing Committee on Foreign Affairs, Defence and Trade for its invitation to make a written submission to its Inquiry into the Commonwealth's treaty making process, in particular it references on bilateral and multilateral trade agreements.

Ai Group, along with its affiliates represents the interests of 60,000 businesses in an expanding range of sectors including: manufacturing, engineering, construction, automotive, food, transport, information technology, telecommunications, call centres, labour hire, printing, defence, mining equipment and supplies, airlines and other industries. Ai Group members operate small, medium and large businesses across this range of industries. The majority of businesses engage in some form of international activity, importing, exporting and a combination of the two. Many participate in global supply chains and offshore production of some kind. Trade is vital to their survival and growth.

Ai Group fully supports the principle of free trade. It considers that multilateral trade agreements are the best means for pursuing truly global trade liberalisation. However, while the recent WTO package of trade facilitation measures was a welcome step, multilateral trade negotiations are clearly failing to keep up with the rapidly changing global trade environment. In these circumstances, Ai Group supports Australia entering into FTAs which advance the national interest.

Ai Group has welcomed the completion of negotiations with China, Japan and Korea for FTAs. But there is general perception within Ai Group members that these FTAs with North Asia have sold short the interests of industry, in particular the manufacturing sector. In submissions to the Joint Standing Committee on Treaties on the ratification of the FTAs with Korea and Japan, Ai Group called for greater business participation in FTA negotiations and for the terms of the agreements to be evaluated with respect to the broader economic framework and the interests of all sectors, and hence the national interest.

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Ai Group welcomes the Inquiry's focus on FTAs. In this submission, we comment on the two terms of reference which are of vital interest to business: (f) the scope for independent assessment and analysis of treaties before ratification; and (g) the current processes for public stakeholder consultation and opportunities for greater openness, transparency and accountability in negotiating treaties.

We hope that our submission will be useful to the Inquiry.

Yours sincerely

Innes Willox
Chief Executive



**AUSTRALIAN INDUSTRY GROUP
27 February 2015**

**SUBMISSION TO THE INQUIRY BY THE SENATE STANDING
COMMITTEE ON FOREIGN AFFAIRS, DEFENCE AND TRADE INTO THE
COMMONWEALTH'S TREATY-MAKING PROCESS**

Reference (h): the current process for public and stakeholder consultation and opportunities for greater openness, transparency and accountability in negotiating treaties

Engagement with Business on Trade Negotiations

Engagement with business in trade negotiations has been a constant recommendation in Ai Group's representations on FTAs.

Ai Group considers that the current process for briefing and consultation with business and industry is not effective. There are two major flaws. The first is the policy of successive Australian Governments not to allow details of Australia's negotiating briefs to be revealed. The second is the lack of a resourced procedure for detailed discussion and involvement by business in the negotiations. As part of this submission, the Ai Group draws the Committee's attention to business participation in other countries' trade negotiations which could serve as models for better business involvement in Australian FTA negotiations.

Ai Group recognises the obligation to maintain the confidentiality of the negotiating position of the other side. However, we do believe that the offers of the Australian side should be explained clearly to those affected by them. It is Australian industry which will implement the advantages of freeing up trade. But it is also industry which will bear the brunt of rapid erosion of domestic markets. And it is industry which has the expertise to advise on the effect of proposed measures and to highlight some of the unintended outcomes.

The Ai Group's submissions to the Joint Standing Committee on Treaties during its Inquiries into the Japan-Australia Economic Partnership Agreement (JAEPA) ⁱ and the Korea Australia Free Trade Agreement (KAFTA) ⁱⁱ

recommended close engagement with the business community in the negotiation and conclusion of FTAs. Written submissions to the Department of Foreign Affairs and Trade in 2004ⁱⁱⁱ and 2014^{iv} on the China FTA also called for closer liaison with the business community, particularly on the importance of non-tariff barriers faced by business in economic engagement with China.

Korea Australia Free Trade Agreement

KAFTA was the first FTA completed with North Asia. Ai Group's submission to the JSCOT Inquiry noted that the fact that free trade agreements involve the abolition of all domestic tariffs in all sectors of the economy had not been widely understood. Business had been caught by surprise at the proposed abolition in early 2015 of Australian tariffs on almost all Korean imports.

"... for the many SMEs that produce for the domestic market, the immediate 5% reduction in the price of competing Korean imports would almost immediately bite into their already narrow profit margin. Their medium term plans for significant reform had not generally factored in such major tariff cuts. Some SMEs show remarkable resilience and are moving to diversify products and services quite quickly. Others are taking longer in terms of product development, workforce training and major recapitalisation. Their competitiveness in the domestic market was suddenly eroded at a very vulnerable time."

Ai Group members have pointed out that, on the Korean side, sensitive products had achieved much longer periods for the abolition of tariffs. Tariffs on beef, Australia's largest agricultural export to Korea, will only be eliminated over 15 years. For other sensitive products, such as cheese, tariff elimination will be over 20 years. Rice has been excluded altogether. Korean agriculture has been treated by both sides as very sensitive and considerable time to restructure has been conceded to it.

Only very few lines in Australia's sensitive manufacturing sector have been given periods of grace for tariff removal. For many SMEs the timing for abolishing tariffs on a particular tariff line - overnight, or over a longer period - is crucial. But through a lack of information on the Australian brief, this level of detail was not available before the negotiations had been concluded.

Japan-Australia Economic Partnership Agreement

Ai Group's submission to the JSCOT Inquiry into JAEPA also noted that the lack of transparency in the course of the negotiations had resulted in a low level of engagement in the process. This had contributed to a perception that the local manufacturing sector was accorded insufficient attention in JAEPA. Like KAFTA, very long lead-times were conceded to Japanese tariffs on agricultural products. Most Australian tariffs are abolished immediately. For the many SMEs that produce for the domestic market, the effect was an immediate 5 per cent to 8 per cent reduction in the price of competing Japanese imports.

“This disparity (of treatment) gives rise to the impression that there has been preparedness on the Australian side of negotiations to make much more significant concessions in the form of gradual tariff reductions and increased quota levels than we have sought on our side of the deals. We know from history that tariff elimination plays a significant role in increasing longer-term domestic competitiveness. But we also know that rapid tariff reductions cause major short-term disruption of local production. Overnight reductions in the price of Japanese imports come at a time when industry is coping with other major domestic and competition challenges: the high Australian dollar, high energy and labour costs, major decline in the automotive assembly and components sector, and intense competition from low-labour cost countries. “

Ai Group expressed appreciation for the efforts made by negotiators to consult, but noted that the smaller domestic manufacturers have not been engaged. The sector is dispersed and heterogeneous in nature and comprises large, medium and small businesses. This makes it difficult for negotiators to get a feel for the very wide range of interests at play. For many businesses, the fine detail of aspects of the negotiations is vital. For example, the timing for abolishing tariffs on a particular tariff line – from one day to the next or over a longer period – can determine whether the restructure plans of a business are successful. In order to introduce transparency and more detailed consultation with the domestic manufacturing industry. Ai Group recommended that a more effective and efficient system of consultation be developed, along the lines of the accredited adviser committees in the United States.

China Free Trade Agreement.

Overall, business has always been very wary of an FTA with China. Lack of information about the content and progress of the negotiation has not dispelled this mistrust. Ai Group surveys in 2004 and in 2014 demonstrated the lack of information had continued over the 10 years of negotiations. In both surveys over one in five respondents had little real idea whether the FTA would be positive or negative for their business.

Ai Group's submission in 2004 to the feasibility study recommended establishing a procedure whereby business could draw the attention of officials in the Department of Foreign Affairs and Trade to issues and problems in China identified by business in a comprehensive survey. These issues had been identified in a wide survey and concerned competition law, trade remedies, intellectual property, standards and labelling, quarantine, tariff classification and duty, different and conflicting requirements between spheres of government, onerous customs procedures, restrictive and non-transparent import licencing agreements, local content quotas, government support for domestic industries, and ownership restrictions.

Ai Group's 2014 survey of businesses raised very similar areas of concern about an FTA:

- The removal of import tariffs under an Australia-China FTA was expected to result in increased competition from lower-priced Chinese manufactured imports;
- Respondents also noted that many manufactured goods imported from China do not meet Australian safety and quality regulations and standards and the removal of tariffs under an Australia-China FTA may exacerbate this situation;
- Related to this are uncertainties about how potential breach of contract and delivery of faulty Chinese products will be properly dealt with, including processes around insurance claims and other legal resolution channels (See **Case study: Infinity electrical cable recall** below^v);
- There is a strong view by local manufacturers that Chinese manufactured exports are subsidised, particularly those made by China's State Owned Enterprises (SOEs), Chinese labour costs do not adequately address things like health cover and superannuation, and the Chinese currency (RMB) is under-valued. All of these factors reportedly create an uneven playing field against locally made goods;
- Local manufacturers also highlighted that it is impossible to protect intellectual property (IP) as advanced Australian made products sold into the Chinese market are "reverse engineered" in China and imported back into Australia, with any chance of finding a patent breach highly unlikely; and
- A substantial number of Australia-based multinational corporations, in particular those that are Chinese owned, require offshore sourcing for large project tenders and this trend of behaviour may worsen under an Australia-China FTA due to perceived lower costs from Chinese suppliers and vertical integration.

Manufacturing exporters pointed towards potential issues under an Australia-China FTA that need to be addressed, including:

- The speed at which Chinese tariffs on Australian exports will be reduced, in terms of their relativity to how quickly Australian duties are to be abolished on Chinese made products under an Australia-China FTA;
- Preference by Chinese customers, including government agencies and departments, to purchase Chinese made products instead of overseas good; and
- How non-tariff barriers to trade (NTBs) on Chinese borders such as administrative hurdles and standards will be dealt with for Australian exports.

The Ai Group's 2014 Report to DFAT on negotiations with China underscored the argument that an FTA should include the negotiation of the best possible arrangements for Australian manufacturers and exporters including in the following areas:

- Reductions in tariffs applying to manufactured goods imported from China should allow sufficient phase-out periods that give domestic businesses time to adjust. Such arrangements are commonly granted to producers in other countries with whom we have negotiated FTAs and, although to a much lesser extent, have also been negotiated to give some Australian manufacturers time to adjust under other FTAs;
- Non-tariff barriers and the preferential treatment afforded to China's State Owned Enterprises, need to be addressed to ensure equitable treatment for Australian manufacturing exporters;
- Effective commercial safeguards in relation to intellectual property (IP) infringements are essential to Australia's ongoing relationship with China; and
- Conformity of Chinese imports with Australian safety and quality standards needs to be strengthened and a process developed for legal enforcement of insurance claims and contract breaches.

Ai Group's submission to DFAT recommended that these concerns should be addressed in the FTA negotiations. The absence of such provisions in the final FTA means that Australian businesses will continue to face the same difficulties even after the FTA comes into force.

Other models for improved business participation in trade negotiations.

The United States Industry Trade Advisory Centre: "Industry's Voice in US Trade Policy"

The United States has the most long-established and well-developed process for engaging business in trade negotiations and policy formulation through its Industry Trade Advisory Centre.

The US Industry Trade Advisory Committees (ITACs) are a public-private partnership that engages business leaders in formulating U.S. trade policy. The ITACs are established under the Trade Act 1974 and jointly managed by the U.S. Department of Commerce and the Office of United States Trade Representative (USTR).

There are sixteen ITACs covering separate sectors, an ITAC Committee of Chairs, and more than 300+ trade advisors, who provide detailed policy and technical advice and recommendations to the Secretary of Commerce and The United States Trade Representative regarding trade barriers, negotiations of trade agreements, and implementation of existing trade agreements affecting industry sectors, as well as a window to the changing trade environment. They also perform other advisory functions relevant to U.S. trade policy matters.

Eligibility to serve on an ITAC is limited to U.S. citizens who are not full-time employees of a governmental entity, and who represent a U.S. entity that trades internationally and is engaged in the manufacture of a product or the provision of a service (including retailing and other distribution services), or an

association of such entities. Consideration is given to balance among sectors, product lines, small, medium, and large firms, and geographic areas. Some civil society groups are critical of the ITACs commercial and business focus, arguing that representatives on issues such as labour standards, environment and civil rights should be included in the trade policy advisory bodies.

The Trade Advisors must hold security clearances and have access to draft texts and US negotiating positions. Advisors are bound by confidentiality undertakings.

Ai Group considers this model could be readily adapted to the Australian context to provide organized, comprehensive engagement of business in trade negotiations and trade policy formulation.

European Union- Japan FTA Negotiations

Ai Group noted in its submissions on the Korean and Japan FTAs that briefings and consultations with Australian business are undertaken by officials engaged in actual negotiations. These officials were already stretched in the handling of three simultaneous sets of negotiations.

Ai Group's counterparts in Europe have drawn attention to the engagement of high-level, expert consultants to facilitate on-going, open and comprehensive engagement by business in the negotiations. This approach could also serve as a model to provide resources dedicated to business liaison during trade negotiations.

In the course of negotiations for a FTA with Japan, the European Commission has engaged the London School of Economics (LSE Enterprises) to conduct a Trade Sustainability and Impact Assessment (Trade SIA) as part of the negotiations of a comprehensive trade and investment agreement. The Trade SIA is to be completed before the final phase of the negotiations, expected to conclude in 2016, since the results will feed into the negotiations and the decision-making process.

The terms of reference for the Trade SIA include extensive, accessible and open consultation with stakeholders. The objective of the consultation process is not only to ensure greater understanding and awareness among stakeholders of the Trade SIA methodology but also to increase transparency and accountability. The SIA provides an expert, arm's-length assessment of the potential economic, social and environmental effects resulting from trade and trade-related provisions of the agreement in the EU and Japan as well as third countries, including developing countries. The final report will include recommendations to maximise the benefits of the agreement while ensuring the competitiveness of enterprises and preventing or minimising potential negative impacts. The recommendations will integrate the analysis and evaluation of relevant recommendations put forward by the extensive stakeholder consultations.

The consultants from the London School of Economics have direct access to the policy makers through briefings and discussions with a Committee comprising almost all EU Commission Directorates (Secretariat-General (SG), Legal Service (SJ), Agriculture and Rural Development (AGRI), Budget (BUDG), Climate Action (CLIMA), Competition (COMP), EuropeAid Development and Cooperation (DEVCO), Economic and Financial Affairs (ECFIN), Employment, Social Affairs and Inclusion (EMPL), Energy (ENER), Enterprise and Industry (ENTR), Environment (ENV), Eurostat (ESTAT), Home Affairs (HOME), Justice (JUST), Maritime Affairs and Fisheries (MARE), Internal Market and Services (MARKT), Mobility and Transport (MOVE), Health and Consumers (SANCO), Taxation and Customs Union (TAXUD) and the European External Action Service (EEAS).

The expertise of the team undertaking the Trade SIA across a large range of economic and business issues has the potential to provide effectively detailed briefings from officials and to evaluate the proposals and comments made by business.

Regional Comprehensive Economic Partnership (RCEP) Negotiations

While still in a very formative stage, the channel for business participation established within the Regional Comprehensive Economic Partnership (RCEP) negotiations may eventually serve as a useful model.

RCEP is an ASEAN-centered proposal for a regional free trade area, which would initially include the ten ASEAN member states and those countries which have existing FTAs with ASEAN – Australia, China, India, Japan, Republic of Korea and New Zealand. The RCEP will build on and expand Australia's existing FTA with ASEAN and New Zealand. Negotiations were launched on 20 November 2012.

The objective of RCEP is a modern, comprehensive, high-quality and mutually beneficial economic partnership agreement that will cover trade in goods, trade in services, investment, economic and technical cooperation, intellectual property, competition, dispute settlement and other issues.

RCEP is being negotiated in parallel with the Trans-Pacific Partnership Agreement (TPP) which has 12 participating APEC countries which largely overlap with the RCEP membership. However, TPP negotiations include the United States, but not China, India and some of the ASEAN countries. TPP is also aiming to be a comprehensive agreement and to cover new areas not covered by existing FTAs.

In 2013, at the outset of the negotiations, the ASEAN Plus Three Economic Ministers asked for a process to ensure effective business inputs into the RCEP negotiations. A Dialogue on RCEP at the 25th East Asia Business Council Meeting in 2013 led to the creation of an Working Group of business representatives in the region under the aegis of the Business Council.

The objectives of the Working Group are to act as the conduit for effective business input into the RCEP negotiations and seek to ensure that the negotiations address business needs and priorities. Having been created in response to the request from the ASEAN Plus Three Economic Ministers, the Working Group has a formal role in feeding business priorities and concerns into the RCEP negotiations.

The Working Group is composed largely of representatives of peak business organisations in the participating countries. The Working Group has already identified some concrete matters which are being included in RCEP negotiations: e-commerce, facilitating access to global and regional value chains and addressing the needs of Small and Medium Enterprises (SMEs).

Term of Reference (f): the scope for independent assessment and analysis of treaties before ratification.

The Ai Group has advocated strongly that the proposed text of FTAs should be subject to independent assessment and analysis to test whether an FTA would be in the interests of the whole Australian economy.

Among industry there is concern that the interests of the manufacturing sector have not been progressed in the North Asia FTAs. In its submission to the Committee's Inquiry on the Japan FTA, Ai Group outlined the concerns of Australian manufacturers that there has been preparedness on the Australian side of negotiations to make much more significant concessions in the form of gradual tariff reductions and quota levels than we have sought for Australian sensitive manufactures. Manufacturers feel that these concessions have been made without an assessment of their implications, at a time when industry is coping with other major domestic and competition challenges: the value of the Australian dollar, high energy and labour costs, major decline in the automotive assembly and components sector, and intense competition from countries with low labour costs.

Ai Group has recommended in its report to DFAT that, based on its survey of Members, negotiations for an FTA with China should only be concluded with a thorough understanding of the full impact of the FTA on the whole economy, including the best possible arrangements for Australian manufacturers and exporters.

The negotiations for all the North Asian FTAs were based on positive conclusions of feasibility studies conducted during preliminary discussions with China, Japan and Korea on strengthening the bilateral economic relationship. The recommendations of these feasibility studies have not been formally reviewed over the course of the negotiations.

The joint feasibility study for the China FTA was released in March 2005. The modelling indicated that in aggregate terms, the annual average real GDP growth rate for both countries could increase by around 0.04 per cent over the

period 2005-2015 – in present value terms. This growth rate would mean that an FTA could boost Australia's and China's real GDP in the order of US\$18 billion (A\$24.4 billion) and US\$64 billion (RMB529.7 billion) respectively over the period 2006-2015. Negotiations began in 2005 and were concluded on 17 November 2014.

The 2006 joint feasibility for the Japan FTA was more nuanced and discussed the broader political and strategic benefits of an Economic Partnership Agreement and the building of an East Asian Community. Two sets of econometric modelling were undertaken and while the results differed, the study group concluded that both countries could expect significant economic gains from an EPA/FTA. The estimated magnitude of the macroeconomic gains varied between the two econometric studies undertaken, ranging from 0.66 per cent to 1.79 per cent for Australia's GDP in 2020, and between 0.03 per cent and 0.13 per cent for Japan's GDP in 2020. Negotiations began in April 2007 and concluded on 7 April 2014.

The joint feasibility study for the Korea FTA was released in April 2008. The modeling indicated that the present value of real GDP of Australia could increase by US\$22.7bn and of Korea by US\$29.6bn over the period 2007-2020. Negotiations began in 2008 and the FTA was signed on 8 April 2014.

The Ai Group's view is that these feasibility studies should be reviewed once agreement had been reached on a proposed text, but before formal government signature. The review should test whether the draft texts would produce the results promised in the feasibility studies and projected in the econometric studies. Ai Group recommends that reviews should be undertaken by independent experts, who are given a realistic timeline, have adequate resources and include consideration of business views. The results of the reviews should be published as a formal part of the national interest analysis.

For the Ai Group, it is most important that independent reviews assess the effect of the agreement on all sectors of the economy, not just the sectors for which improved market access is being sought. Free trade agreements are significant policy tools, not only for market access for agricultural products, but for trade policy, industry policy and broader domestic economic policy.

The reviews should re-examine the baselines of the feasibility studies, taking into account new developments such as the global financial crisis and economic policy shifts in Australia and in the partner country. They should examine changes in the patterns of trade since completion of the feasibility studies.

Tariff arrangement proposals should be assessed on their own merits but also in terms of their relativity to the tariff arrangements being offered to other trade partners. This would include technical issues such as the harmonisation of Rules of Origin between agreements.

The reviews should analyse and take into account interaction with the other trade agreements in which Australia is involved: the other North Asian FTAs, plurilateral negotiations for the Trans-Pacific Partnership and the Regional Comprehensive Economic Partnership, and WTO negotiations on the Trade in Services Agreement, the Trade Facilitation Agreement, the Government Procurement Agreement, the Green Goods Initiative and the Information Technology Agreement.

Given the important role which business says is played by non-tariff barriers in limiting trade, especially with China, the reviews should examine the extent to which these are addressed in the agreements and highlight major non-tariff barriers that have not been addressed. The reviews could recommend where supplementary agreements should be negotiated to cover important issues such as standards and conformity measures.

Most importantly, the reviews should assess the effect of the agreement on the whole economy. The effect on exports of all goods and services, including manufactured items, must be included.

Where the agreement is assessed to have some negative effects, the full economic effects of the proposed agreement should be covered, including the costs to employment and social benefits. In particular, this would involve in-depth analysis of the effect on the manufacturing sector.

ⁱ Attach PDF file of Japan submission

ⁱⁱ Attach PDF file of Korea submission

ⁱⁱⁱ Attach PDF of 2004 China submission

^{iv} Attach PDF of 2014 China report to DFAT

^v **Case study: Infinity electrical cable recall**

The Australian Competition & Consumer Commission (ACCC) has negotiated with 18 local electrical retailers and wholesalers who recalled Infinity electrical cables due to safety concerns on 27 August 2014. It is estimated that around 40,000 homes, commercial and residential buildings could be affected.

Infinity and Olsent-branded Infinity cables, which are imported from China, failed to meet electrical safety standards due to poor quality plastic coating. Testing found the insulation on the concerned cables will become brittle prematurely, especially if exposed to prolonged high temperatures. Once the insulation is brittle, physical contact with the cables could dislodge the insulation and lead to electric shock or possibly fires.

Electrical safety regulation is managed under state and territory legislations. The strength of pre-market verification is risk based. Although the first samples of cable being offered by the importer, Infinity Cable Co Pty Ltd, were accredited testing by certification, subsequent testing by regulators identified the safety issue.

As Infinity Cable Co Pty Ltd, the importer, is now in liquidation, the provisions

of the *Corporations Act* guide the liquidator not to incur any expense during the process of the wind-up unless funds are available. This means Infinity Cable Co Pty Ltd is not necessarily expected to take steps in response to any recall notice.

However, the ACCC also indicated it is challenging to pursue legal action against the manufacturer of these cables in China, as this involves a range of complex international laws and treaties. Against this complexity, the Australian Consumer Law regards the importer as the manufacturer and responsible entity