Senate Select Committee Inquiry into Australia-United States of America Free Trade Agreement

ACTU Submission

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Introduction

1. The Australian Council of Trade Unions [ACTU] is the peak council for organised labour in Australia. Unions affiliated to the ACTU cover all sectors of the economy across all states and territories, representing more than 1.8 million workers.

2. The ACTU welcomes the opportunity to make this submission to the Senate Select Committee Inquiry into the draft free trade agreement with the US.

3. The ACTU believes strongly that trade agreements should be multilateral arrangements. We believe further that trade agreements should be 'positive list' in structure; contain effective provisions that uphold and reinforce labour and environmental standards; and have appropriate exemptions for public, social, and essential services.

4. Regrettably, the Australia-US Free Trade Agreement [AUSFTA] has none of these characteristics.

5. The ACTU's strong commitment to multilateral agreements reflects the following considerations:

   - The economic benefits of such agreements are available to both industrialised and developing countries.

   - The proliferation of bilateral trade agreements leads to different rules of origin and associated complexity and other costs for exporters.

   - There is a significant risk of trade diversion due to bilateral preferential trade agreements. This has been highlighted by the recent Productivity Commission evaluation of around 17 bilateral agreements.

   - The advantage of multilateral negotiations is that smaller countries are able to aggregate their bargaining power to negotiate on a more equal basis with major economies.

   - Multilateral negotiations are more appropriate for Australia given our diverse patterns of trade, with major export markets in Asia, Europe, the Middle East and North America.

6. AUSFTA has a further significant defect. Its patchy outcome in agricultural liberalisation is an adverse precedent for future bilateral and multilateral negotiations.

7. The first key message from AUSFTA is that the US refuses to open its own highly protected agricultural sectors (such as sugar) to competition. That Australia is an English speaking liberal democracy; a long term military and political ally; an active supporter and contributor to the American invasion of Iraq; and a host country of military bases important to US surveillance and intelligence capabilities; counts for nought in this context.

8. The second key message is that Australia, the leader of the Cairns Group, is prepared to accept such an outcome arising out of bilateral negotiations with

the US.

9. Neither message assists the objective of reinvigorating the Doha round of WTO negotiations through securing the agreement of the US, the European Union, and Japan to the dismantling of barriers to trade in agriculture.

10. Notwithstanding the substantial advantages of multilateral instruments, it is necessary to consider AUSTFA in its own terms as a bilateral agreement, and from the perspective of Australia's interests. The agreement is between independent sovereign states with many cultural ties and historical similarities, but it is clearly not an agreement between economic equals.

11. The US has a trade surplus with Australia in the order of $A12 billion annually. Some 93% of US exports to Australia are manufactured goods. The US has a huge domestic market delivering US firms immense advantages in economies of scale and scope, with a significantly larger capital base for its manufacturing and service sector firms. AUSFTA provides US firms with comprehensive access to the Australian market.

12. The fundamental sovereign right of our government to make laws in the national interest should not lightly be forfeited. In our cultural industries for example, the right to implement regulations without constraint has been relevant to the development of our national identity. However the AUSFTA restricts future Australian governments from amending or introducing such legislation if it provides a trade advantage to Australia under the terms of the AUSFTA.

13. Under AUSFTA the US retains its yarn-forward rule for textiles and clothing, which significantly disadvantages the Australian industry seeking to export to the US. The US also retains a comprehensive exemption under national security provisions.

14. In agriculture, where Australia has a competitive advantage, key US markets such as sugar retain comprehensive protection. Others agricultural sectors benefit from long phase-out periods, safeguard mechanisms, and other loopholes.

15. In short, AUSFTA is not a good deal for Australia, which is why there is disquiet among business groups and commentators that are otherwise strong supporters of free trade.

16. Lobbyists for AUSFTA have backhandedly acknowledged the poor quality of some of the outcomes for Australia. Currency appreciation having greatly reduced or eliminated the $4bn 'static gains' previously claimed on the basis of economic modelling as likely to flow to Australia from the agreement, these same lobbyists now disparage "static modelling" and resort to secondary elaboration claiming "dynamic efficiency" gains over time to support the agreement.

17. In this respect the secondary elaboration contained in the supplementary CIE Report "Economic Analysis of AUSFTA" [April 2004] is laughable. The 'static gains' from trade liberalisation suggested by this revised modelling are less than half those suggested in the original study. Cover for the proponents of the AUSFTA is purportedly provided, however, with heroic assumptions delivering additional (small) 'dynamic' gains and huge further gains from

investment liberalisation. Professors Garnaut and Quiggin have hit these claims out of the park. [ABC 'AM' 5/5/04 and Australian Financial Review 6/5/04 respectively]

18. Dynamic efficiencies are said to arise from greater integration with the US economy, in large part as a result of the significant curtailment of national interest screening of American investment in Australia. This argument ignores all potential downside risks of investment liberalisation and greater integration with the American economy.

19. The essential 'dynamic efficiency' claim is that - as a result of more US takeovers, acquisitions, and new business investment in Australia - Australia will obtain greater familiarity with innovative American business models, and secure a significant increase in the transfer technology and intellectual property.

20. The ACTU does not subscribe to the view that foreign investment from the US or other countries is detrimental to Australia however we believe that the dynamic efficiency argument is over-stated by its proponents.

21. The US is already the largest source of foreign investment in Australia, accounting for around 30% of the total inflow. Thus any projected dynamic efficiency gains assume a significant increase in US sourced investment that was apparently previously deterred - by a Foreign Investment Review Board process that rejected very few applications.

22. Alternately, the dynamic efficiency argument rests on AUSFTA generating a significant magnetic attraction to US investors, overshadowing the lure of other economies including China and India that are recipients of US investment. Some of these countries already have or are negotiating their own bilateral trade agreements with the US, with the obvious potential to substantially reduce any dynamic efficiency gains for Australia arising out of AUSTFA.

23. The dynamic efficiency argument also assumes a reasonably high correlation between American investment and transfer of technology and intellectual property, and that the transfer will occur voluntarily. Performance requirements that would make the transfer of technology and intellectual property a condition for the approval of foreign investment are prohibited in AUSFTA.

Labour and Environmental Standards

24. The ACTU acknowledges that AUSFTA breaks with Australian tradition in respect of trade agreements by containing Chapters on Labour and the Environment.

25. It is to be hoped that this approach will apply to other bilateral agreements and that the Commonwealth will henceforth support the proposals in these areas of the International Confederation of Free Trade Unions and international environment organisations in the WTO negotiations.

26. Regrettably however, the detail of Chapters 18: Labour and 19: Environment of AUSFTA indicates that the parties are not serious about regulating this aspect of their trade relationship.

27. The Labor Advisory Committee for Trade Negotiations and Trade Policy in the US has pointed out that the standard of the labour provisions in AUSFTA is below that of other bilateral agreements that the US is party to, including the US trade agreement with Jordan.

28. The remainder of this section of the ACTU submission concentrates on the Labour Chapter, however the observations made are also relevant to the Environment Chapter.

29. AUSFTA does not bind the parties to uphold the core labour standards set by the International Labor Organisation.

30. Article 18.1 of AUSFTA records the parties 'reaffirmation of their obligations as ILO members' and proclaims that each party shall " strive to ensure" that its laws provide for labour standards that are consistent with internationally recognised labour principles and rights. These principles and rights are set out in Article 18.7 in manner that *appears* to give force to the core ILO standards.

31. However, non-compliance by a party with the stated objective, principles and rights is outside the scope of the dispute settlement provisions of the agreement.

32. AUSFTA also states in Article 18.2.2 that it is inappropriate to encourage trade or investment by a party weakening or reducing the protections afforded in its labour laws. The parties commit that they shall strive to ensure that they shall not, in order to encourage trade or investment, waive or otherwise derogate from their respective labour laws, or offer to do so, in a manner that weakens or reduces their adherence to the internationally recognised labour principles.

33. However Article 18.2.2 is not enforceable under the dispute settlement provisions of the agreement.

34. The only provision in this area that is actionable under the dispute settlement proceedings is the failure of a party to effectively enforce its domestic labour standards. Such failure must reflect a sustained or recurring course of action or inaction, in a manner that affects trade between the parties (see18.2.1 (a), 18.6.5 and 21.2).

35. In its terms AUSTFA would prohibit a failure to enforce, but not a decision to weaken or reduce, domestic labour standards. AUSTFA includes no enforcement mechanism whatsoever for labour standards that are consistent with internationally recognised labour principles and rights.

36. Well might it be asked, "Why is it so?"

37. The answer to this question does not lie in any alleged difficulty of enforcing the aspirational language used in 18.1 and 18.2.2. Commitments to uphold core ILO standards and domestic labour standards could have been specified

without recourse to words such as " strive to", but are not in this Agreement.

38. Other AUSFTA provisions that set an objective (such as the obligation in Article 10.7.2 to "endeavour to ensure" that domestic regulation requirements meet certain tests) are not excluded from the scope of application of dispute settlement proceedings.

39. Relevantly in this context, even claimed breaches of 18.2.1 (a), while falling within the scope of application of the dispute settlement proceedings, are treated differently to claimed breaches of other AUSFTA obligations.

40. Specifically, a dispute settlement panel dealing with a failure by the party in breach of 18.2.1 (a) to agree on a resolution or to observe the terms of an agreed resolution must, in awarding compensation, take into account mitigating factors. These include such matters as, the pervasiveness and duration of the breaching party's failure to enforce the labour law; its reasons for non-enforcement of that law; its resource constraints; and its efforts to begin remedying the non-enforcement since the panel's report.

41. No list of mitigating factors can be found in connection with assessment of compensation for other types of breaches, in our analysis of the AUSFTA.

42. In further contrast with compensation provisions for breaches of other AUSFTA obligations, there is a dollar cap on the amount of compensation payable for breaches of the labour obligations. Moreover, the amount is not payable to the complaining party. The compensation is allocated to a fund jointly administered by the two governments for appropriate labour and environmental initiatives.

43. The overall effect of these enforcement provisions is to make the penalty for breaches of labour obligations less onerous than for other breaches of AUSFTA.

44. The ACTU accepts that there may be a case for spending any compensation payable, on initiatives within the territory of the offending party, directed to rectification or prevention of recurrence of such breaches. However, joint administration of the fund created for this purpose confers on the offending party an effective veto on how that compensation money is to be spent. A better alternative would be for the fund to be administered by the ILO.

Jobs

45. The ACTU is concerned about the potential exacerbation effect of AUSFTA on job losses in the manufacturing sector, particularly in the Textile Clothing and Footwear and motor vehicle components industries. The yarn forward rule is to the detriment of Australia's exports, and the Textile Clothing and Footwear Union estimates that around 80% of the industry's goods will not qualify for export to the US using this rule.

46. The ACTU acknowledges that the phase-out of tariffs for certain goods by 2010 or 2015 is broadly in line with that already proposed outside the context of a bilateral free trade agreement. However, the Commonwealth could have amended or delayed that tariff reduction schedule in light of the

circumstances prevailing in the industries at particular points in time. AUSFTA circumscribes this flexibility.

47. The ACTU is concerned not only to avoid job losses but also to ensure that Australia maintains and expands a high value added manufacturing sector. Tariffs are one of a range of policy instruments available to governments promoting industry development. Unfortunately other instruments are also prohibited by AUSFTA. Mention has already been made of the prohibition on performance requirements in the Investment Chapter, but the AUSFTA Chapter of on Government Procurement is also germane in this context.

48. Article 15.2 affects the ability of Australian governments to use procurement policies to foster industry development by prohibiting preference to domestic goods, services and suppliers for measures and procurement covered by the Chapter. Article 15.5 prohibits the seeking, imposition, or enforcement of offsets by procuring entities.

Service Sector Issues

49. The impact of AUSFTA on services occurs as a result of the combination of Chapters 10, 11, and 15, together with the associated annexes and letters of understanding, and the negative list structure of the agreement.

50. 'Negative list' agreements set down in the text of the agreement the general terms and conditions to apply, and list in the annexes the specific exemptions for existing measures and existing services.

51. The ACTU is opposed to negative list free trade agreements. Such agreements provide only one chance for negotiators to identify those exemptions that are to be incorporated in the terms of the Agreement. They also have the effect of applying automatically the terms of the agreement to new services or service sectors, with corresponding limitation on the regulatory options of future governments.

52. The ACTU shares the objections to AUSFTA by its affiliate MEAA [the Media, Entertainment and Arts Alliance], and other organisations in the film, television, radio and cultural sectors.

53. The audio-visual exception notified by the Commonwealth is inadequate and clearly deficient. It is not comprehensive, and therefore fails to empower the government and its successors to remedy deficiencies in our current local content rules for both free to air and pay television. It similarly constrains the government in responding with new regulation to emerging and future delivery platforms.

54. The effectiveness of existing content requirements for free to air television will be undermined by multi-channelling and the limitation in the exception notified on the number of channels to which such requirements may be applied.

55. No exception is listed for broadcasting in general, in contrast to the comprehensive Annex 4-II(A)-10 reservation for broadcasting and audio-visual services listed by the Commonwealth under the Singapore Australia Free Trade Agreement [SAFTA]. While it may be argued that the ABC is

covered by the general AUSFTA exemption for services in the exercise of governmental authority, this argument is problematic in the case of SBS.

56. SBS is a Corporation that competes with other broadcasters not only for viewers but also for commercial advertising and associated revenue. The only other AUSFTA provision that may exempt SBS is the definition of an investment in Article 11.17.4, but this depends upon SBS not being or becoming a government owned enterprise with the characteristics of an investment as set out in that Article.

57. In several areas, the exceptions or non-conforming measures listed by the Commonwealth in AUSFTA fail to match the scope and standard of reservations listed in SAFTA.

58. There appears to be no AUSFTA equivalent to the SAFTA reservations for
- the creative arts, cultural services, and entertainment services;
- public utilities and public transport;
- services in the exercise of governmental authority devolved to the private sector at the time that the agreement came into force; or
- from the national treatment obligation in respect of the supply of secondary and higher education services by commercial providers.

59. We acknowledge that the Commonwealth has listed an Annex II exception for all sectors in AUSFTA, that allows State governments to adopt or maintain any measure not inconsistent with Australia's Market Access commitments under GATS.

60. However, there is neither a general reservation for all sectors (nor equivalent specific reservation for the Commonwealth), that allows the Commonwealth as well as the States to adopt or maintain measures that are not inconsistent with Australia's National Treatment obligations under GATS.

61. There is an important exclusion for subsidies and grants from both the Services and Investment Chapters; this does not extend however, to other forms of preferential treatment of domestic service providers relative to US owned ones. The only exception for all sectors to the National Treatment obligation of AUSFTA, is for existing non-conforming measures at the regional level of government.

62. The Department of Foreign Affairs and Trade, in its Regulatory Impact Statement, makes the following observation on page 10.

> *"A number of trade restrictive measures will be bound at existing levels in the list of reservations to the Cross-Border Trade in Services and Investment Chapters. As is the case with the Commonwealth Government (as described above) this will mean less regulatory flexibility for State and Territory Governments to impose new trade-restrictive measures in those areas or to make existing measures in those areas more trade restrictive."*

63. We note the Department's acknowledgment at page 47 of its 1st Edition March 2004 Guide to the Agreement, that a ratchet mechanism applies to existing non-conforming measures listed as exceptions in Annex I.

64. This means that if an Australian government changes a measure in a way which decreases its degree of non-conformity with the specified AUSFTA obligation, neither government nor any of its successors can shift back to the level of non-conformity of the measure extant at the time AUSFTA came into force. This is an inappropriate restriction on the regulatory power of governments.

65. The impact of AUSFTA on the services sector is not transparent, in contrast with the detail provided in the text itself and in Departmental documents, regarding the agreement's consequences for tariffs.

66. A detailed comparison is required between the AUSFTA obligations and the listed exceptions on the one hand, and Australia's GATS commitments on the other. This exercise is complicated by the fact that the latter are often expressed by reference to numerical codes for a service sector, a sub-sector, or a particular service within a sub-sector.

67. Given this, it is not surprising that in Senate Estimates on Tuesday 2 March Australia's Chief Negotiator, Stephen Deady, elected to take on notice a question from Senator Conroy about what service sector commitments Australia has given in AUSFTA over and above Australia's GATS commitments.

68. No detail in this respect can be found either in the National Interest Analysis or the Regulatory Impact Statement. A rough comparison by the ACTU suggests that service sectors and parts thereof where additional commitments may have been given include:
    - construction;
    - commission agents and wholesale trade in services;
    - repair services of personal and household goods;
    - transport services;
    - post and telecommunications;
    - legal services
    - financial services;
    - real estate services;
    - leasing services
    - computer-related services;
    - research and development services;
    - taxation, architecture and accounting services;
    - other business services;
    - engineering, planning, agriculture, mining and manufacturing services;
    - education;
    - sewage and refuse disposal;
    - sanitation and other environmental services; and
    - recreational , cultural and sporting services.

69. Other services such as energy and water supply may be affected because of the negative list structure of the agreement.

70. The exceptions notified by Australia override nominated obligations, but the Domestic Regulation obligation contained in Article 10.7.2 is omitted from the list of displaced obligations.

71. This Article goes way beyond the GATS equivalent Article and requires Australian governments to ensure that technical standards, qualification requirements and licensing requirements are not more burdensome than necessary to ensure the quality of the service and do not constitute unnecessary barriers to trade in services. The de facto terms of reference for such a review prescribed in the Article are very narrow and unbalanced, and could be used to question those licensing requirements for utilities and other services that reflect considerations such as equitable access, affordability etc.

Investment Liberalisation

72. The ACTU opposes the removal of all national interest screening of investment for new businesses and of takeovers and acquisitions below $800million, other than for the excepted sectors and enterprises. The change from $50 million to $800 million as the threshold for scrutiny of takeovers and acquisitions in the case of US investment is extraordinary.

73. As Australia has a range of bilateral Investment Agreements that promise Most Favoured Nation treatment to the other parties, the changes to thresholds under AUSFTA will also flow on to those other countries.

74. The US is the largest source of foreign investment to Australia. This change puts a big question mark over the government's commitment to the existing foreign investment rules.

75. The Office of US Trade Representative estimates that 90% of US investment in Australia over the last 10 years would have escaped screening had the new rules applied retrospectively. Using a three-year retrospective time horizon, DFAT estimates in its Regulatory Impact Statement a reduction in screened proposals by 65-70%. Some commentators have claimed that, under the proposed AUSFTA rules, around 86% of companies listed on the Australian Stock Exchange could be acquired by US interests without being screened.

76. We acknowledge that the vast majority of applications that are screened by the Foreign Investment Review Board are approved. However, the Board also has a track record of approving applications subject to conditions set to safeguard the national interest. This aspect of the screening process should be borne in mind when it is argued that the current process is simply a time-consuming one that leads to approval anyway.

77. Without wishing to imply the use of these requirements by the Board for conditional approvals, the ACTU is concerned about the removal of reserve powers for industry policy in AUSFTA.

78. Article11.9.1 prohibits the imposition or enforcement of any undertaking to export a given level or percentage of goods or services, to achieve a given level of domestic content, to accord preference to locally produced goods, or to transfer technology, a production process or other proprietary knowledge. Article 11.9.2 prohibits a shorter list of requirements as a condition for the receipt or continues receipt of an advantage.

Manufacturing Sector Issues

79. The manufacturing sector is experiencing major difficulties in Australia in terms of significant job losses and declining share of exports.

80. The original Centre for International Economics (CIE) Report projecting benefits of a free trade agreement with the US indicated that the manufacturing sector would be a prime beneficiary of liberalised trade under AUSFTA.

81. At that time the Australian Manufacturing Workers Union (AMWU) pointed out that the CIE's projections for manufacturing in Australia's case were based on outdated 1997 data, and that the sector's difficulties had worsened since the data was compiled. The projections also assumed full liberalisation, and a long -term exchange rate that may need to be reassessed in light of the recent appreciation of the Australian dollar.

82. The ACTU understands that the AMWU has commissioned econometric modelling on AUSFTA and will seek to make further comments to the Committee, if possible, once that modelling and the new CIE report to the Commonwealth become available.

General Policy Matters

83. The ACTU opposes the concessions granted to the US with respect to the Pharmaceutical Benefits Scheme.

84. There should be no provision for an independent review of product listing decisions. In the absence of text in AUSFTA to the contrary, this provision appears to empower such a review to overturn PBS decisions. To the extent that they create new or additional opportunities, the commitments in the proposed exchange of letters on pharmaceuticals (regarding responding to reports and evaluations; hearings while the Pharmaceutical Benefits Advisory Committee is considering technical reports from sub-committees, and applying for adjustments to a reimbursement amount) are also of concern.

85. The Agreed Principles in Annex 2-C Pharmaceuticals reflect the arguments of US drug companies without any offsetting reference to the importance of affordability of, and equitable access to pharmaceuticals. This in conjunction with the letter reads as criticism of the PBS and its procedures and a joint government statement of expectations of different outcomes from PBS processes.

86. Related concerns include the establishment of the joint Medicines Working Group, with an emphasis upon the importance of pharmaceutical research and development, and the changes to the procedures of the Therapeutic Goods Administration with respect to approval of generic drugs.

87. The ACTU objects to the acceptance of the US copyright standard of 70 years after the author's death or completion of production in the case of audio-visual works. Australia is a net importer of intellectual property from the US and this decision, by taking 20 years of works out of the public domain, will increase the costs borne by libraries and education institutions.