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Draft Productivity Commission report: Bilateral and Regional Trade Agreements

The draft report on bilateral and regional trade agreements is a welcome – and long overdue – independent review of whether such agreements genuinely operate in Australia's interest. This is important as trade agreements have the potential to deliver benefits to narrow sectional interests at community expense. It is a clear and well set out report, providing a sound basis for Australians to engage with this important area of public policy.

This very brief submission covers two main areas: so-called "IP protection" and international arbitration arrangements for foreign direct investment. It also suggests that, based on the available evidence, the Commission should be more forthright in rejecting bi-lateral trade agreements and in dealing with the inclusion in these agreements of anti-competitive policies and policies which stray from the economic arena into issues of social and environmental policy. A stronger focus on the overall context of trade agreements – to maximise competition and remove anti-competitive barriers – would assist here.

Should Australia participate in bilateral trade agreements?

The Commission seems hesitant to make full use of the dispassionate evidence available to it. For example its first recommendation is hedged with provisos and thus does not say as clearly as it might that bilateral and regional trade agreements are rarely in Australia's interests and should be avoided. Considered objectively, many of these agreements have such limited benefit for Australia that it is hard to find any rational basis for them. One thus has to turn to non-economic factors to explain their prevalence. They appear to be undertaken for public relations reasons (to give a visiting minister of state something to announce) or for alleged "strategic benefit" reasons. Given this, a stronger recommendation against undertaking such welfare-reducing activities might have been expected.

> It would be good to see the final report make a strong statement that bilateral agreements should be avoided as a matter of general policy.
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> The more nuanced draft recommendation 1 might better suit regional trade agreements as these may be less damaging. As the Commission recommends, such regional agreements should be restricted to trade matters and only

undertaken where there is clear evidence of benefit to the community as a whole.

At the time the probably welfare-reducing[1] "Free Trade" agreement with the USA (AUSFTA) was signed there was widespread community understanding that it was being pushed for "strategic" reasons.[2] The Commission focuses on the economic impact of these agreements, as is proper. It is a moot point, however, as to whether these agreements deliver any of the "strategic" benefits they are alleged to confer. Without clear evidence of such non-economic benefits, it is extraordinary that democratically elected countries have so vigorously pursued these "trade" agreements when there is little *empirical* evidence that they deliver any positive benefit. The only explanation lies in the realm of interest group theory – the sectional interests which benefit from these agreements have prevailed over the public interest. The Commission's recommendations for a stronger evidence-base and greater transparency might help in the future to offset this lobbying power.

Inclusion of anti-competitive elements in "free trade" agreements

Since the Uruguay Round of international trade negotiations a range of anti-competitive elements have been inserted into so-called "free trade" agreements. The worst of these is legislated monopolies for inventions and published materials, embodied in the badly titled Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS Treaty). Others have demonstrated how particular corporate interests, working in concert through lobbying of key trade negotiating blocks (the USA, the European Union and Japan), were able to hi-jack the international free trade agenda and impose these anti-competitive elements on the international free trade community.[3] Australia, to its shame, was a "friend of intellectual property" in the Uruguay negotiations and assisted in foisting these monopoly interventions on the free trading nations of the world. Why Australia took this position is unclear. It has long been known that extensive patent and copyright systems are not in the economic interests of most countries, including a country such as Australia.[4]

Legislated monopolies, especially patents and copyright

It is clear from the report that the Commission understands that many of the so-called "intellectual property" provisions of bilateral agreements have been anti-competitive and welfare-reducing. Again, however, the Commission's recommendations are very restrained. In draft recommendation 4, it suggests a "cautious approach" to "IP protections" and other non-trade elements of these agreements. The so-called "IP protections" are legislated monopolies. The extension in the copyright term embodied in the AUSFTA came at a significant cost to Australia, especially to Australia's educational and cultural sectors.

In the area of agricultural trade, Australia has not hesitated to take a globally leading advocacy position using evidence-based research to point out the welfare-reducing impact of agricultural subsidies. Australia should take a similar approach to legislated monopolies.

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[1] Weiss, et al., 2004; Dee, 2005; Dieter, 2006.

[2] With a sub-theme that it was an expression of the close personal relationship between the then prime minister of Australia and the then president of the USA.

[3] See for example Drahos with Braithwaite, 2002; Sell, 2003.

[4] See for example Penrose, 1951. At the time of the Uruguay negotiations this analysis – that extensive monopolies for inventions are welfare-reducing for countries without significant innovation exports – was repeated in Deardorff, 1992.

There is no evidence that patent monopolies are generally needed.[5] Indeed it has been demonstrated that most industrial artefacts take time and resources to imitate.[6] Australia may not gain any "strategic" benefits from its trade negotiation policies but it would re-gain respect in the international trade community if it took a leadership position in requiring an evidence base for the inclusion of non-trade items, especially those with clear anti-competitive mechanisms, in trade negations.

The inappropriateness of including monopoly systems in a system designed to promote free trade and the benefits of competition is patently obvious. The language of the beneficiaries – "protection" "piracy" and "free-riding" – does nothing to hide the fact that the "protected" goods have usually already achieved substantial profits for their makers in their home markets and high-income export markets, thanks to the government-granted monopolies. In such circumstances the term "free-riding" is highly questionable – a better term for the demand for further monopolies in sovereign nations would be "rent-seeking".[7] Any "piracy" involved is the transfers of royalties from low-income nations to large multi-national companies who have already made a very healthy return on their innovation investment. At a minimum the Australian government and its agencies should cease using this very loaded language. Preferably they should study the evidence and drop their support for these welfare-reducing policies. Patent and copyright monopolies have never been subjected to systematic, evidence-based economic analysis.[8]

Forum-shifting investment arbitration arrangements

In the period since the establishment of the World Trade Organisation (WTO), major trading nations have found that they have been unable to progress a new round of multi-lateral trade negotiations. This is perhaps because the benefits from the proposals in the Doha Round strongly favour high-income countries (Gallagher, 2008). Despite having achieved a trade playing field clearly and substantially tilted in its favour, the USA in particular has shifted forums persuading lower-income nations to sign up to sweeping agreements by offering "strategic" benefits (including often mythical foreign direct investment) through broad-ranging bi-lateral and multi-lateral "trade" agreements (Drahos, 2001).

These proliferating agreements go well beyond a free trade agenda, leading to substantial interference in national sovereignty for WTO members. The worst of these is the arbitration arrangements for international investment flows. These arbitration arrangements fail all tests of good governance, being neither transparent nor fit for purpose (see, for example, Tienhaara, 2009). It is wrong that Argentina has had to

[5] See, for example, Scherer, et al., 1959; Firestone, 1971; Taylor and Silberston, 1973; Mansfield, 1986; Levin, et al., 1987; Mazzoleni and Nelson, 1998; Cohen, et al., 2000; Scherer, 2006. While these studies show that pharmaceutical and chemical products and processes are more dependent on patent monopolies, Mansfield, 1986 and Boldrin and Levine, 2008, demonstrate that many pharmaceutical products would be or are produced without such monopolies.

[6] Mansfield, et al., 1981; Cohen, et al., 2000.

[7] For a useful discussion of the distorting effect of the use of the term free-riding on consideration of the important issue of knowledge spillovers and technology diffusion see Lemley, 2005.

[8] The closest such analysis remains Machlup's 1958 report to the US Congress (Machlup, 1958) and the supporting documentation to the IPAC review (Mandeville, et al., 1982a; 1982b). The IPAC review was billed as an economic assessment but the sole economist on the committee lodged a dissenting statement saying that '[t]his report does not live up to its claim to have adopted an economic perspective and to have applied economic criteria' (IPAC, 1984: 79). While the IPCRC (IPCRC, 2000) undertook a reasonable analysis of copyright monopolies, in regard to patents it simply assumed these were necessary (see criticism by Lawson, 2005).

compensate overseas corporations for the essential economic policy step it took when, faced with severe economic challenges, it devalued its currency. The world has quietly stood by and let this clear theft take place without any protest.

Gradually, however, the message is getting through that the arbitration arrangements associated with the investment elements of these "trade" agreements fail all tests of good public policy. Australia strongly, and successfully, resisted any such elements in the 2004 AUSFTA. This was done knowingly and for sound reasons. Why then have we forced such iniquitous arrangements on our neighbours? It is hardly an act of friendship to attempt to remove from neighbouring countries the capacity to advance domestic social and environmental policies without risking payment of outrageous fees to well-funded overseas corporations.

The Commission recommends (draft recommendation 5) that dispute settlement processes should not afford greater protections to foreign investors than to domestic firms. This is an important recommendation. Australia should however go further and re-negotiate those agreements where such terms have been forced on our trading partners. That short-sighted policy has the capacity to back-fire in the context of future regional trade negotiations.

Exit and re-negotiation

Australia's trade negotiators should also pay more attention to exit and re-negotiation strategies. In addition to the monopoly ("IP") and investment arbitration provisions that we have included in "trade" agreements with smaller nations, there are elements of the AUSFTA that should be unwound. Means should be found to do this to improve the economic impact of existing agreements rather than to undertake further agreements.

The views I present are my own and should not be taken to represent the views of any institution or organisation with which I may be associated. I have no beneficial interest in the outcome of any trade agreement except as an Australian citizen.

Yours sincerely

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