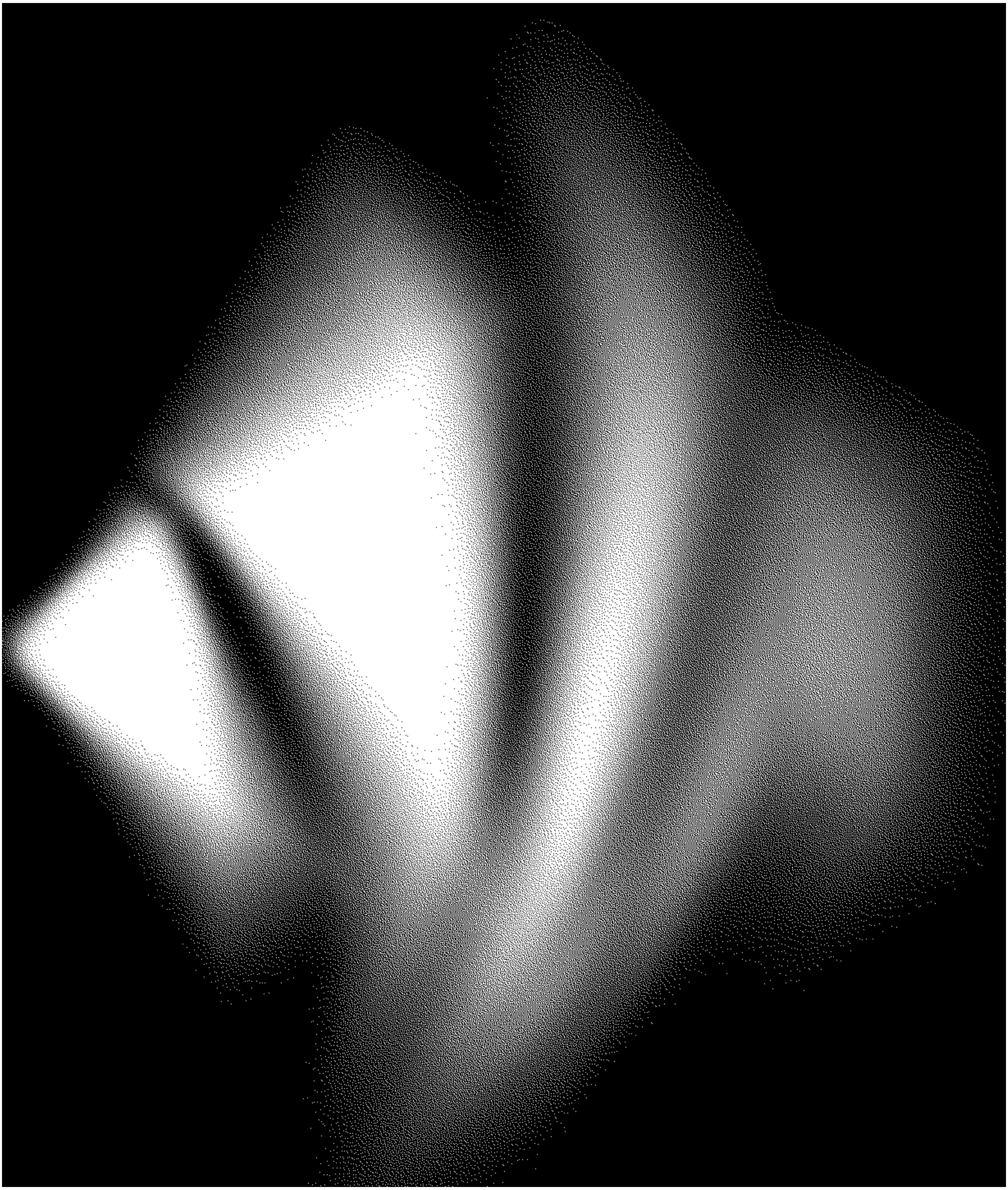
Trade & Assistance Review 1997-98

PRODUCTIVITY COMMISSION



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The Productivity Commission

The Productivity Commission is the Commonwealth's principal advisory body on microeconomic reform. Its activities include:

- holding public inquiries and reporting on matters referred to it by Government
- providing secretariat and research services to government bodies
- investigating complaints about competitive neutrality
- reviewing and advising on regulation through its Office of Regulation Review and
- undertaking other relevant research and advice relevant to enhancing Australia's productivity.

The Commission provides independent analysis and advice, using processes that are open and public and driven by concern for the well-being of the community as a whole.

Information on the Productivity Commission and its current work program can be found on the World Wide Web at http://www.pc.gov.au or by contacting Media and Publications.

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Abbreviations

ABARE	Australian Bureau of Agricultural and Resource Economics
ABS	Australian Bureau of Statistics
ACCC	Australian Competition and Consumer Commission
ACIS	Automotive Competitiveness and Investment Scheme
ACS	Australian Customs Service
ADA	Anti-Dumping Authority
ADI	authorised deposit-taking institution
ANZSIC	Australia and New Zealand Standard Industrial Classification
APEC	Asia Pacific Economic Cooperation
APRA	Australian Prudential Regulation Authority
AQIS	Australian Quarantine Inspection Service
ASIC	Australian Standard Industrial Classification
AWB	Australian Wheat Board
CPA	Competition Principles Agreement
CSIRO	Commonwealth Scientific and Industrial Research Organisation
DIST	Department of Industry, Science and Tourism
EFIC	Export Finance and Insurance Corporation
EMDG	Export Market Development Grants
ERA	effective rate of assistance
EU	European Union
EVSL	early voluntary sectoral liberalisation
FDI	foreign direct investment
GATS	General Agreement on Trade in Services
GATT	General Agreement on Tariffs and Trade
GDP	gross domestic product
GSE	gross subsidy equivalent
IAP	Individual Action Plan
IC	Industry Commission
IR&D	Industrial Research and Development
ITU	International Telecommunications Union
JCPAA	Joint Committee of Public Accounts and Audit
MAI	Multilateral Agreement on Investment
MFN	most-favoured-nation
NCC	National Competition Council
NSE	net subsidy equivalent
OECD	Organisation for Economic Co-operation and Development

PC	Productivity Commission
PMV	passenger motor vehicles
R&D	research and development
RAS	Rural Adjustment Scheme
RBA	Reserve Bank of Australia
TCF	textiles, clothing and footwear
TCS	Tariff Concession Scheme
TEXCO	Tariff Export Concessions
TMRO	Trade Measures Review Officer
TPC	Trade Practices Commission
TQ	tariff quota
TRIPS	trade-related aspects of intellectual property rights
WTO	World Trade Organization

Key Findings

- The Commonwealth Government continues to implement a wide range of policies and programs which assist industry and affect trade. In some cases, these are relatively transparent and assistance can be measured easily, but others are less transparent and, particularly in the growing services sector, difficult to quantify.
- Assistance to the agricultural sector remained largely unchanged in 1996-97, but disparities in assistance widened. While assistance for most commodities is low, pockets of very high assistance remain — most notably for the dairy industry. With the implementation over the next few years of further reforms to assistance arrangements for several commodities, agricultural assistance is expected to fall.
- Manufacturing assistance is projected to continue to fall with the implementation of further scheduled tariff reductions for the passenger motor vehicle and textiles, clothing and footwear industries. However, even in 2000-01, these industries will receive assistance several times higher than all other manufacturing industries.
- With the decline in tariff assistance for manufacturing and the phasing out of statutory marketing arrangements for several agricultural commodities, budgetary assistance is expected to account for an increasing proportion of total assistance afforded to the manufacturing and agricultural sectors.
- The growing importance of Australian and global services trade means that attention is being focused increasingly on restrictions to services trade. These restrictions typically take the form of regulatory controls that, by limiting competition, can protect existing service suppliers at the expense of consumers — in a similar way to measures that restrict trade in goods.
- Australia continues to participate actively in international liberalisation efforts. Important unilateral reforms (including implementation of competition policies) have also been introduced or proposed. However, a wide range of restrictions across many traded service industries are still to be addressed. The next round of negotiations under the General Agreement on Trade in Services (GATS), commencing in 2000, represents an important opportunity to enhance further the transparency of international restrictions and to secure further commitments to liberalisation.

Budgetary assistance

- Assistance through Commonwealth budgetary outlays and tax expenditures fell by 13 per cent to $3.3 billion in 1997-98, but is projected to increase slightly in 1998-99.
- Budgetary outlays remained stable at $1.7 billion in 1997-98. Forward projections suggest that tax expenditures will fall to $1.7 billion in 1997-98 from $2.2 billion in 1996-97, reflecting the tightening of the R&D tax concession and winding down of the development allowance.
- Manufacturing continued to receive the largest share of budgetary assistance in 1997-98 — 43 per cent. Services accounted for nearly 25 per cent, primary production 23 per cent and mining 9 per cent.
- During the past year, significant budgetary assistance initiatives were announced in the *Investing for Growth* Statement (total funding of $1.2 billion allocated over four years). They are expected to affect the level and composition of budgetary assistance in future years. Significant commitments were made for increased R&D support and incentives to attract foreign investment. Details of the new assistance arrangements (post-2000) for the passenger motor vehicle and textiles, clothing and footwear industries were also announced.

Agriculture and manufacturing assistance

- The effective rate of assistance to agriculture remained largely unchanged in 1996-97, at 10 per cent. This was equivalent to a net subsidy to the sector of $1 billion.
- Increases in assistance to dairy, grains, apples and pears, deciduous canning fruit and vegetables were offset by decreases for wool, wine grapes, dried vine fruit, poultry, eggs, cotton and tobacco.
- Disparities in effective rates of assistance across the agricultural sector increased marginally in 1996-97. Dairy remains one of the most highly assisted agricultural activities, with an effective rate nearly 6 times the level for the agricultural sector. If dairy were excluded from the estimates, the effective rate of assistance for agriculture in 1996-97 would fall to 6 per cent.

- Assistance to tobacco is expected to fall substantially over the next few years with the phasing out of statutory marketing arrangements. By 1999-2000, with the completion of the restructuring program for the industry, the effective rate of assistance is expected to fall to only 2 per cent, from around 100 per cent in 1996-97. Recently implemented reforms to the sugar industry will result in significantly lower levels of assistance in 1997-98.
- The effective rate of assistance to the manufacturing sector (which is not strictly comparable to that for agriculture) was estimated at 6 per cent in 1996-97. With further scheduled tariff cuts for the passenger motor vehicle and textiles, clothing and footwear industries, the effective rate of assistance to the sector is projected to fall to 5 per cent in 2000-01.
- The dispersion in rates of assistance across manufacturing industries is declining. However, the PMV and TCF industries are (and in 2000-01 will continue to be) receiving rates of assistance several times higher than all other manufacturing industries.
- While developments in 1997-98 are unlikely to have a significant impact upon measured assistance in the manufacturing sector, recent Government initiatives such as the *Investing for Growth* statement, the Automotive Competitiveness and Investment Scheme and new assistance measures for the TCF industries will have implications for levels of assistance beyond 2000.

Agriculture and manufacturing trade policy issues and developments

- There were 36 new anti-dumping cases initiated by Australia in 1997-98. Initiations have almost doubled in each of the past three years. Internationally, Australia accounted for 8 per cent of total initiations and 6 per cent of measures in force, in 1996. Relative to its share of world trade, Australia continues to be one of the most frequent users of anti-dumping and countervailing measures.
- A new anti-dumping system was introduced on 24 July 1998. It remains to be seen what impact the simpler and faster single stage investigation and the revised review and appeal mechanism will have on the number of initiations and the outcome of investigations. The WTO has questioned whether the shorter investigation period will compromise the thoroughness of dumping investigations and reviews. The Government’s scheduled review of anti-dumping

regulation under the Competition Principles Agreement has been postponed to allow for full implementation of the new arrangements.

- The WTO, in its third Trade Policy Review of Australia, acknowledged progress in a number of areas, including unilateral trade liberalisation and structural reform programs. However, the WTO also highlighted several areas for further reform, including the high levels of assistance afforded to a few industries (notably milk production in the agricultural sector and TCF and PMV within manufacturing). The WTO questioned other areas of policy, such as Australia's relatively strict quarantine regime.
- APEC early voluntary sectoral liberalisation (EVSL) arrangements, initiated in November 1996, are expected to be finalised by November 1998, with implementation scheduled to commence in 1999. There are several issues which need to be addressed if EVSL is to achieve its objectives most effectively. Broadening the product and sectoral coverage in EVSL may be necessary to avoid adverse resource allocation effects.
- Similar considerations are relevant to foreshadowed unilateral tariff reform in Australia, involving the elimination of 'nuisance' tariffs.

International trade in services — policy developments and issues

- Trade in services is an important component of Australian and global trade. Over the past year, Australia has continued to participate actively in WTO, APEC and OECD initiatives designed to liberalise trade in services. Several important unilateral reforms with implications for international services trade have also been introduced or proposed. However, a wide range of restrictions remain across many traded service industries, including the professions, maritime transport and international air services.
- Domestically, a range of Commonwealth and State legislation affecting competition and relevant to services trade is scheduled for review over the next few years under the Competition Principles Agreement. This includes laws regulating certain professions and occupations, international air services agreements, intellectual property legislation, and Part X of the *Trade Practices Act 1974* (international liner shipping exemptions). Changes have recently been made to the *Copyright Act 1968* to permit 'parallel' imports of certain goods and

further changes have been proposed to address concerns raised by the growth of electronic commerce. The recent report on internet commerce by the Joint Committee of Public Accounts and Audit recommended that the Productivity Commission conduct an inquiry into the development and regulatory issues arising from the growth of internet commerce.

- A major international development in the past year was the completion of WTO negotiations on financial services in December 1997, forming the basis for the financial services agreement when it comes into effect no later than 1 March 1999. As a party to the agreement, Australia took the opportunity to amend its commitments to reflect important liberalisation of financial services undertaken as part of implementing the recommendations of the 1997 Financial System Inquiry. Australia has a relatively open financial services sector, but still applies more restrictions on trade in financial services than are scheduled in its GATS commitments.
- The WTO Agreement on Basic Telecommunications came into force in February 1998. The Agreement could assist in realising substantial cost savings for international phone calls over the next few years. However, some further issues need to be reviewed, such as international settlement rates (charged by foreign network owners on completion services for international calls).
- The next round of GATS negotiations commencing in 2000 could focus on services sectors with few commitments and where negotiations have been difficult — for example, maritime transport, air services and professional services. Recognising the importance of links between transport modes, there might be benefit in proceeding with transport negotiations on a multimodal basis. Other options for consideration include locking in to a binding multilateral agreement Australia's recent domestic reforms and scheduling remaining restrictions on trade in financial services to improve the transparency of regulation. The negotiations may also provide an opportunity to improve the structure and scope of the GATS for example, by adopting a 'negative list' approach to scheduling services sectors and commitments.

1 Introduction

The Productivity Commission is required to continue the practice of its predecessors, the Industry Commission and the Industries Assistance Commission, in reporting annually on measures that provide assistance to industry. Assistance is defined broadly to include any act that, directly or indirectly, assists a person to carry on a business or activity, or confers a pecuniary benefit on the person carrying out a business (*Productivity Commission Act 1998*).

Until recently, the focus in the Commission's annual reporting has been largely on assistance to agriculture and manufacturing, particularly the assistance provided through tariffs and other border measures, as well as domestic marketing arrangements designed to support local industry. However, structural and policy changes have meant that a wider range of issues now have to be considered in the Commission's annual *Trade and Assistance Review*.

Structural and policy changes

Since the previous Commissions started reporting on industry assistance, the structure of the economy and the pattern of trade have changed considerably. The services sector now accounts for just over 70 per cent of output and employment in the Australian economy. Services represent a significant proportion of Australia's international trade, accounting for one fifth of the total value of exports and almost one fifth of the total value of imports.

Industry policies have also changed. With a few exceptions, notably for the passenger motor vehicle and textiles, clothing and footwear industries, tariffs and other forms of border assistance have been reduced to low levels. Furthermore, many domestic marketing arrangements have been dismantled, as part of trade liberalisation and domestic competition policy (although some restrictive arrangements at the State level are still in place).

However, the Commonwealth continues to implement a wide range of policies and programs which assist industry and affect trade. In some cases these are relatively transparent — for example, in the case of direct budgetary assistance for certain activities. Others are less transparent. For example, the application of anti-dumping policies may protect and assist local import competing industries, as may the application of quarantine restrictions on imports. In the growing services sector, domestic competition policies and foreign investment policies may restrict opportunities for foreign suppliers to enter the market, and thereby provide some support for local suppliers. While the assistance associated with these types of policies cannot be measured accurately, they are nevertheless an important component of any review of trade and assistance.

Against the backdrop of some significant changes in the economic and policy setting over the past year, this year's review of trade and assistance is particularly important. The significant depreciation of the Australian dollar against some major currencies and the severe economic downturn and instability in several Asian economies, which are both competitors and customers for Australian goods and services, have raised concerns about the effects on particular industries and the wider economy, and the role of the government in providing support. In some quarters this has resulted in calls for increased government assistance and a move away from efforts to open the Australian economy to global competition. To provide a basis for assessing concerns such as these, information on the nature and extent of existing government measures which support particular industries and activities or restrict trade is vital.

Structure of the report

The tools used by the Commission and its predecessors to report on industry assistance — most notably, nominal and effective rates of assistance — are still useful. However, reflecting the policy shift away from forms of assistance that are relatively easy to quantify (such as tariffs and domestic marketing arrangements) and the increasing importance of the services sector, the review of effective and nominal rates of assistance now comprises a relatively small part of this report.

In the following chapter, the most obvious form of assistance to industry, Commonwealth budgetary assistance, is examined. This covers all four sectors — agriculture, mining, manufacturing and services. Assistance to agriculture and manufacturing is examined more closely in chapter 3. This reports nominal and effective rates of assistance, which summarise the effects of a range of quantifiable assistance measures. Chapter 4 covers agriculture and manufacturing trade policy issues and developments, including a review of recent developments in anti-dumping, APEC sectoral liberalisation and the World Trade Organization (WTO) negotiations on agriculture scheduled to commence in late 1999. Chapter 5 is devoted to the services sector, reviewing a range of developments and issues affecting services trade generally. It also has more detailed discussion of some topical service industries, especially financial services, where a major WTO agreement was signed in December 1997 and where there have been some important domestic policy developments over the past year.

The possible rationales for industry assistance and its effects on the economy are not analysed in this report. The aim is to report measures of assistance and related information which can provide a basis for further analysis, both within the Commission and outside. As in the past, the estimates presented in the report cover only Commonwealth assistance. However, key State developments, including reviews of legislation under the auspices of the Competition Principles Agreement, are discussed where relevant. The Commission's detailed report on State, Territory and local government assistance to industry was released earlier this year (IC 1996a).

2 Budgetary assistance

Assistance through budgetary outlays and tax expenditures totalled $3.3 billion in 1997-98, a decrease of 13 per cent in nominal terms from the previous year. Budgetary assistance is projected to increase slightly to $3.4 billion in 1998-99.

Budgetary outlays have been relatively stable at $1.7 billion, following the termination of several programs in 1996-97. Tax expenditures increased significantly to $2.2 billion in 1996-97, due to the revenue impact of the development allowance. Forward projections indicate that tax expenditures will fall to $1.7 billion in 1997-98, reflecting the tightening of the R&D tax concession and winding down of the development allowance.

The Commonwealth Government has recently announced several budgetary assistance initiatives. These measures are expected to affect the level and composition of budgetary assistance in future years.

2.1 Scope of the Commission's estimates

Budgetary assistance comprises budgetary outlays and tax expenditures that selectively benefit firms, industries or activities in the economy. Budgetary outlays include direct financial assistance — bounties, grants, interest rate subsidies, loans, loan guarantees, insurance and equity injection — as well as funding to organisations which perform activities of benefit to industries (for example, to the Australian Tourist Commission for promotion of tourism). Tax expenditures (or concessions) provide financial assistance by reducing the tax burden of certain firms, industries or activities. Tax expenditures take the form of exemptions, deductions, rebates, preferential tax rates and tax deferral.

The coverage of budgetary assistance excludes programs which have major social objectives, such as outlays on defence, health, education and the labour market. Also excluded are generally available measures which do not discriminate between industries or activities. Assistance estimates in this chapter do not incorporate the Diesel Fuel Rebate, which is designed to offset the diesel fuel excise for off-road users in agriculture and mining. The approach adopted in classifying budgetary assistance was discussed in more detail in *Trade and Assistance Review 1996-97*.

The focus in this chapter is on reporting the budgetary assistance provided by the Commonwealth Government. State, Territory and local governments also provide substantial budgetary assistance. The Industry Commission's inquiry into State, Territory and local government assistance to industry (IC 1996a) estimated that budgetary assistance afforded by State and Territory governments totalled $5.7 billion in 1994-95. This consisted of $2.5 billion in budgetary outlays and $3.2 billion in payroll tax exemptions.

Budgetary assistance is also reported by sector — namely, primary production, manufacturing, mining, and selected services. Where data on the recipients of assistance are not available, government programs are allocated to the sector considered to receive the largest share. Due to these data constraints, caution is needed when interpreting the sectoral distribution of assistance.

Budgetary outlay figures are derived from Commonwealth Budget Papers and departmental annual reports. Data for 1997-98 are estimated expenditures and for 1998-99 are budget appropriations.[1] Tax expenditure figures are from Treasury (1997b) and Australian Customs Service (ACS 1998). Data for 1997-98 and 1998-99 are forward projections.

2.2 Trends in Commonwealth budgetary assistance

Commonwealth budgetary assistance to industry is estimated at $3.3 billion for 1997-98 (table 2.1). In nominal terms, this is a decline of 13 per cent on the previous year. Budget appropriations are expected to increase slightly to $3.4 billion in 1998-99.

Table 2.1 **Commonwealth budgetary assistance to industry**
$ million

	1995-96	*1996-97*	*1997-98*	*1998-99*
Budgetary outlays	1 929	1 698	1 685	1 726
Tax expenditures	1 759	2 169	1 668	1 701
Total budgetary assistance	3 688	3 867	3 353	3 427

Source: Commonwealth Budget Papers, Treasury (1997b), ACS (1998) and Commission estimates.

[1] As the 1998-99 Federal Budget was introduced in May, the Budget Statements did not report expenditure outcomes for 1997-98. Actual outlays will be known later in 1998-99.

In real terms, the 1997-98 assistance level is the lowest since 1992-93. Commonwealth budgetary assistance in 1997-98 was delivered through more than 120 government programs and tax expenditures.

Budgetary assistance estimates have been revised for previous years as information on the revenue costs of some tax concessions, most notably the development allowance, is now available. The relatively high level of assistance in 1996-97 mainly reflects the revenue impact of the development allowance. The increase in total assistance from the previous year occurred despite a substantial fall in budgetary outlays, following the termination of several bounties and export programs. The fall in assistance estimated for 1997-98 is attributable mainly to the tightening of the R&D tax concession and the winding down of the development allowance.

Budgetary outlays

Budgetary outlays accounted for $1.7 billion in 1997-98, or half of total budgetary assistance. Budget appropriations indicate no significant change in outlays in 1998-99. Budgetary outlays benefiting industries are provided as direct financial assistance and funding to intermediary institutions.

Direct financial assistance

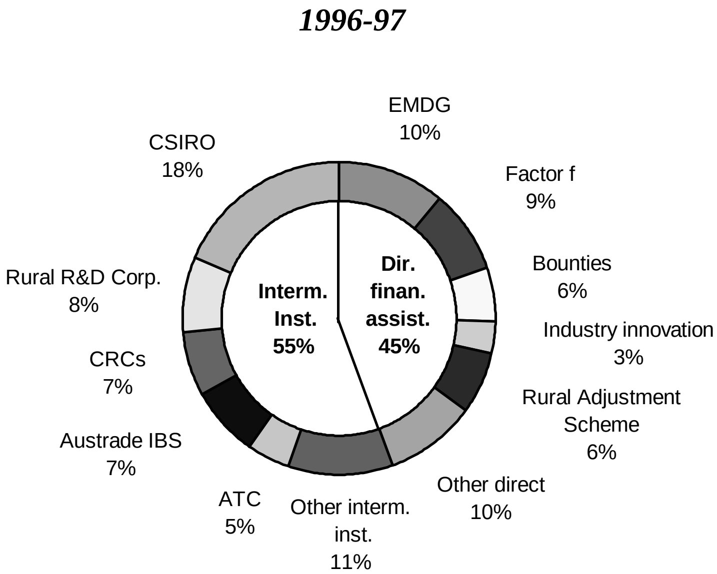
Direct financial assistance accounted for $729 million or 43 per cent of budgetary outlays in 1997-98 (figure 2.1). Direct financial assistance has declined in absolute terms and as a proportion of outlays since the early 1990s. This has been due to the reduction of several outlays, including the termination of bounties and concessional finance schemes.

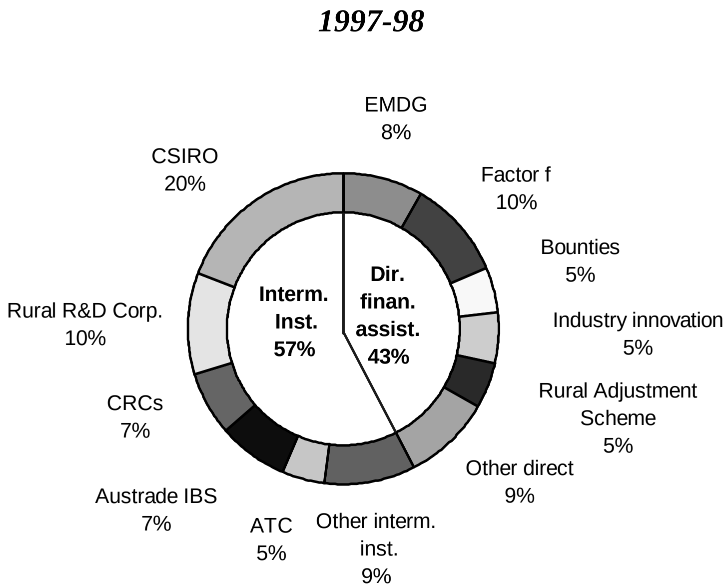
The shipbuilding bounty, recently extended to 30 June 1999, is the only remaining bounty scheme in Australia. The bounty is paid at 5 per cent of eligible costs and outlays on the scheme have accounted for around $20 million in recent years. In January 1998, the Shipbuilding Industry Review Panel was established to review the industry and the need for the bounty in the context of Australia’s possible accession to the OECD Shipbuilding Agreement. The Agreement aims to eliminate subsidies on shipbuilding among member countries. The major recommendations of the Shipbuilding Industry Review Panel (1998) were as follows:

- Australia should accede to the OECD Shipbuilding Agreement subject to certain conditions.

- The bounty scheme should continue to operate from 1 July 1999 to 31 December 2000 at the rate of 3 per cent.
- A grant for innovation be provided to a maximum of 2 per cent of eligible production costs. The grant, on a dollar for dollar funding basis, would operate for five years from 1 July 1999.

Figure 2.1 **Budgetary outlays, by major programs**
per cent of total





Source: Commission estimates.

Based on projections, programs which provided the most significant direct financial assistance to industry in 1997-98 were the Factor f scheme ($174 million, or 10 per cent of outlays), the Export Market Development Grants (EMDG) scheme ($145 million, 8 per cent) and the Industry Innovation Program ($91 million, 5 per cent) (figure 2.1). The Pharmaceutical Industry Investment Program will replace the Factor f scheme on 1 July 1999 and continue partially to compensate the pharmaceutical industry for low drug prices under the Pharmaceutical Benefits Scheme. Funding of the EMDG scheme has been capped at $150 million since 1997-98. Outlays on the Industry Innovation Program (including the R&D Start program) increased in 1997-98. The program also receives substantial additional funding for future years in the *Investing for Growth* Statement.

Funding to intermediary institutions

Commonwealth budgetary assistance is also provided to industries indirectly through the funding of certain intermediaries that perform activities of benefit to industry. Assisted activities — such as export marketing and promotion services, and research and development — raise producers' returns in similar ways to direct financial assistance.

In nominal terms, funding to intermediary organisations has been relatively stable at around $1 billion since 1993-94. In 1997-98, the major outlays (figure 2.1) were:

- CSIRO's research programs ($327 million, 20 per cent of total outlays);
- rural R&D corporations ($160 million, 10 per cent);
- Cooperative Research Centres (CRCs) ($118 million, 7 per cent);
- Austrade's International Business Services (IBS) ($122 million, 7 per cent); and
- the Australian Tourist Commission (ATC) ($78 million, 5 per cent).

Funding to intermediary organisations accounted for the largest share of outlays in the primary production and mining sectors (75 per cent and 96 per cent, respectively) and is predominantly directed at research and development activities in those sectors. Outlays on the manufacturing sector are mainly in the form of direct financial assistance (67 per cent).

The (Mortimer) Review of Business Programs (1997) recommended substantial cuts to funding of CRCs. In August 1997, the Government established the *Review of Greater Commercialisation and Self-funding in the Cooperative Research Centres Programme* (DIST 1998). The Government has decided to adopt the key recommendation of the Review, that funding of CRCs should continue at the current level until a comprehensive review of the program is conducted in 2001 (Moore

1998a). The Government also announced the revision of CRC program guidelines to improve linkages between science and industry and achieve greater levels of commercialisation. A selection round for new CRCs commenced in 1998.

Tax expenditures

Tax expenditures reached $2.2 billion, or 56 per cent of total budgetary assistance, in 1996-97, the latest year for which information on actual revenue forgone is available (table 2.2). Tax expenditures have been revised for all past years to incorporate estimates now available for the development allowance and infrastructure bonds concessions. In addition, the R&D tax concession has been reclassified into the relevant sectors based on tax deduction statistics published by the Australian Taxation Office. Previously, the total revenue forgone from the R&D tax concession was allocated to the manufacturing sector.

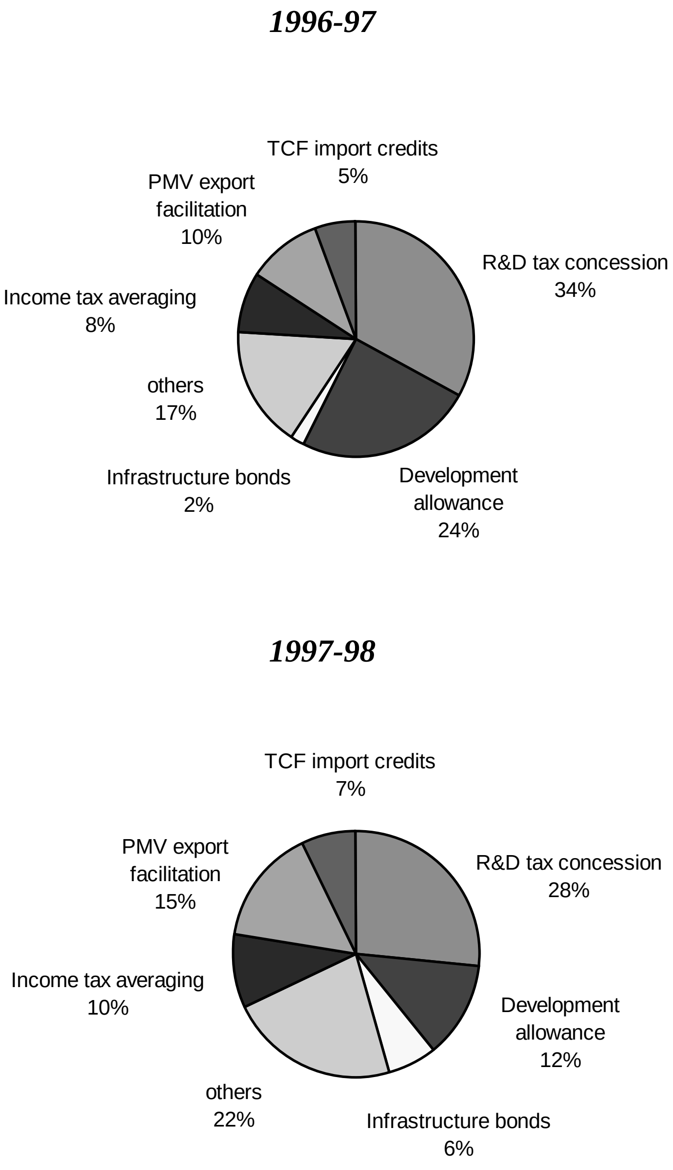
The development allowance and infrastructure bonds were introduced in the 1992 *One Nation* Statement to promote large-scale investment and the private provision of infrastructure. In 1996-97, the development allowance and the infrastructure bonds concession resulted in revenue forgone of $525 million and $40 million, respectively.

Other significant measures in terms of revenue forgone in 1996-97 were: the R&D tax concession ($710 million); the Passenger Motor Vehicle (PMV) Export Facilitation Scheme ($221 million); the Textiles, Clothing and Footwear (TCF) Import Credits Scheme ($118 million); and income tax averaging for primary producers ($180 million) (figure 2.2). The R&D tax concession, in particular, has underpinned growth in total tax expenditures in recent years.

Tax expenditures are projected to fall substantially in 1997-98 due to the tightening of the R&D tax concession and winding down of the development allowance (Treasury 1997b). Revenue forgone under the R&D tax concession is expected to decline from $710 million in 1996-97 to $440 million in 1997-98 and, with respect to the development allowance, from $525 million to $205 million over the same period. In response to concerns about potential abuses of infrastructure bonds, in the 1997-98 Budget the Government replaced the previous scheme with the infrastructure borrowings tax rebate. Capped at $75 million in revenue forgone per year, the tax rebate is available for road and rail projects, as well as infrastructure projects for which applications had been made under the previous scheme.

Figure 2.2 **Tax expenditures, by major measures**

per cent of total



Source: Commission estimates.

The Government has foreshadowed changes to the administration of the R&D tax concession to make the concession more accessible to business. The application period for registration will be increased from four to ten months. The Industrial Research and Development (IR&D) Board will have more flexibility to assess applications according to specific circumstances and consider late applications. To reduce compliance costs for companies undertaking low levels of R&D, different information requirements will be designed to apply to different classes of applicant.

In addition, the Government will retain the current definition of R&D activities and introduce measures to ensure the integrity and efficacy of the R&D tax concession (Costello and Moore 1998b).

Table 2.2 **Commonwealth tax expenditures, 1995-96 to 1998-99**
$ million

	1995-96	*1996-97*	*1997-98*[a]	*1998-99*[a]
PRIMARY PRODUCTION				
Deduction for conserving or conveying water, and conservation measures	30	30	30	30
Deduction of expenditures over four years on acquiring and establishing grape vines	2	3	5	5
Deduction of capital expenditure on establishing horticultural plantations	-	-	1	3
Five year, 10 per cent taxation allowance on drought-prepared assets	2	13	10	9
Income Equalisation Deposits Scheme	9	26	21	-
Farms Management Deposits Scheme	-	-	-	34
Income tax averaging for primary producers	190	180	160	175
Total primary production	**233**	**252**	**227**	**256**
MANUFACTURING				
Brandy excise preferential rate	6	5	5	5
Deduction of relocating expenses for multinational firms establishing regional headquarters in Australia	6	7	2	2
Development allowance[b]	10	242	94	76
Duty drawback	91	97	79	80
Exemption of business funds used for university R&D[b]	<1	<1	<1	<1
General investment allowance of additional 10 per cent deduction on plant and equipment[c]	200	12	-	-
Immediate deduction of expenditure to obtain patent, design or copyright[b]	25	25	30	30
PMV Export Facilitation Scheme	187	221	251	250
Pooled Development Funds	<1	11	12	12
R&D tax concession[b]	284	263	163	137
TCF Import Credits Scheme	149	118	121	120
TEXCO (Tariff Export Concession)	49	57	80	80
TRADEX	-	-	-	15
Total manufacturing	**1 007**	**1 058**	**837**	**807**

Table 2.2 **(continued)**

	1995-96	1996-97	1997-98[a]	1998-99[a]
MINING				
Development allowance[b]	29	147	57	46
Exemption of income from sale, transfer or assignment of rights to mine gold	40	40	38	18
R&D tax concession[b]	95	121	75	63
Total mining	**164**	**308**	**170**	**127**
SERVICES				
Accelerated depreciation of Australian trading ships	18	12	ne	ne
Concessional (10 per cent) tax rate on eligible income from an offshore banking unit	9	13	14	23
Development Allowance[b]	11	137	53	43
Film industry 100 per cent capital deduction	20	22	22	22
Film Licensed Investment Company 100 per cent deduction for investors	-	-	-	na
Infrastructure Bonds	na	40	105	178
Infrastructure Borrowings tax rebate	-	-	38	75
R&D tax concession[b]	297	327	202	170
Total services	**355**	**551**	**434**	**511**
TOTAL	**1 759**	**2 169**	**1 668**	**1 701**

- Nil. **na** not available. **ne** not estimated. **a** Treasury forward projections. **b** Commission estimates based on ATO tax deduction data. **c** Qualifying plant and equipment must be ordered from 9 February 1993 and used before July 1994.

Source: Treasury (1997b), ACS (1998) and ATO (1998).

Legislation has been passed to provide a tax rebate for landcare, as part of the Natural Heritage Trust. Farmers with low taxable income can gain access to the new tax rebate (at 34 cents in the dollar) for landcare expenditures. Those who do not qualify for the rebate are still able to claim for landcare expenditures (immediately or over three years) under the existing deductions.

The *Investing for Growth* Statement provided new incentives to attract foreign investment to Australia through the use of tax concessions. These and other recent tax measures are discussed in section 2.3.

The Government has recently reviewed the effectiveness of the existing suite of tax expenditures, but outcomes of the review have not been released publicly. The review was in response to recommendations of the National Commission of Audit in 1996 for a comprehensive review, and examination of the scope to convert tax concessions to outlay programs. The National Commission of Audit (1996) considered that tax expenditures have not been subjected to the same degree of scrutiny as budget expenditures in the past and may be a source of discriminatory treatment between competing business activities. The Commission said:

> ... tax expenditures are a less transparent, more open-ended, but otherwise equivalent mechanism to public sector expenditures for providing assistance to individuals and business (p. ix).

Budgetary assistance to exports

This section examines Commonwealth budgetary assistance to exports, which is an element of total budgetary assistance. Budgetary measures assisting exports have been consolidated in table 2.3. Chapter 3 discusses other arrangements that assist Australian exports, such as the statutory marketing arrangements.

Commonwealth budgetary assistance to exports has remained relatively stable at $1 billion since 1996-97 (table 2.3). While several export programs (such as the Development Import Finance Facility) were terminated recently (see IC 1997f), assistance under the PMV Export Facilitation Scheme and Tariff Export Concessions has increased. A slight increase in funding for export programs is projected for 1998-99.

The Commission's estimates of budgetary assistance to exports are broader in coverage than estimates of export assistance outlays provided in Commonwealth Budget Papers. The outlays classified as export assistance in the Budget are confined to funding of Austrade's programs and Export Finance and Insurance Corporation (EFIC)'s export credit facilities. In addition to these expenditures, the Commission has classified as export assistance those industry-specific measures which target particular stages of exporting activity, such as export marketing and promotional activities. These include funding to the Australian Tourist Commission, the PMV Export Facilitation Scheme and the TCF Import Credits Scheme. Where the budgetary measures benefit the production of certain goods that are both sold domestically and exported, the share paid on exports is recorded as export assistance.

In response to the recent economic instability in some Asian countries, the Government has provided short-term credit insurance on certain Australian exports to South Korea and Indonesia under the EFIC's National Interest Account. The insurance cover involves actual costs to the Government only if export payments are in default. The original facility of $300 million for exports to South Korea was extended to $500 million. National Interest cover for exports to Indonesia comprised a $500 million guarantee of wheat sales by the Australian Wheat Corporation and a $380 million guarantee of cotton exports. Following a review of EFIC's operations and functions in 1997-98, the Government decided that EFIC is to be retained in public ownership and continue its role of providing export assistance through insurance, guarantee and financing support (Moore 1998b).

Table 2.3 **Commonwealth export assistance, 1995-96 to 1998-99**
$ million

	1995-96	*1996-97*	*1997-98*	*1998-99*
DIRECT EXPORT MEASURES				
Export finance & insurance services				
Development Import Finance Facility	127	12	-	-
EFIC Government Guarantee[a]				
• Commercial account	8	ne	ne	ne
• National Interest Business (NIB)	8	ne	ne	ne
Other assistance from NIB account	ne	ne	ne	ne
Export Finance Facility interest subsidy	<1	-	-	-
Export marketing and promotional services				
Agri-food industry program	3	1	1	-
Asia Business Links	3	-	-	-
Asian Infrastructure initiative	1	-	-	-
Asia Pacific Fellowship program	1	-	1	-
Australia in Asia	3	1	1	-
Australian Horticultural Corporation	1	1	-	-
Australian Tourist Commission	80	77	78	89
Clean Food Export Strategy	2	-	-	-
Export Access program	3	3	3	4
Export Market Development Grants scheme	220	188	145	153
Innovative Agricultural Marketing program	5	-	3	-
International Business Services (Austrade)	144	121	122	130
International Trade Enhancement scheme	-	-	13	-
Primary Industries Marketing Skills program	<1	<1	-	-
Project Marketing Loans Facility	-	-	-	-
AQIS meat export inspection subsidy	7	12	-	-
Rural Enterprise Network program	1	<1	-	-
Wine Industry Export Development Grant	<1	<1	-	-

Table 2.3 **(continued)**

	1995-96	*1996-97*	*1997-98*	*1998-99*
Other direct export measures				
Duty drawback[b]	91	97	79	97
Information Technology Development program	2	-	-	-
PMV Export Facilitation Scheme[b,c]	187	221	251	250
TCF Import Credits Scheme[d]	149	118	121	120
TEXCO (Tariff Export Concessions)[b]	49	57	80	80
TRADEX	-	-	-	15
Sub-total	**1 095**	**909**	**899**	**922**
OTHER MEASURES AFFECTING EXPORTS[e]				
Australian Leather Holdings Package	-	30	13	13
Bounties[f]				
• Computers	29	25	37	18
• Machine tools and robots	3	3	-	-
• Shipbuilding	19	18	18	18
Factor f – pharmaceuticals[f]	48	66	78	72
Private Sector Linkages program	4	3	3	3
Sub-total	**103**	**144**	**133**	**124**
TOTAL EXPORT ASSISTANCE	**1 198**	**1 053**	**1 032**	**1 046**

ne Not estimated. **na** Not available. **-** Nil. **a** Commission estimates. Assistance is assumed to equal the difference between interest payable on EFIC's borrowings at a market interest rate and a government low risk rate of interest. **b** Figures for 1998-99 are Commission estimates. **c** Estimates of revenue forgone are for calendar years, 1995, 1996 and 1997. **d** ACS financial year estimates, representing the actual value of import credits issued, which equals the duty forgone when credits are used. Data for 1998-99 are Commission estimates. **e** Export assistance is also provided under the Commonwealth support arrangement for manufacturing milk — the Dairy Market Support Payments. The arrangement is discussed in chapter 3. **f** Figures for bounty programs and Factor f relate to the export component of the program.

Source: Commonwealth Budget Papers, ACS (1998) and Commission estimates.

The Australian Tourist Commission is to receive additional funding of $41 million over four years for increased promotional activity in the USA, UK and Europe. The Department of Industry, Science and Tourism (DIST) is to receive additional funding of $8 million over four years to develop the tourism potential of rural and regional Australia.

The *Investing for Growth* Statement (discussed below) announced that the Export Market Development Grants scheme will operate for another two years until 2001-02 at the capped funding level of $150 million per year. Funding for the Export Access program will also be extended to 2001-02. A new export program — TradeStart — has been established to improve access to Austrade services for new exporters in rural and regional areas. In addition, the Duty Drawback and Tariff Export Concession schemes — and also the temporary importation provisions of the *Customs Act 1901* — are to be integrated into a single streamlined scheme to be known as TRADEX. TRADEX will provide relief from customs and excise duties, and sales tax on imported goods which are intended for re-export or used as inputs into exports.

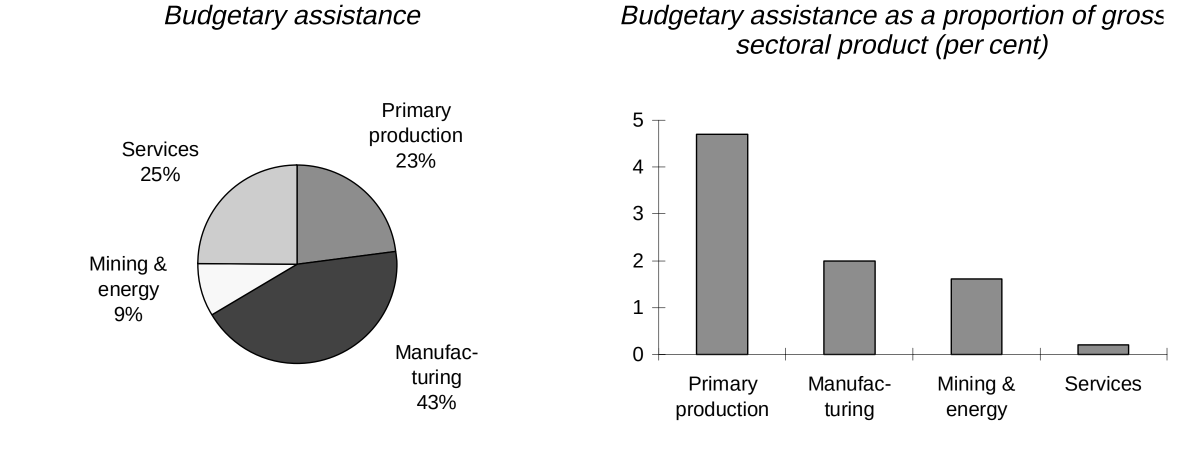
Budgetary assistance by sector

The level and form of budgetary assistance vary markedly between sectors. Manufacturing continued to receive the largest share of budgetary assistance in 1997-98 (43 per cent). Services accounted for nearly 25 per cent, and primary production 23 per cent. Mining received the smallest share (9 per cent) (figure 2.3).

As indicated earlier, the estimation of the sectoral distribution of budgetary assistance this year incorporates the revision of revenue forgone data on the incidence of some tax concessions. This has increased the share of assistance going to services and mining, although manufacturing still receives by far the largest share.

As a proportion of gross sectoral product (GSP), budgetary assistance was highest for primary production in 1997-98 (5 per cent). Assistance represented 2 per cent of GSP for the manufacturing sector, less than 2 per cent for the mining sector, and less than 1 per cent for services.

Figure 2.3 **Budgetary assistance, by sector, 1997-98**



Source: Commission estimates.

Primary production

Budgetary assistance to agriculture, forestry and fisheries fell slightly to $770 million in 1997-98 (tables 2.2 and 2.5). Assistance is provided predominantly by means of outlays (70 per cent). The major outlays are on rural R&D corporations ($160 million), CSIRO research programs on animals and plants ($113 million) and the Rural Adjustment Scheme ($82 million). Changes in assistance arrangements for agriculture, recently announced in the *Agriculture — Advancing Australia* Statement are discussed below.

The major tax expenditure benefiting the sector is income tax averaging. Treasury estimates of the revenue forgone from this concession for earlier years have been revised substantially. For 1996-97 the estimate increased by nearly $50 million to $180 million (table 2.2), accounting for 70 per cent of total tax expenditures for primary production in that year.

Manufacturing

Budgetary assistance to the manufacturing sector declined by 13 per cent to $1.5 billion in 1997-98 (tables 2.2 and 2.6). The decline mainly reflects the reduction in the R&D tax concession. The major programs supporting manufacturing are:

- the R&D tax concession;
- the Factor f scheme;
- the PMV Export Facilitation Scheme; and
- the TCF Import Credits Scheme.

Mining and energy

Budgetary assistance to the mining and energy sector fell by 33 per cent to $290 million in 1997-98 as a result of the reduction in the R&D tax concession and the development allowance (tables 2.2 and 2.7). Budgetary assistance to the sector consists mainly of outlays for CSIRO research into minerals and energy, the R&D tax concession and the development allowance.

Services

Budgetary assistance to the services sector fell by 14 per cent to $840 million in 1997-98 due to the winding down of the development allowance (tables 2.2 and

2.8). The major programs for the services sector include the R&D tax concession (syndication arrangements), development allowance, infrastructure bonds and funding for the Australian Tourist Commission.

2.3 Recent developments

During the past year, the Commonwealth Government has committed to several budgetary assistance initiatives spanning trade, investment and R&D as well as targeting particular industries. The most significant decisions were announced in the *Investing for Growth* Statement and the *Agriculture — Advancing Australia* Statement. Details of the new assistance arrangements (post-2000) for the PMV and TCF industries were also announced.

Investing for Growth

The *Investing for Growth* Statement in December 1997 (Commonwealth of Australia 1997), was a response to the (Mortimer) Review of Business Programs, the Information Industries Taskforce (the Goldsworthy Report) and various industry proposals calling for increased budgetary assistance. The funding commitments amounted to $1.2 billion over the four years to 2001-02, consisting of R&D support, investment incentives, export assistance and specific incentives for the information technology industry (table 2.4).

The funding in *Investing for Growth* does not have a significant impact on assistance levels in 1997-98 and 1998-99. However, the initiatives announced in the Statement will increase total budgetary assistance by more than $200 million in 1999 to 2000, with the impact rising to nearly $500 million in 2001-02. These figures do not include the investment incentives, which have not been costed, but have the potential to provide significant additional assistance.

The composition of budgetary assistance is likely to change as a result of *Investing for Growth*. The industry support measures in the Statement are mainly outlays, rather than tax expenditures. The major outlays — such as the R&D Start program — are in the form of direct financial assistance.

The package of measures in *Investing for Growth* appears to reflect a more proactive approach to industry assistance. Some of the schemes, such as the proposed investment incentives, are characterised by a high degree of discretion and lack the transparency of some of the support measures (such as bounties) that are being phased out. Assistance for R&D also is increasingly taking the form of discretionary grants, assessed on a case-by-case basis, rather than the more generally available R&D tax concession.

Table 2.4 **Investing for Growth Statement**
$ million, constant prices

	1997-98	*1998-99*	*1999-00*	*2000-01*	*2001-02*	*Total over 5 years*
Research and development						
R&D Start	-	43	115	182	216	556
Innovation Investment Fund	-	-	12	15	16	43
Technology diffusion	-	-	17	27	28	72
Investment						
Invest Australia	-	3	3	11	11	28
Investment incentives	na	na	na	na	na	na
Financial services						
Australia as a financial centre[a]	1	14	22	22	22	81
Export and trade						
EMDG	-	-	-	150	150	300
TradeStart and Export Access	-	1	4	4	4	13
APEC Market Integration/ Industrial Collaboration	-	4	4	4	4	18
TRADEX[a]	-	15	30	30	30	105
Information Technology						
Software Engineering Centres	-	7	7	7	7	28
Total budgetary assistance	**1**	**87**	**214**	**452**	**488**	**1 244**
TOTAL FUNDING	**6**	**92**	**217**	**456**	**492**	**1 263**

- Nil. **na** not available. **a** Revenue forgone.

Source: Commonwealth of Australia (1997).

Business R&D

Existing Commonwealth support of business R&D is provided mainly through the broad-based R&D tax concession, and the discretionary and targeted Industry Innovation program. The program, administered by the IR&D Board, includes the R&D Start program and the Innovation Investment Fund. In *Investing for Growth*, the R&D Start program is expanded and receives significant increases in funding (an additional $556 million over the next four years). The Innovation Investment

Fund is also allocated additional funding, with greater emphasis placed on the commercialisation of R&D.

The R&D Start program now has the additional role of attracting foreign investment. *R&D Start* will be used to:

> ... encourage overseas companies to establish R&D facilities in Australia. Where the benefits of R&D are to be retained in Australia, these firms will have access to R&D funding on a competitive basis. This complements the Government's broader strategy to attract foreign investment to Australia. (Commonwealth of Australia 1997, p.33)

Under R&D Start, competitive grants are available through three components. The *core grants* component provides similar benefits to the previous R&D Start program (50 per cent of project cost for companies with average turnover of less than $50 million). The *R&D Start-Plus* component covers large companies and focuses on commercialisation (with grants of up 20 per cent of the project cost). *The R&D Start-Premium* component provides premium assistance over and above the core grants and R&D Start-Plus (up to 72 per cent of project cost), conditional upon the successful commercialisation of technologies. *R&D Start-Premium* will be made available for 'projects deemed to be of exceptional merit and with outstanding prospects for commercialisation' (Commonwealth of Australia 1997, p. 33).

The R&D Start program confers a higher subsidy than that of the 125 per cent R&D tax concession. The core grants give an after-tax benefit of 68 cents in the dollar, equivalent to a 189 per cent tax concession. The after-tax benefit of 54 cents in the dollar under R&D Start Plus is equivalent to a 150 per cent R&D tax concession while R&D Start-Premium provides assistance up to the equivalent of a 200 per cent R&D tax concession (Commonwealth of Australia 1997).

The Innovation Investment Fund was introduced initially as the Small Business Innovation Fund in the 1996-97 Budget. The program provides venture capital funds to small technology firms to assist the commercialisation of R&D. Assistance is through the creation of investment funds (funded on a 2:1 basis with private sector capital) which make equity investments in small companies commercialising technology. *Investing for Growth* allocates another $43 million over four years in addition to the $130 million funding for the program announced in March 1997.

Under the Technology Diffusion program, grants are available to projects that facilitate the uptake of 'new and appropriate technologies'. Eligible recipients include companies, technology centres, universities, cooperative research centres, TAFEs, CSIRO and consortia of these. Grants are made to a maximum of 50 per cent of project cost with a requirement for matching contributions.

Investment incentives

The (Mortimer) Review of Business Programs (1997) recommended the use of large-scale investment incentives to attract foreign investment to Australia. In *Investing for Growth*, the Government has committed to the provision of investment incentives in limited circumstances. The investment incentives — in the form of grants, tax relief or the provision of infrastructure services — are to target major, high technology projects with 'strategic' characteristics. The Office of the Strategic Investment Coordinator has been established to advise the Government on the need for investment incentives and to assess investment projects on a case-by-case basis. In addition to these incentives, investment attraction is to be carried out through the R&D Start program. *Investing for Growth* did not provide any indication of the likely budgetary costs of the proposed incentives.

In June 1998, the Government granted a wholesale sales tax exemption for space vehicles and satellites to be launched in Australia. The exemption is designed to facilitate the development of the commercial space industry in Australia (Costello and Moore 1998a). The Commonwealth has entered into an agreement with Kistler Aerospace Corporation to establish commercial space facilities at Woomera. A Space Licensing and Safety Office has been established for regulation of space activities. No estimates of the revenue forgone from the tax concession have been made public.

In addition, Invest Australia has been established with annual funding of $11 million to promote overseas investment in Australia. Subsuming the Investment Promotion and Facilitation program, Invest Australia undertakes investment promotion activities and provides advice on investment opportunities and proposals. It also undertakes existing Major Projects Facilitation functions and coordinates with State and Territory governments on investment promotion.

Agriculture — Advancing Australia

In October 1997, the Government announced *Agriculture — Advancing Australia* with funding of $500 million over the next four years. The key measures include:

- Rural Adjustment Scheme (RAS) — transitional arrangements ($116 million);
- Farm Business Improvement Program ($50 million);
- Farm Family Restart scheme ($120 million);
- Farm Management Deposits scheme ($60 million);

- Funding for exceptional circumstances, including drought;[2]
- Drought Relief Payment — extended recovery assistance ($41 million); and
- Retiring farmer assistance — access to the age pension ($78 million).

RAS transitional arrangements and Farmbis

Funding for RAS transitional arrangements covers the applications for interest rate subsidies received before 30 September 1997, following the Government's decision to discontinue the interest rate subsidies (Anderson 1997a).

The Farm Business Improvement program (FarmBis) replaces the RAS's education and training components. FarmBis funds projects designed to improve farm business management skills. RAS support for farm management skills and professional advice ended on 1 July 1998 when FarmBis commenced operation.

Farm Family Restart scheme

The Farm Family Restart scheme, commencing in December 1997, provides income support to the farm sector and re-establishment grants to farmers leaving the industry. The income support, payable for a maximum period of one year, is paid at the same rate as the NewStart allowance. Recipients are not required to satisfy an activity test or put the farm on the market, but must obtain professional advice and counselling on future viability of the farm business.

The re-establishment grant (up to $45 000) is available to farmers who sell their land and enter the scheme in the first two years of its operation. Under the new asset test, farmers can have up to $90 000 in assets to qualify for the maximum grant (the previous limit was $45 000).

Farm Management Deposits scheme

The Farm Management Deposits scheme replaces the Income Equalisation Deposits Scheme and Farm Management Bonds. The scheme allows primary producers to make deposits to the scheme when surplus funds are available and withdraw the holdings in less successful years. The fully taxable deposits are subject to a 20 per cent withholding tax when withdrawn, but the withholding tax can be varied in times of financial hardship (due to climatic events or market downturn).

[2] Estimates of outlays are not available.

Administration of the scheme has been transferred from the Department of Primary Industries and Energy to financial institutions.

Exceptional circumstances and Drought Relief Payment

The new Exceptional Circumstances Relief Payment (ECRP) replaces the current Drought Relief Payment. Income support equivalent to the NewStart Allowance is available to eligible farmers in declared exceptional circumstances (rare and severe events, including but not restricted to, extreme drought). Eligibility will be subject to an income test and off-farm asset test. The duration of the payment is to be assessed on a case-by-case basis.

Agriculture — Advancing Australia also allocates $41 million in funding to extend the recovery period for Drought Relief Payments.

Retirement Assistance for Farmer Scheme

Under previous arrangements, gifting of assets of more than $10 000 a year disqualifies aged people from receiving a pension or allowance or reduces their entitlements for a period of five years. The new scheme gives aged farmers a three year moratorium in which their assets can be transferred to the younger generation without loss of entitlement to social security payments. The moratorium is also open to farmers who have transferred their assets in the five years preceding September 1997. To be eligible, farmers must have owned the property for at least 15 years (or have been involved in farming for 20 years) and have an average income less than the age pension.

Automotive Competitiveness and Investment Scheme

The Industry Commission reported last year (IC 1997f) on the Government's announcement of post-2000 assistance arrangements for the passenger motor vehicle (PMV) industry. The Government indicated that a replacement for the Export Facilitation Scheme (EFS) would be introduced after 2000, but details were not available at that time.

Recently the Government announced that the Automotive Competitiveness and Investment Scheme (ACIS) will replace the EFS and operate for five years from 1 January 2001 (Fisher and Moore 1998). The Customs Legislation (Automotive Competitiveness and Investment Scheme) Bill 1998 provides for the creation of the ACIS and the implementation of the announced decisions to maintain PMV tariffs at 15 per cent until 2004 and to reduce them to 10 per cent from 2005.

The ACIS will provide assistance through two sub-schemes, covering passenger motor vehicle producers (the PMVP sub-scheme), and component manufacturers and service providers (the CMSP sub-scheme). Under the ACIS, eligible firms can use transferable credits to reduce the customs duty payable on eligible imports. Reflecting some provisions of the World Trade Organization, the scheme limits the benefits to 5 per cent of sales for an individual firm in any year.

The duty credits available under the PMVP sub-scheme will be calculated on the basis of a broadened duty free allowance and investment allowance. The existing duty free allowance entitles PMV producers to duty free imports of vehicles up to 15 per cent of their value of production in Australian and New Zealand markets. The PMVP sub-scheme provides for an increase in the duty free entitlement to 25 per cent, and the value of production is expanded to cover all markets (including export markets) and includes engines and certain engine parts in addition to PMVs. In addition, import duty credits are available for up to 10 per cent of investment in productive assets. PMV producers are also able to earn credits for R&D investment on behalf of third parties.

The CMSP sub-scheme will provide duty credits at 25 per cent of investment in productive assets and 45 per cent of investment in R&D.

Total import duty forgone for the ACIS is capped at $2 billion over five years from 2001. This estimate excludes the uncapped entitlements under the existing 15 per cent duty free allowance which is projected to cost around $170 million per year.

Textiles, clothing and footwear industries

Last year the Government announced a new package of assistance measures for the TCF industry to operate from 2000 (Howard and Moore 1997). The announcement provided an outline of the key measures, but funding details were not announced until July this year (Moore 1998d).

The package, estimated to cost $772 million, has five major components:

- TCF Strategic Investment Program, including a Regional Adjustment Package;
- TCF Technology Development Fund;
- National Framework for Excellence in TCF Training;
- TCF Market Development Program; and
- Expanded Overseas Assembly Provisions Scheme.

The TCF Strategic Investment Program (SIP) is the most significant component of the package. The program is allocated a capped funding of $700 million for the period 2000 to 2005. Eligible activities are investment in new plant and equipment, research and development and product development. Cash payments will be available for up to 20 per cent of investment expenditures, up to 45 per cent of R&D activities, and up to 5 per cent of value added. Total benefits under the scheme are subject to a limit of 5 per cent of sales of eligible products in the previous year.

As part of the SIP, the Regional Adjustment Package will provide structural adjustment assistance to regions. Payments will be made to assist the purchase of ‘state of the art’ second hand plant and equipment where existing firms have consolidated or merged. Firms will need to demonstrate improvements in business efficiency or outputs, commitment to training of affected staff and other economic benefits.

Other developments

Renewable energy

In November 1997, the Government announced several funding initiatives to address climate change and reduce greenhouse gas emissions (Hill et al. 1997). Costing a total of $180 million over five years, the package includes the establishment of a Renewable Energy Innovation Investment Fund, provision of concessional loans and grants to strategic renewable energy projects, and creation of a Renewable Energy Technology site and a ‘show case’ fund. The Renewable Energy Innovation Investment Fund facilitates equity investment for the commercialisation of renewable energy technology.

Film industry

In November 1997, the Government announced its response to the recommendations of the *Review of Commonwealth Assistance to the Film Industry* (Gonski 1997). The response includes:

- retention of Film Australia in Commonwealth ownership;
- extension of Film Australia’s National Interest program until 2003, with annual funding of $4.6 million for the production of documentaries;
- retention of current tax concessions for investment in Australian film and television production (Divisions 10B and 10BA of the *Income Tax Assessment Act 1936*); and

- introduction of a 100 per cent tax concession for investors in companies licensed to invest in film and television production — the Film Licensed Investment Scheme. The new scheme will operate as a pilot scheme for two years from 1998-99 with total revenue forgone of up to $20 million (Alston 1997).

Pork industry

In December 1997, the Government announced the National Pork Industry Development Program with funding of $10 million to improve the competitiveness of the pork industry (Anderson 1997b). In June 1998, the Government announced additional funding of $8 million for the new Pigmeat Processing Grants Program. These programs aim to assist the industry to meet import competition and develop new export opportunities (Anderson and Fisher 1998a).

Table 2.5 **Commonwealth budgetary outlays on primary production, 1995-96 to 1998-99**

$ million

	1995-96	*1996-97*	*1997-98*	*1998-99*[a]
DIRECT FINANCIAL ASSISTANCE				
Industry-specific programs				
Citrus industry market diversification subsidy	2	2	2	2
Forest Industry structural adjustment Package	4	5	9	39
Wine industry loan conversion	-	2	-	-
Sub-total	**7**	**9**	**11**	**41**
Sector-specific programs				
Drought Relief Payments Scheme	-	-	-	-
Farm Family Restart Program	-	-	21	40
Farm Household Support Scheme	1	1	1	-
Rural Adjustment Scheme	115	106	82	42
Sub-total	**116**	**106**	**103**	**81**
General programs				
Austrade				
• Export Market Development Grants scheme	6	5	4	4
• Innovative Agricultural Marketing Program	5	-	3	-
Commonwealth Development Bank subsidy	10	-	-	-
EFIC —- National Interest Business[b]	17	21	15	17
Tasmanian Freight Equalisation Scheme	3	3	3	3
Sub-total	**41**	**29**	**24**	**24**
Total direct financial assistance	**163**	**144**	**138**	**146**
FUNDING TO INTERMEDIARY ORGANISATIONS				
Industry-specific programs				
Crops				
Australian Horticultural Corporation	1	1	-	-
Australian Plague Locust Commission	1	<1	1	1
Sugar Industry Program	2	4	3	4
Tri-State fruit fly strategy	<1	<1	<1	<1
Livestock, poultry etc				
AQIS meat inspection subsidy	7	12	-	-
Australian Animal Health Laboratory	6	6	6	6
Bovine brucellosis and tuberculosis eradication campaign	3	2	2	-
Exotic disease preparedness programs	2	1	2	1

Table 2.5 **(continued)**

	1995-96	1996-97	1997-98	1998-99[a]
Pork Industry Development Group Grant	-	-	2	4
Forestry				
Commonwealth-NSW Forest Industry Package	2	1	1	3
Commonwealth-Tasmanian Forest Industry Package	9	-	-	-
National Forest Policy Program	3	7	7	6
NSW Southeast Forests Package	2	1	4	-
Plantation initiatives				
• National Forest Policy Program	<1	4	4	3
• North Queensland Community Rainforests Revegetation Program	1	1	-	-
Sub-total	**40**	**42**	**31**	**30**
Research & development[c]				
Cooperative Research Centres	24	36	35	34
CSIRO Institute of Animal Production and Processing	64	d	d	d
CSIRO Institute of Plant Production and Processing	85	d	d	d
CSIRO plant and animal research	-	101	113	118
Fisheries research and development	13	15	11	10
Fisheries resources research	2	2	2	2
Grains (wheat and other[e])	21	29	34	34
Horticulture	11	12	16	17
Land and Water Resources R&D Corporation	11	10	11	11
Other rural research[f]	28	27	35	35
Meat research	23	21	26	25
Rural Industries R&D Corporation	11	6	11	11
Wool	12	10	13	14
Sub-total	**304**	**268**	**308**	**311**
Sector-specific programs				
Agribusiness programs[g]	7	1	-	1
Clean food export strategy	2	-	-	-
Clean Food Production Program	2	-	1	1
Farm Business & Community Programs	-	-	6	22
National Landcare Program	83	66	54	55
Rural Communities Access Program[h]	12	9	5	-
Sub-total	**107**	**76**	**65**	**78**

Table 2.5 **(continued)**

	1995-96	*1996-97*	*1997-98*	*1998-99*[a]
General programs				
Austrade – export promotion operating expenses	4	3	3	3
Total funding to intermediary organisations	**454**	**389**	**406**	**421**
TOTAL OUTLAYS ON PRIMARY PRODUCTION	**618**	**533**	**544**	**567**

- Nil. Figures may not add to total due to rounding. **a** 1998-99 data are Budget appropriations. **b** The estimates reported in this section are net National Interest Business outlays. These payments are insurance pay-outs. Because any difference between the National Interest Business scheme's borrowing and lending rates is underwritten by the Commonwealth, the scheme may provide assistance to agricultural exporters. However, net National Interest Business outlays provide only a weak indication of any assistance provided. **c** Estimates are derived in part from the Science and Technology Budget Statement 1998-99. **d** CSIRO Research Institutes were restructured in 1995-96. Outlays are now apportioned by research purpose. **e** Other includes barley, grain legumes and oilseeds. **f** Other industries, including dairy, chicken meat, pig meat, eggs, cotton, dried vine fruits, grapes and wine, honey, sugar and tobacco. **g** The Agribusiness programs were formed in 1994 to manage five existing programs. These were the Primary Industries Marketing Skills Program, the Rural Development Incentive Scheme, the Rural Enterprise Network Program, the Rural Industries Business Extension Service, and the World Best Practice Incentive Scheme. **h** The Rural Communities Access Program, introduced in 1994-95, combined several existing programs.

Source: Commonwealth Budget and Budget related papers (various years), departmental annual reports (various years) and Commission estimates.

Table 2.6 **Commonwealth budgetary outlays on the manufacturing sector, 1995-96 to 1998-99**

$ million

	1995-96	*1996-97*	*1997-98*	*1998-99*[a]
DIRECT FINANCIAL ASSISTANCE				
Industry-specific programs				
Bounties				
Bed sheeting	<1	-	-	-
Books	22	13	7	1
Computers	64	54	49	40
Ethanol	2	<1	-	-
Machine tools and robots	7	6	4	2
Printed fabrics	<1	-	-	-
Ships	24	23	19	22
Textile yarns	6	-	-	-
Sub-total	*125*	*96*	*79*	*65*
Other industry-specific programs				
Australian Leather Holdings package[b]	-	30	13	13
Equity in the Australian Technology Group	-	-	-	-
Information Technology Development Program	2	-	-	-
Pharmaceutical industry Factor f program	106	146	174	159
Tasmanian wheat freight subsidy	2	1	1	1
TCF programs[c]				
• TCF Industries Development Strategy	<1	-	-	-
• TCF 2000 Strategy	-	3	6	4
Wine Industry Package				
• Grants to wine makers	2	-	-	-
• Export development grant	<1	<1	-	-
Sub-total	*114*	*181*	*194*	*177*
Sub-total	**238**	**277**	**273**	**243**
General programs				
Austrade				
• Asia Business Links	3	-	1	-
• Asia Pacific Fellowship	1	-	1	-
• Export Market Development Grants scheme	88	75	58	61
• International Trade Enhancement Scheme	-	1	13	-
Commonwealth Development Bank subsidy	6	-	-	-
Development Import Finance Facility	109	12	-	-
Interest subsidy for financing eligible export transactions (EFIC)	<1	-	-	-

Table 2.6 **(continued)**

	1995-96	*1996-97*	*1997-98*	*1998-99*[a]
IR&D Board programs				
• Industry Innovation Program grants[d]	52	-	-	-
• Industry Innovation (incl R&D Starts)	-	56	91	128
• Innovation Investment Fund	-	-	-	14
Technology Support Centres	12	7	19	-
Technology Diffusion Program	-	-	-	18
Tasmanian Freight Equalisation Scheme	36	35	30	30
Sub-total	**215**	**110**	**140**	**195**
Total direct financial assistance	**453**	**387**	**413**	**437**
FUNDING TO INTERMEDIARY ORGANISATIONS				
Industry-specific programs				
Agri-Food Industry Program	3	1	1	-
National Space Program	3	3	<1	-
Sub-total	**5**	**4**	**2**	**-**
General programs				
Austrade				
• Export Access Program	3	3	3	4
• Export promotion operating expenses	56	48	49	52
Australian Made Campaign	2	<1	-	-
Best Practice Demonstration Program	2	<1	-	-
Cooperative Research Centres	34	40	42	41
CSIRO Institute of Industrial Technologies	67	e	e	e
CSIRO manufacturing research[e]	-	98	81	83
Enterprise Development Program[f]	29	22	11	11
Enterprise Networking Program	6	7	4	4
Greenhouse Response Strategy	<1	1	2	2
Investment Promotion and Facilitation Program	8	<1	<1	<1
Private Sector Linkages Program	4	3	3	3
Support for Australian suppliers	2	-	-	-
Sub-total	**214**	**224**	**199**	**198**
Total funding to intermediary organisations	**220**	**228**	**200**	**198**
TOTAL OUTLAYS ON MANUFACTURING	**673**	**614**	**614**	**635**

- Nil. Figures may not add to total due to rounding. **a** 1998-99 data are Budget appropriations. **b** The 1996-97 figure includes a grant of $5 million and a loan of $25 million. **c** Some individual programs involve funding for services. **d** Disaggregated information on the schemes included under the Industry Innovation Program is not available. In the *Working Nation* statement, the programs were merged into a single program for which multiple criteria apply. Funding for the R&D Start Program is included here. **e** CSIRO Research Institutes were restructured in 1995-96. Outlays are now apportioned by research purpose. **f** The National Industry Extension Service forms part of the Enterprise Development Program.

Source: Commonwealth Budget and Budget related papers (various years), departmental annual reports (various years) and Commission estimates.

Table 2.7 Commonwealth budgetary outlays on the mining and energy sector, 1995-96 to 1998-99

$ million

	1995-96	*1996-97*	*1997-98*	*1998-99*[a]
DIRECT FINANCIAL ASSISTANCE				
Industry-specific programs				
National Electricity Market Management and Code Administrator Companies – establishment subsidy	-	<1	-	-
National Electricity Market Systems Development Project	<1	3	-	-
Rehabilitation of former uranium mine sites	<1	<1	<1	<1
General programs				
Export Market Development Grants scheme	6	5	4	4
Tasmanian Freight Equalisation scheme	1	1	1	1
Total direct financial assistance	**8**	**9**	**5**	**5**
FUNDING TO INTERMEDIARY ORGANISATIONS				
Austrade – export promotion operating expenses	4	3	3	3
Coal Australia Promotion Program	1	-	-	-
Cooperative Research Centres	16	23	22	23
CSIRO Institute of Minerals, Energy and Construction	68	b	b	b
CSIRO minerals and energy research[b]	-	73	64	68
Energy R&D Corporation	12	7	21	2
Energy sector initiatives	1	-	-	-
National Energy Efficiency Program[c]	4	4	2	4
Office of the Supervising Scientist of the Alligator Rivers Region Research Institute	5	4	4	4
Renewable energy grants	-	-	-	4
Total funding to intermediary organisations	**111**	**113**	**115**	**103**
TOTAL OUTLAYS ON MINING AND ENERGY	**119**	**123**	**120**	**108**

- Nil. Figures may not add to total due to rounding. **a** 1998-99 estimates are Budget appropriations. **b** CSIRO Research Institutes were restructured in 1995-96. Outlays are now apportioned by research purpose. **c** Previously the Energy Management Program.

Source: Commonwealth Budget and Budget related papers (various years), departmental annual reports (various years) and Commission estimates.

Table 2.8 **Commonwealth budgetary outlays on selected services industries, 1995-96 to 1998-99**

$ million

	1995-96	*1996-97*	*1997-98*	*1998-99*[a]
DIRECT FINANCIAL ASSISTANCE				
Industry-specific programs				
Asian Infrastructure Initiative	1	-	-	-
Australian Film Commission[b]	21	28	30	16
Australian Film Finance Corporation & Film Australia[b]	57	55	48	48
Bass Strait passenger subsidy	<1	<1	<1	<1
Capital Grants Scheme for purchase of trading ships (contingent on lower crewing levels)	31	9	4	-
Commercial television production fund	20	8	-	-
Development Import Finance Facility	18	3	-	-
Film industry multimedia development subsidy	2	-	-	-
Pharmacy Restructuring grants	7	5	8	12
Remote air services subsidy	1	1	1	-
Remote commercial television subsidy	1	1	1	-
General programs				
Export Market Development Grants scheme	121	103	80	84
Commonwealth Development Bank subsidy	6	-	-	-
Tasmanian Freight Equalisation Scheme	2	2	2	2
Total direct financial assistance	**288**	**216**	**173**	**163**
FUNDING TO INTERMEDIARY ORGANISATIONS				
Ausmusic	1	-	-	-
Austrade – export promotion operating expenses	77	66	60	71
Australia in Asia	3	1	1	1
Australian Tourist Commission	80	77	78	89
Cooperative Research Centres	17	17	18	19
CSIRO Institute of Information Science and Engineering	38	c	c	c
CSIRO services industry research[c]	-	43	69	70
Multi-Function Polis	3	-	-	
Tourism and Expo programs[d]	13	7	7	2
Total funding to intermediary organisations	**232**	**212**	**234**	**253**
TOTAL OUTLAYS ON SERVICES	**520**	**428**	**407**	**416**

- Nil. Figures may not add to total due to rounding. **a** 1998-99 data are Budget appropriations. **b** Assistance through provision of services is also provided. **c** CSIRO Research Institutes were restructured in 1995-96. Outlays are now apportioned by research purpose. **d** Outlays include funding for the National Tourism Development Plan and the Bureau of Tourism Research.

Source: Commonwealth Budget and Budget related papers (various years), departmental annual reports (various years) and Commission estimates.

3 Assistance to agriculture and manufacturing

The effective rate of assistance for agriculture remained at 10 per cent in 1996-97. Increases in assistance to the dairy and wheat industries were offset by decreases for wool, wine grapes, dried vine fruits, eggs and tobacco. Disparities in assistance increased marginally. Dairy remains one of the most highly assisted agricultural activities, receiving nearly 6 times the average level of effective assistance for the agricultural sector.

While not strictly comparable with the agricultural estimates, the effective rate of assistance for the manufacturing sector was estimated at 6 per cent in 1996-97. It is projected to fall to 5 per cent by 2000-01, given further scheduled tariff cuts for the passenger motor vehicle (PMV) and textiles, clothing and footwear (TCF) industries. The dispersion in rates of assistance across manufacturing industries is declining. However, PMV and TCF industries are (and in 2000-01 will continue to be) receiving rates of assistance several times higher than all other manufacturing industries.

This chapter reports on developments in agricultural assistance (section 3.2) and in manufacturing assistance (section 3.3). Estimates of the Commission's nominal and effective rates of assistance are provided for these sectors. A brief explanation of the assistance measures and methodology used is presented in section 3.1. While these estimates cover the major Commonwealth interventions, they do not include all budgetary assistance, especially for the manufacturing sector (see chapter 2).

3.1 Measuring assistance

The Commission uses several measures to summarise the level or rate of assistance to industries in the agricultural and manufacturing sectors. The measures used reflect different aspects of the assistance provided and allow diverse forms of assistance to be aggregated under simplifying assumptions. The main measures used by the Commission are defined in box 3.1.

The Commission has a statutory obligation to take an economy-wide perspective when assessing the implications of particular policies or programs, and it is therefore often interested in the impact of assistance on the allocation of resources between different activities and industries. The effective rate of assistance (ERA), by summarising the impact of various measures on the net returns to value-adding factors, provides a basis for assessing the extent to which assistance may alter the incentives to undertake particular economic activities.

Box 3.1 **Assistance measures**

The **nominal rate of assistance on outputs** is the percentage change in gross returns per unit of output relative to the (hypothetical) situation of no assistance. The nominal rate measures the extent to which consumers pay higher prices and taxpayers pay subsidies to support local output.

The **nominal rate of assistance on materials (intermediate inputs)** is the percentage change in the prices paid for materials used in the production process, due to government assistance.

The **effective rate of assistance** is the percentage change in returns per unit of output to an activity's value-adding factors due to the assistance structure. It measures net assistance, by taking into account not only output assistance and direct assistance to value-adding factors, but also the costs and benefits of government intervention on inputs.

The **gross subsidy equivalent** is an estimate of the change in producers' gross returns from assistance. It is the notional amount of money, or subsidy, necessary to provide an activity with a level of assistance equivalent to the nominal rate of assistance on its output.

The **net subsidy equivalent** is an estimate of the change in returns to an activity's value added due to assistance. It is the notional amount of money, or subsidy, necessary to provide a level of assistance equivalent to the effective rate of assistance. It is equal to the gross subsidy equivalent plus any assistance to inputs or value-adding factors, minus the tax equivalent of protection on intermediate inputs used in the production process.

The **tax on materials** is an estimate of the net change to user industries' input costs due to government assistance altering the prices paid for intermediate inputs.

The **consumer tax equivalent** is the transfer from consumers paying higher prices due to assistance. It is the sum of the gross subsidy equivalent of assistance, which raises the price of goods consumed during the period, and the tariff revenue on imports, adjusted to exclude those goods which are consumed by other industries as intermediate inputs.

Nominal rates of assistance are useful indicators of the effects of assistance on incentives to produce or consume certain commodities. In contrast to effective rates, however, they do not take account of the net impact of assistance afforded to various inputs and outputs. They simply measure the rate of assistance to particular inputs or outputs.

Estimates of gross and net subsidy equivalents, the tax on materials and the consumer tax equivalent measure the income transfers to producers from final consumers, intermediate users and taxpayers (box 3.1). While these income transfers indicate gains and losses to particular groups, they are not measures of the net economic costs to the community of assistance. Such costs depend on the extent to which the provision of assistance distorts consumption and production, and are usually estimated using economy-wide models (IC 1997f).

The emphasis in the Commission's estimates has been on assistance provided by the Commonwealth and on consistency of treatment between activities within each sector. Excluded from the estimates are measures which apply generally to activities in all sectors or which apply to all activities within a particular sector. In general, the Commission restricts coverage of forms of assistance for its annual sectoral estimates to those which can be reliably quantified on a continuing basis (IC 1995b).

The main interventions included in the Commission's estimates are tariffs, production bounties, certain export incentives, discriminatory domestic pricing and marketing support arrangements for agricultural commodities, input subsidies, tariff concessions and duty drawback. A number of other measures (for example, anti-dumping procedures, government procurement and offsets, and partnerships for development programs) are excluded due to data limitations or because they are particularly difficult to quantify.

Assistance which may arise from Commonwealth or State government provision of infrastructure is not included. This is due to the difficulty of quantifying the level of assistance involved in activities where there is no clear alternative benchmark price. Assistance afforded by State and local governments through budgetary outlays and tax expenditures is also excluded. However, State government interventions that have an impact on the prices of agricultural commodities nationally — for example, statutory marketing arrangements for sugar and rice — have been included in the estimates.

Caution must be exercised when making comparisons of assistance estimates between agriculture and manufacturing. Variations in the estimates may reflect different data sources and the scope of interventions included in the estimates, rather than real differences in the incentives to use resources in different activities. These and other points to consider when comparing sectoral levels of assistance are discussed in IC (1995b).

3.2 Agricultural assistance

The agricultural sector receives assistance from a wide range of government programs and policies. Statutory marketing and regulatory arrangements provide the major component of assistance to agriculture, with budgetary assistance (including research and development, adjustment assistance and tax concessions) and tariffs on outputs being less important. Partly offsetting the assistance from these measures are tariffs and other taxes on the inputs used in agriculture.

The estimates of assistance to agriculture are updated to 1996-97, the latest period for which complete data are available. Revised estimates for 1995-96 are also presented, along with estimates for the years 1992-93 to 1994-95. Nominal and effective rates of assistance to agriculture are reported by agricultural activity in table 3.1 and at the 3-digit ANZSIC level in table 3.2. Assistance to agriculture by form, the gross subsidy equivalent (GSE) and the net subsidy equivalent (NSE) are presented in table 3.3.

Trends in agricultural assistance

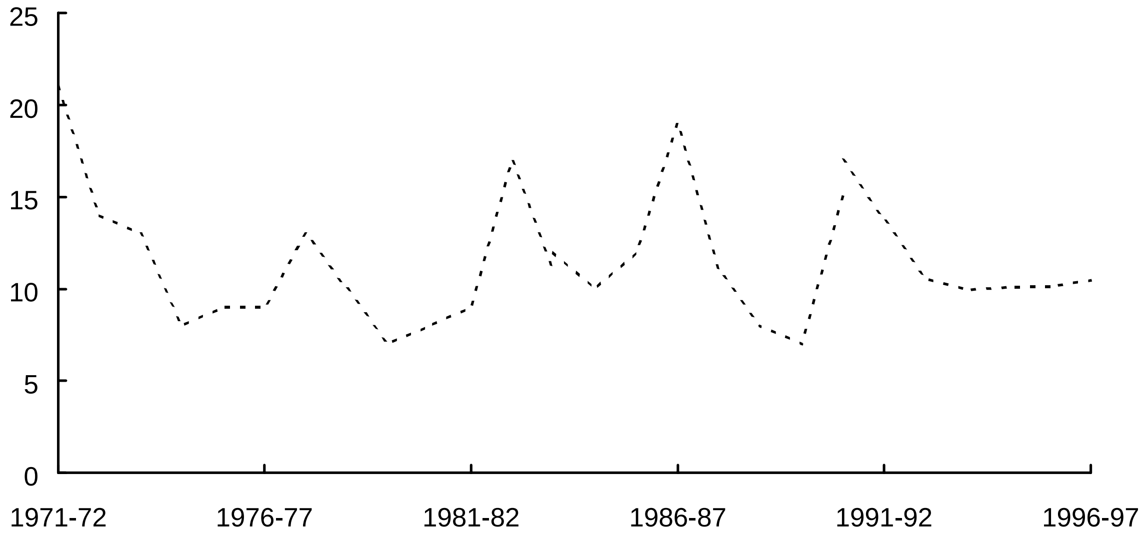
While the assistance afforded by various agricultural arrangements has declined over the past decade, estimated assistance has not fallen consistently across commodities. Assistance to agriculture is inherently more variable than assistance to manufacturing, with changes in estimated assistance reflecting not only changes in assistance policies, but also fluctuations in world commodity prices and the value of output, and the counter-cyclical nature of many agricultural assistance programs. Average effective rates of assistance to agriculture over the last 25 years are presented in figure 3.1.

In 1996-97, the average nominal rate of assistance to agriculture remained largely unchanged at 3 per cent (table 3.1). Nominal rates of assistance fell for wool, wine grapes, dried vine fruits, eggs and tobacco (figure 3.2). Offsetting these falls were increases for wheat, rice and the already highly assisted dairy industry.

The average effective rate of assistance for agriculture also remained largely unchanged in 1996-97 at 10 per cent (table 3.1). Increases in assistance to outputs and lower taxes on inputs were largely offset by decreases in assistance to value-adding factors. In dollar terms, the effective rate of assistance in 1996-97 represents a net subsidy to agriculture of $997 million (table 3.3).

Effective rates of assistance fell for wool, wine grapes, dried vine fruits, poultry, eggs, cotton and tobacco (figure 3.3). The most significant increase in effective rates of assistance was for fresh milk, already in receipt of effective assistance of more than 200 per cent. Smaller increases in effective rates were recorded for apples and pears, deciduous canning fruits, vegetables and most grains (table 3.1).

Figure 3.1 **Average effective rates of assistance, 1971-72 to 1996-97**
per cent



Source: Commission estimates.

For many of the highly assisted agricultural commodities, previously implemented government reforms, designed to promote competition and reduce assistance, began to take effect in 1996-97. Falls in assistance for wine grapes and dried vine fruits in 1996-97 reflected a decline in tariff levels from 8 to 5 per cent for these commodities. Assistance to the sugar industry has been reduced through the removal of the tariff on sugar imports and reforms to domestic marketing arrangements (see below). The Commonwealth Government has committed to reducing assistance to the manufacturing milk sector over the next few years. Reforms have already been carried out in the market milk sector, but in most States these reforms have occurred only downstream from the farm gate. As part of the Competition Principles Agreement, however, most States have either concluded, or made commitments to review marketing arrangements at the farm gate level over the next few years (see below).

Overall, the assistance provided to the dairy industry dominates the estimates for the agricultural sector. When the dairy industry is excluded, the 1996-97 effective rate of assistance for agriculture falls from 10 per cent to 6 per cent.

Disparities in effective rates of assistance among agricultural activities are an important indicator of the potential for inefficiencies in resource use, while disparities in nominal rates provide an indication of the potential for distortions in production or consumption patterns. The Commission measures disparities in assistance using the standard deviation around the sectoral average effective and nominal rates. In 1996-97, the standard deviation of the effective rate of assistance increased to 42 percentage points, from 35 percentage points in 1995-96. The standard deviation in the nominal rate of assistance increased from 9 to 10 percentage points in 1996-97.

Developments in sectoral and commodity assistance

There were relatively few significant changes at the sectoral level in 1996-97. However, recent Government funding announcements, such as the $500 million of commitments contained in the *Agriculture — Advancing Australia* Statement and the outcomes of various reviews at the sectoral and commodity level are likely to have implications for future assistance. Major sectoral and selected commodity developments are discussed below.

Sectoral Assistance

Although remaining a major component of sectoral assistance for agriculture, adjustment assistance fell by $10 million to $105 million in 1996-97 (table 3.3). The beef, wool and wheat industries continue to be the main recipients of adjustment assistance. New South Wales and Queensland together received around 80 per cent of Commonwealth adjustment assistance in 1996-97.

The rural adjustment scheme (RAS) forms the major component of adjustment assistance, accounting for over 90 per cent of total funding in 1996-97. In October 1997, the Government announced, as part of its *Agriculture — Advancing Australia* Statement, the discontinuation of the RAS with some of its components to be transferred to other programs. The Statement also included funding for the family restart scheme, farm management deposits scheme, exceptional circumstances (including drought), drought relief payment and retiring farmer assistance (see chapter 2).

Income tax concessions to primary producers and research and development funding continued to represent major components of sectoral support in 1996-97. Revenue forgone from income tax concessions declined in 1996-97 to $151 million from $163 million in 1995-96. The wheat, beef and dairy industries were the largest recipients of this assistance, together receiving around $69 million (45 per cent) in 1996-97. Research and development funding increased by around $7 million to $161 million in 1996-97. The beef, wool and wheat industries together received around $82 million (51 per cent) of total research and development funding for the sector in 1996-97.

Government expenditure on export inspection services is another important component of agricultural assistance at the sectoral level. The Australian Quarantine and Inspection Service (AQIS) is responsible for carrying out export inspection. AQIS is able to recover the costs of export inspection by charging for its services. For certain programs, however, revenues collected for services fell short of charges — under-recovery — while over-recovery occurred for some other programs. Where over-recovery occurs, AQIS is required to rebate the amounts to exporters, while in cases of under-recovery no adjustment is made. Shortfalls are treated as assistance by the Commission. In 1996-97, shortfalls increased significantly to $9 million but were confined to the meat industry.

Previously announced changes to meat inspection charges took effect in 1997-98. Other reforms to the meat industry, including the establishment of Meat and Livestock Australia, were implemented on 1 July 1998 (Anderson 1998b). The Commission recently released a report into working arrangements in the meat processing sector (PC 1998b).

In addition to inspection services, AQIS is also responsible for providing quarantine services in Australia. The purpose of Australian quarantine is to control the entry into Australia of disease, but quarantine requirements may also have the effect of reducing import competition and assisting local producers (see chapter 4).

Dairy

The dairy industry continues to receive assistance levels many times the average for the agricultural sector. The nominal rate of assistance to the dairy industry increased marginally in 1996-97 to 19 per cent, while the effective rate of assistance increased from 53 per cent in 1995-96 to 58 per cent in 1996-97.

Different assistance arrangements apply to market milk (fresh or drinking milk) and manufacturing milk (used to produce dairy products such as cheese, butter and milk powders). Assistance to market milk is derived largely from State governments setting farm gate prices and rationing production through quotas, while assistance to manufacturing milk is derived largely from Commonwealth marketing arrangements. Typically, assistance to market milk has been much higher than that for manufacturing milk.

A more detailed discussion of the Commission's approach to measuring assistance to market and manufacturing milk is set out in the submission to the NSW Dairy Industry Review (IC 1997a).

Market Milk

The estimated nominal rate of assistance for market milk production increased from 54 per cent in 1995-96 to 60 per cent in 1996-97, while the effective rate of assistance, already over 200 per cent, increased further in 1996-97.

Marketing arrangements for market milk, from farm gate to final consumption, are administered by State statutory marketing authorities. Under the Competition Principles Agreement, all States were required to review government regulation affecting competition. New South Wales has now joined Victoria, South Australia, Western Australia and Tasmania in abolishing most controls on marketing and pricing of milk beyond the farm gate. Post-farm gate deregulation in Queensland is scheduled to take effect from 1 January 1999. Because of the point at which assistance is measured, reforms to post-farm gate milk controls will not have a direct impact upon assistance estimates for the dairy industry.[1]

In all States, farm gate prices and market milk production levels remain under the control of milk marketing authorities, however, most States have either concluded, or made commitments to review price and production controls at the farm gate level. Victoria, shortly to commence its review, is the most significant dairy producing region in Australia. Any decisions adopted in Victoria are likely to have a significant influence on decisions on future marketing arrangements at the farm gate level in other States.

Manufacturing Milk

The estimated nominal rate of assistance for manufacturing milk was 8 per cent in 1996-97, up from 7 per cent in the previous year. The effective rate of assistance increased from 20 per cent to 21 per cent.

In 1996-97, manufacturing milk received most of its assistance from Commonwealth marketing arrangements — the Domestic Market Support Scheme. The scheme includes a levy applied to all milk (market and manufacturing milk) produced in Australia. Producers receive a full rebate of the levy on manufacturing

[1] The measurement of assistance involves choosing an appropriate point in the production chain at which to measure assistance. For agriculture, measurement has been made as far as possible at the farm gate level.

milk used to produce dairy products that are sold on the export market. For dairy products sold on the domestic market producers can pass the levy on to consumers. The funds raised by the levy are used to pay a subsidy to all manufacturing milk. This subsidy is treated as assistance by the Commission. The subsidy rates are being phased down, with the scheme due to expire on 30 June 2000 (IC 1997f).

Tobacco

The estimated nominal rate of assistance for the tobacco industry decreased from 40 per cent in 1995-96 to 30 per cent in 1996-97. The effective rate of assistance also fell substantially over the same period from 159 per cent to 100 per cent.

Statutory marketing arrangements for tobacco are being phased out as part of a restructuring program, which commenced in January 1995. The transitional arrangements have been discussed previously (IC 1996b). Effective rates of assistance are expected to fall to around 2 per cent in 1999-2000 with the completion of the restructuring program.

Sugar

Assistance to the sugar industry in 1996-97 was derived from Queensland's statutory marketing arrangements for raw sugar and a specific tariff on raw sugar imports. These arrangements enable domestic prices to be raised above export parity prices (IC 1996b). In 1996-97, the estimated nominal and effective rates of assistance for sugar remained constant at 4 and 16 per cent, respectively.

Assistance to the sugar industry is expected to change significantly in 1997-98 following the removal of the sugar tariff on 1 July 1997 and implementation of the requirement for the Queensland Sugar Corporation to price at export parity on domestic sales. In 1996-97, the net subsidy equivalent for the sugar industry was $70 million. Full implementation of the reforms to the sugar industry is expected to reduce the net subsidy equivalent by around $50 million. This is equivalent to a reduction in the effective rate of assistance of around 12 percentage points. To offset this reduction in support, the Commonwealth Government is to provide a compensation package to the sugar industry (IC 1997f).

Rice

The Australian rice industry, located primarily in New South Wales, is assisted through statutory marketing arrangements which allow the New South Wales Rice Growers Co-operative to vest and market all rice grown in the State. The nominal rate of assistance for the rice industry increased to 3 per cent in 1996-97 from 2 per cent in 1995-96, while the effective rate of assistance increased from 8 per cent to 11 per cent.

In 1996, the Review of Legislation Establishing the New South Wales Rice Marketing Board recommended the removal of domestic marketing arrangements on the ground that such reform would provide a net community benefit. The New South Wales Government rejected this recommendation. The National Competition Council (NCC) has stated that this decision was not consistent with the State's obligation under clause 5 of the Competition Principles Agreement (CPA). The New South Wales Government has indicated a willingness to resolve the matter in accordance with the CPA. In the event that appropriate reforms are not implemented by 31 January 1999, the NCC has recommended to the Federal Treasurer that $10 million be deducted from the 1998-99 National Competition Policy payment to New South Wales (NCC 1998).

Wheat

The nominal rate of assistance for the wheat industry increased from 1 per cent in 1995-96 to 2 per cent in 1996-97. The effective rate of assistance increased from 4 per cent to 6 per cent over the same period, largely reflecting lower tax penalties following reductions in tariff levels on inputs.

The wheat industry receives assistance mainly from the rural adjustment scheme, tax concessions, research assistance and the government guarantee on Australian Wheat Board (AWB) borrowings. The government guarantee on AWB borrowings accounts for around half of all assistance received by the wheat industry. The assistance afforded by the guarantee is equal to the interest savings resulting from the difference between the assessed 'market', and government-guaranteed, interest rates. The government guarantee is due to expire at the end of 1998-99. From 1 July 1999, the AWB is to be replaced by grower owned companies which will be responsible for wheat marketing.

Wool

The wool industry receives assistance mainly from research and development funding, the rural adjustment scheme and the government guarantee on borrowings by Wool International. The nominal rate of assistance for the wool industry decreased from 2 per cent in 1995-96 to 1 per cent in 1996-97. The effective rate of assistance decreased from 9 per cent to 7 per cent over the same period. The decrease in the effective rate of assistance largely reflects the decrease in output assistance.

In August 1998, the Government announced plans to freeze all sales from the wool stockpile for the remainder of the 1998-99 season (Anderson 1998c). The introduction of the necessary legislation to change the existing wool marketing arrangements was delayed when Parliamentary sittings were suspended due to the calling of the 1998 Federal election. Wool International continued to make sales from the stockpile after the Government's announcement. The objective of the freeze was to provide price support to growers in light of poor market conditions for wool. The implications for support to the wool industry of any stockpile freeze would depend on the extent to which the freeze was successful in raising wool prices and therefore returns to growers.

Pigmeat

Assistance to the pigmeat industry is low relative to many other agricultural activities. The nominal rate of assistance for the pigmeat industry in 1996-97 remained at less than 0.5 per cent, while the effective rate of assistance was constant at around 5 per cent.

The pigmeat industry receives assistance primarily from research and development funding, adjustment assistance and tax concessions. Research and development funding accounted for around half of all assistance received by the industry in 1996-97. The Government recently announced $18 million of additional funding for the pork industry to be provided through the National Pork Industry Development and Pigmeat Processing Grants Programs (see chapter 2).

The Commission has been asked to inquire and report on whether safeguard action, in accordance with the WTO Agreement, is warranted against imports of certain frozen pigmeat. The Commission has been asked also to report on the factors affecting the profitability and competitiveness of the domestic pig farming and pigmeat processing industries (see chapter 4).

Table 3.1 **Average nominal and effective rates of assistance, by agricultural activity, and standard deviations for the agricultural sector, 1992-93 to 1996-97**

per cent

	Nominal rate of assistance on output [a]					*Effective rate of assistance* [b]				
Activity/commodity description	*1992-93*	*1993-94*	*1994-95*	*1995-96*	*1996-97*	*1992-93*	*1993-94*	*1994-95*	*1995-96*	*1996-97*
Horticulture										
Apples and pears	..	..	..	..	..	-6	-4	-2	..	2
Dried vine fruits [c]	26	12	5	5	3	67	29	14	11	8
Wine grapes	13	10	9	7	4	28	24	19	15	11
Citrus	2	2	1	1	1	4	4	4	4	4
Deciduous canning fruits	..	..	..	..	..	..	1	1	2	4
Bananas	..	..	..	..	..	-1	..	..	1	1
Tobacco [d]	62	60	50	40	30	>200	>200	>200	159	100
Vegetables	..	..	..	..	..	-1	..	..	1	2
Average	**4**	**3**	**2**	**2**	**1**	**7**	**6**	**5**	**6**	**5**
Extensive cropping										
Wheat	2	2	2	1	2	5	5	6	4	6
Barley	..	..	..	..	..	..	1	2	1	2
Oats	..	..	..	..	..	1	1	1	1	2
Maize	..	..	..	..	..	..	..	..	1	2
Sorghum	..	..	..	..	..	1	1	1	1	2
Oilseeds	..	..	..	..	..	2	3	5	3	4
Average	**1**	**1**	**1**	**1**	**1**	**3**	**4**	**4**	**3**	**5**
Extensive irrigation and high rainfall crops										
Sugar [e]	5	4	4	4	4	12	12	11	16	16
Cotton	..	..	..	..	..	-3	1	2	3	2
Rice [f]	2	1	2	2	3	9	4	8	8	11
Average	**2**	**2**	**2**	**2**	**2**	**6**	**7**	**8**	**10**	**11**
Extensive grazing										
Beef	..	..	..	..	..	3	3	4	5	5

Table 3.1 **(continued)**

	Nominal rate of assistance on output[a]					Effective rate of assistance[b]				
Activity/commodity description	*1992-93*	*1993-94*	*1994-95*	*1995-96*	*1996-97*	*1992-93*	*1993-94*	*1994-95*	*1995-96*	*1996-97*
Wool	6	4	1	2	1	17	14	6	9	7
Sheepmeat	..	..	..	..	..	5	4	3	3	3
Average	**2**	**1**	**..**	**1**	**..**	**8**	**6**	**4**	**6**	**5**
Intensive livestock										
Pigs	..	..	..	..	..	3	4	5	5	5
Poultry	..	..	..	..	..	..	7	8	11	4
Eggs[g]	2	3	4	2	1	6	9	11	7	3
Milk production	20	19	24	18	19	56	56	77	53	58
Manufacturing milk	9	8	9	7	8	21	20	25	20	21
Fresh milk[h]	49	49	58	54	60	>200	>200	>200	>200	>200
Average	**11**	**10**	**13**	**11**	**12**	**36**	**38**	**51**	**40**	**42**
Total agriculture										
Average	**4**	**3**	**3**	**3**	**3**	**11**	**10**	**10**	**10**	**10**
Standard deviation[i]	**(9)**	**(9)**	**(10)**	**(9)**	**(10)**	**(32)**	**(30)**	**(41)**	**(35)**	**(42)**

.. Between -0.5 per cent and 0.5 per cent. [a] Average nominal rates on outputs are weighted by the unassisted value of output of each activity. [b] Average effective rates are weighted by the unassisted value added of each activity. [c] The estimates of assistance to sultanas are based on a comparison of the lower of either domestic or constructed import parity returns with the export returns. [d] Based on transfers derived by applying the price differential between Australian green leaf and comparable imported green leaf to the domestic sales of Australian leaf. Following the removal of the local leaf content scheme in January 1995, the methodology used for calculating producer transfers was revised for the 1994-95, 1995-96 and 1996-97 estimates. [e] Producer transfers were estimated in accordance with the industry formula used for dividing raw sugar returns between millers and growers. [f] Estimated by comparing domestic and export prices for medium- and long-grain rice. [g] Estimates are derived using a weighted average of retail prices for eggs in the deregulated States to determine a benchmark retail price. This benchmark price is compared with the average retail prices in the regulated States in order to make an estimate of assistance provided at the retail level. Finally, this retail-level assistance is estimated on a pro rata basis from the value of retail prices to provide an estimate of assistance at the farm-gate level. [h] The producer transfer was estimated by multiplying the difference between the fresh milk price and the local manufacturing milk price plus an allowance of 20 per cent of the average Australian manufacturing milk price to represent the cost of assurance of out-of-season supply. [i] The standard deviation in percentage points measures how far from the average items are located in a frequency distribution, thereby measuring the extent of variation or dispersion in the distribution. The larger the variability among individual activities' nominal and effective rates, the larger the standard deviation.

Source: Commission estimates.

Table 3.2 **Average nominal and effective rates of assistance, by 3-digit ANZSIC,[a] 1992-93 to 1996-97**

per cent

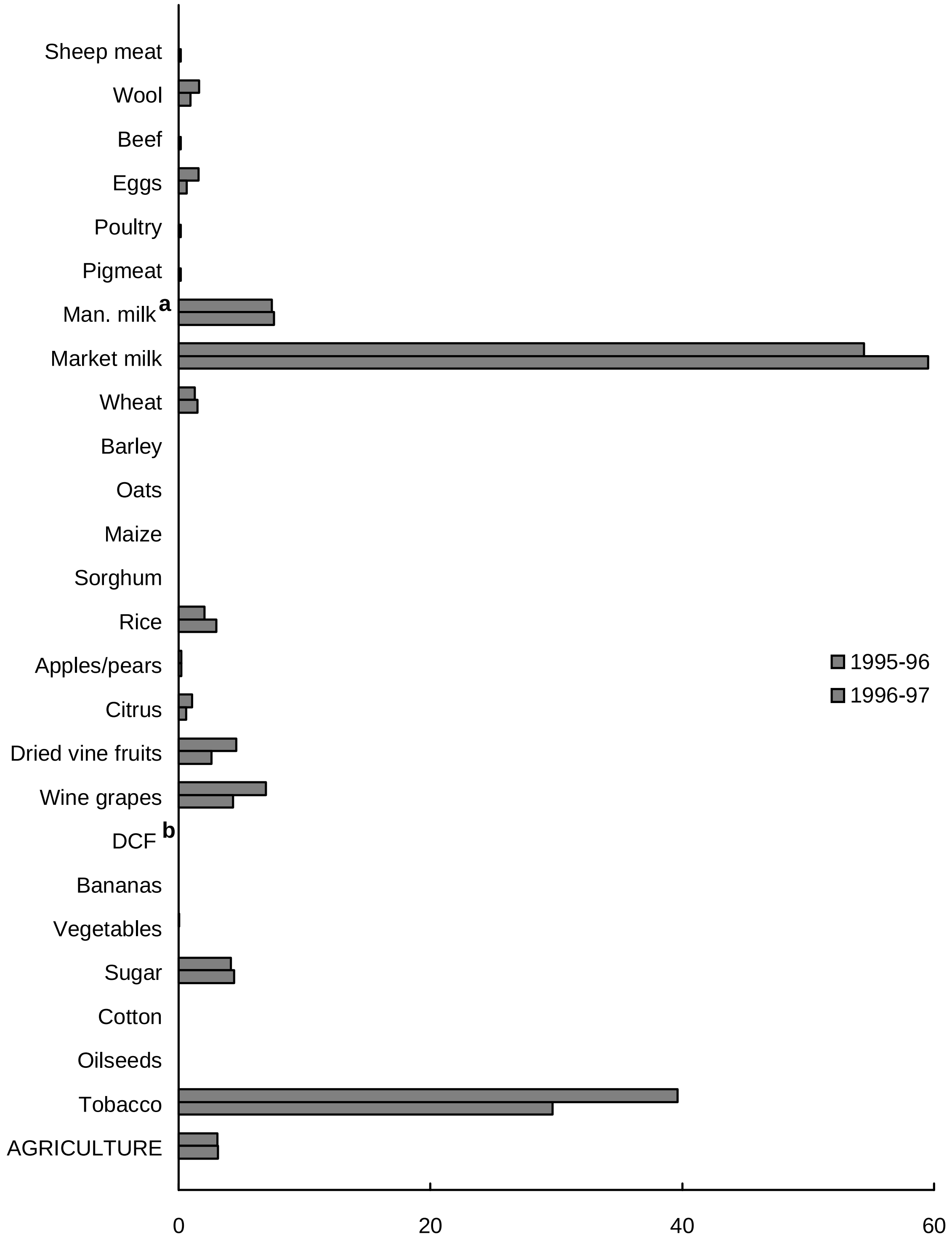
		Nominal rate of assistance on output[b]					*Effective rate of assistance[c]*				
Activity/commodity description		*1992-93*	*1993-94*	*1994-95*	*1995-96*	*1996-97*	*1992-93*	*1993-94*	*1994-95*	*1995-96*	*1996-97*
Code											
011	Horticulture and fruit growing	2	2	2	2	1	4	4	4	5	4
012	Grain, sheep and beef cattle farming	2	1	1	1	1	6	5	5	5	5
013	Dairy cattle farming	20	19	24	18	19	56	56	77	53	58
014	Poultry farming	1	..	1	..	..	3	8	10	10	3
015	Other livestock farming	..	..	..	..	..	3	4	5	5	5
016	Other crop growing	4	3	3	3	3	11	11	9	12	12
01	**Agriculture**	**4**	**3**	**3**	**3**	**3**	**11**	**10**	**10**	**10**	**10**

.. Between 0 per cent and 0.5 per cent. [a] Industry subdivision and group from the Australian and New Zealand Standard Industrial Classification (ANZSIC). [b] Average nominal rates on outputs are weighted by the unassisted value of output of each activity. [c] Average effective rates are weighted by the unassisted value added of each activity.

Source: Commission estimates.

Figure 3.2 **Average nominal rates of assistance to agricultural commodities, 1995-96 and 1996-97**

per cent

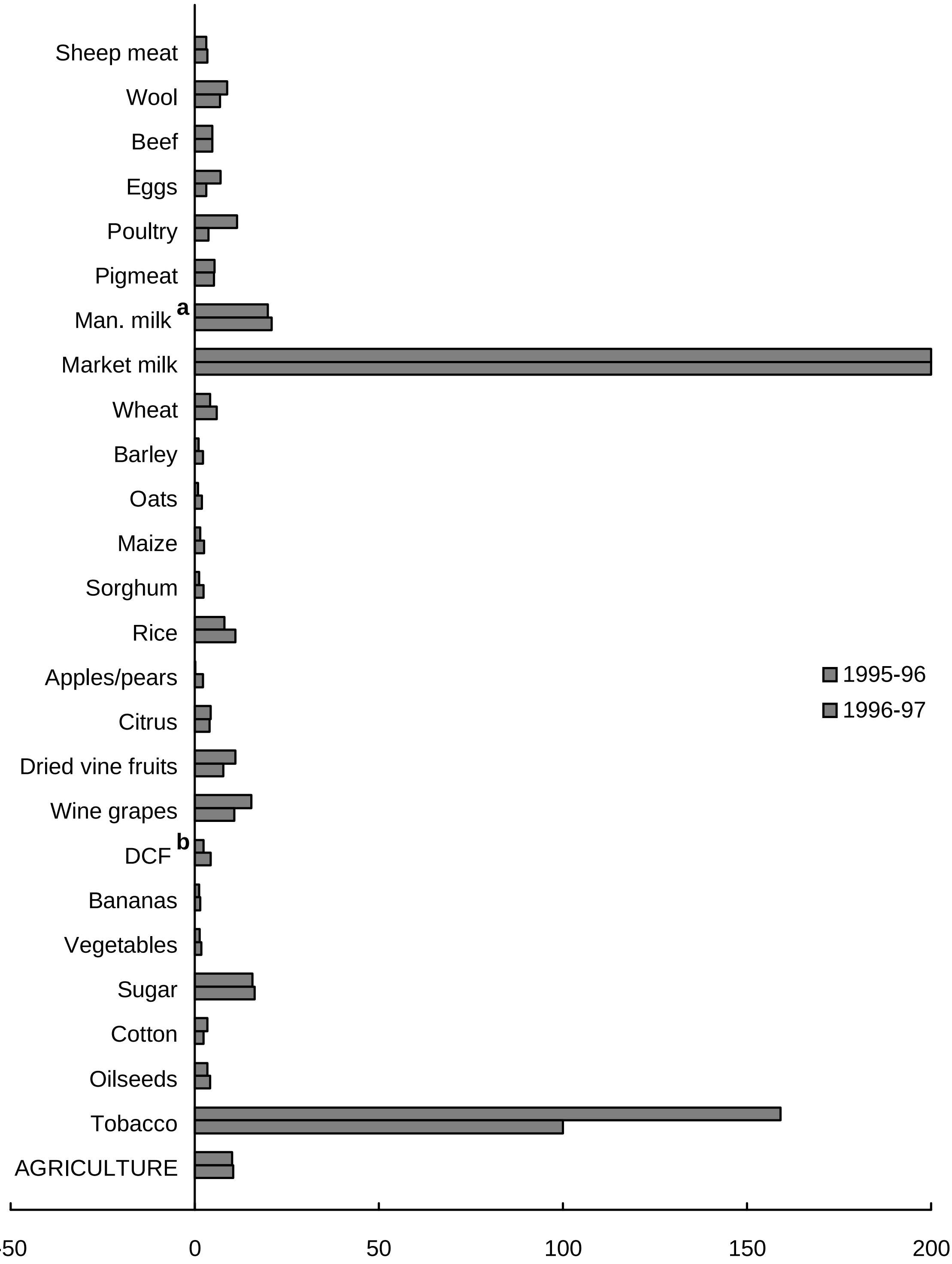


[a] Manufacturing milk. [b] Deciduous canning fruits.

Source: Commission estimates.

Figure 3.3 **Average effective rates of assistance to agricultural commodities, 1995-96 and 1996-97**

per cent



[a] Manufacturing milk. [b] Deciduous canning fruits.

Source: Commission estimates.

Table 3.3 Assistance to agriculture by form, 1992-93 to 1996-97

$ million

	1992-93	1993-94	1994-95	1995-96	1996-97
Assistance to outputs					
Domestic pricing arrangements [a]	403	392	479	513	535
Tariffs	63	58	58	66	54
Local content schemes	30	18	-	-	-
Export incentives	3	2	3	3	3
Export inspection services [b]	11	16	6	..	9
Marketing support	50	22	1	1	1
Government guarantees	116	106	58	85	77
Total	**676**	**614**	**605**	**667**	**679**
Assistance to value-adding factors					
Adjustment assistance [c]	105	105	120	115	105
Agricultural research	148	156	160	154	161
Income taxation concessions	24	70	86	163	151
Natural disaster relief	4	2	1	1	1
Sugar industry program	-	3	4	2	4
Total	**281**	**336**	**371**	**436**	**422**
Assistance to inputs					
Disease control [d]	5	3	3	3	2
Tariffs on inputs [e]	-106	-87	-77	-80	-57
Tariffs on plant and machinery [e]	-67	-64	-62	-61	-49
Total	**-167**	**-148**	**-136**	**-138**	**-104**
Subsidy equivalents					
Gross Subsidy Equivalent	**676**	**614**	**605**	**667**	**679**
Net Subsidy Equivalent	**790**	**802**	**840**	**964**	**997**

.. Between -0.5 and 0.5 million. - Nil. Figures may not add to total due to rounding. [a] For 1994-95, 1995-96 and 1996-97, estimates include transitional assistance to tobacco following the removal of the local content scheme in January 1995. [b] Based on shortfalls from 100 per cent cost recovery. [c] Figures reflect actual Commonwealth interest subsidies and grants provided to producers. [d] Covers assistance provided by the bovine brucellosis and tuberculosis eradication campaign. [e] The additional costs incurred due to assistance raising the prices of inputs. The current series includes the effect of tariffs on materials used in non-traded inputs.

Source: Commission estimates.

3.3 Manufacturing assistance

The main forms of assistance to the manufacturing sector are import tariffs and a range of budgetary measures. The general program of phased tariff reductions, begun in March 1991, was completed in July 1996 with all tariff rates except those protecting the PMV and TCF industries falling to 5 per cent or less. Despite the large reductions in tariff rates under this program, tariff assistance still accounts for around 90 per cent of **measured** assistance to the sector. While the manufacturing assistance estimates are not comprehensive in their coverage of budgetary assistance, even with the inclusion of some of the additional measures identified in chapter 2, tariffs would remain the dominant form of support for the sector.

Estimates have not been revised this year or updated to 1997-98. Given the resource requirements for estimating assistance, the Commission has decided to update estimates only when changes in Government policy result in a significant deviation from previously announced schedules or in major new initiatives. Only PMV and TCF tariffs rates have changed since 1996-97 and changes in budgetary assistance would not have had a significant impact on measured assistance.

The effects of implementing the remaining scheduled tariff reductions for PMV and TCF are reflected in the Commission's projections of assistance for 2000-01.[2] These projections have not been revised. They continue to represent reasonable estimates of future rates of assistance, particularly at higher levels of aggregation. This is because:

- tariffs are the dominant influence on measured assistance;
- the schedule for further PMV and TCF tariff reductions has not changed; and
- no further general tariff reductions have been announced.

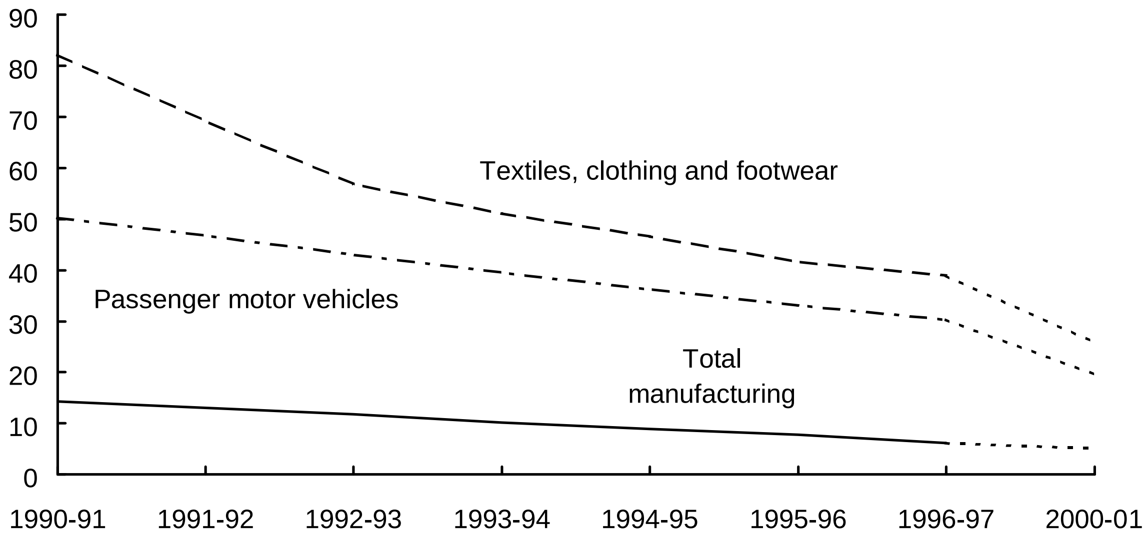
Assistance estimates have been reported at the 2-digit ASIC subdivision level in tables 3.4, 3.5 and 3.6. Previously published estimates of nominal and effective rates of assistance are provided for the years 1993-94 to 1996-97, as well as projections for 2000-01. More detailed estimates down to the 4-digit ASIC industry level were presented in the Commission's 1995 information paper, *Assistance to Agricultural and Manufacturing Industries*.

[2] As tariff reduction schedules were announced several years in advance, the Commission was able to project assistance levels through to the end of the program and in 1995 published a compilation of all assistance estimates and projections of future assistance levels (IC 1995b).

Trends in manufacturing assistance

The nominal rate of assistance to manufacturing was around 4 per cent in 1996-97 and is projected to fall to 3 per cent by 2000-01, while the effective rate of assistance, around 6 per cent in 1996-97, is projected to fall to 5 per cent by 2000-01. PMV and TCF industries continue to receive assistance several times higher than other manufacturing activities (figure 3.4).

Figure 3.4 **Average effective rates of assistance to manufacturing, PMV and TCF, 1990-91 to 2000-01**
per cent



Source: Commission estimates.

The fall in PMV and TCF tariffs relative to the generally applicable manufacturing tariff of 5 per cent is expected to result in a decline in the dispersion of assistance across the manufacturing sector in the period to 2000-01. The standard deviation of effective rates is projected to fall from 10 percentage points in 1996-97 to 7 percentage points in 2000-01.

The estimated NSE of assistance to manufacturing was around $4 billion in 1996-97 and is projected to fall to $3.5 billion in 2000-01. The PMV and TCF industries accounted for around half of the estimated NSE to the manufacturing sector in 1996-97. This share is projected to fall to around 40 per cent by 2000-01.

Policy developments affecting manufacturing assistance

While developments in 1997-98 are unlikely to have a significant impact upon measured assistance in the manufacturing sector, recent Government announcements such as the *Investing for Growth* Statement, the Automotive Competitiveness and Investment Scheme (ACIS) and new assistance measures for the TCF industry will have implications for levels of assistance beyond 2000.

Assistance to the PMV industry

As a result of continuing phased tariff reductions, the effective rate of assistance to the PMV industry is expected to fall to 19 per cent by 2000-01, from 28 per cent in 1996-97 (table 3.6).

The PMV tariff declined by a further 2.5 percentage points to 20 per cent on 1 January 1998 and is to fall to 17.5 per cent by 1999 and to 15 per cent in 2000. The tariff is to remain at 15 per cent until January 2005, when it is scheduled to fall immediately to 10 per cent. Assuming no other changes in assistance, the effect of the pause in tariff reductions will be to maintain effective assistance to PMV at levels nearly 4 times the manufacturing average.

The Government has recently introduced legislation to implement the ACIS. The ACIS replaces the Export Facilitation Scheme. It will commence in January 2001 and operate for five years (see chapter 2).

Assistance to the TCF industries

Assistance to the TCF industries is expected to decline between 1996-97 and 2000-01, reflecting further phased tariff reductions. The effective rate of assistance for the textiles industry is projected to fall to 17 per cent in 2000-01, from 25 per cent in 1996-97, while the effective rate for the clothing and footwear industries is projected to decline to 34 per cent by 2000-01, from 52 per cent in 1996-97 (table 3.6).

In 2000, all TCF imports (apart from those already at 5 per cent or less) will be subject to tariff rates of either 25, 15, or 10 per cent. TCF tariffs are to remain at these levels until 2005, when tariffs on apparel and certain finished textiles, footwear and fabrics are scheduled to decline immediately to 17.5 per cent, 10 per cent and 7.5 per cent, respectively.

In July 1998, the Government announced details of a new package of assistance measures for the TCF industry, comprising the:

- TCF Strategic Investment Program (including a Regional Adjustment Package);
- TCF Technology Development Fund;
- National Framework for Excellence in TCF Training;
- TCF Market Development Program; and
- Expanded Overseas Assembly Provisions Scheme.

The new measures, which will operate from 2000 to 2005, replace some of the existing arrangements providing assistance to the TCF industry (see chapter 2). While these new funding arrangements may have implications for the distribution of assistance within TCF and rates of assistance for individual industries, assistance at the broad industry subdivision level is unlikely to change significantly between 2000 and 2005.

Other budgetary support for manufacturing

Other budgetary outlays and tax expenditures provide assistance to the manufacturing sector. Recent changes to budgetary assistance, including those announced in the *Investing for Growth* Statement, are discussed in chapter 2.

Implementation of the *Investing for Growth* initiatives (covering R&D support, investment incentives, export assistance and specific incentives for the information technology industry) is not expected to have a significant impact on manufacturing assistance in 1997-98 and 1998-99, but is likely to increase budgetary assistance significantly in 2001-02 and may therefore have implications for future effective rates of assistance to the manufacturing sector.

Recent developments in tariff assistance

The Government recently announced the removal of tariffs on business inputs in the information technology and telecommunications industry and on medical and scientific equipment — with revenue forgone of $80 million over a two year period and $40 million over a three year period, respectively. While placing upward pressure on effective rates, the impact of these tariff reductions on assistance to the manufacturing sector at the 2-digit subdivision level is not expected to be significant.

Another development with potential implications for tariff assistance in future years is the recently announced Government review of ‘nuisance’ tariffs. The objective of the review is to identify tariffs (at levels between 3 and 5 per cent) on business inputs which raise little revenue, offer few or no protective benefits to Australian industry and disadvantage Australian industry relative to imported goods (see chapter 4).

Table 3.4 **Average nominal rates of assistance on outputs,[a] manufacturing subdivisions,[b] 1993-94 to 1996-97 and 2000-01**

per cent

Industry[c]						
Code	*Description*	*1993-94*	*1994-95*	*1995-96*	*1996-97*	*2000-01*
21	**Food, beverages and tobacco**	**5**	**4**	**3**	**3**	**3[d]**
234	Textile fibres, yarns and woven fabrics	9	8	7	7	5
235	Other textile products	19	18	16	14	10
23	**Textiles**	**12**	**11**	**10**	**9**	**6**
244	Knitting mills	37	34	31	29	20
245	Clothing	39	36	33	30	21
246	Footwear	31	28	25	23	13
24	**Clothing and footwear**	**37**	**34**	**31**	**29**	**19**
25	**Wood, wood products and furniture**	**7**	**6**	**5**	**4**	**4**
26	**Paper, paper products and publishing**	**5**	**4**	**3**	**2**	**2**
27	**Chemical, petroleum and coal products**	**2**	**1**	**1**	**1**	**1**
28	**Non-metallic mineral products**	**2**	**2**	**2**	**1**	**1**
29	**Basic metal products**	**3**	**3**	**3**	**2**	**2**
31	**Fabricated metal products**	**9**	**7**	**6**	**4**	**4**
323	Motor vehicles and parts	20	19	17	15	10
32	**Transport equipment**	**17**	**15**	**14**	**12**	**9**
33	**Other machinery and equipment**	**9**	**8**	**6**	**4**	**4**
34	**Misc. manufacturing**	**10**	**9**	**7**	**5**	**5**
21-34	**TOTAL MANUFACTURING**	**6**	**5**	**5**	**4**	**3**

.. Between 0 per cent and 0.5 per cent. [a] Assistance provided by tariffs and certain non-tariff measures. The nominal rate of assistance on outputs is an average of the nominal rates on outputs used by that industry, weighted by the unassisted value of output used. [b] The nominal rate of assistance on outputs is provided at the 3-digit ASIC level for the more highly assisted Textiles, Clothing and Footwear and Passenger Motor Vehicle industries. [c] Industry subdivision and group from the Australian Standard Industrial Classification (ASIC) 1983 Edition. The ASIC was replaced by the Australia and New Zealand Standard Industrial Classification (ANZSIC) in 1993. However, manufacturing assistance estimates based on ANZSIC have not been derived. [d] Estimates reflect the Commission's projections of assistance to agricultural commodities.

Source: Commission estimates.

Table 3.5 Average nominal rates of assistance on materials,[a] manufacturing subdivisions,[b] 1993-94 to 1996-97 and 2000-01

per cent

Industry[c]						
Code	*Description*	*1993-94*	*1994-95*	*1995-96*	*1996-97*	*2000-01*
21	**Food, beverages and tobacco**	**5**	**4**	**4**	**3**	**3**[d]
234	Textile fibres, yarns and woven fabrics	3	3	3	2	2
235	Other textile products	8	7	6	5	4
23	**Textiles**	**4**	**4**	**4**	**3**	**2**
244	Knitting mills	9	8	7	5	5
245	Clothing	19	18	16	14	9
246	Footwear	9	8	7	5	5
24	**Clothing and footwear**	**15**	**13**	**12**	**10**	**7**
25	**Wood, wood products and furniture**	**6**	**5**	**4**	**3**	**3**
26	**Paper, paper products and publishing**	**4**	**3**	**3**	**2**	**2**
27	**Chemical, petroleum and coal products**	**1**	**1**	**1**	**..**	**..**
28	**Non-metallic mineral products**	**1**	**1**	**1**	**1**	**1**
29	**Basic metal products**	**1**	**1**	**1**	**1**	**1**
31	**Fabricated metal products**	**6**	**5**	**5**	**4**	**4**
323	Motor vehicles and parts	11	10	9	8	6
32	**Transport equipment**	**10**	**9**	**8**	**7**	**6**
33	**Other machinery and equipment**	**7**	**6**	**5**	**3**	**3**
34	**Misc. manufacturing**	**7**	**6**	**4**	**3**	**3**
21-34	**TOTAL MANUFACTURING**	**4**	**3**	**3**	**2**	**2**

.. Between 0 per cent and 0.5 per cent. **a** Assistance provided by tariffs and certain non-tariff measures. The nominal rate of assistance on materials is an average of the nominal rates on materials used by that industry, weighted by the unassisted value of each material used. **b** The nominal rate of assistance on materials is provided at the 3-digit ASIC level for the more highly assisted Textiles, Clothing and Footwear and Passenger Motor Vehicle industries. **c** Industry subdivision and group from the Australian Standard Industrial Classification (ASIC) 1983 Edition. The ASIC was replaced by the Australia and New Zealand Standard Industrial Classification (ANZSIC) in 1993. However, manufacturing assistance estimates based on ANZSIC have not been derived. **d** Estimates reflect the Commission's projections of assistance to agricultural commodities.

Source: Commission estimates.

Table 3.6 **Average effective rates of assistance,[a] manufacturing subdivisions,[b] 1993-94 to 1996-97 and 2000-01**

per cent

Industry[c]						
Code	*Description*	*1993-94*	*1994-95*	*1995-96*	*1996-97*	*2000-01*
21	**Food, beverages and tobacco**	**3**	**3**	**3**	**2**	**2**[d]
234	Textile fibres, yarns and woven fabrics	37	33	24	23	15
235	Other textile products	37	34	31	28	19
23	**Textiles**	**37**	**33**	**27**	**25**	**17**
244	Knitting mills	92	86	80	76	49
245	Clothing	59	54	50	47	33
246	Footwear	60	54	50	46	24
24	**Clothing and footwear**	**65**	**60**	**56**	**52**	**34**
25	**Wood, wood products and furniture**	**9**	**7**	**6**	**4**	**4**
26	**Paper, paper products and publishing**	**6**	**5**	**4**	**2**	**2**
27	**Chemical, petroleum and coal products**	**6**	**5**	**4**	**3**	**3**
28	**Non-metallic mineral products**	**3**	**3**	**2**	**2**	**2**
29	**Basic metal products**	**6**	**5**	**5**	**4**	**4**
31	**Fabricated metal products**	**12**	**10**	**8**	**4**	**4**
323	Motor vehicles and parts	38	35	31	28	19
32	**Transport equipment**	**26**	**24**	**21**	**19**	**13**
33	**Other machinery and equipment**	**11**	**9**	**8**	**5**	**5**
34	**Misc. manufacturing**	**14**	**12**	**10**	**7**	**7**
21-34	**TOTAL MANUFACTURING**	**10**	**9**	**8**	**6**	**5**

.. Between -0.5 per cent and 0.5 per cent. **a** Assistance to an activity, net of the effects of tariffs and certain other forms of government intervention which alter the prices of material inputs used by the industry. For certain TCF industries the estimates include some assistance to value adding factors. **b** The effective rate of assistance is provided at the 3-digit ASIC level for the more highly assisted Textiles, Clothing and Footwear and Passenger Motor Vehicle industries. **c** Industry subdivision and group from the Australian Standard Industrial Classification (ASIC) 1983 Edition. The ASIC was replaced by the Australia and New Zealand Standard Industrial Classification (ANZSIC) in 1993. However, manufacturing assistance estimates based on ANZSIC have not been derived. **d** Estimates for 2000-01 reflect Commission projections of assistance to agricultural commodities.

Source: Commission estimates.

4 Agriculture and manufacturing trade policy issues and developments

There were 36 new anti-dumping and countervailing cases initiated by Australia in 1997-98. Initiations have almost doubled in each of the past three years. Internationally, Australia continues to account for a relatively high proportion of total initiations and measures in force. A new anti-dumping and countervailing system was introduced on 24 July 1998. It remains to be seen what impact the faster single stage investigation and revised review and appeal mechanism will have on the number of initiations and the outcome of investigations.

The WTO's recent Trade Policy Review of Australia raises a number of issues regarding manufacturing and agriculture policy in Australia. Several of these issues, and others, may be raised by Australia's trading partners at the next WTO negotiations on agriculture scheduled to commence in late 1999.

APEC early sectoral liberalisation arrangements, initiated in November 1996, are to be finalised by November 1998 with implementation scheduled to commence in 1999. There are several issues which need to be addressed if early voluntary sectoral liberalisation (EVSL) is to achieve its objectives most effectively. Some of these issues are also relevant to foreshadowed unilateral tariff reform in Australia, involving the elimination of 'nuisance' tariffs.

4.1 Anti-dumping and countervailing activity

Dumping occurs when a foreign supplier exports goods at a price which is lower than the 'normal value' of the goods in the supplier's home market. The General Agreement on Tariffs and Trade (GATT) allows Members to apply anti-dumping measures on imports of a good with an export price below its normal value if such imports cause or threaten to cause material injury to the domestic industry (WTO 1997).

Anti-dumping action may take two forms:

- the foreign exporter may agree to make a formal undertaking to export future goods to the importing market at a normal price; or
- a dumping duty may be imposed on the relevant imports to bring the export price up to but not higher than the normal value of goods in the exporting country.

There is no single definition of normal value. The price of the good in the exporter's home market is taken as the normal value if possible, but alternatives such as the price of the good in another export market or a constructed price may be used.

Like other measures which affect the price of imports, anti-dumping measures may restrict competition, protect domestic industry and impose higher costs on domestic consumers.

In addition, the WTO Agreement on Subsidies and Countervailing Measures (1995) allows Members to apply countervailing duties where exports benefiting from certain forms of subsidies cause or threaten to cause material injury or serious prejudice to a domestic industry.

Australia's new anti-dumping and countervailing system

A new anti-dumping and countervailing system implemented through amendments to the legislation became effective on 24 July 1998.[1] The new arrangements draw on the recommendations of the *Review of Anti-Dumping and Countervailing Administration* (Willett 1996).

Key changes to anti-dumping and countervailing administration introduced in the new scheme include:

- a significantly shorter (155 day) single stage anti-dumping and countervailing investigation conducted by the Australian Customs Service (ACS);
- the abolition of the Anti-Dumping Authority (ADA);
- provision for the payment of interim duties after 60 days of the investigation period; and
- a new appeal and review mechanism which provides for reviews to be conducted by a statutory officer known as the Trade Measures Review Officer (TMRO).

Table 4.1 provides a summary comparison of the previous and the new systems. A flow chart depicting the new process is provided as figure 4.1.

[1] This follows interim changes announced in February 1997 without any change to the legislation. These changes were discussed in IC (1997f).

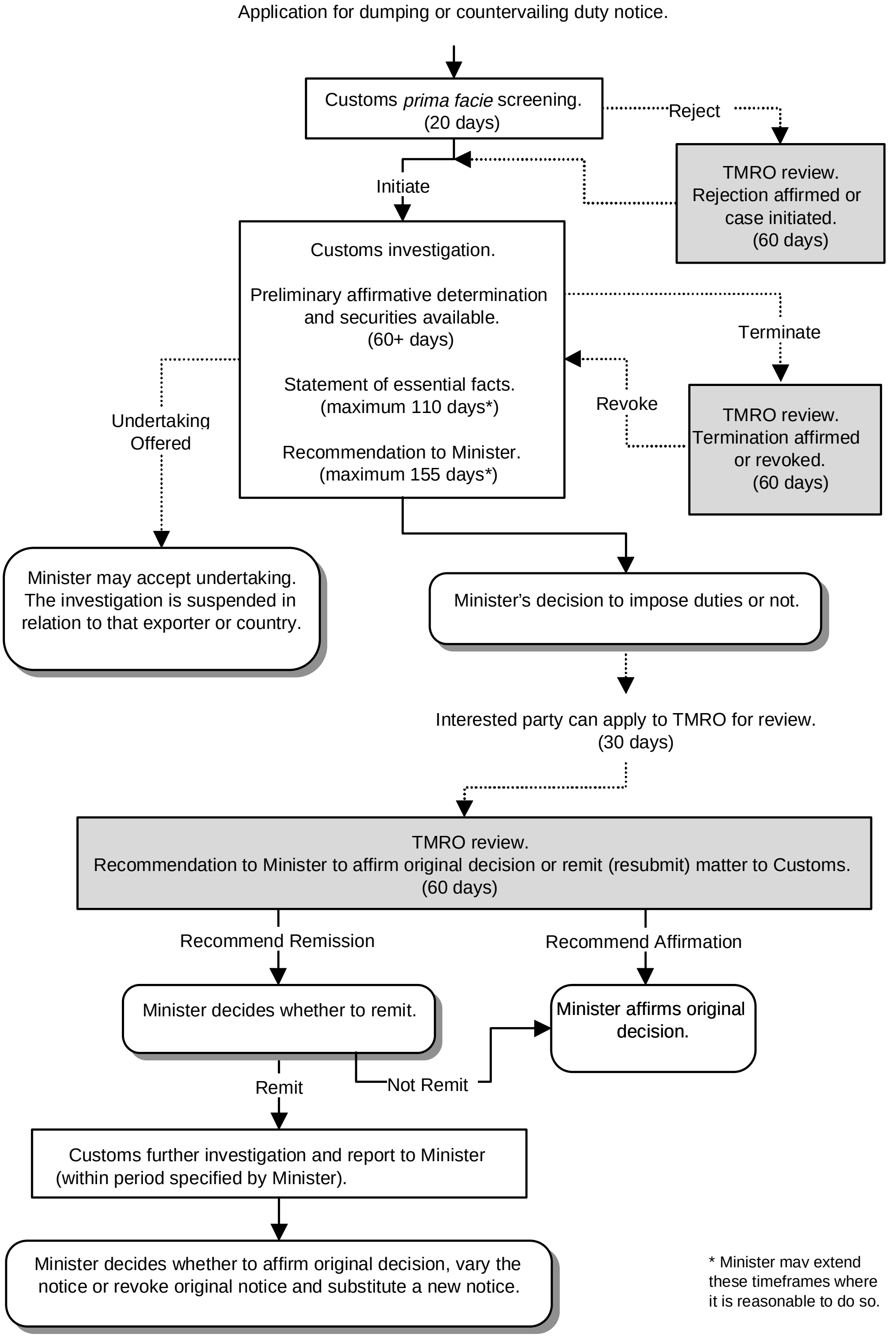
Table 4.1 **Comparison of previous[a] and new[b] anti-dumping and countervailing systems**

Feature	*Previous*	*New*
Total time frame	215 day two stage system conducted by the ACS and ADA.	155 day (175 including screening) single stage system conducted by the ACS.
Screening	20 days for ACS to examine application and to initiate investigation or reject application.	20 day screening period is now outside the formal investigation period.
	Complainants must demonstrate that they are a local industry producing like goods, undertake a substantial process of manufacture (with a minimum local content of 25%), and have the support of a majority of local producers of the good.	25% local content requirement repealed. Other screening requirements unchanged.
Preliminary investigation	85 days for ACS to deliver a preliminary finding at which stage interim duties may be applied.	Interim duties may be applied after 60 days of the investigation period.
Final Finding	In the case of a positive preliminary finding, 110 days for ADA to gather additional information, conduct an investigation and deliver a final finding.	In the case of a positive finding after preliminary investigation, ACS to continue investigation and deliver a final finding within 155 days. Statement of essential facts by day 110 with submissions in response due by day 130.
Review and Appeals	Rejection of initial application subject to appeal, 60 days for ADA to conduct a review.	Rejection of initial application automatically subject to 60 day review by TMRO.
	Negative preliminary finding subject to appeal, 90 days for the ADA to undertake a review of ACS's investigation.	Negative finding after preliminary investigation automatically subject to 60 day review by TMRO.
	Final duty assessment subject to appeal, 90 days for the ADA to undertake a review.	Positive or negative final finding subject to appeal, 90 days for TMRO to conduct a review of ACS's investigation with: • notice of appeal given within 30 days of the final decision; • submissions due by day 60; and • decision delivered by the TMRO by day 90.

a System after the interim reductions to time frames implemented on 1 February 1997. **b** Effective from 24 July 1998.

Source: Truss (1998), Moore and Truss (1998) and Willett (1996).

Figure 4.1 **Process for considering an application for the imposition of anti-dumping or countervailing duties**



Source: Information provided by ACS.

Under the new arrangements, the ACS undertakes the entire investigation. Previously, in the case of a positive preliminary finding by Customs, the ADA would conduct a review of the findings by Customs and also call for additional submissions and gather further information.

The move to a single stage investigation conducted solely by Customs will streamline the administration of anti-dumping and countervailing actions, but it may also have implications for investigation outcomes. It is worth noting that since its establishment in 1988, ADA investigations resulted in a final finding different from the Customs preliminary finding in more than 40 per cent of cases.[2] However, this partly reflects the relatively short time frame for the preliminary investigation by ACS and the benefits the ADA derived from additional information/submissions.

The WTO in its latest Trade Policy Review of Australia questioned "whether the shorter investigation period will enable the ACS to conduct as thorough an analysis and review as previously" (WTO 1998b, p. 57).

As part of the new 155 day investigation period, the ACS is to issue a 'statement of essential facts' after 110 days which affected parties (including importers, exporters, local industry and consumer groups) may respond to within 20 days. Under the previous system, after a positive preliminary finding by the ACS, the ADA carried out a similar consultative function.

Under the new scheme, domestic industry or foreign exporters may appeal against a final finding, but the appeal entails a review of the interpretation of existing information only, with no further investigation. The TMRO conducts the review and draws on the resources of the Department of Industry, Science and Technology (DIST). Appeals must be lodged within 30 days following publication of the final finding.

In addition to conducting the final finding appeal, the office of the TMRO will also review the rejection of applications for dumping and/or countervailing measures at the end of the 20 day screening period, and also the termination of investigations after the preliminary investigation period.

The Government repealed the legislative requirement that companies wishing to have a complaint investigated must have at least 25 per cent local content in the product in question. The other screening requirements have been retained — complainants need to demonstrate that they are a local industry producing like goods, undertake a substantial process of manufacture in Australia, and are supported by the majority of other local producers of the good or goods. The

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[2] Information provided by ADA.

relaxation may enable some producers with high imported input content (for example, producers of certain finished textiles) — previously excluded by the local content requirement — to initiate action against competing imports of finished goods.

Anti-dumping and countervailing action in Australia continues to be subject to a five year sunset clause, with reviews undertaken prior to the expiry date, if there is a request for the action to continue.

The Government's scheduled review of anti-dumping and countervailing regulation under the Competition Principles Agreement has been postponed to allow for full implementation of the new arrangements. The review of the scheme will provide an opportunity to consider such questions as:

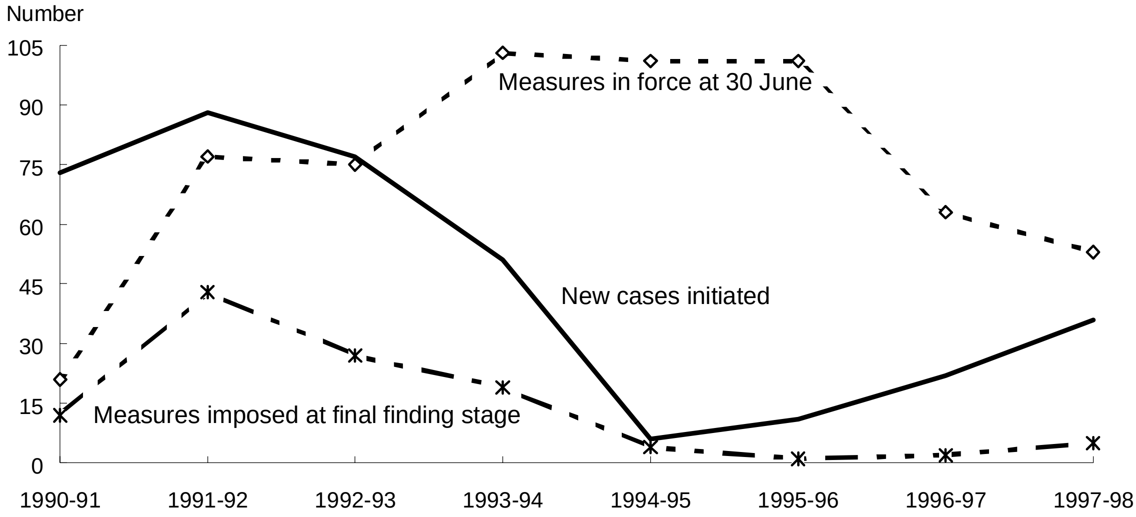
- Does the shorter investigation period provide sufficient time for a thorough examination of the issues?
- Are there adequate opportunities for all parties to defend their interests?
- While the abolition of the ADA has eliminated some duplication, have there been any implications for the quality/rigour of the investigation?
- Has the TMRO been given sufficient time and resources to conduct appeals and reviews effectively and is it appropriate that the TMRO be restricted only to reviewing the interpretation of information collected by ACS?
- Has the new 'simpler and faster' system resulted in an increase in initiations and/or measures imposed?
- Are the new processes consistent with WTO Agreements?

Anti-dumping and countervailing activity in 1997-98

The number of Australian cases reported as initiated increased from 22 in 1996-97 to 36 in 1997-98. Initiations have almost doubled in each of the past three years. Despite this, the number of initiations still remains well below the levels observed in the early 1990s (figure 4.2 and table 4.4).

It remains to be seen whether the upward trend will continue under the new system. However, the simpler and faster processes and the relaxation of the local content requirement would suggest (economic conditions and other factors being equal) the possibility of increased initiations in future years.

Figure 4.2 **Anti-dumping and countervailing activity,[a] 1990-91 to 1997-98**



a A measure or case is counted as one commodity from one economy. If multiple economies are involved, they are counted as separate actions.

Source: ACS and Commission estimates.

The reduction in measures in force as at 30 June 1998 (figure 4.2) predominantly reflects expiry of measures after the 5 year sunset period for which no applications for extensions were lodged. Furthermore, dumping measures were removed on blood collection packs as the sole Australian manufacturer ceased production.

The increase in cases initiated in 1997-98 was largely due to three single commodity initiations which involved four or more economies (table 4.2). Despite the steady increase in initiations over the past three years, the number of measures imposed at the final finding stage has remained low (figure 4.2).

Table 4.2 **New Australian anti-dumping and countervailing initiations[a] in 1997-98**

Commodity	*Economy*
Coated wood-free paper in sheets	Austria, Belgium/Luxembourg, Finland, France, Germany, Indonesia, Italy, Japan, Republic of Korea, Netherlands, South Africa, Sweden, Switzerland, Taiwan
Cotton blankets	China
Clear float glass	Indonesia
Picture frames	China
Polymeric plasticisers	United Kingdom
Polystyrene resin	Hong Kong, Republic of Korea, Singapore, Taiwan
Polyvinyl chloride homopolymer resin	Germany, Hungary, India, Indonesia, Israel, Netherlands, United Arab Emirates/Iran[b]
Tubeless steel remountable rims	Canada, South Africa[c]
Wound/skin closure strips	France, Germany, United States

a Complaints formally initiated by industry. Initiations are defined as one commodity from one economy. **b** Counted as two initiations by ACS. **c** Initiations for dumping and subsidisation.

Source: Information provided by ACS.

Industry incidence

The initiations for 1997-98 are dominated by industries in the paper and paper products and the chemical and petroleum products subdivisions (table 4.3). For both industry subdivisions, initiations involved single commodities, but related to imports from a number of economies (table 4.2). Over the past six years, these two subdivisions together with miscellaneous manufacturing have accounted for over 70 per cent of new cases.

Under the new legislation, initiations may increase from certain industries characterised by a high proportion of imported inputs in the production process (for example, certain textile industries), due to the relaxation of the 25 per cent local content requirement.

Table 4.3 **Anti-dumping and countervailing cases,[a] by industry, 1992-93 to 1997-98**

Industry[b]	*1992 -93*	*1993 -94*	*1994 -95*	*1995 -96*	*1996 -97*	*1997 -98*	*Six-year period* Total	*Six-year period* Per cent of total[c]
Food and beverages	10	–	2	–	–	–	12	6
Textiles	2	10	–	–	–	1	13	6
Paper, paper products	9	–	–	–	–	14	23	11
Metallic minerals	–	–	–	–	–	–	–	–
Chemical and petroleum products	18	16	2	5	11	13	65	32
Non-metallic mineral products	–	4	–	–	2	1	7	3
Metal products manufacturing	3	4	1	2	–	3	13	6
Transport equipment	1	–	–	–	–	–	1	–
Machinery and equipment	2	4	1	3	1	–	11	5
Miscellaneous Manufacturing	32	13	–	1	8	4	58	29
Total	**77**	**51**	**6**	**11**	**22**	**36**	**203**	**100**

- Nil. [a] Complaints formally initiated by industry. Cases are defined as one commodity from one economy. Cases where dumping and subsidisation are alleged for the same economy and commodity are counted as two distinct initiations. [b] Based on Australian and New Zealand Standard Industry Classification subdivisions. [c] The sum of the components does not add to the total due to rounding.

Source: Information provided by ACS.

Country incidence

Over the six years to 1997-98, Australian firms have initiated anti-dumping and countervailing cases against firms from a range of economies (table 4.4). The trading regions which have had the highest incidence of initiations against them over this period are Asia and Western Europe, together accounting for 75 per cent of total initiations. In 1997-98, initiations against these two regions accounted, respectively, for 39 per cent and 36 per cent of new initiations.

Relative to import shares, the number of initiations against Australia's trading partners in North America and Western Europe have been much lower than against economies in the Asian region. The Asian region accounted for more than a third of Australia's merchandise imports in 1997-98 (ABS 1998a), but since 1992-93 has been subject to almost half of total initiations (table 4.4). An exception within this region is Japan, which together with the United States has consistently had the lowest incidence of initiations relative to its import share.

There have been no Australian initiations against imports from New Zealand since July 1990, when the two countries agreed to eliminate anti-dumping and countervailing actions in trans-Tasman trade under changes arising from the Closer Economic Relations Agreement. Since then, anti-competitive conduct in trans-Tasman trade has been covered by competition laws under the Australian *Trade Practices Act 1974* and the New Zealand *Commerce Act 1986*.

International Trends

Australia accounted for 18 (8 per cent) of the 224 anti-dumping and countervailing cases initiated internationally in 1996 (the latest year for which comparable data are available) (table 4.5). South Africa, the European Union (EU), Argentina, the United States and India were the largest initiators of anti-dumping and countervailing actions.

In 1996, four economies together accounted for nearly three quarters of all measures in force — the United States (37 per cent), the European Union (15 per cent), Mexico (10 per cent) and Canada (10 per cent). Australia accounted for 6 per cent of measures in force internationally, down from 11 per cent in 1995. Relative to its share of world trade (less than one per cent), Australia continues to be one of the most frequent users of anti-dumping and countervailing measures.

The industry pattern of anti-dumping and countervailing activity continues to be similar in most countries, with the chemicals or metals industries being the dominant source of initiations. Measures against steel products are particularly common in the United States and Canada. Chemicals continue to figure prominently in the EU's list of measures.

Table 4.4 **Australian initiations of anti-dumping and countervailing cases, by trading region and economy,[a] 1992-93 to 1997-98**

Region/economy	*1992-93*	*1993-94*	*1994-95*	*1995-96*	*1996-97*	*1997-98*	*Six-year period* Total	*Per cent*[b]
North America	***5***	***2***	***0***	***1***	***1***	***2***	***11***	***5***
Canada	2	–	–	–	–	1	3	1
United States	3	2	–	1	1	1	8	4
Western Europe	***17***	***11***	***2***	***3***	***7***	***14***	***54***	***27***
Austria	1	1	–	–	–	1	3	1
Belgium/Lux	3	–	–	1	–	1	5	2
Finland	2	–	–	–	–	1	3	1
France	3	1	–	–	–	2	6	3
Germany	5	1	–	–	3	3	12	6
Italy	1	2	2	–	–	1	6	3
Netherlands	1	3	–	–	1	2	7	3
Spain	–	1	–	–	1	–	2	1
Sweden	–	–	–	–	2	1	3	1
Switzerland	–	–	–	–	–	1	1	–
UK	1	2	–	2	–	1	6	3
Asia	***41***	***27***	***2***	***5***	***9***	***13***	***97***	***48***
China	3	2	1	1	3	2	12	6
Hong Kong	3	2	–	–	–	1	6	3
India	4	–	–	–	1	1	6	3
Indonesia	5	1	1	–	1	3	11	5
Japan	1	2	-	–	–	1	4	2
South Korea	6	5	–	2	–	2	15	7
Malaysia	5	3	–	1	1	–	10	5
Singapore	5	6	–	–	–	1	12	6
Thailand	6	1	–	1	1	–	9	4
Taiwan	3	5	–	–	2	2	12	6
Other	***14***	***11***	***2***	***2***	***5***	***7***	***41***	***20***
South Africa	3	6	2	2	–	3	16	8
Other	11	5	–	–	5	4	25	12
Total	**77**	**51**	**6**	**11**	**22**	**36**	**203**	**100**

– Nil. [a] Cases are defined as one commodity from one economy. Cases where dumping and subsidisation are alleged for the same economy and commodity are counted as two distinct initiations. [b] The sum of the percentages for the individual economies may not add to the regional totals due to rounding.

Source: Information provided by ACS.

Table 4.5 **International anti-dumping and countervailing actions, 1995 and 1996[a][b]**

Country	*Initiation*		*Provisional measures*		*Definitive duties*		*Price undertakings*		*Measures in force at 31 December*		*Per cent of total measures in force*	
	1995	*1996*	*1995*	*1996*	*1995*	*1996*	*1995*	*1996*	*1995*	*1996*	*1995*	*1996*
US	15	23	23	15	38	14	0	1	375	378	42	37
EU	33	24	25	11	19	26	3	6	161	155	18	15
Mexico	1	3	19	3	10	5	6	0	na	106	na	10
Canada	12	5	8	9	28	0	0	0	100	101	11	10
Australia	4	18	2	5	1	0	0	1	101	60	11	6
Turkey	0	0	0	0	11	0	0	0	38	37	4	4
Argentina	1	24	4	4	2	19	1	2	na	31	na	3
Brazil	5	17	11	1	8	6	0	0	27	31	3	3
South Africa	18	30	9	9	2	8	0	0	15	31	2	3
New Zealand	12	8	1	3	4	4	0	0	26	29	3	3
India	5	20	2	5	7	0	0	0	13	15	1	1
South Korea	4	13	3	9	0	5	0	1	8	14	1	1
12 WTO Members	**110**	**185**	**107**	**74**	**130**	**87**	**10**	**11**	**864**	**988**	**-**	**-**
All WTO Members	**141**	**224**	**125**	**92**	**148**	**93**	**10**	**11**	**896**	**1028**	**100**	**100**

na not available. **a** The reporting period covers 1 January to 31 December of each year. **b** The sum of the components does not add to the totals due to missing notifications.

Source: WTO (1996) and (1997).

4.2 Issues from the WTO Trade Policy Review of Australia

The WTO recently completed its third Trade Policy Review of Australia. In the latest report, the WTO Secretariat acknowledged the efforts of successive Australian Governments in continuing unilateral trade liberalisation and structural reform programs. The report noted that Australia has been successful in meeting its Uruguay Round commitments by converting all remaining quantitative restrictions in agriculture to tariffs and by reducing export subsidies. Reductions in subsidies, the introduction of a national competition policy and deregulation and privatisation of Australian industry were judged to have improved significantly the ability of Australian industry to compete successfully on the international market (WTO 1998b).

The Trade Policy Review Report also highlighted several areas for further reform which may have implications for Australia's future competitiveness and trade relationships.

While levels of industry assistance have generally fallen to low levels, assistance remains very high for a few industries, most notably for milk production within the agricultural sector and for the PMV and TCF industries within the manufacturing sector. These activities continue to receive assistance many times higher than the industry average (see chapter 3).

Commenting on several recent developments, such as the tariff pause for the PMV and TCF industries and the Government's recent industry policy statement *Investing for Growth*, the WTO (1998b, p. x) made the observation that:

> The Government may be adopting a more ambivalent attitude to unilateral trade liberalisation and the provision of assistance to industry, perhaps reflecting its increased susceptibility to pressures from certain interest groups.

With regard to the tariff pause in the PMV and TCF industries the WTO (1998b, p. x) also noted that:

> In light of the positive adjustment that has taken place in PMV and TCF industries, largely in response to tariff reductions since 1991, the Government may be providing the wrong signal to these two industries and to the manufacturing sector in general.

The extent to which Australia's relatively strict quarantine measures may provide additional assistance to the agricultural sector was also questioned by the WTO. Quarantine issues are discussed in the following section.

The WTO's comments on the possible dangers of a shorter investigation period for dumping investigations were noted in the previous section.

The WTO acknowledged that significant reforms have taken place in financial and telecommunications services, and to a lesser extent in the air transport services sector, but noted that other areas such as maritime, port services and coastal trade regulations have had little or no reform to date (see chapter 5).

4.3 WTO negotiations on agriculture

The next multilateral trade negotiations for agriculture are scheduled to commence in late 1999. The negotiations are to build on and advance the principles which were developed as part of the WTO Agreement on Agriculture, negotiated under the Uruguay Round. The Agreement on Agriculture is to be fully implemented by the end of 2000 for developed countries and 2005 for developing countries.

The objective of the new multilateral negotiations is to generate benefits to WTO members by removing impediments to trade and reducing the incidence of measures that distort markets. The new round of negotiations represents an opportunity for Australia to benefit from expansion of its export markets through further multilateral reductions in domestic support policies, export subsidies and quantitative restrictions.

The importance of the Uruguay Round and the new negotiations

The WTO Agreement on Agriculture put in place a negotiating framework under which distortions to trade could be addressed in a multilateral context. Prior to the Uruguay Round, agriculture had been practically excluded from multilateral negotiations through a number of special clauses and waivers.

The main advances from the agreement were in setting minimum levels of access to restricted markets, virtual abolition of all border measures except tariffs and tariff quotas, universal binding of tariff rates, and reductions in export and other subsidies. However, the actual reductions in export subsidies and in the 'tariff equivalents' of other trade barriers were, in most cases, small. This is because the base periods which were adopted reflected abnormally high levels of support or protection, and the structure of commodity groupings enabled increases in domestic support for some commodities (ABARE 1997). The next round of negotiations should seek to ensure further significant reductions in trade barriers and subsidies in the shortest time possible.

Potential negotiations on tariff quotas (TQs) is an area of particular interest for Australian agriculture. TQs improve access to restricted markets by allowing a lower rate than the general tariff rate on a specified quantity of imports. Ideally, general tariff rates should be reduced to the point where TQs would no longer be required to improve market access. Failing this, the next negotiations on agriculture provide an opportunity to increase the quantity of imports allowed into restricted markets under TQs.

Australia is in a relatively strong position going into the next negotiations on agriculture as its current levels of protection are quite low after implementing reductions agreed to under the Uruguay Round. However, Australia's statutory marketing arrangements and quarantine restrictions might come under notice during the new negotiations. So too might pockets of high assistance such as for the dairy industry (see chapter 3).

Statutory marketing boards

Sole national exporting and marketing bodies may come under scrutiny at the next round of negotiations. The United States has been a longstanding advocate of limiting the activities of such 'monopoly' bodies (ABARE 1997). Australia has statutory marketing agencies for key agricultural crops such as wheat, rice and sugar.

Reform of statutory marketing arrangements to end compulsory acquisition, production controls and discriminatory pricing arrangements would improve resource use and benefit consumers. In 1993-94, the cost to consumers of supporting agricultural products via domestic pricing arrangements was estimated at more than $500 million (PC 1996).

The WTO recently noted that the Government is committed to reviewing the distribution and marketing arrangements for agricultural products under the Competition Principles Agreement (1995). State and Commonwealth Governments have agreed to restructure the statutory marketing boards to reflect competition policy rules better (WTO 1998b). Recent changes which have been implemented include the restructure and commercialisation of the Queensland Sugar Corporation (QSC) and the Australian Meat and Livestock Corporation (AMLC). From 1 July 1997, raw sugar produced in Queensland has been sold domestically at export parity prices (see chapter 3).

Quarantine

Australia may be required to justify its quarantine system at the next negotiations. This may include justification of specific restrictions, such as those for pigmeat imports.

In October 1997, the Government lifted bans on imports of uncooked pigmeat from Denmark and of cooked pigmeat from Canada. Bans on frozen, uncooked pigmeat from Canada were lifted in 1990. While some uncooked product from New Zealand and cooked, canned hams, can also be imported, Australia maintains a quarantine ban on pigmeat imports from all other countries.

The Government has initiated a generic import risk analysis of quarantine restrictions on pigmeat imports. The assessment is to be conducted under new guidelines designed to ensure that such analyses are completed in a transparent and consistent manner. These new arrangements are in line with the recommendations made by the Nairn Report into Australia Quarantine released in October 1996.

The WTO (1998b) questioned the extent to which Australia's relatively strict quarantine measures may provide assistance to the agricultural sector. A WTO Panel recently found that Australia's ban on uncooked salmon imports was inconsistent with the Sanitary and Phytosanitary (SPS) Agreement (box 4.1), and that the ban nullified or impaired benefits accruing to Canada under the WTO. The finding has been appealed.

Box 4.1 **The SPS Agreement**

Under the Sanitary and Phytosanitary (SPS) Agreement (1994), countries have the right to apply quarantine measures which they deem necessary to keep the risk of disease at an acceptably low level. To help ensure that such measures are scientifically rather than trade based, measures may be challenged via the WTO's Dispute Settlement procedures. The SPS Agreement is scheduled to be reviewed in 2000.

The WTO (1998b) also questioned the length of time and uncertainty involved in gaining access to the Australian market through the quarantine system. It noted that recent decisions by the Government to lift bans on cooked poultry imports from the United States, Denmark and Thailand, and on pigmeat from Denmark and Canada, were based on submissions made over a decade ago.

Pigmeat safeguards

The Commonwealth Government has asked the Productivity Commission to inquire and report on whether safeguard action, in accordance with the WTO Agreement on Safeguards, is warranted against imports of certain frozen pigmeat. The Commission has also been asked to report on the factors affecting the profitability and competitiveness of the domestic pig farming and pigmeat processing industries. The inquiry is to be completed by 13 November 1998.

Article XIX of the General Agreement on Tariffs and Trade (1994) allows for safeguard action against imports of particular products which are deemed to be causing or threatening to cause serious injury to an industry. The Uruguay Round resulted in interpretation and elaboration of Article XIX, embodied in a new WTO Agreement on Safeguards.

Safeguard action is intended to provide temporary assistance for industries to adjust to increased competition from imports. Safeguard measures must be sufficient only to remedy the extent of injury attributable to the imports and must be liberalised progressively in order to promote industry adjustment. There is no requirement under the WTO safeguard provisions to demonstrate that imports are dumped or subsidised.

As a member of the WTO, Australia's safeguard investigations and measures must comply with the rules and criteria embodied in the WTO Agreement, including a requirement for public hearings and admittance of evidence for consideration of the public interest. The general procedures which the Commission must follow, and the questions it must consider, in order to determine whether safeguard action is warranted are set out in a Commonwealth of Australia Special Gazette (Commonwealth Gazette 1998).

Specifically, the Commission is requested to:

a) determine whether safeguard measures (which may be in the form of a quota, a tariff quota, or an increased level of tariff) are justified under the WTO Agreement; and, if they are justified

b) consider what measures would be necessary to prevent or remedy serious injury and to facilitate adjustment; as well as

c) consider whether, having regard to the Government's requirements for assessing the impact of regulation which affects business, those measures should be implemented.

Part (c), in effect, requires the Commission to consider whether application of a safeguard measure would be in the public interest.

4.4 APEC sectoral liberalisation

In the Bogor Declaration of 1994, APEC members made a commitment to achieve the goal of trade and investment liberalisation in Asia Pacific by 2010 for developed countries and by 2020 for developing countries. In 1995, members adopted the Osaka Action Agenda and agreed to develop and regularly update Individual Action Plans (IAPs) which would provide details of specific trade and investment liberalisation commitments.

Early voluntary sectoral liberalisation

In November 1996, APEC Leaders instructed Ministers to identify sectors where early (that is, before the agreed goals of 2010 and 2020) sectoral liberalisation would have a positive impact on trade, investment and economic growth in the individual APEC economies as well as in the region and to submit recommendations on how this could be achieved. Early voluntary sectoral liberalisation (EVSL) is a process to run concurrently with, but separate from, the process of IAPs.

By August 1997, member economies had submitted 62 nominations for EVSL covering more than 30 sectors. At the Ministerial Meeting in November 1997, a subset of 15 proposals clearly emerged as having the most support.

The 15 proposals were divided into two tiers. The first tier comprised nine sectors which were identified for fast-track treatment — forest products, fish and fish products, toys, gems and jewellery, chemicals, medical equipment and instruments, environmental goods and services, energy and telecommunications.[3] The remaining six sectors in the second tier required more preparatory work — oilseeds and oilseed products, food, rubber, fertilisers, automotive and civil aircraft.[4] The measures covered in each proposal included trade liberalisation, facilitation and economic and technical cooperation.

APEC Ministers reviewed progress at their June 1998 meeting in Kuching, Malaysia. Senior Officials met in September and Trade Ministers are to consider the final arrangements at their November meeting with a view to commencing implementation in 1999.

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[3] This sectoral proposal comprises the Telecommunications Mutual Recognition Agreement which has been finalised. The objective of the agreement is to achieve conformity assessment of equipment subject to network terminal attachment or other telecommunications regulation.

[4] Three of the fifteen sectors were nominated by Australia — chemicals and energy in the first tier and food in the second.

The process of EVSL represents an opportunity, outside WTO negotiations, for Australia to advance its trade liberalisation objectives and to develop stronger regional ties. Through the process, Australia has been able to address relatively sensitive areas of protection in the APEC region in an open forum which includes its major trading partners. However, the process needs to address several issues if it is to achieve its trade liberalisation objectives most effectively.

Flexibility in achieving EVSL commitments

At Kuching, in order to enable finalisation of the sectoral arrangements that would maximise participation, Ministers agreed that flexibility would be required to deal with product-specific concerns raised by individual economies in each sector (APEC 1998). Such flexibility would generally be in the form of longer implementation periods. Participation in the nine fast track sectors and all three measures (trade liberalisation, facilitation and economic and technical cooperation) in each sector was seen as essential. Other proposed forms of flexibility (such as choice of products within sectors) were to take into account the broader goal of maximising mutual benefits, and the need to maintain the balance of interests (APEC 1998). It remains to be seen how these principles will be reflected in a final agreement.

Extending liberalisation to include non-tariff measures

Recent analysis shows that it is important for the EVSL commitments to include non-tariff measures (including subsidies) as well as tariff protection (Dee, Hardin and Schuele 1998). Reviews of non-tariff measures (including production and export subsidies) are currently in progress for a majority of the proposals. These studies generally must be completed and ratified by APEC members before such measures can be put forward for liberalisation. There would be benefits in completing this process and broadening the scope of sectoral liberalisation as soon as possible.

Comprehensive coverage

Broadening, rather than restricting, the product and sectoral coverage of the EVSL proposals may be necessary for achieving the broader objectives of EVSL.

Implementation of EVSL proposals which contain predominantly upstream sectors could lead to losses in income (Dee et. al. 1998). This could occur if liberalised resources move into more highly protected downstream processing as a consequence of cheaper imported inputs. Some proposals — for example, those relating to chemicals — contain nominations concentrated at the upstream end of the processing chain. However, other proposals, such as those for forestry products and fish and fish products, broadly cover both upstream and downstream processing. Implementation of these proposals could be expected to lead to gains in income for the APEC region.

The sectoral approach in EVSL makes it difficult to trade off the liberalisation of high and low protection sectors. One way to introduce such a tradeoff would be by taking the EVSL nominations into the WTO forum, to use as negotiating coin for further tradeoffs within that forum.

4.5 Review of 'nuisance' tariffs

The Government has identified lowering business input costs as a key area for future reform in industry policy. In this context, DIST is to review all tariff items between 3 and 5 per cent which offer little or no protective benefit to Australian industry (Moore 1998e). In some instances, these tariffs constitute 'negative' assistance where industries pay tariffs on inputs, but have end products which compete with imports that enter Australia duty free (Moore 1998c). As part of the review process, a preliminary list of over 2000 tariff items identified as 'nuisance' tariffs and individually raising little revenue was compiled and made available to Australian industry for comment by late October 1998.

The review of 'nuisance' tariffs follows recent decisions by the Government to remove tariffs on imported business inputs in the information technology and telecommunications sectors and on medical and scientific equipment. The decision on medical and scientific equipment was in response to a Commission recommendation in the Report on *Medical and Scientific Industries* (IC 1996c).

Any decision to eliminate protection should be considered in an economy-wide context. As discussed in the previous section in relation to the APEC EVSL process, failure to consider and allow for linkages in the production chain could increase disparities in assistance and lead to some adverse resource allocation effects. However, any such effects associated with the elimination of 'nuisance' tariffs or tariffs on specific inputs are unlikely to be very large in an environment of generally low tariffs. Furthermore, to the extent that the elimination of these tariffs is part of a broader policy of removing all remaining tariff assistance over time, as recommended by the Commission in its report on the *Stocktake of Progress in Microeconomic Reform* (PC 1996), any negative resource allocation effects will be minimised.

5 International trade in services — policy developments and issues

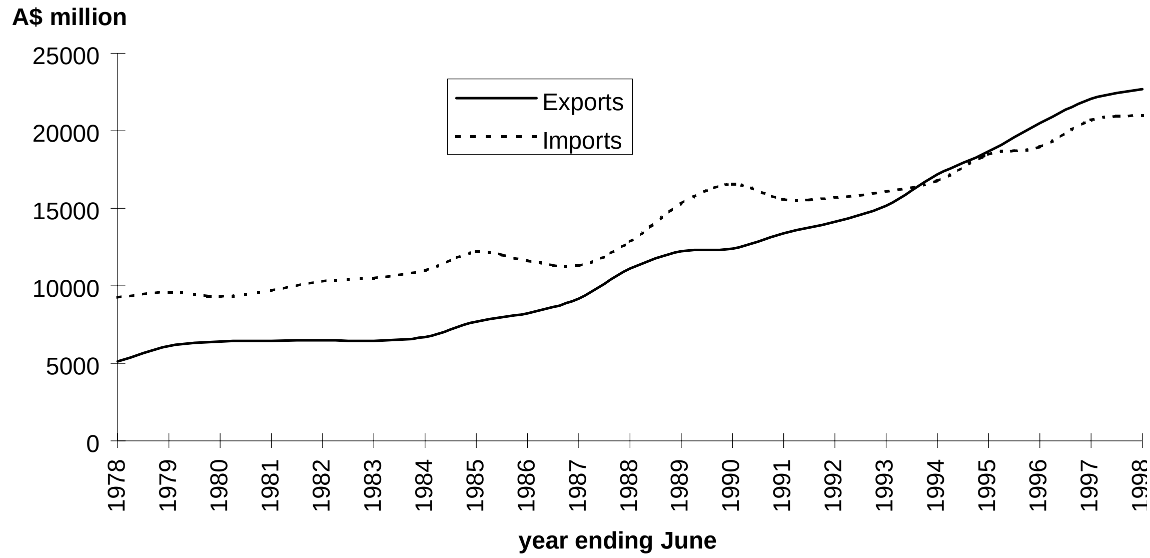
Trade in services is an important component of Australian and global trade. While services trade is growing rapidly — driven by growth in goods trade, policies to open markets to new service suppliers, and technological developments which are making a wider range of services tradeable — it is still subject to a wide range of restrictions that may protect existing suppliers at the expense of consumers. Over the past year, Australia has taken some steps, both unilaterally and multilaterally, to liberalise trade in services.

Legislation affecting trade in services is scheduled for review over the next few years. In addition, the next round of multilateral WTO services trade negotiations is scheduled for the year 2000, and governments are considering responses to matters such as the growth in electronic commerce. The policy setting for international trade in services could undergo some further major changes over the next few years.

5.1 Rapid growth and complex issues

Services account for a significant share of Australia's international trade. In 1997-98, they accounted for 20 per cent of Australia's total exports and 19 per cent of total imports. Over the past five years, exports of services have increased at an average annual rate of 9 per cent whereas imports of services have increased at a slower rate of 5 per cent. Australia has been a small net exporter of services over this period (figure 5.1).

Figure 5.1 **Australia's exports and imports of services 1977-78 to 1997-98**
constant 1989-90 prices



Data source: ABS Cat. no. 5302.0

International trade in services accounted for just over 20 per cent of the value of global trade in goods and services in 1996 (IMF 1997). The estimates for global and Australian trade understate the full significance of trade in services, as they include only the value of services traded across borders (as in international transport) or by the temporary movement of people (as in tourism or education). They do not include the value of services traded via a foreign supplier establishing a commercial presence in a market and supplying services directly to consumers — although royalties, license fees and repatriated profits would generally be included. The commercial presence mode of service trade is generally included in international (including WTO) definitions of trade in services. It has been estimated to be more important than cross-border trade, and its inclusion could more than double the value of international trade in services (OECD 1998).

The growth in international services trade partly reflects the growth in goods trade — as more goods are moved around the world, the demand for associated services such as transport, insurance and other financial services also increases. It also reflects a range of other developments, such as technological progress which has made trade in some services feasible via media such as the internet, as well as foreign investment and competition policy reforms which have allowed foreign suppliers to enter service markets which previously were tightly regulated.

In reviewing policy developments and issues for international trade in services it is necessary to take account of links with policies covering foreign direct investment, competition, intellectual property and electronic commerce. Each of these raise some complex and interrelated issues. They have been identified by the WTO as key issues for future world trade liberalisation debate (WTO 1996 and 1997).

Services trade and foreign direct investment

Ongoing direct contact with consumers is important for services such as communications, financial, retailing and various business and professional services. This means that establishing a commercial presence via foreign direct investment (FDI) may be the best way for a foreign service supplier to enter the market. Restrictions on FDI can therefore have an impact on services trade. While many economies have liberalised their FDI regimes in recent years, most still apply some restrictions, particularly in key services industries such as communications, transport and financial services (Hardin and Holmes 1997).

Recognising the importance of FDI restrictions as a potential barrier to services trade, WTO Members have explicitly included establishment of commercial presence in the coverage of the General Agreement on Trade in Services (GATS). However, many Members have either not scheduled market access commitments for some key service industries or have indicated an intention to maintain FDI restrictions.

Services trade and competition policy

Attempts by foreign service suppliers to obtain direct access to markets can also be hindered by domestic competition policies. For example, exemptions or special treatment provided to local suppliers may place them in a favourable position relative to potential foreign (and other domestic) competitors. Failure to deal with anti-competitive practices may also limit the opportunities for foreign suppliers to enter service markets. For example, without an adequate regulatory framework for access to the 'bottleneck' parts of the telecommunications network, new suppliers — local or foreign — may not enter the market, thereby depriving domestic consumers of the potential benefits of wider choice and lower prices.

Several competition policy initiatives in the Australian economy over the past few years have significant implications for international trade in services — most notably reforms to the telecommunications and financial sectors. The regulatory arrangements for several service industries are also scheduled for review as part of the Commonwealth's national competition policy commitments (see section 5.3).

As global markets become more integrated, via both trade and investment flows, international competition policy issues are becoming more important and complex. International co-operation may be necessary to ensure effective and efficient control of anti-competitive behaviour by multinational firms. Some competition policy issues are dealt with in the WTO Agreement on Basic Telecommunications, which came into force in February 1998 (see section 5.2). However, many difficult issues still have to be resolved for this and other traded service industries, such as the professions, maritime transport and international air services.

Services trade and intellectual property rights

The nature and degree of protection of intellectual property rights can influence international trade in services, particularly for services such as publishing, broadcasting and film, sound recording, entertainment and business services. For example, restrictions on parallel imports of goods containing intellectual property (such as books, sound recordings and films), while having the stated intention of protecting intellectual property and providing incentives to publish and produce original work, will reduce competition and trade, and assist local suppliers in the same way as other restrictions on imports.

Balancing the interests of consumers, who may benefit from more competition in the supply of services containing intellectual property, and suppliers, who seek to obtain a return on the investment they make in intellectual property, is a challenge for policy makers. Growth in the sale and delivery of goods and services via the internet is intensifying the challenge. The recent Joint Committee of Public Accounts and Audit report on internet commerce noted concerns about whether the *Copyright Act 1968* could provide adequate protection and incentives (JCPAA 1998). The Government has proposed changes to the Act to address the concerns (see section 5.2).

Services trade and electronic commerce

The development of electronic commerce is creating a vast range of new opportunities for international trade in services. According to the Australian Bureau of Statistics around 85 per cent of Australian orders for, or purchases of, goods or services over the internet in the year to February 1998 were with overseas suppliers (ABS 1998b). A wide range of business, professional and retail trade services can be supplied via the internet. For example, a growing number of banks are supplying financial services via the internet, which provides a cost-effective alternative to more usual modes of service delivery. According to estimates for the United States, the cost of an average payment transaction on the internet is as low as one US cent, compared with 27 cents for an automatic teller machine, 54 cents for a telephone banking service and US$1.07 for a transaction conducted via a traditional bank branch (Kono et al 1997). Communication services also could be supplied more efficiently via the internet. The WTO estimates that sending a 42 page document from New York to Tokyo by air mail would cost US$7.40, and take 5 days, compared with 10 cents and 2 minutes for sending it by internet email (Bacchetta et al 1998).

Policies affecting internet access and internet transactions will have an impact on the growth in the use of this important vehicle for international trade in goods and services. Progress in recent years in opening access to telecommunications networks should help to foster the development of electronic commerce, but many further issues are to be resolved (see section 5.3).

5.2 Policy developments in international trade in services

The complexity of the issues involved in identifying and assessing restrictions on trade in services is illustrated in this section. Some of the other services trade issues to be considered over the next few years are discussed in the final section and are likely to pose similar challenges for policy makers.

The major multilateral policy initiative affecting international trade in services in recent years was the signing of the WTO General Agreement on Trade in Services (GATS), which came into effect in January 1995. The structure of the GATS and the negotiations for two key sectors — basic telecommunications and financial services — were discussed in previous Commission reports (IC 1996b and 1997f).

Beyond the WTO forum, Australia has continued to participate actively in OECD and APEC initiatives designed to liberalise international trade in services or at least to make restrictions more transparent. Several important unilateral policies with implications for international services trade have also been introduced or proposed over the past year.

Financial services

A major international policy development over the past year was the completion of WTO negotiations on financial services in December 1997. These negotiations will form the basis for the financial services agreement when it comes into effect no later than 1 March 1999. As a party to the agreement, Australia took the opportunity to amend its commitments to reflect some important financial services liberalisation undertaken as part of implementing the recommendations of the 1997 Financial System Inquiry. Australia has a relatively open financial services sector, but still applies several restrictions on trade in financial services.

At the completion of the 1997 negotiations, 102 WTO Members made commitments in financial services. The commitments contain significant improvements over those made at the end of the Uruguay Round. These improvements include relaxation of foreign ownership restrictions of domestic financial institutions, lifting limits on the juridical form of commercial presence and permitting the expansion of existing operations (WTO 1998a). These liberalising commitments were made despite the emerging Asian economic problems.

The GATS framework requires each Member to offer a schedule of commitments outlining how they intend to apply market access and national treatment disciplines. Where a Member intends to retain a restriction on market access or some measure which violates national treatment, it lists the measure in its schedule. Members also have the flexibility not to apply market access and national treatment disciplines to any service, by simply not including it in the schedule of commitments.

At the end of the 1997 negotiations, Australia added eight restrictions to its schedule covering market access and national treatment commitments, removed two restrictions and made minor amendments to five restrictions. Australia added Comcare's monopoly on the provision of workers' compensation insurance to Commonwealth Government employers, four restrictions on State and Territory central borrowing and investment operations, two restrictions on the operations of the Trust Bank of Tasmania, and a restriction on State and Territory guarantees to State-controlled banks.[1] Some of these are discussed further below.

Australia removed from its schedule of commitments a restriction on foreigners acquiring any of the four major banks. In 1997, the Government removed the blanket prohibition on the purchase of any of the four major banks. Any proposed foreign takeover or acquisition of a major bank will be assessed, like any other proposed foreign takeover or acquisition, on a case by case basis in accordance with the *Foreign Acquisition and Takeovers Act 1975*. However, a specific foreign investment policy condition continues to apply to the four major banks. In making assessments on acquisitions or takeovers, the Government will apply the principle

[1] Many Australian commitments contain more than one restriction and cover a number of Australian jurisdictions (Commonwealth, States and Territories).

that any large-scale transfer of Australian ownership of the financial system would be contrary to the national interest (Costello 1997a).

Australia also removed restrictions on ownership and transactions of authorised money market dealers. The arrangements applying to authorised money market dealers were abolished in 1996 as part of domestic monetary policy reform. This restriction could have been removed at an earlier time. The GATS requires Members to inform the Council for Trade in Services promptly and at least annually of any changes to existing measures which significantly affect trade in services covered by its specific commitments (WTO 1994, OECD 1994 and Low 1995).

A most-favoured-nation (MFN) exemption on access to the Australian Stock Exchange was also removed.

Restriction on the provision of workers' compensation insurance

Australia scheduled a restriction on market access for the provision of workers' compensation insurance covering most Australian jurisdictions. Queensland and South Australian workers' compensation insurance is provided mainly by a public sector monopoly.[2] Comcare, a Commonwealth Government agency, has a monopoly over workers' compensation insurance provided to Commonwealth Government employers.[3] In New South Wales, Tasmania, Victoria and Western Australia, insurance companies providing workers' compensation insurance must be licensed by the respective State governments. The Victorian arrangements are scheduled incorrectly as a monopoly — private insurers are able to enter and exit the market. The requirements to be a licensed workers' compensation insurer vary between jurisdictions but include being authorised under the *Insurance Act 1973* (Commonwealth), being financially viable and committing sufficient resources to providing workers' compensation insurance. In some jurisdictions, the type of services that licensed insurance companies can provide is limited — for example, insurers may not be permitted to provide underwriting services. Licensed insurers are supervised by the relevant jurisdiction's regulator.

As part of National Competition Policy reforms, States and Territories are reviewing legislation that restricts competition. Legislation must be reformed unless it can be

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[2] In South Australia, claims managers (usually insurance companies) approved by the WorkCover Corporation of South Australia provide claims management services.

[3] The Government has announced that there will be private sector competition in the delivery of Comcare's claims management services. Comcare is expected to be the sole manager of claims until 1 January 2000 (Reith 1998).

demonstrated that the benefits of the restriction to the community outweigh the costs and the objectives can only be achieved by restricting competition.

Workers' compensation insurance premiums are paid by employers to cover their employees against work accidents. Governments are involved in workers' compensation to put in place arrangements which embody safety incentives and are fair to those who suffer work-related injury or illness, but which do not at the same time impose an unreasonable burden on either firms or taxpayers (IC 1994). Regulation seeks to ensure that funds will be available to meet scheme costs by insisting that employers insure their liability and that insurers have the ability to cover risks. While such arrangements are necessary, there may be scope for greater private sector involvement, especially in those jurisdictions with monopoly arrangements or other competitive restrictions.

Certain other restrictions on the provision of workers' compensation insurance are not included in Australia's GATS schedule. These are Comcare's monopoly over the provision of workers' compensation insurance to Australian Capital Territory Government employers and the licensing requirements that apply in the Australian Capital Territory and the Northern Territory. The New South Wales Joint Coal Board also has a legislated monopoly over the provision of workers' compensation insurance for the New South Wales coal mining industry (IC 1998).

Restrictions on borrowing and investing for Australian governments

Australia scheduled a restriction on market access for borrowing and investment services provided to Australian governments by their central borrowing authorities.[4] The commitment reflects the central borrowing authorities' monopoly over the provision of financial services to governments. Each Australian jurisdiction, with the exception of the Australian Capital Territory and the Commonwealth, is covered by this commitment.

Central borrowing authorities raise and manage debt for general government activities (such as building roads) and government trading enterprises (such as electricity utilities). They are also responsible for investing cash balances, providing financial advice and payment services. The liabilities of the central borrowing authorities are guaranteed by their respective governments.

Many debt raising and cash management services could be supplied by the private sector, provided that a government's cost of raising debt or the risk attached to

4 Australia's schedule also includes the Local Government Financing Authority in South Australia and the Queensland Government's fund manager, Queensland Investments Corporation.

government debt was not increased. In 1997-98, the Australian Capital Territory Government contracted part of its debt raising to the Commonwealth Bank, which arranged and managed a domestic retail bond issue (ACT Government 1998). Some of the Reserve Bank of Australia's (RBA) financial services — provision of bank accounts, payment and revenue collection processing, and financial information services — will also be open to competition. Commonwealth departments and agencies will be able to choose their provider of certain financial services from 1 July 1999 (Fahey 1998).

Licensing of banks

Australia scheduled a restriction on market access for the entry of banks and foreign bank branches. This restriction covers the requirement for a bank to be licensed as a locally incorporated subsidiary or as a foreign bank branch to provide banking services.

The practice of licensing deposit-taking services has changed recently with the implementation of recommendations from the 1997 Financial System Inquiry. A body corporate, including a non-operating holding company structure, seeking to accept deposits and carry on banking business is required to be an authorised deposit-taking institution (ADI).[5] Foreign bank branches are required to be an ADI to carry on banking business within Australia, but are prevented from accepting deposits of less than $250 000.[6] A foreign bank branch is required to be incorporated and recognised under the laws of the home country, and to receive the support of the home supervisor in the supervision of the branch. The new Australian Prudential Regulation Authority (APRA) licenses ADIs or subsidiary banks and foreign bank branches. These new arrangements are not yet reflected in Australia's schedule.

Many WTO Members require their financial service providers to be licensed. Wallis et al (1997) noted that entry requirements contribute to financial system stability and are a justified restriction on competition. The GATS permits Members to license financial service providers, provided that such licensing is non-discriminatory and not excessive in restricting trade in financial services. The GATS

[5] Deposit-taking institutions supervised by State and Territory governments, mainly building societies and credit unions, continue to be licensed by State and Territory financial regulators. The Commonwealth Government is negotiating with the States and Territories for their supervised deposit-taking institutions to be supervised in the same way as Commonwealth authorised deposit-taking institutions.

[6] A previous Industry Commission report discussed the deposit-taking restriction on foreign bank branches (IC 1997f).

establishes safeguards against domestic regulations being operated for industry protection purposes. At the same time it recognises the right of domestic regulators to impose minimum standards and conditions, which relate to qualification requirements and procedures, technical standards, licensing and authorisation requirements (OECD 1994).

International telecommunications services

The WTO Agreement on Basic Telecommunications came into effect on 5 February 1998. It has been estimated that the trade and investment liberalisation initiatives embodied in the agreement — which covers services such as voice telephony, telex and facsimile — could assist in realising cost savings in the order of 80 per cent for international phone calls over the next few years, from US$1 per minute on average to 20 cents per minute (OECD 1998).

From Australia's perspective, probably the main implication of the agreement is that it locks into a binding international commitment a range of domestic liberalisation and deregulation policies that have already been implemented. The agreement also restricts Australia's ability to introduce any new impediments to foreign suppliers entering the basic telecommunications market. New measures which limit market access or violate the national treatment principle in the GATS can be introduced only if there is compensation for all affected parties (IC 1997f).

The specific agreement covering basic telecommunications grew out of a recognition that the general GATS framework could not deal adequately with some of the impediments affecting telecommunications. For example, one of the most important constraints on access to telecommunications markets is a lack of effective regulation ensuring fair network interconnection. Recognising this, the agreement includes a reference paper on regulatory principles for telecommunications. Australia's regulation of anti-competitive behaviour and network access is compatible with the principles set out in the reference paper (IC 1997f).

While the agreement has addressed many issues affecting trade in telecommunications, there are still some further issues that require international co-operation. A key issue is international settlement rates — the rates charged by foreign network owners for completion services for international calls. These rates affect the price of outgoing international calls for Australians. In liberalised markets, settlement rates approach the underlying cost of the service. If that were not so, the Australian carrier could establish a presence in the foreign market (eg by leasing domestic capacity) and complete its own outgoing calls — a process known as 'bypass' (IC 1997b). However, in markets where bypass is not possible, settlement rates tend to be higher. Liberalisation of these markets is the best option for reducing the settlement rates, but an alternative would be for negotiators to try to reform the settlement system directly. This is likely to be difficult, given the rents that accrue to some countries from the current system, where settlement rates are commonly set in bilateral arrangements and vary across trading partners depending on the characteristics of the markets involved.

Setting different settlement rates for different trading partners violates the MFN principle in the GATS and could therefore be subject to challenge in the WTO. However, parties to the Agreement on Basic Telecommunications reached an understanding not to challenge each other's accounting rate systems. They further agreed to review the understanding no later than the commencement of the next round of services negotiations in the year 2000 (Low and Mattoo 1998).

International maritime transport services

Maritime transport services, like financial services and basic telecommunications, were singled out for continuing specific negotiations at the end of the Uruguay Round. While agreements have been finalised for the other two industries, the maritime negotiations have been suspended, to be re-convened as part of the year 2000 GATS negotiations.

Only 36 of the 132 WTO Members made market access and national treatment commitments for maritime transport by the end of the Uruguay Round. Australia made commitments, but several major trading economies including the United States and the European Union did not. The MFN clause, one of the major disciplines of the GATS, has been suspended for those Members which have not made commitments (Ruggiero 1998).

The suspension of the MFN discipline was prompted in part by the reluctance of Members to relinquish their right to take unilateral retaliatory action against trading partners who are perceived to be restricting trade. If a country is concerned only with ensuring that imports enter its market at lowest cost, then the MFN discipline should not be a problem because it means that consumers are free to buy from the cheapest source. However, if a country is concerned also about gaining improved market access for its exporters, the opportunity for retaliation against trading partners that restrict this access may be difficult to resist (Mattoo 1997). The fact that many governments have a direct stake in their domestic shipping lines adds to the difficulties of reaching a maritime transport services agreement.

The desire of governments to maintain some strategic control over market access, rather than unilaterally allowing open access on a MFN basis, also influences policy in other service industries such as international air transport, where bilateral agreements regulate market access, and telecommunications, where bilateral agreements still play a crucial role in the setting of international settlement rates.

Australia's GATS schedule includes market access and national treatment commitments for maritime transport. Australia lists one violation of national treatment. Under Part X of the *Trade Practices Act 1974,* Australian flag operators maintain the right to apply to have the Australian Competition and Consumer Commission (ACCC) examine whether liner shipping conference members or non-conference carriers are hindering Australian flag shipping — in particular, whether they prevent Australian shipping from engaging efficiently in the provision of outward liner cargo services. With respect to market access, Australia has listed its intention to maintain the requirement that shippers have a registered office in Australia.

Australia's GATS commitments do not cover other matters which may affect its international shipping services, such as restrictions on the participation of foreign flagged vessels in coastal shipping and the exemptions which liner shipping conferences receive from certain restrictive trade practices provisions in the *Trade Practices Act 1974*. However, these matters are to be reviewed as part of Australia's national competition policy and APEC commitments.

In its recent review of Australia's trade policies, the WTO noted that while major market opening had taken place in telecommunications and financial services markets and reforms have been implemented in air services and electricity and gas markets, other key service sectors such as maritime and port services are relatively untouched by the reform process (WTO 1998b).

Professional services

Recognising the potential for growth in trade in professional services and the widespread application of restrictions, both the WTO and OECD are continuing to work toward trade liberalisation for professional services. Major issues being addressed include mutual recognition of standards, restrictions on the movement of people, and the treatment of professions in national competition policies. While some progress has been made in addressing these issues — for example, the WTO has released guidelines on mutual recognition in the accounting profession — from Australia's perspective the main policy developments are at the national level. In 1996, Australia's competition laws were extended to the unincorporated sector, thus covering many of the professions for the first time. Over the next few years, several pieces of Commonwealth and State legislation affecting competition in various professions and occupations are scheduled for review (see section 5.3).

The OECD's Multilateral Agreement on Investment

Since 1995, Australia and other OECD members have been negotiating a Multilateral Agreement on Investment (MAI). The MAI is intended to be a legally binding agreement covering all sectors and all forms of foreign investment, including FDI, portfolio investment, real estate investment and rights under contract. It covers laws, regulations and administrative practices at all levels of government (OECD 1997).

Over the past year, negotiations have continued and the deadline for completion of the agreement has been extended to allow further discussion and consultation. The Australian Government has indicated that it will not make a binding commitment to the proposed MAI treaty until it has been subjected to the treaty-making processes established in 1996 (Treasury 1998). As part of this process, a Parliamentary Committee tabled its interim report on the MAI in June 1998.

The proposed MAI contains a set of principles or rules which signatories must adhere to, unless they specify exceptions (discussed below). The core principle in the MAI is non-discrimination. The non-discrimination principle is embodied in both the national treatment and most-favoured-nation rules. National treatment means that foreign investors and investments can be treated no less favourably than domestic investors and investments. The most-favoured-nation rule means that investors and investments from all countries must be accorded treatment equivalent to the most favoured.

Relevance to international trade in services

While the MAI covers all sectors, it is particularly relevant to trade in services. In Australia and other OECD and APEC economies, FDI restrictions apply mainly in the services sector, particularly in the communications (including broadcasting, telecommunications and postal services) and financial services industries (Hardin and Holmes 1997). In Australia, restrictions in addition to those set out in the *Foreign Acquisitions and Takeovers Act 1975* apply to certain sensitive sectors. With the exception of real estate, all of these are in the services sector — banking, civil aviation, shipping, broadcasting, newspapers and telecommunications.

Around half of all FDI in Australia and most other OECD economies is in the services sector. Over the past decade, services have accounted for a steady share of around 55 per cent of the stock of Australia's inward FDI (ABS 1997), with finance and insurance services being around one third of this.

The MAI would not be the first binding multilateral agreement covering FDI in the services sector. As noted earlier, the GATS covers FDI as a mode of entry and its rules on market access, national treatment, MFN treatment and issues such as transparency apply to FDI regimes. However, by focussing on investment, rather than having it as one of several possible modes of service supply as the GATS does, the MAI is likely to intensify pressures on governments to make their measures more transparent. The positive list approach of the GATS, whereby commitments to market access and national treatment apply only to those service industries which each member chooses to schedule, has also undermined the effectiveness of the GATS in relation to FDI. The negative list approach of the MAI — with rules applying to all sectors unless exceptions are made — should make for a more transparent and effective system.

The role of exceptions

The mechanisms for making exceptions to the proposed MAI rules have important implications for the outcomes from the agreement. The MAI rules would not apply in cases addressed by general exceptions, temporary safeguards or country-specific exceptions (OECD 1997). The general exceptions allow countries to take measures necessary to protect national security or to ensure the stability of the financial system. Temporary safeguards measures may be taken to address balance of payments crises. The country-specific exceptions allow each country to maintain laws and regulations that do not conform to the MAI disciplines.

The nature and extent of exceptions will influence the potential benefits that may flow from the agreement. The exceptions also provide a mechanism for addressing concerns such as the impact of the agreement on national sovereignty.

APEC and trade in services

Australia's APEC commitments cover a range of matters relevant to trade in services. The Individual Action Plans (IAPs) submitted annually by members update commitments on trade. The IAPs include reports on services, investment, competition, deregulation and government procurement. While the scope of the commitments is broad, they are voluntary and non-binding, in contrast to the binding commitments in the GATS and in the proposed MAI. Further, while the process of presenting IAPs at the Economic Leaders' Meeting each year helps to improve the transparency of the trade and investment regimes in member economies, it does not necessarily increase the pace of liberalisation. The IAPs largely contain statements on current restrictions, descriptions of recent or proposed changes, and commitments to review existing restrictions. In most cases these do not represent new policy initiatives, but those already undertaken unilaterally.

Australia's most recent IAP, released at the Economic Leaders' Meeting in November 1997, contains actions for 12 service industries. For seven of these (construction and related engineering; distribution; educational; environmental; health and social; tourism and travel; and recreational, cultural and sporting), the entry simply indicates that there are no restrictions. For the other five industries, the actions largely reflect decisions taken to review or change policies. For example, the listed actions for financial services are to remove the blanket prohibition on foreign takeovers of the four major Australian banks, to rationalise the regulatory framework and to introduce reforms to encourage new entry and more effective competition. For maritime transport the actions include a review of cabotage policy and the application of the *Trade Practices Act 1974* (Part X) which provides certain exemptions for shipping conferences. These have already been scheduled for review as part of the Commonwealth's national competition policy commitments.

In relation to foreign investment policy, Australia's listed action is to complete the review of foreign investment policy (also scheduled under national competition policy commitments), taking into account the timing and results of the OECD MAI negotiations. The intention to retain specified restrictions in 'sensitive' sectors is also noted, with those named — media, telecommunications and civil aviation — all in the services sector.

The listed actions in other services trade-relevant areas such as intellectual property rights policy and competition policy also largely involve broad statements of current domestic policy and proposed reviews.

Intellectual property rights and services trade

International co-operation has long been recognised as necessary for the effective protection and enforcement of intellectual property rights. Protection which only applies within national boundaries will not be effective in preventing copying or free riding in other countries. For over a century, multilateral agreements have covered matters such as copyright (the Berne Convention) and patents (the Paris Convention). An international body, now known as the World Intellectual Property Office (WIPO) was established in 1993 to monitor and co-ordinate compliance with the international agreements.

The Trade-Related Aspects of Intellectual Property Rights (TRIPS) Agreement was one of the major outcomes from the Uruguay Round of multilateral trade negotiations. In signing on to the WTO in 1995, developed country Members agreed to comply with all the provisions of TRIPS by 1 January 1996. Developing countries have been allowed a phasing-in period of between 5 and 10 years. Australia agreed to abide by the provisions of TRIPS as from 1 July 1995.

The TRIPS encompasses most aspects of previous conventions, with the added features that more countries are now covered, monitoring of compliance has been tightened and new procedures have been established to resolve disputes. Implementation of the TRIPS is to be reviewed from the year 2000 (WTO 1997). The TRIPS specifies minimum standards of intellectual property protection which must be achieved by all Members.

Australia generally exceeds the minimum standards in the TRIPS. The major change that Australia has made to intellectual property laws to meet its TRIPS commitments has been the extension of patent life, from 16 to 20 years.

Over the past year, the Commonwealth Government has announced some further proposed changes to intellectual property laws which will affect services trade. Changes have been made to the *Copyright Act 1968* to permit 'parallel' imports of certain goods and further changes have been proposed to address concerns raised by the growth of electronic commerce. Further aspects of intellectual property law are to be reviewed over the next few years (see section 5.3).

Parallel imports

Restrictions on parallel imports have been used in Australia and several other economies. Parallel imports are neither prevented nor sanctioned under the TRIPS agreement. The *Copyright Act 1968* has allowed owners of Australian copyright to prevent imports of legitimate copies of the products covered by copyright. The restriction on parallel imports has given the Australian copyright holder a monopoly on distribution of the product in the Australian market. Thus, restrictions on parallel importing allow different prices to be set for the same product in different countries. Without the restriction on parallel imports, price discrimination is limited as legitimate copies of the product can be purchased in the lower price foreign market, then re-sold in the Australian market, undercutting the price set by the Australian copyright holder. It is argued that prevention of parallel imports enables the costs of investing in the product to be recovered.

While the protection of intellectual property rights and the control of free riding is important, finding the optimal level of protection is difficult. Restrictions on parallel imports result in higher prices for consumers, as reported in the recent Senate inquiry into parallel import restrictions for sound recordings (SLCLC 1998), and the costs of this must be balanced against the potential benefits of allowing copyright holders to earn higher profits by segmenting markets. Furthermore, the restrictions on parallel imports provide protection in addition to that provided by the controls on illegitimate or pirated imports. While there is certainly a case for continued control of pirated copies, the case for permitting legitimate imports at world prices is strong.

In July 1998, the *Copyright Act 1968* was amended to allow parallel imports of sound recordings. This will remove some of the protection from imports that the Australian copyright holders, mainly large recording companies, have enjoyed. However, it will not remove their protection from pirated copies of recorded music, which will continue to be illegal. The amendment should also result in lower prices for Australian consumers of recorded music.

A further amendment to the *Copyright Act 1968*, also passed in July, relates to parallel imports of goods with packaging or labelling which is subject to copyright. The aim in removing the parallel import restriction is to prevent copyright in packaging from being used as a trade barrier. For example, prior to the amendment, an Australian holder of copyright over some packaging could effectively maintain a position as an exclusive supplier of the goods inside the packaging, such as liquor, cosmetics or luxury goods, by restricting imports of the packaging.

Further changes to the Copyright Act 1968

The Commonwealth Government has also announced its intention to draft amendments to the *Copyright Act 1968* to deal with the growth of electronic commerce (Williams and Alston 1998). Of particular relevance to trade in services is the decision to adopt many of the recommendations of the Copyright Law Review Committee (CLRC) on computer software protection. However, the recommendations of the CLRC on parallel imports of software are under separate ongoing consideration by the Government (Attorney-General’s Department 1998). The Industry Commission in the past has recommended that restrictions on parallel importing of legal copies of software should be removed (IC 1995c).

5.3 Emerging issues for international trade in services

With several pieces of legislation affecting trade in services scheduled for review over the next few years and the next round of multilateral trade negotiations anticipated for the year 2000, and governments considering responses to matters such as the growth in electronic commerce, the policy setting for international trade in services could undergo some major changes over the next few years.

Domestic competition policy and international services trade

As part of its commitment to a national competition policy, the Commonwealth has scheduled for review a range of legislation affecting competition in the Australian economy (Costello 1996). The review schedule covers several areas which are relevant to international trade in services. These include:

- international air service agreements (an Inquiry was recently completed by the Productivity Commission);
- Part X of the *Trade Practices Act 1974* (international liner shipping);
- foreign investment policy, including associated legislation;
- market-based reforms undertaken by the Spectrum Management Agency;
- the *Broadcasting Services Act 1992*; and
- intellectual property legislation, including the *Designs Act 1906, Patents Act 1990, Trade Marks Act 1995* and the *Copyright Act 1968.*

The guiding principle in the review process is that legislation should not restrict competition unless the public benefits of the restriction clearly outweigh the costs and the objectives of the legislation can only be achieved by restricting competition (Costello 1996).

As noted earlier in this report, reviews of several other pieces of legislation have already been completed. For trade in services, the most important is the comprehensive review of the Commonwealth regulatory framework for the financial system (Wallis et. al. 1997). In addition to the Commonwealth's review commitments, each State has scheduled many pieces of legislation for review, including some which are directly relevant for services trade, such as laws relating to certain professions and occupations.

Restrictions on trade in financial services

The GATS negotiations starting in 2000 provide an opportunity to enhance further the transparency of restrictions applying to financial services in Australia. Using the GATS framework, McGuire (1998) identifies and classifies restrictions on financial services in Australia. The study finds that a greater number of measures apply to financial services than those restrictions currently in Australia's GATS schedule (box 5.1). There may be benefits in scheduling additional restrictions identified by McGuire covering superannuation, insurance and financial advice services.

Box 5.1 **Australia's restrictions on trade in financial services**

Using the GATS framework for classifying restrictions, McGuire (1998) identified 165 financial services measures for Australia compared with 38 restrictions listed in Australia's GATS schedule. Eight of the measures identified by McGuire discriminate against foreigners. The majority of measures identified and restrictions in the GATS schedule are imposed by State and Territory Governments.

The higher number of measures identified by McGuire, reflects the broader coverage — the inclusion of prudential measures and measures which are not scheduled voluntarily as part of the positive listing approach under the GATS. Measures are identified and scheduled in the same way as required under the GATS — against market access and national treatment for each mode of supply, for each Australian jurisdiction.

The GATS defines a measure as any regulation imposed by a government. It is difficult to make an assessment of whether a measure restricts trade in financial services. McGuire suggests that measures which deliberately restrict trade or are more excessive than necessary to maintain an efficient and stable financial sector are restrictions on trade in financial services.

Australia's trade in banking, insurance and securities is very liberal when measured against eight Asian economies — Hong Kong, India, Indonesia, Korea, Malaysia, Philippines, Singapore and Thailand. Using the index measure developed by Claessens and Glaessner (1998), McGuire shows that Australia ranks second behind Hong Kong in banking and securities services and third behind Singapore and Hong Kong for insurance services. Hong Kong has lower limits than Australia, or no limits, for establishment and ownership of banks, securities businesses and insurance companies. Singapore has only minor restrictions on the provision of insurance services.

Source: McGuire (1998)

In the superannuation industry, government agencies have monopolies over the administration of superannuation schemes — essentially collection and recording of contributions and determination and payment of benefits. In certain jurisdictions, governments are involved also in the investment management of public sector superannuation funds.[7] In the insurance sector, general and life insurance

[7] Commonwealth legislation will be introduced to provide employees with choice over which fund receives compulsory employer superannuation contributions made on their behalf (Costello 1997b).

companies are required to be licensed to provide insurance services. Life insurance services can only be provided by Australian companies or through locally incorporated subsidiaries of foreign companies.[8] For financial advisory services, dealers and advisers are required to be licensed. These licensing requirements may be subject to the new licensing arrangements proposed as part of implementing the recommendations from the Financial System Inquiry. A single licence — a financial intermediary licence — will be introduced for financial market dealers and advisers (Treasury 1997a).

International air services

International air services have been almost immune so far to multilateral liberalisation. Restrictions on competition and trade have turned the international airline industry into one of the most regulated in the world. In contrast to trade in goods, which is generally allowed unless specifically restricted, trade in international air services is prohibited unless specifically allowed. Most aspects of production and trade are regulated in bilateral air service agreements, which specify the terms and conditions under which the airlines of two countries can fly to, from, between and beyond each country. Bilateral agreements covering market access are also used widely in some other service industries, such as international postal and telecommunications services.

The regulations in the bilateral agreements restrict the efficient operation of air services in many ways and therefore impose costs on airlines, users and the economy. In its draft report on International Air Services (PC 1998a), the Commission estimated that liberalising markets and allowing more open competition could result in significant gains. Greater competition on a number of Asian routes following the entry of Ansett International has resulted in lower fares, increased traffic and a net economic gain for Australia, with gains to airline users more than offsetting any falls in airline profits.

The Commission has argued in the draft report that the presence of an entrenched system of bilateral agreements (over 3000 worldwide and 51 involving Australia) has important implications for the best path to liberalisation for Australia. As long as the rest of the world remains committed to the bilateral system, a policy of unilateral open skies is unlikely to enhance welfare, and may even leave Australians worse off than under the current system.

[8] A limited explanation of this restriction is included in Australia's schedule. Branches of foreign incorporated life insurers operating prior to the introduction of the *Life Insurance Act 1995* are allowed to continue to operate.

The Commission recommended in its draft report that Australia should negotiate reciprocal bilateral 'open skies' arrangements with like-minded countries and invite those countries to discuss the formation of an open club of nations committed to liberalising international aviation though a common plurilateral 'open skies' agreement. This could open up opportunities for airlines to operate more efficiently and provide more diverse and competitive services. An open club could enhance the economic welfare of its member nations.

While recognising the difficulties with multilateral liberalisation, as reflected in the exclusion of most aspects of international air services from the GATS, the Commission in its draft report also recommended that Australia should promote discussion within the WTO membership to determine a process for including all air services in the GATS.

International shipping services

Around 78 per cent of Australia's exports and 70 per cent of imports (by value) are transported by sea. For many commodities, particularly those which are heavy and bulky or not valuable enough to make air transport economic, there are no viable alternatives to shipping as a transport mode. Policies or practices which restrict competition and inflate the costs of shipping services or reduce the quality of service can therefore have a significant impact on the Australian economy.

The international shipping legislation that is scheduled for review in 1998-99 relates to international liner shipping services, which are services on scheduled voyages, most commonly in container vessels. They differ from contract services in bulk vessels, which are used for some high volume commodities such as coal and iron ore. Liner services are provided often by liner conferences, which are groups of liner shipping operators who collude to co-ordinate schedules and capacity, and also to set common freight rates. In Australia, conferences account for around 66 per cent of the value of liner imports and 58 per cent of the value of liner exports. The conference market share is considerably higher for some routes and some valuable commodities.

Part X of the *Trade Practices Act 1974* provides these liner shipping conferences with exemptions from the restrictive trade practices provisions in the Act which otherwise would make the collusion and price setting illegal. The rationale is that such coordination can minimise unused capacity and lower the total costs of the shipping network. Similar liner shipping exemptions are applied by most of our trading partners. Part X also contains explicit protection for Australian flagged vessels.

In return for the exemptions, some obligations are imposed on conferences — most notably the obligation to negotiate with peak shipper bodies. There is no monitoring or regulation of the negotiated freight rates and, in contrast to the approach taken with most other exemptions in the *Trade Practices Act 1974*, no public interest test applies.

Part X was last reviewed in 1993 (Brazil et al 1993). The Review Panel recommended that Part X be retained, with a few amendments designed to expand the coverage to inward liner trade, strengthen protection of shippers, and provide a commercially oriented procedure for dealing with problems. The Review Panel did not address explicitly the issue of whether the exemptions are in the public interest. In support of its recommendations, the Review Panel argued that the contestability of the liner shipping market and the countervailing market power of exporters provide an effective constraint on the market power of shipping conferences. The Review Panel emphasised that Australia should not try to take unilateral action to remove the exemptions. Unilateral removal of exemptions has also been rejected in some other economies. This then raises the issues of whether and how some multilateral reform should be pursued. One possible forum is the WTO's GATS negotiations (discussed below).

In the pending review of Part X, under the auspices of national competition policy, the Review Panel's findings will need to be re-examined and it will be necessary to establish whether the legislation results in a net community benefit. To do this, account will need to be taken of changes in market conditions since 1993 and some of the arguments which the Review Panel offered in support of its recommendations will need to be reassessed. A number of questions will need to be addressed. For example, is there an effective competitive fringe of independent carriers limiting the market power of conferences on all inward and outward routes and for all commodities? Are outcomes negotiated by single conferences and single peak shipper bodies necessarily in the best interests of the consumers and producers of shipped commodities and the wider economy? Should the shipping-specific exemptions be retained, amended, or replaced by the general competition rules, with scope for exemptions (via authorisations) where the public interest warrants.

Professional services

Restrictions on market entry and operations for certain occupations and professions can assist the suppliers of those services and impose costs on consumers. The ACCC (and its predecessor, the Trade Practices Commission) have examined a range of anti-competitive restrictions in certain occupations and professions, including detailed studies of the accountancy, architectural and legal professions

(TPC 1992a, 1992b, 1994). The Industry Commission has shown that restrictions can result in higher prices for these and other services, such as some specialist medical services (IC 1995a).

In 1996, the Commonwealth and State governments took a major step toward controlling restrictive trade practices in the professions by enacting legislation to extend competition laws to all businesses in Australia. Prior to this reform, government businesses and unincorporated businesses, such as lawyers, doctors, architects and engineers, were exempt from the competition laws which may make certain restrictive trade practices such as price-fixing agreements illegal.

While certain restrictive trade practices in the professions are now subject to legal action by the ACCC or private individuals or companies, there are still many potentially anti-competitive practices which are supported by legislation, particularly at the State level. A range of regulations governing professions and occupations are listed for review over the next few years as part of the national competition policy. Some of the professions and occupations covered include architects, legal practitioners, licensed surveyors, electrical contractors, plumbers and gasfitters, building practitioners and certifiers, employment agents, travel agents, auctioneers and real estate agents (Samuel 1998).

The legislative review process should examine closely the rationale for the rules which restrict competition. Some forms of regulation, such as accreditation standards, may be in the public interest. They may restrict competition for the licensed suppliers, but the costs of this — higher prices and less incentive to innovate — may be more than offset by the benefits to consumers of being able to make more informed decisions. However, it is not clear that other types of restrictions, such as restrictions on advertising or ownership structures, are in the public interest (Fels 1997). In the legislative review process, the onus will be on those sheltered by the laws to establish that the laws result in a net benefit for the community.

Electronic commerce, intellectual property and services trade

Electronic commerce can increase competitive pressures on domestic service suppliers in many ways. For example, where goods such as books or magazines are ordered from a foreign supplier and delivered electronically, foreign suppliers are competing with domestic publishers and also domestic suppliers of distribution services such as postal or courier services. Where the goods are only ordered over the internet but delivered by traditional means, the foreign supplier is still competing with domestic publishers.

The major products purchased over the internet by Australians in 1997 — non-educational software, books, music, and magazines — were all service-related. Books have been the fastest growing market (JCPAA 1998). Services such as travel bookings are also increasingly being supplied electronically. There is also potential for some professional services, such as medical services, to be delivered via the internet. This could provide competition for existing suppliers and also make services available in areas which may otherwise not be served, such as remote areas.

Given that many of the products currently traded over the internet involve intellectual property (in software, books and magazines and music), intellectual property rights policies are particularly important. As noted in the recent parliamentary report on electronic commerce:

> ... while the internet provides a major distribution tool, sellers must be confident that their intellectual property is protected. At the same time, consumers must be confident that they are receiving authentic goods and services (JCPAA 1998, p. 169).

Some of the issues have been addressed in the Digital Agenda report (Attorney-General's and Department of Communications and the Arts 1997), and the Government has announced its intention to amend the *Copyright Act 1968* in response. A new broad-based technology-neutral right of communication to the public will apply to works made available on the internet and other on-line services, as well as works transmitted or broadcast to the public (Williams and Alston 1998).

The issues extend beyond national borders. As outlined in a recent WTO report on electronic commerce, the 'borderless' nature of the internet and the difficulties in determining the applicable laws in certain situations mean that international co-operation and the effective implementation of the TRIPS agreement are vital (Bacchetta et al. 1998). The implementation of the TRIPS is to be reviewed from the year 2000 (WTO 1997).

The JCPAA also noted that the regulatory framework will shape the development of internet commerce. It recommended that the Productivity Commission conduct an inquiry into the development and growth issues and regulatory issues arising from the growth of internet commerce (JCPAA 1998).

In its submission to the JCPAA inquiry, the Commission focussed on one of the many issues affecting the development of internet commerce — the pricing of access to the internet.

In Australia, competition among internet access and service providers has lowered the price of internet access substantially. However, a number of factors continue to distort the cost of providing internet access and have an impact on the price, quality and take-up of internet commerce. Two existing cost distortions are those associated with:

- the cost of access to the domestic telecommunications network; and
- the cost of international internet capacity between Australia and the United States.

Also important are potential cost imposts which may result from the introduction of new regulations governing use of the internet, including any new taxes. The Commission has recommended that a proper regulatory cost-benefit analysis, including a Regulatory Impact Statement, be undertaken before the introduction of any taxation measures which could affect internet commerce (IC 1997c).

The next round of GATS negotiations

While no definite agenda has been set for the next round of GATS negotiations in 2000, a wide range of matters could be addressed — some relating to particular sectors, others to the structure and scope of the agreement. From Australia's perspective, the negotiations provide an opportunity to amend commitments, locking in to a binding multilateral agreement reforms which have been implemented in recent years. Some of the potential sectoral negotiations also should be of particular interest for Australia. For example, as a trade-oriented and geographically relatively isolated economy, Australia could gain from multilateral agreements to liberalise international transport services. Australia will need to develop its negotiating position on matters such as market access for foreign airlines and shipping lines.

The next round of GATS negotiations could focus particularly on areas where trade in services can be liberalised significantly. One such area is services sectors with few commitments and where negotiations have been difficult — for example, maritime transport, air services and professional services. Sector-specific agreements may be required to cover complex issues in these sectors. While individual agreements can facilitate negotiations by allowing more detailed consideration of difficult issues, they can also weaken liberalisation efforts by discouraging cross-sectoral trade-offs.

With this in mind, there might be benefits in proceeding with transport negotiations on a multimodal basis (Mattoo 1997). This could recognise the importance of links between transport modes, as more than one mode is used in providing door-to-door services for consumers. It also could create opportunities for those Members with particular interests in one transport industry to put pressure on those in another to liberalise, and thereby generate net benefits for the users of the transport sector as a whole.

The shortcomings in the structure and scope of the GATS are well documented (Hoekman 1995; IC 1995d). The next round of negotiations might be an opportunity to consider the adoption of a 'negative list' approach to scheduling services sectors and commitments, clarification of the definitions of market access and national treatment disciplines, and expansion and strengthening of generally applicable rules. As one of the signatories which has made relatively strong commitments under the GATS, Australia could also support moves which result in greater transparency and commitment to liberalisation among other WTO Members.

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