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**Working Paper**

## Regional economic integration and multilateralism: The case of the ASEAN-Australia-New Zealand FTA and the Malaysia-New Zealand FTA

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## **ADB Working Paper Series**

### **Regional Economic Integration and Multilateralism: The Case of the ASEAN-Australia-New Zealand FTA and the Malaysia-New Zealand FTA**

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**Abstract**

Regional economic integration is back in vogue following the “stumble” in the Doha Round in July 2008. Preferential trade agreements (PTAs) are driving this trend in Asia and the Pacific as well as in Central and South America, and the sheer volume of PTAs is striking. In the 1990s there were barely five PTAs in force, but now there are more than 200 either under negotiation or in force. In this regard, Asia and the Pacific has developed a rapidly evolving regional economic architecture that spans two major plurilateral agreements, the Trans-Pacific Partnership (TPP) and the Regional Comprehensive Economic Partnership (or ASEAN+6 RCEP), as well as the putative Free Trade Agreement of the Asia-Pacific (FTAAP), which received a new lease on life through the Asia-Pacific Economic Cooperation (APEC) leaders’ meeting in Beijing late last year. ASEAN, as a group or individually, has been particularly busy in this sphere, deliberately using PTAs as a supplement to its own regional integration process. In Central and Latin America, economic integration has been similarly pursued at variable speeds and in variable geometries. In the meantime, there have been some concerns about the proliferation of PTAs for all the usual reasons. Trade diversion is a reality and with their less-than-comprehensive approach to sensitive issues like agriculture and burdensome rules of origin (ROO), many PTAs are perceived as being at best of marginal business interest and at worst a “stumbling block” to conclusion of the Doha Development Round. This paper argues, however, that more recent PTA outcomes, like the ASEAN-Australia-New Zealand FTA (AANZFTA) and the Malaysia-New Zealand FTA (MNZFTA) present a rather more nuanced picture. There may even be some grounds for modest optimism about how PTAs can be building—not stumbling—blocks for multilateralism. Four distinct criteria are used to assess the AANZFTA and the MNZFTA. These include: 1) the breadth and depth of agricultural market access liberalization; 2) the existence (or non-existence) of WTO-plus commitments; 3) how the risks of complex ROO, etc., are mitigated; and 4) the introduction of bespoke solutions of direct commercial value to business (e.g., facilitated business visitor access). The paper suggests that both the AANZFTA and the MNZFTA provide the basis for engagement at the WTO on how to multilateralize the outcomes secured through the AANZFTA and the MNZFTA. The role and experience of New Zealand in both of these high quality and comprehensive PTAs is something that may be of enduring interest.

**JEL Classification:** F13, F15, F53

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# 1. INTRODUCTION

When Francis Fukuyama (1992) declared the “end of history,” there was an implicit assumption that the world would become a simpler one where liberal capitalism triumphed over its alternatives, heralding an era of Kantian perpetual peace, universal World Trade Organization (WTO) membership, and general harmony. We know now that Fukuyama was wrong. We are in fact in a rather more complex and challenging era—what some have called a “great unravelling” of existing certainties, stalling multilateralism, and rising regionalism (Cohen 2014; Ferguson 2006; Haas 2014).

This provides the backdrop for the re-emergence of the People’s Republic of China (PRC) as a major global actor, the recent United States (US) “re-balance” to Asia and the Pacific, the rise of India, and the struggle for international relevance by the European Union. In the meantime, key developing countries are accelerating their global engagement including through the leveraging of their own regional integration processes through for instance, the 10-member Association of Southeast Asian Nation (ASEAN) bloc as well as the rapidly evolving Pacific Alliance (Meacham 2014). All of this is imposing new points of reference, shaping trade and international economic policy in new and interesting directions (Bayne 2011: 59–62).

In fact, around the time that Fukuyama declared that history was at an end, the Asia and Pacific region was increasingly catching up with other parts of the world in turning to preferential trade agreements (PTAs) as an instrument of its own regional economic integration.<sup>1</sup> This is a universal trend. The Asian Development Bank FTA database, for instance, indicates the number of concluded PTAs has risen from barely five in the mid to late 1990s to 119 at present.<sup>2</sup> There is evidence too that this trend will be sustained, with a further 120 PTAs under negotiation or proposed for negotiation.

In Central and South America, regional economic integration is continuing at variable speeds and in variable geometries of membership. Most recently, the Pacific Alliance (Alianza del Pacifico), founded in April 2011, has generated significant momentum in its efforts to bring together and potentially broaden the “alliance” beyond its foundation members of Chile, Colombia, Mexico, and Peru. There is evidence, too, that the Pacific Alliance is reflecting on how best to engage with the Asia and Pacific region. This is an acknowledgment of the fact that this is a region where regional economic integration continues apace, not least in the context of the rapidly evolving economic architecture that spans two major plurilateral agreements, the Trans-Pacific Partnership (TPP) and the ASEAN+6 process, or the Regional Comprehensive Economic Partnership (Meacham 2014: 3–6; Wignaraja, Ramizo, and Burmeister 2013: 391–410; Estevadeordal, Kawai, and Wignaraja 2014), not to mention the putative Free Trade Agreement of the Asia-Pacific (FTAAP), which received a new lease on life through the Asia-Pacific Economic Cooperation (APEC) Leaders’ meeting in Beijing in 2014 (APEC 2014).<sup>3</sup>

A range of reasons for this proliferation of PTAs across the Asia and the Pacific and more generally have been posited (Francois and Wignaraja 2008; Meacham 2014; Gilbert, Scollay and Bora 2004). Perhaps four factors identified in the wider literature

<sup>1</sup> For the purposes of this paper, Asia and the Pacific is defined as including the ten ASEAN member states, Asia’s newly industrialized economies (i.e., Hong Kong, China; the Republic of Korea; and Taipei, China), the People’s Republic of China, India, Japan, Australia, and New Zealand.

<sup>2</sup> ADB FTA database available at: <http://www.aric.adb.org/fta> (accessed on 1 March 2015).

<sup>3</sup> For an analysis of Asia–Latin America FTAs, see Wignaraja, Ramizo, and Burmeister (2013: 385–415).

most plausibly explain the rapid growth of PTAs within the region. These are: 1) deepening regional market integration; 2) the reality of European and North American economic integration; 3) the Asian financial crisis of 1997–1998; and 4) the slow progress in the WTO Doha negotiations (Francois and Wignaraja 2008).

The proliferation of PTAs in Asia and the Pacific and indeed more generally has, however, fuelled a pre-existing concern about their efficacy and indeed their ability to deliver to the commercial opportunity which they appear to promise. The original accusation remains that PTAs are “stumbling blocks” to the multilateral process (Baldwin 2006; Bhagwati 1995, 2008). Many of these criticisms of PTAs are well known, including the low levels of coverage of agricultural products in many PTAs concluded in the region; their low quality and lack of WTO-plus elements (Baldwin 2006; Fiorentino, Crawford, and Toqueboeuf 2009); the perceived low uptake of PTA preferences by business; the risk of a growing “Asian noodle bowl” effect (i.e., overlapping trade agreements); and the potential for these PTAs—“termites in the system”—to undermine the WTO itself (Bhagwati 2008; Freund and Ornelas 2010). Most recently, Heydon (2014) has persuasively reminded us that while there are powerful incentives—both political and commercial—driving the negotiation of preferential trade agreements, there remain a number of countervailing factors, including the risk of “discord” in international trade law; the continued negative impact of trade diversion; and the disincentive to non-discriminatory liberalization, not least through the construction of protective rents created by preferences and by the proliferation of rules—even where the PTA meets the obligations of Article XXIV.

This paper concurs with Heydon’s assessment but acknowledges that countries continue to pursue PTAs, including to drive regional economic integration—a process that has accelerated since July 2008, when the Doha Development Round appeared to stall. Compounding the concern about the impact of PTAs on multilateralism has been the non-trivial development whereby three of the world’s five largest economies have launched bilateral PTAs among themselves in the form of the European Union (EU)-Japan FTA<sup>4</sup> and the Trans-Atlantic Trade and Investment Partnership (US-EU).<sup>5</sup> These set of announcements exacerbated an underlying unease about the way in which these PTAs might “suck oxygen” away from the Doha Round. There are therefore good reasons to continue to be concerned about the rise of PTAs generally, not least for trade diversion-related reasons but also because of their ability to frustrate multilateralism.

While one may prefer multilateralism for all of the usual reasons, it is also clear that there may be some grounds for cautious optimism about the inter-relationship between PTAs and the multilateral system. This is because more recent PTAs are seeking to address some of the concerns about “stumbling blocks” and in some cases may even become “building blocks” to wider plurilateralism, potentially in support of the Doha Round itself. Moreover, the fact that some of the major global players are now pursuing bilateral and plurilateral PTAs with an ever increasing number of partners, particularly developing countries, suggests a continued interest in market opening and the welfare gains that derive from high-quality outcomes in PTAs. Moreover, there is something of a “virtuous economic circle” whereby PTA-driven integration processes can catalyze the intensification of trade and investment activity, which in itself further reinforces the integration catalyzed by the PTA. The original PTA between New Zealand and Australia, for instance, has driven an ever widening and deepening process of integration that has evolved from a straight-forward traditional PTA negotiation to a

<sup>4</sup> <http://ec.europa.eu/trade/policy/countries-and-regions/countries/japan/> (accessed on 28 February 2015).

<sup>5</sup> <http://ec.europa.eu/trade/policy/in-focus/ttip/> (accessed on 1 March 2015).

highly innovative Single Economic Market agenda between the two economies that, *inter alia*, now involves the notion of “mutual equivalence” and a range of other genuinely “behind-the-border” issues (Messerlin 2014: 9–10; Leslie and Elijah 2012: 981–989). Specifically, this paper argues that since the Doha “stumble” in July 2008, ASEAN and its individual members have demonstrated that they can and do conclude commercially meaningful and comprehensive PTAs that:

- 1) support the reform and liberalization of the agricultural sector in a way that is consistent with Article XXIV of the General Agreement on Tariffs and Trade (GATT) (see below) and may yet provide a platform for the successful conclusion of the Doha Round;
- 2) contain significant WTO-plus elements in areas like services and investment;
- 3) mitigate the risk of complex rules of origin, thereby encouraging the uptake of PTA preferences by companies in the region; and
- 4) introduce new and creative bespoke “solutions” of direct commercial interest and relevance to businesses both in the medium and long term.

Interestingly, the PTAs that have delivered to the four elements identified above have been concluded by ASEAN and its members with either or both of New Zealand and Australia. That is perhaps another powerful argument in favor of the inclusion of these two Organisation for Economic Co-operation and Development (OECD) economies in broader regional economic integration efforts over time.

It is against this background that this paper briefly outlines the development of the ASEAN-Australia-New Zealand Free Trade Agreement (AANZFTA) and the Malaysia-New Zealand FTA (MNZFTA). It then describes how each of these agreements has delivered to the four components identified above. In this context, the paper briefly outlines how New Zealand (with Australia) worked with ASEAN to ensure that the post-AANZFTA implementation phase was broadened and deepened through the development of a new framework—the ASEAN Closer Economic Relations (ASEAN-CER) Integration Partnership Forum—to complement the ongoing AANZFTA “living agenda.” This provides the basis for an ongoing engagement between New Zealand (and Australia) with ASEAN on the evolution, facilitation, and development of regional trade and economic integration, beyond simply “at-the-border” to “behind-the-border.” The paper concludes by suggesting that the role of New Zealand in these processes is worth highlighting. As Leslie (2015) has persuasively argued, New Zealand has operationalized a non-linear, evolving “stepping stones” or “building blocks” strategy that carefully cultivates and supports the evolving regional economic architecture (Leslie 2015: 18–22). This is driven in no small measure by its determination to negotiate PTAs that conform to GATT Article XXIV principles and the APEC-inspired concept of “open regionalism” (New Zealand Ministry of External Relations and Trade 1993 and Bergsten 1997).<sup>6</sup>

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<sup>6</sup> GATT Article XXIV provides the legal exemption from the requirement to provide Most Favoured Nation status and, in this context, outlines the conditions and measures for the establishment of customs unions and free trade agreements that would not violate GATT rules. In particular, it stipulates that “duties and other restrictive regulations of commerce...are eliminated on substantially all the trade” between the parties to the agreement “within a reasonable length of time” (The full text of Article XXIV is available at [http://www.wto.org/english/res\\_e/booksp\\_e/analytic\\_index\\_e/gatt1994\\_09\\_e.htm](http://www.wto.org/english/res_e/booksp_e/analytic_index_e/gatt1994_09_e.htm) (accessed on 1 March 2015)).



## 1.1 The ASEAN-Australia-New Zealand Free Trade Agreement

At the time of the conclusion of the FTA in August 2008 and its subsequent signature in February 2009, ASEAN was New Zealand's fourth most important trading partner. For ASEAN partners, while New Zealand was not a key market, it remained a high-value one to which they exported textiles, clothing, footwear, machinery, and furniture products, among others. Investment flows were also expanding, with investors from Indonesia, Malaysia, Thailand, as well as Singapore demonstrating increasing interest in New Zealand's economy. For New Zealand, key export items included beef, dairy and horticultural products. The evolution of New Zealand's effort to contribute to the creation of the AANZFTA building block and therefore secure a place in the emerging regional economic architecture was achieved through its long investment in and history of engagement with ASEAN over the past 30 or so years (Smith 1998: 238–252).

Over time, the set of security and political arrangements that underpinned New Zealand's engagement with ASEAN gradually developed a more specific economic and commercial focus. This was accelerated by the development of the ASEAN Free Trade Area, which was applied between ASEAN members and had been under negotiation for some years. This was concluded in 1992. It was progressively reviewed and updated in the intervening period and it was alongside this process that the ASEAN-CER senior economic officials' dialogue was established.<sup>7</sup> This provided a mechanism through which New Zealand, Singapore, and Australia sought to generate momentum behind a longer term objective: an agreement that would link the (Australia-New Zealand) CER process through an FTA with ASEAN countries.

The Report of the High Level Task Force on the AFTA-CER Free Trade Area (the Angkor Agenda) took the shared ambitions of Singapore, Australia, and New Zealand a step forward by providing the formal impetus for the launch of negotiations by ASEAN and CER ministers in November 2004.

The AANZFTA negotiations involved particular challenges, not least the differing levels of development between the various negotiating partners—Singapore, Australia, and New Zealand had per capita incomes significantly above those of most of the ASEAN partners and the three Least Developed Countries in the grouping, Myanmar, Cambodia, and the Lao People's Democratic Republic (Lao PDR) (with the Lao PDR not even being a WTO member and Cambodia only having recently acceded). Following nearly 5 years and 16 rounds of negotiations, the ASEAN-Australia-New Zealand FTA was concluded and signed in February 2009 (Mugliston 2009).

AANZFTA is particularly significant for New Zealand, not only in commercial terms but because it forms the anchor for the country's participation in the RCEP negotiations. RCEP will be a "mega-plurilateral" that encompasses nearly a third of global trade and over 3 billion people.<sup>8</sup> It was made clear by ASEAN when it launched the RCEP negotiations that only partners with which it had an FTA could participate and in this sense AANZFTA represented New Zealand's "ticket" into RCEP.

More directly, the AANZFTA delivered significant commercial benefits to New Zealand. This included, for instance, the elimination of ASEAN tariffs on 99%–100% of New Zealand's then current goods exports within 12 years and, unlike with previous

<sup>7</sup> CER is a broad and comprehensive free trade agreement that was reached between Australia and New Zealand in 1983.

<sup>8</sup> More information about RCEP is available at: <http://mfat.govt.nz/Trade-and-Economic-Relations/2-Trade-Relationships-and-Agreements/RCEP/index.php> (accessed on 14 February 2015).

PTAs there were no special safeguards for agricultural products. For its part, New Zealand eliminated 100% of its tariff lines (NZMFAT 2009a).<sup>9</sup>

## 1.2 The Malaysia-New Zealand Free Trade Agreement

The MNZFTA has its origins in a similar process to that pursued through AANZFTA. It represents the culmination of bilateral engagements and regular dialogue between Kuala Lumpur and Wellington since the 1970s. On 5 September 2004 in Jakarta, Malaysian Minister for International Trade and Industry Dato Seri Rafidah Aziz and the New Zealand Minister for Trade Negotiations Hon Jim Sutton agreed that Malaysia and New Zealand would conduct parallel studies on a possible bilateral FTA. These studies concluded that there would be value to a negotiation between the two partners.<sup>10</sup> Less than a year later, on 31 March 2005, the prime ministers of New Zealand and Malaysia agreed to launch negotiations for a bilateral FTA. Negotiations were substantively concluded nearly 5 years later on 30 May 2009 and the agreement was signed in Kuala Lumpur on 26 October 2009.

At the time of the conclusion of the negotiations, Malaysia was New Zealand's eighth most important trading partner and a significant regional distribution hub for a range of products (dairy, kiwi fruit, etc.) and services, primarily education and engineering services. In fact, between 2003–2008, the number of fee-paying Malaysian students in New Zealand increased by over 70%, making it New Zealand's third largest source of fee-paying university students and second largest source of PhD students. For Malaysia, New Zealand was an important destination for furniture products and a range of textiles, clothing and footwear, and steel products—goods for which it expected to improve access over and above that negotiated through the AANZFTA, thereby providing Malaysian exporters with a first-mover advantage over ASEAN competitors.

The agreement had not been a straightforward one to negotiate. Negotiations were suspended for a period following a failure by the parties to agree on whether to include trade and labor and trade and environment standards in the agreement, as well as disagreements on how to schedule market access commitments in services and investment. Negotiations were resumed shortly after the conclusion of AANZFTA on the basis that the MNZFTA should be both WTO and AANZFTA-plus. So it proved. Legally binding treaty-status outcomes on trade and labor and trade and environment were agreed and a consensus was reached on the scheduling of market access for investment and services. Furthermore, the agreement provided that by 2016 (i.e., within 7 years compared with 12 under the AANZFTA), 99.5% of total current New Zealand exports to Malaysia would be duty free and for its part New Zealand eliminated all tariffs with 7 years (NZMFAT 2009b: 3–17).

The following section describes how the AANZFTA and the MNZFTA were able to address the four inter-related issues identified in the introduction, i.e., ensuring that agriculture was comprehensively liberalized in line with GATT Article XXIV; the inclusion of substantive WTO-plus commitments by the parties, including in services, investment, labor, and environment; mitigating the risk of further “noodles” in the ROO “noodle bowl”; and making the agreements relevant for business in the medium to long term.

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<sup>9</sup> More information about AANZFTA is available at <http://www.asean.fta.govt.nz> (accessed on 1 March 2015).

<sup>10</sup> The New Zealand parallel study is available at <http://www.mfat.govt.nz/downloads/trade-agreement/malaysia/nzmalaysiafta-march2005final.pdf> (accessed on 1 March 2015).

## 2. ASIA AND THE PACIFIC PTAS AND AGRICULTURE: THE CHALLENGE TO COMPREHENSIVITY AND GATT ARTICLE XXIV

It has been widely remarked that early PTAs in Asia and the Pacific have failed to comprehensively liberalize the agriculture sector as a consequence of domestic sensitivities (Plummer 2007, Tumbarello 2007, Freund and Ornelas 2010). Certainly, many PTAs concluded in the region either exclude entire supposedly “sensitive” agricultural subsectors from the PTA altogether (e.g., the ASEAN-India FTA), or exclude particular products (Japan-Philippines Economic Partnership Agreement) or devise ways in which to limit the impact of the PTA, including by not fully liberalizing (i.e., reducing to zero) the tariffs on a range of agricultural products (ASEAN-PRC FTA, Japan-Malaysia FTA, etc.). Even when the PTA eliminates the relevant agricultural tariffs, the time frames for elimination can be considerable (ASEAN-India FTA, ASEAN-Republic of Korea FTA). There is a question therefore as to how these agreements might meet the GATT Article XXIV “test” that they cover “substantially all trade” and “within a reasonable length of time.”

More recently, however, there may be some grounds for optimism. Several key Asia and Pacific economies have demonstrated an ability to conclude PTAs particularly with OECD countries like Australia and New Zealand. These agreements include the elimination of up to 99% of all tariffs on existing trade (i.e., including agriculture). This is particularly significant since both Australia and New Zealand are major agricultural exporters in a way that, for instance fellow OECD members, Japan and the Republic of Korea are not. The fact that both Australia and New Zealand are significant exporters of dairy and beef, for instance, suggests that the liberalization of agricultural market access through PTAs by key developing country players, like Indonesia, Thailand, and Malaysia, may make it easier to address the same agriculture-related market access issues through the Doha Development Round.

In fact, notwithstanding the agriculture-related sensitivities that a PTA with New Zealand (or Australia) presented ASEAN countries, the latter were able to conclude an agreement that easily meets GATT Article XXIV requirements, as well as ensuring a high quality and comprehensive outcome for all partners. This can be illustrated with reference to the ASEAN-Australia-New Zealand FTA, as well as the individual PTAs negotiated with ASEAN members after the AANZFTA was concluded, e.g., for the purposes of this paper the Malaysia-New Zealand FTA.

The AANZFTA is the first “single undertaking” agreement concluded by ASEAN countries and arguably also the first in which ASEAN members made significant liberalizing commitments in agriculture. Before the conclusion of the AANZFTA in 2008–2009, ASEAN had hitherto proved unable to make comprehensive commitments to eliminate tariffs on substantially all trade, including agricultural products (e.g., the PRC-ASEAN FTA, Japan-ASEAN FTA, etc.). Even individual ASEAN partners, such as Thailand, which had concluded bilateral comprehensive outcomes with both Australia and New Zealand in 2004–2005 had included tariff elimination timeframes in excess of 15 and in some cases up to 20 years, supplemented by special agricultural safeguards.<sup>11</sup>

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<sup>11</sup> More information about the Thailand FTAs with both New Zealand and Australia is available through <http://www.mfat.govt.nz/Trade-and-Economic-Relations/Trade-Relationships-and-Agreements/Thailand/index.php> and <http://www.dfat.gov.au> (accessed on 1 March 2015).

By 2008–2009, ASEAN collectively was to demonstrate a level of ambition and commitment to liberalization across domestically sensitive areas like beef and dairy which had not been readily discernible before. Under the terms of the AANZFTA, for instance, key ASEAN partners like Indonesia, Philippines, Malaysia, and Viet Nam agreed timeframes for tariff elimination of up to 12 years in general for between up to 96% of the then current Australian trade and 99% of New Zealand's existing trade. These commitments applied to a range of sensitive agricultural products, including beef, dairy, fruit, vegetables, and wood products.

Significantly too, given their position in the WTO (particularly that of Indonesia and the Philippines) and the precedent provided by Thailand's earlier bilateral agreements with both Australia and New Zealand in 2004 and 2005 where special agricultural safeguards apply, including for instance on a range of dairy products (NZMFAT 2005: 18–19), there are *no* special agricultural safeguards in the AANZFTA (NZMFAT 2009a).<sup>12</sup> This demonstrates that the ASEAN countries, working with Australia and New Zealand, could find a way to successfully conclude a PTA that takes into account domestic sensitivities (i.e., through extended time frames for tariff eliminations) but do not need anymore the additional distortions that were required in the middle of the decade by individual ASEAN countries like Thailand.

There is no doubt that these agreements could have done more to liberalize agricultural products more ambitiously. This could have included, for instance quicker tariff elimination (i.e., less than 12 years) and could have dealt comprehensively with alcoholic beverages, which were excluded from tariff elimination altogether or had only limited tariff reductions as a consequence of religious sensitivities. Nevertheless, the outcomes were liberalizing and involved tariff elimination on agricultural tariff lines on which ASEAN members had never before made such deep and broad commitments. In this way, the AANZFTA outcomes in agricultural goods signaled that Asia and Pacific economies can deal creatively with their domestic agricultural constituencies, while ensuring meaningful tariff liberalization. The agreed commitments and subsequent trade that has flowed between the parties has served to underline the fact that fears about New Zealand (and Australian) competitiveness and possible impacts on domestic producers were misplaced.

### **3. WTO-PLUS ELEMENTS: SERVICES, INVESTMENT, LABOR, AND ENVIRONMENT**

Before 2008, most ASEAN FTAs and those concluded by the PRC and even OECD members Japan and the Republic of Korea with ASEAN partners had been goods-only agreements with an ongoing process of adding further chapters to the agreement over time (e.g., services and investment, etc.). As noted above, these agreements were characterized by a significant range of exemptions and “carve-outs” in deference to domestic sensitivities. Relatively few of these agreements dealt comprehensively with services, let alone investment, and most did not have stand-alone chapters on issues such as sanitary and phytosanitary standards, technical barriers to trade, competition policy, intellectual property rights, labor and environment standards, and so on.

By contrast, the AANZFTA and the bilateral Malaysia-New Zealand FTA are both comprehensive “single undertakings.” Both contain significant WTO-plus elements, with

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<sup>12</sup> More information about the AANZFTA outcomes is available through <http://www.asean.fta.govt.nz/> and <http://www.dfat.gov.au/fta/aanzfta/AANZFTA-Creating-business-opportunities.html> (accessed on 28 February 2015).

the MNZFTA both WTO-plus and AANZFTA-plus in outcomes for both parties. Both agreements comprise the kinds of chapters generally associated with high quality and comprehensive FTAs, including WTO-plus elements in the chapters on competition policy (AANZFTA and MNZFTA), investment chapters that include a range of additional protections above and beyond the existing ones in place across the region, with both Australia and New Zealand drawing on a “best of BITs (bilateral investment treaties)” approach (i.e., seeking to secure the best elements of ASEAN members’ individual bilateral investment treaties, including with other OECD countries, e.g., from the EU, the US, and Canada in particular). The agreements also include compulsory investor–state dispute settlement, albeit with a number of built-in safeguards to prevent frivolous claims, limit damages, and to mitigate as far as possible claims that would infringe on or otherwise limit regulatory policy space. It is worth noting that the investment chapters concluded with ASEAN (in the AANZFTA) and Malaysia represent the highest quality outcome concluded in this area for ASEAN members to date—a process reinforced by the Malaysia-Australia FTA (MAFTA).

More particularly, the AANZFTA and Malaysia-New Zealand FTAs include significant WTO and even Doha-plus market access commitments in services, in particular, but in the rules governing services as well. Table 1 below lists the number of WTO and Doha-plus outcomes committed by key ASEAN partners through the AANZFTA. This shows that ASEAN countries were prepared to go considerably further in making services commitments under the AANZFTA than they appeared prepared to undertake at the WTO. In total, eight of the ASEAN countries made WTO and Doha-plus commitments. The exceptions were Cambodia, which had recently acceded to the WTO. There was agreement that given the quality of its WTO commitments and its LDC status, further commitments were not required from Cambodia. The Lao PDR, which was not a WTO member at the time of the conclusion of the AANZFTA, made a range of commitments which essentially mirror the negotiated outcome of its WTO accession. In terms of those ASEAN members that made WTO-plus commitments, the case of Indonesia is particularly striking. It made 67 WTO-plus commitments under the AANZFTA, some 50 of which were in addition to Indonesia’s existing Doha offer on services.<sup>13</sup>

The breadth and depth of the commitments was also a highlight. They included commitments in a range of services sectors across all four modes of supply depending on the sector, including in accounting services; transport; tourism, education; legal services; engineering; environmental; urban planning; landscape architectural services; health services, construction and related services; and a range of other business services (including consulting, advertising, technical testing, and analysis services). The Malaysia-New Zealand FTA builds on the AANZFTA by including an MFN provision for commercially significant services of interest to both partners as well as a general MFN provision for investment. This helpfully future-proofs the agreement and, together with MAFTA, appears to have been the first time MFN has been provided in an agreement with an ASEAN partner that does not include Singapore.

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<sup>13</sup> The extent of these commitments by Indonesia does in part reflect the reality that Indonesia’s existing WTO commitments were of a relatively modest quality.

**Table 1: AANZFTA: Services Commitments**

(number of commitments)

	<b>WTO-plus Commitments</b>	<b>Doha-plus Commitments</b>
<b>Indonesia</b>	67	50
<b>Malaysia</b>	50	29
<b>Philippines</b>	39	27
<b>Thailand</b>	21	2

AANZFTA = ASEAN-Australia-New Zealand Free Trade Agreement, WTO = World Trade Organization.

Source: Author's calculations derived from the relevant services schedules of AANZFTA parties available at [www.aseanfta.org](http://www.aseanfta.org) and compared with schedules listed at [www.wto.org](http://www.wto.org) (accessed on 28 February and 1 March 2015).

In addition to the WTO- and Doha-plus commitments made for services market access, both the AANZFTA and the MNZFTA contain a significant number of WTO-plus elements in their rules governing trade in services as well. Numerous enhancements build upon existing WTO obligations, including the following.

- *Telecommunications and financial services.* Two separate Annexes on these sectors provide for greater legal certainty for Australian and New Zealand exporters of telecommunications and financial services, including by prescribing that the relevant laws and regulations in ASEAN countries must be transparent, objective, and non-discriminatory, thereby limiting the prospect of anti-competitive use of market power, etc.
- *Domestic regulation.* A commitment by all parties to AANZFTA to accelerate authorization and licensing procedures and processes as well as a legal commitment to limit the extent to which these can be used as informal barriers against competitors. In the case of the MNZFTA the domestic regulation disciplines apply to all services sectors, not just those in Malaysia's or New Zealand's services schedules. This means the regulations relating to authorization, licensing, standards, and qualifications for all services sectors must meet certain standards of transparency and objectivity and be no more burdensome than necessary.
- *Transparency.* A built-in legal requirement that any changes to existing laws and regulations, or new laws and regulations must be developed in a transparent and consultative manner.

In line with the WTO-plus nature of the wider agreements, the Malaysia-New Zealand FTA, as well as the outcomes negotiated with the Philippines and Indonesia (both of the latter in the context of AANZFTA), include legally binding trade and labor and trade and environment agreements. None of these countries had agreed to such instruments before the conclusion of the negotiations with New Zealand. These treaty-level outcomes link trade with labor and environmental standards and represent further WTO-plus outcomes in these areas.<sup>14</sup>

Taken together, it is clear that the PTAs by ASEAN and Malaysia in their negotiations with New Zealand have been prepared to go significantly further than ever before in a range of domestically sensitive areas including services, investment, and a range of other WTO-plus areas such as competition policy and even labor and environment—issues which ASEAN members have resisted incorporating into the WTO process.

<sup>14</sup> The Labor and Environment Memorandums of Agreement between New Zealand and the Philippines and New Zealand and Indonesia in the context of AANZFTA are available at [www.aseanfta.org](http://www.aseanfta.org) and the similar treaty-level outcomes with Malaysia are available through the general website [www.mfat.govt.nz](http://www.mfat.govt.nz) (accessed on 1 March and 7 March 2015).

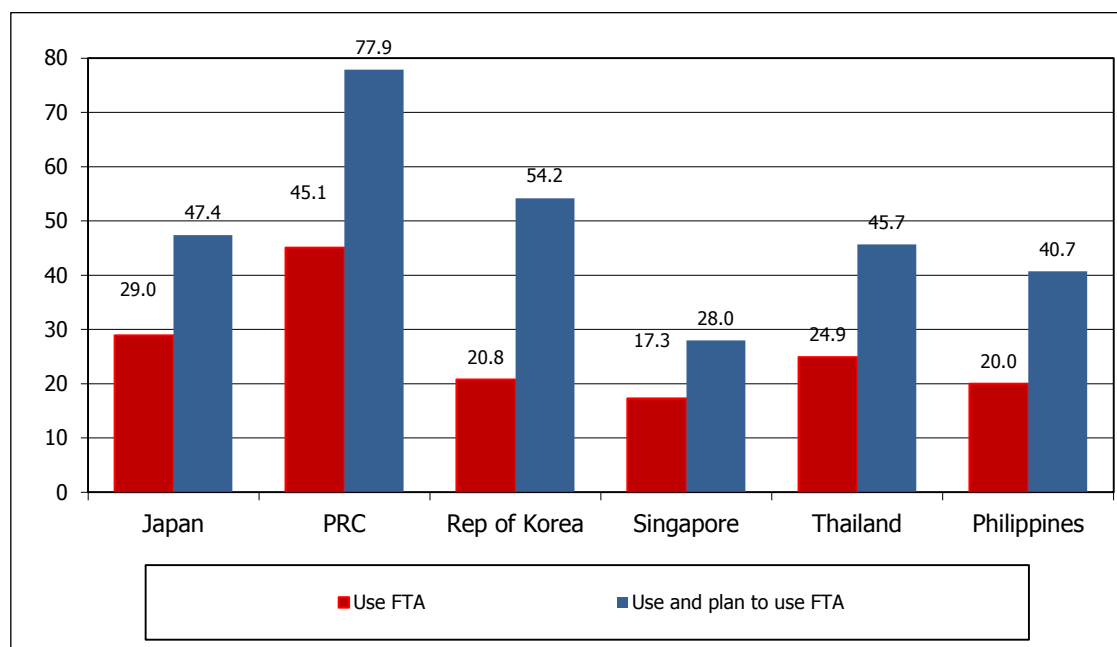
## 4. DEALING WITH THE NEW “NOODLES” IN THE BOWL

There is an existing body of work that has maintained that companies in general do not utilize PTA preferences because of the relatively high transaction costs of compliance and the general complexity of the specific rules of origin in PTAs (World Bank 2007; Takahashi and Urata 2008). That analysis is, however, becoming increasingly out of date.

Ground-breaking work undertaken by Kawai and Wignaraja (2009, 2010, 2011) has revealed that in fact there is rather more interest in securing FTA preferences than was previously expected. Figure 1 illustrates some of the key points. Of the 841 Asian companies surveyed, some 28% reported that they were using PTA preferences.<sup>15</sup> Once this figure is combined with those firms which reported that they intended to use preferences negotiated through a PTA in the future, the overall number is nearly doubled to 53%. Clearly, there are companies in the region who judge that the benefit derived from a preferential tariff rate is worth securing through compliance with a PTA's rules of origin. That said, as Kawai and Wignaraja (2010: 11) observe, while this outcome is “encouraging” there is obvious “room for improvement.”

**Figure 1: FTA Utilization Rates**

(% of responding firms)



FTA = free trade agreement, PRC = People's Republic of China.

Source: Kawai and Wignaraja (2011: 35).

Negotiators have understood the risk of low utilization rates. There is evidence that recent FTAs concluded by countries within the region have explicitly tried to limit the additional transaction costs imposed by rules of origin and sought to ensure that, wherever possible, familiar approaches are maintained. In this way they have encouraged the uptake of PTA preferences. The AANZFTA outcome is particularly

<sup>15</sup> Note that this survey did not include firms from Australia or New Zealand.

interesting in this regard. Negotiators from both Australia and New Zealand on the one hand and ASEAN partners on the other sought to mitigate the risk of overly complex rules of origin for their exporters through some creative adaptation of existing approaches.

ASEAN exporters in general are more familiar with the regional value content (RVC) approach with a 40% free on board threshold. Conversely, Australian and New Zealand exporters have a preference for the change in tariff classification approach adopted in their most recent FTAs. Both approaches have their advantages. The Change of Tariff Classification (CTC) approach provides greater certainty as to the origin (i.e., “once qualify, always qualify”) and in particular reduces transaction costs for SME exporters because the burden of administrative compliance is sharply reduced, including through the removal of much uncertainty inherent in the RVC approach (i.e., as a result of price and currency fluctuations over time). Conversely, the RVC approach ensures that in areas of particular sensitivity, such as iron and steel, where the CTC approach is comparatively restrictive, exporters may still claim a preferential treatment by meeting, for instance, the 40% RVC threshold.

With a view to minimizing new or additional compliance and transaction costs for business, AANZFTA negotiators agreed to “co-equal” or alternative rules for the majority of product lines. In effect, this means that manufacturers and exporters can self-select either the CTC or the RVC approaches, depending on which approach best suits their business model.

In addition, negotiators sought to ensure that the certificate of origin required to secure the AANZFTA tariff preferences was as similar as possible to other COOs utilized in the region. New Zealand negotiators, for instance, sought to ensure a format as similar as possible to that which New Zealand exporters have to comply with under the PRC-New Zealand FTA (NZMFAT 2009a: 17).

Most recently, New Zealand and Malaysia demonstrated an even more flexible and business friendly approach to the risk posed to the “noodle bowl” of rules of origin. Through the Malaysia-New Zealand FTA, the countries agreed that rather than completing a certificate of origin (as is the case in the AANZFTA and in all of Malaysia’s previous FTAs), New Zealand companies could “self-declare” their compliance with the ROO and claim the relevant tariff preference (NZMFAT 2009b: 34). That represents a significant reduction in transaction costs for companies from New Zealand trading into Malaysia and it is to be hoped that as the Royal Malaysian Customs Service becomes accustomed to such a *modus operandi*, it may agree to allow its own firms to use a similar approach and even extend the approach agreed with New Zealand and subsequently Australia (through its bilateral FTA with Malaysia) throughout the region.

## **5. MAKING AND KEEPING PTAS BUSINESS-RELEVANT**

A key challenge in negotiating any PTA is ensuring that it is business-relevant, not simply on day one of the implementation of the agreement, but into the future. In this regard, there is evidence of real creativeness in the way in which ASEAN economies have approached this matter. The following are snapshots of the approach adopted by ASEAN countries and their partners from New Zealand and Australia in the AANZFTA and the MNZFTA.



- *Living agreement.* Both the AANZFTA and the MNZFTA contain an elaborate architecture of committees and other bodies designed to meet regularly to refresh aspects of the agreement and the parties' understanding thereof. There are also built-in opportunities to review and consider emerging issues, including for instance non-tariff barriers and services scheduling issues. In addition, there are programmed negotiating processes established (with agreed and binding time frames) for the preparation of investment market-access schedules. These processes supplement and occur before and after the built-in review clause when AANZFTA is to be formally reviewed in 2016 (a date selected because of its proximity to the expected conclusion of the ASEAN Economic Community process).
- *Movement of businesspeople.* A major difficulty for many companies seeking to operate across the region is certainty of access for businesspeople (services suppliers, goods sellers, and investors). Both the AANZFTA and the MNZFTA provide for creative mechanisms to facilitate access to the various economies involved, including through reporting and publication mechanisms and bindings on existing levels of access, with the MNZFTA broadening the application of measures to all types of businesspeople. In particular, and in response to a frustration expressed by many business in the region, there is a commitment by all parties to provide detailed information on the status of their applications for temporary entry (NZMFAT 2009a: 22) several countries in AANZFTA and through MNZFTA have agreed to extension of stay visas for both visitors and businesspeople seeking to work from the country in question. Indonesia, the Lao PDR, the Philippines, and Thailand agreed to extension of stay commitments for business visitors in the sectors listed in their schedule. Similarly, there have been improvements made by Indonesia, Malaysia, the Philippines, and Thailand for the extension of stay (or new commitments) for intra-corporate transferees (NZMFAT 2009a). The MNZFTA builds further on these types of commitments. Information about Malaysian (and New Zealand) policies affecting movement of natural persons covered under the agreement is to be published much more quickly than the AANZFTA requires (within 6 weeks of entry into force, rather than 6 months). Any changes to policies must be published within 30 days (rather than 90 days under the AANZFTA). Also in the MNZFTA, both countries have agreed on legally binding timeframes for providing information back to applicants about their request for temporary entry access. These are very specific and include a maximum of 15 working days to advise of the receipt of an application; and a maximum of 40 working days for an application to be processed. The length of time that New Zealand businesspeople or services suppliers in financial services can operate in Malaysia has increased from 5 to 10 years. There are no such timeframes in the AANZFTA (NZMFAT 2009b: 23–24). These represent practical and targeted benefits that would not exist in the absence of the PTA. It is also worth noting that these are not the kinds of issues that one can negotiate through the WTO.
- *Customs clearance.* Many companies operating in the region complain bitterly of differential customs procedures and practices and of the impact this has on their ability to service “just-in-time” demands from local importers. The AANZFTA and MNZFTA outcomes were sensitive to this issue with both providing for explicit and legally binding treaty-level commitments designed to facilitate customs clearance in practical ways. The MNZFTA in particular provides for a commitment to 48-hour customs clearance—a practical and immediate benefit in terms of transparency and certainty of processing

procedures to both Malaysian and New Zealand companies (NZMFAT 2009b: 35).

- *Economic cooperation.* A major difficulty with many FTAs has been their incomplete or partial implementation, which in turn reduces their effectiveness both in terms of delivering benefits to the wider population of all parties as well as directly to business. To mitigate this as far as possible, both the AANZFTA and MNZFTA outcomes include a specific chapter on economic cooperation. This is *not* development assistance. The relevant chapter establishes a framework for trade and investment-related cooperation that is designed to enable maximum commercial benefit to be derived from the agreement. In the case of the AANZFTA, for instance, there is a targeted work program that is deliberately designed to develop and enhance technical capacity among the AANZFTA partners in a range of areas including the effective implementation of the agreement's rules of origin, standards and technical regulations and conformity assessment procedures, customs procedures, and so on. The benefits to business are obvious in terms of enhanced technical capacity on the part of importing countries to, for instance, facilitate customs clearance or effectively implement the agreements' certificates of origin; technical and standards-related commitments, and so on. Significantly too, these benefits are in effect multilateral since it will be difficult economically and inefficient to exclude other partners from enhanced technical regulations of customs facilitation procedures. In this way, the PTA can help support exporters from ASEAN and Australia and New Zealand in particular, but indirectly, the multilateral process as well.

## 5.1 CER-ASEAN Integration Partnership Forum: From AANZFTA “At-the-Border” to Economic Integration “Behind-the-Border”

Both Australia and New Zealand are already actively involved in a range of trade and investment-related initiatives with ASEAN. That set of initiatives is designed to help support and drive forward economic integration, albeit through a more traditional PTA-style (i.e., “at-the-border”) focus. Existing vehicles for this include the AANZFTA and MNZFTA processes through their built-in “living” agendas. In particular, the AANZFTA remains a core component of both Australia and New Zealand's broader strategy of economic integration with ASEAN. As noted earlier, the AANZFTA was deliberately conceptualized by negotiators as a “living agreement” through which Australia and New Zealand could continue to engage with ASEAN on trade and investment-related issues beyond the conclusion of the agreement itself. The focus of that engagement, however, was largely and, of necessity, focused on “at-the-border” issues.

To supplement the “at-the-border” focus of the AANZFTA, Australia and New Zealand worked with ASEAN partners to launch the CER-ASEAN Integration Partnership Forum. This was deliberately designed to move the dialogue between the CER partners and ASEAN away from simply the negotiation of issues affecting primarily trade and investment flows “at-the-border” to a conversation with ASEAN about “behind-the-border” integration-related issues. In this sense, the Integration Partnership Forum (IPF) process is designed to share the experiences of Australia and New Zealand in developing the Closer Economic Relationship, which over the past decade has evolved into the Single Economic Market, the focus of which is primarily deepening integration behind the border, e.g., through convergence of regulatory approaches. It is

these experiences that have been of most interest to ASEAN members as they work toward their own stated objective of becoming a regional economic community.

## 6. CONCLUSION

Concerns remain about the rise of PTAs in Asia and the Pacific. These are compounded by the apparent preference of many of the major players to pursue such arrangements bilaterally or plurilaterally in preference to the WTO process. These concerns are also a consequence of the risk of trade diversion, as well as a fear that these agreements may be less than comprehensive in their approach to sensitive issues such as agriculture and have potentially limited ambitions to do much that is WTO-plus. The well-known “noodle bowl”-related concern is another issue that raises the spectre of PTAs facilitating the proliferation of increasingly complex and burdensome ROO, which quite literally may ‘turn-off’ business. Taken together therefore, one may be forgiven for concluding that the PTA agenda is at worst damaging to the region and at best of marginal business interest, while simultaneously acting as a brake—or even a “stumbling block”—to the WTO negotiations through the Doha Development Agenda.

Certainly there is evidence that many, if not quite all, of the FTAs concluded since the late 1990s through until relatively recently were indeed low quality and non-comprehensive undertakings. Many would struggle to meet the GATT Article XXIV test for coverage of “substantially all trade.” This paper, however, has argued that more recent PTA negotiations, particularly since 2008 present a rather more nuanced and complex picture. There may even be some grounds for modest optimism given the high quality, comprehensive, and WTO-plus nature of recent outcomes.

Since 2008, for instance, PTAs concluded between ASEAN countries and Australia or New Zealand (or both) have demonstrated that ASEAN is able to successfully conclude and implement commercially meaningful and comprehensive PTAs. In particular, these recent PTAs are helping to support the liberalization of sensitive agricultural sectors considerably more quickly than those same ASEAN countries had been prepared to do before 2008, let alone at the WTO. There is also evidence that ASEAN members both collectively and individually are prepared to go considerably further in terms of actual commitments that are WTO-plus, outside the goods area, e.g., in services, and to agree to address issues that are not even included in the WTO Doha Round, such as investment, competition policy, and even labor and environmental standards.

There is evidence too that negotiators have understood the message from business and academics about the need to mitigate the risk of complex PTA rules of origin, i.e., of adding more “noodles” to the noodle bowl. Particularly intriguing perhaps is the way that recent PTAs have sought to maintain their relevance over time through creative mechanisms designed to “refresh” the agreement, as well as to include immediate commercial benefits for traders and investors in areas not normally covered by FTAs, let alone any of the existing WTO agreements (or indeed forming part of the Doha Round), including business visitor access and so on.

As this paper has observed, the agreements that reach the highest levels of quality and comprehensivity and address the kinds of issues noted above have involved Australia and New Zealand, either together or separately. This also serves to underline these two countries’ credentials as meaningful and useful partners in the ongoing regional economic integration process, both in Asia and the Pacific, but more broadly as well. It suggests too that when managed well and with the right partners, PTA negotiations can

deliver genuinely “win–win” outcomes that foster and enhance the regional economic integration process.

In conclusion, there remain good reasons to be concerned about the rising number of preferential trade agreements. At the same time, the worst fears of those arguing that regional and bilateral PTAs are simply “stumbling blocks” to multilateralism have not been fully realized either. There are some grounds for optimism that the way in which modern PTAs are evolving is through supporting comprehensivity and quality, including through meaningful liberalization of agriculture; WTO-plus commitments across a range of goods and non-goods-related areas; attempts to address the “noodle bowl” of ROO; as well as an encouraging level of creativity in the development of practical and bespoke solutions for businesspeople trading in the region.

Taken together therefore, the PTA processes in Asia and the Pacific—specifically those that have involved New Zealand and Australia where deep and wide market access and rules-related commitments exist—may now provide the foundation for the conclusion of the multilateral negotiations underway in Geneva. In particular, the current range of WTO-plus commitments provided on a preferential basis to bilateral and plurilateral PTA partners by ASEAN, through the MNZFTA and the AANZFTA, for instance, offer scope for a serious discussion about how the commitments enshrined in those agreements can be brought into the multilateral process, including to facilitate the conclusion of the Doha Development Round. That, after all, is the kind of contribution that Asia and Pacific leaders have in mind with their continued emphasis on “the value, centrality and primacy of the multilateral trading system” (APEC 2014).

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\* ADB recognizes China as the People's Republic of China.

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