# The China-Australia Free Trade Agreement

## A 21st-Century Model

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# 1

# *Australia, China and ChAFTA: Punching Above both Belt and Weight*

COLIN B PICKER

## I. INTRODUCTION

THIS BOOK PROVIDES readers with a unique opportunity to learn about a new regional trade agreement (RTA)—the China–Australia Free Trade Agreement (ChAFTA or the Agreement).[1] This new Agreement, which only came into operation in late 2015, reflects much of the most modern and up-to-date approaches within the international economic legal order (IELO)—at a substantive as well as formative/developmental level. Furthermore, it involves two important participants in the IELO—China and Australia. As such, it is an important modern and ongoing development that should be understood internationally as well as regionally and locally. This introduction will briefly make that case.

Substantively, ChAFTA is very typical of one type of the modern generation of RTAs, far removed from its earlier cousins that came into being decades ago. Many of those older RTAs were negotiated in the years before and in the decade after the World Trade Organization (WTO) was created in 1995—before it was known in what ways or how quickly (or slowly) the overlaying IELO architecture (mainly the WTO) would develop or how the new post-Cold War economic legal order would shape up.[2] Those early RTAs were created in the shadow of the Bretton Woods system (and specifically the subsequent International Trade Organization (ITO) and the General Agreement on Tariffs and Trade (GATT) negotiations) and

[1] Free Trade Agreement between the Government of Australia and the Government of the People's Republic of China (signed 17 June 2015, entered into force 20 December 2015) [2015] ATS 15 (ChAFTA).

[2] The vast majority of today's RTAs have been negotiated prior to 2005. See 'Facts and Figures: How Many Reginal Trade Agreements Have Been Notified to the WTO?' (WTO RTA Gateway, 2017), www.wto.org/english/tratop_e/region_e/regfac_e.htm.

out of the eventual compromise that led to Article XXIV of GATT 1947.[3] In contrast, more recent RTAs are now too far removed from that time and its contexts, and now may represent a new approach, one that begins to shift away from the conceptual confines of Article XXIV. Article XXIV when conceived was primarily concerned about trade diversion—and indeed, historically RTAs were often crafted so as to divert trade in a mutually beneficial way for the parties—to the harm of everyone else.[4] But, arguably today RTAs are more often born from the need to bypass the gridlock of the moribund WTO or for experimentation in liberalisation within the more specific contexts of bilateral or regional relationships. The concern today is less likely trade diversion and more likely the long-term harm to multilateralism as opposed to individual economic dislocations. If so, perhaps it is time to rethink Article XXIV and its equivalent under the General Agreement on Trade in Services (GATS)—Article V of GATS. In the meantime, the new generation of RTAs are leading the way. ChAFTA, as one of the newest of the modern generation RTAs, is also at the forefront of innovation, for example, through its built-in renegotiation commitments[5] and deliberately asymmetric commitments reflecting current realities that are expected to change going forward (eg, its inclusion of both positive and negative list approach to services commitments).[6] Given these and its other developments, the many different contributions in this book that explore ChAFTA's commitments are clearly relevant and important even outside China and Australia.

In addition to a move away from the original concerns of Article XXIV, modern RTAs reflect different geopolitical and economic realities from even 20 years ago—ones radically different from 1947, from 1995, and even from 2015. Today, unlike 1947 and even 1995 the IELO includes a strong and active China, which is now asserting itself regionally (eg, in the South China Seas) and globally (eg, through the One Belt One Road (OBOR) policy). Also, Australia is today not the subservient cousin of the United States it was in 1947, or 1995—and perhaps even significantly less than in 2015, as it slowly emerges from its post-war military reliance on the United States and given confused Trump national security and foreign policy signals. Similarly, the IELO would seem to no longer be led by either the Americans or the Europeans. The United States under Trump drifts in a

[3] See generally CB Picker, 'Regional Trade Agreements v the WTO: A Proposal for Reform of Article XXIV to Counter this Institutional Threat' (2005) 26 *University of Pennsylvania Journal of International Economic Law* 267, 280–81.

[4] ibid.

[5] See, eg, ChAFTA (n 1) Art 8.24.3. After the entry into force of this Agreement, at a time to be mutually agreed by the Parties, the Parties shall initiate the next round of the negotiation on trade in services in the form of negative listing approach, and conclude such negotiation as soon as they could.

[6] See the chapters in this book on services for detailed discussion of the differentiated commitments.

destructive manner through the world order (from undermining NATO to the WTO to NAFTA), while the EU is struggling with an existential crisis brought on by Brexit and other pressures (such as the refugee crisis). While ChAFTA was negotiated before all these most recent developments, it is nonetheless scheduled for further negotiations to extend and correct aspects of the current Agreement—with those negotiations taking place during this new post-Trump, post-Brexit, post-OBOR reality. Hence, following the development of ChAFTA may be akin to observing the conduct of an experiment, with the results of utility across the world—for new RTAs, for understanding China's future directions in the IELO, and for seeing how America's traditional allies operate in this new reality.

Therefore, this introductory chapter focuses on developing further this idea that ChAFTA represents something important for international economic law (IEL) scholars, practitioners and officials—supporting the very title of the book, 'The China–Australia Free Trade Agreement: A 21st-Century Model'. In other words, this chapter will develop the case that ChAFTA is worth exploring not only for the reasons already noted, but also due to the specific parties that are involved—parties whose historic and ongoing role and relationships are both critical in the development of the new IELO and also provide a counterpoint to the usual subjects of IEL analysis—the United States and Europe. In so doing, this introductory chapter will also consider how the book's individual chapters, focusing on specialised aspects of the Agreement, explore the many new features that were not present when the WTO or early RTAs were negotiated, providing insights and lessons about those new or more important trade issues for the twenty-first century, specifically, with focus on the latest approaches to the regulation of investment, twenty-first century services and the emerging digital/knowledge economy.

Finally, in addition to being important for IEL participants around the world wishing to understand the latest approaches and movement in IEL, early analyses of ChAFTA will be important locally and regionally. For, as noted above, ChAFTA has built-in commitments to further negotiations and therefore this book's contributions should also be critical for those ongoing and planned negotiations. In addition to providing deep level analyses of ChAFTA in general and in context, specific chapters will be of direct importance in those renegotiations. For example, the chapters exploring the investment provisions of ChAFTA are especially relevant given both parties have committed to begin discussing unfinished business, such as the investment provisions, and to work to further deepen and liberalise the Agreement.[7] This book is therefore both of local and current salience, as well as providing timeless analysis of features of the IELO for other states

[7] See, eg, ChAFTA (n 1) Art 9.9.3.

and IEL participants in the region and indeed around the world as they all develop their own approaches and find their way through the IELO.

## II. AUSTRALIA AND CHINA: PUNCHING ABOVE WEIGHT AND WAISTLINE

It is legitimate to wonder why IEL practitioners, scholars, students or government officials would be interested in an RTA between the relatively empty and barren country of Australia and the newly emergent quasi-developed quasi-market economy of China. Similarly, the relevance of ChAFTA is not immediately clear to outside observers, but that is discussed in the next section of this chapter (the analyses and insights in the contributions to this book provide the evidence to make a strong case that ChAFTA's substantive aspects should be of more than local interest). This section, however, first focuses on the global, and specifically IELO relevance of the two parties. This section explores why their respective positions within the world are in fact significantly greater than would have been thought given their size (Australia—too small in the IELO) or 'youth' and behaviour (China—too newly joined to the IELO or too different in its behaviour).

### A. Australia: 'Punching Above its Weight'

Australia is not the first country that comes to mind when considering IEL. While geographically impressive, being the only continent-size country, it is sparsely populated with a mere 24 million or so inhabitants.[8] Many cities in the world easily exceed that number (eg, Tokyo, Manila, Delhi, etc).[9] Much of the continent is inhospitable desert, while its climate fluctuates from flood to drought. Furthermore, it is somewhat off the main trade routes—located far down in the southern hemisphere. Nonetheless, it has a very high participation in the world's economy, both in relative and in absolute terms. Despite being fifty-first by population, it is ranked as the twelfth biggest economy in the world.[10] Its educational base is very well developed, especially in the fields relevant to the IELO—it has four law schools in the top 20 of the world, with corresponding significant contributions to IEL scholarship and activity.[11] That influence is also reflected at the governmental

[8] 'The World Factbook' (Central Intelligence Agency), www.cia.gov/library/publications/the-world-factbook/geos/as.html.

[9] See 'World's Largest Cities' *Worldatlas* (2016), www.worldatlas.com/citypops.htm.

[10] 'World in Figures: Rankings' *The Economist* (2017), worldinfigures.com/rankings/topic/7.

[11] QS Subject Rankings in 2017. See 'QS World University Rankings: Law' (QS Top Universities, 2017), www.topuniversities.com/university-rankings/university-subject-rankings/2017/law-legal-studies.

levels—with the Australian government taking a leading role in international activities around the world, and especially in IEL. Australia has been a major influence in the development of free trade agreements (FTAs) in the region.[12] It has also been exceptionally active in the development of mega-RTAs, as evidenced by its involvement in the Regional Comprehensive Economic Partnership (RCEP) and the Trans-Pacific Partnership (TPP) (and its likely successor). Although Australia is today not as active in the WTO's Dispute Settlement Body (DSB) as it used to be, that recent inactivity should not be a measure of its relevance to the IELO—for participation in the DSB is not just a factor of involvement in the IEL, but rather likely reflects cultural and political forces that either encourage or discourage participation in disputes or reflect a willingness to settle disputes rather than permit them to go to the panel stage. That being said, it has been involved in recent important disputes, most notably and currently in the seminal 'Plain Packaging' case.[13] Australia's role in IEL is thus well established—from its significant involvement in the creation of the ITO and GATT[14] to its creation of the Cairns Group[15] to frequent participation in the Doha Round as one of the 'group of five'.[16] To use a boxing metaphor, Australia truly does 'punch above its weight'.[17]

Australia is also geopolitically important. Since the Second World War it has been one of America's closest allies. The fact that Australia sent its own soldiers to fight in Vietnam, Iraq and Afghanistan alongside the United States' military is evidence of a commitment no other country has shown to their alliances with the United States. And yet—China has become a critical economic partner of Australia.[18] Furthermore, from a regional

[12] See T Sekine, chapter 5, section III, page 85 bottom.

[13] 'DS434: Australia—Certain Measures Concerning Trademarks and Other Plain Packaging Requirements Applicable to Tobacco Products and Packaging' (WTO, 7 July 2016), www.wto.org/english/tratop_e/dispu_e/cases_e/ds434_e.htm.

[14] See, eg, A Capling, 'The "Enfant Terrible": Australia and the Reconstruction of the Multilateral Trading System 1946–48' (2000) 40 (1) *Australian Economic History Review* 1, 1–21.

[15] See, eg, RA Higgott and AF Cooper, 'Middle Power Leadership and Coalition Building: Australia, the Cairns Group, and the Uruguay Round of Trade Negotiations' (1990) 44 (4) *International Organization* 589, 589–632. See also P Gallagher, 'Setting the Agenda for Trade Negotiations: Australia and the Cairns Group' (1988) 42 (1) *Australian Outlook* 3, 3–8.

[16] The group included the EU, the United States, Japan, Canada and Australia. See P Blustein, *Misadventures of the Most Favoured Nations: Clashing Egos, Inflated Ambitions, and the Great Shambles of the World Trade System* (New York, Public Affairs, 2009).

[17] To 'punch above weight' means '[i]f a country or business punches above its weight, it becomes involved in, or succeeds in, an activity that needs more power, money, etc. than it seems to have'. 'Meaning of "Punch Above Your Weight" in the English Dictionary' (*Cambridge Dictionary*, 2017), dictionary.cambridge.org/dictionary/english/punch-above-your-weight. The origin comes from boxing when contestants would only fight competitors of comparable weight—there being a heavy weight advantage when it comes to punches. See G Martin, 'The Meaning and Origin of the Expression: Punch Above One's Weight' (*The Phrase Finder*, 2017), www.phrases.org.uk/meanings/290900.html.

[18] It is Australia's number one export and import partner. See 'The World Factbook' (n 8).

perspective Australia has a strong belief and commitment to its future in Asia, and it does seem that Asia is likely of more relevance, especially in the long term, than North America.[19] Hence, Australia's interaction with both China and the United States can perhaps be viewed as a 'bell weather' of global geopolitics—especially in the post-Trump and in the current China Sea disputes environment. Eyes will be on Australia—and its economic relationship with China, especially when it comes time for the next round of negotiations of ChAFTA. At that time, the world will observe Australia's ability to navigate its complex and potentially conflict-ridden relationships with the United States and China.

### B. China: 'Punching Above the Waistline'

While academic publications rarely focus on Australia's involvement with the IELO, it is a different matter with respect to China. Indeed, yet another book on China and its interaction with the IELO will come as no surprise and may also be viewed as not being all that worthy of attention (especially if it involves its interaction with a smaller country like Australia). But, many analyses of China in the IELO are concerned with China being the 'other'—as being outside the 'Club' due to its different characteristics and contexts and consequent perceived behaviours.[20] This is not surprising given how different China appears to the traditional power bases of the IELO (Europe and America). The perceived sources of China's difference include the fact that China: has the largest population in the world; is relatively newly industrialised/modernised; is a new superpower; is under tight internal political control, including restrictions on free speech; employs a centralised non-market economy structure; has perceived rampant corruption; is at least nominally a socialist system; has had historic and destructive instabilities (even in the second half of the twentieth century); and finally has strong and ancient non-Western characteristics. These traits are often viewed by many as obstacles to China having a 'regular' or 'normal' participation in the IELO. For some there is an even greater concern, that China's differences create a critical challenge to the established, largely Western, neo-liberal approaches of the modern international legal order. Many, rightly or wrongly, then believe China is a power that is outside what is considered normal or acceptable in the IELO. Those views are informed, rightly or wrongly, by

[19] See, eg, Australian Government, *Australia in the Asian Century* (White Paper, 2012), www.defence.gov.au/whitepaper/2013/docs/australia_in_the_asian_century_white_paper.pdf.

[20] See T Webster, 'China's Implementation of WTO Decisions' in C Picker, L Toohey and J Greenacre (eds), *China in the International Economic Order: New Directions and Changing Paradigms* (New York, Cambridge University Press, 2015) 98–102 (providing background of these sorts of views).

the perception that the IELO is mostly made up of middle-sized neo-liberal countries where governmental participation in the economy is viewed with disfavour. China is also often viewed, again—rightly or wrongly, as a rule breaker in the IELO, that it continually fails to honour its commitments—with abuses ranging from permitting violations of intellectual property to providing unfair subsidies to currency manipulation and so on. To extend the boxing metaphor, it is believed by many that China too often 'punches below the belt'.[21]

But, China today is perhaps no more of a rule breaker in the IELO than the other major powers. Indeed, many recent analyses of China's actions in the IELO suggest it is no worse than the other large powers. For example, recent studies suggest it behaves comparably in such critical measurements as WTO DSB compliance.[22] Furthermore, its domestic non-market centralised controls are diminishing more and more each year (via such initiatives as the Shanghai Free Trade Zone), and certainly may also suffer from decentralised provincial level challenges as opposed to centrally directed violations of IELO obligations. Certainly, there remain areas of concern for other members of the IELO, but then every complex economy provides areas of concern to others, just as many have provinces and other sub-federal entities with actions that lead to IEL liabilities for the federal or central government. So, while China may still occasionally 'punch below the belt', as do so many others in the IELO, it also can be viewed more and more as a party that now regularly 'punches above the belt' in the IELO arena—becoming a rule follower more than a rule breaker. Indeed, China is now much more active in the WTO's ongoing negotiations, in its DSB, in developing investment treaties, and in regional arrangements such as the RCEP. Hence, more and more it will be the case that China's interactions with the IELO will be viewed as 'normal'. Therefore, when it is innovative in the IELO, as is the case in ChAFTA, its actions should be worthy of emulation and attention from the rest of the world.

So—while both Australia and China are often viewed as largely irrelevant to the positive development of the IELO, one because of its size, the other because of its perceived character and behaviours, it may in fact be the case that both play a role different from expected—one punching above its weight, the other punching above the belt. As such, both deserve to be

[21] This phrase comes from boxing and other contact sports where it is not permitted to hit below the waist belt. It means, among other things, to act unfairly. See G Martin, 'The Meaning and Origin of the Expression: Below the Belt' (*The Phrase Finder*, 2017), www.phrases.org.uk/meanings/61100.html.

[22] Webster (n 20) 110–11. "China's compliance with the WTO, in contrast, has significantly exceeded its performance in other legal regimes. In many instances, China has made major revisions to its domestic legal system in order to comply with the DSB rulings. Moreover, China has done so typically within the reasonable period of time in which it agreed to do so." (footnotes omitted).

taken as seriously as the other major participants in the IELO. Accordingly, when they enter into a modern and innovative RTA, that RTA then deserves to be considered for it is likely to be of relevance to the development of the IELO. The next section further develops this idea as it draws on this book's contributions to show the many interesting and innovative approaches and issues for the larger IELO that are explicitly part of ChAFTA.

## III. THE RELEVANCE OF CHAFTA'S APPROACHES FOR THE REST OF THE WORLD

As the contributors to this book note, ChAFTA has certain interesting features that can be explored to better understand the content of these new generations of RTA. ChAFTA also provides an example of an RTA that can be assessed to see how it may survive and thrive in the dynamic post-Brexit, post-Trump, post-OBOR economic legal environment—environments that are clearly both more dynamic and more static than anyone would have predicted at the birth of this modern international trade environment in 1995. As a result, a modern RTA needs to anticipate rapidly changing technologies and other forces even as it copes with the profound depression of a dysfunctional WTO in the IELO. Yet, these new RTAs must also navigate the turbulent waters caused by new and emerging mega-RTAs that engulf or encircle its participants. It is precisely issues such as these that the contributions in this book consider as they explore the many significant aspects of ChAFTA, from domestic constitutional concerns to encircling mega-RTAs to the challenges raised by pre-existing investment agreements to the role that ChAFTA will play in nurturing the dynamic 'innovation economy'.

In exploring these issues and the challenges to a modern RTA this book is divided into four main themes: (A) ChAFTA in its many contexts; (B) services; (C) investment issues; and (D) the knowledge economy. The first part focuses on the wider contexts of ChAFTA because the contexts provide both the rationale and fundamental environments within which ChAFTA will either succeed or fail. The next three parts then delve down into ChAFTA's details as the contributions address the themes raised above, for it is ChAFTA's approaches to services, investment and the knowledge economy which highlight its value as a lesson and harbinger of China's and other states' future RTAs and interactions with the wider IELO. Other subfields could also have been explored—such as its approach to goods or technical barrier to trade—but it is ChAFTA's consideration of these three other fields that are mostly novel or critical for the parties and the development of IEL.

But before those sections, this book also provides a second introduction to consider in detail ChAFTA's provisions—albeit from an analytical perspective. That chapter, by Heng Wang in 'An Analytical Introduction to ChAFTA: Features and Challenges', takes readers through ChAFTA's

central components during which Wang notes the role of pragmatism and innovation in ChAFTA. Might this suggest that ChAFTA can serve as a safe opportunity for China to experiment with a developed Western country? The lessons from which could then be used in its later negotiations with other Western systems? Specifically, Wang's discussion of ChAFTA's scheduled approach—with renegotiation built in—suggests a model that might suit China as it permits the creation of an initial agreement even before reaching the confidence levels required for a more detailed and demanding RTA—one that can then be created as part of the later negotiations.

## A. Contexts

Following the introductory chapters, the first part of the book then considers the contexts relevant to ChAFTA—from internal to regional to global contexts. The first explores a context insufficiently explored in most IEL works—the legal-cultural context.[23] Nicholas Morris' chapter, 'A Comparative Context: Ensuring Australian and Chinese Legal Systems Coexist to Facilitate Harmonious and Trustworthy Trade', explores the role of the Australian and Chinese legal cultures and in particular their impact on such critical issues as the trust needed to make the Agreement work. His examination and recommendations should be considered by those directly involved in the implementation and renegotiation of the Agreement. Given the levels of mistrust in the world with China's involvement in the IELO (the massive accession agreement, although now an old example, still reflects the lingering issue) and China's mistrust of the rest of the world's motivations for their approaches (such as the continuing de facto non-market status), the pathway Morris describes is one that should be taken on board as other countries work with China on RTAs and other IEL agreements.

Of course, ChAFTA does not take place in isolation—it must coexist in the larger region and among and within the various other IEL agreements existing and under consideration. Chang-fa Lo in his chapter, 'ChAFTA's External Impact on Related Mega-FTAs', explores the role of ChAFTA on other agreements, especially the TPP Agreement and the RCEP—and the role of those Agreements, whether ultimately enacted or not, on ChAFTA. The relationship between all these Agreements spans everything from the geopolitics of the TPP Agreement to more technical issues such as the overlap in commitments among all the agreements. Geopolitically, Lo notes the critical role that is played by ChAFTA—counteracting the United States' attempted containment of China, especially as Australia is such an ally of

[23] But see CB Picker, 'Comparative Legal Cultural Analyses of International Economic Law: Insights, Lessons and Approaches' (2014) 6 *The Indian Journal of International Economic Law* 54, 54–83.

the United States. ChAFTA is strategically a critical part of the geopolitical puzzle of the region. But, the fact that Australia can simultaneously enter into ChAFTA and play a more adversarial role with China strongly suggests that it can be possible to separate geopolitics and economics. This supports a long-held view that progress within the IELO is typically independent of geopolitics.[24]

A more specific example of the fact that ChAFTA cannot be considered in isolation is found in Takemasa Sekine's chapter, 'The Australia–China FTA and Australia's FTAs with Other Asian Countries: Their Implications for Future SOE Regulation'. In that chapter, Sekine explores the many different ways that RTAs have dealt with SOEs (state-owned enterprises), from strict to moderate to no regulation, and finds that ChAFTA, surprisingly, follows the last—essentially no regulation of SOEs. Sekine's detailed analysis dives deep into the regulations of SOEs in the ChAFTA parties' other RTAs. This leads him to the conclusion that an Australian-style competitive neutrality approach would be compatible with ChAFTA and that the parties should and can progressively work towards that goal. Thus, this wider context suggests the future direction that should be taken with respect to SOEs between the ChAFTA parties.

### B. Services

After considering the different context surrounding and impacting ChAFTA, this book turns to one of the most critical areas of the modern IELO—trade in services. As states become ever more developed more of their economy ends up falling within the services sector, and indeed the share of their international trade will increasingly be dominated by services. This is already the case for the United States.[25] Australia too is significantly reliant on its services sector, with ChAFTA's main benefits perhaps being the potential opening up of China to Australian service exporters.[26] Four of the book's authors focus on services—covering very different perspectives and aspects of the Agreement—and correspondingly different insights and lessons for the parties, the region and the rest of the IELO.

First Jingxia Shi in her chapter, 'Services Liberalisation in ChAFTA: Progress Assessment and the Way Forward', presents an overview of the unprecedented market access commitments provided by ChAFTA. She then focuses on the unique mixed scheduling approach of ChAFTA—that

[24] See, eg, A Reich, 'The Threat of Politicization of the WTO' (2005) 26 *University of Pennsylvania Journal of International Economic Law* 779.

[25] See 'The World Factbook' (n 8).

[26] 'The services sector is the largest part of the Australian economy, accounting for about 70% of GDP and 75% of jobs'. ibid.

Australia has committed to a negative list approach while China makes its services commitments via a positive list approach. This bifurcated approach reflects the current fundamental differences in the two parties' trade in services—each at different points on the economic development ladder. Shi then discusses the anticipated eventual move of China to a negative list approach via the planned negotiations—a mechanism that has much to offer—within ChAFTA and as a model for other agreements that face similar asymmetric economic development challenges.

The services discussion in the book then proceeds to consider at a detailed level three service areas that are especially relevant to the parties and to the rest of the world: the movement of individual cultural services providers; legal services; and education services. Each of the analyses provides valuable insights to the states, the IELO and, most relevantly some might say, to our readers (typically being lawyers and/or educators). These contributions clearly show the critical nature of services in the IELO—especially to advanced economies and their IELO specialists!

The first analysis of a detailed area of services, by Shin-yi Peng, Han-wei Liu and Ching-fu Lin, considers cultural services in the chapter 'Culture-Oriented Mode 4 under ChAFTA: Policy Considerations'. There they note that cultural services are invariably associated with individuals—be they chefs or musicians, all of whom can deliver those services via their presence in another market (Mode 4 delivery). This chapter's analysis is especially critical in today's world given the prominence of immigration and foreign workers in domestic politics. Indeed, this is even more the case as it relates to participation in the IELO—as evidenced by the significant role that migration and immigrants played in the lead up to the Brexit referendum. The analysis in this chapter shows that ChAFTA has clearly approached the issue in light of this modern context, but did so in a culturally focused and respectful manner.

The next examination of services, by Weihuan Zhou and Junfang Xi in their chapter, 'Breakthrough or Standstill? China's Liberalisation of Legal Services under ChAFTA', is important in showing the relationship between real and illusory services gains from trade agreements. It explores the trade in legal services provisions of the ChAFTA and hence is also of personal relevance to the many legal services providers that would be the likely readers of this book! The chapter's examination finds that ChAFTA has not really provided greater market access to Australian legal professionals than has been extended by China to other foreign legal professionals through such Chinese domestic initiatives as the Shanghai Free Trade Zone. Perhaps it is going too far to describe it as an illusory liberalisation, but certainly the lack of tangible benefit does raise some serious concerns.

Finally, and perhaps most relevant for Australia's economy is a chapter by Eva Chye, 'Trade in Education Services under ChAFTA: What does it Mean for Australia?' As Chye notes, this chapter explores the number three export

and the number one services export of Australia—education services.[27] ChAFTA's new treatment of this vital industry is especially important as the industry has changed greatly since GATS was launched in 1995—with a dramatic reliance by the universities now on revenue generated by international students. ChAFTA thus provides a timely approach for this vital industry—updating approaches from GATS and reflecting, as noted by Chye, the specific context that China is the primary supplier of foreign students to Australia. Thus, for Australia given the centrality of education services to the economy, they were always going to be considered front and centre—especially when its number one export market, China, was the counterparty. This chapter also allows examination of the very industry of which many of the readers (be they scholars or students) are members, as well as by readers that used to be in that industry, for all government and private practitioners were themselves trained in those very universities—often outside their own country and hence were participants in the trade itself.

Critically, all these chapters on services show how an intensive goods-exporting economy, such as China, can reach a fair deal with a services-strong modern Western economy, such as Australia, so that both feel they have got a fair deal. In a time when trade deals are much maligned, ChAFTA is a breath of fresh air, clearly showing the benefits to sophisticated, but different economies, and how they can gain from trade. In some sense, it is a perfect example of Ricardian comparative advantage being used properly (or perhaps the more modern factor theorem approaches at play).

### C. Investment

The next section of the book focuses on one of the linchpins of the future of the Australia–China relationship—investment. Four of the contributors explore different aspects of investment regulation and ChAFTA and in so doing provide insights of universal applicability for the IELO in general, for other RTAs specifically, and for Australia and China individually.

As with the services section of this book, first an overview is provided. Vivienne Bath delivers an in-depth general overview of the investment provisions in her chapter, 'Substantive Provisions in ChAFTA's Investment Chapter'. But, she also rightly notes the fact that 'after 10 years of negotiation, completion of most of the substantive provisions of the Investment Chapter

[27] 'The latest figures firm up education's position as Australia's third-largest export after coal and iron ore, as well as its position as the largest services export, well ahead of tourism'. T Dodd, 'Education Revenue Soars to Become Australia's 20 Billion Export' *Australia Financial Review* (3 February 2016), www.afr.com/news/policy/education/education-revenue-soars-to-become-australias-20-billion-export-20160203-gmke3k#ixzz4jkkXtrs0.

has been deferred for later negotiations'.[28] As such, this chapter provides analysis of the many interesting possibilities that may result from the future negotiations of the parties. Consequently, for the parties this is a critical chapter for when they sit down to negotiate. For the rest of the world it is also important, for it shows that even when an agreement does not tackle hard issues, it does not need to totally abandon them. Rather, it can merely postpone them for a later agreed upon time, during which mutual trust and understanding can develop to provide a more fertile field for the negotiations.

The book's consideration of investment then moves to tackle a fundamental issue for new agreements—what to do about prior agreements. Specifically, Tania Voon and Elizabeth Sheargold in their chapter, 'Australia, China and the Coexistence of Successive International Investment Agreements' consider the role and function of ChAFTA's investment provisions in light of a pre-existing 1988 Australia–China BIT.[29] As they note, the fundamental problem is that ChAFTA is but a skeleton of an investment chapter[30] with its focus being national treatment and Most-Favoured-Nation (MFN) treatment, yet still reflecting the very modern approach of providing substantive and procedural protections for state policies. In contrast, the older and pre-existing BIT contains the usual investment protections (fair and equitable treatment and expropriation protections) but does not carve out policy exceptions. This chapter unfortunately concludes that ChAFTA's new provisions and approaches are unlikely to displace the applicability of the prior BIT, leaving Australia open to outdated Investor–State Dispute Settlement (ISDS) claims. Luckily, as noted above, the parties will be sitting down to negotiate more comprehensive investment provisions which will hopefully cure this issue.

Given investment is at its heart an action within a country, more so than trade which involves the movement across borders, it makes sense to consider the investment provisions from the internal perspectives of the two countries involved. Accordingly, Shu Zhang considers internal Chinese aspects of ChAFTA's investment provisions in her chapter, 'A Comparative Review of the Investor–State Arbitration Clause in ChAFTA from China's Perspective: Moving Forwards or Sideways?' The chapter at a fundamental level considers whether or not ChAFTA's investor–state arbitration clause reflects China's progression towards including more comprehensive investor–state arbitration provisions in its IEL relations. Ultimately the chapter suggests it is not, which is a step backwards from China's other recent agreements. This raises many questions, of course. Among them is

[28] V Bath, chapter 10, page 195.

[29] Agreement between the Government of Australia and the Government of the People's Republic of China on the Reciprocal Encouragement and Protection of Investments (signed 11 July 1988, entered into force 11 July 1988) [1988] ATS 14.

[30] T Voon and E Sheargold, chapter 11, 215.

whether this is an indication of increased Chinese investment regulation conservatism. Regardless, other states need to be aware of this regression if they are going to be seeking investment arrangements with China.

The last investment chapter then looks at the investment provisions from an Australian perspective—albeit one focused on the internal constitutional challenges presented by Agreements such as ChAFTA. Lisa Burton Crawford, Patrick Emerton and Emmanuel Laryea in their chapter, 'Investor–State Dispute Settlement and the Australian Constitutional Framework', situate their analyses completely within Australia's constitutional law as they consider the constitutionality of ChAFTA's ISDS provisions. While ultimately the chapter finds that the Australian executive is not necessarily permitted to enter into these sorts of agreements in the absence of explicit legislative authorisation, this procedural requirement is not insurmountable.[31] But, if legislative support is provided then the democratic legitimacy of ISDS would be bolstered and given the often negative view of ISDS it would seem to be worth ensuring that those sorts of provisions are as embedded in the democratic process as possible. The constitutional analysis here, while centred on Australia, is nonetheless instructive in a time of continued challenge to the legitimacy of many aspects of the IELO. Furthermore, this chapter presents some of the constitutional and democratic challenges that may arise in today's IELO for new 'players' in the IELO—for example, newly democratic states (eg, Myanmar) or states that are recently re-entering the IELO as independent participants (eg, Britain post-Brexit).

### D. The Knowledge Economy

The last section of the book provides three chapters that focus on cutting-edge issues in IEL that result from the interaction of new technologies and globalisation—as part of e-commerce or the knowledge economy. As in the other sections, the first chapter of this section, by Henry Gao in his chapter, 'E-Commerce in ChAFTA: New Wine in Old Wineskins?', provides an overview of e-commerce provisions—in ChAFTA, other RTAs, especially those of Australia and China, as well as providing the background on the efforts to develop provisions within the WTO. Ultimately, using those comparisons Gao concludes with recommendations that would improve the e-commerce chapter of ChAFTA were it to be part of the renewed negotiations.

Jeanne Huang in her chapter, 'Expanding the E-Commerce Chapter in ChAFTA: A Green Box, Orange Box and Red Box Approach', takes the analysis of ChAFTA's e-commerce into even deeper detail and critique,

[31] L Burton Crawford, P Emerton and E Laryea, chapter 13, page 277.

employing a green, orange and red box form of analysis of what might be possible when the parties seek to renegotiate and improve ChAFTA's e-commerce provisions. In doing so, she draws on other agreements, such as the TPP Agreement, as examples of what might be possible. Nonetheless, she takes into account the other critical contexts that may stand as obstacles to the further liberalisation of e-commerce—especially for China. In particular, she notes that China's approach towards the internet, freedom of expression and national security may very well present some significant challenges to future change in some of the areas of e-commerce.

The book concludes with Ken Shao's chapter, 'The Ideas Boom: The Innovation Economy in the Post-ChAFTA Australia–China Relationship', which explores the role of ChAFTA's intellectual property provisions in the context of what is emerging to be perhaps one of the most critical parts of the economy around the world—the boom in what Shao calls the 'innovation economy'. While admitting that ChAFTA's intellectual property provisions do not really go beyond those already committed in other agreements, especially the WTO, he applauds its 'flexible approach' as being ideally suited to nurturing this critical sector in both economies.

## IV. CONCLUSION

This book's contributions will be critical for the ongoing development of ChAFTA. Hopefully the insights from those contributions will play a role in the forthcoming negotiations to improve, deepen and extend ChAFTA. But, as noted above, this book and ChAFTA itself, may also have a larger role to play in the IELO. While ChAFTA may seem to regulate a far-off narrow part of the world's trade, it is in fact of great relevance and importance beyond the two countries involved. Its relevance and importance is related to many very different factors, including: the fact that it reflects recent innovations in trade regulation, includes unique and innovative aspects; concerns two important countries and their regions for the IELO; and presents a model for RTAs between such disparate countries (Western and non-Western, developed and developing, massive and medium/small, and so on).

While of course ChAFTA involves two powers not typically part of the traditional power bases of the IELO, it nonetheless reflects the importance of the Asia-Pacific region, especially North–South economic relationships. ChAFTA also reflects the needs of Western middle powers (Australia) and newly developed non-Western powers (China), an interesting and all too often neglected bilateral relationship form. Also, given the United States' withdrawal from multilateralism and IEL while Europe is in an extended period of instability, it remains for countries like Australia and China to help lead any progress in the IELO. Fortunately, the many lessons for the world are clear from the contributions here.

Finally, as ChAFTA shows, the IELO is a world project. All are players. All contribute. By focusing mainly on the European Union and America or on clusters such as developing states or the BRICS or on the mega-RTAs it is too easy to miss developments elsewhere. ChAFTA is thus excellent for showing that there are other parts of the IELO that include sophisticated development within the IELO. Indeed, it is good for scholars, practitioners and officials to focus on run of the mill 'old-school' RTAs instead of the usual focus on the mega-RTAs (many of which are doomed to not be ratified or where the substantive parts simply reflect the lowest common denominator of the many parties). Regular RTAs are here to stay, continuing to form the backbone of the trade system. It would be too easy for scholars and IELO officials and practitioners to miss the lessons and insights of an agreement such as ChAFTA. This book's value is thus both in its contribution to the further development of ChAFTA, the RCEP, the TPP, the regions other relationships (economic as well as geopolitical) but also to the wider IELO. True, while China's participation in the IELO is not normally the place that many would look for global models or for new innovations and while Australia is too little considered at all, as the contributions in this book suggest, the ChAFTA example may be a place to look as the world wends its way through this new IELO.

# 5

# *The China–Australia FTA and Australia's FTAs with Other Asian Countries: Their Implications for Future SOE Regulation*

TAKEMASA SEKINE

## I. INTRODUCTION

AUSTRALIA HAS RECENTLY enhanced its presence in East Asia in terms of trade relations. This is best illustrated by the series of free trade agreements (FTAs) it concluded, between 2014 and 2015, with China,[1] South Korea[2] and Japan.[3] It also joined the Trans-Pacific Partnership (TPP),[4] which also embraces some Asian countries.

However, regarding the content of trade agreements, Australia's approach is not always consistent and prominent differences can be seen in the regulation of state-owned enterprises (SOEs) in its agreements with other states. Australia partially succeeded in including a provision based on the concept of 'competitive neutrality'—in the current context, this mainly implies the internal policy that Australia has developed to regulate its own SOEs—in the Singapore–Australia FTA (SAFTA),[5] the Korea–Australia FTA (KAFTA)[6] and the Japan–Australia Economic Partnership Agreement (JAEPA).[7]

[1] Free Trade Agreement between the Government of Australia and the Government of the People's Republic of China (signed 17 June 2015, entered into force 20 December 2015) [2015] ATS 15 (ChAFTA).

[2] Free Trade Agreement between the Government of the Republic of Korea and the Government of Australia (signed 8 April 2014, entered into force 12 December 2014) [2014] ATS 43 (KAFTA).

[3] Agreement between Japan and Australia for an Economic Partnership (signed 8 July 2014, entered into force 15 January 2015) [2015] ATS 2 (JAEPA).

[4] Signed on 4 February 2016.

[5] Singapore–Australia Free Trade Agreement (signed 17 February 2003, entered into force 28 July 2003) [2003] ATS 16 (SAFTA).

[6] KAFTA (n 2) Art 14.4.

[7] JAEPA (n 3) Art 15.4.

These SOE-related provisions are distinguishable from those included in the FTAs concluded by the North American Free Trade Agreement (NAFTA)[8] Members.[9] While the provisions in two recent Australian FTAs—KAFTA and JAEPA—are somewhat toned down compared with SAFTA, those three Agreements as a whole serve as an effective stepping stone for dissemination of a broad and flexible approach in internationally regulating SOEs.

Conversely, the China–Australia FTA (ChAFTA) did not establish any rules on the behaviours of SOEs beyond those prescribed in the World Trade Organization (WTO) agreements. This is more notable given that other FTAs concluded by China shortly before ChAFTA—for example, the Switzerland–China FTA—require application of competition law to all undertakings of the parties, including undertakings with special and exclusive rights.[10]

Amid those developments, the TPP Agreement, embedded with SOE regulation, was signed in February 2016. Although the TPP itself is unlikely to come into force due to US opposition, it is likely that a successor agreement involving many of the other TPP signatories and much of the substance of the TPP will eventually come into force; hence the relevance of the detailed discussion of the TPP in this chapter. Indeed, the TPP has succeeded in incorporating not only the traditional disciplines inherited from the General Agreement on Tariffs and Trade (GATT) and NAFTA, ie, non-discrimination and commercial considerations, but also the new legal framework labelled as non-commercial assistance (NCA). Some of the new rules set forth under the NCA framework are quite ambitious and without precedent.

We can therefore see at least three options for transnationally regulating SOEs: the strict regulation invented in the TPP Agreement; the more moderate and flexible approach incorporated in SAFTA, KAFTA and JAEPA; and no additional regulation.[11] Among these, ChAFTA chose the third option, despite other possibilities—in particular the second option. This chapter will investigate the implications of this policy selection in ChAFTA, taking into account the evolution of the other options. Section II of this chapter considers Australia's overall approaches in its FTA to SOE regulation. Sections III and IV examine more specifically SOE regulations in SAFTA, KAFTA and

[8] North American Free Trade Agreement (signed 17 December 1992, entered into force 1 January 1994) 32 ILM 289 (1993) (NAFTA).

[9] See, eg, ibid Arts 1502, 1503; see also, Free Trade Agreement between Canada and the Republic of Korea (signed 22 September 2014, entered into force 1 January 2015) Arts 15.2, 15.3.

[10] Free Trade Agreement between the Swiss Confederation and the People's Republic of China (signed 6 June 2013, entered into force 1 July 2014) (Switzerland–China FTA).

[11] With regard to FTAs concluded between countries outside the Asia-Pacific region, the Canada–EU FTA, for instance, explicitly confirms the application of competition law to SOEs (Art 17.3) in addition to provisions directly addressing SOEs' behaviours that are comparable to those in NAFTA (n 8) Arts 18.4, 18.5.

JAEPA, and consider the trends in these Agreements. Section V examines the peculiarity of ChAFTA in light of the other FTAs. Section VI considers the SOE chapter of the TPP Agreement which may influence, in some way, future SOE regulation under trade agreements. With these in mind, section VII considers how ChAFTA and other FTAs can contribute to the development of SOE regulation in the Asia–Oceania region.

## II. AUSTRALIA'S FTAs AND SOE REGULATIONS

Although Australia is perceived as having succeeded in becoming an exemplar of SOE regulation in the domestic market,[12] its same efforts in regulating SOEs in the international space are not yet so innovative. The contents of SOE regulation in its FTAs are comparatively less demanding than the US approach and are inconsistent. SOE regulation in Australia's FTAs can be roughly divided into two categories: NAFTA-style and competitive neutrality style (Table 1).

**Table 1: SOE Regulations included in Australia's FTAs**

| Name of Agreement | Provision(s) relating to SOE | Approach |
|---|---|---|
| Australia–Papua New Guinea | – | |
| SPARTECA | – | |
| ANZCERTA | – | |
| Singapore–Australia FTA | Ch 12, Art 4 | Competitive neutrality |
| Thailand–Australia FTA | – | |
| US–Australia FTA | Arts 14.3 and 14.4 | NAFTA-style, with competitive neutrality applicable to Australia |
| Australia–Chile FTA | Arts 14.4 and 14.5 | NAFTA-style |
| ASEAN–Australia–New Zealand FTA | – | |
| Malaysia–Australia FTA | Art 14.4(3) | Application of competition laws |

*(continued)*

[12] M Rennie and F Lindsay, 'Competitive Neutrality and State-owned Enterprises in Australia: Review of Practices and Their Relevance for Other Countries' (2011) OECD Corporate Governance Working Papers No 4, 44 www.oecd-ilibrary.org/governance/competitive-neutrality-and-state-owned-enterprises-in-australia_5kg54cxkmx36-en?crawler=true.

**Table 1:** ***(Continued)***

| Name of Agreement | Provision(s) relating to SOE | Approach |
|---|---|---|
| Korea–Australia FTA | Art 14.4 | Competitive neutrality |
| Japan–Australia EPA | Art 15.4 | Competitive neutrality |
| China–Australia FTA | – | No competition chapter; no specific SOE regulation |
| TPP | Ch 17 | Commercial considerations and non-commercial assistance |

The NAFTA-style agreements' regulation of SOEs is founded on the concept of 'non-discrimination and commercial considerations', rooted in the prescriptions of GATT Article XVII. The first two subparagraphs of Article XVII provide:

> 1. (a) Each contracting party undertakes that if it establishes or maintains a State enterprise, wherever located, or grants to any enterprise, formally or in effect, exclusive or special privileges, such enterprise shall, in its purchases or sales involving either imports or exports, act in a manner consistent with the general principles of non-discriminatory treatment prescribed in this Agreement for governmental measures affecting imports or exports by private traders.
>
> (b) The provisions of subparagraph (a) of this paragraph shall be understood to require that such enterprises shall, having due regard to the other provisions of this Agreement, make any such purchases or sales solely in accordance with commercial considerations, including price, quality, availability, marketability, transportation and other conditions of purchase or sale, and shall afford the enterprises of the other contracting parties adequate opportunity, in accordance with customary business practice, to compete for participation in such purchases or sales.

According to the Appellate Body in *Canada—Wheat Exports and Grain Imports*, GATT Article XVII:1(b) should be interpreted in accordance with paragraph 1(a), which means that the former must be understood as clarifying the scope of the latter.[13] Therefore, the requirement of commercial considerations becomes relevant only when the transaction at issue is discriminatory (including the treatment of dissimilar situations in a formally identical manner). In other words, the commercial considerations requirement will be taken into account when examining whether discriminatory behaviour can be justified under GATT Article XVII.[14] It does not

[13] Appellate Body Report, *Canada—Measures Relating to Exports of Wheat and Treatment of Imported Grain* 89, WT/DS276/AB/R (30 August 2004) (*Canada—Wheat Exports and Grain Imports AB Report*).

[14] ibid 110–12.

require state trading enterprises (STEs)[15] to act commercially in any transactions.

Another notable interpretation given by the Appellate Body in the above case was that paragraph 1(b) 'refers to purchases and sales transactions where: (i) one of the parties involved in the transaction is an STE; and (ii) the transaction involves imports to or exports from the Member maintaining the STE'.[16] Given this interpretation, GATT Article XVII:1 will not be applied to an STE's transaction when no foreign enterprises are directly involved in the transaction. For instance, an STE's sale of goods to domestic enterprises with non-commercial low prices that are to the detriment of imports *competing with* the STE, falls outside the scope of GATT Article XVII:1.[17]

While SOE regulation under NAFTA shares basic elements with GATT Article XVII, the former's detail differs slightly, in particular from the above interpretation given by the Appellate Body. NAFTA contains two provisions pertinent to the regulation of SOEs: the first addresses monopolies (Article 1502) and the second applies to state enterprises (Article 1503). Article 1502(3) prescribes as follows:

> Each Party shall ensure, through regulatory control, administrative supervision or the application of other measures, that any privately owned monopoly that it designates and any government monopoly that it maintains or designates:
>
> (a) acts in a manner that is not inconsistent with the Party's obligations under this Agreement wherever such a monopoly exercises any regulatory, administrative or other governmental authority that the Party has delegated to it in connection with the monopoly good or service, such as the power to grant import or export licenses, approve commercial transactions or impose quotas, fees or other charges;
> (b) except to comply with any terms of its designation that are not inconsistent with subparagraph (c) or (d), acts solely in accordance with commercial considerations in its purchase or sale of the monopoly good or service in the relevant market, including with regard to price, quality, availability, marketability, transportation and other terms and conditions of purchase or sale;
> (c) provides non-discriminatory treatment to investments of investors, to goods and to service providers of another Party in its purchase or sale of the monopoly good or service in the relevant market; and

[15] While there is no definition of STEs in GATT, the Understanding on the Interpretation of Article XVII of the General Agreement on Tariffs and Trade 1994 adopted a 'working definition', in which STEs are described as: 'Governmental and non-governmental enterprises, including marketing boards, which have been granted exclusive or special rights or privileges, including statutory or constitutional powers, in the exercise of which they influence through their purchases or sales the level or direction of imports or exports'.

[16] *Canada—Wheat Exports and Grain Imports AB Report* (n 13) 157.

[17] However, the Appellate Body's decision intimates a different interpretation may be adopted in a different situation. ibid 160.

(d) does not use its monopoly position to engage, either directly or indirectly, including through its dealings with its parent, its subsidiary or other enterprise with common ownership, in anticompetitive practices in a non-monopolized market in its territory that adversely affect an investment of an investor of another Party, including through the discriminatory provision of the monopoly good or service, cross-subsidization or predatory conduct.

Article 1503 stipulates that the parties must ensure that any state enterprise[18] (a) acts in a manner that is not inconsistent with the concerned party's obligations under NAFTA regarding investment and financial services when the said enterprise exercises its delegated governmental authority;[19] and (b) accords non-discriminatory treatment in the sale of its goods or services to investments of investors of the other party.[20] These have become standard requirements in NAFTA Members' subsequent FTAs.[21]

One of the main differences between the provisions in NAFTA and GATT concerns the scope of a transaction that needs to be based on 'commercial considerations'. As detailed above, the Appellate Body has ruled that 'commercial considerations' are required when the transaction at issue is between an STE and an enterprise of the other Member. However, Article 1502(3)(b) of NAFTA does not imply such a limitation.[22] Consequently, inconsistency with Article 1502 would result when a foreign enterprise, which is competing but not directly contracting with a certain government monopoly, is excluded from the market due to non-commercial practices of the SOE.

Among agreements to which Australia is a party, the US–Australia[23] and Australia–Chile FTAs[24] adopted this NAFTA-style SOE regulation (the Australia–Chile FTA requires commercial considerations only when the state monopoly exercises special or exclusive rights).[25] Nevertheless, these

[18] 'State enterprise' is defined as 'an enterprise owned, or controlled through ownership interests, by a party.' NAFTA (n 8) Art 1505.

[19] ibid Art 1503(2).

[20] ibid Art 1503(3).

[21] Examples are the Free Trade Agreement between the Republic of Korea and the United States of America (signed 30 June 2007, entered into force 15 March 2012) (Korea–US FTA); the Canada–Peru Free Trade Agreement (signed 29 May 2008, entered into force 1 August 2009); and the Free Trade Agreement between the State of Israel and the United Mexican States (signed 10 April 2000, entered into force 1 July 2000).

[22] While the transactions contemplated in para (c) presuppose the direct involvement of another party's enterprises, para (b) broadly addresses any transactions other than those for complying with the terms of its designation that are consistent with para (c).

[23] Australia–United States Free Trade Agreement (signed 18 May 2004, entered into force 1 January 2005) [2005] ATS 1 (US–Australia FTA).

[24] Australia–Chile Free Trade Agreement (signed 30 July 2008, entered into force 6 March 2009) [2009] ATS 6 (Australia–Chile FTA).

[25] ibid Art 14.4(2). This discussion regarding the *exercise* of exclusive or special rights or privileges may have a strong connection with the similar discussion over this phrase under GATT Art XVII and the Understanding on the Interpretation of Article XVII of GATT 1994. On this point, see EU Petersmann, 'GATT Law on State Trading Enterprises: Critical

Agreements also entertain competitive neutrality in the final paragraphs of provisions regarding state enterprises, which thus appears to have only a secondary role.[26]

Apart from NAFTA-style agreements, Australia has introduced competitive neutrality as a main framework for SOE regulation in several agreements, in particular with Singapore (SAFTA), South Korea (KAFTA) and Japan (JAEPA). The significance of this will be analysed in the following sections, in addition to the China–Australia FTA.

## III. SOE REGULATIONS UNDER SAFTA, KAFTA AND JAEPA

In terms of concluding FTAs, Australia is one of the most proactive countries penetrating the Asia region; to date, in addition to SAFTA, KAFTA, JAEPA and ChAFTA, it has concluded agreements with ASEAN (the ASEAN–Australia–New Zealand FTA)[27] and individually with some of its Members (Thailand[28] and Malaysia).[29,30] In light of these FTAs, Australia seems to have exerted a strong influence in constructing the basic framework of FTAs in this region. Among those Australian FTAs, this chapter focuses on SAFTA, KAFTA and JAEPA in this section, since they embrace the concept of competitive neutrality in regulating SOEs.

### A. SAFTA

SAFTA was signed on 17 February 2003 and entered into force on 28 July 2003.[31] A provision regarding SOEs is included in the competition policy chapter (Chapter 12) and prescribes as follows:

> Article 4 Competitive Neutrality
>
> 1. The Parties shall take *reasonable measures* to ensure that governments at all levels do not provide any competitive advantage to any government-owned businesses in their business activities simply because they are government owned.

Evaluation of Article XVII and Proposals for Reform' in T Cottier et al (eds), *State Trading in the Twenty-First Century* (Ann Arbor, MI, University of Michigan Press, 1998) 88.

[26] Australia–Chile FTA (n 24) Art 14.5(4); US–Australia FTA (n 23) Art 14.4(3).

[27] Agreement Establishing the ASEAN–Australia–New Zealand Free Trade Area (signed 27 February 2009, entered into force 1 January 2010) [2010] ATS 1.

[28] Australia–Thailand Free Trade Agreement (signed 5 July 2004, entered into force 1 January 2005) [2005] ATS 2.

[29] Malaysia–Australia Free Trade Agreement (signed 22 May 2012, entered into force 1 January 2013) [2013] ATS 4.

[30] Moreover, agreements with India and Indonesia are under negotiation.

[31] WTO, 'Welcome to the Regional Trade Agreements Information System (RTA-IS)' (2016), rtais.wto.org/UI/PublicShowMemberRTAIDCard.aspx?rtaid=60.

> 2. This Article applies to the business activities of government-owned businesses and not to their non-business, non-commercial activities (emphasis added).

As is apparent from the title and its contents, this provision is distinguishable from previous SOE regulation in trade agreements, such as that in GATT or NAFTA. Under SAFTA, the parties are required to adopt reasonable measures to ensure a level playing field of enterprises in their domestic markets. In what conditions would such 'reasonable measures' be enforced? There is no guidance in SAFTA. If it is assumed that these 'reasonable measures' or the provision itself are established with Australia's competitive neutrality framework in mind,[32] such measures would be applicable when required to ensure: taxation neutrality, debt neutrality, commercial rate of return, regulatory neutrality, and that prices charged by SOEs (government-owned businesses) reflect full cost attribution.[33] However, some of these obligations demanding fairness in competition overlap with the Agreement on Subsidies and Countervailing Measures (SCM Agreement)[34] or national treatment obligations and other obligations provided under either SAFTA[35] or the WTO agreements.[36] Therefore, the prime benefit of this provision might be that it can require appropriate measures to be taken regarding the activities of SOEs that would not be caught by other provisions in SAFTA or the WTO agreements: the most plausible situation would be when activities relating to trade in services are concerned, given that subsidies connected to the services are comprehensively excluded from the scope of the services chapter in SAFTA.[37]

### B. KAFTA

KAFTA was signed on 8 April 2014 and entered into force on 12 December 2014.[38] For Australia, South Korea is its third largest export market and

[32] For detail, see below section IV.

[33] Commonwealth Competitive Neutrality Policy Statement (1996), archive.treasury.gov.au/documents/275/PDF/cnps.pdf, 16–19.

[34] SAFTA (n 5) Art 7(2), Ch 2 confirms that the parties will abide by the provisions of the SCM Agreement. In addition, the Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994 (Anti-Dumpling Agreement) may also be applied in certain cases.

[35] SAFTA (n 5) Art 2, Ch 2; Art 12, Ch 7.

[36] As these rules are more effective because disagreements can be referred to the dispute settlement mechanism of either the WTO or SAFTA, application of these rules would be preferred over this catch-all competitive neutrality clause, which is excluded from the scope of the dispute settlement mechanism under SAFTA. SAFTA (n 5) Art 8(2), Ch 12.

[37] SAFTA (n 5) Art 2(2)(a), Ch 7. However, subsidies provided in relation to services supplied by SOEs might also be excluded from the scope of SAFTA, under Art 8(3), Ch 12 thereof. The relationship between Art 4, Ch 12 and Art 2(2)(a), Ch 7 is ambiguous.

[38] WTO (n 31).

fourth largest overall trading partner.[39] It was the first FTA to be concluded by Australia with a major trading partner in North Asia.[40]

Regarding the SOE regulation, KAFTA embraces the concept of competitive neutrality. Article 14.4 prescribes as follows:

> Article 14.4: Competitive Neutrality
>
> The Parties *recognise the importance* of ensuring that governments at all levels in their territories do not provide any competitive advantage to any state enterprise in its business activities as a result of it being a state enterprise. This Article shall apply to the business activities of state enterprises and not to their non-business, non-commercial activities. The application of this Article shall not obstruct the performance of the particular public tasks assigned to them (emphasis added).

This provision is somewhat modest compared with its equivalent in SAFTA discussed above since it only confirms the *common recognition* that the creation of a level playing field among state enterprises and private enterprises is important. Nonetheless, it is notable in view of the previous practices that South Korea has preferred to adopt a competition law-based approach towards SOE regulation (Table 2).[41] Those Agreements have typically prescribed that a party's competition laws should be applied to state enterprises and designated monopolies.

**Table 2: SOE Regulations included in South Korea's FTAs**

| Name of Agreement | Provision(s) relating to SOE | Approach |
|---|---|---|
| Korea–Chile FTA | Art 14.8 | Application of competition laws |
| Korea–Singapore FTA | Art 15.4 | Competitive neutrality |
| EFTA–Korea FTA | Art 5.1(2)(b) | Application of competition laws |
| ASEAN–Korea FTA | – | – |
| Korea–India CEPA | – | – |
| EU–Korea FTA | Arts 11.4 and 11.5 | Application of competition laws, non-discrimination |
| Peru–Korea FTA | Art 15.9 | Application of competition laws |
| Korea–US FTA | Arts 16.2 and 16.3 | NAFTA-style |
| Korea–Turkey FTA | Framework Agreement Art 3.8 | Application of competition laws |

*(continued)*

[39] Australian Government, 'KAFTA: A Snapshot', dfat.gov.au/trade/agreements/kafta/fact-sheets/Pages/kafta-a-snapshot.aspx.

[40] ibid.

[41] For examples of exceptions see, eg, Korea–US FTA (n 21) Arts 16.2, 16.3.

**Table 2:** ***(Continued)***

| Name of Agreement | Provision(s) relating to SOE | Approach |
|---|---|---|
| Colombia–Korea FTA | Art 13.9 | Application of competition laws |
| Korea–Australia FTA | Art 14.4 | Competitive neutrality |
| Canada–Korea FTA | Arts 15.2 and 15.3 | NAFTA-style |
| China–Korea FTA | Art 14.5 | Application of competition laws |
| Korea–Viet Nam FTA | Art 11.4 | Application of competition laws |
| Korea–New Zealand FTA | Art 12.1(2)(a) | Application of competition laws |

The competition law-based approach can be characterised as moderate and deferential compared with the competitive neutrality or NAFTA approach. This is because SOEs may readily be excluded from competition laws at the discretion of competent government; and if this occurs, FTAs could no longer require a party to take any measures to regulate the behaviours of SOEs. Contrary to this, the NAFTA approach, ie, requiring commercial considerations in a government monopoly's transactions, may warrant more coercive control over the conduct of SOEs, since commercial considerations can be required irrespective of the SOE concerned being excluded from the application of domestic competition laws. Competitive neutrality may stand in between these approaches. Although competitive neutrality may share the same deficit with the competition law approach, it has an additional advantage in that—if it is constructed somewhat similarly to the Australian policy—it could include matters that are usually not captured by competition laws.[42] However, it is not clear from the text of KAFTA to what extent South Korea gave serious consideration to a competitive neutrality policy. At any rate, the fact that South Korea has deviated from its previous practices suggests that, despite the weakness of the provision in KAFTA, South Korea has indicated its readiness to adopt an alternative approach in its FTA with Australia.

Moreover, it is intriguing to note that the Korea–Singapore FTA includes a provision regarding competitive neutrality.[43] Unlike KAFTA, yet like SAFTA, the competitive neutrality provision in the Korea–Singapore FTA is more straightforward: parties are required to take reasonable measures to

[42] OECD, 'Roundtable on Competition Neutrality: Issues Paper by the Secretariat' (2015) DAF/COMP(2015)5, www.oecd.org/officialdocuments/publicdisplaydocumentpdf/?cote=DAF/COMP(2015)5&docLanguage=En, 17.

[43] Free Trade Agreement between the Government of the Republic of Korea and the Government of the Republic of Singapore (signed 4 August 2005, entered into force 2 March 2006) (Korea–Singapore FTA) Art 15.4.

ensure a level playing field among government-owned businesses and non-government-owned businesses. In light of this, it is a fair observation that Korea is showing a positive attitude towards disseminating the concept of competitive neutrality through trade agreements, while not adopting the concept as a standard discipline for SOE regulation. The impact of KAFTA will be examined after analysis of JAEPA in the next subsection.

### C. JAEPA

JAEPA was signed on 18 July 2014 and entered into force on 15 January 2015.[44] While, for Australia, it is the third agreement to incorporate the concept of competitive neutrality,[45] this agreement is notable for Japan since it is the latter's first agreement that explicitly introduced a provision intended to regulate the behaviours of SOEs. As demonstrated in Table 3, despite its large number of FTAs, Japan had never previously incorporated specific SOE regulation in its FTAs. At best, Japan's preceding agreements contained provisions regarding monopoly service suppliers, which merely replicates Articles VIII and IX of the General Agreement on Trade in Services (GATS).[46]

**Table 3: SOE Regulations included in Japan's FTAs**

| Name of Agreement | Provisions relating to SOE | | | |
|---|---|---|---|---|
| | State trading enterprise (GATT XVII) | Monopoly supplier of a service (GATS VIII and IX) | Original Provisions | Approach |
| Japan–Singapore EPA | – | Arts 65 and 66 | – | – |
| Japan–Mexico EPA | – | – | – | – |
| Japan–Malaysia EPA | – | Art 105 | – | – |
| Japan–Chile EPA | – | – | – | – |

*(continued)*

[44] WTO (n 31).

[45] Recall that the US–Australia FTA and the Australia–Chile FTA both incorporated the competitive neutrality policy, but only gave it a secondary role.

[46] Previous Japanese FTAs can be understood as requiring the application of competition laws to SOEs, but they do not clearly indicate so.

**Table 3:** ***(Continued)***

| Name of Agreement | Provisions relating to SOE | | | |
|---|---|---|---|---|
| | State trading enterprise (GATT XVII) | Monopoly supplier of a service (GATS VIII and IX) | Original Provisions | Approach |
| Japan–Thailand EPA | – | Art 83 | – | – |
| Japan–Indonesia EPA | – | Art 86 | – | – |
| Japan–Brunei EPA | – | Art 83 | – | – |
| Japan–ASEAN EPA | – | – | – | – |
| Japan–Philippines EPA | – | Art 80 | – | – |
| Japan–Switzerland EPA | – | Arts 51 and 52 | – | – |
| Japan–Viet Nam EPA | – | Art 67 | – | – |
| Japan–India EPA | – | Art 67 | – | – |
| Japan–Peru EPA | – | – | – | – |
| Japan–Australia EPA | – | Art 9.10 | Art 15.4 | Competitive neutrality |
| Japan–Mongolia EPA | – | Arts 7.10 and 7.11 | – | – |
| TPP | Art 17.4 | Art 17.4 | Art 17.6–8 | Commercial considerations and non-commercial assistance |

JAEPA contains the following provision on SOEs:

> Article 15.4: State-Owned Enterprises
>
> In addition to Article 15.3, bearing in mind the relationship between the promotion of competition and other policy objectives, the Parties *recognise* that seeking to ensure that governments do not provide competitive advantages to state-owned enterprises simply because they are state owned can contribute to the promotion of competition (emphasis added).

As with KAFTA, this Article seems to be based on the concept of competitive neutrality, although it does not spell out the term anywhere in the provision.

Meanwhile, it remains to be seen whether Japan will promote this principle in its other FTAs since Japan did not include equivalent provisions in its EPA with Mongolia, which was concluded in the same period as JAEPA. Moreover, the Japan–Singapore FTA[47] did not contain any provisions pertaining to competitive neutrality, in contrast with the Korea–Singapore FTA.[48]

## IV. COMPETITIVE NEUTRALITY IN THE ASIA-OCEANIA NETWORK

As revealed in the previous section, Australia is diffusing the concept of competitive neutrality[49] in East Asia countries; it appears that these attempts have partially succeeded, as those countries agreed to include this concept in FTAs even though some of those provisions were limited to 'recognition' of the concept. It is possible, therefore, that the concept of competitive neutrality will evolve cooperatively through the relationship between Australia and its Asian FTA partners.

Australia's competitive neutrality policy[50] has advantages compared with the existing SOE regulation under GATT, NAFTA, or the WTO agreements. First, it encourages an ex ante resolution.[51] For instance, where a certain government activity of a commercial nature (significant government business activity) is exempted from taxation and this is liable to disadvantage competing private entities, such an SOE may pay, to the Official Public Account, an amount required to ensure parity with the tax levied upon their competitors (taxation equivalent regime, TER),[52] or alternatively, with regard to particular activities, adjust its price to that which would be

[47] Agreement between Japan and the Republic of Singapore for a New-Age Economic Partnership (signed 13 January 2002, entered into force 30 November 2002) (Japan–Singapore EPA).

[48] However, this absence of a provision pertinent to SOEs is understandable because the Japan–Singapore EPA was concluded very early (in 2002) in both countries' ventures into FTAs. The outcome might be different if the Agreement had been concluded more recently.

[49] The concept of 'competitive neutrality' may take various forms. In the following sections, the term will be used with the system akin to the Australian policy in mind. This is because the present chapter analyses the concept based on that contained in the trade agreements between Australia and Asian countries.

[50] For a comprehensive description of the Australian competitive neutrality policy see, eg, D Healey, 'Competitive Neutrality: Addressing Government Advantage in Australian Markets' in J Drexl and V Bagnoli (eds), *State-Initiated Restraints of Competition* (Cheltenham, Edward Elgar, 2015) 3.

[51] OECD, 'Roundtable on Competition Neutrality' (n 42) 17; D Healey, 'Competitive Neutrality: The Concept' in D Healey (ed), *UNCTAD Research Partnership Platform, Competitive Neutrality and its Application in Selected Developing Countries* (Geneva, United Nations, 2014) 14.

[52] Australian Government, 'Australian Government Competitive Neutrality Guidelines for Managers' (2004), consult.treasury.gov.au/market-and-competition-policy-division/competitive-neutrality-review/supporting_documents/2004%20Competitive%20Neutrality%20Guidelines%20for%20Managers%20AGCN_guide_v4.pdf, 18.

determined in the absence of the tax deduction (taxation neutrality adjustment, TNA).[53] Under this framework, distortion of competition can be prevented before the infliction of actual harm. Although the SCM Agreement's procedures may be applied, for instance, in the case of threat of material injury to domestic industry,[54] it does not deviate from the basic framework designed for ex post response to the actual injury.[55] Second, it may have broader coverage compared with the approach adopted under GATT, the WTO, or NAFTA. Certainly, under the current WTO system (and FTAs based on the WTO system), SOEs' market distorting conduct or the competitive advantages that SOEs may gain from government assistance may be eliminated, to some extent, through certain disciplines and mechanisms provided in GATT (eg, Article XVII), the SCM Agreement, and GATS (eg, Articles VIII and IX). However, several scenarios fall outside the scope of the existing WTO rules.[56] Apart from the rules regarding subsidies connected to trade in services, which are largely absent from the WTO agreements,[57] subsidies (pertinent to trade in goods) provided to an SOE by another SOE, for instance, will not necessarily be regulated under the SCM Agreement. This is due to the Appellate Body's current interpretation of the SCM Agreement, which presumes SOEs that do not possess, exercise, or have vested in them any governmental authority are outside the definition of 'public body' in Article 1.1(a) of the SCM Agreement.[58] The Australian model, encapsulating a flexible approach to government's assistance, may address the loophole in the WTO system (as well as FTAs based on the WTO system)[59]

[53] ibid 19.

[54] GATT Art VI, and fn 45 SCM Agreement.

[55] OECD, 'Roundtable on Competition Neutrality' (n 42) 19. F Kawashima, 'Competitive Neutrality Principles in Australia: Lessons for the TPP Negotiation on Disciplines over State-Owned Enterprises' (2015) RIETI Discussion Paper Series 15-J-026, www.rieti.go.jp/jp/publications/dp/15j026.pdf, 23 (in Japanese).

[56] This was obviously the biggest motivation for creating new rules in the TPP Agreement, which will be discussed in section VI below.

[57] However, some obligations under GATS, eg, the Most-Favoured-Nation (MFN) obligation and, to a limited extent, the national treatment obligation, will be applied to subsidies pertaining to trade in services. P Sauvé and M Soprana, 'Learning by Not Doing: Subsidy Disciplines in Services Trade' (E15 Initiative, International Centre for Trade and Sustainable Development (ICSTD) and World Economic Forum, 2015), e15initiative.org/wp-content/uploads/2015/04/E15_Subsidies_Sauve-and-Soprana_final.pdf, 6. See also, General Agreement on Trade in Services (GATS) (15 April 1994) LT/UR/A-1B/S/1 Art XV docsonline.wto.org.

[58] See, eg, Appellate Body Report, *United States—Antidumping and Countervailing Duties (China)* (15 March 2011) WT/DS379/AB/R, docsonline.wto.org, 317–18. See also, Appellate Body Report, *United States—Countervailing Measures on Certain Hot-Rolled Carbon Steel Flat Products from India* (8 December 2014) WT/DS436/AB/R 4.54, docsonline.wto.org.

[59] Many FTAs, including those concluded by the US, do not usually contain any supplementary rules (so-called 'WTO-plus' provisions) regarding subsidies or countervailing measures (eg, US–Australia FTA (n 23); JAEPA (n 3) Art 2.12). As such, FTAs' rules do not normally differ from WTO disciplines. TJ Prusa, 'Trade Remedy Provisions' in JP Chauffour and JC Maur (eds), *Preferential Trade Agreement Policies for Development: A Handbook* (Washington DC, World Bank Publications, 2011) 185; T Voon, 'Eliminating Trade Remedies from the WTO: Lessons from Regional Trade Agreements' (2010) 59 *International & Comparative Law*

and enable comprehensive treatment of the anticompetitive situation caused by SOEs. Third, it takes an educative approach.[60] According to an OECD report, this is because the 'competitive neutrality policy and enforcement bodies work with governments to achieve implementation'.[61]

As discussed above, the Australian competitive neutrality policy also has advantages over the simple application of competition laws, the only policy tool that can be discerned as a formal competitive neutrality policy in most countries. This is a corollary of Australia's policy since it was developed based on the premise that (traditional) competition laws alone are insufficient to address the issues stemming from the participation of government businesses in a competitive market.[62]

Nevertheless, a comprehensive competitive neutrality policy founded on the basic principles adopted in Australia is not widely supported by other countries in their international agreements. Perhaps this is because the policy is not 'designed for internationalization'.[63] As the Australian competitive neutrality policy depends heavily on the regulating government's ambition and capacity, it provides no means for impacted countries to prevent their private competitors from being driven out of the market if the governmental institutions in charge of regulating SOEs are reluctant in meeting their duties.[64] This appears to be one of the core reasons why the system incorporating straightforward and explicit provisions proscribing certain practices relating to SOEs, such as those stipulated in Articles 1502 and 1503 of NAFTA, being preferred over competitive neutrality policy in the TPP negotiations (see the discussion in section VII below).[65]

*Quarterly* 625, 638; R Teh, TJ Prusa and M Budetta, 'Trade Remedy Provisions in Regional Trade Agreements' (2007) WTO Staff Working Paper ERSD-2007-03, www.wto.org/english/res_e/reser_e/ersd200703_e.pdf, 21.

[60] A Capobianco and H Christianse, 'Competitive Neutrality and State-Owned Enterprises: Challenges and Policy Options' (2011) OECD Corporate Governance Working Papers No 1, www.oecd-ilibrary.org/governance/competitive-neutrality-and-state-owned-enterprises_5kg9xfgjdhg6-en?crawler=true, 15.

[61] ibid.

[62] FG Hilmer et al, 'National Competition Policy' (Canberra, Australian Government Publishing Service, 1993) 6–7.

[63] D Scissors, 'Why the Trans-Pacific Partnership must Enhance Competitive Neutrality' (2013) Backgrounder 2809, thf_media.s3.amazonaws.com/2013/pdf/bg2809.pdf, 3. Accordingly, during the TPP negotiation, Australia has proposed an internationalised version of its competitive neutrality policy. Under this proposal, while the primary responsibility would fall on domestic institutions, an affected country may initiate state-to-state dispute settlement proceedings when it is not satisfied with the implementation of a system. Inside US Trade, 'Business Groups Wary of Australian Approach on SOE Disciplines in TPP' (24 May 2013).

[64] Scissors (n 63) 4. It is also highlighted that some developing countries do not have the capacity to implement a similar system to that required under the Australian competitive neutrality policy. T Kawase, 'Trans-Pacific Partnership Negotiations and Rulemaking to Regulate State-owned Enterprises (Policy Update 053)' (22 April 2014), www.rieti.go.jp/en/special/policy-update/053.html.

[65] Inside US Trade (n 63).

Despite this opposition, the ex ante and flexible approach contemplated in the Australian competitive neutrality policy still warrants consideration in securing equal competitive conditions throughout the Asia-Oceania region, and furthermore the foundation for such an approach seems to be in place. For instance, in Japan, competition-distorting subsidies provided by the local government may be withheld through ex ante consultation with the Japanese Fair Trade Commission (JFTC). In 2007, the JTFC published its consultation cases with local governments.[66] Among them was a case regarding a subsidy provided by an anonymous city (City A) for promotion of a co-generation system. City A, which was simultaneously a distributor of co-generation systems, ie, an 'enterprise' under the Antimonopoly Act,[67] considered introducing a policy providing a subsidy to residents who purchased a co-generation system from City A, whereas the same subsidy would not be offered to residents who purchased the same system from private companies. According to the JFTC, this subsidy was likely to distort competition among co-generation distributors, thereby infringing the Antimonopoly Act. More specifically, it would fall within the definition of 'Below-cost Pricing'[68] if the provision of this subsidy resulted in the retail price being reduced to far below the cost incurred to supply the services at issue.[69] Including this example, the JFTC's consultation records imply that an ex ante and flexible approach may prevail in Japan.[70] Although there is no comprehensive policy dealing with competitive neutrality at this stage in Japan,[71] it would be possible to construct a system that is harmonic and supplemental to the Australian competitive neutrality policy, or to develop a system more appropriate for the international implementation of competitive neutrality framework. Eventually, such a system may be embraced by other Asian countries.[72]

[66] JFTC, 'Consultation Cases from local government' (2007), www.jftc.go.jp/houdou/pressrelease/kako/07062001.files/07062001-tenpu.pdf, 1 (in Japanese).

[67] Act on Prohibition of Private Monopolization and Maintenance of Fair Trade (Japanese Act No 54 of 14 April 1947).

[68] Antimonopoly Act, Arts 2(9)(iii) 19; Designation of Unfair Trade Practices (Fair Trade Commission Public Notice No 15, 18 June 1982) para (6); The Guidelines for Exclusionary Private Monopolization under the Antimonopoly Act 2009, pt II:2.

[69] JFTC (n 66) 2.

[70] Under the consultation procedure, it is possible to take a more flexible approach in preventing the distortion of competition. Indeed, in some consultation cases, the JFTC exhibits concerns over the adverse effects on competition without indicating any infringement of specific provisions of the Antimonopoly Act.

[71] OECD, 'Roundtable on Competitive Neutrality in Competition Enforcement: Note by Japan' (2015) DAF/COMP/WD(2015)6, www.oecd.org/officialdocuments/displaydocument/?cote=DAF/COMP/WD(2015)6&docLanguage=En, 2.

[72] See also, S Gaur, 'Competitive Neutrality Issues in India' in D Healey (ed), *UNCTAD Research Partnership Platform, Competitive Neutrality and its Application in Selected Developing Countries* (Geneva, United Nations, 2014) 159. It notes that India may espouse Australian-style competitive neutrality policy in some form.

## V. ChAFTA AND OTHER FTAs CONCLUDED BY CHINA

Against this background, Australia and China concluded ChAFTA: signed on 17 June 2015, it came into force on 20 December 2015. However, the Agreement did not contain any explicit regulations regarding SOEs.

At first glance, this outcome might be attributed to China's concerns about the regulation of SOEs. One can imagine that the SOEs in China resisted the introduction of SOEs-related provisions.[73] However, this assumption is at odds with China's typical practices. China has already introduced forms of SOE regulations in its FTAs (Table 4). For instance, the Iceland–China FTA provides that the Agreement's competition chapter will be applied to undertakings with privilege and exclusive rights authorised by law.[74] An obligation to apply either party's respective competition laws is also prescribed in the same Article.[75] Hence, both parties may not exclude their SOEs from the application of competition law (to the extent that the competition chapter's application does not prevent the SOEs fulfilling their legal functions).[76] A similar provision was inserted in the Switzerland–China FTA, with slightly more succinct expression: this Agreement's competition chapter applies to *all undertakings* of the parties.[77]

**Table 4: SOE Regulations included in China's FTAs**

| Name of Agreement | Provisions relating to SOE | | | |
|---|---|---|---|---|
| | State trading enterprise (GATT XVII) | Monopoly supplier of a service (GATS VIII and IX) | Original Provisions | Approach |
| China–Macao CEPA | – | – | – | – |
| China–Hong Kong CEPA | – | – | – | – |

*(continued)*

[73] Y Jiang, 'Australia–China FTA: China's Domestic Politics and the Roots of Different National Approaches to FTAs' (2008) 62(2) *Australian Journal of International Affairs* 179, 183. See also, G Song and WJ Yuan, 'China's Free Trade Agreement Strategies' (2012) 35(4) *The Washington Quarterly* 107, 115. It exhibits several examples of SOEs hampering or affecting several FTA negotiations.

[74] Free Trade Agreement between the Government of Iceland and the Government of the People's Republic of China (signed 15 April 2013, entered into force 1 July 2014) (Iceland–China FTA) Art 62(2).

[75] ibid Art 62(4).

[76] ibid Art 62(2).

[77] Switzerland–China FTA (n 10) Art 10(2). Again, such application will be required insofar as it does not hinder those undertakings from exercising their special and exclusive rights.

**Table 4:** ***(Continued)***

| Name of Agreement | Provisions relating to SOE | | | |
|---|---|---|---|---|
| | State trading enterprise (GATT XVII) | Monopoly supplier of a service (GATS VIII and IX) | Original Provisions | Approach |
| ASEAN–China FTA | – | Services Agreement, Arts 7 and 8 | – | – |
| Chile–China FTA | – | – | – | – |
| China–New Zealand FTA | – | Art 123 | – | – |
| Pakistan–China FTA | – | Services Agreement, Arts 7 and 8 | – | – |
| China–Singapore FTA | Art 9 | Arts 69 and 70 | – | – |
| Peru–China FTA | Art 17 | – | – | – |
| China–Costa Rica FTA | – | – | – | – |
| Iceland–China FTA | – | Arts 76 and 77 | Art 62(2) | Application of competition laws |
| Switzerland–China FTA | Art 2.6 | Arts 8.10 and 8.11 | Art 10(2) | Application of competition laws |
| China–Korea FTA | Art 2.11 | Art 8.12 | Art 14.5 | Application of competition laws |
| China–Australia FTA | – | Art 8.23 | – | – |

Even more noteworthy is the China–Korea FTA.[78] This Agreement contains a competition chapter that, in terms of the number and detail of the provisions, is far more sophisticated than previous agreements concluded by China, and the SOE-related provision is incorporated in the context of this holistic competition policy, which seems to have reflected South Korea's intentions.[79] After affirming that the competition chapter will be applied to

[78] Free Trade Agreement between the Government of the People's Republic of China and the Government of the Republic of Korea (signed 1 June 2015, entered into force 20 December 2015) (China–Korea FTA).

[79] Most of Korea's FTAs emphasise the application of competition laws to state enterprises through a separate provision, rather than simply noting the equal application of competition

*all undertakings* of each party[80] and confirming that the same chapter does not prevent a party from establishing or maintaining public enterprises,[81] this Agreement requires each party not to adopt or maintain, regarding public enterprises, any measure contrary to the principles contained in its prevailing provision that advocates the proper implementation of competition laws,[82] and to ensure that those enterprises are subject to competition laws.[83]

In sum, China is amenable to a certain level of SOE regulation in FTAs.[84] Moreover, it may be inferred from China's agreed rules to date on the application of competition laws that those rules would be included in its future trade agreements. The prime benefit—though, in certain cases, it is actually a weakness—of the competition law-based approach is that it does not curtail the regulating country's discretion in conducting SOE regulation. Considering the current status of SOEs and their role in the Chinese economy, the competition law-based approach can be seen as the more realistic and acceptable, and thereby more effective, option for regulating conduct by SOEs that affects trade with China.[85] Indeed, China seems to be gradually applying its Antimonopoly Law (AML) to SOEs, although the AML's enforcers still appear hesitant to enforce the law against big SOEs.[86] The concept of competitive neutrality policy nurtured in Australia does not intrinsically conflict with this premise of autonomy.[87] Therefore, it is regrettable that

laws to all enterprises in general terms. See, eg, Free Trade Agreement between the Republic of Colombia and the Republic of Korea (signed 21 February 2013, entered into force 15 July 2016) Art 13.9.

[80] China–Korea FTA (n 78) Art 14.5(1).

[81] ibid Art 14.5(2).

[82] ibid Art 14.5(3)(a).

[83] ibid Art 14.5(3)(b).

[84] This suggests that Australia, rather than China, felt reluctant to introduce SOE-related provisions, in particular those demanding the application of competition laws to SOEs, in ChAFTA. One reason for this speculation is the limited scope and enforceability of competition law-based regulation. The effectiveness of the competition law-based approach highly depends on the regulating country's ambition; another potential constraint is where its scope does not extend to SOEs' conduct not usually captured under competition laws, such as subsidies or preferential arrangements provided to SOEs by the government. Considering that ChAFTA's negotiation was partially in parallel with the TPP negotiations, omitting SOE-related provisions was probably the better choice to avoid infecting the outcome of the TPP negotiations, since the latter Agreement is obviously concerning as regards Chinese SOEs, despite the non-participation of China.

[85] B Jin, 'Competitive Neutrality in the Trans-Pacific Partnership (TPP) Negotiations on International Investment' (2015) 1 *Transnational Dispute Management* 30–31. It argues that China is not prepared to accept the SOE regulation that the US seems to have advocated during the TPP negotiations.

[86] H Chen and J Whalley, 'The State-Owned Enterprises Issue in China's Prospective Trade Negotiations' (2014) CIGI Papers No 48, 3.

[87] See, eg, X Shiying, 'Competitive Neutrality of SOEs in China' in D Healey (ed), *UNCTAD Research Partnership Platform, Competitive Neutrality and its Application in Selected Developing Countries* (Geneva, United Nations, 2014) 76. It recommends that a complaints process

ChAFTA does not contain any provisions regarding the treatment of SOEs, even in the modest way that can be found in KAFTA and JAEPA.[88]

## VI. SOE REGULATION UNDER THE TPP AGREEMENT

Despite the fact that it will not formally come into effect, the likelihood of a very similar successor agreement including similar approaches suggests that there is great value in considering the relevant approaches of the TPP in this chapter. Critically, the conclusion of the TPP Agreement (signed 4 February 2016) has paved the way to widen the application of SOE regulation under trade agreements in general.[89] The TPP Agreement established an independent chapter concerning SOEs, accomplishing the incorporation of not only the traditional disciplines inherited from GATT and NAFTA—ie, concepts of non-discrimination and commercial considerations—but also the new framework labelled as non-commercial assistance (NCA). While some of these rules are completely novel, the SOE chapter as a whole would essentially be evaluated as an expansion of the WTO-based approach. This is because the new NCA rules espouse the basic disciplines of the SCM Agreement and simultaneously extend those disciplines, without significant modification, to fields that are not covered under the SCM Agreement, such as non-commercial assistance provided with respect to trade in services. Considering this generic concordance with previous rules, it is not unreasonable to expect that the SOE disciplines in the TPP Agreement should become standard rules, rather than being limited to the Pacific Rim.[90]

in China should not be established, due to the government's lack of motivation to weaken the economic advantages of SOEs, while advocates the strict enforcement of competition law in controlling exclusive business conduct by SOEs.

[88] See, eg, R Tomasic and P Xiong, 'Chinese State-Owned Enterprises in Australia: Legal and Investment Challenges' (2015) 30(2) *Australian Journal of Corporation Law* 151, 176. It submits the necessity of regulating SOEs within the China–Australia relationship, focusing particularly on investment issues; but see, M Bowman et al, 'The Australia–China Free Trade Agreement and the Growing Acceptance of Chinese State Capital Investment' (2015) 8(1) *Asian Journal of Public Affairs* 1, 11. It predicts the future softening of investment review policy towards Chinese SOEs by the Australian government.

[89] At the time of writing, the fate of the TPP Agreement is unclear. While the US administration has formally announced its 'withdrawal' from the Agreement, some of the remaining TPP signatories are considering the possibility of establishing TPP-11, ie, the TPP Agreement without the US. In addition, there is the potential for SOE-related provisions in the TPP Agreement to become a template for SOE regulation and transplanted into other FTAs. Inside US Trade, 'Language in NAFTA Draft Notice Similar to TPP Text on Investment, IP, SOE' (7 April 2017) In light of these developments, the present chapter's discussion assumes that SOE-related provisions established in the TPP Agreement may survive in some form in the future.

[90] It is noteworthy that the TPP Agreement appointed a committee specifically to consider SOE matters; one of its tasks is to contribute to the dissemination of TPP-style SOE disciplines. Trans-Pacific Partnership Agreement (TPP Agreement) Art 17.12.2(c), ustr.gov/trade-agreements/free-trade-agreements/trans-pacific-partnership/tpp-full-text. See also, MK Lewis,

Conversely, the TPP rules are not without concerns and problems. First, the new rules are, by their nature, coercive. Under the TPP rules, if a certain form of non-commercial assistance is causing adverse effects or injury to another party, the providing country needs to take appropriate action to remove those effects or withdraw the assistance concerned; otherwise, it will be confronted with the countermeasures permitted under the TPP dispute settlement procedure.[91] While the TPP rules do not contain a mechanism of countervailing duty, they also do not clearly specify a more flexible approach. For instance, they do not contain a mechanism somewhat akin to the undertakings system envisaged under Article 18 of the SCM Agreement.[92] In essence, the complaining party is given discretion and control over all the counteracting processes and the providing party will be directly condemned through the rules in the TPP Agreement.[93] Second, and on the contrary, some lacunae remain under the new rules, even when they are combined with the SCM Agreement. For instance, although the TPP Agreement NCA rules seek to cover non-commercial assistance that may not be caught by the SCM Agreement (eg, assistance provided by SOEs not vested with governmental authority),[94] they do not contemplate the situation where assisted exports adversely affect the domestic industry of another TPP party operating within that party's domestic market, ie, the case that would be subject to countervailing duties under the SCM Agreement.[95]

'The TPP and the RCEP (ASEAN+6) as Potential Paths toward Deeper Asian Economic Integration' (2013) 8(2) *Asian Journal of WTO and International Health Law and Policy* 359, 370. It suggests that the conclusion of the TTIP would raise the TPP's SOE rules as a global standard, since it is likely that the former would incorporate the latter.

[91] TPP Agreement (n 90) Arts 28.19, 28.20.

[92] Steinbach acknowledges the difficulty of monitoring, and casts doubt on the effectiveness of price undertakings in eliminating the injurious effects of dumping practices. These deficiencies might explain why this mechanism was not introduced under the TPP NCA rules. See, eg, A Steinbach, 'Price Undertaking in EU Anti-dumping Proceedings: An Instrument of the Past?' (2014) 29(1) *Journal of Economic Integration* 165, 174. See also, L Rovegno and H Vandenbussche, 'A Comparative Analysis of EU Antidumping Rules and Application' (2011) IRES Discussion Paper 2011–23, 18. It briefly portrays, in the context of anti-dumping procedures, the US' limited willingness to engage in price undertakings measures. However, it seems that the TPP Agreement does not a priori exclude such 'mutually satisfactory resolution'. TPP Agreement (n 90) Art 28.2. In addition, the TPP Agreement embraces the system of monetary payments: TPP Agreement (n 90) Arts 28.20.7–15.

[93] By contrast, apart from the FTAs concluded by NAFTA Members, most countries have conventionally adopted a system that: (i) is based on the application of competition law; and (ii) excludes the competition chapter from the scope of their FTAs' dispute settlement procedures. This demonstrates more deferential attitudes towards SOE regulation predicated on domestic legislation.

[94] TPP Agreement (n 90) Art 17.6.2. Regarding the meaning of 'government' under Art 1.1(a) SCM Agreement, see above section IV.

[95] Art 17.7.1(b)(i) TPP Agreement only stipulates the situation where sales of a covered investment (namely, a third TPP party's investment) or imports from a third TPP party, but not products of the domestic industry of an importing party, are displaced or impeded from the market of the party importing assisted products.

Therefore, if assistance is provided to the SOE in a form that does not fulfil the definition of 'subsidy' under the SCM Agreement, the importing party may have no means to address the adverse effects upon its domestic industry emanating from assisted exports.[96] Third, the new TPP rules do not properly respond to the public services concerns.[97] In this respect, services provided by SOEs are excluded from certain provisions in the SOE chapter of the TPP Agreement when 'supplied in the exercise of governmental authority'.[98] The meaning of this phrase is clarified under GATS,[99] enunciated as 'any service which is supplied neither on a commercial basis, nor in competition with one or more service suppliers'.[100] However, this exception is narrow, especially when considered at face value. Services that fit this definition are very limited as most public services contain commercial aspects or (potentially) compete with other suppliers.[101] Moreover, according to the TPP Agreement, 'a service supplied by [an SOE] of a party within that party's territory shall be deemed not to cause adverse effects';[102] thereby, NCA rules will not be applied to assistance given in relation to those services. However, this exception is too broad. It muddles all domestic services, irrespective of whether they have public purposes.[103] Admitting that this represents a compromise in the negotiation and, hence, tentatively the best solution for all parties, it is nonetheless, at least theoretically, not ideal.[104]

[96] It should be noted, however, that under the TPP NCA rules, if the assistance leads to significant price undercutting, significant price suppression, price depression, or the phenomenon of lost sales, an importing party may react to the importing of goods produced by assisted SOEs. Art 17.7.1(c)(i) refers to 'the market of a Party' (and 'in the same market'), with no limitation upon what constitutes the affected market, suggesting that the importing party may claim, under the TPP's dispute settlement procedure, the existence of adverse effects if one of the aforementioned phenomena occurs in its domestic market. However, in the case of significant price undercutting, the same provision explicitly stipulates that the comparison of price must be between the price of the good at issue and the price of 'imports of a like good of another Party' or 'a like good that is produced by an enterprise that is a covered investment in the territory of the Party'. In short, the comparison is not between the price of the good at issue and that of like goods produced by the domestic industry (unlike under Art 17.8.2).

[97] M Yun, 'An Analysis of the New Trade Regime for State-Owned Enterprises under the Trans-Pacific Partnership Agreement' (2016) 20(1) *Journal of East Asian Economic Integration* 3, 27.

[98] TPP Agreement (n 90) Art 17.2.10.

[99] TPP Agreement (n 90) Ch 17, fn 11.

[100] GATS (n 57) Art I:3(c). See also, above (n 11); TPP Agreement (n 90) Ch 17.

[101] R Adlung, 'Public Services and the GATS' (2005) WTO Working Paper ERSD-2005-03, 8–12. It explores, simultaneously, the possibility that GATS Art I:3(c) would be interpreted more broadly than its literal meaning.

[102] TPP Agreement (n 90) Art 17.6.4.

[103] There is also the concept of the 'public service mandate' in Arts 17.1, 17.4 TPP Agreement and the public policy/public interest exceptions for competition laws in Art 16.1.2.

[104] Y Tojo, 'International Discipline on SOEs: Development of Fair Competition Rules' (2016) RIETI Discussion Paper Series 16-J-011, 23 (in Japanese). There are some additional exceptions. For instance, in certain circumstances, the supply of financial services by an SOE pursuant to a government mandate will be deemed not to give rise to adverse effects under certain provisions in the TPP Agreement where the party in which the financial service is supplied requires a local presence to supply those services. See TPP Agreement (n 90) Art 17.13.3.

On balance, there are fears that SOE regulation under the TPP Agreement may come under heavy fire from both sides: it could be blamed as too weak from the proponents of strong SOE regulation and too bold from those who view SOEs as important instruments in developing societies.

## VII. FUTURE SOE REGULATION AND CHAFTA

Currently, there are variations in SOE regulation provided under FTAs. At one end of the spectrum, there is the TPP Agreement, which enables direct regulation of SOEs based on the rules it deploys with viable enforcing mechanisms. At the opposite end is ChAFTA, which does not contain any particular SOE regulations and the conduct of SOEs are principally not condemned beyond the existing WTO framework. SAFTA, KAFTA and JAEPA, those that can be labelled as the competitive neutrality group, are located between those two poles (Figure 1).

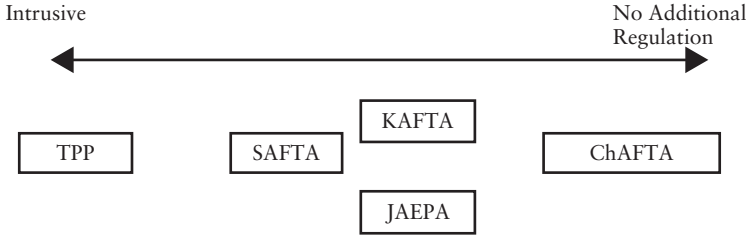


**Figure 1: Spectrum of SOE Regulation under Australia's FTAs**

At the time of writing, the fate of the TPP Agreement is undetermined though looking less likely to come into effect. On one hand, if the TPP Agreement or a TPP-like agreement enters into force, it would serve as a strong driving force for toughening SOE regulation in the Asia-Pacific region. Not only would it refine existing SOE regulation under the trade agreements that are already in force, but it would also affect future agreements by tempting TPP parties to use its framework as a template when concluding new agreements with other countries. On the other hand, the demise of the TPP will result in most operative SOE regulations being confined to no or small-scale regulations, ie, concentrating on the right side of Figure 1 above.[105] ChAFTA's omission of specific provisions addressing the behaviours of SOEs would

[105] The SOE chapter established under the TPP Agreement might survive, even with the failure of the Agreement, by the adoption of a similar chapter in future bilateral agreements concluded by TPP Members, in particular the US. Nevertheless, such attempts may not have the same impact as the TPP Agreement, which involves 12 countries and nearly 40% of the global GDP.

send a negative signal regarding the development of SOE regulation to the region or international community, and may entrench this custom of indifference. This is the scenario that needs to be avoided.

Bearing this in mind, it is necessary to revisit the strategy for proper SOE regulation. As discussed herein, China's FTAs are gradually introducing competition law-based SOE regulation. This approach is not in conflict with Australia's competitive neutrality policy. Therefore, the first option for a new strategy may be to create new principles or rules on SOE regulation, either inside or outside ChAFTA. The hardest approach would be to amend ChAFTA and insert the provisions focusing on the behaviours of SOEs. This can be achieved through the review and amendment processes provided in the Agreement.[106] The more tempered approach is to append a side letter or to create cooperative agreements. The former may either be integrated into the Agreement, analogous to the current side letters attached as Annex IV to the Agreement,[107] or isolated from the Agreement, such as the side letter regarding Chinese Medicine[108] or the several memorandums of understanding associated with the Agreement.[109] The creation of a cooperative agreement, on the other hand, can be achieved via the mechanism prepared within ChAFTA that aims to enhance collaboration in competition matters. Pursuant to Article 16.7 of ChAFTA, Australia and China will devise new or use existing mechanisms to cooperate in enforcing competition laws and policies. This commitment could serve as a stepping stone for future development of comprehensive cooperation in competition matters. Furthermore, it would be more constructive if the concept of competitive neutrality is clearly recognised as a part of competition policy for the purpose of this cooperation.

Another route for the development of SOE regulation is to create rules in different frameworks that could involve both Australia and China, such as the Regional Comprehensive Economic Partnership (RCEP). However, introducing SOE regulation in the RCEP might be too ambitious, with the existence of ChAFTA operating as a hurdle to that end. The first step that Australia should take, therefore, is to develop SOE regulation in bilateral agreements, to generate an atmosphere that would embrace a certain degree of cross-border SOE surveillance in the region. This will require Australia to further develop a competitive neutrality concept with Singapore, South

[106] ChAFTA (n 1) Arts 16.5, 17.3.

[107] Side letters included in Annex IV are binding, in principle (ChAFTA (n 1) Art 17.1). However, as some provisions in the Agreement are excluded from the application of dispute settlement procedures established under the Agreement, side letters connected to those provisions will be dealt with in the same manner.

[108] Side Letter on Traditional Chinese Medicine.

[109] eg, Memorandum of Understanding between the Government of Australia and the Government of the People's Republic of China on an Investment Facilitation Arrangement.

Korea and Japan under the current FTAs, and to foster competition cooperation among other Asian countries through new FTAs. The same would be true for China and countries that are candidates for counterparts in China's FTAs. From this perspective, the China–Korea FTA can be praised, since it advanced cooperative regulation for the behaviour of SOEs, and this effort should be continued with expectations of spilling over to other FTAs.

In any event, ChAFTA, as it stands, represents a missed opportunity to diffuse more flexible methods of regulating SOEs. However, there remains a path to develop SOE regulation that may suit the Asia-Oceania region.[110] If this is achieved, in particular within the framework of ChAFTA, it may be said that SOE regulation in ChAFTA has contributed to developing SOE regulation in the region. Alternatively, proper SOE regulation may be established via a different path. While an ideal way may be through plurilateral FTAs, steady effort through bilateral agreements also contributes to such a goal. It is important to keep up the effort to pursue proper cross-border or region-wide SOE regulation irrespective of the fate of the TPP Agreement, and ChAFTA should have a role to play in such endeavours.

## VIII. CONCLUSION

As analysed herein, there is no comprehensive SOE regulation in ChAFTA, despite strong interest in that topic on the part of Australia, which has succeeded in diffusing the concept of competition neutrality to some Asian countries, such as Singapore (SAFTA), South Korea (KAFTA) and Japan (JAEPA). Even compared with China's previous FTAs, ChAFTA may be assessed as taking a step backwards; the Agreement does not even mention the application of competition laws to SOEs. Nevertheless, there remains a possibility to elaborate comprehensive SOE regulation within the Australia–China relationship. A competitive neutrality policy may work harmoniously with existing competition laws, as well as entailing additional advantages derived from its flexibility and ex ante nature that cannot be attained in the simple application of competition laws. Therefore, both countries need to continue their efforts to enhance cooperation and develop mechanisms with Australian competitive neutrality policy in mind, to ensure equal opportunity for competition between private and public enterprises; such a course can eventually contribute to the development of appropriate SOE regulation in the Asia-Oceania region. Concurrent with this, it may also be sensible to

[110] P Kowalski and K Perepechay, 'International Trade and Investment by State Enterprises' (2015) OECD Policy Papers No 148, 25. It suggests that stringent regulation at the international level, such as that in the TPP Agreement, does not always fit the circumstances of individual countries.

embrace other countries that can afford to share the spirit of Australian-style competitive neutrality policy, such as Singapore, South Korea and Japan. As economic integration is evolving, thanks to the enhancement of trade agreements in the Asia-Oceania region, it also needs to create cross-border cooperative mechanisms to properly ensure a level playing field among various competitors, so that the signatories are not deprived of the benefits of free trade. It is expected that the cooperative relationship between Australia and China will achieve this, through long-term effort.