Australian Services Roundtable

Securing Australia's Place in the Global Services Economy

Submission to the Mortimer Review

Export Policies and Programs

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EXECUTIVE SUMMARY AND RECOMMENDATIONS

Services well and truly dominate the modern Australian economy. The services sector generates the vast bulk of Australia's GDP and the services sector employs most Australians. Services innovation and productivity have driven national economic growth for the last 15 years.

Services exports are notoriously difficult to measure, but official estimates put them on a par with manufactures, ahead of agriculture and, consistent with global trends, growing much more rapidly than either.

But if Australian services industries are to reverse their recent apparent decline in global market share, there needs to be not just greater priority attention given to services, but a distinct paradigm shift in Australian trade policy thinking.

Conventional Australian trade policy was designed for a relatively closed, goods-oriented economy.

By convention, trade policy had nothing much to do with investment flows nor investment or capital markets policy.

By convention, trade policy had nothing much to do with movement of people or immigration policy.

By convention, trade policy had nothing much to do with provision or regulation of the internet.

Those conventions should long ago have been relegated to history, with the conceptual breakthroughs achieved in the thinking – a full 2 decades ago - that led to the WTO General Agreement on Trade in Services (GATS).

The GATS highlighted the fact that services trade does not look even remotely like goods trade.

The closest that services exports ever come to looking anything like conventional goods exports is when services are delivered via the internet and the service itself crosses the border. What the Australian Bureau of Statistics (ABS) measures as services exports also importantly includes services sold to non-residents temporarily visiting Australia and services which Australians sell to non-residents when they travel temporarily to other countries. But an additional important method by which Australian services are currently being delivered offshore, though this is not described by the ABS as services "export" activity, is through Australian–owned affiliates offshore.

Policy makers have struggled to come to grips with all this and, in particular, to accept that "trade", when we come to services, can not be kept analytically or operationally entirely distinct from "investment and capital flows" or even from "people flows".

One consequence is that services trade is still relatively rarely researched and relatively poorly understood. Another consequence is that services exports have far from reached their full potential.

This is a trade policy failure which the new Rudd Government is clearly seeking to redress.

It matters more now than ever before, as the process of globalisation intensifies, leading all firms to focus more on their core strengths under pressure to enter the global supply chain.

The Australian Services Roundtable calls on this Review to help deliver a more modern trade policy which embraces all the realities of offshore services delivery.

This will require an all-of-government focus on understanding and measuring how the services economy works.

It will require the deployment of a new tool kit and the building of new institutions, globally and at home.

It will require, in a nutshell, a consistent articulated national services export strategy, around which the services sector itself can continue to mobilise.

We need, first, to significantly improve the global competitiveness of many areas of our services sector through competition and innovation policy, reduction of debilitating regulation, skills development, and services infrastructure investment.

Second, we need to open more markets for our services firms offshore - a very complex process compared with good exports - which will require major reform of the way in which government organises itself for this purpose.

Key components of a National Services Export Strategy which addresses both these objectives, must include:

On the Home Front

- Continuous rigorous efforts to reduce unnecessary burdens of business regulation
- Significant domestic investment in knowledge economy infrastructure, including education and broadband
- Elevation of Services to the status of a National Innovation Priority

- Introduction of a new outcomes-oriented "Innovate and Compete" taxation incentive specifically for non-laboratory export-oriented innovation in services
- Introduction of a taxation deferment plan for project-based services export activity
- Better coordinated Trade, Investment, Capital market, Taxation and Immigration policies
- A national research effort, in partnership with industry (for example via the proposed ASR Services Stock-take) to understand the drivers and inhibitors of competitiveness in Services
- Funding for the Australian Bureau of Statistics for improved Services Trade and Services Innovation metrics

Supporting Services Excellence

- Setting of aspirational growth targets
- Specially designed domestic interventions to stimulate or support the accumulation of resident pools or "hubs" of globally competitive services expertise, interalia in:
  - financial services
  - education services
  - ICT services
  - R&D services
  - professional and technical services
  - audiovisual, cultural and entertainment services
  - health and wellbeing and
  - tourism services

New Promotional Tools

- Significant joint government/industry innovation in export promotion, branding and marketing methods to accommodate the unique and complex manner of international services delivery
- Stronger Government presence in support of Australian services tendering into global services supply chains
- More deliberate Government focus on assisting services suppliers to establish commercial presence offshore
- Creation of centralized services export intelligence data banks
- Provision of specialized export training for small and medium sized services firms
- Creation of services exporter networking opportunities, especially for smaller firms

New Negotiating Fora and Vehicles

- A big Australian initiative to ensure immediate commencement post Doha, of critical mass plurilateral, mfn-based, services trade

negotiations, preferably within the WTO but not necessarily located in Geneva
- Cessation of automatic Australian support for a "single undertaking" on joint Services and Goods (Agriculture) negotiations in the WTO
- New international Australian Government advocacy for multilateral and plurilateral negotiations on trade and investment and trade and competition policy
- Explicit Australian Government support for a WTO role in promoting domestic regulatory transparency in member countries
- Priority resource allocation to the APEC Structural Reform Behind-the-Border agenda
- Significant redesign to services trade and investment liberalization vehicles to achieve priority objectives with respect to behind-the-border regulatory barriers to doing business, including specifically with respect to the currently inefficient bilateral "Free Trade Agreement" vehicle
- Cessation of automatic Australian priority to "comprehensive" bilateral negotiations covering Goods (Agriculture) as well as Services

Organisational Reforms

- Reorganisation of the Department of Foreign Affairs and Trade, Austrade and EFIC, to facilitate dedicated pursuit of a National Strategy for Services Exports
- Appointment of an Associate Secretary for Services Globalisation in the Department of Foreign Affairs and Trade
- Creation of a Standing Inter-Departmental Committee on Services Globalisation
- Creation by the Minister for Trade of a high-level Services Competitiveness Council for industry consultation and awareness raising, including across portfolios
- Creation of a Services Globalisation Unit in the Department of Prime Minister and Cabinet
- Reorganisation of the Department of the Treasury and the Department of Broadband, Communications and the Digital Economy to enable greater attention to Services Globalisation
- Allocation of more significant resources in the Department of Innovation, Industry, Science and Resources to activities to boost competitiveness and international business development of the Services Economy

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1. The Opportunity

Services constitute two-thirds of world gross domestic product (GDP). Services are intrinsically people-intensive industries and, despite rapid growth in labour productivity in services, are also the source of most global job growth over the last decade.

In Australia, services account for 78 percent of GDP and 60 percent of domestic investment. Services employ 8.5 of every 10 Australians, with all net job growth over the past two decades taking place within the services sector. Austrade estimates 82 percent of Australian firms to be services firms, though only 3 percent of them appear to be exporting. Most are small and medium sized and don't appear on the trade policy radar. There is a big opportunity ahead of us as our services industries globalise.

Services exports in 2005, as measured by the ABS, were $37b and growing at about 4 percent a year:

- Tourism $11b
- Passenger Transport $7.5b
- Education $7b
- Finance & Insurance $1.5b

At 23% of total exports, services exports are already larger than rural exports and almost on a par with manufactures exports.

But this is known to be a significant under-statement of actual services exports. Much more work needs to be done to determine the true value of the sector's share of exports.

We know the services sector makes a much larger contribution to exports than its direct share, as services are often integrated with other goods. On average the ABS data suggests that about one-fifth of the value of Australia's goods exports is composed of services.

We also know that the Balance of Payments (BoP) data does not measure services exports delivered via offshore commercial presence (branches overseas) or franchises. Recent ABS surveys of Australian-owned foreign affiliates show the BoP is probably picking up less than one third of the actual "exports" of services taking place. Recent EFIC data shows Australia's offshore investment flows now exceed inward investment flows, reinforcing the evidence of significant unmeasured services "export" activity. [1] One

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[1] Importantly, services contributed more than half the companies on the Global100 complied by IBISWorld/EFIC of Australia's top international companies by foreign revenue. Many different service industries are involved including: financial, property, engineering, transport, communications, media and consumer services. Moreover, the world's top companies in many service industries such as engineering, architecture, property management and analytical services have a strong representation from Australian firms.

source of difficulty around the measurement of services relates to its definition. The term “services” covers a broad range of industries that produce value by providing solutions to customers’ problems. Despite their great diversity, services industries are in fact less heterogeneous than is commonly understood. Services have many important common characteristics, interests and priorities that distinguish them sharply from the goods-producing sectors. These include:

- high labour-intensity
- high knowledge-intensity
- high ICT-intensity
- strong influence from cultural issues
- unique challenges in intellectual property
- difficulties in collecting statistics
- complex and unfamiliar barriers to trade, typically not applied “at the border”
- strong sensitivity to immigration issues
- deep political “sensitivities” with respect to national sovereignty
- comparatively heavy dependence on offshore investment in order to export
- prevalence of government ownership and monopolistic structure
- marked legacy of heavy regulatory intervention
- while this is changing, the strong historical legacy means that services generally are at an earlier phase of the cycle of market liberalisation and globalisation, compared to goods sectors
- special issues facing public/private partnerships in services infrastructure delivery, including offshore
- quite different financial structures for services businesses, compared to goods-based sectors, and hence different sensitivities to tax and financial reporting regulation and to capital markets conditions
- rapidly changing business processes and methods of service delivery.

In addition, the services industries typically provide the essential infrastructure and enabling networks for the goods-producing sectors. Services industries essential to the productivity of the economy as a whole include education, health, energy, water, banking and financial services, telecommunications and transport.

Many goods, moreover, have traditionally been “bundled up” with “product-related” services and many goods-producing processes contain “embedded” value-adding services. In a globalised environment, however, services can become increasingly “unbundled”. Lower value-add services, like goods, become “commoditised” and can and do enter global supply chains.

These and other characteristics of services industries tend to be poorly understood throughout the public policy community. This is hardly surprising given that the official statistics which inform policy thinking are still published via out-dated and analytically not very useful ANZSIC categories.[2] In exploring issues related to trade in services, it is often analytically ore useful to draw on the categories in the WTO General Agreement on Trade in Services, namely Communications, Construction and related services; Distribution services; Education services; Energy services; Environmental services; Financial services; Health and social services; Tourism services; Transport services.

In all of these industries, there is a major export growth opportunity for Australia.

Most of these industries are currently, however, facing significant challenges in the global market. There are warning signs of potential decline in Australia's competitiveness, including price sensitive slowdown in in-bound tourism and exports of education and IT services, declining share of Australian services exports in global services trade and widespread knowledge-intensive skills shortages. The services unions and employer firms alike rightly worry that Australia is not attracting its potential share of global work onshore.

These realities need to be addressed jointly by both Government and industry. There is much that industry can do, but it can not do it alone. The role for Government has its origin in the fact that global services markets are more distorted than goods markets because they have a deep history of government intervention, including ownership, and a consequent intense regulatory legacy.

To achieve our shared export objectives, and to design appropriate new policy settings and instruments, we first need to bring about a paradigm shift in Australian trade policy thinking.

2. The Paradigm Shift Required

Trade Policy has to be thoroughly redefined to take account of Services. There is huge inertia in the system against this. It is very important to recognise this, because without the paradigm shift in trade policy mind set required, any attempt to boost services export performance will be largely doomed to failure. The shift required is summarised in the box below.

The Old Model

In a relatively closed, goods-oriented economy, "trade" was the flow of goods across the border and "trade policy" was about managing that flow.

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[2] We look forward to the rollout of statistical collections according to the new iteration of ANZSIC.

Trade in "money" and in other "financial instruments" also took place, but the management of capital flows (ie the extent to which the national market was segmented from the global market) was generally considered beyond the realm of "trade" policy as such.

The same applied to foreign investment. People also crossed borders, but management of that flow was similarly considered to be beyond the realm of "trade" policy.

In that historical paradigm, "export policy", the topic of this review, was focused on maximizing the contribution to GDP growth from net foreign exchange earnings on the current account. It followed that boosting export performance of goods was about;

1) where market failures or positive externalities exist, designing "appropriate" domestic interventions to stimulate or support production, subject to WTO rules on subsidies
2) investment in physical infrastructure
3) export promotion, branding and marketing overseas and
4) trade negotiations, generally of a reciprocal nature, to remove barriers to goods export market access at "offshore" borders

The New Model

In a globalizing services economy, the concept of "trade" necessarily becomes extended to cover all economic interaction between residents and non-residents and "trade policy" becomes about managing the extent of non-resident participation in every national economic transaction.

Every domestic regulatory regime takes on an international "trade policy" dimension. The notion of "border" becomes much less relevant.

Management of capital market integration is nolonger irrelevant to "trade" policy. Nor is management of foreign investment flows. Services are delivered[3]to non-residents via fly in/fly out of both provider and consumer; internet enablement, and commercial presence offshore.

In this more modern trade policy paradigm, the objective of "export policy" is about developing a strategy to maximize Australian residents' earnings, directly or indirectly, from engagement in global economic activity[4]. This is a very much larger policy task.

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[3] We use the word "delivered" because the ABS is reluctant to describe all of this as "export"

[4] The idea of "resident" rather than "national" is imposed, somewhat problematically, by global statistical convention.

A strategy to boost services export performance will look a bit different then from a strategy to grow Australia's goods exports. The strategy will require

1) designing "appropriate" interventions to stimulate or support the accumulation of resident pools or "hubs" of globally competitive services expertise[5], and in the absence of any WTO rules on subsidies for services
2) infrastructural investment in the knowledge economy (education, broadband etc)
3) export promotion and marketing methods which specifically accommodate the unusual manner of services delivery
4) trade negotiations will need to embrace immigration and investment regimes as well as inefficiencies in other countries' micro-economic sector-specific "behind-the-border" regulatory regimes - these differences are such that it can not be taken for granted that the traditional goods-trade negotiating fora and goods-trade liberalization vehicles will necessarily work for services.

In moving from the old goods-based model to the new services-oriented model, a complete shift in policy mind set is required.

In thinking about exporting a service, it can be helpful to think in terms of exporting a solution[6]. For Australia to brand itself successfully as a services exporter, Australians have to build a reputation for excellence in coming up with solutions. We have to build visible centres of services expertise. We examine these issues in section 3 below..

We also examine, in section 4 below, ways to open up the global market place. This is complicated by the fact that services are delivered internationally in 4 distinctly different ways:

1 Mode 1 Cross-border supply: the service itself flows from the territory of the exporter into the territory of the importer, usually transmitted via telecommunications;
2 Mode 2 Consumption abroad: the services consumer travels temporarily into an exporting country's territory to obtain a service abroad;
3 Mode 3 Commercial presence: a services provider establishes a local presence, including through ownership or lease of premises, in another country's territory to provide a service in that market
4 Mode 4 Movement of natural persons: the services exporters travel temporarily to the territory of another country to supply a service.

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[5] Expertise for example, in financial services, in ICT services, R&D services, logistics and supply chain services, professional and technical services, education services, health and well-being services or tourism services etc.

[6] Often, of course, that solution has a good attached to it as well.

The trade barriers encountered vary with the mode of delivery employed. The major barriers tend to relate to Modes 3 and 4 ie they lie in investment and immigration regimes. But the 4 modes are substitutable and firms tend to use them all; in particular firms avail themselves, in any particular jurisdiction, of the least restricted mode. The GATS identifies the major barriers as:

- Limitations on the number of service suppliers
- Limitations on the total value of services transactions or assets
- Limitations on the total number of service operations or on the total quantity of service output
- Sector specific Economic Needs Tests or limitations on the number of persons that can be employed
- Measures that restrict or require specific types of legal entity or joint venture through which a service may be provided
- Limitations on the participation of foreign capital in terms of a maximum percentage limit on foreign shareholding or the total value of individual or aggregate foreign investment.
- Measures which affect nationals differently from foreigners
- Measures which affect established foreign companies differently from established nationally-owned companies

3.Globalising Australian Services

Industry and export assistance programs straddle several government agencies and different levels of federal, state and territory governments. Relatively few of them were designed specifically with services exporters in mind. We do not, in this report, argue their case. Services firms will seek to avail themselves of whatever assistance is available, but none of the existing schemes are of sufficient interest to justify strong ASR support.

What we are looking for is something a bit different.

Typically what services industries require, in order to boost local industry development and export performance, is a “whole lot of little things” across a range of policy portfolios. Many of these are identical across all services sectors. Getting the conditions right to enable development of Australia as a financial services centre, for example, is not dissimilar from what is required to get the conditions right to enable development of an IT services centre, or a regional education hub, or a health or eco-tourism destination. In each case, it requires a whole-of-government approach to building services excellence.

In Attachment 1 “ Building a Financial Services Centre” we take one specific sectoral example and explore whole-of-government ways in which Australia might move to support local excellence and expertise in financial services. We hope in so doing to start the process of creating a new “policy template” for services industry development and export policy, in which the fundamental onus is on industry itself to "innovate and compete", within a policy and regulatory environment which is conducive to doing so.

To the extent that government assistance is relevant, we prefer outcome- or performance-based measures which facilitate the process of innovation for the global market. One measure we consider would be helpful in assisting services providers offshore is introduction of a taxation deferment plan for project-based export activity.

Unlike the regime applying in the WTO with respect to trade in Goods, there are no international trade rules which discipline subsidies or incentives to services industries, whether for production, employment, innovation, environment or any other local or international policy consideration.[7]

It is pause for thought, therefore, to consider why, in Australia, there has never been any effort to design any services-specific export facilitation instrument? So much effort has gone, over the years, into designing and redesigning instruments such as EMDG consistent with the rules on trade in Goods, yet no Australian government has ever yet designed and offered the services industries any generic services–oriented export development support.

The explanation lies largely in the Goods oriented paradigm in which public policy has been locked. It also lies in the fact that apart from one or two sectors creating critical local cultural content, Australia's services industries do not have any history of clamouring for industry assistance nor any current leaning to do so.

But services representatives do look at the Government's almost $16 billion spend on industry support in other, largely declining non-taxation paying sectors and weep! And again, unlike the services sector, we are clearly witnessing now a vocal call from Australia's carbon-intensive trade exposed sectors for additional protection and support.[8]

In its "Trade & Assistance Review 2006-07, the Productivity Commission noted that Australia's services industries are put at a competitive disadvantage as a result of the industry assistance which the Government still provides to the agricultural and manufacturing sectors.

"While industry assistance has declined greatly over recent decades, assistance provided by the Australian Government remains significant.

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[7] This is part of the "unfinished business" of the GATS and is highly likely to remain "unfinished" at the end of the Doha Round.

[8] This submission does not touch specifically on WTO jurisdictional or other trade-related issues associated with allocation of permits under an emissions trading scheme. ASR would however wish to participate in and contribute to any trade-related stakeholder consultation process on this issue.

In 2006-07, the government measures covered in this report provided assistance to industry equivalent to $15.7 billion in gross terms, and $8 billion in net terms. The automotive, textiles, clothing and footwear and dairy industries received the highest rates of assistance within manufacturing and agriculture. Services industries typically attract negative assistance because tariffs inflate their input prices."

Not only has the services sector attracted net negative industry assistance, but the sector has also received relatively less attention on the export promotion front. The Trade portfolio, via Austrade, is already gearing to become more active in the promotion and facilitation of Australian services export, including importantly for small and medium sized firms and ASR welcomes this development. There has been a prolonged policy gap, also, with respect to facilitation of Australian investment in commercial presence offshore. ASR appreciates that the Government has recognized, in its recent reorganization of Austrade and Invest Australia, that this gap needs finally to be addressed.

No government agency yet offers, however, a coherent "one stop shop" which can help address all the relevant aspects of services export promotion. We recommend, therefore, the establishment of a specific services export promotion mechanism within Austrade which would assist existing and potential services exporters interalia with offshore investment, with tendering into global services supply chains and with visa facilitation for staff to come to Australia and for Australians to locate off shore.

Our pilot study in South Australia (see Attachment 6) also identified a need to create centralized services export intelligence data banks, to facilitate services exporter networking opportunities, especially for smaller firms and to facilitate access to specialized export training for small and medium sized services firms.

The ASR also seeks greater equity for services in all existing trade promotion programs. If DFAT continues to find it effective to provide travel assistance to the agricultural sector to participate in overseas meetings, this assistance must also in our view be extended to the representatives of the services sector.

Similarly we note that the Department of Agriculture, Forestry and Fisheries provides funding for agricultural sector industry stocktakes through its Industry Partnerships Programme. An equivalent programme should be instituted for the services sector. In Attachment 5 to this report, we reiterate our request of the Federal government to partner with ASR in undertaking a major Services Sector Stocktake.

4. International Trade Diplomacy and Negotiation

Giving services export interests proper priority in bilateral, regional and multilateral trade negotiations is critically important because the potential gains are so large. With respect to Australia, Productivity Commission estimates suggest that the gains from liberalising trade in services could double or even triple the potential gains estimated by DFAT to accrue from liberalizing agriculture.

But in ASR's view, the current suite of services trade negotiating mechanisms are unlikely to help us reap these potential gains.

To put it simply, they aren't working. They aren't working multilaterally and, unless certain conditions apply, as set out in the relevant section below, they are in our view, unlikely to work on a bilateral or regional basis either.

WTO market access outcomes on services to date have been poor. Bilateral "WTO plus" outcomes are rare. To reap the Trade Minister's recently announced objective of "WTO plus plus" outcomes, Australia will need to drop a lot of old negotiating habits and develop a next generation tool kit.

Interestingly, ASR has found a high degree of common ground on this matter with services export coalitions in our trading partners, whether they be from developed or developing economies. ASR is an active and respected member of the Global Services Coalition and the Financial Services Working Group. In both groups we find that we all want similar outcomes ie harmonization around better regulatory practice both at home and abroad and fewer investment and immigration barriers.

This business experience suggests that whether it be in the multilateral, regional or bilateral context, concerted services liberalization has the potential to be genuinely win-win if governments can make the negotiating paradigm shifts required.

4.1 Multilateral Trade Agreements

4.1.1 Doha Development Agenda

Attachment 2 sets out our joint objectives, along with other global services industry coalitions, for the Doha Development Agenda. As our media release of May 2008 makes clear, we are not close to achieving these objectives.

In general, the Doha offers on services are thin and patchy in their sectoral coverage. ASR members, nevertheless, would rather reap what harvest there is than risk losing it altogether.

The Australian services offer, despite its essentially standstill rather than liberalising nature, is among the best offers on the Doha negotiating table and we expect that Australia's revised offer will place it again amongst the most ambitious.[9]

We are encouraging the Australian government in its efforts to bring the Doha Round to rapid closure. If this does not prove possible, we will be looking for ways to avoid losing what progress has been made in the services arena, including on a plurilateral basis. And if the Doha Round does come to a rapid conclusion, we are calling on the government to ensure the deal includes a built-in agenda of ongoing critical mass, mfn-based negotiations on services.

The problems associated with the Doha Round have caused us also to think more broadly and more deeply about our multilateral objectives. Australian services exporters, being outward looking, have much in common with Australian agricultural exporters. We each face artificial distortions in overseas markets which are uneconomic even for the communities they claim to protect.

A higher level of transparency of government intervention in the business environment and a deeper focus on independent analysis of the costs and other impacts of this intervention would assist in building constituencies which would be more supportive of local reform.

In the case of services, the interventions and distortions take the form chiefly of inefficient, i.e. opaque, burdensome, duplicative, mutually inconsistent and overlapping domestic regulations affecting who can participate in services industries and limiting in particular the scope of business for foreigners.

4.1.2 Transparency

The current paucity of WTO services offers from developing countries suggests that before any substantive progress can be made via international negotiations to reform the regulatory environment in these trading partners, a prior step is required to increase the transparency of their regulatory regimes.

The ASR and the New Zealand Services Group have therefore joined forces with the National Farmers Federation and the Federated Farmers of New

[9] This is appropriate. We want to be world's best practice because it's good for us. Of course we also want our trading partners to shift towards better regulatory practice and offer us some market access. But it only damages us to hold back and wait on them to reciprocate. Australia, in the WTO, is a demander on Agriculture. And a somewhat reluctant party on Manufactures. We aren't bringing much that's new to the negotiating table in these sectors. On Services, we should be signalling big intentions.

Zealand to sponsor the Tasman Transparency Initiative to strengthen the WTO.

The initiative, which we have called on the Australian and New Zealand Governments to support, proposes the establishment, inside the WTO Secretariat of a unit oriented to promoting and facilitating the building, in WTO members, of institutions which will enhance the transparency of barriers to trade and investment in both the goods and the services sectors.

Enhanced transparency is important because it is the first essential ingredient in managing the political economy of domestic regulatory reform.

4.1.3 Post Doha Agenda

Whether Doha succeeds or fails, services providers know now that we will need ongoing negotiations in services because the level of ambition for services liberalisation to date has not been (and the evidence is that it will not be) high enough to meet private sector expectations.

ASR is therefore calling on the Government to lead a major post-Doha initiative on Services. The first steps must be reflected in a final Doha agreement on a built-in agenda to recommence immediate negotiations on services market access, and outstanding rules, especially on domestic regulation.

What this means is that we are no longer as firmly committed as we once were, to the notion of a single undertaking, ie comprehensive negotiations on all sectors simultaneously with nothing agreed until everything is agreed.

We tend to favour, in future, post Doha, the idea of services specific negotiations, whether or not the critical mass also exists to get a further round of negotiations under way simultaneously on agriculture or manufacturers.

For critical mass negotiations to succeed, they require the key national players in services to participate. We accept that negotiations might only attract say 30-40 initial players. Less than a third of the WTO members have in any case submitted Doha Round offers on services to date.

We believe there will however be a strong incentive for countries initially outside the agreement to ultimately join in, or fail to attract critical investment in services infrastructure. Already the evidence is that countries which have not signed the telecoms reference paper, for example, do not attract telecommunications investment. In our view an international services agreement that covers the major players would place heavy pressure on non-participants to co-operate or face significant competitive disadvantages. For this reason, we call for any such critical mass negotiations to be based on mfn and to take place under the umbrella of the WTO.

We would however see advantage in shifting the meeting place from Geneva to a location in Asia-Pacific eg Hong Kong.

4.1.4 Investment

The relationship between investment flows and trade flows in complex and evolving and significantly the policy divide has become blurred.

In goods sectors, inward flows of foreign direct investment are thought of as acting as a substitute for trade. Foreigners are motivated to invest overseas in order to get around tariff and non-tariff border barriers in the host country by servicing the host market from inside. “Pre-establishment” barriers to investment limit this option.

Foreign investment also acts a complement to trade. Investment may be focused on exploiting comparative advantages in the host economy, boosting bilateral or global export from the host economy. Investment also seems to stimulate export growth from the home economy of both goods and services, including via intra-industry trade.

When their domestic clients invest offshore, services providers try to follow them abroad. Often they require a commercial presence in the offshore market to service them effectively, so they also invest. If the policy regime is sufficiently open, foreign investment in goods can breed foreign investment in services. Services providers also look for foreign clients in their own right - and to service them effectively, they need to pursue their own offensive investment interest to achieving commercial presence in that market.

As services activities which traditionally have been government-owned and operated enter the realm of the private market place, they also became attractive to the international market. Foreign participation in these activities requires inward direct (and portfolio) investment.

Investment is of fundamental importance to the way in which services firms do business offshore. Investment doesn’t figure on the WTO agenda. But it is not completely absent either.

The Uruguay Round achieved both the Agreement on Trade-Related Investment Measures and the GATS provisions on Mode 3 (Commercial Presence). Services trade negotiators have had to learn a lot about investment issues because most services trade restrictions lie in mode 4 (immigration regimes) and mode 3 (investment regimes) and apply horizontally i.e. economy-wide.

The concept of Commercial Presence/Right of Establishment, when combined with GATS rules on National Treatment, necessarily takes services negotiators into both pre- and post- establishment issues.

ASR supports the idea of multilateral negotiations in Investment taking place in the WTO.

4.2 Bilateral Trade, Investment & Tax Agreements

A number of ASR members have contributed to the Review Questionnaire outlining their specific commercial experience with individual existing FTAs. Our objective in this section of our submission is to draw out some broad lessons learned on the services front, not only with existing FTAs but with those under negotiation.

It is probably fair to say that services issues have played a prominent role in Australia's FTA negotiating agenda. The experience, however, is that in FTAs with developing country partners, services and investment liberalisation are not proving much easier to negotiate one-on-one than they are in the multilateral context. In every FTA negotiation in which Australia has been engaged to date, with a developing country partner, services and investment aspects have been exceedingly difficult. This is because services markets typically have very high levels of government intervention, liberalisation of trade and investment in services tends to be highly politically sensitive and most developing country governments are not displaying the will to undertake the necessary regulatory reforms. It is also our view that more services trade-related capacity building and technical assistance is required to build awareness and understanding of the costs and benefits of liberalisation in trade in services.

The most constructive aspect of the FTA negotiating process with respect to developing countries has been that it allows Australia to undertake a much deeper policy dialogue on services related matters, including what constitutes regulatory best practice, than is otherwise possible with non-OECD trading partners. Such a policy dialogue should over a period of time be able to facilitate regulatory cooperation and harmonisation, carrying the promise of deeper economic and business integration over the medium term.

Unfortunately, in the context of formal trade negotiation, this has not been Australia's apparent attention. The negotiating intention has been to obtain , and to the extent possible retain, a margin of preference for existing Australian exporting firms. Australia's negotiating mandates have been too narrowly focused on achieving small wins on market access, rather than on achieving deeper microeconomic reforms. Domestic regulatory issues have been largely off the agenda as not part and parcel of bilateral preferential negotiation.

As a consequence, Australia's FTA agenda has been of limited actual value in improving the business environment for enhanced trade and investment in services. The most constructive outcomes have been the establishment of ongoing working groups and committees to examine possibility for regulatory harmonization or mutual recognition over time. To be effective, however, panels/committees which are established pursuant to a PTA need to have teeth.

To sum up, the value, as we see it, of bilateral engagement with trading partners, lies simply in establishing a vehicle, which in itself may be of limited utility, can nevertheless provide a platform to keep chipping away at behind the border barriers, bringing the domestic constituency on board over time, hopefully in time facilitating a staged approach to regulatory reform. We have little consequent interest in the further pursuit of FTAs as currently constructed and call for a new suite of bilateral instruments focused on policy and regulatory micro-economic dialogue.

ASR has been disappointed with the lack of progress made in Geneva to tighten the WTO's own rules covering FTAs. We support fast tracking of the WTO's new Transparency Mechanism for newly signed PTAs.

Given the number of FTAs already under negotiation or proposed, we set out in Attachment 4 a detailed set of principles which we consider should guide negotiations with respect to services trade and investment issues. Importantly these principles cover trade, investment, capital market, taxation and immigration policies.

We support development of a negotiating template to reflect these principles which in our view should apply to all trading partners, with adjustment on a case by case basis to reflect the level of their economic development.

4.3 Regional Architecture - APEC

From a services industry perspective, Australia's key objective in the region should be to free up the regional environment for doing business, so that business can operate relatively seamlessly as if in a single market across the region.

Improving the business environment for services firms requires an intensified regional effort towards harmonisation and mutual recognition of standards and professional qualifications and convergence in other regulatory practices.

This is a two step process. The first step, for the reasons set out above, is to improve the transparency of regulatory and other behind-the-border inefficiencies. Importantly, appropriate domestic and regional institutions need to be built to support this process. The second step, as the inefficiencies are made more visible, and the costs associated with them more obvious, especially to domestic stakeholders, is to build a concerted regional effort to eliminate the most inefficient (discriminatory and non-discriminatory) aspects of these omnipresent regulatory barriers beyond the border.

With respect to the first step, ASR's experience is that targeted strategic technical assistance and the building of research capacity inside our trading partners is the key to unlocking real progress. We are expecting that the new Structural Reform agenda, to be kicked off with an inaugural Ministerial meeting in Melbourne this year, will prove to be a powerful central mechanism in future to realising our broad objectives in this respect.

With respect to the second step, ASR's repeated experience as outlined in the previous sections, is that formal international trade negotiations are not necessarily the only or the best international diplomatic vehicle by which regional barriers to trade in services can be addressed.

Our experience in the WTO Doha Round and with Australia's bilateral FTA agenda, has served to strengthen our conviction that the worst barriers to services trade and investment lie largely outside the traditional trade negotiating arena. For this reason, we see little value in pursuing the traditional concept of a regional FTA.

We are more interested in potential new mechanisms that can address behind-the-border regulatory obstacles to doing business. We are hopeful therefore that the Structural Reform agenda will deliver an intensified micro-economic policy dialogue on regulatory best practice, and a continued redirection of technical assistance towards building sectoral regulatory capacity and public policy research institutions which can assist regional governments to manage the political economy of trade reform.

In most APEC economies, Trade Ministries are the least well informed about what goes on domestically in any particular regulatory regime. In the interests of trade and economic integration, its time for Trade Ministries to get on top of this issue and start to champion regional regulatory review.

The regional business experience with regulatory red tape is not good. The obstacles to doing business are very considerable. New market entrants cant necessarily obtain a licence to operate – or when they do can its scope is often unexpectedly limited and the regulatory compliance obligations unexpectedly expensive. Importantly for services companies (where human capital costs are often 70-80 % of total cost) everything to do with recruiting, training and deploying people can be extraordinarily complex.

Regulatory reform is a top priority for business in meeting today's global challenges. The extent to which firms can connect effectively with business elsewhere in the region depends on how familiar the regulatory environment is. Effective connection is critically important for business performance, as the global supply chain model becomes increasingly pervasive. The APEC Structural Reform agenda will hopefully provide a consciously articulated, dedicated policy focus on reducing the region's regulatory burden.

5. Cross-Portfolio Institutional Reform

In ASR's view, federal government policy making and regulatory structures have not adjusted sufficiently to take full account of the implications of globalisation.

Many separate government departments and agencies have carriage for aspects of government policy and programs which impact on services trade outcomes. Many regulatory authorities also have responsibility for matters which impact importantly on services trade outcomes.[10] And insufficient coordination or interaction takes place.

The time has come in our view to review the separate mandates of these various agencies with the purpose of improving economic policy coordination and coherence. Globalisation means that artificial policy separation of the "domestic" and "international" dimensions of national economic performance is not only increasingly difficult but is also likely in any case to lead to increasingly poor policy-making outcomes.

The Trade portfolio has been focussed on trade diplomacy and trade promotion. At last, responsibilities for trade promotion have been combined, in Austrade, with on- and off-shore investment promotion responsibilities. Bringing together inwards and outwards investment facilitation within Austrade is a solid step in the right direction in supporting all modes of services trade and coordinating trade and investment facilitation efforts. This constructive institutional reform needs to be complemented by similar coordination and integration of the associated policy making responsibilities.

In particular, the Trade portfolio needs a mandate which allows it to extend beyond a "postbox" approach to services trade policy matters and assert a much stronger international negotiating perspective vis-à-vis other services-related policy agencies to ensure that our own regulatory house is truly in order.[11] The fact is that Australia's own barriers to trade in services lie deep inside our borders in our domestic regulatory systems. The barriers we face to doing business offshore are similarly to be found in our trading partners'

[10] As well as the Department of Foreign Affairs and Trade and Austrade, these include the Departments of Treasury, Broadband/Communications, Education, Immigration, Health, Transport/Infrastructure, Innovation/Industry, as well as agencies such as the Tax Office, Intellectual Property Office, Customs and regulatory bodies such as ASIC and the ACCC.

[11] DFAT's recent efforts to establish individual Services Sector Reference Groups have been helpful in bringing all relevant Government agencies together with industry stakeholders to commence a more coordinated approach to facilitating services exports. But much more needs to be done to ensure that all relevant Government agencies are engaged in the trade process and the necessary mechanisms are in place to obtain industry advice on impediments to doing business offshore in a comprehensive and timely way.

regulatory regimes. As long as the Trade portfolio and our trade negotiators focus primarily on barriers at the border, the challenges facing Australia's services exporters will not get adequately addressed.

The problems we face would be eased if there existed a visible pool of resources within the bureaucracy dedicated to developing the services economy. The malaise in Australia's services trade performance will only be overcome when international services issues stop being a part time job for many people, and a single area of government takes high level responsibility for creating the right policy environment to improve the sector's export performance.

In order to overcome current piecemeal arrangements, ASR specifically proposes the following:

- Internal reorganisation within the Department of Foreign Affairs and Trade, Austrade and EFIC, to facilitate dedicated pursuit of a National Strategy for Services Exports

- The creation of a new senior position in DFAT to be termed Associate Secretary for Globalisation who would be located between the Secretary and the Deputy Secretaries

- Creation of a Standing Inter-Departmental Committee on Services Globalisation chaired by the Associate Secretary comprising representatives at Deputy Secretary level of all agencies with responsibilities impacting on services trade competitiveness issues

- Creation by the Minister for Trade of a high-level Services Competitiveness Council for industry consultation and awareness raising, including across portfolios

    -This new institution, to comprise senior representatives from the services sector, would take a holistic approach to understanding the internal and external drivers of Australia's competitiveness in services, hence helping to enlighten Australian services trade diplomacy

- Creation of a Services Globalisation Unit in the Department of Prime Minister and Cabinet

- Reorganisation of the Department of the Treasury and the Department of Broadband, Communications and the Digital Economy to enable greater attention to Services Globalisation

- Allocation of more significant resources in the Department of Innovation, Industry, Science and Resources to activities to boost competitiveness and international business development of the Services Economy

- Creation of a Services Competitiveness Sub-Committee of Cabinet
- A more radical approach, which ASR would also support, would be to create a new Department of Globalisation which would take carriage of all issues impacting on Australian businesses in both the goods and services sectors pursuing offshore revenues

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