

## WHAT IMPACT HAS THE AUSTRALIA-UNITED STATES FREE TRADE AGREEMENT HAD ON PUBLIC PROCUREMENT

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**ABSTRACT** The United States procurement market, including the military is the largest in the world and one that is very competitive for those that are able to access it. On the 18 May 2004, Australia and the United States signed a comprehensive free trade agreement. The Australia - United States Free Trade Agreement (AUSFTA) took effect on 1 January 2005 and provided access for Australia to the largest government procurement market in the world. The agreement also provided the same access to the Australian procurement market for US suppliers. The core objective of the government procurement chapter of the AUSFTA (Chapter 15) is an agreement to provide non-discriminatory access to the procurement framework of each country. It is now over five years since the signing of the AUSFTA and the aim of this working paper is to assess the impact and benefits of this agreement on both economies, including public procurement.

### INTRODUCTION

Free trade agreements between two or more countries generally include commitments to reduce or eliminate tariffs on goods traded between countries party to the agreement, as well as the liberalisation of the trade in services and investment. The agreements usually include provisions seeking to maximise the benefits of liberalised trade – covering such matters as government procurement, intellectual property and competition policy.

Between 1995 and 2008 more than 200 free trade agreements were concluded globally and the World Trade Organisation expects this to grow to 400 by 2010.

Australia has a range of bilateral and regional trade agreements, including a long standing one with New Zealand, which commenced in 1922. Following this, the New Zealand – Australia Free Trade Agreement was

signed in 1965 and the Australia – New Zealand Closer Economic Relations, commenced in 1983.

In more recent times Australia has signed bilateral agreements with:

- Singapore – Australia (commenced 28 July 2003)
- Thailand – Australia (commenced 1 January 2005)
- Australia - United States (commenced 1 January 2005)
- Chile – Australia (commenced 6 March 2009)
- ASEAN – Australia - New Zealand (commenced 1 January 2010)

Negotiations by the Australian government for further bilateral agreements are underway with a range of countries and regional groups including the Republic of Korea, China, Japan, Malaysia and the Gulf Cooperation Council.

Feasibility studies are also currently being conducted on bilateral agreements with India and Indonesia.

The Australian government has asked the Productivity Commission (December 2009) to undertake a study of the bilateral and regional trade agreements signed. The study is to examine the effectiveness of trade agreements in reducing trade barriers and also the impact on our trade performance.

The recent free trade agreements signed by Australia were the product of the former Howard government (1996 – 2007), which commenced the negotiations for the Singapore agreement in 2000. That same year George Bush was elected as US President and it was no secret that the Howard government wanted a free trade agreement with the world's largest economy. The Howard government announced its intentions to pursue a free trade agreement with the US at the end of 2000.

Whilst, the primary focus of a preferential trade agreement should be commercial, it was clear that there were foreign policy goals in the negotiations with the US. The 11 September 2001 terrorist attacks in the US and the 2002 Bali bombings close to Australia reinforced the political dimensions of security to the negotiations of the agreement with the US.

Research undertaken by Adrian Rollins details the linking of trade and foreign policy by the Howard government, so evident in the AUSFTA. Rollins states that the AUSFTA “fell far short of early ambitions for an arrangement that would deliver true trade openness between the two nations, particularly regarding the US’s heavily subsidised agricultural sector. The heavily compromised deal was an inevitable consequence of its political origins. Howard’s desperation to secure an outcome in the

heightened atmosphere of the war on terrorism meant political imperatives trumped economic sense, saddling the nation with an agreement that was more significant for its political symbolism than its commercial gains.” (Rollins 2010)

On the 18 May 2004, Mark Vaile, Australian Trade Minister and Robert Zoellick, US Trade Representative, signed the Australia - United States Free Trade Agreement. The AUSFTA took effect on 1 January 2005 and immediately provided access for Australia to the largest government procurement market in the world. The agreement provided the same access to our procurement market for US suppliers. The Australian government and each state and territory amended their existing procurement processes in order to comply with the AUSFTA. On 1 January 2005 the *Commonwealth Procurement Guidelines* were revised to meet our international obligations under the bilateral free trade agreement with the United States.

## **GOVERNMENT PROCUREMENT**

The bilateral agreement between the two nations has raised the standard of market openness to both economies for government procurement. The AUSFTA had a larger impact on government procurement in the United States than in Australia, since Australian government procurement was already open, with US suppliers being free to bid for government work in Australia. In contrast, Australian companies were restricted by the US Trade Agreements Act from bidding for US federal government work, because Australia did not have an agreement with the United States on government procurement, prior to 2005.

In 2005, at the commencement of the AUSFTA, procedural regulation for Australian government procurement was low, in contrast to that in the United States. In Australia the central procurement policy objective is value for money, whilst in the US it is due process.

The agreement sets out rules, procedures and transparency requirements for government purchasing which gives Australian businesses non-discriminatory access the federal government procurement market and a large number of state governments in the United States.

The structure of government procurement between both countries is different in that Australia's is very much a principles-based procurement framework, whereas the US is highly regulated through rules governing all aspects of the acquisition process. Our *Commonwealth Procurement*

*Guidelines* are 46 pages in length, as opposed to the over 2,000 pages of US Federal Acquisition Regulations.

The core objective of the government procurement chapter of the AUSFTA (Chapter 15) is an agreement to provide non-discriminatory access to the procurement framework of each country. Chapter 15 applies to covered procurement, which means procurement of goods, services or both:

- By any contractual means.
- For which the value equals or exceeds the relevant threshold, for example, \$US64,786 (US federal government contracts) and \$US7,407,000 (US construction services contracts).
- Conducted by a procuring entity.
- Is not excluded from coverage by the agreement.

There are numerous exclusions from the operation of Chapter 15, for example, security related procurement by the Australian Department of Defence is excluded. We also retained the Australian industry involvement in defence procurement.

Chapter 15 also lists mandatory procurement procedures for covered procurements. It is no longer permissible to discriminate against tenderers on the basis of their US origin or that they are owned by a US entity. As a result of the non-discrimination provisions Australia is listed as a designated country under the US Trade Agreements Act (1979). This allows Australian companies to bid directly on US government procurement contracts. The AUSFTA also requires the US to provide Australia with a waiver on the 6 per cent penalty imposed on foreign goods under the Buy American Act (1933).

The AUSFTA bans offsets, which means procurement contracts cannot build in restrictions such as local content, technology transfer and export performance requirements. Australia has continued its policies that assist small and medium enterprises. Also there must be public notification of all covered procurement, with adequate time for the submission of tenders. Chapter 15 requires that all tenderers work towards a common deadline. Tender documentation must include all information necessary for potential contractors to submit responsive tenders.

For US businesses, the major impact of the government procurement Chapter 15, is the documented increase in openness and transparency of Australian government procurement processes. For Australian businesses, the impact of Chapter 15 is their eligibility to bid directly on US federal and state government tenders on an equal footing with local suppliers, as a

result of Australia becoming a designated country under the US Trade Agreements Act and being relieved of what was effectively a six per cent surcharge on Australian goods and services under the Buy American Act.

### **Size of the government procurement market**

The US government procurement market is approximately \$500 billion in size, with \$200 billion in annual spending at a federal level. At a state and local level in the US there is expenditure of approximately \$300 billion annually, with the military a \$250 billion market. Whilst not all local and state government and defence procurement can be accessed through the AUSFTA by Australian organisations, the US procurement market provides unprecedented opportunities for Australia. Thirty-one states of the United States have signed up to the agreement, including the largest procuring governments of California, Florida, New York, Pennsylvania and Texas. The US procurement market is huge, but also extremely competitive. As a comparison the Australian federal, state and territory procurement of goods and services is approximately \$100 billion.

### **IMPACT OF THE AUSFTA**

#### **International trade between Australia and the United States**

At the commencement of the AUSFTA the United States was Australia's fourth largest export market and number one for imports (merchandise trade). The balance of trade favoured the USA by \$11.8 billion.

In 2008-2009, whilst exports have increased to \$11.6 billion, the US has been overtaken by India and is now our fifth largest export market. The US has also dropped to number two in terms of imports, with China now our largest source of imports. The gap in America's favour has grown to \$13.7 billion. Australia's imports from the US have grown quicker than its exports to America.

In 2004 Australian exports to America were worth approximately 54 per cent of the value of imports from the US. In 2009 this had fallen to 41 per cent. (Tiffen)

The University of Sydney academic, Professor Tiffen points out that "Australia's exports to the US in the five years to last year [2009] grew by only 2.5 per cent, compared with double-digit growth for exports to all the major Asian trading partners." The value of Australian exports to the US is now about a quarter of those to the two leading customers, China and Japan. (Tiffen)

**Australia: International Merchandise Trade 2004-2005**

<b>Country</b>	<b>Exports \$m</b>	<b>Imports \$m</b>	<b>Balance of Merchandise Trade \$m</b>
Japan	24 955	17 161	7 794
China	13 003	19 812	-6 809
Republic of Korea	9 720	5 006	4 714
<b>United States of America</b>	<b>9 462</b>	<b>21 270</b>	<b>-11 809</b>

**Australia: International Merchandise Trade 2008-2009**

<b>Country</b>	<b>Exports \$m</b>	<b>Imports \$m</b>	<b>Balance of Merchandise Trade \$m</b>
Japan	52 768	17 842	34 926
China	39 325	37 044	2 281
Republic of Korea	19 274	6 523	12 751
India	15 425	2 114	13 311
<b>United States of America</b>	<b>11 600</b>	<b>25 334</b>	<b>-13 734</b>

In 2008-2009 Australia's top four export markets Japan, China, Republic of Korea and India grew between 35 – 65 per cent, compared to the previous year. The United States, the fifth largest export market grew only 9.4 per cent.

It is clear that the growth in trade has occurred in our region, rather than with the United States. In reviewing the trade statistics it is difficult to determine the impact of the free trade agreement on government procurement and whether there has been an increase in activity as a result

of the AUSFTA. It appears that the United States has benefited more from the free trade agreement, than Australia.

The Australian government Review of Export Policies and Programs (2008) assessed the impact of the three free trade agreements (Singapore, Thailand and the United States in relation to trade intensity.

The table below is a calculation of the share of Australia's exports to the United States divided by the share of US imports in global imports (net of Australia's). Whilst not conclusive and given the index only covers the first three years of the AUSFTA (2005 – 2007), it appears there is no increase in trade intensity between Australia and the United States.

**Australia: Trade Intensity 1997-2007 index**

<b>Year</b>	<b>United States</b>
1997	0.57
1998	0.66
1999	0.63
2000	0.63
2001	0.59
2002	0.60
2003	0.61
2004	0.57
<b>2005</b>	<b>0.49</b>
<b>2006</b>	<b>0.48</b>
<b>2007</b>	<b>0.51</b>

The second trade intensity index below is a calculation of total trade for United States as a percentage of Australia's gross domestic product. Whilst not conclusive and given the index only covers the first three years of the AUSFTA (2005 – 2007), it appears there has been a decrease in trade intensity between Australia and the United States.

#### **Australia: Trade Intensity 1997-2007 index**

<b>Year</b>	<b>United States</b>
1997	6.0
1998	6.8
1999	6.5
2000	7.0
2001	6.3
2002	6.1
2003	5.1
2004	4.8
<b>2005</b>	<b>4.5</b>
<b>2006</b>	<b>4.7</b>
<b>2007</b>	<b>4.4</b>

The Australian Industry Group (2010) in its submission to the Australia government's Productivity Commission on the effectiveness of bilateral and regional trade agreements stated that the benefits of trade agreements are not being fully realised by Australian exporters. The Australian Industry Group, with over 10,000 members, is a leading national industry body representing various sectors including manufacturing, engineering, defence, aerospace and service industries. The Australian Industry Group points out that only one in twenty Australian businesses export, which is lower than comparable industrialised economies.

The Australian Industry Group also state that there has only been a modest increase in export values since 2003, and that the growth of export volumes has been slower in the current decade than in the previous two decades. After rising rapidly in the 1980s and 1990s, the share of exports in our gross domestic product in the noughties has declined.

In late 2009, the Australian Industry Group surveyed its members regarding the effectiveness of Australia's existing bilateral free trade agreements. In terms of the AUSFTA, 55 per cent of the surveyed firms rated the agreement effective. This reported effectiveness of agreements in assisting export activities was the highest of the five countries, which have bilateral agreements with Australia.

The companies surveyed, who export to the USA, were asked specifically how effective was the AUSFTA in providing access to government contracts in the United States. Eighty seven per cent of the Australian exporters said that the AUSFTA was not effective in accessing US government contracts. The companies surveyed indicated that they now had improved access to bid on US military contracts with no duty imposition. However, the imported content requirements on government contracts in the United States were still a barrier to trade. “Five years on from the implementation of AUSFTA, Australian exporters are still finding it tough to do business in the United States because of costs, complex compliance regimes and subtle protectionism.” (Australian Industry Group) They point out in their submission that the Australian government should implement support programs and education and training to increase the awareness and benefits that free trade agreements can deliver.

**What exporters said about the AUSFTA (Australian Industry Group)**

<b>Activity</b>	<b>Moderate to highly effective</b>	<b>Low or not effective</b>
Access to new export opportunities	22%	78%
Access to US domestic markets	59%	41%
Access to set up US operations / base	15%	85%
<b>Access to US government contracts</b>	<b>13%</b>	<b>87%</b>
Access to US direct investment in Australia	0%	100%

**Case studies of success**

There are a number of Australian companies who have successfully accessed the US Defense and government procurement market during the first five years of the AUSFTA. One is Austal, a Perth based ship builder. Austal commenced operations in 1988 with a vision to build high quality commercial vessels for the international market. The company targeted the US procurement market before the AUSFTA came into effect in 2005. However, the FTA with the United States would have assisted Austal, particularly with its recent US contracts. Today Austal is the world’s largest builder of fast ferries and with a new Alabama shipyard it was successful in gaining significant US Navy contracts. Austal has a \$1.7 billion order for ten high-speed military catamaran transports. The

company recently handed over the first of two \$550 million inshore or Littoral Combat Ships.

Marand Precision Engineering is another Australian company that has successfully accessed the US government procurement market. Marand, an automotive engineering company, has built \$30 million of trailers to install jet engines for the US military Joint Strike Fighter project. The contractor for the JSF project, Lockheed Martin, has signed a memorandum of understanding to manufacture titanium and composite tails for the JSF project. This contract could potentially be worth up to \$700 million over 12 years. Prior to this Marand had not exported anything.

Compucat Research, a Canberra based company, won a \$US8 million contract with the US Department of Justice in 2006. The contract was for communications system that controls the content of confidential data passing between government networks. Following this Compucat were also successful with Australian government contracts. The company has since been acquired by Raytheon Australia in February 2010. Austrade estimates it has assisted in \$105 million worth of sales to the United States procurement market in 2005 and 2006. (Sutherland)

RuleBurst won a contract in 2006 with the US Inland Revenue Service supplying software which converts government policy into practice, facilitating the calculation of new tax assessments and child support payments. The chief executive officer of RuleBurst stated that “they now see that we are a credible force in the US market...and cracking the market would have been a lot more work without the FTA.” (Sutherland)

### **Australian business assistance in accessing the US procurement market**

Austrade is the main government agency assisting Australian businesses to access the US procurement market. The Australian government is funding extra export facilitators, including a US based Selling to the US Government team, in Washington DC. Another initiative has been the release of the *Selling to the United States Government* guide, which sets out six steps to help Australian exporters access the US procurement market. The guide aims to provide Australian businesses with a better understanding of the US procurement policies, rules and procedures.

Austrade have also held national seminars to assist potential Australian exporters. For example, “Finding and responding to US government opportunities: US Homeland Security” was held in March 2006. Other Austrade sponsored seminars have been held in 2005, often involving visiting Australian and US experts.

The US government has also provided seminars to assist Australian potential exporters to access the procurement market. In July and August 2006 the US Department of Defense funded a visit by contracting experts to Australia. The visit was supported by Austrade, with two day workshops on contracting to the US military held in Sydney, Brisbane, Canberra, Perth, Adelaide and Melbourne. To date the private sector is not providing much assistance, apart from consultants based in Australia with US procurement experience offering consultancy services.

### **Conclusion**

Five years on from the implementation of the AUSFTA, Australian exporters are still finding it tough doing business with the United States. The US export market is declining in importance to Australia, with East Asia and India growing rapidly, as a result of the resources boom. It appears that the motivation for the free trade agreement with the United States was more diplomatic and strategic, than economic.

It is over five years since the opening of the US procurement market to Australia through the AUSFTA and it is difficult to quantify the benefits to our economy and Australian businesses. In the US procurement markets there are instances of Australian businesses successfully accessing and securing government and defence contracts. However, it is difficult to determine whether the AUSFTA has had a positive impact on access to government procurement work. Accessing the US procurement market will take time and money over the medium to long term for Australian businesses targeting this large sector of the US economy.

Government procurement in both countries has been opened through the AUSFTA and whilst there are many similarities between both procurement processes, there are also many differences. The impact of the AUSFTA will gather pace over the next ten years and hopefully provide benefits to both economies through an increase in trade in goods and services. There needs to be more research over a longer period of time before we can gauge the true impact and benefits of the AUSFTA to Australian and US businesses.

There is enormous goodwill being extended to Australia from the US as a result of the long term relationship and our support in the Iraq and Afghanistan wars. At present the US Senate has before it a Defence Trade Cooperation Treaty. The treaty would free up defence trade between Australia and the United States, giving Australian based companies licence free access to the US defence market. It aims to do away with cumbersome licences and approvals for Australian companies doing business with the US under the existing arms export control system.

Coupled with globalisation and the AUSFTA, Australian businesses now have an unprecedented opportunity to access the largest procurement market in the world. Whilst the market is the largest in the world, it is very competitive and also still contains many barriers for exporters. In order to assist Australian businesses to increase their access of the US market there needs to be both public and private sector assistance.

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