

The changing architecture of the Asia-Pacific trading system: Implications for the Indonesia-Australia Comprehensive Economic Partnership Agreement (IA-CEPA)

Briefing paper for the Australia-Indonesia Business Partnership Group (IA-BPG), June 2016

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Executive Summary

- Since IA-CEPA negotiations began in 2010, the regional and national context for Australian and Indonesian trade policy has changed dramatically.
- A past focus on bilateral FTAs has since given way to new strategies to 'multilateralise' the Asia-Pacific trade architecture. The Trans-Pacific Partnership (TPP) and the Regional Comprehensive Economic Partnership (RCEP) are currently the two leading approaches.
- There is now a wider range of institutional vehicles via which aspirations to deepen the Australia-Indonesia economic relationship can be realised
- Australia has also completed a much more extensive set of bilateral FTAs. These can provide a template for how to implement several of the 'WTO-Plus' issues on the IA-CEPA agenda.
- The IA-BPG should take this new context into account in setting its IA-CEPA priorities ahead of the next round of (relaunched) negotiations, scheduled for August 2016.

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1. The Asia-Pacific trade architecture in the 2010s: From bilateralism to multilateralism?

In recent years, the trade architecture of the Asia-Pacific has been rapidly transformed. For most of the late 20th century, governments in Asia had been ‘committed multilateralists’ – pursuing trade liberalisation either globally through the World Trade Organisation, or regionally through ASEAN and APEC. But at the turn of the 21st century, this pattern changed dramatically. Governments instead began aggressively pursuing bilateral FTAs with key trade partners, as part of an effort to push liberalisation ahead further and faster than was proving possible in large multilateral bodies. Between 2001 and 2015, the number of bilateral FTAs signed by regional government exploded from 14 to 107. This process dramatically restructured the trade system in the Asia-Pacific, from one based on regional multilateralism to one criss-crossed by numerous bilateral deals.

However, many trade policy analysts began to express concerns regarding the effects of trade bilateral in the Asia-Pacific. Chief amongst these was the so-called ‘*noodle bowl problem*’. Rather than have a single integrated set of trade rules, the region had become fragmented into over a hundred bilateral agreements. These also varied widely in their content and scope, with each including (and excluding) different sectors, imposing different liberalisation requirements, and implementing technical procedures in incommensurate ways. Economists have identified this fragmentation as a new type of trade barrier, with companies and governments struggling to manage the regulatory complexity imposed by the bilateral architecture.

As a result, efforts have been undertaken ‘multilateralise’ the region’s existing FTAs. These have proposed *regional* rather than bilateral approaches to liberalisation, designed to reimpose a degree of consistency in the regional trade system. Two so-called ‘mega-regional’ agreements were launched. The first is the US-led *Trans-Pacific Partnership* (TPP), which involves twelve developed and developing countries¹ members on the Pacific Rim. The second is the ASEAN-centred *Regional Comprehensive Economic Partnership* (RCEP), which aims to integrate the existing FTAs between the ASEAN bloc and its Plus Six partners². TPP negotiations were completed in October 2015, and the agreement is currently mid-way through a two-year ratification process. RCEP negotiations began in 2013, and the parties have declared an intention to complete the agreement by end 2016.

Importantly, the TPP and RCEP embody competing visions for how the regional trade system should evolve. The TPP is described by its members as a “21st century trade agreement”, which ambitiously pushes liberalisation into new policy areas such as intellectual property, services, investment, telecommunications and e-commerce. RCEP instead offers relatively lower ambition approach, focussed on integrating the existing ASEAN-Plus-Six FTAs rather than breaking new policy ground. They also have markedly different membership structures. The TPP is an open agreement to which new members make accede, and welcomes all countries from the Asia-Pacific region. RCEP uses a closed structure based on ASEAN’s existing FTA partners, and thus advances a more Asia-focussed concept of the region. China, Korea and Indonesia are not presently signatories to the TPP, though both the Korean government and Indonesian governments have publicly expressed interest in future accession while. The RCEP membership model, by its design, excludes the US from participation in negotiations.

¹ The TPP members include Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, the United States and Vietnam.

² The ASEAN Plus Six partners include Australia, China, India, Japan, Korea, and New Zealand. All currently have bilateral FTAs with the ASEAN bloc.

It remains unclear which of these two models will become the principal vehicle for multilateralising the regional trade system. The TPP has been controversially linked to Sino-US geopolitical rivalry; and ratification currently faces headwinds due to the US Presidential election. Its high ambition approach to liberalisation will also impose significant reform costs on several developing countries in the region, particularly Indonesia. For its part, RCEP negotiations are still ongoing, and it is unclear whether a promised late-2016 completion will materialise. Both agreements could potentially co-exist, but the success of one proposal may undermine regional governments' interest in progressing the other. Whatever the outcome, it is clear that the Asia-Pacific trade architecture is entering yet another transition phase, where bilateral FTAs will need to operate alongside and in conjunction with, larger multilateral agreements.

2. The changing regional and national context for bilateral IA-CEPA negotiations

Since IA-CEPA was initially conceived, the 'game has changed' for trade agreements in the Asia-Pacific. When formal negotiations commenced in 2010, bilateral FTAs were the principal vehicle through which regional governments were pursuing trade liberalisation. Governments were also relatively inexperienced in negotiating these agreements, as many talks had been opened but few successfully completed. In the years since, governments have developed a more experience in FTA negotiations; while new and more ambitious mega-regional FTAs have been proposed. As a result, the regional and national contexts for trade policymaking – for both Indonesia and Australia – are now markedly different.

Australia has accumulated a much greater body of experience in bilateral FTAs. In 2010, most of its agreements had been with relatively minor trade partners (with the exception of the US), and talks with key regional economies were still in nascent stages. Today, Australia's suite of bilateral FTAs is far better developed. Agreements with the three Northeast Asian economic powerhouses of Japan, Korea and China were completed; while progress with regional economic heavyweights such as India and Indonesia has moved from the proposal and negotiation phase. Australia is also party to both of the new mega-regional FTAs in Asia, making it an active participant in recent multilateralization efforts. These provide a body of knowledge and precedent, in both bilateral and multilateral agreement-making, that can inform Australia's future approach to FTA negotiations.

Table 1 Australia's free trade agreements, 2010 and 2016 compared

Agreement	Status as of June 2010	Status as of June 2016
Australia-Singapore	In-force (2003)	
Australia-Thailand	In-force (2004)	
Australia-US	In-force (2005)	
Australia-Chile	In-force (2008)	
ASEAN-Aust-NZ (AANZFTA)	In-force (2009)	
Australia-China	Under negotiation (2005)	In-force (2015)
Australia-Malaysia	Under negotiation (2005)	In-force (2013)
Australia-Japan	Under negotiation (2007)	In-force (2015)
Australia- Gulf Cooperation Council	Under negotiation (2007)	Suspended
Australia-Korea	Under negotiation (2009)	In-force (2014)
Trans-Pacific Partnership (TPP)	Under negotiation (2010)	Signed, awaiting ratification (2015)
Australia-Indonesia	Proposed (2007)	Under negotiation (2010)
Australia-India	Proposed (2008)	Under negotiation (2011)

Regional Comprehensive Economic Partnership (RCEP)	NA	Under negotiation (2013)
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For its part, Indonesia has been less focussed on bilaterals. Most of its FTAs have been negotiated through the ASEAN bloc, reflecting a hesitance about bilateral agreements amongst policymakers and its longstanding commitment to economic integration through ASEAN processes. It has completed only two bilateral agreements (with Japan and Pakistan). While negotiations are currently underway with five countries, the Indonesia government has comparatively less experience negotiating bilateral deals on its own. It is also an RCEP – but not TPP – party, which was a function of Indonesia’s reluctance to (initially) sign onto to the far more ambitious TPP liberalisation agenda. Some Indonesian officials have suggested the country may seek TPP accession once the treaty is ratified, including President Jokowi during his visit to the US in 2015. But as TPP members have yet to design a formal accession mechanism, it is unlikely this process could begin until 2018 at the earliest.

Table 2 Indonesia’s free trade agreements, 2010 and 2016 compared

Agreement	Status as of June 2010	Status as of June 2016
ASEAN FTA	In-force (1993)	
ASEAN-China	In-force (2005)	
ASEAN-Korea	In-force (2007)	
Indonesia-Japan	In-force (2008)	
ASEAN-Japan	In-force (2008)	
ASEAN-Aust-NZ	In-force (2009)	
Indonesia-Pakistan	Under negotiation (2005)	In-force (2013)
Organisation of the Islamic Conference	Proposed (2004)	Signed, awaiting ratification (2014)
Indonesia-India	Proposed (2005)	Under negotiation (2011)
Indonesia- European Free Trade Association	Proposed (2005)	Under negotiation (2011)
Indonesia-Australia	Proposed (2007)	Under negotiation (2010)
Indonesia-Chile	Proposed (2008)	Under negotiation (2014)
Indonesia-EU	NA	Proposed (2009)
Indonesia-Korea	NA	Under negotiation (2012)
Regional Comprehensive Economic Partnership (RCEP)	NA	Under negotiation (2013)

These developments mean both sides’ approach to IA-CEPA negotiations should now be reappraised. In August 2016, the fourth round of IA-CEPA talks will be held in Australia; only the second since the process was ‘restarted’ by Ministers Lembong and Ciobo in March. However, the most recent Indonesia-Australia Business Partnership Group (IA-BPG) position paper on the agreement was produced in October 2012³. It is recommended that IA-BPG review and revise its principles, goals and recommendations for the IA-CEPA in light of these recent developments.

³ Indonesia-Australian Business Partnership Group (2012). *Position Paper on Considerations Towards the Indonesia-Australia Comprehensive Economic Partnership Agreement*, 31 October. <https://dfat.gov.au/trade/agreements/iacepa/Documents/ia-bpg-position-paper.pdf>

Two areas warrant particular attention: (1) the emergence of new vehicles for bilateral economic cooperation; and (2) the potential use of recent FTAs as a template for WTO-Plus elements in the IA-CEPA text.

3. New multilateral vehicles for economic cooperation in the Australia-Indonesia relationship?

When IA-CEPA was initially developed – first proposed in 2007, before proceeding to formal negotiation in 2010 – the number of trade policy options open to regional governments were more restricted than it is today. The Asia-Pacific shift to bilaterals was in full swing, with Indonesia taking its first steps towards independent FTA negotiation and Australia moving to open talks with all its major trade partners in the region. Few alternative mechanisms for trade liberalisation were available. Progress in the economic reform agendas of APEC and ASEAN had slowed to a crawl, while the WTO's Doha Round became bogged down in disputes between developing and developed country members. Multilateralisation efforts had not yet begun, and there was nothing comparable to the mega-regional TPP and RCEP processes.

IA-CEPA was one of the few institutional vehicles for Australia-Indonesia economic policy cooperation available at the time. As a result, almost all of the reform aspirations from stakeholders on both sides were had to be placed on IA-CEPA agenda. This is reflected in the 'consolidated recommendations' proposed by the IA-BPG in late 2012 (pp. 12-14). Some fifty-three recommendations were made, across an extremely diverse set of policy areas. Reflecting IA-CEPA's status as an *economic partnership* (rather than *free trade*) agreement, many were only indirectly related to trade policy itself. The movement of natural persons, service sector regulations, educational links, investment rules, and information exchange all fall into category of 'trade related' reforms.

However, since 2010 a much wider range of vehicles for promoting economic cooperation between Australia and Indonesia have emerged. Where reform aspirations previously had to be pursued bilaterally through IA-CEPA, a range of new multilateral options are now also available. Some of the most prominent include:

- **Ongoing RCEP negotiations.** Both governments are parties to RCEP negotiations, which covers many of the same trade and trade-related policy reforms included on the IA-CEPA agenda.
- **Consultation/review mechanisms built into AANZFTA (2009).** This agreement established institutional mechanisms to advance ongoing policy consultations over a range of issues relevant to IA-CEPA. These include technical barriers to trade, sanitary and phytosanitary measures, services, investment and customs procedures.
- **Indonesian accession to the TPP.** Once the TPP is ratified and members have implemented an accession mechanism, Indonesia may seek membership of the group. The TPP text already addresses many issues on the IA-CEPA agenda (especially surrounding foreign investment, transparency and value-chains). Australia could play an important role in supporting Indonesian accession to the TPP when this option becomes available; as well as assisting with the preparatory work required in the interim.

In some policy areas, these new multilateral vehicles might provide a superior approach than bilateralism through IA-CEPA. An instructive example are policies which impact on the operation of global value chains, such as rules-of-origin, customs procedures, service provision and local content definitions. These have been identified as a key priority in IA-CEPA (particularly in the agricultural sector); but are also addressed in RCEP and the TPP. Given the inherently multi-national character of these global value chains, multilateral harmonisation through the TPP and/or RCEP would be much more impactful than a bilateral Australia-Indonesia approach. It may therefore make sense to pursue this goal through one of these new multilateral institutions instead.

Of course, there are many issues in the Australia-Indonesia economic relationships which are definitively bilateral in nature. Movement of natural persons is one, especially in relation to vocational qualifications, skills recognition and visa/work permits. These should remain squarely on the IA-CEPA agenda. Others might be functionally divided across different agreements. For example, in the context of investment policy, provisions for investment protection might best be located in RCEP, while rules for the establishment of educational institutions are more suited to IA-CEPA. A case-by-case approach, which deliberately focusses efforts to the *agreement most suited to the particular issue in question*, is the most appropriate way forward.

Given that the range of institutional vehicles has now greatly expanded, it would be beneficial to review the 2012 IA-BPG priorities to determine which agreement provides the most appropriate institutional home for each issue. It is likely that some of these goals may be relocated from the IA-CEPA agenda to either RCEP negotiations, the AANZFTA consultations mechanism, and/or the TPP.

4. New templates for policy reform in regional trade agreements?

One of the principal motives for negotiating bilateral FTAs is to seek concessions in so-called ‘WTO Plus’ policy areas. While the WTO provides a well-developed set of disciplines for core trade policy areas (such as tariffs, subsidies and quantitative restrictions), there are a number of trade-related policy areas in which its rules are comparatively under-developed. These include investment regulations, trade in services, intellectual property, finances, labour, environment, agriculture and movement of natural persons. Many governments use bilateral FTAs to negotiate concessions in these areas with their key trade partners. IA-CEPA is no exception. All of the aforementioned issues are currently on the negotiating agenda, and the majority of the fifty-three recommendations made by the IA-BPG in 2012 fall under the definition of a WTO-Plus provision. Recent aspirations to ensure IA-CEPA embodies the standards of a “21st century” agreement mean these chapters will be critical elements on the negotiating agenda.

One challenge for this type of liberalisation lies in devising appropriate, balanced and effective legal texts. By their very nature, WTO-Plus issues are unable to build upon the WTO’s legal instruments as a template for devising agreements. While some attempts to produce standardised legal text have been made – such as the investment chapters in the US government’s *Model Bilateral Investment Treaty*⁴ – these often do not meet the needs of specific needs of FTA parties. As a result, each bilateral negotiation is forced to devise new legal texts from scratch, posing questions about how agreed reforms should be designed, implemented and enforced.

⁴ See State Department (US) (2012). *US Model Bilateral Investment Treaty*, <http://www.state.gov/documents/organization/188371.pdf>

These texts often vary widely from FTA to FTA, contributing to the regulatory inconsistencies in the regional trade architecture. Managing these differences poses unnecessary transaction costs for businesses, and undermines the value of an FTA as a trade promotion instrument.

Fortunately, since IA-CEPA was first launched, the suite of completed FTAs available to negotiators has dramatically expanded. Australia now has eight in-force bilateral FTAs and Indonesia two, many of which have been in operation for between five- and ten-years. These provides a set of developed legal texts, which have now been ‘trialled and tested’ through several years of operation, that can help inform the drafting process. Additionally, many of the WTO Plus issues that are presently on the IA-CEPA agenda have been implemented – in some cases for the first time – in the recently signed TPP treaty. Chapters on transparency, e-commerce, labour standards and financial services are all pertinent. Notwithstanding Indonesia’s formal position vis-à-vis TPP membership, these chapters may function as a template upon which IA-CEPA negotiators can begin when designing its WTO-Plus provisions. In the event of a future Indonesian accession to the TPP, the use of similar legal texts in IA-CEPA would help build initial experience and familiarity with the rules and procedures of the larger trade agreement.

Table 3 below summarises the coverage of WTO-Plus issues in other comparable FTAs signed since 2010. It reveals that there is no single agreement would be appropriate as a template for IA-CEPA on its own. However, an approach of ‘strategic selectivity’ – which borrows from and builds upon relevant provisions in other FTAs – offers an attractive approach:

- For widely covered issues of regional impact – such as e-commerce, financial services and intellectual property – drawing on multilateral agreements (such as AANZFTA and TPP) will help ensure IA-CEPA is consistent with the emerging regulatory frameworks in the Asia-Pacific
- In areas more specific to the Australia-Indonesia relationship, selective borrowing can instead be used to good effect. For example, JAEPa includes an energy and minerals clause; ChAFTA addresses education; while MAFTA provides a template for the mutual recognition of qualifications.
- Given Indonesia’s economic similarities with China and Malaysia, the ChAFTA and MAFTA agreements will provide the best template for implementing some provisions in a developing country-suitable manner.

Table 3: Coverage of WTO-Plus issues on IA-CEPA agenda in other comparable FTAs

Issue	TPP	AANZFTA	JAEPa	KAFTA	ChAFTA	MAFTA
e-commerce	X	X		X	X	X
Competition policy	X	X		X		X
Government procurement	X		X	X		
Intellectual Property	X	X		X	X	X
Environment	X			X		S
Labour	X			X		S
Transparency	X			X	X	X
Movement of natural persons		X	X	X	X	X
Financial services	X	X	X	X	S	
Recognition of qualifications			X		S	X
Energy and minerals cooperation			X			

Telecommunications	X	X		X S		X
Investor-State Dispute Settlement	X	X		X S	X	
Education					S	

Note: **X** indicates formal inclusion in the legal text of the FTA via a dedicated clause. **S** indicates issue is addressed through an exchange of side letters.

5. Summary of recommendations

1. IA-BPG should review its 2012 ‘consolidated recommendations’ in light of the emergence of new multilateral vehicles for Australia-Indonesia economic cooperation.
 - a. Attention should be paid as to which issues are to remain IA-CEPA priorities, and which might be best addressed via alternate mechanisms.
 - b. RCEP, the AANZFTA consultation mechanisms, and the TPP all provide new institutional vehicles through which certain aspirations may be better advanced.
2. IA-BPG should review its approach toward WTO-Plus areas in light of Australia’s more recent FTAs.
 - a. These agreements provide templates on which IA-CEPA negotiations can build and innovate.
 - b. AANZFTA and the TPP provide instructive models for issues of regional impact; whereas ChAFTA and MAFTA may be more suited to matters with specific developing-country concerns.

6. About the author

Dr Jeffrey D. Wilson is a Research Fellow with the Perth USAsia Centre, where he specialises in Asia-Pacific trade policy. He has consulted widely for governments in Australia on trade, energy and security policy issues; and is a sought-after expert commentator on Asian affairs in local and international media. He was the inaugural winner of the Australian Institute of International Affairs’ *Boyer Prize* (2012) for his work on China-Australia mining investment. He is currently the Chief Investigator (with Mark Beeson, UWA) on an Australian Research Council Discovery Project on the politics of Australia-China economic relations. He is also a faculty member of the Asia Research Centre at Murdoch University, where he is a Senior Lecturer in International Political Economy.