

HD Japan and South Korea – Australia's new Free Trade Agreements

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Introduction

JAEPAAOn 7 April 2014, Australian Prime Minister Tony Abbott and Japanese Prime Minister Shinzo Abe announced the new Japan-Australia Economic Partnership Agreement (). The Australian Department of Foreign Affairs and Trade describes it as "the most liberalising bilateral trade agreement that Japan has ever concluded".

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KAFTAOn 8 April 2014, Hon Tony Abbott and President of South Korea Ms **Park** Geun-hye attended the signing of the new Korea-Australia Free Trade Agreement (). The formal signing of KAFTA followed the previous announcement of that agreement in December 2013.

We intend to provide a more detailed briefing note and comparison between the two free trade agreements once the text of the JAEPAA is released later this year. However, this initial briefing note provides some context to both free trade agreements and summarises their salient features.

The context to Australia's free trade agreements

The Australia Commonwealth Government currently has a policy of negotiating free trade agreements (FTAs) with Australia's most significant trading partners. This policy was partly adopted due to delays in the Doha Round of multilateral trade negotiations within the World Trade Organisation.

Japan and South Korea are Australia's second and third largest export markets behind **China**. Collectively these three east Asian nations consume half of Australia's entire export trade.

Japan is particularly important to Australia. Japan is Australia's third largest source of imports, ranked behind **China** and the United States. Japan is also Australia's third largest source of foreign direct investment, currently aggregating to some AUD 126.4 billion.

Australia is also important to Japan. Australia is Japan's third largest source of imports, principally Australian coal, liquefied natural gas (LNG), iron ore, copper ore, and beef. Australia is also Japan's tenth largest export destination, principally motor vehicles, goods vehicles and refined petroleum.

Two-way trade with Japan aggregated to AUD 71.1 billion in 2012. Two way trade with South Korea aggregated to AUD 31.9 billion. On a two-way trade basis, Japan and South Korea are ranked as Australia's second and fourth most important trading partners, as shown in the following diagram.

Australia's main trading partners by percentage of two-way trade

Australia currently has seven FTAs in force. The Japanese and Korean FTAs will now take this number to nine. Australia is continuing to negotiate bilateral FTAs with **China**, India and Indonesia. Australia is also currently negotiating four important plurilateral trade agreements.

The Japan - Australia Economic Partnership Agreement (JAEPAA)

Australia and Japan enjoy one of the most significant economic partnerships in the east Asian region. The Japanese-Australian relationship has developed on the basis of strong complementary interests and

co-operation in a wide range of areas. JAEPA now signifies a deepening and broadening of that historic trading relationship

As at April 2014, Australia and Japan have reached substantive agreement on the text of the JAEPA, but have not yet formally finalised the JAEPA text. Both nations expect to formally sign the concluded text of the JAEPA in the coming months.

As the text of the JAEPA is not yet publicly available, the following information is a summary of what is currently known.

Japanese investment into Australia

The threshold for foreign investment review will be increased, thereby encouraging further Japanese investment into Australia. In practical effect, less Japanese investments into Australia by private sector corporations will be subject to foreign investment review.

FIRBSpecifically, the screening threshold will be increased, being the threshold at which private Japanese investment into Australia's non-sensitive sectors will be considered by the Foreign Investment Review **Board** (). The concessions will be in line with the preferential treatment already accorded by Australia to the United States and New Zealand, namely an increase in the screening threshold from AUD 248 million to AUD 1,078 million.

The threshold for FIRB scrutiny will remain at zero for investments by state-owned entities (such as the Government Pension Investment Fund of Japan) and will be set at \$15 million for the **purchase** of established agricultural land and \$53 million for agribusinesses. This means that all investment by state-owned entities will be subject to scrutiny by FIRB, with particular protection in place for agriculture in Australia.

While JAEPA may provide enhanced protections and certainty for bilateral investments, we understand JAEPA will not confer rights to private parties by way of investor-state dispute resolution provisions.

Australian agricultural exports to Japan

Japan has some of the highest agricultural tariffs in the world and a powerful domestic agricultural lobby. Australia has been a longstanding proponent of Japanese agricultural tariff reductions.

The reductions in Japanese agricultural tariffs contemplated by JAEPA represent a clear win for Australia, particularly as Japan is Australia's second largest agricultural market. Moreover, Australia agricultural products will now receive more favourable Japanese tariff treatment than the products of other agricultural nations (at least until those other nations seek the same concessions from Japan under their own FTAs).

The following Australian agricultural industries will be affected in the following ways:

Beef: The biggest export winners are Australia's beef exporters. Japanese tariffs applied to Australian beef will be progressively reduced. Japan's tariff on frozen beef will be reduced from 38.5% to 19.5% over 18 years. For fresh beef, the tariff will reduce to 23.5% over 15 years. While these time frames are lengthy, they reflect a major Japanese concession that could boost Australian exports by some AUD 5.4 billion.

Dairy: The duties currently imposed by Japan on Australian dairy products will be reduced. Australia will have a quota of 20,000 tonnes of cheese to export duty-free and preferentially.

Sugar: Australia exported AUD 226 million of sugar to Japan in 2013, accounting for a third of Japan's sugar imports. Australian sugar exporters will benefit from tariff elimination and reduced levies for international standard raw sugar.

Horticulture: Tariffs will be eliminated on fresh produce such as fruit, vegetables, nuts and juice as well as canned products such as tomatoes, peaches and pears.

Wine and seafood: Bottled, sparkling and bulk wine will gain from tariff elimination over seven years. Tariffs on many key seafood exports will be eliminated.

Australian energy and mineral exports to Japan

Energy and mineral products account for nearly 90% of the value of Japan's merchandise imports from Australia. However, many of Australia's major resource exports, such as coal, iron ore and LNG already enter Japan duty-free.

Under JAEPA, all remaining tariffs on energy and mineral products will be eliminated within 10 years and most on entry into force of JAEPA. In practice, this means there will be immediate tariff elimination for coking coal, petroleum oils, aluminium hydroxide and titanium dioxide.

Japanese manufactured exports to Australia

Australia will immediately remove its 5% tariff on certain imported Japanese cars, meaning that those Japanese cars should become cheaper for Australian consumers. As yet, little detail is available as to what other concessions may have been given, if any. However, the Australian Government has indicated that the price of an AUD 30,000 Japanese car in Australia should reduce by around AUD 1,500.

Australian services exports to Japan

JAEPA guarantees Australian services suppliers access to the significant and well developed Japanese market in key areas of **commercial** interest including financial, education, telecommunications and legal services.

The JAEPA provides Australia with outcomes equal to or better than, the best commitments Japan has made in any of its other trade agreements.

Other features of JAEPA

The remaining features of JAEPA have not yet been publicly identified by the Australian Government. However, the content of JAEPA is likely to closely follow the content of the Korea - Australia Free Trade Agreement (KAFTA) discussed below.

The Korea - Australia Free Trade Agreement (KAFTA)

South Korea is Asia's fourth-largest economy with a population of some 50 million people. Australia's trading profile with South Korea is very similar to that of Japan. Australia and South Korea have one of the strongest and most complementary trading relationships in the Asia-Pacific.

The public text of the KAFTA was released in February 2014 and adopts an approach similar to that of other FTAs that Australia has recently entered into. We expect that the text of JAEPA and KAFTA should be very similar.

The Australian Department of Foreign Affairs and Trade has estimated that KAFTA will deliver over AUD 5 billion in additional income to Australia between 2015 and 2030.

South Korean investment into Australia

As with JAEPA, Australia has raised the screening threshold for Korean investments in non-sensitive sectors of the Australian economy from AUD 248 million to AUD 1,078 million. In practice, less Korean investments into Australia will therefore be subject to foreign investment review.

As with JAEPA, Australia retains the ability to screen investments in sensitive sectors, including media, telecommunications, defence, and agriculture at lower levels

Unlike JAEPA, the KAFTA give private investors the ability to directly enforce investment obligations through an investor-State dispute settlement (ISDS) mechanism. An ISDS claim can only be made on the basis of a breach of an investment obligation, being a breach of a treaty obligation under the Investment Chapter of KAFTA or a breach of an investment agreement between the investor and the government of the other Party.

Various exceptions to the ISDS mechanism apply. For example, ISDS does not apply to decisions made concerning investments which are subject to review under Australia's foreign investment policy. An ISDS claim cannot be based on a breach of commitments in other parts of KAFTA including the intellectual **property** and environment chapters.

Australian agricultural exports to South Korea

South Korea is another market that has historically applied high agricultural tariffs. In a free trade agreement that commenced in 2012, the United States has already achieved significant successes in reducing those tariffs for its own agricultural exports into South Korea. Australia was therefore seeking to follow in the footsteps of the United States.

Under KAFTA, Korea has agreed to eliminate tariffs immediately on entry into force for raw sugar, wheat, wine, and some horticulture. Tariffs of up to 550 per cent on most other agricultural products will be eliminated within short time frames.

Beef: Beef is Australia's biggest agricultural export to Korea; Australia is the largest supplier of beef to Korea; and Korea is Australia's third-biggest export market for Australian beef. Korea has agreed to eliminate its 40% tariff on beef progressively over 15 years. Under the United States FTA with Korea, US beef exports have been benefiting from beef tariff cuts, so the FTA will ensure Australian beef producers are given the same favourable consideration.

Dairy: High tariffs of 36% on cheese and 89% on butter will be eliminated over a period of up to 20 years. Australian dairy exporters will also benefit from growing duty free quotas for cheese, butter and infant formula. The cheese quota volume represents around two thirds of Australia's cheese exports to Korea in 2013.

Sugar: Korea will abolish its 3% tariff on raw sugar on entry into force.

Horticulture: Many products will enter Korea duty free on entry into force, removing tariffs of between 8 and 24%. Tariffs on other priorities such as macadamia nuts, fruit juices, mangoes, asparagus and lentils, ranging from 27 to 54%, will be phased out over 3 to 10 years.

Australian energy and mineral exports to South Korea

While many Australian resources and energy products already enter Korea duty free, Korea applies tariffs of up to 8% on a range of resources.

Upon implementation of KAFTA, some 88% of Australia's resources and energy exports will enter Korea duty free, with Korea phasing out all remaining tariffs within 10 years. Tariffs on priority products for Australia, including LNG (3%) and titanium dioxide (6.5%) will be eliminated.

South Korean manufactured exports to Australia

Following implementation of KAFTA, some 86% of South Korea's manufacturing exports will enter Australia duty free. Australia will be required to phase out remaining tariffs for the most import-sensitive manufacturing products progressively within eight years.

Australian services exports to South Korea

KAFTA will provide Australian services exporters with the best treatment Korea has agreed with any trading partner, equivalent to FTAs that Korea has concluded with the United States and Europe.

Key outcomes relate to legal services, accountancy services, telecommunications services and financial services providers. Education, engineering and other professional services will also benefit from Korea's commitments to guarantee existing market access for Australian providers and work towards improving mutual recognition of qualifications.

Other features of KAFTA

The KAFTA includes chapters on intellectual **property**, electronic commerce and competition policy. These chapters are too lengthy to summarise in a short briefing note, but have the objectives of:

providing appropriate protection and enforcement of intellectual **property** rights;

including disciplines on anti-competitive practices; and

promoting a secure and liberalised environment for the growth of electronic commerce.

KAFTA also contains a number of other important features:

KAFTA opens new markets in Korea for Australian law firms, accountants and telecommunications providers. It guarantees access in a wide range of other sectors including education and financial services.

Under KAFTA, Korea will guarantee access for Australian traders and investors (and their families) to stay in Korea for up to two years.

KAFTA contains an Audio-visual Co-production Annex which will deliver new opportunities for the Australian film and television industry.

KAFTA establishes a Professional Services Working **Group** to facilitate cooperation and mutual recognition between professional bodies in both countries.

KAFTA guarantees Australian suppliers access to the Korean government procurement market and contains commitments that will ensure transparency and facilitate participation in procurement processes.

The content of this article is intended to provide a general guide to the subject matter. Specialist advice should be sought about your specific circumstances.

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