

DOMESTIC TRANSPARENCY

AND THE

FUNCTIONING OF THE GATT SYSTEM

A Report prepared for the Trade
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AUTHORS' NOTE

In accordance with a commission from the Trade Policy Research Centre, this report examines the issues involved in implementing the "domestic transparency procedures" proposed in the Long Report and now under discussion in the GATT.

It is clear from our examination of the proposal that what is at issue for each Contracting Party is nothing less than the capacity of GATT negotiations to deliver market access for its internationally competitive producers.

Having said that, we wish to make it clear that the purpose of domestic procedures is to strengthen the functioning of the GATT system. Our evaluation of the proposal is strongly supportive of that system, and is in no way intended to diminish the role of international co-operation in trade policy. Throughout the early life of GATT, particularly in the fifties and sixties when tariffs were the principal barrier, trade negotiations achieved substantial reductions in protection - with nationally rewarding outcomes for participants. But the development of less transparent forms of protection since then, to avoid GATT rules, has placed the system under great pressure. The purpose of domestic transparency procedures is to re-establish the GATT's role, in a way which recognises the interactive nature of the domestic and international dimensions of trade policy.

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CHAPTER 1. BACKGROUND

Since the Tokyo Round there has been a growing recognition that the GATT system is in trouble, and that something fundamental needs to be done to strengthen it. This was reflected in the November 1982 GATT Ministerial 'crisis meeting' (only three years after the conclusion of the Tokyo Round) and in the lead-up to the Uruguay Round, where it culminated in a special negotiating group devoted to the 'functioning of the GATT system (FOGS)'.

The agenda of that group was influenced by two reports by international study groups, one initiated by the current Director-General of the GATT and headed by Fritz Leutwiler, (former Chairman of the Bank for International Settlements) the other by the previous Director-General of the GATT, Olivier Long.¹

The Leutwiler and Long Reports

Both reports attribute particular importance to the domestic origins of the growing distortions in international trade. They identified a lack of openness and information in national policy-making as contributing to the influence of protection seekers, at the expense of the general community. They recommended that there be greater 'transparency' at the domestic level, to help counteract the protectionist bias in the policy environment and enable governments to approach GATT negotiations and commitments with a better understanding of what is in the interests of their own economies.

'This report is built on the premise that trade policy is the international dimension of national policies adopted primarily for domestic reasons. Trade ministers, meeting in Punta del Este in Uruguay, secured agreement in September 1986 on what should be the general objectives for the Uruguay

round negotiations. An additional ingredient, to make it possible for governments to act against the protection they have themselves introduced, is greater public awareness within protecting countries of the domestic costs of protection and subsidies. Governments have demonstrated that they are not likely to remove such measures just out of concern for their adverse effect on foreign producers. They are much more likely to do so out of concern for the costs they impose on domestic constituents.²

Both reports argued that the achievement of a more informed domestic policy-making process would be facilitated by domestic transparency arrangements in GATT member countries. The Long Report set out basic characteristics that a body responsible for this function should have and recommended that work towards an agreement on domestic procedures be carried forward in the FOGS group. The IAC in Australia was identified as a model for such a transparency institution by both reports.

Developments in the FOGS group

An important focus of the FOGS group is on improving the transparency of trade-related policies (reducing their 'fogginess'). Government measures affecting trade have become increasingly difficult to identify and evaluate. The logic behind this focus in the FOGS group is that national barriers need to be made visible before something can be done about them.

Two different approaches to overcoming the information problem have been considered: multilateral surveillance and domestic transparency.

Multilateral surveillance

The FOGS negotiating group spent the first two years of the negotiations developing a 'multilateral surveillance' mechanism

in the GATT, along similar lines to that existing in the OECD for general economic policies. The objective was 'to contribute to improved adherence by all contracting parties to GATT rules, disciplines and commitments...by achieving greater transparency in, and understanding of, the trade policies and practices of contracting parties.'³

At the Montreal mid-term review, Trade Ministers were able to agree on the establishment of a 'Trade Policy Review Mechanism', the function of which is 'to examine the impact of a contracting party's trade policies on the multilateral trading system.'⁴ Periodic reviews are to be conducted in the GATT Council (which all members attend). They are to be based on two reports - one submitted by countries being reviewed and one by the GATT Secretariat on its own responsibility - both of which will be published after the review. The reports will describe a country's trade policies and practices, according to an 'agreed format to be decided by the Council' and are to include 'all components of policy affecting trade.'

Domestic transparency

A proposal on 'domestic transparency' procedures was made by the New Zealand government in late 1987. Drawing on the recommendations and analysis in the Leutwiler and Long Reports, New Zealand proposed that the FOGS group develop criteria to assist Contracting Parties establish domestic surveillance bodies - to facilitate greater transparency and a better understanding within member countries of the economy-wide effects of their own policies.

New Zealand noted two limitations of multilateral surveillance in influencing policy outcomes: (a) it is an examination after the fact - when policies are already in place; and (b) it is focussed on the external effects of policies, rather than their effects within the country imposing them. Domestic transparency differs

in both respects: it is intended to have an impact on policy as it is being made, and it is an internal assessment of the domestic economic effects of national barriers.

This proposal was discussed within the FOGS group, where a number of countries supported its inclusion on the agenda. The idea was also endorsed at international meetings of trade ministers at Bali (January 1988), of Commonwealth representatives in London (July 1988) and in the plenary of UNCTAD VII, which noted:

'Governments should consider as part of the fight against protectionism, as appropriate, the establishment of transparent mechanisms at the national level to evaluate protectionist measures sought by firms/sectors, and the implications of such measures for the domestic economy as a whole and their effects on the export interests of developing countries'.⁵

In his summing up at the Bali Ministerial Conference, the Chairman observed:

'The importance of underpinning a greater surveillance role in the GATT by greater transparency at the national level - for example, by independent 'domestic transparency agencies' - was stressed. The need to increase public understanding of the economy-wide effects of protection was identified as an important requirement for promoting freer trade'.⁶

Despite widespread recognition of the need for domestic transparency procedures, however, the FOGS group decided in the lead-up to the Montreal meeting to put the New Zealand proposal on the 'back-burner'- in order to concentrate its efforts on getting agreement about the Trade Policy Review Mechanism (multilateral surveillance).

Several governments have indicated their wish to advance the proposal for domestic transparency procedures in the FOGS group as a matter of urgency when the Mid-Term Review has been completed. The Trade Policy Research Centre in London has asked us to examine the proposal in the light of Australian experience and to evaluate the Australian Industries Assistance Commission as a possible institutional model for domestic transparency procedures - in order to provide a wider information base for discussion of the Long Report's proposals.

The purpose of the present report is to discharge that commission. Part A sets out the logical basis for the conclusion that the GATT system needs to be underpinned by domestic transparency procedures; and then examines Australia's experience as a participant in the Tokyo Round - to provide an historical test of that logic. Part B contains an account of the IAC's role in a domestic policy context; and then examines institutions in other countries against the criteria in the Long Report.

PART A: WHY DOMESTIC TRANSPARENCY PROCEDURES?

CHAPTER 2. TRADE LIBERALISATION AS A DOMESTIC ISSUE

The established approach to trade negotiations.

The GATT is both a 'rule book' for trade policy conduct and a forum for negotiations to liberalise international trade. It is an international agreement imposing external obligations and commitments on member countries ('contracting parties').

GATT rules are concerned with specifying in what circumstances, and in what forms, protectionist action is permissible. The trade liberalising commitments that contracting parties make are the outcome of multilateral negotiations. These negotiations have traditionally been based on the concept of 'reciprocity', in which trade representatives of member countries exchange 'concessions' in an attempt to achieve a 'balance of obligations'. The extent and nature of one country's liberalisation is determined by what other countries are prepared to do.

In this approach, the emphasis is on:

- . 'international' commitment as the basis for governments reducing barriers in the context of multilateral trade negotiations;
- . trade liberalisation, through international diplomacy and bargaining, as part of external policy; and
- . internationally negotiated rules providing an external discipline on the trade conduct of member countries.

With the emphasis on meeting 'external' commitments, most countries have approached negotiations with a relatively clear idea of what they have wanted from their trading partners, in

terms of market access, but have given less attention to what domestic barriers they should reduce to promote national efficiency. In fact, most have worked out their concessions only in response to the requests of their trading partners.

In this situation, trade diplomats have inevitably been forced into a defensive posture, trying to 'give away' no more than the minimum necessary to achieve gains in foreign markets. Thus in the international bargaining environment, concessions have come to be seen as involving a cost to the domestic economy (instead of just to the particular industries whose protection is reduced). The word 'concession' conveys this.

While successive GATT rounds have resulted in substantial reductions in tariff levels in industrial countries, it was inevitable that the concession-minimisation mentality would lead to perverse results for domestic efficiency in many participating countries. While tariffs were being bargained away in multilateral forums, governments were finding alternative ways of protecting their least competitive industries. These measures have either made use of the 'exceptions' within the GATT system for introducing protection (such as for emergency relief, or against 'unfair' practices); or exploited loopholes or ambiguities in the rules (such as 'domestic' production subsidies and regulations of various kinds); or simply occurred outside the GATT system altogether (voluntary export restraints being the most important example). A number of recent studies on non-tariff barriers have shown their incidence to have doubled through the 1970s and 1980s, affecting up to one-half of world trade.⁷

In coming to terms with the "new" (non-tariff) protection, negotiations of the traditional kind face very great difficulties:

- . unlike tariffs, the new forms of protection lack transparency;

- some have 'GATT cover';
- some are seen as being out of bounds to the GATT - involving sensitive questions of 'domestic policy';
- and some - in contrast to tariffs - are 'illegal' under the GATT and therefore, in GATT terms, not legitimate negotiating coin. (Developing countries may therefore ask: "Why should we have to reduce our legitimate protection as a quid pro quo for industrial countries reducing barriers which are illegal and should be eliminated anyway?").
- Most importantly, in providing protection in these forms governments have demonstrated that the external disciplines which GATT rules place on their conduct are not effective.

Domestic origins of trade barriers

We have attempted to explain what difficulties the GATT system is facing, but not why. The Long Report identified the domestic source of the difficulties:

"Why is it then that governments - collectively, through GATT, and individually at home - lack the will to arrest the drift into ever increasing protection? Clearly this drift is not something that they have deliberately sought to bring about. Why do governments act to assist industries to resist changes in the trading environment - in contradiction of their stated policy objectives?"

"The answer is that, in the domestic arena, short-term political imperatives ensure that public attention is focussed on the problems for those sections in domestic industries which stand to lose from adjusting to changes in

the trading environment, not on the benefits for domestic industries as a whole from doing so. The domestic debates on such issues are normally one-sided. Those who stand to lose from adjustment are usually well organised and vocal and their arguments, which focus on the quite visible costs to them of adjustment, are politically persuasive. Governments tend to succumb to those pressures as a matter of political survival. When confronted with the immediate and obvious difficulties facing ailing industries, they have little room to manoeuvre - because the politically realistic policy alternatives open to them are severely constrained." ⁸.

The Long Report identified two interlocking causes of this 'one-sidedness' in protection policy-making:

On the 'demand' side, there is the much greater incentive for losers from trade liberalisation (uncompetitive industries) to effectively organise and lobby government, than there is for the potential gainers. ⁹. This is a well-known phenomenon, resulting from the relative concentration of protection's benefits compared to its costs.

On the 'supply' side, the 'fragmented administrative arrangements' existing in most countries leads to reactive, short-term decision-making that tends to be captive to the demands of particular industry 'clients'. Each part of the administration is concerned with separate parts of the economy, none with the effects of particular policy proposals on the whole. ¹⁰.

The combination of these phenomena ensures that domestic policy-making environments have an in-built bias in favour of the needs of particular industries. The activity of industry pressure groups, as well as the expansion of the government sector, has facilitated the development of this parts-oriented

approach to policy. The Long Report concludes:

"The point has now been reached in which those engaged in the traditional concession-swapping process have been forced, by domestic constraints, to do so in ways which involve no visible domestic losers. This has meant that their concessions are confined to those trade barriers which have the least domestic protective significance. At the same time, their colleagues in domestic 'industry departments' are busy devising methods of public assistance which are no less effective than the traditional forms of protection, but which are less visible - domestically and internationally.

"The traditional bargaining approach, because it is usually undertaken against a background of domestic political pressures to safeguard particular interests, has tended to distract attention away from what is in the best interests of a country's over-all economy - which should be the foundation of the whole process. In these circumstances, it is hardly surprising that multilateral trade negotiations have been yielding only illusions of liberalisation. In fact, if trade deliberations continue to be carried out at that level (and at that distance from home capitals), perverse outcomes are only to be expected." ¹¹.

Domestic solutions

If external disciplines alone cannot secure or sustain a liberal world trading environment, it is important to underpin them with internal disciplines that will help do so. Any proposal to strengthen the GATT system must link the functioning of that system more directly to the national economic welfare of participants. The logic establishing the need for domestic

procedures to achieve that is as follows:

- . the prospect of national gains provides the rationale, and the justification, for participating in the GATT system;
- . in that system, trade liberalisation is pursued through multilateral trade negotiations (MTN) - in the expectation that reductions in national barriers which meet the objectives agreed between participants will enhance global efficiency and the economic welfare of participants;
- . but individual MTN participants may well make 'concessions' which are inimical to national and international economic welfare - by maintaining barriers protecting their least efficient industries and reducing those protecting more efficient domestic production;
- . if governments individually approach the negotiations in this way, they cannot collectively increase the opportunities for participating in world trade on the basis of what each does best;
- . there are no rules or procedures to help participating governments bring into account the effects on national economic welfare of reductions in national barriers negotiated in the MTN context;
- . the process of deciding which national barriers should be reduced to enhance domestic efficiency involves ~~sensitive domestic policy issues;~~
- . these can only be worked out in the domestic environment through domestic processes;

because worthwhile gains in external markets (for what each does best) depend on it, MTN participants individually have an incentive to encourage all others to invest in the effort required to approach negotiations with a good understanding of the domestic effects of reducing their own barriers.

With one important difference, what is at issue nationally when barriers are reduced to meet external bargaining commitments is the same as when they are reduced in a domestic policy context to enhance domestic efficiency. The one difference is that each participant in the international bargaining process can secure greater access to external markets for the things they produce best only if the other participants, when selecting their own barriers to reduce, are also seeking to enhance domestic efficiency.

That is the rationale for the domestic procedures proposed in the Long Report. Without such procedures, to enable MTN participants to bring into account the domestic issues and choices involved in negotiations, they may well leave in place a structure of national barriers for participants that is not consistent with domestic efficiency and a structure of global barriers that does not allow national participation in world trade on the basis of comparative advantage. In that event, internationally competitive producers everywhere will remain disadvantaged - in their domestic environment against less efficient domestic industries, and in the external markets they should command on the basis of comparative advantage. There is nothing in existing MTN negotiating modalities working against such outcomes.

A further compelling reason why domestic transparency procedures are needed to underpin MTN bargaining is that the important barriers are increasingly in non-tariff (often non-frontier) forms. These are less visible, nationally and internationally, and often take forms which have traditionally been viewed as part

of domestic policy. They are not likely to be brought into account in international negotiations unless national governments practising them choose to place them 'on the record'. Their reason for doing so must be to help them decide, after bringing all their barriers into account, which of the many alternative ways of meeting their external commitments would be nationally most rewarding. The ability of MTN bargaining to increase opportunities to engage in world trade on the basis of comparative advantage depends on the decision each MTN participant makes on that issue.

The Long Report proposal

A GATT initiative on domestic transparency procedures was proposed in the Long report to help individual contracting parties generate better information about the extent and domestic effects of their own barriers. It proposed that a domestic institution be assigned by each contracting party as the vehicle for improving domestic visibility of domestic protective measures and of their economy wide effects.

The Long proposal elaborated three criteria for such domestic transparency arrangements:

"(a) The institution responsible should be independent of domestic political pressures and should not be identified with any industry-specific branch of the domestic bureaucracy. The framework for its work must be economy-wide.

"(b) Arrangements should be structured in such a way that the institution has a broad mandate to enquire into all forms of public assistance to industries. Moreover, the information about the effects on the economy of public assistance to

industries should be communicated as a matter of course to policy makers, to members of the legislature and to the community at large.

"(c) Its activities should be purely advisory, with no executive or judicial role; and its concern should be solely to provide the information about the wider implications of industry and trade policy which legislatures and their constituents now find it so difficult to address, to understand and to resolve." ¹².

CHAPTER 3. THE AUSTRALIAN EXPERIENCE

Whether trade bargaining enhances international trading opportunities for internationally competitive producers depends on how participants individually reduce their trade barriers. Contracting Parties cannot collectively (through bargaining) increase the opportunities for participating in world trade on the basis of comparative advantage unless they are individually trying to secure the domestic gains, to national efficiency, when meeting external commitments to reduce barriers. This crucial and unforgiving link between the domestic and international dimensions of trade liberalisation is not captured in the procedures and rules which constitute the framework for the operation of the GATT system.

It is therefore important to explore whether participants do, as a matter of course, approach negotiations with a good understanding of the effects on their domestic economy of the barriers they are reducing to meet their MTN commitments. We will do so by examining Australia's experience in a multilateral negotiating context, in the Tokyo Round, and compare that with its performance when reducing them unilaterally - for domestic policy reasons. Although we will go beyond Australian experience to the extent that we feel confident in doing so, generally the performance of other MTN participants must be left to others better qualified by experience to undertake that task.

The Australian Experience.

The domestic implications of participating in MTN bargaining simply to meet international commitments are evident from Australia's experience in the Tokyo Round. Because external commitments were perceived as driving the approach to reducing barriers, the national efficiency criteria which apply as a matter of course when Australian barriers are changed in a

domestic policy context were felt to be inappropriate for external negotiations. As a result, Australia's negotiating position was worked out through processes which involved no rigorous consideration of the economy wide domestic effects, no opportunity for public evaluation of the domestic trade-offs involved in the negotiating choices under consideration and no strategy for dealing with domestic adjustment. The result was an approach to MTN which sought access to other markets while avoiding domestic adjustment.

Preparation for Barrier Reduction in the Tokyo Round.

In May 1972, the Government asked the Tariff Board - the independent statutory body from which Australian governments sought public advice before changing protection - for a confidential report on reducing barriers in the Tokyo Round. The reference noted that Australia's participation in the Round would "involve the granting by Australia of tariff concessions" and asked the Board to examine those areas of the Australian Tariff where "rates of duty at present imposed may be higher than are necessary to protect existing Australian production."¹³ The restrictive terms of reference, a short reporting deadline and the fact that the advice was sought in a non-public report meant that the advisory process contributed nothing to public understanding of what was at issue.

Six years later, in 1978, concern was still being expressed about the lack of information then available on the expected domestic effects of our MTN offer. The Confederation of Australian Industry wrote to the Prime Minister in the following terms:

"Australia's negotiating position has been developed within Government without having acquainted industry with the detailed options and their consequences: we are concerned that an agreement may be reached without regard to ...its effects on industry generally".¹⁴

And at about the same time, the Minister responsible for Australia's negotiating position responded to concern expressed about its domestic effects in the following way:

"It might be that the Government would have to take some steps, but that would be a matter for decision at the time. It would, I think, be very premature for a government in 1978 to be trying to plan or commit itself to a situation which ... won't occur until 1980".¹⁵

In this way the government itself contributed to uncertainty about the extent of domestic adjustment involved. Apprehension about the magnitude, direction and domestic consequences of Australia's Tokyo Round MTN offer was pervasive. The community's understanding of the effects, reflecting that uncertainty, itself decisively influenced the Australian Government to develop a package of concessions intended to produce no visible domestic losers.

Australia's preparation for those negotiations reflected the formal bargaining approach. Barrier reduction was approached as an external issue arising from GATT membership and institutionalised in the MTN processes. The effects on domestic efficiency were a residual outcome of MTN participation, rather than a central objective in deciding which barriers to reduce.

Domestic effects of Australia's Tokyo MTN participation.

During the 1970's, when the Tokyo Round was in progress, Australia's border protection was reduced overall by forty per cent. While the average level of frontier barriers declined, however, disparities in the levels of assistance between industries increased markedly (and it is these disparities which reduce domestic efficiency and national welfare when substantial industries continue to be highly protected).¹⁶ These two things occurred simultaneously as a result of reducing protection

to lightly protected industries (partly by using, as negotiating coin, protection they did not appear to be using) and increasing protection, in the form of import quotas, to industries that were already highly protected.

From an international bargaining viewpoint, this outcome was seen as fulfilling Australia's external commitment to reduce trade barriers. In reporting to Parliament on the outcome of Australia's participation in the Tokyo Round, the then Trade Minister confirmed that Australia's negotiating objectives in the Round were met:

"In a debate in September I informed the House that Australia had agreed in the bilateral negotiations to bind against increasing the tariff rates on about 120 tariff headings or parts of tariff headings covering agricultural and industrial products. With the exception of three items - namely tobacco, certain fancy cheese and an item relating to frozen poultry - the tariff rates are at or above current applied rates. This means that Australia has achieved a meaningful and advantageous settlement with the United States, EEC and Japan without reducing the current level of tariff protection on a single tariff item applicable to any manufacturing industry.....This was, I believe - I am sure industry agrees with me - a commendable result". ¹⁷.

In that view of the world, the purpose of engaging in international bargaining is to secure market access without giving away anything that would adversely affect protected home producers. MTN participation becomes a vehicle for consolidating, rather than reducing, domestic distortions.

Australia's least competitive producers were shielded from adjustment pressure. The outcome was negative for both domestic and global efficiency. The increasingly distorted structure of domestic barriers provided less opportunity for international

competition in Australian markets on the basis of comparative advantage, and Australia's own internationally competitive producers were increasingly disadvantaged in their production environment against less efficient domestic producers.

Liberalising in a domestic policy context.

The largest reductions in Australia's trade barriers have been made for domestic policy reasons and have involved a good domestic understanding of what was at stake domestically.

The largest reduction in tariffs was made in 1973. It did not follow a public inquiry, but was made after extensive public exposure by the Tariff Board of the domestic costs of maintaining the then existing levels of protection. There was general acceptance by domestic constituents that a reduction of barriers was needed. This was reflected in the public reaction of the peak union organisation:

"We have to have a concern for the totality of the workforce and the economic problems with which they are confronted. The interests of the whole require us to endorse what has been done".¹⁸

That response captured the domestic issues at stake in reducing national barriers. It is not possible to do so without adjustment. The choice in trade bargaining, as in domestic policy, is whether the inevitable adjustment burdens should fall on the more efficient or the less efficient domestic industries.

A substantial further liberalisation of Australian barriers, foreshadowed in May 1988, was also decided in an economy-wide context - and in pursuit of domestic efficiency. There is now fairly wide acceptance in Australia of the inevitability of reducing assistance to highly protected industries, to make the national economy more competitive. One of the industries most

likely to be affected said about the prospect of reduced protection:

"MTIA accepts the Government's view that Australian industry must become more internationally competitive".¹⁹.

It concluded that:

"...we must look to the development in Australia of an internationally competitive metal and engineering industry regardless of size."²⁰.

It seems to be more generally accepted, when the domestic choices are visible to domestic constituents, that the overall competitiveness of the economy should receive priority over the adjustment difficulties for particular parts.

Implications of Australia's experience.

Australia's participation in the Tokyo Round was an exercise in market access, not in domestic adjustment. In the MTN context, when external commitments were perceived as driving the approach to reducing barriers, we were unable to require our least competitive industries to adjust. Subsequently, in a domestic policy context, it was decided that the less competitive industries that had been quarantined from negotiated reductions should have their protection reduced in order to make the national economy more internationally competitive. In other words, we could address the domestic adjustment implications of reducing barriers to our less competitive industries when the domestic costs of maintaining them was the issue, but not when the context was trade bargaining.

So established was the view of trade liberalisation as part of external policy in Australia during the Tokyo Round that, when the Industries Assistance Commission (IAC) was established in

1973 to provide advice on industry assistance against criteria that promote national economic efficiency, preparation for international trade bargaining was specifically excluded from the range of matters which its statute made mandatory for governments to receive advice before changing barriers. In early preparations for the Uruguay Round a decision was taken not to involve the established public inquiry procedures - which apply as a matter of course when barriers are changed for domestic policy reasons - on the grounds that to do so would disclose Australia's negotiating position to other parties in the MTN process. The Government was advised that:

"From a trade perspective ... the very process of public inquiry and report advertises to the world the very nature of the Government's concerns and likely direction of reactions, thereby leaving little or no negotiating possibilities." ²¹.

In a trade bargaining context, preserving secrecy about negotiating intentions was more important than helping domestic constituents understand the domestic issues involved in the negotiating choices being considered.

The effect on domestic efficiency has been the test when changing barriers to protect domestic production, but not when doing so to meet external commitments. It seems that the absence of any formal recognition in GATT procedures of the crucial link between national and international efficiency has, in Australia's case, caused us to forget the domestic efficiency test we apply when changing barriers in a domestic policy context.

The implications of Australia's experience go beyond this. As observed earlier, there is a symmetry between the outcome for domestic efficiency - resulting from how each country meets international obligations to reduce national barriers - and the prospects for internationally competitive industries in external markets. If participants generally reduce their barriers in

accordance with comparative advantage, this will improve their domestic efficiency and the access of their internationally competitive industries to external markets. If, however, they generally meet their GATT obligation as Australia did in the Tokyo Round, the outcome must compound existing (domestic and international) distortions.

From Australian experience, it seems likely that when reductions stem solely from external commitments there is a tendency to shield uncompetitive domestic industries from adjustment pressure. This diminishes the prospect of global reductions which increase access to external markets for producers who are internationally competitive. If negotiations leave in place a structure of national barriers for each participant that is not consistent with domestic efficiency, and a structure of global barriers that does not allow national participation in world trade on a basis reflecting comparative advantage, the scope for national gains through the negotiating process is minimised.

In that event, internationally competitive producers everywhere are disadvantaged in the domestic production environment against less efficient domestic industries and in the external markets they should command on the basis of comparative advantage - when other countries also meet their external commitment without liberalising markets for less efficient domestic production. We are not saying that Australia's experience has applied to all MTN participants. But in the absence of any discipline in the bargaining process to encourage participants to reduce their barriers in a way that is nationally rewarding, and of any procedural basis for promoting domestic understanding of what is at stake nationally in meeting the external commitment, it would be surprising if Australia's approach to trade negotiations has been atypical.

Australian developments since the Tokyo Round demonstrate how the distorted structure of global barriers inevitably becomes

accepted as a permanent feature of the trading environment, apparently beyond the capacity of governments to influence. Because the negotiating process could do little to increase access to external markets for Australia's own internationally competitive industries, these industries have tended to be discounted - as having only a limited contribution to make - in advice subsequently offered to promote Australian participation in world trade. The advice has favoured industries judged more likely to gain access to export markets, given the existing distorted structure of global barriers and the resulting trading opportunities.

There is in Australia at present a coincidence of domestic policy objectives and external, trade policy, commitments. As a result, the Government is approaching negotiations in the Uruguay Round with national economic efficiency in mind. It is doing so because of the high priority presently accorded micro-economic reform in domestic policy, but not in a way that will necessarily secure access to external markets for our internationally competitive producers. For instance, the IAC has been asked to report on Australia's barriers to trade in services in order to improve national efficiency in meeting our Uruguay Round commitments on services. Whether Australian producers of services gain greater access to external markets on the basis of their comparative advantage will depend, however, on whether other MTN participants are similarly seeking to improve the efficiency of their services sectors.

Experience Elsewhere

We have dwelt on Australian experience, because we are familiar with it. But it is clear that other governments have also been able to reduce barriers unilaterally in a domestic policy context in recent years, while having great difficulty doing so to meet external policy commitments in a multilateral context.

For instance, there are many developing countries which have achieved major reductions in protection outside the multilateral negotiating framework, despite their special status in not having to comply with many GATT rules for 'development reasons'. Important examples include Korea, Indonesia, Sri Lanka, Turkey, Israel and Uruguay. The experiences of these and several other countries have been examined recently in a major World Bank project on "the timing and sequencing of trade liberalisation".²² While there have been individual differences among these countries, the World Bank studies have shown clearly that the motivation for engaging in trade liberalisation has in all of them been overwhelmingly domestic in origin - in many cases, representing a response to adverse economic developments. It is also true that in several countries trade liberalisations have subsequently been stalled or reversed, but this too has happened for domestic reasons. One of the principals of the World Bank project has concluded, in an overview of the project's findings:

"The framework of a multinational commitment and the desire to share in a multinational agreement, may be a contributing factor to the survival of liberalisations once some fundamental, other elements are in operation. When such fundamental components are absent, on the other hand, the multinational framework of liberalisation would not insure its survival. This holds similarly to instances of response to the urging of outside entities - most often the U.S. Government, the World Bank, or the IMF"²⁴.

New Zealand, which has had a similar record to Australia when liberalising in an MTN context, has in recent years undertaken a program of substantial reductions in import barriers as part of a broad economic reform strategy.²³ While New Zealand was for many years unable to comply with GATT rules against the use of quantitative restrictions, these barriers have now been largely removed to promote domestic economic efficiency.

Recently, Japan has taken some significant initiatives to liberalise its agricultural protection regime. These include reducing producer prices for rice, milk and beef; lowering tariffs on a range of products; and removing import quotas on beef, fresh oranges and some processed foods.²⁵ While Japan has been under pressure to liberalise for many years within GATT and bilaterally, especially from the United States, its decision to act at this time coincides with the build-up of domestic pressures. These include the need to alleviate the adjustment burden on the export sector resulting from the rising yen and the increasing cost of scarce residential land.

The U.S. and the EC, together blocking collective agreement and progress on agricultural barriers in Uruguay negotiations, are also individually making some adjustments to the level of their agricultural support in a domestic policy context. For instance, the EC is cutting intervention prices and storage subsidies - an action estimated to reduce EC farm returns by 10 per cent for some commodities - and the U.S. has also cut support prices and placed limits on subsidy payments.²⁶

It seems clear that domestic considerations provide a more positive market-opening motivation for national governments than have external commitments. That conveys a good deal about the potential contribution of domestic procedures to enhancing the quality of MTN outcomes and, hence, the functioning of the GATT system.

Reductions in national barriers that produce positive outcomes for national (and therefore international) efficiency occur more naturally in a domestic policy context because the adjustment pain they bring for some is more likely to be seen as worth it, in view of the larger national gains in prospect. What is at stake is reasonably visible in that context. The domestic

trade-offs can be brought into play and resolved, because governments and their constituents have something tangible to hold on to.

There is no such discipline in the way international bargaining is structured at present. In that external arena, the outcomes for national and international efficiency are a residual product of what negotiators are able to agree about. The mystique surrounding the secretive nature of the bargaining process provides an opportunity for well organised domestic constituents to ensure that the 'concessions' affecting their industries are minimised. The generality of domestic constituents find the whole process bewildering. It should therefore not be surprising that governments are having difficulty mobilising a strong domestic commitment to reduce their national barriers in a bargaining context.

CHAPTER 4. WHAT SORT OF GATT ACTION?

To be acceptable and effective, action to strengthen GATT negotiations must meet two conditions:

- . It must respect the autonomy of national governments over domestic policy, in the means devised to bring to the negotiating table the new (non-frontier, non-tariff) barriers.
- . It must provide the technical information governments need, about the domestic effects of national barriers, to make it possible for countries to participate in negotiations in a way that is nationally rewarding - that is, to ensure they do not shoot themselves in the foot.

Which of the options under consideration meet these conditions?

- Tighter rules?
- International surveillance?
- Domestic transparency procedures?

Given the non-transparent forms of the new protectionism, there is clearly little scope for progress through tightening the existing rules defining the circumstances under which the granting of protection is justified. All such criteria are based on the problems change poses for particular domestic industries and have nothing to do with national economic welfare. Because of differing perceptions in national capitals about what formal criteria for such action would be compatible with national economic welfare, an inherently domestic concept and issue, it seems unlikely that international rules reflecting that concept could be agreed through negotiations.

The proliferation of voluntary export restraints and orderly marketing arrangements negotiated outside the GATT in recent years points to the serious dilemma in relying primarily on internationally agreed rules to achieve and/or maintain a liberal international trading order. On the one hand there is a danger that if safeguard provisions are too liberal, and frequently invoked, they undermine the objectives of the agreement. Conversely, if safeguard provisions are very strict there is an incentive for countries to go outside the agreement and negotiate bilateral arrangements. To some extent this has happened in recent years, as countries have sought to avoid the stringent conditions imposed by Article XIX when introducing quantitative import restrictions on particular products. The highest priority should not therefore be placed on tightening the existing rules but on procedures for making the effects of protective actions more transparent.

Governments will continue to be under pressure to protect special interests and it is unrealistic to suppose that this will stop. There is, however, a choice between alternative ways of imposing a transparency discipline on that process. One option, agreed in the Mid-Term Review, is to implement procedures for international surveillance. The purpose and effect of this option is to introduce greater transparency into the conduct of national trade policies from the outside, and reflects the established view of the GATT as an external discipline.

The other option is to negotiate an agreement on domestic procedures to make more transparent domestically the domestic implications of domestic decisions on protection. That approach, proposed in the Long Report, recognises that protectionism stems from a bias in domestic policy-making environments, in which the larger domestic interests which bear the costs of protection tend to be disenfranchised. In this approach transparency is a domestic, not an external, discipline. It requires a new set of domestic rules which involve: each Contracting Party nominating a

domestic agency to generate the information needed about the totality of existing barriers (all trade measures), thus helping secure nationally rewarding outcomes from future MTN negotiations; and agreeing that decisions about changing protection be preceded by a public airing of their implications for the domestic community as a whole.

Transparency: An international or domestic issue?

Increased access to external markets by internationally competitive producers depends on how participants individually respond to their external commitments to reduce barriers. Those decisions involve domestic policy choices beyond the reach of external disciplines. It follows that international surveillance cannot address the domestic issues at the heart of trade liberalisation. An approach to negotiations is needed in which each government is encouraged to do only what is worth doing for domestic reasons. In the long haul, external pressure alone is not likely to sustain market-opening motivation on the part of governments.

The proposed arrangements to ensure that transparency comes from 'within' is based on the premise that in international trade matters, as in all relations between countries, domestic constituents within each national economy regard the motives of foreigners as suspect. We see foreigners as acting in their own interests, even when they are telling us what is in ours.

The focus in domestic transparency arrangements is consistent with the principle, deeply embedded in the GATT and other international agencies, that nothing can or should disturb the hegemony of national governments over domestic policy. That focus is also important because so much of the 'new protectionism' is in forms which are traditionally viewed as part of domestic, rather than external trade policy.

The way ahead

As progress in the FOGS group to date demonstrates, there are difficulties in advancing a proposal for domestic transparency procedures in an environment of international bargaining. The established approach, through negotiated agreements based on reciprocity, is itself part of the problem. Yet a decision to do nothing, because of perceived difficulties for progress in a negotiating context, is a decision to continue to pursue trade liberalisation solely as an external issue - as though it is not also, for participating governments, about national economic efficiency and domestic welfare.

If further progress (particularly within the new areas of agriculture and services) depends on appropriate domestic procedures, which at once maintain the hegemony of national governments over domestic policy and help them resolve the domestic issues involved in MTN bargaining, that question should be high on the agenda for GATT discussion. The importance of the issue for strengthening the GATT system, not the difficulties of working through established modalities, should determine the priority given it.

In discussions of the proposed agreement on domestic procedures, in the FOGS group in Geneva and in other trade policy forums, a number of concerns and perceived difficulties have been raised. These questions and concerns are important, because they reflect perceptions about the proposal which require and deserve clarification. They cannot be dealt with in the body of this report, however, without breaking its continuity. We have therefore included them as Appendix I.

Whatever happens in the FOGS group, there is an opportunity (and a strong incentive) for trade ministers to pursue the Long Report proposal - at the ministerial, rather than diplomatic, level in GATT discussions and directly in their own policy conduct at

home. The incentive for doing so is the certainty that they can not collectively secure greater access to external markets for their internationally competitive producers unless each, when choosing its own barriers to reduce, is also seeking to improve the efficiency of its domestic economy. Since the prospects for internationally competitive producers in external markets depends on how their governments respond to multilateral obligations to reduce national barriers, there is a potentially strong natural constituency favouring domestic transparency procedures - to help trade ministers achieve collectively in Geneva, and individually in their conduct of trade policy at home, the worthwhile objectives about which they agree but are unable to advance solely through international diplomacy and bargaining.

We suggest that discussion between ministers should aim for agreement to introduce two procedures into national decision making about protection, in order to help GATT members secure (and maintain) the national benefits which MTN bargaining alone cannot deliver:

- . each to nominate a domestic agency to prepare, at arms length from the national executive, a public report annually on the structure of national trade barriers and their effects on the performance of the national economy;
- . each to subject requests for new or additional protection to public enquiry and report by that agency on a basis that gives the highest priority to the health of the national economy.

Many GATT members have an existing domestic agency which could be given the necessary economy-wide charter and public scrutiny capacity.

**PART B: INSTITUTIONAL MODELS FOR
DOMESTIC TRANSPARENCY**

CHAPTER 5. THE INDUSTRIES ASSISTANCE COMMISSION

In presenting information about the IAC to help judge its relevance as a model for domestic transparency procedures, we have had to decide whether to concentrate on answering questions beginning with 'why' or on others beginning with 'how'. In order to avoid the discontinuity for readers that would result from moving constantly between material describing how the institution operates in procedural terms and explaining why it does so, we have chosen to focus on the rationale behind its operations and to include descriptive detail about operating procedures, indeed most answers to the 'how' questions, in Appendix II.

Origins

In this vein we think it important to explain the Commission's origins in the context of the major domestic influences then at work, rather than provide a formal account of how it was created, because those influences convey more about the relevance of such arrangements for other environments.

The first thing to note about the historical context is that the Commission was established by extending the charter of an existing institution, the Tariff Board, which had conducted public enquiries on protection since 1921. Until 1967, the Board's advice was based almost entirely on the circumstances of each particular industry referred to it. In 1967 it began to include information in its public reports about the effects of protection on activities elsewhere in the economy.²⁷ This helped public understanding of what was at issue nationally in providing protection on an ad hoc basis. In particular, the information showed how the protection of import-competing industries disadvantaged Australia's internationally competitive industries and adversely affected general community welfare.

Another influence at work was the strong commitment to welfare goals which the Government in 1973 deemed could only be met if the national economy was able to produce the increment to national wealth needed to service those goals.

These influences explain the context in which the IAC was created, in 1974, with bi-partisan support in the Australian Parliament. The then Prime Minister explained that the purpose in establishing the IAC was to secure "a better use of the nation's resources". He gave two reasons for expecting the institution to make a contribution to that objective which other, sectorally oriented, institutions could not. The first stemmed from the fact that:

"The Commission will be a single institution, with responsibility for advising on the assistance which should be given to industries in all sectors of the economy. It will therefore be very conscious of the need to develop a rational and consistent approach to all industries. This Government has inherited a complex, confusing and inconsistent collection of measures which discriminate between individual industries - particularly as between primary and secondary sectors of the economy. In many cases, the total amount of the assistance afforded particular industries is obscure, and its effects are even more obscure." ²⁸.

In an environment of fragmented domestic institutional arrangements, each oriented to a particular industry or sector, the Commission was established in recognition that the economy operates as one system and that the goal of making that system more productive could only be achieved if policy towards particular parts was consistent with the objective for the whole economy.

The second reason stemmed from its role in generating the information, through public inquiries and public reports, needed

about the domestic costs of protection:

"The Commission will be able to develop and pursue a long term program of inquiries, free from day-to-day political pressures. This in turn has very important implications for the amount and quality of its information and for the depth of analysis which the Commission can undertake. This of course includes analysis of the effects of its recommendations in the use of resources in different industries. For example, industries which are comparatively wasteful in their use of resources and which impose a significant cost on the community can be systematically examined through public inquiries, and obliged to justify any special assistance they receive from the Government by demonstrating the benefits they bring to the community." ²⁹.

Its operations were thus expected to facilitate public understanding that the ultimate objective of policy towards all industries throughout the economy is to improve community welfare - and that development of particular industries is a means to this end, rather than an end in itself.

The formal independence of the Commission was secured by its statute, but it was not an independence that could be exercised capriciously. Its powers and its general functioning are subject to the public scrutiny it was established to promote:

"The Commission will be obliged, through its public reports, to explain why it considers that certain industries should receive more assistance than others." ³⁰.

Its statute, and associated administrative arrangements, established the Commission as the public statutory vehicle for "a deliberate, orderly and widely accessible system of communication between the Government, industry and the wider public" on the long term, general welfare questions raised by protection -

questions which the executive of the day and the legislature had great difficulty resolving, because of the immediate contingent costs for those depending on protection.

Those industries depending on protection for their profitability naturally wished things to remain as they were, with governments vulnerable to pressure and the community uninformed about what was at issue. In that situation those responsible for decisions about protection were less likely, and less able, to advocate action which posed a threat to established structures of production. The Commission's public advisory function was therefore deemed "necessary in the interests of fair dealing and open dealing". The influence of greater domestic transparency was to reduce the political costs of decisions made to enhance the performance of the economy, as small groups adversely affected would be hard pressed to get public support for resisting change generally perceived to be beneficial.

It should be said that the IAC was never intended to be the only source of advice on these long term, economy-wide issues, and that governments are not bound to accept its advice. In supporting the legislation creating the institution, the major political parties in the Australian Parliament provided for future governments to receive public advice from the Commission - on the basis of criteria that give priority to national economic efficiency - before providing selective assistance to particular industries.

The system of communication, influence and advice the Commission replaced is evident from the following contribution to the parliamentary debate by a former minister responsible for that communication in earlier years:

"What this legislation means, of course, is the end of the long established and successful system under which industry policy has been devised - the system of discussion,

consultation and negotiation between industry and government..... The access which industry of all kinds has had to the Government through its contacts with Ministers, with members and with Government departments will, if it does not cease, become pointless. What will be the point of industry talking to the Government?.... Governments are very reluctant to be accused of being influenced by vested interests".³¹.

The principal reason for establishing the Commission was to remove from the political arena a source of advice on the long term issues embedded in protection policy, while leaving decision-making firmly with the executive. The IAC was therefore created as an advisory body only - with no judicial, executive or administrative functions. It is required to provide public information and advice about protecting particular domestic industries on the basis of criteria which give priority to the overall competitiveness of the Australian economy and of procedures which enhance public involvement in, and scrutiny of, the advisory process.

Statutory charter

The IAC's charter was established by statute following a report commissioned by the Australian Prime Minister. The report, by Sir John Crawford,³² recommended that:

- the Tariff Board be expanded into an Industries Commission to advise the government on all forms of assistance to all sectors of the economy.
- the Minister could refer any form of assistance to any industry to the Commission, but that he be required to refer to the Commission before taking any action, questions of granting or changing

- . duties or other barriers to imports
- . subsidies, bounties or other forms of direct monetary subvention to any primary or secondary industry where the period of entitlement exceeded twelve months;
- the Commission have the power to initiate inquiries;
- the Commission set out periodically in its annual reports the amounts of assistance afforded all industries, the economic performance of those industries and the effects of industry assistance on the economy;
- all important communications between the government and the Commission be published.

These recommendations provided the basis for the Commission's charter embodied in legislation passed by the Australian Parliament in December 1973, and proclaimed on 1 January 1974. The IAC'S charter contains a public information function, and a public scrutiny function, which together constitute its contribution to the domestic transparency of industry assistance in Australia.

The Public information function

The IAC'S public information function has two dimensions: (i) an on-going, economy-wide, 'mapping' of domestic barriers and an annual public accounting of their domestic effects; and (ii) industry specific questions of assistance or adjustment referred to it. The emphasis in both is on an economy-wide perspective: the first is concerned with describing the structure of Australia's protective barriers and their national economic effects; the second uses that economy-wide perspective to analyse, for each inquiry referred to it, whether a particular

change contemplated in the existing structure of barriers would make the economy more efficient and productive or less.

- General reporting

Information about the forms and overall structure of barriers throughout the economy is published in the IAC's annual reports, with each report adding to the overall picture as the Commission's inquiry or research activities bring more barriers into account. Its annual reports also contain the results of Commission analysis of the intersectoral and economy wide effects of Australia's barriers. The measurement and analytical techniques used are published separately in technical papers.

The general 'overview' function is aimed at enhancing the information available about the incidence and effects of barriers within and on the economy. Its purpose is to provide a good understanding of the overall structure of existing national barriers, needed to make judgements about whether a particular change in that structure will improve domestic efficiency and national welfare. Without an economy-wide perspective we have a poor basis for deciding whether a particular change will take us closer to or further away from a more productive economy, making a better use of national resources.

Obtaining and retaining an economy-wide perspective over time involves an ongoing process which raises the domestic visibility of the overall assistance structure. The IAC's approach to this work has been incremental. It has recognised that, although perfect knowledge will never be obtained, decisions about changing particular barriers in a way that is nationally rewarding cannot be made without an understanding of their expected effects on overall nationally efficiency.

The Commission's general information function therefore provides a public earnest of governments' concern to have the information they need when making changes in Australia's barriers which are intended to be nationally rewarding.

- Inquiry reporting

The general 'overview' element of the Commission's information function is a precondition for it fulfilling the second - providing advice on industry specific questions of protection referred by governments. It is required to provide public advice on such industry specific questions of assistance or adjustment in a way that will enhance the efficiency of the domestic economy as a whole.

As we have noted, all such questions can be resolved in a nationally rewarding way only by providing an information basis to enable the Government, and domestic constituents, to determine which of the available options for change would enhance national efficiency. This second aspect of the Commission's public information function involves a public inquiry process, in which all domestic constituents with an interest in the outcome may participate, followed by a public report containing the Commission's advice and the analysis and information on which it is based.

The authority for the first, more general, part of the Commission's public information function is written into the statute under which it operates. That authority is exercised directly and as a matter of course by the Commission in its annual reports and associated publications. The authority for the second part, involving industry specific questions of protection or adjustment, rests with the Minister responsible for administering the IAC act. The authority for this second part is exercised when that minister sends a reference to the Commission,

specifying in writing the matters to be covered by an inquiry and the reporting deadline. The stages and procedures which characterise the Commission's inquiry process are outlined in Appendix II.3.

In the fifteen years since it was established, the IAC has completed a little more than four hundred public inquiries and reports in response to references covering most industries in the manufacturing and agricultural sectors, as well as many general information reports related to its general transparency function on assistance issues. ³³.

Public scrutiny function

The purpose of the Commission's public information function is to provide the information about Australia's barriers needed by the executive, the legislature and the community as a basis for decision-making in the national interest. The public scrutiny function involves public participation in the processes by which that information is generated. Its importance was expressed by the then Prime Minister when introducing the IAC legislation in 1973:

"The essence of the Tariff Board system is that it makes public inquiries and public reports on questions of assistance for industry referred to it by the Government. The Government proposes to extend this system to industries in other sectors of the economy because it believes the system has, over a long period, proved its value to successive governments in an important area of government decision making. The first and most important reason for establishing the Commission is to allow public scrutiny of the process whereby governments decide how much assistance to give different industries.... It means public hearings, at which interested parties can support or oppose industries' claims for assistance.... It means the systematic collection

and analysis by the Commission and other organisations of information relevant to the Commission's inquiries. Finally, it means public reports which explain in detail the reasons for the Commission's recommendations.... The application to all industries of the advisory system which has long been accepted for manufacturing industries is necessary in the interests of fair dealing and open dealing." ³⁴.

The contribution of public scrutiny to the integrity of the IAC system, under which Australian governments receive public advice on the national economic implications of changing industry assistance before doing so, was expressed by the Prime Minister in the following terms:

"It will be apparent that the reference to the Commission of questions relating to assistance for individual industries cannot be optional: if some industries, particularly those which stand to lose most from public exposure of their claims, can avoid the process of public inquiry the fundamental purpose of the Commission will be frustrated." ³⁵.

Opportunities for public scrutiny are formalised in the IAC's inquiry and reporting procedures. As explained in detail in Appendix II.3, each public inquiry begins when the IAC receives a reference and publishes all the information it then has about the issues under inquiry; after an initial set of public hearings, it publishes its report to government in draft form, and holds public hearings thereafter to give inquiry participants an opportunity for further scrutiny; and final Commission reports are published by governments when they are received, and before a decision is taken.

In this way, the IAC's advice on the particular matters referred to it is subject to public scrutiny at all stages. Its more general information function, involving the overview on the economy-wide structure of barriers and their effects, is also

exposed to public scrutiny - in its annual reports and associated technical publications and other general reports. Its ability to promote public scrutiny and understanding of the economy-wide implications of protecting domestic industries, in accordance with the formal requirement in its statute, is the basis on which its public credibility - and perceptions about its relevance - are determined.

Professional support

The value and integrity of the policy information and public scrutiny functions depend heavily on the quality of analysis and professional support servicing the IAC's work. The institution comprises two interacting groups: a small number of statutory members of the Commission, collectively responsible for determining how the Commission discharges its statutory functions; and a larger number of staff providing the professional support needed to discharge those functions. The statutory members together are responsible for the general reporting function and individually conduct public inquiries and prepare public reports on the matters referred to the Commission. In an operational sense, the quality of the informational outputs depends crucially on the interaction between the two groups.

Most of the analysis within the Commission is undertaken in an economy-wide perspective and much of the numerical analysis uses a multi-sectoral framework, reflecting the structure of the Australian economy. This helps the Commission understand and explain the likely effects, throughout the economy, of any particular policy change under consideration.

A fuller explanation of the assistance measurement and analytical methods used in the Commission's work involves technical detail which may distract readers from what we wish to convey here - a general understanding of how the institution functions. A summary account of those methods is included in Appendix II.5 and II.6. We simply note that it would be difficult to overstate the

importance of the close working relationship between statutory office holders in the Commission and the professionals servicing its work.

How closely the public perception of the IAC's impartiality and integrity is related to the quality of its own research and analytical capacity is reflected in the following statement by the principal Australian manufacturing organisation:

"Despite ACMA's long standing opposition to the IAC (and its predecessor the Tariff Board) ..., we recognise that an independent body, such as the IAC, has a legitimate role as an advisor to Government. To be effective in this role it does need a strong and well qualified research and development section - a section that should be housed within the Commission and not within a Government department. To the extent to which confidentiality permits, IAC information and research findings should be publicly available. At least its reports are open to public scrutiny and challenge - but there is a danger that if the Commission's research facility was transferred across to a policy department, reports produced could have a restricted circulation, a perceived bias and in some instances even be withheld from public examination. Governments are not unknown to restrict access to information, particularly if that information undermines conventional wisdom". 36.

What can be learned from IAC experience?

It would be unrealistic to base international consideration of institutional arrangements for the domestic transparency function on any particular model. It is more important to get the general design of arrangements right, recognising that the choice of particular institutional forms is a matter for governments in each national capital. In this context, it needs to be emphasised that formal public scrutiny procedures, without an

economy-wide perspective, are likely to add nothing to an understanding of the domestic choices involved in changing national trade barriers. They may simply lend an air of openness and justice to a formal process in which national economic welfare is not considered.

Despite our statement of what is obvious, that the IAC system was established for Australian conditions and will not necessarily apply in other environments, there are several important insights from its experience which seem relevant for the general design of domestic transparency arrangements.

Operational integrity of the transparency function.

As mentioned there are two elements to the IAC's economy-wide, public information role. The first is general: it involves placing all national barriers on the public record, raising their visibility to domestic constituents and providing a public account annually of their effects on the performance of the national economy. The authority for this general transparency function is conferred directly on the Commission by its statute, and provides the basis for a substantial program of general research undertaken to extend the IAC's own understanding of the intersectoral and economy wide effects of Australia's trade barriers.

The second element of its transparency role relates to the particular, usually industry-specific, matters referred to it. The authority for this second element rests with the Minister responsible for administering the IAC act. That authority is exercised when the Minister sends a reference to the Commission, specifying in writing the matters to be covered by an inquiry and the reporting deadline. In reporting on those matters, the Commission applies the 'effects on national efficiency' test for which its general transparency function provides the economy wide informational context. Over the Commission's life there has been

considerable operational tension between the general transparency function, for which the Commission has statutory responsibility, and industry specific inquiries which are generated by ministerial references.

The yardstick traditionally applied in the budgetary process to decide what level of professional resources is required to sustain its work has been the number of ministerial references on hand or in prospect at any time. Because the total level of professional support available to the Commission has been tied to trends in the number of particular matters referred to it for advice, the resources available for the general transparency function has been what is left after servicing the day to day inquiry program.

Sometimes the forward program of references has been carefully structured, mindful of the fixed quantum of resources available to the Commission. More often, however, the flow of references has arisen on an ad hoc basis - reflecting what industry departments wished to have publicly reviewed at any time. Thus the IAC's capacity to fully discharge its general statutory research and reporting function has in practice been constrained by large and unpredictable variations in its inquiry workload. Over most of its life its total resources have been determined by the priorities and perceptions about what matters should be referred to the Commission by advisors in sectorally oriented institutions. An industry minister, who for a time also had responsibility for administering the IAC Act, concluded that:

'...in ... various departments which have bureaucratic empires of their own, there is a reluctance to refer issues to the IAC ... There is a reluctance in some departments of government to use the full scope of the IAC, as I believe it might be used.'

In the past the IAC's work has concentrated on manufacturing and agriculture; the job is still largely ahead of it for services and mining. This uneven performance results from the fact that its capacity to generate information depends, in an operational sense, on the industry coverage of the references it receives and on the professional resources available to it. Thus the IAC's ability to sustain the transparency function for all forms of assistance, as required by its statutory charter, has been constrained.

Without labouring this point, the IAC's experience confirms that things are usually as they are for very powerful reasons. There is always likely to be some tension between the resources available to such bodies and what they are charged to do by public charter. With this in mind, we suggest that the operational integrity of domestic transparency agencies be secured by regular performance reviews. These public reviews could be conducted on say a four yearly basis by a group of domestic constituents large enough to cancel out special interests. Their purpose would simply be to provide a public review mechanism to establish whether the transparency agencies are doing what they are required by public charter to do. That seems the simplest, and most direct, way of matching their performance with public expectations.

It is most important that all requests for industry assistance, including cases involving emergency protection under GATT rules, be subject to public review and that the reviewing agency be required to report on the national economic effects of providing protection. It is no less important that the general transparency function be maintained, because it provides the information needed to judge whether a particular change under consideration is likely to make the national economy more productive or less. We believe that countries which initially introduce a general transparency function, to generate the information needed to secure the domestic gains from meeting

their external commitment to reduce barriers, will see the merit of extending that function to require all industries seeking assistance to pass the national efficiency test. That is indeed the best way of ensuring that any aberration in the conduct of policy to meet the demands of particular industries will, in time, be self correcting.

Ministerial responsibility.

An important reason for domestic transparency arrangements in the Australian environment has been to provide a public information counterweight to the particular pressures on government from industries seeking economic preferment. Australian experience confirms that industry ministers have industry constituencies, and must be seen to respond to them. It is therefore important that ministerial responsibility for the domestic transparency function rest with a Minister who is responsible for the health of the economy as a whole, rather than for a particular sector of it. It also confirms that institutional arrangements are needed which secure the transparency function against manipulation by sectorally oriented government departments.³⁸ Australia's experience with such arrangements is described in Appendix II.2.

MTN preparations

As mentioned, changes in Australia's trade barriers to meet external bargaining commitments have been specifically excluded from the public scrutiny processes and national efficiency criteria that apply when those same barriers are changed in a domestic policy context. The well established view of trade liberalisation as being part of external policy, manifest in Australia's preparation for the Tokyo Round, is also reflected in our preparations for the Uruguay Round.

Because of the very considerable lead time involved in seeking and securing advice through procedures providing scope for public

participation and scrutiny, the IAC proposed in February 1984 - two years before the Uruguay Round began - that:

It would be logical, and consistent with promoting national welfare, if the general strategy developed for Australia's participation in a further MTN round were consistent with the objective of gradually restructuring domestic industry to make it more internationally competitive. That would mark a profound change from the way preparation for the last MTN was conducted and provides the basis for the suggestion that the issues be referred to the IAC now - so that the process of identifying and understanding what is at stake can begin sooner rather than later ... and so that Australia's contribution to the MTN reflects a conscious choice between the available options.

The reasons why preparations for the Uruguay MTN should involve the public scrutiny processes and national efficiency test which apply when Australian barriers are changed for domestic reasons have been elaborated in subsequent annual reports of the IAC. ³⁹.

Although the Commission's professional staff has made some technical contribution to preparations at the bureaucratic level, and the Commission has been engaged in an 'informational' inquiry into impediments to trade in services, the idea of developing a negotiating position through procedures which provide an opportunity for public evaluation of the options being considered has not gained sufficient support among Australia's trade policy advisors to provide the basis for national preparations.

If having domestic transparency procedures and not using them in our own preparations appears to be wasteful and inconsistent with what happens when barriers are changed for domestic reasons, it also provides a very weak basis for persuading other MTN participants to seek nationally rewarding outcomes in the barrier reductions they make. Yet it is clear that increased access to

external markets for their internationally competitive producers, and ours, depends on MTN participants generally approaching negotiations with national economic efficiency in mind.

A very great impediment to progress in the Australian environment has been the mystique and complexity that surrounds discussion and understanding of international trade issues. That has created public uncertainty about the extent of domestic adjustment involved and, as our experience in the Tokyo Round attests, makes it difficult for trade ministers to see MTN negotiations as providing an opportunity to secure the domestic gains from meeting their bargaining commitment. And trade diplomats continue to have a mind-set about MTN negotiations as an exchange of 'concessions' with foreigners.

This means that trade ministers must assert their primacy over trade diplomacy, if an approach to MTN bargaining is to be developed which is nationally rewarding for participants. ⁴⁰.

Domestic transparency and 'political will'.

The reason for establishing the IAC as an independent advisory body on protection was to remove the source of advice on such matters - which affect the long term productive capacity of the economy - from the political arena and from the many sectorally oriented public institutions dealing with industry issues on a daily basis. Its public information and scrutiny functions were put in place to help reduce the political costs of changing protection in a way that is nationally rewarding. That is why the national efficiency criteria were written into its statutory guidelines, and why it is required to explain in its public reports why it considers some industries should receive more assistance than others.

It is significant in this context that the difficulty of progressing MTN negotiations is usually attributed to a lack of

'political will' on the part of national leaders, as though they simply need to wish things to be different for that to be so. This observation explains no more than that leaders often lack the power in their domestic environments to make difficult decisions about trade barriers, in the face of pressure from particular economic constituents wishing to avoid the adjustments such decisions would bring for them. That has led to proposals for liberalisation strategies which are opportunistic in terms of pre-empting, rather than resolving, the domestic issues involved. Proposals of this type encourage stealth by national leaders in using opportunities created by national electoral cycles to pre-empt the influence of adjustment averting constituents. Such strategies lack durability. They are the antithesis of the approach based on domestic transparency procedures proposed in the Long Report, and sponsored by New Zealand in the Working Group on the Functioning of the GATT system. That is not to say that 'windows of opportunity' do not occur, but simply that they do not constitute a credible or durable basis for liberalising trade barriers.

The approach through domestic processes recognises that the policy conduct of governments cannot get ahead of domestic understanding about what is at stake domestically, in meeting external trade bargaining commitments. The contribution of domestic transparency to trade liberalisation is therefore the same as its contribution in domestic policy, when changes in barriers are being made to enhance domestic efficiency. Its function is to provide the information domestic constituents (and national executives) need to reduce the political costs of liberalising national barriers, by making the outcomes for domestic efficiency more of a conscious domestic choice and less a by-product of external trade diplomacy and bargaining. That approach must also help trade ministers, when they meet in the international forums where liberalisation is pursued as an external issue, look less like distant spectators of their own actions at home.

Exceptions and exclusions

It hardly needs to be said that arrangements to promote public visibility of the domestic costs of existing forms of protection will lead to pressure for new forms which fall outside the scope of the public scrutiny discipline.

In Australia this has over time produced an innovative array of special arrangements - including 'industry plans', offset requirements in defence procurement, local content schemes and government purchasing preferences. Once in place, there is pressure to enshrine such arrangements as part of established industry policy and therefore beyond the procedures which apply when more straightforward and obvious forms of protection are under consideration. All are manifestations of the 'new protectionism' that has emerged to replace the more traditional forms of border protection.

These less transparent barriers, whether or not they are referred to the IAC for inquiry and report, fall within its general reporting function - and their effects have been dealt with extensively in the Commission's annual reports. It is not possible to say that the IAC's existence has caused these new forms of protection to disappear from the Australian environment. It would be unrealistic to expect the kaleidoscope of new forms to cease, since they continue to emerge and change as existing forms lose their appeal or efficacy. It can be said, however, that the transparency the IAC has brought to bear on their costs has helped ensure that the aberrations which they reflect tend, over time, to be self correcting.

IAC's longer haul influence

The influence of transparency on the policy environment has operated through public understanding. The IAC's main contribution to domestic policy has been to influence the general

environment of expectations and perceptions among Australian producers, rather than to generate spectacular or discontinuous changes in the levels or structure of Australia's barriers.

There is now much less disagreement in Australia about the national economic effects of protection than when the Commission was established. There is greater awareness that the economy operates as one system; that protection for particular industries impedes the growth of others; and that questions of industry assistance will be resolved with a knowledge of their effects on the performance of the economy as a whole. In that environment, there is less scope for particular industries to press for new forms of protection that would diminish national economic welfare and greater scope to remove barriers retarding the performance of the economy.

The influence of transparency in the Australian environment has therefore been to shift expectations about the likely success of requests by producers for special treatment, and to help discourage investment in the effort required to secure it. Perhaps the most objective measure of its efficacy is the differing outcomes for national efficiency when barrier reduction has been undertaken in a domestic policy context and in trade bargaining. Its influence has been brought to bear in a domestic policy context, with benefit to national economic efficiency, but not when meeting external trade obligations. There is no reason to suppose that the IAC's transparency function in domestic policy would not transfer to preparations for barrier reduction in a trade negotiating context, in accordance with the Long Report's proposal.

CHAPTER 6. INSTITUTIONS IN OTHER COUNTRIES.

There is a wide range of institutions in other countries which provide advice on industry assistance. Some of these have also been identified as models for domestic transparency arrangements. Perhaps the most commonly cited is the United States International Trade Commission; the Economic Council of Canada and the Economic Development Commission in New Zealand have also been proposed. It may therefore be useful to look more closely at these bodies, in the context of the criteria in the Long Report.

The United States International Trade Commission (USITC)

The USITC had its origins as the International Tariff Commission, which was established by Act of Congress in 1916 to "investigate the administration and fiscal effects of the Customs laws, study the revenue aspects of the tariff structure and the conditions of competition that US industries faced abroad, spot unfair trade practices and dumping, and conduct other, similar investigative functions".⁴¹ Despite changes in its mandate through successive Acts of Congress, and a change of name in the 1974 Trade Act, the agency's role has remained broadly the same.

In its annual report for 1988, the USITC described its recent activities as including:

- making recommendations to the President regarding relief for industries seriously injured by increasing imports;
- determining whether US industries are materially injured by imports that benefit from pricing below fair value or subsidisation;

- directing actions, subject to Presidential disapproval, against unfair trade practices such as patent infringement;
- advising the President whether agricultural imports interfere with price-support programmes of the US Department of Agriculture;
- conducting studies on trade and tariff issues and monitoring import levels; and
- participating in the development of uniform statistical data on imports, exports, and domestic production and the establishment of an international harmonised commodity code." ⁴².

The USITC has quite elaborate procedures to provide for its independence. It has no direct policy-making or administrative role; it functions as an advisory and investigative agency. No more than three of its six Commissioners can be from the same party and the conditions and timing of appointments have been designed to minimise the scope for Executive manipulation of its membership. In addition, the 1974 Trade Act removed the Commission's budget from Executive control. The Commission may initiate its own inquiries, as well as responding to requests from interested parties, the US Trade Representative and Congressional Committees.

The USITC also has procedures which facilitate the openness and public scrutiny of its inquiries. It holds public hearings in Washington DC as a normal part of its work in formulating advice on specific assistance matters, such as escape clause or anti-dumping investigations. The matters on which the Commission provides advice are themselves publicly known and the 'operating instructions' of the USITC spelt out in legislation. Submissions from interested parties, such as domestic producers, importers

and consumers, can be made orally or in writing. The Commission's reports are published after decisions on them have been made by the Executive. In addition, the Commission publishes an annual report and, throughout the year, a range of informational reports of a more general nature.

It is against the third important criterion - an economy-wide perspective - that the appropriateness of the USITC as a transparency institution falters. The USITC has no general, economy-wide guidelines for its recommendations and reports. On the contrary, the bulk of its work is concerned with determining whether protection should be awarded to particular industries, according to narrow criteria laid down in legislation.

For example, under Section 201 of the Trade Act of 1974 (Escape Clause) the Commission investigates whether an article is being imported in such increased quantities as to be a 'substantive cause of serious injury or the threat thereof' to a particular domestic industry.

"If the Commission's finding is affirmative, it must recommend a remedy to the President, who has discretion to take action to provide import relief, such as an increase in duties, the establishment of quantitative restrictions, the negotiation of orderly marketing agreements, or specified types of adjustment assistance to groups of workers, firms, or communities." ⁴³.

Recommendations to the President based on similar industry-specific criteria are also made in the areas of 'unfair practices in import trade', countervailing duty investigations against subsidised imports, anti-dumping ('imports marketed at less than fair value') and import interference with agricultural programmes.

While the Commission does not contribute to an economy-wide perspective on decisions about protection to particular industries, it does produce a range of studies on its own initiative, or on request, which serve a useful informational role. These include economic assessments of multilateral or regional trading proposals or agreements, or of particular trade barriers. For example, in late 1988 the USITC began a study analysing the likely impact on US trade of reductions in protection in the context of the Uruguay Round. Another recent investigation is into the effect of the voluntary restraint arrangements applying to steel imports on domestic steel producers and users.⁴⁴ However, most studies have been on issues other than the national economic costs of industry assistance. Published studies of that kind have tended to be produced on a one-off basis by other Federal agencies, such as the Federal Trade Commission, as well as by private research organisations. (See for example, Morkre and Tarr, 1980 and Hufbauer, 1986).

The Economic Council of Canada

The Economic Council of Canada (ECC) was established by act of Parliament in 1963, as an independent, economic policy advisory body. The ECC has a dual advisory and educational role, and the objective of promoting community consensus about desirable economic policy directions in the longer term. In introducing the resolution to establish the ECC, the Prime Minister stated:

"The government's hope ... is that we can establish an Economic Council of Canada which will be an effective instrument for creating in Canada this kind of economic consensus, this kind of economic understanding that we need if we are to make the most of our resources, achieve and maintain high levels of employment, make our economic growth adequate for that purpose and compete successfully, as we must, in the new trading world."⁴⁶

The Council's statutory responsibilities include:

- regularly to assess, on a systematic and comprehensive basis, the medium-term and long-term prospects of the economy, and to compare such prospects with the potentialities of growth of the economy;
 - to study how national economic policies can best foster the balanced economic development of all areas of Canada;
 - to encourage maximum consultation and co-operation between labour and management; and
 - to seek full and regular consultation with appropriate agencies of the governments of the several provinces."
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Independence.

The ECC has no executive or direct policy-making role. It is a statutory agency separate from the government bureaucracy and reports to the Prime Minister. The Council comprises three full-time members (a Chairman and two Directors) and twenty-five part-time members. The Council's work is supported by sixty professional economists and other permanent staff.

The ECC generally initiates its own work, which ranges over all economic policy issues. The legislation also provides for the federal government to ask the Council to undertake 'special references', but the nature of its recommendations is not subject to government instruction.

Openness.

The Council is responsible for the publication of an annual review which is both an analysis of economic conditions and policy evaluation, and an assessment of contemporary issues. It has adopted the policy that "no council recommendations are to be made privately to the federal government or to any other body".⁴⁸ Its studies and research are published in consensus documents, research studies, discussion papers, conference papers, and in a quarterly bulletin. The ECC holds seminars on various policy issues, but does not conduct public hearings nor receive formal submissions.

The ECC has a number of features conducive to an economy-wide perspective. The legislation states the "it shall be the duty of the Council to advise and recommend ... how Canada can achieve the highest possible levels of employment and efficient production in order that the country may enjoy a high and consistent rate of economic growth and that all Canadians may share in rising living standards."⁴⁹ The Council may investigate and report on any economic issues relevant to overall performance. It focuses on longer-term economic research and has sponsored the development of a quantitative model of the Canadian economy ('Candide'), which it uses in preparing its annual reviews.

The Council does not, however, focus on industry assistance or protection issues in any systematic way. The bulk of its output has been devoted to other microeconomic issues (such as the labour market, productivity and technical change), macroeconomic issues (monetary and fiscal policy, the balance of payments), and social issues such as housing, education, health and welfare. Also, its capacity to abstract from sectional viewpoints would appear to be hampered by the composition of its membership - with representatives of management, labour, economic sectors and

regions - together with the statutory requirement for consensus within the Council in its annual review and other reports.

New Zealand's Economic Development Commission

The New Zealand Economic Development Commission (EDC) has only been in operation since early 1987. It replaced the Industries Development Commission, which had in turn superseded the Tariff and Development Board in 1975. The two earlier bodies, while operating under legislation which formally secured their independence, and having open procedures - involving public hearings and published reports - were more concerned with determining the levels and forms of assistance needed for the development of particular industries, than providing advice based on national welfare considerations.

The EDC was created following the report of an advisory body appointed by the government to advise on the establishment of an Industrial Development Board, foreshadowed in the 'Labour Party Policy Document'. It was envisaged that the Board would have a direct role in planning the development of New Zealand industry, by advising the Government how it could encourage those industries and economic activities of greatest benefit to New Zealanders as a whole.

Instead of recommending the establishment of a body that would be 'picking winners', however, the Steering Committee considered that the national welfare objectives behind the proposal would be best served by having an advisory agency to "increase public scrutiny and understanding of government economic policies and hence ... the achievement of a more prosperous and fair economy". The Steering Committee stressed that, in reaching its conclusion, "the body should not adopt a sectoral or purely financial approach, looking only at the profit or loss for one activity or project. Rather it should consider the implications of a proposal from a national or broad community perspective".⁵⁰

The Committee's proposals were consistent with the three basic requirements for domestic transparency. They recommended that a Chairman and three Commissioners be appointed for periods of up to five years and that their independence be ensured by an Act of Parliament. While Government was not obliged to receive advice from the EDC before changing protection levels (as is the case with the IAC in Australia), Commissioners have the power to initiate their own inquiries (which the IAC does not). The openness of their work was to be achieved through the mandatory publication of their reports to the Government and by the power, though not obligation, to hold public hearings. An economy-wide perspective was to be built into the statutory guidelines for its work, with an emphasis on 'achieving higher living standards for New Zealanders as a whole'.

In the event, the EDC was created by Cabinet directive rather than by Act of Parliament, although in other respects it conforms to the arrangements proposed by the Steering Committee. So far, its inquiries have focussed mainly on specific regulatory issues in the services sector, rather than a more general evaluation of industry assistance.

Other institutions

Numerous other institutions have been surveyed in the Long Report, which placed them under three headings: private research organisations, 'protection tribunals' and broader review bodies. That report concluded, however, that most of these organisations as they stand do not satisfy all the necessary criteria to fulfil a domestic transparency function.

For example, private research organisations, such as universities and 'institutes', have in many cases produced work of high quality and relevance on the economy-wide consequences of industry assistance. But it has tended to be sporadic and somewhat remote from the policy-making process. Private bodies

of this kind normally have neither the resources nor the incentive to do such work on a continuous basis.

Protection tribunals include agencies established to advise on tariff levels needed by industries, as well as quasi-legal bodies making judgements about industries' claims under emergency or unfair trade laws. Apart from the USITC, organisations in this category can be found in Canada (Canadian International Trade Tribunal), Sri Lanka (Presidential Tariff Commissions), Philippines (Philippines Tariff Commission), Thailand, Jamaica and other countries. While these bodies have generated useful information about the tariff structure in their countries and in some cases have been involved in reform programmes, they generally have authority to report only on tariff assistance, and their operating guidelines emphasise the needs of industries, as well as broader objectives. For example, while the Sri Lankan Tariff Commission's guidelines refer to the objective of 'an efficient allocation of resources', mention is also made of the "need to encourage local industry by the adoption of protective measures".⁵¹ These bodies also vary in the extent to which they meet the 'independence' and 'openness' requirements.

The broader review procedures referred to in the Long Report range from what are essentially 'budgetary watch-dogs' (such as the General Accounting Office in the United States, or the agency of the German Federal Government responsible for providing information and evaluation of all subsidy programmes) to advisory and reporting bodies on economic issues generally (the Council of Economic Advisers, or the Economic Council of Canada). While being closer to the policy making process than private research organisations, and not constrained by the narrow legislative criteria of the protection tribunals, these bodies do not report or advise on industry assistance issues on a regular or comprehensive basis and vary in the extent to which they facilitate public scrutiny.

Scope for adapting existing agencies

While most of the institutions reviewed do not presently discharge a domestic transparency function as envisaged in the Long Report, many could be adapted to do so without major difficulty. This applies in particular to the protection tribunals as well as some of the agencies with broader economic review responsibilities.

For a number of the broader review bodies, the main requirement would be to channel at least part of their activities into industry assistance and protection questions on a permanent basis. (This applies to the Economic Council of Canada, for example.)

In the case of the 'protection tribunals', the main deficiency is the narrowness of their criteria for evaluating industry assistance, as well as in some cases a focus on particular sectors of the economy or on tariff assistance alone. These characteristics, however, were largely shared by the Australian Tariff Board and were addressed through new legislation which transformed it into the Industries Assistance Commission. ⁵²

In some countries, there may be difficulties in changing the existing industry-specific legislative responsibilities of the agency (such as those related to emergency protection or 'unfair' trade), but in such cases it should be possible to add economy-wide criteria to their operating guidelines. For example, the following observation on the USITC has been made by a leading American trade policy analyst:

"The U.S. International Trade Commission must, under present law, limit its injury investigations to the petitioning industry, although it can and does consider broader effects when it decides what forms of trade relief to recommend. One approach would be to widen the USITC's mandate so it would be required to publish a more comprehensive assessment of the

impact of import restrictions, as well as the industry-specific findings on which its injury determination is based. This would include, but go beyond, the proposal of Senator John H. Chafee (R-RI) that the USITC evaluate the impact of trade relief on consumers." 53.

FOOTNOTES

1. See Olivier Long et al (1987) and Fritz Leutwiler et al (1985). The Ministerial Declaration on the 'Functioning of the GATT System' is as follows:

"Negotiations shall aim to develop understandings and arrangements:

- (i) to enhance the surveillance in the GATT to enable regular monitoring of trade policies and practices of contracting parties and their impact on the functioning of the multilateral trading system;
- (ii) to improve the overall effectiveness and decision-making of the GATT as an institution, including, inter alia, through involvement of Ministers;
- (iii) to increase the contribution of the GATT to achieving greater coherence in global economic policy-making through strengthening its relationship with other international organisations responsible for monetary and financial matters."

2. Long et al, p(i).
3. GATT, News of the Uruguay Round of Multilateral Trade Negotiations, No.23, 14 December 1988, p.35.
4. Ibid
5. UNCTAD VII, Final Act, para. 105, sub.para. 4.
6. Nam Duck-Woo, Chairman's statement concluding the Fourth Asian-Pacific Trade Conference, Bali, Indonesia, 10 Jan. 1988.
7. Long et al, p.4.

8. See for example, Laird and Yeats, 1988.
9. Long et al, pp.7-9
10. Ibid, pp.9-11.
11. Ibid, p.15.
12. Ibid, PP.27-28.
13. Reference to the IAC on General Rates of Duty, 3 May 1972.
14. Confederation of Australian Industry, letter dated 31 August 1978.
15. The Minister for Special Trade Representations, National Rural Press Club Luncheon, Canberra, 1 August 1978.
16. See the IAC's annual reports for 1983/84 and 1984/85.
17. Underlining added. See, Hansard House of Representatives, 21 November 1979, pp.3280-1.
18. R.J.L. Hawke, President of the ACTU, Press Release, June 1973, following the 25 per cent across-the-board reduction of Australian tariffs.
19. Metal Trades Industries Association (MTIA) Submission to Arbitration Commission, April 1986, p.4.
20. MTIA, 'The Current State of Australia's Manufacturing Industries', June 1986.
21. Department of Trade comment in a Cabinet Submission following the Uhrig Review of the IAC, 1984.
22. See, World Bank, 1987.

23. Bates and White, 1988.
24. Michaely, 1988, p.6.
25. See GATT, 1988, pp.12-13.
26. See Miller, 1986.
27. See Rattigan, 1986.
28. Hon. E.G. Whitlam, Second Reading Speech, Hansard, Australian House of Representatives, 27 September 1973.
29. Ibid
30. Ibid
31. Hon. D.G. Anthony, Hansard, Australian House of Representatives, 18 October 1973, p.2356.
32. Sir John Crawford, 1973.
33. Some of the general reports are included in the bibliography. For a more complete list, see Rattigan, 1988.
34. Whitlam, op cit, p.1652.
35. Ibid
36. Associated Chambers of Manufacturers of Australia, Newsletter, August 1976.
37. Hon. J.N. Button, Senate, Hansard: Estimates Committees, 19 September 1986, p.451.

38. See Rattigan, 1986.
39. See IAC, Annual Report 1983/84, AGPS Canberra, and subsequent issues to 1986/87.
40. The need to inject greater ministerial control into the MTN process has been recognised by trade ministers, who have included the question of "greater ministerial involvement" in deliberation of the FOGS group.
41. Dobson, 1976, p.87.
42. USITC, 1988, p.6.
43. USITC, 1986, p.66
44. USITC, 1988.
45. See, for example, Morkre and Tarr, 1980 and Hufbauer et al, 1986.
46. Smith, 1981, p.72.
47. Newton, 1983, p.5
48. Smith, op cit, p.82.
49. Ibid, p.73.
50. New Zealand Government, 1986, p.15.
51. Cuthbertson, 1987.
52. See Rattigan, 1986 and 1988.
53. I.M. Destler, 1986, pp.220-1.

APPENDICES

I: QUESTIONS RAISED ABOUT THE PROPOSED DOMESTIC TRANSPARENCY PROCEDURES.

II: THE INDUSTRIES ASSISTANCE COMMISSION

1. The Commission's Charter
2. The Institutional Setting
3. The Commission's Inquiry Procedures
4. The Commission's General Reporting Function
5. Measurement of Assistance to Industries
6. Analysis of Effects of Assistance

APPENDIX I:

QUESTIONS RAISED ABOUT THE PROPOSED DOMESTIC TRANSPARENCY PROCEDURES.

The Long report's proposition was that the effectiveness of international negotiations in reducing trade barriers would be enhanced if national preparations were underpinned by domestic transparency arrangements to make more visible the domestic costs of protection and the domestic gains from liberalising home markets. This is a new approach to a long-standing problem.

As is natural in coming to terms with unfamiliar things, the approach has led to questions and concerns expressed in FOGS group discussion and in other forums. The following explanations are intended to provide clarification on those questions and concerns.

Why is there now a greater need to emphasise the domestic gains from trade liberalisation rather than continuing to rely on the international obligations of GATT members to reduce trade barriers?

The present impasse in international trade results from the tendency of governments to view what is at issue externally and domestically in liberalisation as separate matters. Under the bargaining approach, trade diplomats have become preoccupied with maximising concessions in foreign markets in return for domestic concessions which require a minimum of adjustment by protected local producers. As a result, the negotiating coin has not been put together in a way calculated to reflect the domestic welfare objective which underpins membership of GATT and which provides the rationale for their efforts.

In the bargaining framework within which they have worked, any mutually agreed exchange of concessions between the parties has been counted as a contribution to the international objective of trade liberalisation. Yet, for the individual countries engaged in the bargaining process, trade liberalisation is about domestic choices. The traditional bargaining approach, because it has usually been undertaken against a background of domestic political pressure to maintain particular interests at home, has distracted attention away from the domestic welfare choices which are the foundation of the process.

The Australian experience in the Tokyo Round, described in the body of the report, illustrates what may happen when countries engage in external bargaining without any domestic discipline to help ensure that the result for them is nationally rewarding. Whereas, from an international bargaining viewpoint, that outcome could be represented as consistent with the international objective of reducing barriers to trade, it did not improve domestic economic efficiency.

So long as domestic preparation for international bargaining is conducted in a way which generates such outcomes it is difficult to see how progress can be made - in either removing barriers to domestic efficiency or international trade. To bring the domestic and external dimensions of trade liberalisation - which in reality are indivisible - into greater harmony, the negotiating positions must be worked out with a good domestic understanding of their domestic effects.

Aren't the prospects for a negotiated solution to agricultural trade problems much greater now that it is firmly on the MTN agenda?

The barriers which efficient agricultural exporters face in world markets are the result of national policies adopted for domestic reasons. In the US, the EC and Japan, policy toward agricultural production and trade has been largely shaped in response to domestic producers - and without much regard for the effects on the rest of the economy. That is why an approach to international negotiations is needed in which each government is encouraged to do only what is worth doing for domestic reasons. History tells us that governments will not open their markets just to satisfy the demands of foreign producers. But they are more likely to take steps in response to the demands of domestic constituents who are bearing the costs of subsidising local production.

What is meant by the term "domestic transparency"?

It refers to procedures that provide for public scrutiny of protective action and that promote domestic understanding of its effects on, and within, the domestic economy. It focuses on domestic processes for the making of protection and trade policy that give the national interest priority over sectional interests.

Domestic transparency thus extends beyond the issue of whether or not information on industry assistance is available to domestic constituents. Many countries already provide such information in official publications - customs schedules, periodic gazettes, etc. - but this is unlikely to cover the forms (such as voluntary export restraints and domestic regulations) which constitute the 'new protectionism'. And even if all the relevant information were available, it has no influence on the policy-making process. The role of 'transparency', in promoting positive market opening motivation for national governments, therefore involves not simply raising the domestic visibility of particular barriers to trade, but also domestic understanding of their effects - within the economy imposing them.

Within GATT there are already provisions to promote transparency of trade policy. Can a new set of arrangements do more?

The transparency provisions in the GATT are there to permit international surveillance of the bargains struck in trade negotiations. The domestic transparency proposal, by contrast, is about bringing wider domestic influences to bear on the national policy-making process, rather than verifying policy outcomes after the fact.

The transparency proposal in the Long Report is built on three propositions: that the important barriers are increasingly in non-tariff forms, which have traditionally been viewed as part of domestic policy; that because outsiders usually cannot see, let alone measure, them the barriers cannot be brought into account in international negotiations unless governments imposing them choose to place them 'on the record'; and that they are more likely to do so to enhance national efficiency than to make concessions sought by foreigners.

Without domestic transparency arrangements, it is difficult to imagine how the provisions within GATT for international

surveillance of trading partners' policies could be made effective. Information which is not available domestically can not be used in international forums. The problems which voluntary export restraints have posed for the GATT are one illustration of this. The negotiations on barriers to trade in services may prove to be another.

Why is it important that an understanding of the domestic costs of trade barriers or production subsidies be promoted by national processes rather than by 'foreigners'?

The proposal for negotiating arrangements to ensure that transparency comes from 'within' is based on the premise that in international trade matters, as in all relations between countries, domestic constituents within each national economy regard the motives of foreigners as suspect.

Is it being suggested that the bargaining process has no place in international trade liberalisation?

No. The proposition is to place on the GATT negotiating agenda the question of domestic procedures for national preparations, seeking only to establish an agreed basis for governments (and their domestic constituents) to identify what domestic barriers to trade they should reduce in order to yield more rewarding outcomes nationally. It has to do with national preparations for negotiations and with the basis for the 'concessions' offered and sought.

It needs to be emphasised that such an initiative would underpin and not replace the bargaining process. Its contribution to liberalisation of world markets is that it would enable bargaining to be undertaken in a way that reflects domestic understanding, in each participating country, of the domestic costs of closing domestic markets - rather than in a way that perpetuates the illusion of gaining advantages at the expense of

foreigners through an exchange of trade concessions.

How are the domestic transparency proposals related to attempts to reform the safeguard clauses of the GATT?

GATT rules attempt to quarantine any new trade restrictions, by specifying the special circumstances in which they may be applied. In some cases these provisions have been abused (anti-dumping); in others, they have been side-stepped (Article 19). Attempts to reform the safeguard clauses have largely focused on further refinement of, or changes to, the rules - relating to injury, discrimination, etc.

The danger of this approach is that specifying the rules more precisely is likely to result in more complex systems of protection. Protection administered through complex rules and criteria makes it more difficult to determine both the extent of assistance and its effects on the rest of the economy. Increased complexity, and the lengthy technical consideration implied by it, lends an air of science and justice to rules which have nothing to do with collective welfare.

The highest priority in our view should not be placed on tightening the existing rules but on opening up domestic procedures for taking protective action so that all affected domestic interests can provide an information input into, and public scrutiny of, decisions. The role of transparency would be to ensure that the domestic implications of protective actions were known domestically. This approach recognises that protectionism stems from a bias in domestic policy-making environments, in which the larger domestic interests which suffer through protection tend to be disenfranchised. Because industry-specific injury criteria take no account of their interests, there is a lack of information about how their well-being is affected when such rules are applied. Consequently, a greater role for transparency implies not so much a clarification of

existing international rules but rather a new set of domestic rules which requires that changes in industry assistance be preceded by a public airing of its implications for the domestic community as a whole.

Does this mean the establishment in all GATT member countries of agencies modelled on the Industries Assistant Commission in Australia?

No. It would be unrealistic to base international consideration and discussion of institutional arrangements on any particular model. It is more important to get agreement about the general design of arrangements that would be acceptable to all countries. The choice of particular institutional arrangements must then be a matter for governments in each national capital. Their choice is likely to reflect the cultural, social and political environment in each country. It is the capacity to promote domestic understanding of what is at stake domestically that matters, and international discussion should be aimed at agreed guidelines for achieving this within each country.

What are the risks if governments appointed compliant people to their national transparency agencies to produce results favouring continued protectionism?

The experience of the IAC is that, although governments of the day have sometimes appointed people supportive of them, this has not produced advice or information favouring protection. The public charter of the proposed national transparency agencies is to publicly account for the effects of protection measures on domestic welfare. Their focus is therefore on the distribution of costs within and on the domestic economy. Because their reports (like the IAC's) would be public, the contents would be subject to public scrutiny. If they didn't get it right, and favoured particular groups benefiting from protection over the generality of domestic constituents bearing the costs, this would

be self-correcting as public evaluation was brought to bear.

While tame agencies might be able to mislead foreign observers, they would be operating within a charter focussed on the domestic effects of domestic barriers and in the context of public scrutiny. This provides the greatest guarantee that they would not fool domestic constituents.

Even if most governments failed to get it totally right, the all-important question remains: are the results of the approach likely to promote a more positive and genuine domestic market opening motivation for national governments than the existing approach - in which almost no attempt is made to bring into account the domestic implications of the concessions offered?

Is not the proposal, based as it is on raising the domestic visibility and costs of national barriers, relevant only to some cultural and political environments?

No. All governments need information about the totality of their national barriers to make negotiating decisions which they judge is in their national interest. That is so regardless of the cultural and political environment in which such decisions are made, and regardless of the perception of national interest on which those decisions are based. To suggest otherwise is to argue that decisions about reducing national barriers are better made without knowing their likely domestic effects.

It is also important to consider whether the task of bringing the less visible barriers to the negotiating table should be seen as a national or an international one. Since such barriers were in most cases introduced to avoid existing external disciplines, it seems unlikely that governments imposing them would welcome rigorous external surveillance of their policy conduct.

Finally, it has been suggested in FOGS group discussion that developing countries in particular would resist efforts to introduce domestic (rather than international) transparency procedures. In fact, developing countries in April 1988 proposed in UNCTAD that agreement on domestic transparency procedures is needed to shed more light on the domestic costs of trade barriers.

For all these reasons, domestic transparency procedures are less likely to be intrusive than international surveillance.

Is yet another institution warranted, in an already crowded arena?

There are already many institutions dealing with questions of protection in most countries, but nearly all are sectorally oriented. They are a large part of the problem, and it is important not to add to their number.

The difficulties governments face in resisting protectionist pressures and in addressing the economy-wide issues involved in trade liberalisation stem, in part, from the fragmented structure of their bureaucracies. The attention of each tends to focus on industry-specific issues and problems when representations are made by 'client' industries experiencing competitive pressures. In this situation, there is an overwhelming concern with the visible short-term adjustment problems of specific industries, with little attention given to the less visible and longer-term implications for the economy as a whole of the policies they propose for dealing with adjustment problems.

It is for this reason that the Long Report recommended that an economy wide charter and perspective be written into the proposed arrangements for domestic transparency agencies. As noted in Chapter 6 of the present report, in most countries an existing institution could be identified as more appropriate than others

and given the economy-wide charter.

We can provide an indication of the budgetary cost of operating such an agency, compared with the cost of sectorally oriented institutions, by drawing on Australian experience. In 1988-89, the budget appropriations for the three largest sectorally oriented, industry policy institutions was 500 times greater than that for the IAC. In budgetary terms, it therefore represents a relatively small price for a large informational return.

Would not such an approach be slow in delivering trade liberalisation?

It has been proposed in order to correct the fundamental weakness of the present adversarial approach to multilateral trade negotiations. The test of its usefulness is not whether it will immediately move all countries to terminate protection, but whether gains are likely to result from international negotiations without the underpinning provided by domestic awareness of the costs within the subsidising countries.

If the Long proposal to strengthen the GATT system through domestic procedures were adopted, what would be the role for the 'Trade Policy Review Mechanism' agreed at the Mid-Term Review?

The answer depends on what Contracting Parties see as belonging to national policy on the one hand and the role of international co-operation on the other. The less transparent forms of protection that both (international and domestic surveillance) proposals are intended to bring to the negotiating table were in most cases introduced to avoid existing external disciplines. It seems unlikely that governments imposing them would welcome rigorous external surveillance of their policy conduct. Domestic transparency procedures are not intrusive; international surveillance procedures may, however, be viewed as intrusive.

If domestic procedures are to be preferred because they respect the hegemony of national governments over domestic policy, a very positive role for international co-operation (via the 'Trade Policy Review Mechanism') would be to service the technical needs of Contracting Parties wishing to establish domestic transparency procedures. Some of the technical tools used in measuring barriers and in analysing their domestic effects are covered in Appendix II.5 and II.6. There is considerable scope for the GATT to mobilize the technical resources needed to upgrade the capacity of the institutions which Contracting Parties nominate for the domestic transparency function. Each country could thus share the technical fruits of international co-operation, and develop their own domestic surveillance capability more quickly, without the prospect of having to 'give ground' to international bureaucrats on what domestic constituents may perceive to be domestic policy issues.

APPENDIX II - THE INDUSTRIES ASSISTANCE COMMISSION

1. THE COMMISSION'S CHARTER

The Industries Assistance Commission is established under legislation of Australia's Federal Parliament as an advisory body on industry assistance and related matters. The Commission has no judicial, administrative or executive functions relating to the provision of assistance to industries. The rationale for establishing the Commission and the philosophy of approach that should underlie its charter, functions and procedures were set out in a report that Sir John Crawford prepared for the Commonwealth Government (Crawford, 1973).

The main reasons Crawford advanced for establishing a Commission to advise on industry assistance were that it could:

- . assist the Government to develop co-ordinated policies for improving resource allocation among industries in Australia,
- . by virtue of its independence, provide impartial advice on those policies, and
- . facilitate public scrutiny of assistance policy formulation.

Crawford's report and recommendations provided the basis for the Industries Assistance Commission Act 1973. This Act

endows the Commission with such a broad charter that the Government can request the Commission to report on any form of assistance affecting resource allocation and on any industry or activity be it in the rural, mining, manufacturing or services sector of the economy. The IAC Act also specifies: policy guidelines within which Commission advice must be tendered; the Commission's reporting functions and public inquiry procedures; and the structure and distribution of responsibilities within its membership.

The Meaning of Assistance

All forms of industry assistance fall within the Commission's purview. Assistance is defined in the IAC Act to cover government action

"... by way of the imposition of duties or the doing of any other act that would in any way, directly or indirectly, assist a person to carry on a business or activity or confer a pecuniary benefit on ... a person in respect of the carrying on of a business or activity" [Section 4, IAC Act].

Much of the Commission's inquiry work has been directed to reviewing border assistance measures for individual industries - particularly tariffs, quotas and subsidies. However, the Commission's charter explicitly encompasses the wider array of measures by which governments seek to influence production and exchange decisions in the economy - especially through regulatory, taxation and purchasing policies.

Industry Coverage

The Commission's charter gives it an economy-wide mandate: "industry" is defined to cover primary, secondary, and services industries and includes any business or activity

concerned with or related to producing or supplying goods or services [Section 4, IAC Act].

Establishment of the Commission extended to all sectors of the economy an inquiry system already applying to import-competing industries.¹ The initial focus of the Commission's inquiry program was heavily influenced by the Tariff Review - the first systematic industry-by-industry program for reviewing assistance to manufacturing industry in Australia.² And from the mid-1970s, the Commission's inquiry work was increasingly directed towards manufacturing industries in competitive difficulties. Even non-industry specific references tended to be on forms of assistance principally associated with the manufacturing sector (eg export incentives, research and development grants, investment and depreciation allowances and Australia's by-law system of tariff concessions).

There were references on agricultural industries, some mining and petroleum industries (eg gold, copper and crude oil pricing), and a few service sector activities (eg, tourist accommodation and the performing arts). Nevertheless, the overriding perception is of an inquiry program dominated by the examination of assistance in less than a quarter of the Australian economy.

In spite of the Government's 1984 re-affirmation that the Commission's charter covered all sectors and that greater recourse would be made to the Commission in examining service sector activities, no new initiatives were forthcoming until 1987-88. With the ministerial responsibility for the Commission moving to the Treasurer in July 1987, new directions for the inquiry program were announced that relate

1 See Rattigan (1986) for an account of the operation of the Tariff Board and the basis its work provided for transformation into the Industries Assistance Commission.

2 The Tariff Review had been initiated by the Commission's predecessor, the Tariff Board, and had commenced in 1971.

the Commission's role to the overall operation of the economy.³ The new focus for inquiry activity was demonstrated by the broad ranging references forwarded during 1988 on government (non-tax) charges, international trade in services and the travel and tourism industries.

Guidelines

In his report leading to the establishment of the Commission, Crawford considered at length the question of whether to specify a policy framework for the Commission's operations. He concluded that some general guidelines should be provided and outlined the objectives to which the Commission could be directed to have regard:

"The purpose of listing objectives is to provide a settled policy framework for the Commission's work and advice. Because this advice will relate, in the main, to the long term development of industry, the objectives chosen for the Commission should be as relevant twenty years hence as they are today; and because the advice must be based on consideration of the interests of the community as a whole, and not on any particular section of it, the objectives specified must be widely accepted as relating only to settled and long term goals of national policy." (Crawford, 1973, p. 6.)

This approach was adopted and Section 22 of the IAC Act incorporates a general set of policy guidelines. Though the wording has been amended over the years, the focus on economy-wide considerations has remained: improving the efficiency with which the economy uses its resources, facilitating structural change in the economy and taking account of the interests of consumers and users.

3 Statement by the Treasurer on the Industries Assistance Commission, Press Release No. 7, 26 January 1988.

There is a large gap between the statement of such general objectives of economic policy and the formulation of advice to achieve these objectives. It was recognised at the outset that it would be necessary for the Commission to develop a consistent, industry-neutral framework in which to cast its advice on all forms of assistance to industries in all sectors of the economy (Crawford 1973, p. 7).⁴ The Commission has outlined its general approach to assistance issues in its annual reports (see Appendix II.4). In assessing and publicly explaining what changes in assistance would advance or retard the achievement of the Government's objectives, the Commission is helped by the professional and technical support provided by its staff.

The matters which the Commission is required to take into account in its inquiries and reports transcend sectoral boundaries. Since inquiries do not of themselves produce the required broad economic analysis, the Commission has to provide an analytical input to complement information obtained and analysed in particular inquiries. Such research is necessary to ensure that consistent criteria and principles are used in advising on assistance matters.

Reference of Matters to the Commission

Although any form of assistance may be referred to the Commission, there has been general acceptance by governments that, in the main, certain forms of assistance should not be changed before a Commission inquiry and report. Though not binding on the Parliament, this so-called "mandatory" provision covers import tariffs, import quotas and any financial assistance exceeding two years duration. Action necessary to implement bilateral or multilateral trade negotiations and developing country tariff preferences are exempt from automatic referral, and decisions on a Commission

4 See also the Prime Minister's Second Reading Speech on the IAC Bill 1973, Hansard, 27 September 1973, p. 1633.

report can be changed within 12 months of the receipt of the report. Legislation currently before the Parliament will widen the scope for administratively changing tariffs without first obtaining a report from the Commission.

In referring matters to the Commission, the Government notifies:

- . the subject for inquiry and report, including if necessary, additional policy guidelines and priorities,
- . whether the Commission is to formally proceed to detailing policy options and recommendations or provide an "information" report,
- . whether the Commission is to prepare and publish a draft report for public scrutiny before forwarding its final report to the Government, or after holding public hearings proceeds* directly to finalising its report,
- . whether the Commission can proceed to an early round of public hearings in advance of releasing a draft report or is confined to conducting hearings only after publishing a draft of its report, and
- . the reporting deadline.

General Reporting Function

In addition to reporting on the inquiry matters referred to it, the Commission has a more general function of reporting on the effects of the assistance structure. So far as is practicable, the Commission's annual reports are obliged to report on:

- . the assistance provided to industries and the effect of that assistance on the development of those industries,
- . the economic performance of those industries and the principal factors affecting that performance, and
- . the general effect of that assistance on the Australian economy.

Membership and Structure of the Commission

The 1973 Crawford report provided the basis for the structure of the Commission which is formalised in the IAC Act. Although some of his recommendations on membership were of a type that could not be included in the legislation, the report has nevertheless been accepted as providing the basis for selecting members and for structuring responsibility within the Commission.

Crawford suggested that members of the Commission should be appointed on the basis of their general competence to grasp the complexities of policy issues and not as representatives of particular interest groups in the community. In accordance with Crawford's recommendations, the Commission consists of two categories of membership - Commissioners and Associate Commissioners - with different responsibilities.

Commissioners

The IAC Act provides that the Commission consist of between 5 and 9 Commissioners (including a Chairman) who are permanent members with authority over the full range of matters dealt with by the Commission. In addition to inquiry work, these matters include the formulation and review of the Commission's operating framework, its procedures, and the preparation of the annual report. Commissioners are appointed for periods of up to 5 years at a time.

Although the Commission as a whole has sat on some inquiries, it is more usual for divisions to be formed to discharge the inquiry reporting function. The Chairman is nominally a member of every division but typically another Commissioner is delegated to preside over the inquiry, assisted by other Commissioners and/or Associate Commissioners.

Associate Commissioners

The IAC Act provides for the appointment of Associate Commissioners. Crawford saw Associates as a means for:

- . catering for considerable variations in workload over time without sacrificing the cohesion and consistency of approach possible with a small permanent membership, and
- . ensuring maximum flexibility for the Commission to attract well-qualified people who may be available only for the duration of one or two inquiries.

Associate Commissioners take no part in framing the principles and guidelines underlying the Commission's approach to its inquiry and general reporting functions - they have responsibility only in relation to the inquiry in which they participate. Although the Act provides for full-time Associates, such appointments are not conducive to varying the size of the Commission and its ability to respond to changes in workload. For some time, therefore, the emphasis has been upon the appointment of part-time Associate Commissioners for the duration of individual inquiries.

2. THE INSTITUTIONAL SETTING

References to the Commission and advice by the Commission to the Government are co-ordinated through a single Minister, currently the Treasurer. The scope of the Commission's charter extends across the portfolios of many Ministers, so there is a need to co-ordinate the initiation of inquiries, establish priorities for the inquiry program and ensure appropriate processing of Commission reports. The effectiveness of the Commission as a policy advisory body is very much influenced by the administrative machinery for co-ordinating departmental advice on matters within the Commission's charter.

Communication between the Government and the Commission

The IAC Act provides that all important communication between the Government and the Commission be public. Apart from matters publicly specified in references, there is explicit provision for the Government to publicly notify the Commission of additional policy concerns and priorities. The practice has been that any communication to the Commission conveying some view or policy is regarded by the Commission as public and is published in the appropriate report.

During the course of an inquiry, government departments and their various research bureaus can be active participants in the inquiry process itself - providing information, analysis and views on assistance options.

Consultation with departments can occur after the Commission's final reports have been forwarded to the Minister. The Commission is occasionally requested to respond to post-report queries, and sometimes, to

representations made outside the public hearing process. There is an expectation that exchanges of correspondence on such matters are made public. In January 1988, the Treasurer announced that the Government would make available, where appropriate, relevant submissions and any material put to it after a Commission report had been received.

Programming and Processing the Commission's work

In its first year of operation, responsibility for the Commission rested with the Prime Minister. The task of co-ordinating departmental proposals involving industry assistance and planning a program of references for the new Commission rested with a standing interdepartmental committee chaired by the Prime Minister's department. In subsequent years, ministerial responsibility for the Commission was transferred to a succession of industry-neutral portfolios. However, in early 1978 the chair of the interdepartmental committee reverted from an industry-neutral department to the particular department with primary responsibility for the industry matter under consideration. In March 1983, Ministerial responsibility for the Commission was transferred to the Minister for Industry and Commerce. From then on there was no formal, ongoing machinery to co-ordinate either a forward work program for the Commission or departmental advice on Commission reports.

In July 1987, the Commission was transferred to the Treasury portfolio. With this change the Commission again reports to an industry-neutral Minister and its references are linked to the work of the Cabinet Committee dealing with industry assistance matters. Nevertheless, on industry-specific matters industry Ministers and their departments continue to co-ordinate references and the consideration of Commission reports. The current inquiry program of the Commission consists predominantly of broad-ranging inquiries for which the Treasury exercises a co-ordinating role.

3. THE COMMISSION'S INQUIRY PROCEDURES

Initiation of Inquiries

The Minister responsible for the Commission initiates an inquiry by referring matters to the Commission for inquiry and report. These matters are specified in writing in a 'reference'.

In sending references to the Commission, the Ministers have often been acting in response to requests from particular industries experiencing adjustment problems. In other instances, the reason for sending references is related to the Government's need for information and advice in reviewing its policies. For example, in the 1970s a program of inquiries was held to review assistance to manufacturing industries, while in the 1980s major inquiries were held on textiles, clothing and footwear, chemicals, and several other major manufacturing and rural industries. Current inquiries on government charges, trade in services and tourism are associated with the Government's micro-economic reform objectives.

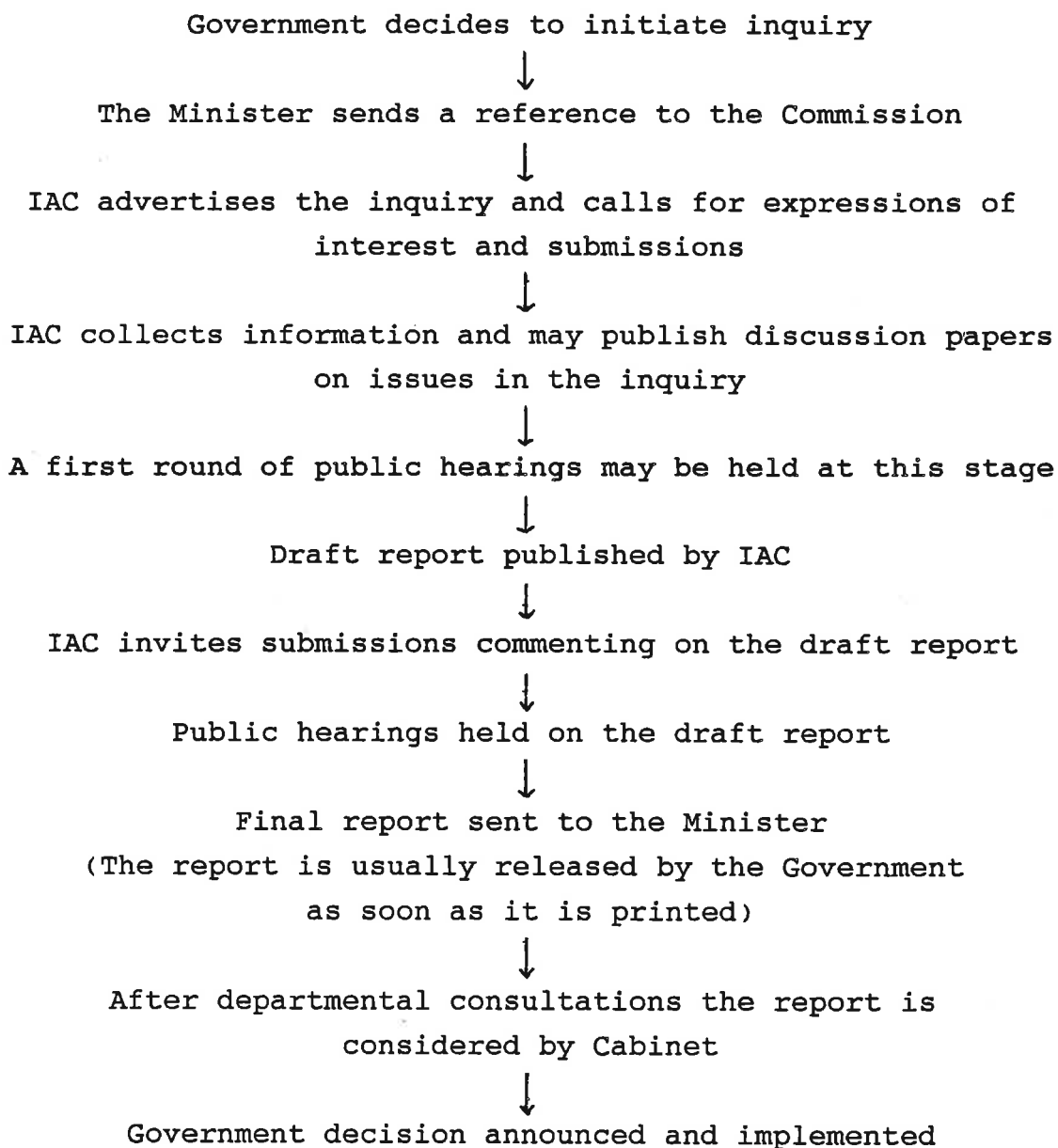
The range of inquiries conducted by the Commission is illustrated by the following list of reports published in 1987-88:

- The Tobacco Growing and Manufacturing Industries,
- Razors and Razor Blades,
- The Rice Industry,
- The Customs and Excise Bond Systems,
- Transport Containers,
- Fresh Fruit and Fruit Products Industries,
- The Wheat Industry,

Precious Metals, Gems and Jewellery,
Mining, Construction and Agricultural Equipment,
Ships, Boats and Other Vessels, and
Coastal Shipping (draft report)

The stages in a typical inquiry are outlined in Figure 1 and described in the following pages.

Figure 1 : Stages in IAC Inquiry Process



Preliminary Stages of Inquiries

After it receives a reference, the Commission advertises in the press and in the Commonwealth Gazette the commencement of the inquiry and calls for any person or organisation with an interest to notify it. The Commission distributes a circular giving details of the reference to industry organisations, trade unions, domestic producers, importers, users and others likely to be interested in participating in the inquiry. The circular gives names and telephone numbers of staff who can answer questions about the inquiry. Those expressing interest receive all subsequent circulars relating to the inquiry.

For many inquiries the Commission distributes information and discussion papers which focus attention on matters specified in the reference and on issues which the Commission considers to be particularly relevant. They also include information available from official statistics and other sources. The aim is to help interested parties to present submissions, and to stimulate discussion on the issues likely to arise in the inquiry.

Early in the life of the inquiry, the Commission seeks written submissions from interested parties. They are asked to comment on the matters covered by the inquiry and to put forward proposals and to advance reasons in support of those proposals. Commission staff are available to discuss any problems encountered in preparing submissions. The Commission may accept information in confidence where it is satisfied that it would be in the public interest to do so.

Circulars listing participants' submissions are forwarded to all interested parties, who have access to or may buy copies of non-confidential sections of submissions through the Commission.

The Minister may authorise public hearings prior to the

release of the draft report should the timing or other aspects of a particular inquiry warrant. Such hearings provide an opportunity for participants to voice concerns, advance suggestions and to respond to issues raised by the Commission. The hearings also provide an incentive for participants to present written submissions early in the life of an inquiry. This assists the Commission in its preparation of a draft report and enhances public scrutiny of the information, analyses and views put forward during the course of an inquiry.

Draft Report

The draft report is based on written submissions, official statistics and information gathered by the Commission. Investigatory work may include visits to industry and informal discussions with organisations and individuals with an interest in the inquiry. The Commission seeks to ensure that a cross-section of activity and views are considered. However, such contacts are not a substitute for written submissions and attendance at the public hearing which allow other interested parties to be aware of, and comment on, views expressed.

The draft report is distributed to participants and to the press free of charge, and is available to the public on request. It gives interested parties an opportunity to examine the Commission's analysis and discussion, and to offer comment either through written submissions or at a subsequent public hearing. The draft report usually discusses options for action that are being considered and proposes a course of action that the Commission considers to be the most advisable. Following the release of the draft report, views which participants wish the Commission to consider in formulating its final report are presented at a public hearing.

Public Hearings

Any person, company or organisation may participate in a public hearing. There is no legal representation or cross-examination by other participants. An oath or affirmation is not required, but the IAC Act specifies that a person shall not give evidence that the person knows to be false or misleading. Participants are encouraged to submit written submissions well in advance of the public hearing so that the Commission has time to consider their arguments and requests. At the hearing, participants are usually asked to read or to speak to the main parts of their submission and to respond to Commissioners' questions.

Attendance at a public hearing by those presenting submissions is not compulsory. However, the hearing serves an important function in allowing elaboration and clarification of submissions and in ensuring public awareness of relevant issues. The Commission therefore encourages participants to present their submissions at the public hearing.

The dates and places of public hearings are notified in circulars distributed to interested parties, and are advertised widely in the press. Public hearings are usually held in centres convenient for most participants. For a small inquiry they may be held in a single centre and may last no longer than a day or two. Hearings for a large inquiry may be held in several centres and extend over several weeks.

The proceedings are recorded. Transcripts are available for people to read and may be purchased through the Commission. Transcripts do not contain the written submissions presented at the hearing. However, the transcript may include a brief summary statement if this is provided by the participant.

The conclusion of the draft report public hearings usually

marks the end of direct involvement in an inquiry for most participants. However, some participants may be asked to provide additional information, and anyone may comment on the submissions of other participants. The Commission then prepares a final report.

Final Report

After the Commission has concluded its inquiry the report is signed and is forwarded to the Minister. After consultation within Government, final consideration is undertaken by Cabinet. The Government has stated that it intends, on most occasions, to publish the Commission's final reports before a Government decision is taken. The Government also has indicated that it is prepared to make publicly available, where appropriate, any relevant submissions and material put to it in relation to IAC recommendations after a report has been received.

4. THE COMMISSION'S GENERAL REPORTING FUNCTION

Approach to Annual Reporting

As noted in Appendix II.1, the Commission must report annually on assistance to industries, its effects on the Australian economy and factors affecting the performance of industries.

In practice the Commission has usually chosen to report on different factors affecting Australian industries in each year. A more comprehensive statistical account of assistance to industries has been provided in most years in appendices to the annual report, or in separate information papers.

The First Annual Report

The Commission's first annual report, for 1973-74, was a landmark document because it set out plainly the Commission's perception of its role and its approach to industry assistance. In most respects, what the Commission had to say in its first annual report remains relevant to its operations today.

The following quotes on selected aspects are illustrative of the approach taken:

Role of the Commission

"In summary, the Commission's role is to advise the Government on how individual industries, and industry in general, should be encouraged to develop in Australia. In providing this advice, it is required to have regard to the interests of the community as a whole, and relate

its advice to the generally accepted economic and social objectives of the community. The Commission is concerned primarily with the long term development of industries, rather than with the fluctuations which may occur in their rate of development from one year to another, due to temporary changes in their business environment. The principles and objectives in the Industries Assistance Commission Act provide the general policy basis for the long term development of Australian industries." (IAC, 1974, p. 3.)

Significance of Relative Levels of Assistance:

"It is important to realise that although many industries in Australia appear to receive some assistance - because they have positive nominal or effective rates - some are really being penalised by the present structure of assistance. The fact that a particular industry is afforded a rate of assistance greater than zero means little; what is more significant is its effective rate of assistance relative to that of other industries. Assistance does help an industry to meet competition from other industries, usually in overseas countries, which make products that are similar to, or substitutes for, its own products. But more fundamentally, assistance helps an industry to obtain the inputs of materials, capital, and labour which it requires, and must bid for in competition with other potential domestic users of those resources. If an industry is given a high effective rate of assistance, it is being helped at the expense of industries with lower rates of assistance." (IAC, 1974, p. 12.)

Meaning of Economic Efficiency:

"...`efficiency' includes much more than the technical efficiency with which particular production is undertaken - as measured by output per machine hour or per acre.

For instance, the factories or farms in an industry might be managed in a way which is technically very efficient. But their use of the community's basic resources would nevertheless be inefficient from the community's point of view, if their production were relatively unsuited to local conditions - that is, to the general production and marketing environment and the resource endowment of Australia - and thus required relatively high levels of public assistance to support it.

... When the Commission is assessing the efficiency of a particular industry, it must therefore be concerned primarily with the industry's economic or relative efficiency; that is, it must have regard to the way other industries throughout the economy might use the basic resources which are employed in that industry. If the resources employed in one industry yield more real wealth for the community than they would if employed in another industry, that first industry is using the community's resources more efficiently than the second industry." (IAC, 1974, p. 17.)

Relationship Between Economic Efficiency and Relative Assistance Levels:

"The less the production of particular goods is suited to local conditions, the more likely it is that the producers of those goods will want assistance to compete with producers in other countries, where conditions are more suited, relatively, to producing the goods concerned. Thus as a general rule, the higher the long term level of assistance required by an Australian industry to enable it to compete profitably in the markets for its products, the lower the relative efficiency with which the industry uses the community's resources. It follows from this that actions which encourage the use of a higher proportion of resources in

industries which require relatively low levels of assistance, or none at all, will tend to improve the general efficiency with which the community's resources are used." (IAC, 1974, p. 17.)

General Strategy Proposed:

"The approach which the Commission has proposed will involve a gradual reduction of levels of assistance which are relatively high - rather than raising those which are relatively low." (IAC, 1974, p. 22.)

Some Themes in Subsequent Annual Reports and Discussion Papers

The themes developed in subsequent annual reports and discussion papers reflect both the Commission's perception of its role, as concerned with the long term development of industries, and the issues which happened to be relevant or topical at the time. A brief outline of some themes of enduring interest is provided below.

Structural Change

The Commission saw the development of an improved public understanding of structural change as having a high priority throughout the 1970s. This is reflected in several annual reports and in a series of discussion papers published in 1977 (IAC, 1977 a, b and c).

Particular issues explored included: the causes of structural change in the Australian economy; the relationship between growth in employment and structural change; the extent to which macro-economic problems of the 1970s could be attributed to structural change; the effects of reductions in industry assistance; the concept of a "back-log" of structural change associated with provision of increased assistance to uncompetitive activities; the implications of

interdependence between various sectors of the Australian economy; and the circumstances under which provision of various forms of adjustment assistance might be warranted.

Australia's Participation in the World Economy

The Commission saw the development of a more outward-looking approach as being essential to Australian industry development.

Particular issues explored included: the extent to which Australia's trade performance differed from that in countries of comparable size; the opportunities for development of trade with rapidly growing countries in Asia; and the implications of Australia's trade and protection policies.

Role of Transparency in Industry Assistance Reform

This theme was developed most fully in the Commission's 1984-85 annual report. The report made the following points:

- . The Government's objectives of restructuring Australian industry to improve its international competitiveness and opening the international trading environment are "two sides of the one coin". International trade distortions are a product of national governments reacting to the problems of domestic industries.
- . Since industry restructuring must proceed on the basis of public understanding of what is at stake, a means must be found to service the community's information needs over the range of choices involved in industry development. Decision-making can then reflect informed public choices about the trade-offs involved.
- . The trade-offs which arise in pursuing industry and trade objectives are between particular domestic

interests and collective domestic welfare. It is important to develop a public understanding of what is at stake in these trade-offs.

Impediments to Development of a More Competitive Industry Structure

In recent annual reports the Commission has developed the theme that impediments to a more adaptable industry structure include the accumulation of decisions by governments to shield particular industries from competitive pressures. They also include less visible, more pervasive, influences in the economic environment, such as the accumulation of regulations and institutionalised arrangements. The general effect has been to make the economy less flexible and to support a 'quiet life' for uncompetitive activities, managements, technologies and work practices.

In its most recent annual report the Commission noted the substantial micro-economic reforms announced by the Government in May 1988 and argued that reform needed to be seen as an ongoing process. This is because the range of impediments to competitiveness throughout the economy is extensive and because there will always be an incentive for vested interests to seek preferment at the cost of the wider community. The Commission re-emphasised that "if continuing progress is to be made, community understanding of what is at stake will be very important" (IAC, 1988, p. 4). Public inquiries were advanced as means of uncovering information about the nature of impediments to efficiency and competitiveness and developing the economy-wide perspective that is a prerequisite for beneficial reforms.

5. MEASUREMENT OF ASSISTANCE TO INDUSTRIES

The Purpose of Assistance Measurement

Assistance measurement is undertaken to help the Australian community to make better decisions about industry assistance.

Information on a comparable basis on how much assistance is received by individual industries helps to make the assistance structure more transparent. This knowledge has had a direct influence on the behaviour of industry organisations. Industries which receive little or no assistance have frequently questioned the provision of high levels of assistance to other industries and in recent years have had some success in modifying government policies adopted towards highly assisted industries.

Assistance measurement also provides information which is necessary to enable those advising the government to assess whether policies towards individual industries are contributing to efficiency of resource use. In order to understand the implications of changing assistance to particular industries it is necessary to have knowledge of assistance provided to other industries which are competing for the use of resources.

The approach to assistance measurement adopted by the Commission recognises that this is an area in which perfect knowledge will never be attained and that government policy development is an ongoing process. The Commission's aim is to prepare and publish the most relevant information in as timely a manner as possible.

The main focus of assistance measurement in the Commission has been on manufacturing and agriculture but some work has been published in the mining sector and some preparatory work has been undertaken to consider whether assistance measurement can be extended to the services sector.

What Measurement Involves

Assistance measurement is one aspect of the Commission's research which aims to provide a better understanding of industry assistance and other government instruments that influence the incentives faced by industry. Economic modelling to assess the effects of assistance on output, employment etc at an economy-wide level is discussed in Appendix II.6. This modelling work makes use of information produced in the assistance measurement process.

Measurement involves:

- . qualitative analysis - identifying and classifying interventions providing assistance and describing the incentives they provide; and
- . quantitative assessment of industry incentives and weighting together measures of price distortion to obtain comparable averages for different industries, etc.

The identification, classification and description of incentive measures enables an assessment of the nature and implications of the incentive structure. Assessment of the effects of some forms of assistance on expectations and behaviour of firms may sometimes be just as valuable as the measurement of assistance provided. For example, assistance which is provided under a scheme that underwrites per unit producer returns may have a significant effect on investment

decisions even if the measured level of payments turns out to be low in the period under consideration.⁵

The qualitative stage in assistance measurement sometimes leads directly to more complete micro-economic analysis of the effects of government interventions. In such micro-studies attention may be given to the incentives which particular forms of assistance provide for production of one type of good rather than another; use of a particular technology (new/old, small scale/large scale, etc); managerial inefficiency; expansion of bureaucratic controls; and for investment to be undertaken in the expectation that assistance will be available if needed.

The main focus of assistance measurement in the Commission has been on quantifying the assistance provided by different policy instruments - tariffs, quantitative restrictions, etc - and aggregating them on a comparable basis to obtain estimates of the average level of assistance for various industries and sectors.

Some Concepts Used in Measurement

The Commission's assistance measurement has been based largely on the effective rate of assistance (ERA) concept (an extension of the effective rate of protection). One of the appealing aspects of the effective rate concept is its relative simplicity and ability to incorporate diverse forms of assistance into a summary measure.⁶

5 The assistance provided in this instance could in principle be measured by the annual premium which would have to be paid to obtain this insurance through market transactions.

6 For a more complete discussion of methodology, see IAC (1985).

The ERA measures the initial impact of assistance arrangements on industry incentives and is not intended to take into account the supply/demand responses which assistance arrangements induce throughout the economy, or the effects on world trade volumes and prices.

The ERA concept views production in the economy as being composed of discrete activities/industries which are influenced by the combined effects of all government assistance. The ERA is concerned with the measurement of the initial impact on prices of all government assistance that directly affects each activity/industry.

To simplify such measurement, the following assumptions and measurement conventions are used:

- . For each tradeable good produced locally there exists a perfect substitute available from world trade.
- . In the absence of assistance, domestic prices of tradeable goods would be set by world trade prices. For import-competing goods, domestic prices would be import-parity prices approximated by the landed-duty-free (ldf) or cost-insurance-freight (cif) price of competing imports. For goods exported, domestic prices would be export-parity prices approximated by export returns equivalent to the domestic wholesale price.
- . The direction of trade in the absence of assistance can be assessed. Usually this is further simplified by assuming that import-competing goods remain import-competing and that goods exported continue to be exported.
- . The production relationships between inputs, between outputs and between inputs and outputs for each

activity remains unchanged by the structure of assistance.

The above assumptions and conventions considerably reduce the data required to enable the different forms of government assistance to be measured on a consistent basis. They allow the difference between actual returns to value-adding factors and equivalent 'world-trade' returns to be used to measure the initial impact of government assistance on each activity/industry.

Trade barriers are usually applied to internationally traded goods and services in order to selectively assist the domestic activities which produce them. Assistance to domestic industries need not, however, take the form of a border barrier. The assistance may result from government interventions such as subsidies or purchasing preferences that reduce the level of trade (and the gains from trade) without physically restricting entry of foreign products.

The ERA framework explicitly recognises this connection between obstacles to trade and other forms of assistance to domestic productive activities by including the direct effects of all interventions that assist domestic activities. Specifically, the ERA incorporates the separate impact of government interventions which assist:

- . returns from outputs,
- . the use of materials, and
- . value added.

The two most widely used measures are the nominal rate of assistance which measures the assistance provided to outputs and the effective rate of assistance which measures the net assistance to an industry's value added.

Output Assistance

Various forms of assistance to outputs, such as tariffs, production subsidies, import quotas, voluntary export restraints, and purchasing preferences increase the gross receipts of producers.

The direct impact of government interventions on the gross returns from production may be expressed as a rate or as its equivalent lump sum.

The nominal rate of assistance on outputs or products (NRP) is the percentage change in gross returns per unit of output relative to the (hypothetical) situation of no assistance.

Where assistance is in forms which increase producers' returns by raising prices (such as tariffs, import quotas and, in some years, domestic pricing arrangements), the nominal rate on outputs will be the percentage change in domestic price. However, the nominal rate also includes other forms of assistance (eg, production subsidies) which raise producers' returns without increasing prices paid by consumers and user industries. The nominal rate is given by:

$$\text{NRP} = \frac{(\text{AP} + \text{Sp} - \text{UP})}{\text{UP}} \times 100 ,$$

where

AP = value of output,

Sp = subsidies on output, where not included in the value of output, and

UP = unassisted value of output (ie the estimated value of output without assistance).

The gross subsidy equivalent (GSE) expresses the nominal rate on output in money terms by estimating the change in producers' gross returns from assistance. It is the notional amount of money, or subsidy, necessary to provide an industry

with a level of assistance equivalent to the nominal rate of assistance on its output. The gross subsidy equivalent is given by:

$$\text{GSE} = \text{AP} + \text{Sp} - \text{UP} .$$

Input Assistance

Input assistance changes the prices paid by user industries for inputs. Like output assistance, the separate impact of government intervention on the activity's cost of materials may be expressed as a rate or its equivalent lump sum.

The nominal rate of assistance on materials (NRM) is the percentage change in the prices paid for materials used in the production process resulting from government intervention.

For example, tariffs and excise taxes on intermediate inputs penalise user industries by raising prices while subsidies assist user industries by lowering prices. Unlike the nominal rate of assistance on outputs, the nominal rate on inputs excludes those forms of assistance (eg production subsidies) which benefit the production of intermediate inputs without affecting prices paid by user industries. The nominal rate is given by:

$$\text{NRM} = \frac{(\text{AM} - \text{Sm} - \text{UM})}{\text{UM}} \times 100 ,$$

where

- AM = value of material inputs used in the production activity,
- Sm = subsidies on inputs, and
- UM = unassisted value of material inputs (ie, the estimated value of material inputs without assistance).

The tax on materials (T_m) is an estimate of the net change in costs to user industries due to government intervention altering the prices paid for intermediate inputs. It is the notional amount of money equivalent to the nominal rate of assistance on materials. The tax on materials is given by:

$$T_m = AM - S_m - UM .$$

Value Added Assistance

Value added is the net return to the primary or value-adding factors (land, labour and capital) after deducting from gross returns the cost of material inputs used in the production activity.

Assistance to value added can be measured as either a rate or as a lump sum.

Direct assistance to value-adding factors (S_{va}) is an estimate of the sum of money equivalent to any direct subsidies that increase the return from the use of value-adding factors in a particular activity: for example, special income-tax concessions to an industry or select group of industries.

The effective rate of assistance (ERA) is the percentage change in returns per unit of output to an activity's value-adding factors due to the entire assistance structure. It measures net assistance to an activity by taking into account not only assistance to output and value-adding factors, but also the penalties (eg tariffs and excise taxes) and benefits (eg input subsidies) of government intervention on inputs. It is given by:

$$\begin{aligned} ERA &= \frac{AVA - UVA}{UVA} \times 100 \\ &= \frac{[AP - AM + S_p + S_m + S_{va}] - [UP - UM]}{[UP - UM]} \times 100 , \end{aligned}$$

where

AVA = value added with assistance, and
UVA = value added without assistance.

The net subsidy equivalent (NSE) is an estimate of the change in returns to an activity's value-adding factors due to assistance. It is the notional sum of money, or subsidy, necessary to provide a level of assistance to an activity equivalent to its effective rate of assistance.

The NSE is the gross subsidy equivalent plus assistance to value-adding factors, minus the tax on materials. It is given by:

$$\text{NSE} = (\text{AP} + \text{Sp} - \text{UP}) - (\text{AM} - \text{Sm} - \text{UM}) + \text{Sva} .$$

Criteria for Assessment of Changes in Assistance

It is dangerous to base assessments of changes in the structure of assistance on trends in averages. One commonly used indicator in international negotiations - average (import-weighted) tariff rates - ignores non-tariff assistance, and may give the misleading impression that assistance is falling if certain tariffs are raised to the point where they become prohibitive; it also gives the impression that assistance is falling if tariffs are reduced on imported inputs for which there are no domestically produced substitutes.

Reliance on movements in more sophisticated averages such as the (production weighted) average effective rates of assistance for manufacturing and agriculture can also provide a misleading impression. Reductions in the average effective rate of assistance may occur, for example, as a result of a decline in assistance to lightly assisted activities which are relatively efficient users of resources. The net result

can therefore be a worsening in the allocation of resources despite a reduction in average assistance levels.

Factors considered by the IAC to assess whether or not changes in the structure of assistance are consistent with more efficient resource use include:

- . whether disparities in assistance have been narrowed;
- . whether the scope for increases in assistance to occur in response to declines in the competitiveness of industries has been reduced; and
- . whether the complexity of the assistance structure has been reduced and its transparency enhanced.

Disparities in assistance relate to the extent to which assistance levels vary between activities. It is important to focus on disparities because equal assistance to all industries may be broadly equivalent to no assistance. With equal assistance to all, the assistance provided to one industry would tend to cancel out the effects of assistance provided to other industries. However, where there are substantial disparities, some industries are being advantaged relative to others in their access to resources.

The Commission's concern about the responsiveness of the assistance structure to the needs of industries with declining competitiveness is in recognition that adjustment to changes in the trading environment is necessary if the economy is to grow. Governments often have to choose between policies which promote a flexible industry structure that adapts to changing market opportunities, and policies which maintain an inflexible industry structure - less capable of growth. When producers ask governments to shield them from changes occurring in their trading environment they are asking governments, in effect, to adopt an incentives policy that will detract from the growth of the economy as a whole.

The Commission's concern about the complexity of the assistance structure arises because some forms of assistance are inherently less transparent than others - the assistance delivered under some non-tariff barriers is less visible to the public, or more difficult to measure. The greater the complexity of the assistance structure, the more difficult it is for industry groups and consumers to assess whether they are being assisted or disadvantaged by particular instruments.

Within an assistance structure which is complex and lacking in transparency it is often relatively easy for interest groups to obtain preferment through the application of technical rules such as those associated with tariff classification and anti-dumping action. In some instances, laws are expressed in sufficiently vague terms that they can be agreed to be in the public interest, but the executive is given enormous discretionary power to take care of the details. Arrangements which involve the exercise of substantial administrative or ministerial discretion are particularly likely to encourage firms to devote resources to making representations to have technical rules interpreted more favourably from their point of view.

Making the assistance structure more transparent has the added advantage of helping governments to make better-informed policy choices. It will often not be possible to assess whether changes towards a more simple and transparent form of assistance will directly improve community well-being. However, movement toward a less complex assistance structure makes it possible for more reliable assessments to be made of whether subsequent changes to the assistance structure are likely to encourage the movement of resources from uncompetitive to competitive activities.

Agenda for Assistance Measurement in the IAC

The Commission has developed a reasonably comprehensive picture of industry-specific Commonwealth assistance to manufacturing and agriculture.⁷ Apart from this, there are substantial gaps in knowledge of all aspects of the incentives environment. Although work on many aspects of government intervention in Australia has been undertaken within other organisations, there has been no systematic attempt to assess the industry incentives involved.

Early in 1988, the Commission released a discussion paper on the effects of government intervention in the mining sector (IAC, 1988a). The paper explored the conceptual issues in the measurement of assistance to mining and examined the availability of the data required for a comprehensive study of the effects of intervention by both the Commonwealth and States on that sector's contribution to national wealth. In 1988, the Commission also published its first attempt to measure the assistance from State budgetary outlays directed to agriculture (IAC, 1988b).

Regulatory barriers to competition - both international and domestic - were identified by the Commission in its 1984-85 annual report as an aspect of the incentive environment subject to substantial information gaps. Regulatory barriers were also identified as potential sources of disparities in assistance, with implications for efficiency of resource use throughout the economy. For example, inefficiency in service sector industries associated with cross-subsidisation of uneconomic activities within public authorities, was observed to be supported by regulatory restrictions on domestic competition.

7 The most recent results of this work are published in the Commission's 1987-88 annual report.

The Commission's current inquiries on International Trade in Services and on Government (Non-Tax) Charges require it to assess many issues related to regulatory barriers to competition. In its 1987-88 annual report, the Commission noted that these inquiries were posing special problems in terms of measurement:

"In its traditional areas of inquiry - traded goods industries - the Commission has used disparities in assistance as indicators of efficiency in resource use. There have been relatively few practical qualifications to the observed inverse relationship between economic efficiency and levels of assistance. Moreover, for the products of the manufacturing and agricultural industries there are generally observable world prices which can be used as benchmarks in evaluating the effects of government intervention and measuring assistance.

Measurement is more difficult in the services sector. The relationship between efficiency and assistance may be less robust; the information base is more limited; and there is also the problem of determining a benchmark against which to measure assistance. For non-traded services, such as those provided by many public utilities, there is no world price against which to measure assistance. For some traded services world prices are available, but measurement problems are still profound." (IAC, 1988c, p. 18.)

Where there is no world price benchmark readily available, the only way to progress in measurement of the effects of regulatory or institutional arrangements is through comparison of the performance of industries and enterprises under different arrangements. This is involving more emphasis on comparison of the performance of service sector industries in different States within Australia as well as attempts to compare performance of those industries in countries which have different regulatory arrangements.

6. ANALYSIS OF ECONOMY-WIDE EFFECTS OF INDUSTRY ASSISTANCE

The Purpose of the IMPACT Project

The IMPACT Project was initiated by the Commission, soon after its establishment in 1974, to extend and upgrade its capacity to assess the intersectoral and economy-wide effects of changes in industry assistance and other factors such as demographic change. The Project is supported by several Commonwealth Government agencies and universities in addition to the IAC. Some of the models developed have been widely used, both in the public and private sectors.

The Project was designed to provide a consistent analytical framework and data base to be used for policy analysis across a number of fields and to assist in co-ordination between policies (Powell, 1977, pp. 1-3).

The ORANI model, developed as part of the IMPACT Project, has been extensively used by the Commission. The aim of the model was to analyse industry assistance, trade and development issues within a comprehensive, economy-wide framework. That is, it was designed to provide information on the impact of policy and other changes on directly-affected industries, on other industries and on the economy as a whole.

Characteristics of the ORANI Model

ORANI is a large-scale, multisectoral, general equilibrium model of the Australian economy. It is large in scale because it embodies considerable detail on supplies and demands in the economy. It is multisectoral in that it treats the economy as a complete system of interdependent

industrial sectors. The model identifies direct and indirect links between industries.

'General equilibrium' reflects the attention given to the structural detail of the economy, the inter-relationships between both product and factor markets, and to the notion of equating demands and supplies in those markets.

The model presents comparative static results. ORANI is assumed to be in equilibrium before any changes are introduced. The results assume sufficient time is allowed for the economy to return to an equilibrium state after the changes have occurred. Short- or long-run equilibria can be defined, depending on what is assumed about changes in industries' capital stocks, and adjustments in other markets.

The simulation results of any quantitative model, such as ORANI, reflect a combination of two key components: its data base, and the theoretical structure embodied in its system of equations that describe how various economic decision-makers react to changing circumstances.

The ORANI data base is built around the Australian Input-Output Tables. The model reflects conventional microeconomic theory. In essence, the model portrays producers as seeking to minimise costs (within certain constraints), while consumers (again, within limits) maximise utility.

The model is extremely flexible because it is solved linearly. It contains more variables than equations. The model user chooses which variables are to be exogenous (not determined by the model). This decision is important since it specifies the economic environment under which the simulation is conducted. For example, with real wages assumed to be constant the model can be used to simulate the effects of policy changes on aggregate employment. Alternatively, with aggregate unemployment assumed to be

constant, the model can be used to simulate the effects of policy changes on real wage levels.

Use of ORANI in the IAC⁸

The value of the ORANI model is that it provides a framework for analysing important elements of an issue, rather than a definitive answer. It organises a large body of information in an explicit, systematic way. Modifications can be introduced to enhance the model's suitability for analysing special features of particular industries and/or policy issues. Since the model is laid open for scrutiny, discussion about the appropriateness of ORANI analysis can focus on particular elements of data or particular assumptions as warranting further attention. The important point is that there is a comprehensive and cohesive framework upon which to build improvements and within which to test alternative views.

The ORANI framework is especially suited to the analysis of 'what if ...' questions. That is, the basic methodology of ORANI simulations corresponds to saying, 'In a given economic environment which abstracts from the multitude of other factors that could affect industry performance, what if (say) tariff assistance to industry X were changed by Y per cent?' The type of answer provided would not be a forecast of the actual outcome (since this could be influenced by many other factors) but would be a conditional projection of the influence of that policy change alone. 'Forecasts' are, however, also possible if the user can specify likely values for all of the exogenous variables.

The Commission has always seen that an integral part of its work is to provide information on the effects of assistance to industries and changes in these assistance arrangements.

8 A more extensive discussion of the IAC's use of ORANI is contained in IAC (1987c).

Perhaps the most comprehensive discussion of the Commission's approach to reporting on effects of changes in assistance was provided in its 1979-80 annual report. It stated that analysis of three aspects of effects can be influential in the formulation of the Commission's recommendations - although the extent of influence of each varies according to the circumstances of individual inquiries. The three types are:

- . consideration of effects of assistance changes in isolation from other developments in the economic environment;
- . assessment of effects from the perspective of the longer-term economic and social environment in which the policies would operate; and
- . analysis of the short-term consequences of moving from the existing to proposed levels of assistance.

The ORANI model can provide helpful insights into each of these assessments.

The Commission also emphasised the importance of taking an economy-wide approach to the assessment of effects and a balanced reporting of potential gains and losses for various groups in the community.

Where appropriate, the Commission has used other analytical frameworks in place of or to supplement the ORANI model. For example, the Commission has used world commodity trade models such as the World Food Trade Model in some inquiries. Irrespective of the extent of quantitative analysis in particular cases, the formulation of a policy recommendation continues to require the exercise of considerable judgment.

Agenda for Further Development of Quantitative Analytical Frameworks

The participating Commonwealth agencies and academic institutions reached agreement in mid-1988 for a further three years of development of the IMPACT project. Topics for the current round of further theoretical development include: integration of modern investment theories into applied general equilibrium analysis; incorporation of financial and monetary variables into applied general equilibrium analysis; and detailed work on economy-wide implications of restructuring of industries in which scale economies are important. The implications of scale economies is a topic of particular interest to the Commission.

In many of the industries currently under review by the Commission pricing is conditioned to varying extents by monopoly powers, community service obligations and other features inconsistent with the assumption of perfectly competitive behaviour. The Commission plans to give high priority to consideration of how alternative pricing behaviour might be incorporated in the ORANI model.

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