

NEW ZEALAND – CHINA FREE TRADE AGREEMENT

(AND ASSOCIATED INSTRUMENTS)

NATIONAL INTEREST ANALYSIS

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EXECUTIVE SUMMARY

(i) Background

New Zealand and China signed the New Zealand–China Free Trade Agreement (FTA) in Beijing in April 2008. The two countries have also concluded an Environment Cooperation Agreement (ECA) and a Memorandum of Understanding on Labour Cooperation (MOU). Subject to ratification, the agreements are expected to enter into force by 1 October 2008.

The New Zealand Prime Minister Helen Clark and the Chinese President Hu Jintao announced the commencement of negotiations on the FTA at the APEC Leaders meeting in Santiago, Chile in November 2004. This announcement followed completion of a Joint Study Report¹, which concluded that a high quality FTA could be expected to deliver positive benefits for both countries.

The first round of negotiations was held in December 2004. Negotiations continued over 15 rounds, held in both China and New Zealand. The negotiations concluded substantively in Beijing in December 2007.

This National Interest Analysis (NIA) assesses the FTA, ECA and MOU from the perspective of their impact on New Zealand and New Zealanders. The three agreements are considered as part of the same NIA given that they were negotiated at the same time and the existence and purpose of the ECA and MOU are referenced in the FTA. The NIA does not seek to address the impact of the agreements on China.

(ii) Reasons for New Zealand to become a party to the treaties

The main values for New Zealand in entering into the FTA and associated instruments are:

- Increased access for New Zealand trade and investment, which will contribute to growth, jobs and higher living standards
- The framework the FTA establishes for resolving trade and investment issues that may arise in the future
- The framework established by the MOU and the ECA for discussing and cooperating on labour and environment issues
- The support the treaties give to New Zealand's objective of broadening and deepening relations in Asia and with China in particular²
- The support the FTA gives to New Zealand's wider trade policy interests in strengthening economic integration in the Asia-Pacific and multilaterally
- The FTA's assistance in raising the commercial profile for New Zealand companies in China.

¹ *A Joint Study Report on a Free Trade Agreement between China and New Zealand*, Ministry of Commerce, China and Ministry of Foreign Affairs and Trade, New Zealand, 2004.

² As outlined in the 2007 White Paper *Our Future with Asia*, the Government supports regional integration in Asia and sees it as a big opportunity for New Zealand's economic transformation and for linking New Zealand's growth to the growth of Asian economies. *Our Future with Asia* is available on the MFAT website (www.mfat.govt.nz).

(iii) Advantages and disadvantages to New Zealand in becoming a party to the treaties

Advantages

New Zealand will benefit from the removal over time of tariffs on 96 percent of New Zealand's current exports to China, which will equate to an annual duty saving of NZ\$115.5 million based on current trade.

For New Zealand goods exports that meet the required rules of origin, market access gains include:

- On entry to force, tariffs on over NZ\$200 million worth of New Zealand's exports will be eliminated
- Over the first 5 years, China's tariffs on NZ\$621 million of current exports will be eliminated including infant milk formula, casein, frozen fish, frozen fish fillets, methanol, animal fats & oils, apples and wine
- Over the first 9 years, China's tariffs on NZ\$77 million of current exports will be eliminated, including beef and sheep meat, edible offals, sheepskins and kiwifruit
- Creation of a country-specific tariff quota for New Zealand wool, which will provide initial duty free entry for approximately 75 percent of average annual exports in the 2004–2006 period
- By the end of the tariff phase-out period, tariffs on all but \$80 million of current trade will have been eliminated.

New Zealand will benefit from China expanding its commitments in services including in education and environmental services.

New Zealand will also benefit from provisions to facilitate the movement of business people in China.

The FTA contains measures relating to customs procedures and cooperation, sanitary and phytosanitary measures, technical barriers to trade and intellectual property, designed to reduce barriers to doing business between New Zealand and China.

Goods entering China under the FTA are required to be released within 48 hours of arrival and exporters may apply for 'advance rulings' in respect of origin.

The FTA also retains New Zealand's rights under the World Trade Organisation (WTO) to take actions against unfairly traded imports from China and contains a prohibition against export subsidies.

In the area of investment, New Zealand will benefit from enhanced national treatment and investment protection provisions, as well as a 'Most Favoured Nation' (MFN) non-discrimination provision to ensure that New Zealand investors remain no worse off than investors of any other countries. The FTA also provides New Zealand investors with access to binding third-party arbitration procedures if the Chinese Government breaches the investment provisions. As well there are provisions to facilitate dialogue between the two countries on investment matters.

The FTA establishes a framework for cooperation to enhance the benefits of the FTA. The objective is to build on the existing cooperative relationship and create new opportunities.

The FTA includes a Mutual Recognition Agreement on Electrical and Electronic Equipment (EEEMRA), which will facilitate conformity assessments of electrical and electronic products traded between New Zealand and China.

Legally binding agreements on labour and environment were concluded in association with the FTA. These agreements will enhance communication and cooperation on these issues and help towards the objectives of raising working standards and improving environmental protection in both countries.

Disadvantages

The FTA includes a special safeguard mechanism and a mid-term review mechanism for certain dairy products which China considers to be sensitive. However, the practical effect of these mechanisms is expected to be limited as they will apply only if triggered and for a limited time.

The tariff liberalisation under the FTA will not apply to certain processed wood and paper products that account for approximately 4 percent of New Zealand's current exports to China.

China has maintained its WTO tariff rate quota (TRQ) for a range of primary products. However, New Zealand does not currently export these products to China.

A country-specific tariff quota (CSTQ) has been established for wool and wool tops exported to China. The initial quota level equates to approximately 75 percent of New Zealand's current exports, which is not as much as New Zealand sought.

The removal of New Zealand's tariffs on imported Chinese products can create adjustment effects for import competing sectors. The FTA attempts to mitigate these effects with various protections, described later in this document.

The FTA includes a bilateral safeguard mechanism under which China can impose additional duties on New Zealand products if the exports under the FTA are causing serious injury to the Chinese industry. However, given the small size of New Zealand exports in relation to Chinese production, and the conditions attached to it, the effect of the mechanism is likely to be limited. In addition, New Zealand industries will also have recourse to this mechanism.

The services commitments under the FTA were not made on the basis of a "negative list" as New Zealand would have preferred and China's upfront commitments in addition to its existing WTO commitments are limited.³

³ A negative list contains all the reservations on a Party's services commitments. The provisions of the Agreement apply to all services sectors and activities not expressly reserved against in the negative list.

(iv) Obligations under the FTA

Key new obligations for New Zealand under the FTA include:

- The eventual elimination of tariffs on all goods originating from China, with up to a 9 year phase out period on some goods
- Rules of Origin (ROO) using primarily a change of tariff classification (CTC) approach, and for some products an additional requirement that the products must have a specified percentage of regional value content (RVC)
- A Certificate of Origin System for exports obtaining preferential treatment under the FTA
- A framework to enhance bilateral implementation of the WTO Agreement on the Application of Sanitary and Phytosanitary Measures (SPS Agreement)
- A mutual recognition agreement in respect of electrical and electronic equipment (the EEEMRA)
- An obligation of market access and national treatment in services sectors where FTA commitments go beyond New Zealand's WTO commitments.
- Commitments on the temporary entry of Chinese business visitors where FTA commitments go beyond New Zealand's WTO commitments and on the temporary employment entry of specified skilled workers
- MFN non-discrimination for investment, together with enhanced investment protection disciplines and a provision for investor recourse to arbitration procedures

Obligations in a number of other areas of the FTA are fully consistent with existing New Zealand law and practice. These include customs cooperation, trade remedies and transparency measures. New Zealand's ability to regulate for national policy objectives is explicitly recognised in the Preamble to the FTA. The FTA does not prevent New Zealand from taking measures it deems necessary to fulfil its obligations to Māori, or to support creative arts of national value.

(v) Obligations under the MOU and ECA

The MOU requires New Zealand to commit to further cooperation with China on labour issues, including establishing a cooperation programme, seeking funding for cooperation activities and holding regular meetings between senior officials.

The ECA requires New Zealand to commit to further cooperation with China on environment issues, including establishing a cooperation programme, seeking funding for cooperation activities and holding regular meetings between senior officials.

(vi) Economic, social, cultural and environmental effects

Economic Effects

The FTA is expected to have an overall positive effect on the New Zealand economy, with gains to GDP, trade and welfare.

The FTA is expected to deliver economic benefits through the removal of tariffs and the reduction of other impediments to bilateral trade and investment between New Zealand and China over time.

Modelling undertaken as part of the Joint Study Report suggested that as a result of a high quality FTA:

- Over a 20-year period from 2007 to 2027, New Zealand exports to China were expected to be between US\$180–280 million higher per year (between 20 and 39 percent above baseline). Chinese exports to New Zealand were expected to increase by an annual average of between US\$40–70 million per year (between 5 and 11 percent above baseline) over the same period.
- Over this timeframe economic welfare (real consumption) was expected to increase by US\$1.6 billion (a maximum of 0.35 percent above baseline) in ‘static’ terms and US\$2.3 billion (a maximum of 0.55 percent above baseline) using ‘dynamic’ modelling assumptions.

The bulk of these gains were estimated to result from outcomes in the merchandise trade area, with the model based on immediate removal of barriers.

The phased opening of markets under the FTA as concluded and the fact that regulatory cooperation benefits will also accrue over time suggest the value to New Zealand may be nearer the low end of the range (ie US\$180 million in increased annual exports and US\$1.6 billion in welfare gains over 20 years).

Alternatively the fact that economic modelling does not capture the potential ‘demonstration effect’ conclusion of an FTA may have in stimulating interest among both business communities suggests the actual positive impact of the FTA could be higher than the findings of the Joint Study.

Social Effects

The FTA is not expected to have any discernable negative social effects in New Zealand. In employment, some negative effects can be expected to be found in industries previously protected by tariffs or other barriers to trade, though tariff removal in sensitive areas will be gradual. Positive employment effects can be expected from increased export opportunities and as a result of cheaper imports. The MOU affirms the commitment of both parties to maintaining sound labour policies and practices.

The conditions attached to temporary entry by skilled Chinese workers to New Zealand’s employment market – including the limitation of numbers, skill level requirements and the requirement as employees to observe New Zealand labour market conditions – are designed to avoid negative impacts on New Zealand employment.

Cultural Effects

The FTA contains safeguards to ensure that there are no adverse effects on New Zealand cultural values including Māori interests.

Environmental Effects

New Zealand has sufficiently robust environmental laws, policies, regulations and practices in place to manage any potential negative impacts of the FTA. The FTA and the ECA reinforce the commitment of both parties to improving environmental protection standards.

(vii) Costs

One-off costs associated with implementing the FTA, incurred in the 2007/08 financial year are estimated to amount to NZ\$960,000, as funded from the inter-agency FTA Growth and Innovation Fund (GIF) pools for promotion and outreach activities and cooperation and capacity building. There will be ongoing costs of meeting New Zealand's obligations under the FTA including staffing, the establishment of new institutions, developing implementing arrangements, and technical assistance and implementation costs.

(viii) Subsequent Protocols and/or amendments to the treaties and their likely effects

The FTA includes general provision for review and amendment subject to the agreement of the parties and completion of necessary domestic legal procedures. There are specific provisions which envisage amendments for the acceleration of tariff elimination, services commitments, and the conclusion of annexes and/or implementing arrangements for SPS measures and TBT.

The MOU and ECA have no formal provision for amendments.

(ix) Implementation

Legislative and regulatory amendments are required to align New Zealand's domestic regime with rights and obligations created under the FTA – in particular those relating to tariffs, ROO and the EEEMRA.

There are no legislative or regulatory requirements for New Zealand to implement the ECA and MOU.

(x) Consultation

The study, preparation and negotiating phases for the FTA and associated instruments involved extensive consultation between government agencies and with non-government stakeholders in New Zealand. A communication programme kept stakeholders informed of progress in the negotiations and provided opportunities for input.

1 NATURE AND TIMING OF PROPOSED TREATY ACTIONS

The New Zealand–China Free Trade Agreement (FTA), the Memorandum of Understanding on Labour Cooperation (MOU) and the Environment Cooperation Agreement (ECA) were signed by New Zealand in early April and in late March 2008 respectively. For all three treaties, entry into force is subject to the domestic legal procedures of both parties and will occur 60 days after the parties exchange written notification that such procedures have been completed (FTA Article 213; ECA Article 6.1; MOU Article 5.1). Both parties hope to have completed necessary procedures in time for the FTA to enter into force by 1 October 2008 at the latest. It is expected the ECA and MOU will enter into force on or before that date.

2 REASONS FOR NEW ZEALAND BECOMING A PARTY TO THE TREATIES

2.1 Background to the Treaties

In October 2003 Chinese President Hu Jintao and Prime Minister Helen Clark agreed to negotiate a Trade and Economic Cooperation Framework. In this Framework the two countries agreed to undertake a joint feasibility study on a bilateral FTA negotiation. The Joint Study was completed in October 2004. The Joint Study concluded that a high quality FTA could be expected to deliver positive benefits for both countries. Economic modelling undertaken as part of the Joint Study suggested positive GDP, trade and welfare gains for both economies would flow from a high-quality FTA.

The Government has developed frameworks on integrating labour and environment standards in trade agreements.⁴ The Joint Study also recognised the increasing international awareness of the linkages between sustainable development and trade.

The New Zealand Prime Minister Helen Clark and the Chinese President Hu Jintao announced the commencement of negotiations on the FTA at the APEC Leaders meeting in Santiago, Chile in November 2004, following the completion and publication of the Joint Study.

The first round of negotiations was held in December 2004. Negotiations continued over 15 rounds, held in both China and New Zealand. The negotiations concluded substantively in Beijing in December 2007.

2.2 Benefits from enhanced trade and economic links

This section sets out the direct and indirect benefits of the FTA in each key area.

2.2.1 Direct benefits from enhanced trade and economic links with China

A fundamental objective of New Zealand's trade policy is to expand the opportunities available to New Zealand exporters by removing barriers to trade, and to establish sound frameworks under which trade and investment linkages can flourish. Concluding bilateral agreements with key trading partners to remove trade barriers on a reciprocal basis is one of the avenues for achieving this objective.

The FTA contributes to the government's goal of sustainable growth as set out in the Growth and Innovation Framework (GIF) – in particular its “international connectedness dimension”. The FTA also contributes to the outcome stated in the Ministry of Foreign Affairs and Trade's Statement of Intent that “New Zealand's international connections support transformation of the New Zealand economy and sustainable economic growth through increased trade and through improved flows of investment, skills and technology”.⁵

⁴ The 2001 Framework for Integrating Labour Standards and Trade Agreements and the 2001 Framework for Integrating Environment Standards and Trade Agreements are available on the MFAT website (www.mfat.govt.nz)

⁵ Ministry of Foreign Affairs and Trade Statement of Intent 2007–2010 Intermediate Outcome II. The Statement of Intent is available on the MFAT website (www.mfat.govt.nz)

China is one of the largest economies in the world and one of the fastest growing. New Zealand's commercial relationship with China has grown substantially. China is now New Zealand's third largest individual trading partner with merchandise trade having grown significantly over the past ten years, with services trade and investment also increasing.

Reflecting the high rate of economic growth achieved in China over the past two decades, as well as the complementary nature of the two economies, China is now New Zealand's fourth largest merchandise export market. New Zealand exports to China total are around \$2 billion per year, and have increased 245 percent since 1996.

The elimination of tariff and other barriers to trade under the FTA will open up further opportunities for New Zealand exporters in the Chinese market.

As a result of China's commitments under the FTA tariffs will be eliminated, over 12 years, on roughly 96 percent of New Zealand's current exports. More than 70 percent of New Zealand's exports, covering exports other than of certain agricultural products, will be duty free within the first six years.

Beyond market access for goods, the FTA will provide more opportunities, and greater certainty and transparency, for New Zealand businesses wishing to operate in China.

The FTA contains a range of mechanisms which provide a platform for enhanced regulatory cooperation to facilitate trade and reduce associated transactions costs in both goods and services trade. This includes frameworks for resolving issues concerning technical barriers to trade (TBT) and sanitary and phytosanitary (SPS) measures and for cooperating on a range of other trade-related issues such as customs procedures and intellectual property rights and their enforcement.

Bilateral services trade has expanded in recent years, particularly in the sectors of tourism and education. China is now New Zealand's 5th largest source of tourists with 120,800 visitors coming to New Zealand in 2007. In the area of education China remains the largest market for New Zealand with 31,905 fee-paying students enrolled in courses of study in New Zealand in 2006. Along with the development of direct air links and the introduction of a Working Holiday Scheme, the FTA will help facilitate further growth in these and other services exports.

Reflecting the growing investment relationship between New Zealand and China, the FTA will also provide greater security for New Zealand investors in China, including through the potential for recourse to binding investor-state arbitration procedures.

With the increasing number of preferential trade agreements being concluded internationally, avoiding disadvantage in key export markets relative to competitors from third countries under such agreements is another important reason for New Zealand's pursuit of FTAs.

China is active in negotiating FTAs with other countries. China has concluded agreements with ASEAN, Chile and Pakistan and has negotiations underway with a range of countries including Peru, South Africa, Singapore and Australia.

New Zealand is the first OECD country with which China has concluded an FTA. The upfront outcomes in terms of commitments on goods, services and investment and the mechanisms which provide for further development of the agreement over time should help keep New Zealand at the forefront of the evolution of trade and investment relationships with China.

2.2.2 Indirect benefits from enhanced trade and economic links with China

As well as offering direct economic benefits, the FTA advances a number of New Zealand's strategic interests.

Globally, New Zealand and China are both members of the World Trade Organisation (WTO) and trade liberalisation through the WTO remains New Zealand's primary trade policy objective. New Zealand was the first WTO member to finalise its bilateral accession negotiation with China. Entering into a comprehensive FTA with China should help maintain momentum towards New Zealand's wider goal of multilateral trade liberalisation.

At the regional level, China and New Zealand are also both members of Asia Pacific Economic Cooperation (APEC) and the East Asia Summit (EAS) process. APEC has made significant progress in facilitating trade and opening markets in member economies towards the goal of free and open trade and investment in the Asia-Pacific region, with work now being undertaken on the possibility of a Free Trade Agreement of the Asia-Pacific (FTAAP). Within the EAS, a Comprehensive Economic Partnership for East Asia (CEPEA) is proposed.

With more than 70 percent of New Zealand's trade and investment occurring in the Asia-Pacific the potential contribution that entering into a comprehensive FTA with China may make to broader regional integration initiatives could also be significant.

The two countries also work together on trade and economic issues in a range of other multilateral organisations including the World Intellectual Property Organisation (WIPO), the International Labour Organisation (ILO), the United Nations Economic and Social Commission for Asia and the Pacific (ESCAP), the United Nations Development Programme (UNDP), the United Nations Conference on Trade and Development (UNCTAD) and the United Nations Food and Agriculture Organisation (FAO).

2.3 Benefits of closer cooperation with China on Labour and Environment

In the context of the FTA, New Zealand has concluded a legally binding inter-governmental Memorandum of Understanding on Labour Cooperation (MOU) and a legally binding inter-governmental Environment Cooperation Agreement (ECA). These instruments are consistent with the Government's frameworks on integrating labour and environment standards in trade agreements. Together the FTA and these associated instruments will help to mutually reinforce the objectives of raising working standards and improving environmental protection in both countries.

The MOU and ECA are the first legally binding inter-governmental instruments on labour and environment that China has concluded in the context of a free trade agreement. Both instruments are linked to the FTA through the requirement in the FTA for both parties to enhance their communication and cooperation on labour and environment matters through the MOU and ECA.

The MOU and ECA have broadly similar structures and provisions to the labour and environment outcomes negotiated with Thailand and with Brunei Darussalam, Chile and Singapore under the Trans-Pacific Strategic Economic Partnership (P4) Agreement.

Both the MOU and ECA establish mechanisms for ongoing cooperation and dialogue, and for addressing any issues that may arise in these areas.

The MOU and ECA also provide opportunity for the New Zealand Government to seek input on implementation from union representatives and relevant non-governmental organisations (NGOs) and make provision for public participation in cooperation activities.

3 ADVANTAGES AND DISADVANTAGES TO NEW ZEALAND OF THE TREATIES ENTERING INTO FORCE

3.1 Advantages to New Zealand in entering into the Free Trade Agreement

3.1.1 Goods

China is the fourth largest individual country destination for New Zealand exports, taking an average of NZ\$2 billion worth of New Zealand products annually in the period 2004–2006. Duty payments on those exports averaged NZ\$118.5 million annually.

The FTA provides for elimination over time of tariffs on 96 percent of New Zealand's current exports to China, which on full implementation will equate to an annual duty saving of NZ\$115.5 million based on current trade.

This tariff elimination will deliver benefits to exporters including;

- The immediate removal of tariffs on over NZ\$200 million of current exports including certain types of fibreboard, fish meal, scrap metal (copper and aluminium), coking coal and iron slag.
- Elimination over 5 years of tariffs on NZ\$621 million of current exports including infant milk formula, yoghurt, casein, frozen fish, frozen fish fillets, methanol, animal fats & oils, apples and wine.
- Elimination over 9 years of tariffs on NZ\$77 million of current exports including products such as beef and sheep meat, edible offals, sheepskins and kiwifruit.
- Elimination over 10 years of tariffs on butter, cheese, liquid milk currently worth NZ\$50 million; and elimination over 12 years of tariffs on whole milk powders and skim milk powders, currently worth NZ\$305 million. Exports of these products currently pay an annual tariff duty on entry into China of NZ\$36 million. Although accompanied by a special safeguard mechanism and, for whole milk and skim milk powders only, a mid-term review, the guaranteed tariff elimination on these products provides certainty for New Zealand exporters. Tariff cuts begin on day one, meaning an estimated NZ\$3.2 million in duty savings on exports of these products in the first year, based on current trade.
- Creation of a Country-specific Tariff Quota (CSTQ) for New Zealand wool. This will provide duty free treatment for an initial quantity of 25,000 tonnes of wool and 450 tonnes of wool tops, with an annual growth rate of 5 percent over 8 years through to 2017. The CSTQ provides New Zealand exporters with duty-free access for approximately 75 percent of current exports (which equates to an average of \$122 million per year) in this competitive market. For exports outside the CSTQ, New Zealand exporters will still be able to access China's global wool quota.

The phase out of tariffs on New Zealand's imports also has advantages for New Zealand. New Zealand's economy is dependent on imports in order to supply a range of goods and services to producers and consumers. Consumers will benefit directly from cheaper products. Cheaper imports of equipment and machinery, which account for 35 percent of New Zealand imports from China, will have benefits for New Zealand manufacturers.

3.1.2 Rules of Origin (ROO)

As in any free trade agreement, products must meet the relevant ROO criteria in order to qualify for preferential tariff treatment. This prevents goods from other sources from accessing the benefits of the agreement by entering 'through the back door'.

The FTA rules of origin are based primarily on a change of tariff classification (CTC) approach and are designed to facilitate trade and minimise compliance costs for exporters. The outcome represents the most extensive use of the change of tariff classification (CTC) methodology that China has agreed in its FTAs to date. The CTC approach is generally regarded as being:

- helpful in enabling manufacturers to access materials within the global supply chain and allow for changes in manufacturing processes;
- simpler and cheaper for business to use, with less need to maintain costly records systems;
- easier for government to administer; and
- inherently more predictable and consistent for business in terms of origin outcomes ('once qualify, always qualify').

While CTC forms the basis for the rules of origin, supplementary Regional Value Content (RVC) apply to some products. Supplementary RVC rules are mostly in the vicinity of 40 percent.

The agreement introduces a requirement for export certification of origin. The certificates of origin system is intended to facilitate trade and will provide New Zealand exporters with the ability to access the tariff benefits of the FTA if they follow the agreed processes.

The certificates of origin will be issued by Authorised Bodies approved by the New Zealand Government and notified to China. The Authorised Bodies will be able to recover the approximate cost of the certification services which they provide to exporters. The net result will be that additional costs for both the business stakeholders and for New Zealand Government will be minimised.

In accordance with long-established practice, New Zealand will not require that certificates of origin accompany imports from China. Normal risk management techniques will provide sufficient assurance that only goods of Chinese origin under the rules of origin will receive the benefits of the FTA tariff preference. New Zealand's approach towards imports from China will provide facilitation benefits for importers and their clients.

3.1.3 Trade Remedies

New Zealand has retained the ability to take trade remedy actions against unfairly traded imports from China which are dumped or subsidised and injure New Zealand producers, consistent with WTO rights and obligations.

The ability to take global safeguard action is also retained, but the FTA provides for the possibility of excluding imports from the other party if such imports are non-injurious. This is potentially valuable for a small supplier such as New Zealand in any global safeguard action taken by China.

The FTA also contains a clear prohibition on any form of export subsidy in bilateral trade. This provides for a bilateral course of action against any such measures.

3.1.4 Trade Facilitation, Regulatory Environment and Transparency

The cost of complying with technical regulations can constitute as significant a barrier to trade in goods as tariffs. Without formal arrangements, it is difficult to engage with other countries at the technical level in a way that will produce tangible solutions to adverse impacts of technical regulations and standards and conformance requirements on trade flows.

The FTA establishes mechanisms, such as regular meetings and working groups on specific issues for regulators, other officials and technical experts to work together more effectively to address barriers to trade in the areas of standards and conformance, SPS measures and customs procedures.

The FTA also contains a separate chapter setting out each party's obligations generally across the whole Agreement for the transparency of laws, regulations, procedures and administrative rulings, consistent with New Zealand's existing law and administrative practice. This should help contribute to predictability and certainty in the bilateral trade and investment relationship.

3.1.5 Customs Procedures and Cooperation

Provisions on customs procedures are intended to ensure predictability, consistency and transparency in the application of customs laws and administrative procedures to ensure efficient and economical administration and the expeditious clearance of goods in order to facilitate trade.

In the normal course of events, goods entering China under the FTA are required to be released within 48 hours of arrival. Traders will also be able to apply to customs authorities for advance rulings in respect of origin and tariff classification (Article 52). New Zealand exporters can obtain a ruling on origin and enjoy the benefit of not needing a certificate of origin for goods covered by an advance ruling on origin from China. However, due to legislative requirements in China, applicants for advance rulings on tariff classification need to be registered with China Customs, which will generally require a presence in China. Applications for rulings may be made at least three months before the date of importation.

3.1.6 Sanitary and Phytosanitary (SPS) Measures/Technical Barriers to Trade (TBT)

In the SPS area, the FTA provides a framework for enhanced cooperation on the application of sanitary and phytosanitary measures, including risk analysis, adaptation to regional conditions, equivalence and technical assistance. The objective is to facilitate trade in goods affected by sanitary and phytosanitary measures, and to provide a means to improve transparency, communication and consultation on SPS issues.

In the TBT area the FTA establishes a framework for regulator-to-regulator cooperation aimed at facilitating the removal of technical barriers to trade while strengthening the management of risks to health, safety and the environment. The framework includes a range of mechanisms to achieve these objectives including through mutual recognition of standards and conformance assessment. Consistent with this approach a mutual recognition agreement entitled the “Agreement between New Zealand and China on Cooperation in the Field of Conformity Assessment in relation to Electrical and Electronic Equipment” (EEEMRA) has been concluded and is included in the FTA as Annex 14.

3.1.7 Mutual Recognition Agreement on Electrical and Electronic Equipment (EEEMRA)

The EEEMRA concerns electrical and electronic products that are subject to the China Compulsory Certification (CCC) system and to the requirements of New Zealand supplier declarations of conformity for such products.

Currently Chinese exports to New Zealand must be tested to New Zealand standards while New Zealand exports to China must be tested, inspected and certified by Chinese conformity assessment bodies. The EEEMRA gives suppliers in both countries an alternative way to demonstrate compliance with electrical safety and electromagnetic compatibility (EMC) regulatory requirements.

The benefits of the agreement include:

- Enabling New Zealand exporters to apply the CCC mark to products before being exported to China, on the basis of accreditations and conformity assessment procedures carried out by New Zealand agencies which have been formally accepted in China and to have their products recognised as meeting Chinese requirements on importation;
- Improved monitoring and enforcement capabilities for New Zealand regulators of electrical safety and EMC of imported products, including through providing for cooperation with Chinese regulators in surveillance and enforcement actions;
- Reduced language barriers for both New Zealand and Chinese stakeholders;
- Improved probability of compliance of Chinese imports within the scope of the EEEMRA by providing a method of demonstrating compliance that will be easier for Chinese manufacturers who also supply China’s domestic market; and
- Improved quality assurance through requirements for factory inspections and certification.

Some standards applied to electrical and electronic products by China are earlier versions of the international IEC standards than those applied in New Zealand. The EEEMRA, however, provides for deviations from the Chinese standards where necessary to ensure satisfactory levels of safety.

The EEEMRA is a first for China. No other country, to date, is able to accredit conformity assessment bodies in their territory for testing, inspection or certification that will be accepted by the Chinese authorities. This will provide New Zealand exporters with the competitive advantage of being able to carry out all conformity assessments on the covered products by New Zealand conformity assessment bodies prior to export. New Zealand regulators will also have the ability to request Chinese authorities to take enforcement measures against any manufacturers who export defective goods to New Zealand.

In addition to the benefits for trade in covered products, conclusion of the EEEMRA will also provide a basis for the exploration with China of similar approaches to reduce transactions costs and manage risks associated with regulation of other areas of interest to New Zealand in the bilateral trading relationship.

Under the Trans-Tasman Mutual Recognition Arrangement (TTMRA) with Australia, any product that may legally be sold in New Zealand may be sold in Australia. Thus, products imported into New Zealand under the provisions of the EEEMRA (i.e. subject to the standards and compliance obligations) may be sold in Australia under the provisions of the TTMRA. In this context it will be important to ensure ongoing compliance with the requirements under Annex 14 and continue to liaise with the relevant Australian authorities.

3.1.8 Services

The FTA is intended to facilitate expansion of trade in services between New Zealand and China.⁶ Both sides have made commitments in the FTA that expand on their respective commitments in the WTO General Agreement on Trade in Services (GATS).

China's GATS-plus commitments are in the following sectors:

- Computer and Related Services – including software implementation services, data processing services, and input preparation services;
- Services related to management consulting;
- Education – a binding commitment to keep names of key NZ educational institutions on the China Ministry of Education “Study Abroad Website”, and a commitment to initiate joint work on quality assurance criteria for qualifications which include a distance delivery component;
- Environmental services – an improved Mode 3 (investment in environmental services) commitment permitting wholly foreign-owned enterprises;
- Sporting and other recreational services;
- Air transport services – aircraft repair and maintenance services, and air travel computer reservation services; and
- Road Transport services – freight transportation by road in trucks or cars; maintenance and repair of motor vehicles; storage and warehousing services; and freight forwarding agency services.

⁶ The four 'modes' of service supply referred to in this document are: Mode 1: Cross-Border Trade; the service is supplied by a provider physically located in one country, to a consumer in another; Mode 2: Consumption Abroad; a customer travels to another country to consume a service; Mode 3: Commercial Presence; a foreign service supplier establishes a presence in another country to provide a service, through incorporation, branch offices, a joint venture or other form of business entity; and Mode 4: Movement of Natural Persons; the temporary movement of a person into a country in order to supply a service directly.

The effect of China making these GATS-plus commitments in the FTA in the above services sectors is that, subject to specific reservations or exemptions listed in China's schedule, New Zealand service suppliers will be able to access the Chinese market without quotas and operate in China on the same footing as domestic Chinese services suppliers in the certainty that the environment in which they are operating cannot be altered adversely. Suppliers of these same services from countries which do not have such FTA commitments do not enjoy that level of certainty.

The FTA also includes a reciprocal 'Most Favoured Nation' (MFN) provision. This provision requires that any better treatment relating to services that China extends to third countries must also be extended to New Zealand. China's MFN obligations to New Zealand cover the following services sectors:

- Construction⁷
- Environmental services
- Services incidental to agriculture and forestry⁸
- Engineering services
- Integrated Engineering services
- Computer and related services
- Tourism services

The inclusion of an MFN provision means that New Zealand exporters of these services will automatically receive the benefit of commitments China makes in future agreements that are more liberal than those in the FTA.⁹ This will help to ensure that the competitive position in the China market of New Zealand exporters of these services is not eroded.

Education

Education is New Zealand's single most important services export sector after tourism. In 2006 there were a total of 31,905 Chinese fee-paying students enrolled in courses of study in New Zealand. The estimated economic value of this to New Zealand was some NZ\$745 million.

China has made a binding commitment to include on the China Ministry of Education "Study Abroad Website" the eight New Zealand universities, the twenty Institutes of Technology and Polytechnics, Te Wananga o Aotearoa, Te Whare Wananga o Awanuiarangi and Te Wananga o Raukawa, and six degree conferring Private Training Establishments duly approved and accredited by NZQA. The Open Polytechnic of New Zealand, a 100 percent distance education provider, is among the twenty New Zealand Institutes of Technology and Polytechnics included on the website. The commitment provides these institutions with a high degree of certainty that they cannot arbitrarily be removed from the website with the result that Chinese students are deterred from using them. This addresses what has in the past been a major problem for New Zealand education services exporters to China.

⁷ The following construction services are covered: construction work for buildings; assembly and erection of prefabricated constructions; installation work; and building completion and finishing work.

⁸ China has entered a reservation against its commitment on this sector to the effect that it applies only to agreements China concludes with the countries (including New Zealand) which are members of the Organisation for Economic Cooperation and Development (OECD).

⁹ An exemption for preferences either party grants under prior FTAs means New Zealand service suppliers will not automatically receive the benefit of any preferences China grants to ASEAN countries, Chile, Pakistan, or under any other FTA that China signs prior to entry into force of the New Zealand-China FTA.

China has also agreed that both parties will jointly initiate work at the official level on the evaluation of the quality assurance criteria for qualifications that include a distance delivery component. With New Zealand education suppliers increasingly looking to deliver their services via electronic platforms this is an important step forward. China's commitment to engage in a joint project with New Zealand on quality assurance criteria provides New Zealand with the opportunity to build confidence in the New Zealand quality assurance systems and to strengthen New Zealand's education profile as a whole.

Both parties have agreed to establish a Joint Working Group to explore possibilities for mutual recognition of respective vocational qualifications. This work is important as vocational education is one of the biggest growth areas in the New Zealand–China education relationship. Removing barriers to the recognition of vocational qualifications would benefit New Zealand education providers delivering vocational education services in China and in the wider New Zealand vocational training industry.

3.1.9 Movement of Natural Persons

The FTA includes a separate Chapter on the Movement of Natural Persons – designed to facilitate business opportunities under the Agreement. China has agreed to expeditious processing of visas applications by New Zealanders visiting China for business purposes, including services suppliers, investors and good sellers, and to greater transparency in processing the applications. This will ensure that the procedures that New Zealand business people need to follow in order to gain entry to do business in China do not become more onerous, and provides New Zealand with a good basis on which to seek to work to improve these conditions over time.

China has also made specific commitments under this Chapter in respect of its rules for Mode 4 entry by New Zealand services exporters which improve over its commitments in the GATS. This means that in sectors included in China's services schedule, New Zealand services suppliers will receive better or more certain treatment than those of other countries in the following areas:

- a commitment providing entry of up to three months for installers and servicers;
- an improved commitment covering business visitors providing for a maximum period of stay of six months as compared to the 90 days maximum under China's GATS commitments.

New Zealand has made limited commitments (details are set out in section 4.10) providing for temporary entry to the New Zealand employment market for a limited number of skilled Chinese workers. Although involving only a limited number of Chinese workers, these commitments may help to ease labour shortages in the context of New Zealand's current tight employment market. Should the labour market in New Zealand loosen in the future, the requirement that such workers hold a bona fide job offer will protect conditions for New Zealanders.

People entering New Zealand under Working Holiday Schemes are currently assisting in meeting labour shortages in areas such as the hospitality and horticulture and viticulture industries. The Working Holiday Scheme associated with the FTA will add to the pool of people available for this work.

3.1.10 Investment

The investment relationship between New Zealand and China is a growing one. A number of New Zealand companies have begun to establish operations in China, and investment into New Zealand from China has increased in recent years. As at 31 March 2006, total Chinese investment in New Zealand was NZ\$1.66 billion. Total New Zealand investment in China at that time was NZ\$333 million.

Investments between New Zealand and China are already subject to an Investment Protection and Promotion Agreement (IPPA), which came into force in 1989. Subsequent to this IPPA, China has entered into a number of higher-quality bilateral investment agreements with other OECD countries. It was important to include investment provisions in the FTA in order explicitly to ensure that New Zealand investors are not disadvantaged relative to treatment available to foreign investors of other countries in China.

To this end the FTA includes provisions on national treatment and Most Favoured Nation (MFN) non-discrimination together with investment protection disciplines and provision for investor recourse to arbitration procedures.

China is committed to providing to New Zealand investments approved and established in China the same level of post-establishment treatment and protection as it provides to Chinese nationals investing in China, subject to an exception for existing non-conforming measures.¹⁰ The commitment includes a 'ratchet' mechanism under which any improvement in such measures is automatically then locked-in for New Zealand investors. The practical effect of the national treatment provision (and its exceptions) is that China is not able to bring in new discriminatory measures, and can only adjust existing discriminatory measures in way that favours New Zealand investors.

Under the MFN provision any better treatment relating to either market access or protection for investment agreed by China with third countries will automatically be extended to New Zealand investors. An exception for preferences either Party grants under prior FTAs means New Zealand investors will not automatically receive the benefit of any preferences China grants to ASEAN countries, Chile, Pakistan, or under any other FTA that China signs prior to entry into force of the New Zealand–China FTA. Aside from this exception, this provision future-proofs the investment commitments and ensures that the level of treatment afforded to New Zealand investors will not fall behind as China agrees new commitments with third countries.

The FTA provides for additional protections for New Zealand investments in China beyond those available under the existing IPPA. These include protection from unjustified expropriation; compensation for losses arising from war, armed conflict and similar situations; provisions to allow the free transfer of investment funds; and the incorporation of minimum international law standards of fair and equitable treatment and full protection and security.

In contrast to the existing IPPA which applies only to New Zealand citizens investing in China, the protection provisions of the FTA will apply also in respect of New Zealand's permanent residents. A large number of those who qualify as permanent residents do so by virtue of their business skills or level of economic investment in New Zealand. As such, having the benefits of the chapter apply also to permanent residents is potentially of significant benefit for the New Zealand economy.

The expropriation and fair and equitable treatment provisions are key protections for New Zealand investors. They minimise the risk of arbitrary government action on established investment and ensure that any such actions are appropriately compensated in the event they occur.

The FTA provides New Zealand investors with investments in China with access to binding third-party arbitration procedures in the event of breaches of the obligations of the Chapter by the Chinese government authorities. Such procedures can be accessed only after time-limited consultations and negotiations for settlement between the disputing parties have been exhausted. There are also safeguards to preserve government regulatory prerogative and minimise government exposure to inappropriate or frivolous expropriation claims. The existence of this mechanism will enhance the protection of New Zealand investments in China through providing New Zealand investors with the same kind of recourse to dispute resolution processes outside the Chinese legal system as that enjoyed by investors from a number of other OECD countries.

At the intergovernmental level the FTA provides for a Committee on Investment to oversee the implementation and operation of the investment part of the Agreement. The FTA's intergovernmental dispute settlement mechanism is also fully applicable in respect of the rights and obligations of the Parties.

The FTA will provide a more certain basis for the facilitation of bilateral investment flows with more advanced dialogue between New Zealand and China at the investor and governmental levels, and smoother resolution of potential investment issues.

3.1.11 Intellectual Property

The intellectual property provisions of the FTA support more certainty over the provision and enforcement of intellectual property rights in the bilateral trade and investment relationship.

The FTA requires that China establishes and maintains a transparent intellectual property rights system that provides certainty over the protection and enforcement of intellectual property rights. To this end the FTA incorporates the provisions of the WTO TRIPS Agreement as relevant to the bilateral context. This means that New Zealand rights and obligations *vis-à-vis* China under the TRIPS Agreement are actionable under the FTA, as well as in the WTO.

The FTA also requires China to notify New Zealand of any new laws that enter into effect in relation to intellectual property and to exchange information on developments in its intellectual property policy and systems, including regarding enhancement of intellectual property rights enforcement.

A consultation mechanism means that New Zealand can request consultations to seek a timely and mutually satisfactory solution on any intellectual property issue within the scope of the Agreement.

3.1.12 Government Procurement

Under commitments made as part of its accession to the WTO, China pledged to initiate negotiations to accede to the WTO Government Procurement Agreement (GPA). In the interim, China is obligated to conduct its government procurement in a transparent manner and extend MFN treatment to all WTO members including New Zealand. This obligation, however, lapses when China finally joins the GPA.

In a joint understanding concluded in association with the FTA, China has agreed that as soon as possible following the completion of its accession to the GPA it will begin negotiations on government procurement with New Zealand. While New Zealand is not a GPA member, this commitment to negotiate will provide an opportunity to ensure New Zealand suppliers are not disadvantaged in the Chinese procurement market as a result of China's joining the GPA.

3.1.13 Other outcomes of the FTA

Consistent with New Zealand's previous free trade agreements, the FTA:

- maintains and reinforces New Zealand's existing rights and obligations under the various WTO Agreements. As well as providing mechanisms for bilateral cooperation, both parties still retain their rights to use mechanisms available within WTO frameworks (for example in the areas of TBT, SPS and trade-related aspects of intellectual property rights (TRIPS));
- recognises the government's rights to regulate for national policy objectives;
- maintains New Zealand's ability to take measures it deems necessary to accord more favourable treatment to Māori, including in fulfilment of its obligations under the Treaty of Waitangi;
- does not preclude parties from taking measures necessary to protect national treasures or specific sites of historical or archaeological value or to support creative arts of national value; and
- includes robust and transparent dispute settlement provisions.

3.2 Advantages to New Zealand in entering into the Memorandum of Understanding on Labour Cooperation and the Environment Cooperation Agreement

Both the MOU and the ECA are linked to the FTA through Article 177, which requires the parties to enhance their communication and cooperation on labour and environment matters through the MOU and the ECA.

3.2.1 Advantages to New Zealand in entering into the MOU

The MOU is the first legally binding inter-governmental agreement on labour that China has concluded in the context of a free trade agreement. The MOU reflects a common aspiration to promote sound labour policies and practices in China and New Zealand.

The MOU enumerates a set of shared commitments which include the recognition that it is inappropriate to set or use labour laws, regulations, policies and practices for trade protectionist purposes and that it is inappropriate to encourage trade or investment by weakening or reducing the protections afforded in domestic labour laws, regulations, policies and practices (Article 1.3 and Article 1.4). Issues that may arise that touch on these or any other commitments can be consulted on with a view to their resolution. A time frame of 90 days is established for a meeting to “assist in the resolution” of any specific issues and the MOU envisages the possibility of meetings between Ministers as part of this process.

The MOU represents an opportunity for New Zealand to improve dialogue and conduct cooperative activities with China in the following areas (Article 2):

- Labour laws, policies and practices, including social dialogue, and raising the awareness of the legal rights and obligations of employers and employees, to realise decent work;
- Compliance and enforcement systems and labour inspection;
- Sound labour relations, including management labour consultation, cooperation and labour dispute settlement;
- Working conditions;
- Human capital development, training and employability; and
- Promotion and protection of the employment rights and obligations of migrant workers.

This is not an exhaustive list and other items may be added to the cooperative programme. The MOU also provides for the participation of unions and employers in identifying areas for cooperation.

3.2.2 Advantages to New Zealand in entering into the ECA

The ECA is the first legally binding inter-governmental agreement on the environment that China has concluded in the context of a free trade agreement. The ECA recognises that environmental laws and policies should be administered in pursuit of environmental objectives in a way that contributes to the mutual supportiveness of these and other policies to achieve sustainable development (Article 1.2).

The ECA establishes a set of shared commitments which include the recognition that the primary purpose of environmental laws, regulations, policies and practices should be to achieve environmental objectives and that these should be administered in a way that contributes to the mutual supportiveness of these and other policies to achieve sustainable development (Article 2.2).. As with the MOU on Labour Cooperation, the ECA provides for a mechanism to consult on issues that may arise that touch on these commitments or any others in the text with a view to their resolution. There is agreement that when a Party seeks a meeting to resolve any issues, this will be held “as soon as practicable.”

The ECA requires China to engage with New Zealand on cooperative activities in relation to environmental management, environmental remediation, nature conservation, and technologies (including systems and processes) for environmental benefit. Examples of such activities identified in the text are (Article 2.2):

- Management of water environment;
- Coastal ecological conservation and pollution control;
- Air pollution control and monitoring;
- Improvement of environmental awareness, including environmental education and public participation;
- Management and disposal of waste including hazardous waste;
- Environmental management of chemicals;
- Environment and trade;
- Biodiversity conservation; and
- Other areas mutually agreed upon.

This is not an exhaustive list and other items may be added to the cooperative programme. The ECA also provides for the participation of members of the public or non-governmental organisations in identifying areas of cooperation.

3.3 Disadvantages to New Zealand in entering into the Free Trade Agreement

3.3.1 Market Access – Exports

New Zealand would have preferred more ambitious outcomes in the following areas:

Dairy

New Zealand did not consider that a mid-term review mechanism or a special safeguard on dairy products were warranted given the small volume of imports from New Zealand relative to the overall size of China's fast-growing dairy sector. However, the inclusion of these mechanisms was necessary in order to secure China's agreement to full tariff elimination in the dairy sector over a commercially meaningful timeframe. The practical effect of the mid term review and the special safeguard mechanism is also expected to be limited.

The review is a one-off exercise at the year 6 tariff cut (2013) that at worst could result in a one-year extension to the overall tariff phase-out period for milk powders. This extension can only be made if both parties agree to it.

The special safeguard is a temporary mechanism, available for China during the phase out period and for an additional 5 years once tariffs have been eliminated. The safeguard allows China to apply an additional tariff for imports of the specified products (liquid milk, butter, cheese and milk powders) in any given year above an agreed trigger level. The initial trigger levels are all at or above current export levels and grow at a rate of five percent compounding annually over the life of the mechanism.

If triggered, the special safeguard allows China to raise tariffs on sendings above the trigger level up to China's WTO tariff rate (MFN tariff rate), which is currently 10 percent for whole and skim milk powders and butter, 12 percent for cheese and 15 percent for liquid milk.

Tariff Rate Quota Products

China insisted on maintaining its WTO Tariff Rate Quota (TRQ) system, which currently applies to a range of primary products including wheat, maize, rice, vegetable oils, sugar, some fertilisers, wool and cotton. China will not provide any additional market access under the FTA for these products (except wool) beyond the access already available to New Zealand exporters through the TRQ arrangements established under the WTO.

As noted in Section 3.1.1 the FTA establishes a country-specific tariff quota (CSTQ) that provides for duty free treatment for an initial quantity of 25,000 tonnes of wool growing at 5 percent per year over 8 years to reach 36,936 tonnes in 2017. For wool tops the initial CSTQ level of 450 tonnes will increase to 665 in 2017. For any exports outside the quota in each year, New Zealand exporters will need to pay the applicable tariff; either the one or three percent in-quota rate for product within the WTO TRQ quantity limits or the 38 percent out-of-quota rate if the global quota is filled.

While the CSTQ is a welcome development it is disappointing that the initial level equates to only 75 percent of current wool exports to China (120 percent of wool top exports) and its growth rate is unlikely to keep up with market demand. Against this, the future of China's WTO TRQ arrangements for wool is uncertain, especially if demand for imported wool continues the strong growth of recent years. Under current arrangements, with the WTO global quota having been essentially filled in 2007, Chinese customers are facing the imminent prospect of paying an additional 38 percent for their wool.

Wood and Paper Products

China has not made any bilateral tariff reductions under the FTA for a range of processed wood and paper products that account for approximately 4 percent of New Zealand's current exports to China. The reason for this is that, as part of its accession to the World Trade Organisation, China agreed that any preferential commitments it makes on wood and paper products in an FTA must be offered to all WTO Members.

While China will not make tariff reductions under the FTA for these products, it has agreed that the WTO commitment mentioned above will apply to these products. This obliges China to give to New Zealand any preferential treatment that it offers to any third country and means that New Zealand exporters will not be at a competitive disadvantage *vis-à-vis* other suppliers to China.

Bilateral Safeguard Mechanism

The FTA includes a bilateral transitional safeguard mechanism under which China can impose additional duties, up to the level of China's WTO tariff rate (MFN tariff rate) applied at the time, on New Zealand products if exports of that product under the FTA are causing serious injury to the associated Chinese industry. The safeguard mechanism is described in more detail in section 4.5. Given the small size of New Zealand exports in relation to Chinese domestic production and consumption for most products, New Zealand did not consider it necessary to include such a mechanism in the FTA.

The design of the mechanism, however, contains a number of protections against abusive use. These include the requirement for a full injury and causation investigation in accordance with the relevant provisions of the WTO Safeguards Agreement. The overall period during which safeguard action can be taken on any product and the maximum length of time of any safeguard measure are limited. There is also a requirement for offsetting compensation that China would have to provide to New Zealand, in the form of substantially equivalent concessions, except in the first year of a safeguard that has been taken as a result of an absolute increase in imports.

3.3.2 Market Access – Imports

Any trade agreement involving reciprocal tariff removal can create adjustment effects for import-competing sectors deriving from increased exposure to foreign suppliers, at the same time as export-focused sectors secure improved access to offshore markets.

In order to help mitigate the potential for any negative adjustment effects, the FTA includes longer tariff phase out periods for import-sensitive sectors in New Zealand, such as textiles, clothing, footwear and carpets. Slower initial tariff reductions will apply to other products such as steel, plasterboard and whiteware.

The FTA has preserved New Zealand's rights to apply anti-dumping, countervailing and global safeguard measures for trade with China, consistent with WTO rights and obligations. The bilateral transitional safeguard mechanism will also provide an additional safety net for any New Zealand industries that might be seriously affected by tariff reductions under the FTA and allow New Zealand to address situations of serious injury to a domestic industry caused by increased imports from China due to tariff reductions under the FTA by reverting to higher tariffs for a certain period.

3.3.3 Services

New Zealand would have preferred services sectoral commitments to have been made on a 'negative list' basis¹¹ together with an across-the-board approach on MFN. A 'negative list' approach provides greater legal certainty and transparency about the barriers that exist to services trade and its dynamic nature renders it better capable of capturing changes in the regulatory environment.

¹¹ A negative list contains all the reservations on a Party's services commitments. The provisions of the Agreement apply to all services sectors and activities not expressly reserved against in the negative list.

Although New Zealand did not achieve as much as it was seeking by way of upfront improved sectoral commitments from China, China's existing GATS commitments (which will be bound in the FTA) are of a relatively high quality. The review clause in the services chapter will also provide an opportunity to pursue progressive liberalisation of bilateral services trade over time, including extension of MFN to additional sectors.

3.3.4 Investment

The investment chapter does not contain any upfront market access commitments. Throughout the negotiations, New Zealand had sought to gain immediate commitments on market access in order to provide additional benefits to New Zealand investors setting up business in China, or expanding their operations there. While the FTA does not include any initial market access improvements, the MFN clause of the chapter will extend to New Zealand investors any future commitments in access conditions granted by China to investors from third countries.

3.4 Disadvantages to New Zealand in entering into the Memorandum of Understanding on Labour Cooperation and the Environment Cooperation Agreement

There are no disadvantages to New Zealand entering into the MOU and the ECA.

4 LEGAL OBLIGATIONS WHICH WOULD BE IMPOSED ON NEW ZEALAND BY THE TREATY ACTIONS AND AN OUTLINE OF THE DISPUTE SETTLEMENT MECHANISMS

The FTA provides for the liberalisation of trade between the parties and imposes a general obligation on New Zealand to work with China to implement the provisions of the agreement. The specific obligations that New Zealand will assume in each chapter of the FTA are set out below in the sequence in which they appear in the FTA. Also included in this section are the obligations arising from the accompanying ECA and MOU.

4.1 Initial Provisions

The FTA will not undermine New Zealand's rights and obligations in the WTO (Article 3).

4.2 Trade in Goods

New Zealand is required to eliminate its customs duties (or tariffs) on goods originating from China in accordance with the phase-out schedule in Annex 1¹² to the FTA, and may not increase existing customs duties. There is provision for parties to consult to consider accelerating the agreed phasing of tariff elimination (Article 8).

The FTA imposes obligations, consistent with WTO requirements to accord national treatment (Article 6), to ensure that all fees and charges are commensurate with the cost of the services provided, and that any non-tariff measures are consistent with WTO rights and obligations and do not create unnecessary obstacles to trade (Articles 9 and 11). The parties agree not to introduce or maintain any export subsidy on agricultural goods destined for the territory of the other party (Article 10).

The parties are also required to provide legal means for interested parties to prevent the sale of products in their territory which, under their laws, are labelled in a false, deceptive or misleading manner with respect to the character, composition, quality or origin of the product (Article 12).

4.3 Rules of Origin (ROO)

The FTA sets out rules for determining whether goods traded between the parties qualify as originating goods and therefore receive tariff preferences under the FTA.

For products that contain third party inputs, the FTA predominantly uses a change of tariff classification (CTC) approach to determine origin. Under the CTC approach, a good will qualify in principle as 'originating' if all third party inputs used in the production of that good have undergone a specified change of tariff classification. Annex 5 to the FTA details the precise form of CTC that will apply to a particular good.

For some products there are additional regional value content (RVC) rules where the product must meet CTC plus an additional RVC requirement. For example, certain machine tools must meet a CTC rule plus 40 percent RVC.

Some products require either a stand alone RVC or an alternative RVC (for example chemicals and boats respectively) and for others there is either a stand alone process rule or an alternative process rule (for example live animals and chemicals respectively).

Some agricultural products must be wholly obtained from a party in order to qualify for tariff preference into the other party. This means they must have no input materials from third countries. For example, some meat products (fresh, chilled or frozen beef and lamb) must come only from animals born and raised in a party in order to qualify for preference.

For any good to qualify for preference it must be consigned directly between the two parties (Article 25). If transport involves transit through one or more non-parties the goods must not enter trade or commerce there or undergo anything more than simple logistical processes, such as unloading and reloading, repacking, or any operation required to keep them in good condition.

Granting preferential access in China under the FTA normally requires the presentation of a Certificate of Origin. In certain cases (Article 37), for example where the value of the consignment does not exceed US\$1,000 or an 'advance ruling' on origin has been obtained in accordance with the procedures (Article 52) of the Agreement, a Declaration of Origin can be used instead. The templates for these documents are in Annex 6 and Annex 7 to Chapter 4 of the FTA.

A Certificate of Origin can be issued only by an authorized body in the exporting party (Article 40).

Under the FTA New Zealand is obliged (Article 39) to require producers, exporters and importers to retain origin documents for the period specified in its domestic legislation, which is currently seven years.

4.4 Customs Procedures and Cooperation

The FTA contains provisions to ensure predictability, consistency and transparency in the application of customs laws and administrative procedures to ensure efficient and economical administration and the expeditious clearance of goods.

In the normal course of events, Customs administrations in both parties are required to release originating products within 48 hours of arrival (Article 57).

Traders can apply for advance rulings in respect of origin and tariff classification (Article 52). This may be done at least three months before the date of importation.

New Zealand exporters will be able to request advance rulings on origin direct from China Customs. There will be no need to channel such requests through a Chinese importer.

Applications for an advance ruling on tariff classification, on the other hand, will only be accepted from persons registered with China Customs. Chinese legislation requires applicants for an advance ruling on classification to have a physical presence in China.

4.5 Trade Remedies

The New Zealand–China FTA does not affect New Zealand's rights to apply anti-dumping, countervailing and global safeguard measures for trade with China, consistent with WTO rights and obligations.

Neither party is permitted to introduce or maintain any form of export subsidy on goods destined for the other party (Article 63).

Both parties are required to advise each other of the initiation of any safeguard investigation and the reasons for it (Article 64.2), and also of the initiation of any anti-dumping investigation in respect of goods from the other party (Article 62.2).

A party taking a global safeguard action may exclude imports of originating goods from the other party if such imports are non-injurious (Article 64).

The FTA also provides for application of bilateral transitional safeguards to imports during the period that tariffs are phasing out for any particular good and for two years beyond that. These allow either party to address situations of serious injury to a domestic industry caused by increased imports due to tariff reductions under the FTA by reverting to higher tariffs for a certain period.

To apply such a safeguard measure New Zealand would have to follow the requirements to undertake an investigation into the matter, publish the findings, and only apply an increase in tariff to the minimum extent necessary to remedy the injury being caused (Articles 66 to 72). Compensation, in the form of substantially equivalent concessions, would have to be provided to China except in the first year of a safeguard that has been taken as a result of an absolute increase in imports (Article 72).

4.6 Sanitary and Phytosanitary (SPS) Measures

The FTA maintains New Zealand's existing rights and obligations under the WTO Agreement on the Application of Sanitary and Phytosanitary Measures (SPS Agreement).

The FTA also provides for the development of mechanisms to allow parties to enhance implementation of the SPS Agreement, including the development of arrangements to determine and recognise the equivalence of each other's SPS measures, and each other's areas of pest freedom or low pest prevalence. Recognition of equivalence and regionalisation will be done through Implementing Arrangements established under Article 77.

The FTA emphasises communication between the competent authorities of each party, including the establishment of a Joint Management Committee on SPS matters (Article 88). There are specific procedures outlined in the chapter concerning notification, verification and import checks.

Decisions on matters affecting biosecurity and food safety will continue to be made and enforced in accordance with New Zealand's existing regulatory regime. The right of each country to determine its appropriate level of sanitary and phytosanitary protection is preserved.

4.7 Technical Barriers to Trade (TBT)

New Zealand's existing rights and obligations under the WTO Agreement on TBT are maintained under the FTA, including the right to adopt or maintain technical regulations necessary to ensure national security, the prevention of deceptive practices and the protection of human health or safety, animal or plant life or health, or the environment.

The parties will promote trade facilitation through joint work on standards, technical regulations and 'conformity assessment' procedures. They are encouraged to work towards equivalence of technical regulations and standards (Article 95) and towards acceptance of each other's conformity assessment procedures (Article 97). Where either party does not accept equivalence or the results of a conformity assessment procedure, it must explain the reasons for its decision. The parties will use international standards as a basis for their technical regulations (Article 94).

Article 100 establishes a Joint TBT Committee, which is to meet at least once a year. The Committee's functions include developing and adopting new annexes and Implementing Arrangements on TBT issues.

4.8 Electrical and Electronic Equipment Mutual Recognition Agreement (EEEMRA)

Under Annex 14 (EEEMRA), New Zealand's electrical safety and electromagnetic compatibility (EMC) regulators will be required to recommend conformity assessment bodies (CABs) to the Certification and Accreditation Administration of the People's Republic of China (CNCA) on the basis of accreditations and assessments to the Chinese Implementing Rules of the China Compulsory Certification (CCC) system by International Accreditation New Zealand (IANZ) and the Joint Accreditation System – Australia New Zealand (JAS-ANZ). CABs recommended in this way will be accepted by China for the purposes of the EEEMRA, as will CCC marks applied to products in conformity with the EEEMRA.

New Zealand regulators will also be required to report to the CNCA any recommended changes in the status of New Zealand CABs based on the New Zealand accreditation agencies' assessments and to investigate any concerns that the Chinese authorities may have.

In turn, New Zealand regulators will be required to recognise imports from China that comply with the provisions of the EEEMRA – namely that imports meet Chinese standards with deviations to meet New Zealand essential safety requirements and have been tested, inspected and certified by Chinese bodies in the same way as those products are tested in China for sale on Chinese markets.

To fulfil its obligations under Annex 14, New Zealand must also ensure that its regulatory framework for electrical safety and EMC permits legal action to be taken in respect of:

- the application in New Zealand of any CCC marks for electrical safety or EMC compliance to an electrical or electronic product exported, or intended for export to China, in a manner inconsistent with the requirements for that marking; and
- the production or use of documentation (including test certificates, inspection reports or certification documents) relating to electrical safety or EMC compliance of an electrical or electronic product exported, or intended for export to China, in a manner inconsistent with the requirements for that documentation.

The EEEMRA preserves the sovereign right of each party to set and apply mandatory requirements in relation to the covered products; and to take any measures deemed necessary in relation to non-compliant products.

4.9 Trade in Services

The FTA seeks to facilitate expansion of trade in services between New Zealand and China by establishing provisions for transparency and progressive liberalisation. But the FTA recognises the right of the parties to regulate services and the role of governments in providing and funding public services. The Chapter on services excludes services supplied in the exercise of government authority,¹³ government procurement, subsidies and some air transportation services (Article 105).

The FTA establishes the general obligation of national treatment (Article 106) and market access (Article 108) in sectors listed in the services schedules to the FTA, subject to the restrictions specified in the schedules. To the extent of associated commitments made in New Zealand's services schedule (Annex 8) these obligations entitle Chinese service suppliers wishing to operate in New Zealand to access the market without quota (market access) and on the same basis as domestic suppliers (national treatment).

Annex 8 has the effect of binding New Zealand's existing GATS commitments in the FTA. New Zealand has also made GATS-plus commitments covering Modes 1–3 in the following sectors:

- Other Education Services (training provided in specialist language institutions, language assessment services provided through Chinese language testing centres, and tuition in subjects taught at the primary and secondary levels in specialist institutions operating outside the New Zealand compulsory school system)
- Environmental Services (the provision of consultancy services, and the delivery of services, across the full range of environmentally related services)
- Computer Services (Maintenance and Repair of office machinery and equipment, including computers; and other computer services)
- Photographic Services
- Duplicating Services
- Construction services (consultancy related to construction services)

None of these commitments go beyond New Zealand's current regulatory environment or policy settings in any respect. There are also provisions to ensure that domestic regulation is administered in a reasonable, objective and impartial manner, and that regulations do not become unnecessary barriers to trade in services (Article 111). There are provisions also to encourage recognition of professional qualifications and registration (Articles 112 and 113).

¹³ Services supplied in the exercise of governmental authority are defined as a services supplied neither on a commercial basis nor in competition with one or more service suppliers.

New Zealand has made reciprocal MFN commitments requiring that any better treatment relating to services that New Zealand extends to third countries must also be extended to China. New Zealand's MFN commitments cover the following services sectors:

- Construction¹⁴
- Environmental services
- Services incidental to agriculture and forestry¹⁵
- Engineering services
- Integrated Engineering services
- Computer and related services
- Tourism services.

These commitments mean that any more favourable treatment granted by New Zealand to other countries in these sectors in the future would automatically need to be extended to China. Preferences granted to New Zealand's existing FTA partners – Australia; Thailand; Brunei, Chile and Singapore (under the P4 agreement) and the Pacific Islands under PACER – are excluded.

4.10 Movement of Natural Persons

The Movement of Natural Persons chapter of the FTA covers the categories of 'temporary entry' and 'temporary employment entry'. Temporary employment entry concerns access to the labour market of the host country. Temporary entry covers service suppliers who enter to provide a service (i.e. the GATS 'Mode 4' concept) and, reflecting the fact that the FTA covers goods and investment as well as services, extends the scope of temporary entry of business visitors to cover investors and goods sellers as well as services sellers. Definitions of these and other terms are provided in Article 125.

Temporary Entry

New Zealand's commitments (Annex 10) provide for entry of Chinese business visitors and installers/servicers for up to three months in any calendar year. Executives and managers are permitted to enter, as intra-corporate transferees, for up to three years. Also as intra-corporate transferees, senior specialists are permitted to enter for up to 12 months and other specialists – subject to labour market tests – for up to three years.

In each of the sectors listed in Section 4.9 where New Zealand has made GATS-plus commitments in respect of Modes 1–3, Chinese executives or managers may extend their initial three-year stay for up to a further three years if the need for the executive or manager still exists. Specialist personnel may also enter in these sectors for an initial period of up to three years, again extendable for up to a further three years if the need for the specialist still exists.¹⁶

¹⁴ The following construction services are covered: construction work for buildings; assembly and erection of prefabricated constructions; installation work; and building completion and finishing work.

¹⁵ China has entered a reservation against its commitment on this sector to the effect that it applies only to agreements China concludes with the countries (including New Zealand) which are members of the Organisation for Economic Cooperation and Development (OECD)

¹⁶ 'Specialist Personnel' are defined as natural persons with trade, technical or professional skills who are responsible for or employed in a particular aspect of an organisation's operations in New Zealand, and whose skills are assessed in terms of the applicant's employment experience, qualifications and suitability for the position.

While going beyond New Zealand's existing GATS commitments, all these commitments in as far as they relate to services (Mode 4) are within New Zealand's 2005 services offer in the WTO Doha Round. Extension of commitments to goods sellers and investors reflects the coverage of goods and investment under the FTA.

Temporary Employment Entry

New Zealand's commitments in the area of Temporary Employment Entry are set out in Annex 11. All the elements of Annex 11 are new commitments and apply only to China.

Commitments provide for entry as employees for up to three years, without labour market testing and subject to specified qualifications requirements, of up to:

- 200 entrants at any one time in each of the occupations of Traditional Chinese Medicine (TCM) Practitioners (including nurses) and Chinese Chefs;
- 150 entrants at any one time in each of the occupations of Mandarin Teaching Aides and Chinese "Wushu" Martial Arts Coaches; and
- 100 entrants at any one time in the occupation of Chinese Tour Guides.

Commitments also provide for entry as employees for up to three years, without labour market testing and subject to specified qualifications requirements, of up to 1000 entrants at any one time across 20 specified skilled occupations. Within the overall limitation of 1000, the number of entrants in any of the specified occupations is limited to a maximum of 100 at any one time.

The 20 specified occupations are all occupations in which New Zealand has an identified skills shortage and which appear currently on New Zealand's long-term skills shortages list. In practice therefore entry without labour market testing is already permitted as a corollary of the occupations being identified in skills shortage under general policy.

The effect of the commitments is that (within the 1000/100 caps) Chinese skilled workers can continue to enter without labour market testing even if labour market testing has been introduced in any of the specified sectors generally, and can continue to enter at the level of qualifications or work experience requirements specified in the FTA arrangement even if those qualifications or work experience requirements become more restrictive generally.

The list of 20 specified occupations is to be reviewed every five years by the Committee on Movement of Natural Persons. If agreement cannot be reached in a review, or as otherwise mutually agreed, the list existing at the time of that review will remain in place.¹⁷

Visa Facilitation

Annex 12 contains two new visa facilitation commitments by New Zealand: a commitment to provide a decision on Chinese student visa applications within 10 working days; and a commitment to create a new group transit visa for Chinese nationals.

¹⁷ The list of occupations upon entry into force is as follows (all occupations have attached qualification and experience requirements): Computer Application Engineer, Senior Test Analyst, Structural Engineer, Veterinarian, Fitter and Turner, Registered Nurse, Fitter Welder, University or Higher Education Lecturer, Early Childhood Education Teacher, Design Engineer – Electronics / Product Engineer, Auditor, Electronics Technician, Medical Diagnostic Radiographer, Medical Radiation Therapist, Nuclear Medicine Technologist, Boatbuilder, Film Animator, Electrician, Plumber, Automotive Electrician, Diesel Mechanic, Motor Mechanic.

Working Holiday Scheme

In conjunction with the FTA negotiations, but not as part of the FTA, New Zealand has agreed a working holiday scheme with China. The scheme is non-reciprocal and provides for a maximum of 1000 Chinese entrants per annum. As with other similar schemes, the scheme is an arrangement of less than treaty status. Entrants must be between 18 and 30 years of age, have a level of proficiency in English that is assessed as at least functional, and a minimum educational qualification that is equivalent within the Chinese system to a New Zealand student completing Year 13 and having gained Level 3 NCEA.

4.11 Investment

The principal obligations of the FTA in the area of investment concern national treatment and MFN non-discrimination, together with a range of investment protection disciplines and provision for investor recourse to arbitration procedures.¹⁸ As in the case of services, the obligations on investment do not apply in respect of subsidies or government procurement.

National Treatment

The national treatment obligation (Article 138) applies for investments after their establishment in New Zealand.¹⁹ Under this obligation New Zealand is required to treat all established investments made by investors of China no less favourably than domestic investments.

The obligation is subject to an exception for existing non-conforming measures, which in turn is subject to a 'ratchet' mechanism under which any improvement in such measures is automatically then locked-in for Chinese investors (Article 141.1). Furthermore the scope of the obligation is also limited to the best treatment contained in existing bilateral investment agreements (Article 141.3).²⁰ This means the FTA places no more constraint on the introduction of new non-conforming measures than exists under New Zealand's existing bilateral investment treaties with China and Hong Kong, China.

The provisions of the national treatment obligation safeguard New Zealand's existing regulatory and policy settings and, together with the exceptions available generally under the Agreement (see Section 4.17), do not compromise policy flexibility in areas of vital national interest.

Most Favoured Nation (MFN) Treatment

The MFN obligation (Article 139) applies in respect of all treatment of investments, both before and after establishment in the host market. This obligation requires that any better treatment relating to investment New Zealand extends to third countries must also be extended to China.

As in the case of services the obligation does not apply to treatment granted under any free trade agreement or multilateral international agreement in force or signed prior to the date of entry into force of the FTA, or to any measures taken as part of a wider process of economic integration between the parties to such existing agreements (Article 139.3 and 139.4). This means preferences granted to New Zealand's existing FTA partners – Australia; Thailand; Brunei, Chile and Singapore (under the P4 agreement), and the Pacific Islands under PACER – are excluded.

¹⁸ The national treatment and MFN obligations of the investment chapter do not apply to services investment that falls within the scope of the 'Mode 3' (commercial presence) category of service suppliers. For services 'Mode 3' investment those obligations are dealt with under the services chapter. The protection disciplines apply to all investment including those made in services sectors.

¹⁹ The New Zealand Overseas Investment Act 2005 will continue to apply to proposed investments in New Zealand by Chinese investors.

²⁰ New Zealand has existing bilateral investment treaties only with China and Hong Kong, China.

There is also an exception for differential treatment New Zealand may accord to third countries involving fisheries and maritime matters.

Investment Protection

The FTA contains provisions that, subject to specific limitations, require the free transfer of all payments relating to an investment, including capital necessary for establishing the investment, and the returns generated from that investment (Article 142.8).

The FTA also contains a range of protection elements relating to the treatment of investments once established in the host market.

These include protection from unjustified expropriation (Article 145) under which neither party may expropriate or nationalise the investments of investors of the other party, unless such an action is done for a public purpose; in accordance with domestic law; in a non-discriminatory manner; not contrary to any prior undertaking; and on payment of compensation which must be equivalent to fair market value.

The protection provisions incorporate the minimum international law standards of fair and equitable treatment and full protection and security (Article 143), and also provide for equitable treatment of investment in the event of compensation for losses arising from war, armed conflict or similar situations (Article 144).

None of the FTA's protection provisions contrast with New Zealand's existing regulatory settings or practice.

Investor/State Arbitration

Section Two of the Investment Chapter provides a mechanism for the compulsory settlement of disputes between foreign investors and the country in which the investment is made. If a dispute cannot be settled within six months through consultation and negotiation, and unless the parties to the dispute agree otherwise, the investor is able to submit the issue to conciliation or arbitration by the International Centre for the Settlement of Investment Disputes (ICSID) or arbitration under the rules of the United Nations Commission on International Trade Law (UNCITRAL). Three months notice has to be provided to the state party involved in the dispute. Where a dispute has been submitted to a competent domestic court, it may be submitted to international dispute settlement through the FTA provisions, but only if the investor has withdrawn the case from the domestic court before a final judgment has been reached. (Article 153)

This means that New Zealand could be required to be subject to international arbitration of a dispute brought by a Chinese investor. There are, however, a number of provisions designed to safeguard a government's right to regulate and to avoid exposure to frivolous expropriation claims.

Annex 13 to the expropriation provisions (Article 145) provides a number of additional protections for a government subject to international arbitration. It maintains the ability for a country to exercise its regulatory powers as may be reasonably justified in the protection of the public welfare, including public health, safety and the environment.²¹

²¹ In rare circumstances where such actions are discriminatory in their effect, either as against a particular investor or against a class of which the investor forms part; or where a country breaches a prior binding writing commitment to the investor, a case could be arguable.

Obligations on New Zealand to engage in any arbitration process are also shaped, and potential risks mitigated, by a series of other provisions set out in Section Two of the Investment Chapter. This includes a clear time-limit for the admissibility of claims, and allowing preliminary objections to avoid claims that are frivolous or manifestly without merit (Article 154). The provisions for compulsory investor state dispute settlement also provide for consultation on the consolidation of claims arising out of a common question of law or fact (Article 156); protection of confidential documents (Article 157); and limitation of any awards to real damages, costs and fees only, thus avoiding the possibility of punitive damages (Article 158). There is also the possibility for New Zealand and China to reach a joint decision on any issue disputed by an investor. Any such joint decision is binding on the arbitral tribunal (Article 155).

Finally investor-state arbitration applies only to disputes “directly concerning investments” made in the territory of the other party (i.e. actual investments which have been made). As a consequence, decisions related to the screening of investment into New Zealand under the Overseas Investment Act 2005 are not subject to such arbitration.

4.12 Intellectual Property

Both parties are required to establish and maintain transparent intellectual property rights regimes and systems that provide certainty over the protection and enforcement of intellectual property rights (Article 161.1). The FTA incorporates the provisions of the WTO TRIPS Agreement as relevant to the bilateral context (Article 161.3). This means that New Zealand rights and obligations vis-à-vis China under the TRIPS Agreement are actionable under the FTA.

There are also requirements for notification and information exchange, including in relation to enhancement of intellectual property rights enforcement (Article 163); and in relation to cooperation, including to promote awareness of intellectual property rights and systems (Article 164).

Each party has the obligation to enter into consultations at the request of the other party to resolve any intellectual property issue that arises within the scope of the Intellectual Property chapter (Article 166).

The FTA also recognises the right of a party to establish appropriate measures to protect genetic resources, traditional knowledge and folklore, consistent with international obligations including the TRIPS Agreement (Article 165).

4.13 Transparency

The FTA contains obligations ensuring transparency of laws, regulations, procedures and administrative rulings (Article 168). Due process requirements are established for administrative proceedings and reviews or appeals (Articles 169 and 170). These transparency provisions are consistent with New Zealand’s existing law and administrative practice.

4.14 Cooperation

The FTA sets out objectives and indicative activities for economic cooperation and cooperation on small and medium sized enterprises as a means to enhance the benefits of FTA (Articles 175 and 176).

The parties are required (Article 177) to enhance their communication and cooperation on labour and environment matters through the Environment Cooperation Agreement (ECA) and the Memorandum of Understanding on Labour Cooperation (MOU).

4.15 Institutional Provisions

The FTA establishes a FTA Joint Commission to oversee the implementation and development of the Agreement. The Commission is to meet in regular session once a year and at other times on request of either party (Article 181.2). The Commission will review the operation of the Agreement and consider any proposal to amend it within two years after entry into force of the FTA and at least every three years thereafter.

The Commission can meet at either senior official or vice-ministerial/ministerial level. New Zealand and China have existing vice-ministerial and ministerial mechanisms covering trade and economic matters being respectively the Joint Trade and Economic Commission and the Joint Ministerial Commission. The FTA (Article 182) provides that these bodies may meet in special session to consider matters arising under the FTA, in which case they shall exercise the powers and functions of the FTA Joint Commission meeting at vice-ministerial and ministerial level respectively.

4.16 Dispute Settlement

The FTA includes a robust and transparent dispute settlement mechanism to resolve any disputes that arise regarding the interpretation or implementation of the FTA, with provision for the establishment of an arbitral tribunal should consultations fail to settle the dispute. Rules of procedure for arbitral tribunals are provided in Article 191. The dispute settlement procedures in the FTA are in line with New Zealand's standard practice and accord with WTO procedures.

If, in any such dispute, New Zealand was found by an arbitral tribunal to be in breach of the Agreement there is an obligation to comply with the findings of the tribunal (Article 195). Should New Zealand fail to comply within a reasonable period of time there is an obligation to provide equivalent compensation agreeable to China or, absent a mutually satisfactory solution otherwise, China has the right to suspend the application of benefits to New Zealand of equivalent effect (Article 198).

4.17 Exceptions

Provided that such measures are not used for trade protectionist purposes, the FTA will not prevent New Zealand from taking measures (including environmental measures) necessary to protect human, animal or plant life or health, or public morals. This also applies to measures to prevent deceptive practices, protect national works, items or specific sites of historical or archaeological value, to provide support for creative arts of national value, or to conserve living and non-living exhaustible natural resources (Article 200).

The FTA will also not prevent New Zealand from taking any actions necessary to protect its "essential security interests" or to respond to a "serious balance of payments and external financial difficulty" (Articles 201 and 202).

Taxation measures are excluded from the FTA except to the extent they are covered by the WTO Agreement or Article 145 (Expropriation) of the FTA. Any bilateral agreement relating to the avoidance of double taxation takes precedence over the FTA (Article 204).

Provided that such measures are not used in order to avoid commitments, the FTA will not prevent New Zealand from taking measures for prudential reasons, including for the protection of investors and others owed a fiduciary duty by a financial service supplier, or to ensure the integrity and stability of the financial system (Article 203).

Provided that such measures are not used for protectionist purposes, there is also a general exception to ensure that the FTA will not prevent New Zealand from taking measures it deems necessary to fulfil its obligations to Māori, including under the Treaty of Waitangi (Article 205).

4.18 Final Provisions

The FTA applies to the territory of New Zealand, not including Tokelau. Consistent with New Zealand's commitments in the WTO and in the Trans-Pacific Strategic Economic Partnership (P4) Agreement, the Government is obligated to take "such reasonable measures as may be available to it" to ensure observance of the FTA by local government (Article 209).

4.19 Notification to WTO

Upon signature, New Zealand and China will need to notify the FTA to the WTO as a free trade area within the meaning of GATT Article XXIV (goods) and GATS Article V (services).

4.20 Memorandum of Understanding on Labour Cooperation (MOU)

The FTA (Article 177) provides that New Zealand and China are to enhance communication and cooperation on labour matters through the MOU.

The MOU contains the generally recognised 'core' trade and labour principles from the Government's 2001 policy framework. These include the recognition by both parties that it is both inappropriate to set or use labour laws, regulations, policies and practices for trade protectionist purposes, or to encourage trade or investment by weakening or reducing the protections afforded in domestic labour laws, regulations, policies and practices. The parties also acknowledge the value of transparency and domestic consultation in the formulation of their labour policies.

The specific (reciprocal) obligations for New Zealand under the MOU are (Article 3):

- To appoint a coordinator within six months to facilitate communication;
- To enter into non-binding arrangements where necessary to conduct specific activities or projects;
- To seek the funds required to support the cooperation activities and undertake coordination;
- For senior officials from both countries to meet within the first year of the operation of the MOU, and then on a regular basis every two years subsequently unless otherwise mutually agreed. These meetings serve to oversee the activities, set a cooperation programme, and serve as a channel for dialogue.

Both parties reaffirm their obligations as members of the international Labour Organisation (ILO), including their commitments under the ILO Declaration on Fundamental Principles and Rights at Work and its Follow-up.

Each party may invite its non-government sectors or relevant organisations to take part in cooperative activities or consult with its public over the operation of the MOU.

The MOU requires consultation in the event of an issue arising over its interpretation or application (Article 4). The parties are required to make every effort to reach consensus through cooperation, consultation and dialogue. If a party seeks a meeting to discuss any issue, the meeting needs to be held as soon as practicable and no later than 90 days following the request.

4.21 Environment Cooperation Agreement (ECA)

The FTA (Article 177) provides that New Zealand and China are to enhance communication and cooperation on environment matters through the ECA.

New Zealand and China recognise that the primary purpose of their environmental laws, regulations, policies and practices should be to achieve environmental objectives and that these should be administered in a way that contributes to the mutual supportiveness of these and other policies to achieve sustainable development. This draws on language agreed by the World Summit for Sustainable Development (WSSD) referencing the mutual supportiveness of trade, environment and development.

In addition to this general iteration of principles, the parties reaffirm commitments made at the Rio Earth Summit in 1992 and the WSSD in 2002, as well as those made under multilateral environment agreements.

The specific (reciprocal) obligations for New Zealand under the ECA are (Article 3):

- To appoint a coordinator at the level of a senior official within six months to facilitate communication;
- To enter into non-binding arrangements where necessary to conduct specific activities or projects;
- To seek the funds required to support the cooperation activities and undertake coordination;
- For senior officials to meet with their counterparts from China within the first year of the operation of the ECA, and then on a regular basis every two years subsequently unless otherwise mutually agreed. These meetings serve to oversee the activities, set a cooperation programme, and serve as a channel for dialogue.

In the case of an issue arising over the interpretation or implementation of the ECA, the parties are required to make every effort to settle it amicably through cooperation, consultation and dialogue. If a party seeks a meeting to assist in the resolution of any such issue, the parties are required to meet as soon as practicable.

Each party agrees to give opportunities for the members of its public or domestic non-governmental organisations to submit views relating to the operation of the instrument and may invite its non-government sector or relevant organisations to take part in identifying and carrying out cooperative activities. The ECA also encourages the parties to promote direct contact between their respective environmental protection organisations, enterprises and municipalities, research institutions and other entities.

5 MEASURES WHICH THE GOVERNMENT COULD OR SHOULD ADOPT TO IMPLEMENT THE TREATY ACTIONS

A small number of legislative and regulatory amendments are required to align New Zealand's domestic legal regime with certain rights and obligations created under the FTA and thereby enable New Zealand to ratify the FTA.

No legislative change is required to enable New Zealand to comply with the obligations under the MOU and ECA. New Zealand's legislation and practices are consistent with the key commitments contained in these instruments as well as to engage with China on labour and environment-related issues and consult with it as specific issues pertaining to the instruments arise.

The following legislative changes have been identified as being required:

- An amendment to the Tariff Act 1988 to enable the application of preferential tariff rates and bilateral transitional safeguards to imported goods under the China FTA.
- Amendments to the Fair Trading Act 1986 to extend the application of that Act to misleading and deceptive conduct relating to the supply of goods and services outside of New Zealand when necessary to meet New Zealand's obligations under an international agreement. The EEEMRA requires New Zealand to ensure that it has the power to take legal action related to goods for export that is similar to the power to take legal action for goods for sale in New Zealand;
- Amendments to the Electricity Act 1992 and the Radiocommunications Act 1989 to create regulation-making powers to enable legal action to be taken against persons who do not fulfil the requirements of international obligations while purporting to do so, and to provide for the seizure, sealing or impounding of products in cases of non-compliance with the requirements of the two Acts, including in relation to the EEMRA;
- An Order in Council under the Electricity Act 1992 and the Radiocommunications Act 1989 to enable legal action to be taken against persons who do not fulfil the requirements of international obligations while purporting to do so, and to provide for the seizure, sealing or impounding of products in cases of non-compliance with the requirements of the regulations, including in relation to the EEEMRA;
- Amendments to the Customs and Excise Act 1996 to create regulation making powers to provide for a system of authorised bodies charged with issuing certificates of origin for goods exported from New Zealand; and
- Amendments to the Customs and Excise Regulations 1996 to implement the agreed rules of origin and to create a system of authorised bodies charged with issuing certificates of origin.

It has been proposed that the New Zealand–China Free Trade Agreement Bill be included in the 2008 Legislation Programme with priority 2 (must be passed in 2008).

The Bill, Orders in Council, and regulations need to be passed this year as both parties intend for the FTA to enter into force on 1 October 2008. The goal of entry into force by 1 October is important because the FTA provides that tariff reductions shall occur upon entry into force of the FTA and thereafter on 1 January of each year. Under the Chinese tariff administration system, tariff cuts are implemented quarterly. The last date for implementation of tariff cuts for 2008 under this system is 1 October.

The proposed amendments need to be in place by the end of July to allow for the diplomatic notes bringing the FTA to be exchanged on 1 August 2008. The FTA would then enter into force two months after the exchange of diplomatic notes, 1 October 2008 (Article 213).

A comprehensive communications plan is in place to notify the business community, media and other stakeholders of how to benefit from and comply with the FTA and what the new requirements are:

- A dedicated website – www.ChinaFTA.govt.nz – is accessible through the websites of the Ministry of Foreign Affairs and Trade and New Zealand Trade and Enterprise (NZTE). The website contains detailed information on the text of the FTA, MOU and ECA, information about the bilateral relationship and extensive information on doing business with China. A ‘tariff finder’ tool enables traders to locate the tariff and ROO applying to their products. A summary of key outcomes and a synopsis of the FTA is also available;
- Officials are undertaking a series of ‘roadshows’ in five main centres to explain the details of the FTA, the opportunities and any requirements it presents for New Zealand businesses. These roadshows will be led by NZTE and MFAT but will include presentations from a number of agencies;
- A booklet setting out the key elements of the FTA and accompanying agreements, and information to assist businesses to benefit from and comply with the FTA is also planned for publication in mid-2008.

6 ECONOMIC, SOCIAL, CULTURAL AND ENVIRONMENTAL COSTS AND EFFECTS OF THE TREATY ACTIONS

6.1 Economic effects

6.1.1 Introduction

The FTA and associated instruments are expected to have an overall positive impact on the New Zealand economy. The economic impacts of the FTA are assessed in sections 6.1.3 and 6.1.4 under a framework outlined below, which has been used to assess both the NZ–Thailand CEP and the Trans Pacific Strategic Economic Partnership. This was also the underlying framework used for the modelling in the Joint FTA Study between New Zealand and China.

6.1.2 Relationship between trade and macroeconomic performance

Trade is an important factor in driving our national economic performance. Changes in trade can impact on the economy – for example, by affecting levels of prices, income or employment. Trade also affects macroeconomic performance in terms of the dynamics of the economy’s growth, stability and distribution. Extensive economic research has demonstrated that trade and growth are positively related, and an economy’s openness to trade has been linked to the explanation of differences in the economic growth rate of countries.

6.1.2.1 Static Effects

The direct impact of trade liberalisation on economic growth may be described as the “static” effects. These include the gains derived from:

- lowered tariff and non-tariff barriers in export markets generating higher export returns and volumes;
- domestic tariff liberalisation generating efficiency gains from a better allocation of resources (“allocative efficiency”), cheaper consumption and competitive effects.

Where improved market access under trade agreements enables exporters to achieve net increases in the value of their exports, this may translate directly into higher Gross Domestic Product (GDP), job growth and income. Moreover, the opportunity for local companies to increase market size through greater exports can increase productivity and efficiency through economies of scale. This may be achieved, for example, by the introduction of new processing technologies to service the larger market.

Output and productivity levels rise when resources shift to the more efficient sectors of the economy as tariffs reduce. In a previously tariff-protected sector, imports will be cheaper and can be expected to expand their share of the market. Domestically focused firms with higher cost structures shielded by tariff protection will respond by increasing their efficiency, reducing output sufficiently to reduce

their costs or shifting resources into more competitive production. Over time, these processes will lead to greater specialisation and increased comparative advantage. These effects are primarily driven through simple tariff removal, suggesting that countries that liberalise the most are likely over time to benefit the most. At the same time there are likely to be phases of adjustment that affect sectors in different ways.

The extent to which domestic prices change as a consequence of FTAs depends on the size of the distortions being removed. It is also dependent on the degree of competition already prevailing in the domestic market. In general, lower tariffs will result in lower domestic prices. Producers gain access to intermediate goods, thus making their finished products more competitive in the domestic and export markets.

When an economy liberalises under preferential trade agreements, the gains may be reduced or even reversed due to the phenomenon of trade diversion. This describes situations where imports are sourced from FTA partners due to the margin of preference they enjoy over more efficient producers. Where the FTA partners are already internationally competitive suppliers, however, the risk of trade diversion and thus welfare reduction is lower.

The quantitative impact of changes to China's tariff regime on New Zealand exporters to China, and the impact on New Zealand domestic sectors of changes to the New Zealand tariff regime are considered in section 6.1.3.2.

6.1.2.2 'Second-Order' Effects

An increase in openness to trade helps spur productivity increases and growth within a country through more efficient allocation of resources, the stimulation of innovation and the transfer of knowledge and technology between countries. Productivity increases derived from the more efficient allocation of resources following tariff removal ('allocative efficiency gains') are considered to be static gains and were described in section 6.1.2.1.

The other source of productivity growth flowing from trade agreements is 'dynamic productivity gains'. These effects are harder to quantify. They accumulate over time and may be attributable to the downstream effects of trade agreements, rather than the immediate impacts driven by tariff removal and improvements in market access alone. They are known as 'second-order' effects. How they are generated is outlined in the paragraph below.

Trade and investment may be stimulated through both the market access liberalisation provisions of FTAs and improvements in the regulatory framework brought about by the FTAs which increase transparency, fairness and predictability for businesses. As a result of the facilitation of increased trade and investment flows, companies are more exposed to competition and international benchmarking and develop stronger links with international business partners. Such exposure helps maintain New Zealand companies at the leading edge in terms of best practice across a range of issues (innovation, technology, knowledge, research and product/service development, etc). Spillovers from this process into the domestic economy can include the generation of ongoing productivity improvements (dynamic productivity gains) across the wider economy.

The 'second-order' effects relating to the regulatory frameworks for bilateral trading relationships under FTAs are of particular relevance. These gains in the case of the FTA are assessed in section 6.1.4.

6.1.2.3 Measuring the Macroeconomic Impact of FTAs

FTAs impact on the macroeconomic indicators that measure the growth and trade flows of our economy.

Economic theory suggests that the most relevant measure of the quantifiable impact of FTAs on the New Zealand economy as a whole is through the change in 'welfare' (that is, the value to New Zealand consumers of a FTA in terms of enhanced income). The preferred welfare indicator is 'real consumption' – the aggregated quantity of goods and services that the household can consume given current and future income flows. Changes in real GDP reflect only changes in the overall level of economic activity and not changes in net national income or welfare.

In broad terms, the magnitude of the macroeconomic effect of FTAs will be determined by the following factors:

- the contribution of exports and imports to the economy
- the size of the barriers to trade being addressed in the FTA
- the relative significance of bilateral trade between the two countries
- the extent of dynamic productivity improvement.

6.1.3 Static effects on the New Zealand Economy of the FTA

When applied to the FTA, the framework for assessing the economic impacts suggests that the FTA will make a significantly positive contribution to New Zealand's economic growth prospects over time.

6.1.3.1 Magnitude of Effects

The section below applies the three factors outlined in section 6.1.2 to the FTA and explains why the overall impact of the FTA on the New Zealand economy is expected to be positive.

Contribution of trade to the New Zealand economy

Overseas trade makes a fundamental contribution to the New Zealand economy with exports of goods and services accounting for around 29 percent of GDP. As a small, geographically isolated nation, New Zealand firms are reliant on access to foreign markets to gain economies of scale and remain internationally competitive.

Our modern economy is also dependent on imports to help supply the range of goods and services to our producers and consumers. Imports are currently worth around 30 percent of GDP. New Zealand's ability to engage and compete successfully in the global economy will, therefore, be a defining factor in our future economic performance. The more successful New Zealand is at trading, the higher the standard of living it can afford.

Size of the barriers to trade being addressed in the FTA

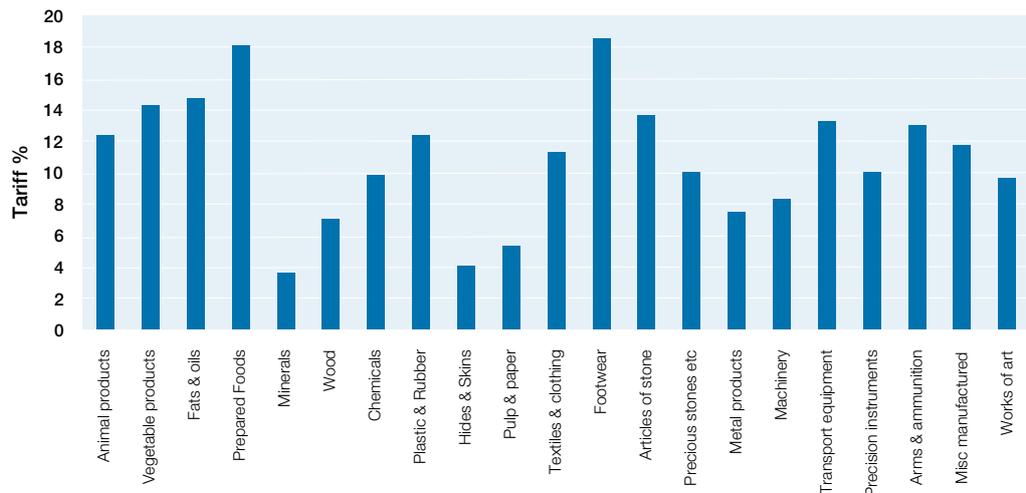
China

In 2005 China's average applied tariff was 9.9 percent across all products, with a higher average of 14.6 percent applying to agriculture products.²² There is little difference between these applied tariff rates and China's WTO bound rates, which set the upper limit on China's possible tariffs. The bound rates are on average 10 percent for all products and 15.3 percent for agriculture products.

China has tariffs applying to the majority of products, with only 8.5 percent of tariff lines currently duty free.

China operates a Tariff-rate Quota (TRQ) system on a range of primary products including wheat, maize, rice, vegetable oils, sugar, some fertilisers, wool and cotton. Of these products, wool is the only area of significant trade interest for New Zealand. The WTO wool TRQ has in-quota rates of 1 or 3 percent, with out-of-quota rates of 38 percent.

TABLE 1 CHINA'S APPLIED AVERAGE TARIFFS 2005



Source: *Customs Import Tariff of the People's Republic of China 2005*

Notes: Excludes in-quota rates.

New Zealand

New Zealand is a relatively open economy, with 59 percent of all tariff lines currently duty free. In 2005 New Zealand's average applied tariff across all products was 3.5 percent, with higher tariffs of between 17 and 19 percent applying to certain clothing and footwear products and carpet. The Post-2005 Tariff Policy agreed by Cabinet in September 2003 set a programme for reduction of those high tariffs down to 10 percent by 1 July 2009 and for all other tariffs between 5 and 12.5 percent to be harmonised at 5 percent by 1 July 2008.

Relative significance of New Zealand–China bilateral trade

The Joint Study demonstrated that New Zealand and China have a complementary goods trading relationship and bilateral trade flows have grown significantly in recent years.

New Zealand exports to China have increased 245 percent since 1996 and amount to around \$2 billion per year. Over the same period, imports from China have increased 520 percent to almost NZ\$5 billion in calendar year 2006. This growth in imports is consistent with the explosive growth in Chinese exports worldwide, which have grown 506 percent in the ten-year period to 2006.

China is New Zealand's fourth largest individual country destination for exports and third largest source of imports. From China's perspective, New Zealand ranks as China's 57th largest export destination and 49th largest source of imports.

Detailed data on the composition of bilateral trade is set out in the tables below.²³

TABLE 2 TOP TEN NEW ZEALAND EXPORTS TO CHINA

Product	Export value (NZ\$ million average 2004–06)	% of total exports
Dairy produce	363.0	18
Wood and articles of wood	252.9	13
Wood Pulp	170.5	9
Wool	167.1	8
Raw hides and skins	110.8	6
Other food preparations	93.3	5
Fish and other seafood	90.1	4
Paper and paperboard	65.5	3
Animal or vegetable fats and oils	64.8	3
Ores, slag and ash	57.4	3
Subtotal top ten exports	1,435.3	72
Total exports	2,001.3	

Data Source: World Trade Atlas

²³ Use of 2006 data reflects the fact that 2006 was the most recent calendar year data available to negotiators. Data for the year to June 2007 indicates that New Zealand's imports from China are now roughly \$5.3 billion. The data for New Zealand's exports to China are measured as China's recorded imports from New Zealand. Presentation of 3-year average figures in Tables 2, 3, 4 and 5 is again consistent with data used by negotiators. Average figures were used as a way of smoothing out abnormal fluctuations that can occur in annual data and because use of 3-year averages reflects international practice in the base calculation of product-specific safeguard measures.

TABLE 3 TOP TEN NEW ZEALAND IMPORTS FROM CHINA

Product	Import value (NZ\$ million 2004–2006)	% of total imports
Machinery	706.0	18
Electrical machinery	642.3	17
Apparel and clothing (knitted)	364.2	9
Apparel and clothing (not knitted)	330.4	9
Furniture	189.2	5
Toys and games	177.0	5
Footwear	158.2	4
Iron or steel articles	124.9	3
Plastics and articles thereof	111.6	3
Textiles	104.8	3
Subtotal top ten imports	2908.6	75
Total imports	3838.2	

Data Source: World Trade Atlas

6.1.3.2 Specific Market Access Outcomes

The FTA will result in the removal of tariffs, and reduction of other impediments to bilateral trade with China over time.

That tariff elimination will take place on the basis of several categories as described below and in Table 4.

Other than for certain 'sensitive' products as outlined below, the majority of exports will fall into one of the following three categories:

(1) Immediate elimination: tariffs at or below 5 percent will be eliminated upon entry into force of the agreement. This category will mean that approximately 35 percent of current trade is duty free on day one. Specific products that will benefit from this immediate elimination include certain types of fibreboard, fish meal, scrap metal (copper and aluminium), coking coal and iron slag.

Approximately 75 percent of New Zealand's current wool exports (6 percent of total exports to China) will be duty free from 1 January 2009.

(2) Elimination over 5 years: tariffs in the range 6–20 percent will be subject to annual cuts over 5 years (on a linear or straight-line basis) through to full elimination on 1 January 2012.²⁴ Products in this category account for 31 percent of current New Zealand exports to China and include products such as infant milk formula, yoghurt, casein, frozen fish, frozen fish fillets, methanol, animal fats & oils, apples and wine.

²⁴ These dates assume entry into force of the FTA in 2008.

TABLE 4 TARIFF ELIMINATION UNDER THE FTA

Category		Modality	% exports	Key export products	% imports	Key import products
General product categories	1	Immediate elimination of all tariffs 5% and below (includes elimination from 1 January 2009 of tariffs on wool through establishment of a CSTQ for 25,000 tonnes of NZ's wool exports and 5% annual growth)	41.3	Certain types of fibreboard, fish meal, scrap metal (copper and aluminium), coking coal and iron slag	38.6	37% of trade is already duty free
	2	5 year phase out for NZ tariffs in the range 6–12% and Chinese tariffs in the range 6–20%	31.1	Infant milk formula, casein, frozen fish, frozen fish fillets, methanol, animal fats & oils, apples and wine	35	Steel, whiteware plastics, furniture, tyres, pens
	3	Initial cut to the threshold level then a linear year phase out by year 6. (Chinese tariffs above 20%, and NZ tariffs above 12%)	0.1		0.2	Some fabrics, twine
Sensitive products	1	7 year linear phase out			4.2	Textiles, clothing, footwear and carpets
	2	9 year linear phase out	4	Edible offal, oranges, orange juice, milking machines Sheep & beef meat, kiwifruit, sheepskins	21.5	Clothing and footwear
	3	10 year linear phase out accompanied by a quantity-based safeguard	2.5			Butter, cheese and liquid milk
	4	12 year linear phase out accompanied by a quantity-based safeguard and a mid-term review mechanism	15.2			Skim and whole Milk powders
MFN products		No tariff reductions under the FTA. The prevailing MFN tariff rate applies.	4			Paper products and certain processed wood products.

Data Source: World Trade Atlas

(3) Elimination of over 6 Years: tariffs greater than 20 percent will be reduced to 20 percent on day one, and then reduced to zero by year 6, using a linear phase out, and providing full tariff elimination on 1 January 2013. Products in this category account for only 0.1 percent of current New Zealand exports to China.

China indicated a degree of domestic sensitivity to imports of certain products and these have been given some special treatment under the agreement.

Wool

The FTA creates a country-specific tariff quota (CSTQ) for New Zealand wool exports to China. The CSTQ will provide duty free treatment for an initial quantity of 25,000 tonnes. This represents approximately 75 percent of current New Zealand wool exports to China. This initial quantity will grow by 5 percent annually through to a maximum of 36,936 tonnes in 2017. For wool tops the initial CSTQ level of 450 tonnes is equivalent to 120 percent of New Zealand's current exports. It also increases by 5 percent per annum over 8 years to a level of 665 tonnes. Any increases beyond that date will be by mutual agreement between the parties. Access to the CSTQ will not impinge on right of New Zealand exporters to access to China's WTO MFN quota for wool.

Dairy

Dairy products were the most import sensitive area for China. Tariffs on cheese, butter and liquid milk will be phased out over 10 years while tariffs on milk powders will be phased out over 12 years. For all these products China will have recourse to a product-specific safeguard mechanism. This special safeguard is a temporary mechanism, available for China during the phase-out period and for an additional 5 years once tariffs have been eliminated. The safeguard allows China to apply an additional tariff on imports of the specified products above an agreed trigger level. The initial trigger levels are all at or above current export levels and grow at a rate of five percent compounding annually over the life of the mechanism. If triggered, the special safeguard allows China to raise tariffs up to the MFN rate for one year. The MFN rate is currently 10 percent for milk powders and butter, 12 percent for cheese and 15 percent for liquid milk.

Tariffs on other dairy products, including infant milk formula, casein, yoghurt and whey will be subject to a 5 or 6-year tariff phase out.

A mid-term review mechanism has also been included in the dairy outcome under the FTA. Under this mechanism, the Trade in Goods Committee will undertake a review following the year 6 tariff cut (in 2013 assuming a 2008 entry into force) to determine whether increased imports from New Zealand have caused an overall negative impact on the Chinese dairy industry. If the Committee determines that an overall negative impact has occurred, then the next scheduled tariff reduction, on whole and skim milk powders only, may be postponed by one year. This extension can only be made if both parties agree to it. Such a determination can only be made if the review demonstrates, on the basis of objective evidence, the existence of a causal link between tariff reductions under the Agreement, increased imports of the products concerned from New Zealand and the overall negative impact on the Chinese dairy industry.

Other sensitive products

A further 32 product lines have been classified as sensitive by China and will be subject to a linear tariff phase out over 9 years. These products include beef and sheep meat, edible offals, sheepskins and kiwifruit. These products combined account for 4 percent of current exports to China.

MFN Products

China has created a special category for those products that will not be subject to tariff cuts under the FTA but for which the prevailing MFN rate will continue to apply. These products fall into two broad areas:

- **Tariff Rate Quota (TRQ) Products**

For a range of primary products (wheat, maize, rice, vegetable oils, sugar, some fertilisers and cotton) China will not provide any additional market access under the FTA beyond the access already available to New Zealand exporters through the TRQs for these products established under the WTO. New Zealand has no significant exports to China in any of these products.

- **Certain Wood and Paper Products**

For a range of processed wood and paper products China has not offered to make any bilateral tariff reductions under the FTA. As part of its accession to the World Trade Organisation China agreed that any preferential commitments it makes on wood and paper products in an FTA must then be offered to all WTO Members.

The exclusion is limited to paper products and certain processed wood products. In total, these products account for 4 percent of current exports to China.

While China will not make tariff reductions under the FTA for these products, it has agreed that the WTO commitment mentioned above will apply to these products. This obliges China to give to New Zealand any preferential treatment that it offers to any third country and means that New Zealand importers will not be at a competitive disadvantage vis-à-vis other suppliers to China.

Logs, sawn timber and wood pulp (with a current average export value of \$377 million) comprise the bulk of New Zealand's current forestry exports and already enter China duty free. That zero duty will be bound under the FTA. That will provide some potential advantage to New Zealand exporters as China has scope in its WTO tariff bindings to apply a 1 percent tariff on logs and sawn timber.

Other key export areas

- **Raw hides and skins**

This category has an export value of NZ\$110.8 million (average over 2004–2006) and amounts to 6 percent of New Zealand's total exports to China. Most products are in the category for tariff elimination over 5 years. Those products which currently have a tariff of 5 percent or less will become duty-free on entry into force of the FTA. Some products (sheep and goat skins) are included in the sensitive category described above.

- **Other food preparations**

This category has an export value of NZ\$93.3 million (average over 2004–2006) and amounts to 5 percent of New Zealand’s total exports to China. Except for those products included in China’s sensitive category (described on previous page) for elimination over 9 years, tariffs on most of these products will be eliminated over 5 or 6 years.

- **Fish and other seafood**

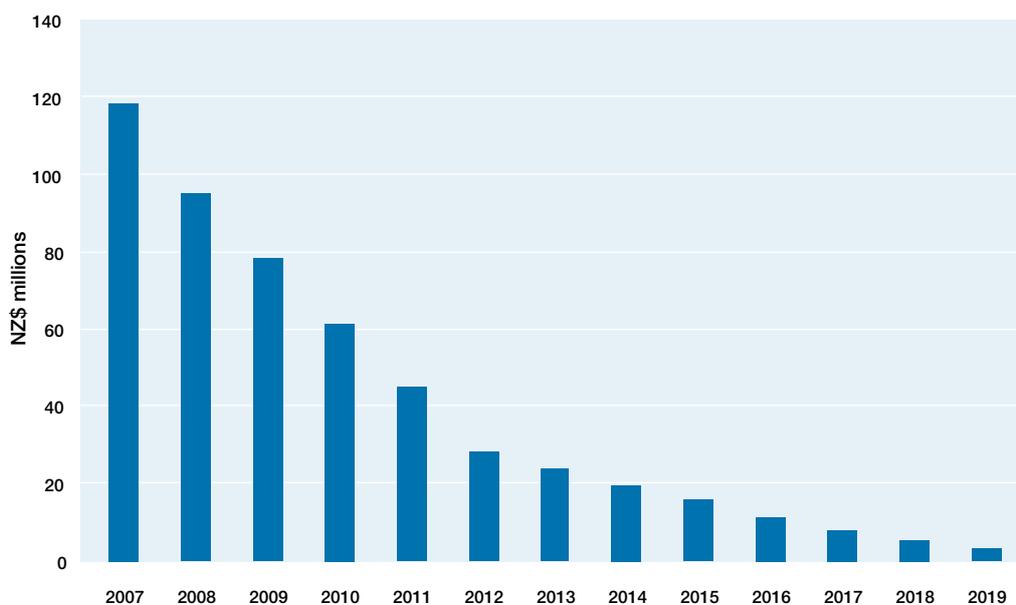
This category has an export value of NZ\$90.1 million (average over 2004–2006) and amounts to 4 percent of New Zealand’s total exports to China. Other than for products such as live fish fry and shellfish for cultivation, most of which are already duty-free, tariffs on these products will be eliminated over 5 years.

- **Animal or vegetable fats and oils**

This category has an export value of NZ\$64.8 million (average over 2004–2006) and amounts to 3 percent of New Zealand’s total exports to China. Most tariffs on these products will be eliminated over 5 years.

New Zealand exports to China incurred duty payments averaging \$118.5 million annually over 2004–2006. Table 5 shows the estimated reduction in duty payments on current exports to China over the implementation period of the FTA. Increased exports in response to tariff liberalisation will generate additional duty savings on a cumulative basis.

TABLE 5 REDUCING DUTIES ON NEW ZEALAND EXPORTS TO CHINA UNDER THE FTA



Data Source: World Trade Atlas

6.1.3.3 Potential Impacts on New Zealand of Tariff Liberalisation under the FTA

China is New Zealand's third largest source of imports overall, and is the biggest supplier of products in the traditionally sensitive areas of textiles, clothing, footwear and carpets (TCFC). It is these product areas where New Zealand maintains the highest applied tariffs, currently up to 15 percent. China is also a significant source of imports of a wide range of manufactured products where New Zealand tariffs are in the 5 to 7 percent range, such as furniture and plastics. Even for some product areas where current imports from China are at low levels, such as whiteware, steel and carpets, domestic industry has indicated a concern about potential imports from China, based on a global import sensitivity of these products. Table 6 shows these key areas of domestic sensitivity and the corresponding tariff outcomes under the FTA.

TABLE 6 TARIFF OUTCOMES IN KEY AREAS OF DOMESTIC SENSITIVITY

	Trade value (NZ\$ million 2004–2006)	Duty paid (NZ\$ million 2004–2006)	Tariff eliminated by
Less highly traded clothing/ textiles	141.9	12.3	2014
Most highly traded clothing/ textiles	657.4	117.9	2016
Carpets	3.6	0.3	2014
Less highly traded footwear	11.6	1.50	2014
Most highly traded footwear	146.6	23.9	2016
Furniture	189.2	8.7	2012
Articles of Steel	124.9	2.4	2012
Plastics	111.6	3.8	2012
Whiteware	10.23	0.3	2012

Data Source: World Trade Atlas

The combination of a high volume of imports from China in the area where New Zealand maintains its highest levels of tariff protection indicates that there is the potential for tariff reductions under the FTA to have an impact on domestic industry. That fact was recognised during the Joint Study, which recommended that both sides take this into account during the negotiation.

Consultation with New Zealand industry has shown that views vary on the issue of elimination of New Zealand tariffs for China. However, three themes were evident in the majority of import-sensitive sectors:

- Businesses are planning on the basis of the post-2005 tariff programme that sets out unilateral cuts in tariffs through to July 2009;
- There was general comfort with the phase out schedules agreed under New Zealand's previous FTAs, which sees a high percentage of tariffs eliminated on day one, further mid-range tariffs eliminated by 2008/10 and the highest, most sensitive, tariffs eliminated by 2015;
- There was a desire to ensure that the trade remedies regime available under the WTO to protect domestic industry from import surges and unfair competition was not watered down in the FTA.

The outcome of the negotiation has delivered a phase out schedule that is consistent with that agreed under other FTAs. For the period through to 2009 the preferential rate available to China under the FTA will not, in the majority of cases, be lower than the prevailing MFN rate under the scheduled unilateral tariff cuts. However, all FTA rates will eventually reduce to zero. Specific outcomes include:

- Tariffs on the most highly traded clothing and footwear products and some textile products will be phased out on a linear basis by 2016. This is one year longer than the end date agreed by New Zealand in the NZ–Thailand CEP and the Trans-Pacific SEP.
- Tariffs on carpet, the remaining clothing, footwear products and certain highly traded textile products will be phased out on a linear basis by 2014.
- There is less immediate tariff elimination in the China FTA than in New Zealand's previous FTAs. The China FTA provides for elimination of tariffs at 5 percent or below, whereas previous FTAs also included immediate elimination of some higher tariffs. A small number of non-sensitive textile products are included in this category. These are products for which there is no known domestic manufacture and for which extensive tariff concessions apply, so that the products already enter duty-free.
- The FTA provides for phase outs for mid-size tariffs (in the range 6–12.5 percent) by 2012, compared to 2008/2010 under previous agreements. This includes products such as whiteware, steel, plastics and furniture. Some less sensitive textile and clothing products are also included in this category.
- New Zealand has retained a slower initial tariff phase out programme for particular steel and whiteware products to ensure that tariff reductions under the FTA go no faster than the unilateral tariff programme through to 2009, in line with strong industry views in these sectors.

The Trade Remedies chapter has preserved New Zealand's rights to apply anti-dumping, countervailing and safeguard measures for trade with China, consistent with WTO rights and obligations. The FTA also has an additional bilateral transitional safeguard mechanism that can be applied to imports during the period that tariffs are phasing out for any particular good and for 2 years beyond that. This allows either party to address situations of serious injury to a domestic industry caused by increased imports due to tariff reductions under the FTA by reverting to higher tariffs for a certain period.

China already has significant import share in many of New Zealand's import-sensitive sectors. The phase-out periods included in the agreement should help to mitigate any negative impacts of the tariff reductions under the FTA by allowing domestic industry some time to adjust. Should some negative effects emerge, New Zealand can have recourse to all existing WTO trade remedies measures and the additional bilateral safeguard mechanism.

6.1.3.4 Potential Impacts on the New Zealand Economy of the Services Outcome

As noted in Section 4.9, the services sectoral commitments New Zealand has made to China are all within existing policy settings. In practice, therefore, these sectors are already open to foreign competition. It is not expected that the binding of this degree of openness to China in the FTA will have any adverse impact on the New Zealand economy.

The commitments New Zealand has made to China in respect of temporary access to the New Zealand employment market for specified categories of Chinese workers are a significant new feature of the FTA in comparison to New Zealand's other FTAs. (The only comparable commitment New Zealand has made in the context of any other FTA was in respect of Thai chefs in the New Zealand/Thailand Closer Economic Partnership Agreement.)

While reflecting the high priority China attached to an outcome of this type, it is not expected that these commitments will have a significant impact on the New Zealand labour market, including on the ability of New Zealanders to secure employment in the areas in question.

The 20 specified skilled occupations are all occupations in which New Zealand has an identified long-term skills shortage, while the occupations with Chinese characteristics are occupations in which employees from China can bring particular skills not present in the domestic labour market. There are also limitations on the total number of potential entrants – 800 in the specified occupations with Chinese characteristics and 1000 across the 20 specified skills occupational areas, and limitations on the maximum number of entrants in any one sector. Together with the requirement to observe New Zealand labour market conditions, these features are designed to avoid commitments under the FTA being used to displace New Zealand workers while offering economic opportunity to China under the Agreement.

On the export side, China's non-education services sectoral commitments constitute a useful improvement over China's GATS commitments in the sectors in question. The inclusion of MFN commitments on sectors of export interest to New Zealand, including tourism, will also help ensure the competitive position of New Zealand services exporters is not eroded. Over time, these commitments should encourage greater exports of these services from New Zealand to China.

In respect of education, New Zealand's single most important services export sector after tourism, China's commitment to include specified New Zealand educational institutions on the China Ministry of Education "Study Abroad Website" addresses what has in the past been a major problem for New Zealand education services exporters to China.

China's agreement that both parties will jointly initiate work at the official level on the evaluation of the quality assurance criteria for qualifications which include a distance delivery component is also an important step forward given that New Zealand education suppliers are increasingly looking to deliver their services via electronic platforms.

It is difficult to measure the specific economic effect of the outcome of the services component of the FTA due to the difficulty in collecting sufficiently disaggregated data on a sectoral basis upon which to base quantitative analysis.

The Joint Study suggested that both sides should make gains in the services area as a consequence of an FTA which removed barriers to services trade in both directions. The gains for New Zealand were estimated at around US\$100 million over the 20-year period 2007–2027.

Given that the outcome on services is less ambitious than New Zealand had hoped, the gains for the economy are likely to be less than those projected in the Joint Study results. The Joint Study recognised that the modelling results, however, do not account for the possible 'demonstration' effect that conclusion of China's first FTA with a developed country might have in the business world. The stimulus the FTA is likely to give to private sector interest in both countries in doing business together could lead to a more significant expansion in bilateral services trade than the modelling would suggest. The FTA outcome also provides the basis for further liberalisation of bilateral services markets over time.

6.1.3.5 Potential Impacts on the New Zealand Economy of the Investment Outcome

The investment relationship between China and New Zealand is relatively small when compared with other New Zealand investment relationships. It is, however, a growing relationship with total investment stocks between the two countries on the rise. New Zealand's total stocks of investment in China have risen from NZ\$101 million in 2002 to NZ\$333 million in 2006. In the same period China's total stocks of investment in New Zealand have risen from NZ\$1.04 million to NZ\$1.66 billion.

Because of the historically small investment relationship, modelling in the Joint Study assumed that the change in investment and capital stock as a consequence of the FTA would be minimal and hence none of the estimated gains identified in the Joint Study were specifically attributed to the investment area. As noted in Section 3.10, however, there are a number of positive elements in the FTA outcome on investment – commitments on MFN and post-establishment national treatment together with provisions on investment protection and investor-state arbitration – that should contribute to an increase in investor confidence in the investment regime between the two countries. This combined with the positive demonstration effect of concluding the FTA, as noted above, could result in increases in bilateral investment flows.

Given the importance of the availability of foreign capital and opportunities for internationalisation of New Zealand business in New Zealand's economic development, a growing bilateral investment relationship with China resulting from the FTA would be expected to have a positive impact on the New Zealand economy. The FTA outcome, however, does not compromise New Zealand's regulatory environment and New Zealand's investment screening regime under the Overseas Investment Act 2005 will continue to apply to investments from China.

6.1.3.6 Conclusions Regarding Static Gains to the New Zealand Economy

The Joint Study found that the static gains (comprising removal of tariffs and non-tariff barriers on merchandise trade, and services liberalisation) account for around two-thirds of the total GDP and welfare gains estimated to arise under the FTA.

The key finding of the study on 'static' gains was:

- Over the 20 year period following entry into force the static gains to New Zealand from the FTA in welfare (real consumption) terms were estimated at around US\$1.6 billion (a maximum of 0.35 percent above baseline).

As noted above, the services and investment components of these estimated gains were relatively small. The bulk (roughly US\$1.5 billion) of the estimated gains were attributed to the removal of barriers to merchandise trade.

The Joint Study assumed immediate comprehensive elimination of identifiable barriers to New Zealand–China bilateral trade. On merchandise trade the final agreement does not deliver immediate tariff elimination in all sectors but, with the exception of 4 percent of New Zealand exports in the paper and processed wood products area, it does deliver tariff elimination on traded products over time and provides a bilateral framework for addressing non-tariff barriers.

On non-tariff barriers the FTA contains a general prohibition on non-tariff measures that are not consistent with the parties WTO rights and obligations and a requirement to ensure that permitted non-tariff measures do not create unnecessary obstacles to bilateral trade (Article 11).

This will provide a bilateral course of action under the FTA on any unjustifiable non-tariff measures. It also provides a basis for the development, again over time, of outcomes designed to facilitate trade and reduce associated transactions costs in particular regulatory areas and for specific products. The Mutual Recognition Agreement on Electrical and Electronic Equipment (EEEMRA) is one such outcome that can be expected to provide a foundation for similar approaches in other product areas.

With the greater part of the estimated gains in the Joint Study accruing from goods market liberalisation, the FTA as negotiated should deliver the bulk of the estimated ‘static’ gains, albeit over time as opposed to the immediate liberalisation scenario modelled in the Joint Study.

6.1.4 ‘Second order’ effects on New Zealand of the FTA

As outlined in section 6.1.2.2, increased trade and services flows facilitated by regulatory improvements under trade agreements can help generate wider dynamic productivity gains throughout the national economy. These effects are harder to quantify. They accumulate over time and may be attributable to the downstream effects of trade agreements over time, rather than the more immediate impacts driven by tariff removal and other market access improvements alone.

This section identifies those aspects of the FTA that might produce ‘second-order’ benefits for the New Zealand economy. These relate to the provisions outlined in sections 3 and 4 and in particular include: customs procedures, TBT, SPS measures, intellectual property rights, and consultation and dispute settlement procedures. The primary provisions that will improve the regulatory framework governing trade with China include:

- transparency requirements – these cover general laws and policies affecting trade and investment (Chapter 13) as well as specific areas such as consumer protection from deceptive practices or the use of false or misleading descriptions in trade (Article 12), international agreements on trade in services and investment (Articles 116 and 146), movement of natural persons (Article 131), and intellectual property (Article 163);
- technical cooperative mechanisms for minimising the impact of regulations on trade and enhancing understanding of each other’s regimes – for example in respect of customs procedures (Articles 47 and 50), SPS measures (Article 85 and 87) and TBT (Articles 96 and 100);
- mechanisms that provide for the development of arrangements to recognise the equivalence of the other party’s SPS measures (Article 81) and regional disease status (Article 80);

- mechanisms to facilitate reduced transactions costs in merchandise trade – including through harmonisation and recognition of the equivalence of the other party’s technical regulations and conformity assessment procedures (Articles 95 and 97) – as illustrated in the agreed MRA on electrical and electronic equipment;
- mechanisms (ranging from consultations to full bilateral dispute settlement mechanisms) if necessary to resolve concerns about SPS measures (Article 88) or TBT (Article 101);
- mechanisms for promotion of greater certainty and predictability – for example advance rulings on tariff classification or origin (Article 52), notification of changes in SPS health status or new SPS measures (Article 86) and advice about the initiation of anti-dumping or safeguard actions (Articles 62, 64 and 71);
- mechanisms for recognition of standards or criteria for licensing or certification of services suppliers (Article 112) and encouraging recognition of professional qualifications (Article 113);
- cooperation provisions and opportunities for policy dialogue – including on promotion and facilitation of investment (Article 151) and on intellectual property rights and their enforcement (Article 164);
- built-in mechanisms for monitoring and reviewing the operation of the FTA – notably through Joint Commission meetings and three-yearly reviews (Chapter 15).

Collectively, these provisions should, over time, significantly enhance the predictability and transparency of the New Zealand trading relationship with China. Taken together with the market access improvements related to reduction of tariffs and services in the static effects section (section 6.1.3), these are expected to help generate the ‘second-order’ effects related to dynamic productivity.

Although it is not possible to quantify the precise economic effects of these provisions, it can be assumed that New Zealand companies are more likely to benefit than lose from the application of improvements to the regulatory framework governing the trade and economic relationship with China. The Joint Study estimated these dynamic productivity gains to be worth around an additional US\$700 million in welfare (real consumption) terms to the New Zealand economy over the 20 year period following entry into force of the FTA.

6.1.5 Conclusions regarding overall gains to the New Zealand Economy

Economic modelling work undertaken during the course of the Joint Study, which used the underlying framework cited in 6.1.2, suggests that:

- Bilateral trade between New Zealand and China will grow significantly;
- Production and welfare gains will flow to both the New Zealand and Chinese economies; and
- There will be positive impacts for the goods and services sectors in both New Zealand and China.

The key findings of the study were:

- Over a 20-year period from 2007 to 2027, New Zealand exports to China are expected to be between US\$180–280 million higher per year than otherwise. Chinese exports to New Zealand are expected to increase by an annual average of between US\$40–70 million per year over the same period.
- In percentage terms, this equates to New Zealand's exports to China increasing by between 20 and 39 percent above the baseline. China's exports to New Zealand are expected to be between 5 and 11 percent higher than the baseline over the 20-year period.
- Over this timeframe the FTA is expected to deliver US\$2.3 billion of welfare (real consumption) gains to New Zealand (a maximum of 0.55 percent above baseline).

As noted in Sections 6.1.3 and 6.1.4 the modelled outcomes on merchandise trade were responsible for generating the bulk of the expected gains from an FTA. In the merchandise trade area the outcome of negotiations substantially accords with the assumption of elimination of barriers to trade used in the study, albeit delivered over time rather than immediately as assumed in the model.

This suggests it can reasonably be assumed that the economic value of the FTA would fall within the range of outcomes identified in the Joint Study.

The phased opening of markets under the FTA outcome and the fact that the benefits of enhanced regulatory cooperation will also accrue over time would suggest the value may be nearer the low end of the range (ie US\$180 million in increased annual exports and US\$1.6 billion in welfare (real consumption) gains over 20 years).

Alternatively, the fact that economic modelling does not capture the potential 'demonstration effect' conclusion of an FTA may have in stimulating the interest of both business communities in the bilateral trade and economic relationship suggests that the actual positive economic impact of the FTA could be higher than the findings of the Joint Study.

6.2 Social effects

The FTA and associated instruments are expected to have overall benefit to New Zealand socially. They are not expected to have any discernable negative social effects in New Zealand. This section examines potential effects on domestic employment, domestic social regulation and immigration.

6.2.1 Employment

Bilateral free trade agreements may have both positive and negative employment effects. Given that such agreements facilitate greater two-way trade by removing or reducing trade barriers and distortions, the major negative effects can be expected to be found in industries previously protected by tariffs or other barriers to trade, which may find it difficult to compete with cheaper imports under an FTA. Positive employment effects, however, can be expected in industries likely to gain from increased export opportunities under the agreement and in areas of the economy where activity increases, either domestically or in exporting to third countries, as a result of cheaper imports available under the Agreement.

As noted in section 6.1.5 it is expected that the FTA will result in an increase in New Zealand's net exports to China and an increase in overall economic activity in New Zealand. That suggests that in aggregate the effect of the FTA on employment in New Zealand will be positive.

In import sensitive industries the FTA provides for phased reduction of tariffs to facilitate adjustment over time. Moreover products from China already have significant market presence and import share in a number of New Zealand's import sensitive industry sectors. That suggests the removal of tariffs on Chinese products under the FTA is unlikely to result in significant increases in imports in those areas.

The FTA also includes commitments for temporary entry by skilled Chinese workers to New Zealand's employment market. As noted in section 6.1.3.4, the conditions attached to those commitments – including the limitation of numbers, skill level requirements and the requirement as employees to observe New Zealand labour market conditions – are designed to avoid negative impacts on New Zealand employment.

The non-binding Working Holiday Scheme will also have positive social impact allowing young, skilled Chinese to engage in tourism and incidental employment in New Zealand. The benefits of this scheme should accord with those of similar schemes New Zealand participates in.

6.2.2 Social regulation and labour standards

New Zealand's social, legislative and regulatory frameworks will not be affected by the FTA. The government's right to regulate for national policy objectives, including labour protection, is explicitly recognised in the Preamble to the FTA. In the area of services the FTA follows the structure of the WTO General Agreement on Trade in Services (GATS) and therefore excludes services supplied in the exercise of government authority. Moreover, the FTA makes clear that both parties recognise the role of governments in providing and funding public services and New Zealand has not made any commitments in respect of publicly provided services such as public health, education, housing, and social welfare.

In terms of labour standards, the MOU reaffirms the commitment of both parties to maintaining sound labour policies and practices. In line with the government's *Framework for Integrating Labour Standards and Trade Agreements* the MOU establishes mechanisms through which specific labour issues can be addressed via both cooperative and consultative processes with China. The provisions of the MOU are outlined in section 4.20.

As noted in section 6.1.3.4 New Zealand's commitments on movement of natural persons under the FTA include a number of safeguards designed to avoid negative impacts on the New Zealand labour market. New Zealand labour standards apply to all people receiving remuneration in New Zealand, including entrants under New Zealand's temporary employment entry commitments in the FTA.

6.2.3 Immigration

Outside the specific commitments entered into in respect of short-term entry, the FTA will not cause any changes in New Zealand's immigration policy. The promotion of trade and investment opportunities under the FTA and subsequent rise in New Zealand's profile in China may, however, encourage Chinese interest in immigration to New Zealand (including by skilled migrants) and vice versa.

6.3 Cultural effects

The FTA contains safeguards to ensure that there are no adverse effects on New Zealand cultural values including Māori interests.

The FTA incorporates the full range of exceptions in respect of trade in goods and trade in services provided under the WTO through Article XX of GATT 1994 and Article XIV of GATS. These exceptions cover measures necessary for the protection of public morals and those imposed for the protection of national treasures of artistic, historic or archaeological value.

In addition, subject to the same provisos as in the WTO that such measures are not used for trade protectionist purposes, the FTA also provides general cultural exceptions covering:

- protection of national works and items or specific sites of historical or archaeological value;
- support for creative arts of national value (including performing arts, visual arts and craft, literature, film and video, language arts, and indigenous traditional practice and contemporary cultural expression).

It is also made clear that the FTA will not prevent the parties from taking any necessary measures to restrict the illicit import of cultural property from the other party under the framework of the United Nations Educational, Scientific and Cultural Organisation (UNESCO) 1970 Convention on the Means of Preventing the Illicit Import, Export and Transfer of Ownership of Cultural Property.

Provided such measures are not used for trade protectionist purposes, the FTA also gives successive New Zealand governments the right to adopt measures they deem necessary in relation to Māori, including fulfilment of Treaty of Waitangi obligations. Furthermore, interpretation of the Treaty of Waitangi is not subject to the FTA dispute settlement provisions.

The FTA also recognises the right of each party to establish measures to protect genetic resources, traditional knowledge and folklore consistent with international obligations.

6.4 Environmental effects

New Zealand approached the FTA negotiations in the context of the Government's policy of ensuring that sustainable development and environmental objectives are appropriately supported by trade agreements as set out in the 2001 *Framework for Integrating Environment Standards and Trade Agreements*. New Zealand's approach was also in line with the Growth and Innovation Framework (GIF) which seeks a higher level of economic growth in the context of a 'sustainable path and one that adequately protects natural capital.'

The FTA and the ECA can contribute to positive outcomes for New Zealand on environment and sustainable development. Both the FTA and the ECA support the aim of harmonising objectives for trade and environment and provide opportunities to enhance capacity in both China and New Zealand for improved environmental management and to promote trade in goods and services that benefit the environment.

The ECA sets out a list of specific, although not exclusive, areas for cooperation identified as being of mutual interest and benefit to the parties. These include management of water environment; coastal ecological conservation and pollution control; air pollution control and monitoring; improvement of environmental awareness, including environmental education and public participation; management and disposal of waste including hazardous waste; environmental management of chemicals; environment and trade; biodiversity conservation; and other areas as may be mutually agreed upon. These cooperation activities may lead to the development of environmental practices and systems that could have a positive impact on environmental management.

FTAs have the potential to affect the environment in positive and negative ways. There are four means by which the environment can be affected: through changes in environmental regulation; changes in the types of goods and services that are traded; changes in the distribution and intensity of production and consumption; and changes in the scale of production. These are discussed below.

6.4.1 Regulatory Effects

Trade agreements may, in principle, have positive and negative regulatory effects. These potential effects relate to the impact of changes in trade policies on the parties' existing environmental policies and standards.

In general terms, the international experience on the effect of trade agreements is that positive regulatory effects can be assured if care is taken not to undermine the ability of the government to pursue appropriate and effective environmental policies. As previously noted, the FTA will not affect the government's ability to regulate for environmental protection.

The general exceptions to the FTA incorporate the relevant WTO (GATT and GATS) exceptions relating to measures necessary to protect human, animal or plant life or health, or measures relating to the conservation of exhaustible natural resources and make clear those exceptions – as incorporated in the FTA – include environmental measures. These exceptions apply across the whole FTA, including trade in goods and in services, subject to the requirement that they are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination or a disguised restriction on trade in goods or services or investment. As noted in section 4.11 Annex 13 (Expropriation) also makes it clear that, in the normal course of events, environmental regulation does not constitute an indirect expropriation and hence is not subject to investor challenge under the Agreement.

New Zealand's environmental laws, policies, regulations and practices constitute an environmental management system that is designed to deal with any adverse effects of economic activity (including activity resulting from trade agreements) in a manner consistent with the aims for sustainable development.

Relevant legislation includes the Resource Management Act 1991, the Hazardous Substances and New Organisms Act 1996, the Ozone Layer Protection Act 1996, the Soil Conservation and Rivers Control Act 1941, the Energy Efficiency and Conservation Act 2000, the Climate Change Response Act 2002, the Aquaculture Reform (Repeals and transitional Provisions) Act 2004, the Biosecurity Act 1993, the Conservation Act 1987, the Crown Minerals Act 1991, the Fisheries Act 1949 (amended 1993), the Forests Act 1949 (amended 1993), and the Wildlife Act 1953.

The FTA will not compromise New Zealand's ability to apply these laws, policies and regulations, nor will it constrain New Zealand's ability to set new laws, policies and regulations.

In addition, the government has instigated a range of voluntary initiatives to assist in addressing potential adverse environmental effects. These include the New Zealand Packaging Accord and the Clean Streams Accord. The government also promotes adherence to the OECD Guidelines on Multinational Enterprises which encourage multinational firms to establish and maintain environmental management systems and take into account the environmental effects of their activities.

The ECA promotes high levels of mutual supportiveness between parties' environment and other policies. The ECA explicitly acknowledges the sovereign rights of each country to set their own policies and national priorities and to set, administer and enforce its own environmental laws and regulations. It also provides for cooperation and information exchange, which can potentially encourage 'best practice' on environmental regulations being shared between the parties.

No adverse impacts on New Zealand's biosecurity regulations are anticipated as existing policy and practice will be maintained.

6.4.2 Product Effects

Product effects concern changes in the composition of New Zealand's trade arising from the removal of trade restrictions. Positive product effects arising from the liberalisation of trade in goods and services that benefit the environment can in principle help offset any negative scale and structural effects of freer trade. Increased trade can also benefit the environment by enhancing access to less ecologically damaging inputs (for example, cleaner technologies) to New Zealand production systems. An increase in the movement of goods, however, can also bring with it a possible increase in biosecurity risk, and may require increased attention to and monitoring of movements of environmentally hazardous or environmentally sensitive goods and endangered species.

The FTA may open up new opportunities for New Zealand production and export of goods that benefit the environment. This is a rapidly growing area of trade for New Zealand and was worth \$1.5 billion in 2006²⁵, with the growth in New Zealand's global exports of these products expanding by five percent a year over the past four years. Under the FTA, tariffs on more than 99 percent of New Zealand's environmental goods exports to China will be eliminated by 2013.

The FTA is unlikely to pose significant risks in relation to movements of environmentally hazardous or environmentally sensitive goods and endangered species. New Zealand's environmental laws, regulations, policies and practices are considered to be sufficiently robust to deal with any particular issues related to product effects that might arise.

6.4.3 Structural Effects

The structural effects of the FTA are not expected to be significant for New Zealand. These effects can be both positive and negative. Positive effects arise when an FTA results in the removal of policies that contribute to environmental damage, for example, the removal of subsidies to agriculture that contribute to over-production and result in land degradation. Negative effects can arise in situations where an increase in production of goods for trade leads to environmental damage and policy interventions are inadequate to deal with this.

Economic and environmental policy reforms over the past 25 years in New Zealand leave few distortions in the economy, so positive structural effects from the removal of policies are expected to be minimal. Any negative structural effects are expected to be manageable within existing environmental policies, regulations and practices. New Zealand's environmental legislation and policies provide for the establishment of sustainable production and management practices.

²⁵ Figure based on New Zealand exports of items in the "Convergence List" of environmental goods tabled by New Zealand and other WTO members at the WTO in April 2007 (JOB (07)/54).

6.4.4 Scale Effects

Where a trade agreement augments growth in the New Zealand economy, this can have the positive effect of helping leverage additional financial resources, which can be used to address wider environmental concerns (for example, enabling companies to invest in cleaner technologies and governments to raise revenues for financing environment-related infrastructure).

Potential negative effects stem from pollution and other environmental risks associated with the expansion of economic activity and the increase in the movement of goods. These may not be completely offset by the advantages derived from increased growth. Environment-related policy instruments therefore need to be kept under review to help ensure the overall sustainability of economic growth, including that driven by trade agreements.

The Joint Study indicated that the overall economic impact of the FTA on the New Zealand economy could result in up to a 0.25 percent increase in GDP above baseline over the 20 years following entry into force. This is not expected to generate substantive negative scale effects that cannot be addressed by New Zealand's current framework of environment and sustainable development-related legislation, policies and practices.

7 COSTS TO NEW ZEALAND OF COMPLIANCE WITH THE TREATY

7.1 Tariff revenue

In the period 2004–2006 the average annual revenue collected on imports from China was NZ\$193 million. As tariffs are phased out over the transition under the FTA, the New Zealand Customs Service will progressively collect less revenue from duty payments.

The exact amount of duty collected will be influenced by the pattern of actual imports and the proportion that qualify for preference under the agreement Rules of Origin. The majority of current duties collected on imports from China are on textile, clothing and footwear products, which will see gradual tariff reductions over a 7 or 9-year period, depending on the particular product, through to 2014 or 2016.

Based on current trade patterns, around 40 percent of the tariff revenue on imports from China is already being foregone under the domestic tariff reduction programme in place for the period 1 July 2006 to 1 July 2009.

7.2 Costs to government agencies of implementing and complying with the FTA

One-off costs associated with implementing the FTA, incurred in the 2007/08 financial year are estimated to amount to NZ\$960,000, as funded from the inter-agency FTA Growth and Innovation Fund (GIF) pools for promotion and outreach activities and cooperation and capacity building. Key activities include:

- NZTE's development of a suite of materials to assist New Zealand companies build their capability for doing business with China;
- the development of a whole-of-government China FTA website to provide comprehensive information on the content of the FTA and on doing business with China;
- the production of publications in both English and Chinese;
- a two-day roadshow programme to be held in Auckland, Hamilton, Wellington, Christchurch and Dunedin from late May 2008 to outline the content of the FTA to the New Zealand business community (day 1) and capability building for doing business in China (day 2). NZTE will manage this whole of government exercise;
- Non-recoverable costs associated with preparing a new edition of the Working Tariff (other costs will be recovered through sales of the new edition);
- Training Customs Service staff and the trading community for implementation of the new ROO;
- The development of a new certification of origin system.

There will be ongoing costs of meeting New Zealand's obligations under the FTA including staffing, the establishment of new institutions, developing implementing arrangements, technical assistance and implementation costs. It is difficult to estimate those costs at this stage. Key government agencies (Ministry of Foreign Affairs and Trade, Ministry of Agriculture and Forestry, Ministry of Economic Development, Ministry for the Environment, Department of Labour, New Zealand Customs Service, New Zealand Food Safety Authority) will seek funding for these activities, together with the funding of activities associated with other FTAs as part of the Economic Transformation budget initiative.

Government agencies will also be working with the private sector and others to implement strategies for leveraging opportunities from the FTA. Such activities represent an investment in the FTA rather than a compliance cost.

7.3 Costs to businesses of complying with the FTA

As outlined in section 3.1 the predominant effect of the FTA should be to reduce transactions costs for New Zealand business in trading with China through trade facilitating outcomes in areas such as customs procedures, technical barriers to trade (TBT), and sanitary and phytosanitary (SPS) measures. Some of these outcomes, such as trade facilitating provisions for customs procedures, will help reduce transactions costs from the outset of the FTA. Other outcomes are expected to develop over time from the platform the FTA provides in areas such as TBT and SPS for enhanced regulatory cooperation to facilitate trade. Two areas of identified expected impact on business costs are the certification of origin system and the EEEMRA, covered respectively in sections 3.1.2 and 3.1.7.

Certificates of Origin

The FTA introduces a requirement for export certification of origin which New Zealand will administer through approved Bodies authorised to issue certificates. The Bodies authorised to issue the certificates of origin will be able to recover the approximate cost of the certification services which they provide to exporters but the system will be designed to minimise those costs while providing necessary robustness as to authenticity. The existence of the certificate will provide unique access for products of New Zealand origin to the tariff and trade facilitation benefits under the FTA. It is expected that the additional costs for businesses will be minor in comparison to the benefits of the associated preferences and the certainty certificates of origin will deliver.

EEEMRA conformity assessment procedures

The EEEMRA will provide New Zealand exporters with an alternative way to demonstrate compliance with regulatory requirements and apply compliance marks (the Chinese CCC marks) to electrical and electronic products before the products are exported to China. The EEEMRA is intended to reduce compliance costs for New Zealand businesses.

8 COMPLETED OR PROPOSED CONSULTATION WITH THE COMMUNITY AND PARTIES INTERESTED IN THE TREATY ACTIONS

8.1 Inter-departmental consultation process

Negotiation of the FTA and associated instruments was conducted by an inter-agency team led by the Ministry of Foreign Affairs and Trade and comprising officials from the Ministry of Agriculture and Forestry, the Ministry of Culture and Heritage, the Department of Labour, the Ministry of Economic Development, the Ministry of Education, the Ministry for the Environment, the Ministry of Transport, Treasury, New Zealand Customs Service, New Zealand Food Safety Authority, Te Puni Kokiri, New Zealand Qualifications Authority, Tourism New Zealand and New Zealand Trade and Enterprise (NZTE).

Relevant departments and agencies were also consulted during the negotiations in the preparation of New Zealand's position, in particular in preparation of New Zealand's tariff schedule and services schedule.

The Department of Labour and Ministry for the Environment were directly involved in the negotiation of the MOU and ECA respectively.

The Department of the Prime Minister and Cabinet was also generally consulted on the FTA process.

8.2 Public consultation process

From early 2004, the Ministry of Foreign Affairs and Trade, together with other government agencies, organised and conducted a wide-ranging consultation programme to raise public awareness of the negotiations and to seek stakeholder views.

This programme used printed, emailed and website information, supported by extensive specific discussions with key stakeholders, such as exporters and industry sectors likely to be interested in or affected by the outcomes of the FTA (including the MOU and ECA).

Communications programme

The communication programme supporting the consultations included:

- A call for submissions to contribute to the Joint Study in July 2004
- The release of a feasibility study entitled "A Joint Study Report on a Free Trade Agreement between China and New Zealand in November 2004
- Regular bulletins posted on the MFAT website, which provided information about the negotiations and requested views from stakeholders and the general public
- Updates in the bimonthly MFAT news bulletin, Business Link, which is also posted on the MFAT website
- Ongoing presentations on the negotiations as part of wider trade policy consultations with interested parties including NGOs
- Regular updates on the negotiating process, emailed to stakeholders who had registered interest in the negotiations

Consultation programme

Public outreach and consultation has taken place throughout the negotiation of the FTA, including with key stakeholders on negotiating objectives. In particular, stakeholders have been consulted on the phase-out of tariffs, rules of origin, services and investment commitments including the shape of potential outcomes on movement of natural persons, and associated labour and environment outcomes. The communications programme provided the basis for a consultation programme involving:

- Meetings and email correspondence with companies and sectoral organisations with an interest in access to the China goods and services markets
- Meetings and email correspondence with companies and sectoral organisations with an interest in New Zealand's tariff phase-out arrangements under the FTA
- Meetings with organisations with a broad interest in the negotiations, including Business New Zealand, Chambers of Commerce, the Council of Trade Unions, The Export Institute, the Federation of Māori Authorities, the Employers and Manufacturers Association (Northern), the Canterbury Manufacturers Association, the Asia Foundation, New Zealand China Trade Association
- Meetings with a range of Chinese business groups in New Zealand and New Zealand business groups in China
- The *International Treaties List*, produced every 6 months by the Ministry of Foreign Affairs and Trade, provided an update on the negotiation process, identifying in particular issues of interest to Māori. This was distributed to iwi, and provided contact details for feedback from iwi.

Submissions process

The consultation process, particularly in connection with the joint feasibility study, elicited close to 90 submissions as well as information and responses from a range of individuals and organisations, including:

- Business or sector organisations including: Asia Foundation, Association of Rotational Moulders of Australasia, Business New Zealand, Canterbury Development Council, Chambers of Commerce, Cold Storage Association of New Zealand, New Zealand Council of Wool Exporters, Crop and Food Research, Council of Trade Unions, Deer Industry New Zealand, Engineering Printing and Manufacturing Union, Employers and Manufacturers Association (Northern), Fashion Industry New Zealand, Federated Farmers, New Zealand Footwear Industry Association, New Zealand Forest Industries Council, Marine Industry Association, Meat Industry Association, Meat & Wool New Zealand, New Zealand Mussel Industry Council, National Council of New Zealand Wool Interests, National Distribution Union: Clothing Union and Textile Division New Zealand-China Traders Association, Retailers Association of New Zealand, Plastics New Zealand, New Zealand Retailers Association, Screen Council, New Zealand Sports Turf Institute, Textiles New Zealand, Trade Liberalisation Network of New Zealand, Wellington Chamber of Commerce, Wool Services International, Council for International Development

- Local government
- Consultation with Māori groups with trade and economic interests, including Federation of Māori Authorities, Te Awe and Māori exporters including Ngai Tahu Seafoods
- Companies, including: Advance Marketing, Academic Colleges Group, Alliance Group, ANZ National Bank, Anzco Foods, ASB, Air New Zealand, Astrograss, Autex, Beijing Evolution Fitness Centre, Beijing English International Alliance, Bendon, Bridgestone New Zealand, Cawthorn Institute, China Link, Comfort Socks, Commonwealth Bank, Deane Apparel, Directus International, DHCL, DN Palmer New Zealand, Equipment Engineering, Earth, Sea and Sky, Elastomer Products, Feltex, Fisher & Paykel, Fonterra, FFOVCS Williams, H Dawson Sons & Co (Wool) New Zealand, Hayes International, Heinz Wattie, HKS Travel, HRI Consultants, INEX, Interweave, James Capital Partners, Jayel Trading Ltd, Jeffco International, Kathmandu, Kerry New Zealand, Ketchum Newscan, Kumfs Shoes, Lanewalker Rudkin, Lockwood, Macpac, Mahon China, McCulloch Medical, MWH, Nalco, Nelson Pine Industries, Natural History New Zealand, Netmaster, New Zealand Milk (Hong Kong), Niagara Sawmilling, Nuphlo Pumps, Pacific Steel, Prime Consultants, Pumpkin Patch, Rayonier MDF, Rembrandt Suits, Sanfords, Scott Technology, Sealand, Tasman Insulation New Zealand, Silverdale Knitware, South East Resources, Spray Dried Products, Tait Electronics, Talbot Plastics, Taupo Language and Outdoor Education Centre, Temperzone, The Learning Web, TL Jones, Tenon, Tohu Wines, Tradeskins, Tse Group, Ullrich Aluminium, Villa Maria, Viscount Plastics, Waihi Tool and Die, Westland Milk Products, Winstone YAKKA, Wakatu, Waimea Sawmills, Wool Board Disestablishment Company, Westpac, Zespri
- Educational Institutions including: Lincoln University, Otago University, Victoria University, Centre For Innovation, Research and Enterprise, Auckland Institute of Studies, Wellington Institute of Technology.

Issues covered in the consultation process

The key messages from the submissions were:

- There was strong overall support for an FTA with China.
- Those in support of the FTA saw the removal of tariffs as a significant benefit to many businesses and consumers.
- Many organisations stressed the need for a comprehensive FTA which addressed non-tariff measures such as standards, labelling requirements, quarantine requirements and mandatory testing. Organisations gave the message that these measures caused many of the problems encountered in doing business in China.
- Submissions relating to services highlighted the existing restrictions on services that can be provided in China by wholly owned foreign enterprises, making it difficult for some services, for example education, to be provided. Negotiators raised these issues during the negotiations and China has made commitments beyond its WTO GATS commitments as set out in section 3.1.8 but these do not address all the interests of New Zealand services exporters.

- Some submissions identified intellectual property protection as an issue for goods and services. As set out in section 3.1.11, the FTA requires China to establish and maintain an intellectual property rights system that provides certainty over the protection and enforcement of intellectual property rights and incorporates the relevant provisions of the WTO TRIPS Agreement into a bilateral context.
- Some submissions said that investment is hindered by restrictions on the movement of foreign exchange and onerous capital requirements for foreign businesses including banks. As set out in section 3.1.10, the investment provisions of the FTA include provisions on national treatment and MFN non-discrimination and provisions to allow the transfer of investment funds.
- Some unions and organisations in the manufacturing and textile, carpet clothing and footwear sectors expressed concern about the removal of New Zealand tariff protection beyond current levels. In order to help mitigate the potential for any negative adjustment effects, the FTA includes longer phase out periods for clothing, footwear, carpet and some textile products.
- The whiteware, aluminium, steel, plastics, food processing and clothing industries wanted to ensure that tariff removal is accompanied by an overall levelling of the playing field between Chinese and New Zealand industrial policies. Negotiators have achieved a slower phase-out for whiteware and some steel products and have retained a strong trade remedies regime and some additional measures to protect against dumped and subsidised goods.
- Concerns were also raised about China's non-adherence to internationally accepted labour and environment standards and the need to pursue the Government's objectives on integrating labour and environment standards in the FTA. Some other respondents argued that these issues have no place in an FTA. Negotiators were able to take this into account by establishing treaty-level agreements on labour and the environment (the ECA and MOU), a first for a country negotiating a trade agreement with China. The result is an approach that takes into account both views.

9 SUBSEQUENT PROTOCOLS AND/OR AMENDMENTS TO THE TREATIES AND THEIR LIKELY EFFECTS

The FTA includes general provision for review and amendment subject to the agreement of the parties and completion of necessary domestic legal procedures (Article 212).

Specific provisions envisage the possibility of amendments arising in areas such as acceleration of tariff elimination (Article 8), commitments on services (Article 124) and the conclusion of annexes and/or implementing arrangements in respect of SPS measures (Article 77) and TBT (Article 102).

The MOU and ECA make no formal provision for amendments.

New Zealand would consider any amendments to the FTA and associated instruments on a case by case basis, and any decision to accept an amendment would be subject to the usual domestic approvals and procedures.

10 WITHDRAWAL OR DENUNCIATION

Either party, on giving written notice to the other party, may withdraw from the FTA. The FTA terminates 180 days after the date of the notice of termination (Article 213).

The ECA can be terminated by 6 months notice to the other party (ECA Article 6(1)). Termination would not affect the validity of any arrangements made under the ECA (Article 5(2)).

The MOU can be terminated by 6 months notice to the other party (MOU Article 5(1)). Termination would not affect the validity of any arrangements made under the MOU (Article 5(6)).

It is important to note that the FTA requires the parties to enhance their communication and cooperation on labour and environment through both the MOU and the ECA (Article 177 of the FTA). Therefore, while the FTA is in force the parties are expected to cooperate under the ECA and MOU. Any decision by New Zealand to terminate the FTA, MOU or ECA would be subject to the usual domestic approvals and procedures.

11 ADEQUACY STATEMENT

The extended NIA incorporates Regulatory Impact Statement elements. The exigencies of the negotiation and conclusion timetable have meant that it has not been possible for the Regulatory Impact Analysis Unit to form a view on the adequacy of these elements. MFAT and the relevant policy agencies (Ministry of Economic Development in respect of the EEEMRA and in respect of tariffs and rules of origin; the New Zealand Customs Service in respect of Certificate of Origin system) confirm that the requirements of the Regulatory Impact Analysis were followed and the principles of the Code of Good Regulatory Practice have been complied with.