DLA PIPER

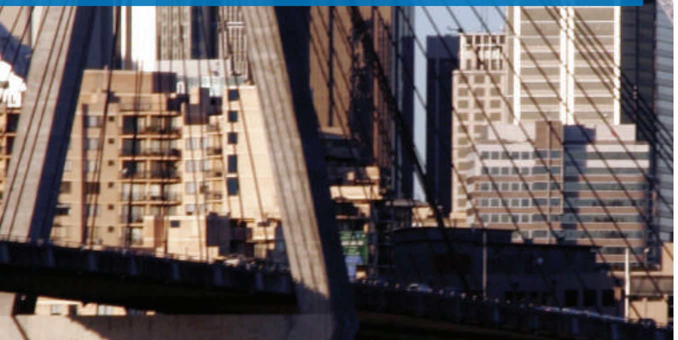
The Trans-Pacific Partnership Series

NAVIGATING A NEW ERA OF TRADE IN THE PACIFIC-RIM

Part II – The TPP and the Infrastructure & Construction Sector

July 2016

THE TPP AND THE INFRASTRUCTURE & CONSTRUCTION SECTOR



The Trans-Pacific Partnership (**TPP**) was signed on 4 February 2016. It is the largest global trade agreement in the last 20 years and is the culmination of five years of negotiations between 12 participating countries. The TPP is a regional free trade agreement between the United States, Canada, Australia, New Zealand, Japan, Singapore, Malaysia, Vietnam, Mexico, Chile, Peru and Brunei (**TPP Parties**).

In **Part I** of our TPP Series we considered the Trans-Pacific Partnership (**TPP**) Investment Chapter, looking closely at the investor-state dispute settlement (**ISDS**) regime. In this **second part of our two-part series,** we consider the impact of the **TPP** on the infrastructure and construction sector.

The TPP presents enormous opportunity for members of the infrastructure and construction sector to grow and diversify, both domestically and globally. By improving access to foreign markets and liberalising trade, the TPP provides building, construction and engineering companies, particularly those in the resources and energy industries, with access to new markets and the potential to achieve greater benefits from existing markets.

As Australia's economy shifts from a reliance on commodity-driven growth to focussing on professional services, its ability to better infiltrate global markets and mobilise its workforce will likely become key to its stability. The TPP facilitates this stability through a number of initiatives: increased transparency and certainty in government procurement; liberalisation of trade through tariff reductions and harmonisation of regulations; mobilisation of professional skills and services across TPP Parties; and the provision of investment protections.

While there are benefits for the infrastructure and construction sector, the TPP will also present challenges for domestic companies. The liberalisation of trade will attract greater competition as a result of increased imports and foreign bids for government infrastructure projects.

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GETTING THE DEAL DONE

HOW DOES THE TPP AFFECT PROJECTS FROM START TO FINISH?

Government Procurement

The TPP will be the largest agreement in Asia to incorporate government procurement commitments, and is set to attract even more regional participants with Indonesia and Korea contemplating signing-up. This means Australian companies will have greater access to Asian markets than ever before. The TPP improves access through requirements for transparency, predictability and fairness in government procurement.

Trade Liberalisation and Harmonisation

The TPP reduces pecuniary, regulatory and policy based barriers that affect trade in goods and services. This elimination of trade barriers for the purposes of supplying goods and services in construction projects, coupled with harmonised trading rules, standards and procedures, will provide improved transparency and accessibility in cross-border trade.

Entry for Business Persons

The TPP includes an agreement to make it easier for business persons to temporarily visit TPP Party countries, not only to assess and pursue potential trade and investment opportunities, but also to improve the mobility of skills and personnel between jurisdictions and projects.

Protection from Discrimination and State Action

The TPP seeks to strengthen protection and security of investments such as construction contracts, safeguard investors' rights and provide fair and equitable treatment through its investment provisions. The investment provisions incorporate an investor-state dispute settlement mechanism, which enables investors from TPP Parties to make a claim against a TPP Party.

GOVERNMENT PROCUREMENT

The TPP's Government Procurement provisions in Chapter 15 set certain minimum standards for government procurement to ensure that TPP Parties do not discriminate against foreign suppliers when assessing tenders and awarding contracts. This is largely achieved through increased transparency and certainty. The TPP does however allow governments to retain some flexibility by expressly providing that TPP Parties are permitted to develop new procurement policies, procedures or contractual means, provided that they are not inconsistent with the Government Procurement provisions.

WHAT IS THE EFFECT ON AUSTRALIAN BIDDERS IN TPP COUNTRIES?

Australian companies may face informal barriers in bidding for foreign government work or supply agreements, due to a lack of transparency and fairness. These barriers can increase transaction costs and, in doing so, reduce competition and discourage foreign investment.

In Asia, it is common for free trade agreements to be silent on government procurement. The Asian Development Bank's Asian Economic Integration Monitor concluded that the Association of Southeast Asian Nations' trade agreements do not effectively address government procurement or other non-tariff barriers.

The TPP seeks to provide certainty for companies involved in government procurement tenders by requiring TPP Parties to:

- Treat foreign parties or domestic parties with foreign affiliation the same as domestic parties;
- Provide opportunities for electronic procurement, publish notices of intended procurement and planned procurement, and make procurement information available by promptly publishing it and by providing all necessary information on request;
- Limit conditions for participation to legal and financial capabilities and commercial and technical abilities;
- Prepare technical specifications or conformity assessment procedures without creating unnecessary obstacles for bidders;
- Provide sufficient time for bidders to obtain tender documentation and prepare a response;
- Guarantee fairness, impartiality and confidentiality in the treatment of tenders;
- Award contracts in accordance with the stated evaluation criteria to the supplier with "the most advantageous tender" or "if the price is the sole criterion, the lowest price";
- Upon request, provide an explanation as to why an unsuccessful bidder was not selected;
- Ensure that criminal or administrative measures exist to address corruption in government procurement; and
- Maintain, establish or designate at least one impartial administrative or judicial authority to review challenges or complaints by bidders.

Green light: Governments that sign up to the TPP Government Procurement rules are sending a welcome green light to Australian bidders that they are open for international business.

HOW DOES THE TPP APPLY TO PROCUREMENT IN AUSTRALIA?

The Government Procurement Chapter will only apply to procurement which meets or exceeds the below thresholds:

	TPP (central entities)	TPP (sub-central entities)	TPP (other entities)
Goods and services	130,000 SDR AUD 253,755*	355,000 SDR AUD 692,946	400,000 SDR AUD 780,729
Construction services	5 million SDR AUD 9,759,072	5 million SDR AUD 9,759,072	5 million SDR AUD 9,759,072

*Conversions from International Monetary Fund Special Drawing Rights as at May 2016

The Government Procurement provisions generally apply to:

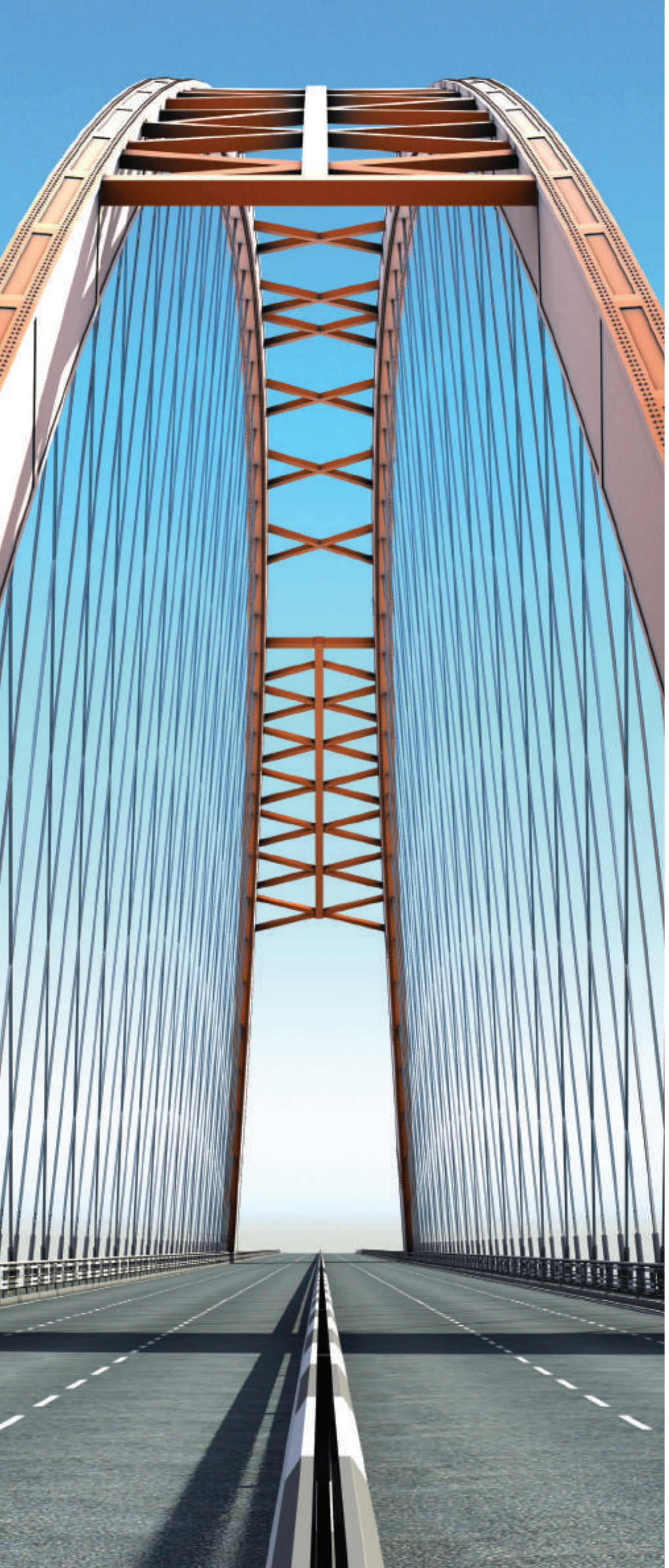
- Goods and services;
- Contracts such as purchase, rental, lease, build-own-operate and public works concession agreements; and
- Open, "selective" and "limited" tendering.

In Australia, the following procurement entities are subject to the Government Procurement provisions:

- **67** "central government entities", being a broad range of Commonwealth entities including the Department of Education and Training, Department of Infrastructure and Regional Development, and, with some exceptions, the Department of Defence;
- **242** "sub-central government entities", being various State and Territory bodies. In the case of New South Wales, this includes the Department of Education and the Department of Planning and Environment. Australia is currently extending coverage to sub-central government entities only in relation to bidders from Canada, Chile, Japan, Mexico and Peru; and
- **25** "other entities" such as the Export Finance and Insurance Corporation and Australian Institute of Health and Welfare.

The Government Procurement Chapter does not apply to certain procurements including:

- The acquisition or rental of land, existing building or other immovable property;
- Non-contractual agreements for grants, loans, equity infusions, guarantees, subsidies, fiscal incentives and sponsorship arrangements;
- Public employment contracts; and
- Procurement for the specific purpose of providing international assistance, including development aid.



IMPACT ON COMPANIES ENGAGING IN PROCUREMENT IN AUSTRALIA

Australian companies should be aware of the key differences between existing procurement obligations and the TPP.

At a Federal level, the following table outlines key differences between the TPP and the Commonwealth Procurement Rules (**CPRs**):

Requirement	TPP	CPR
Procurement entity should consider whether offer delivers the core measure of best "value for money"	×	✓
Procurement entity should promote the proper use and management of public resources, which requires that the procurement is "efficient, effective, economical and ethical"	×	✓
Procurement entity must establish processes for the identification, analysis, allocation and treatment of risk when conducting procurement. Risk should be borne by the party best placed to manage it	×	✓
Procurement entity should consider costs of participating in procurement when designing a process commensurate with the scale, scope and risk of the proposed procurement	×	✓
Procurement entity must use electronic procurement for open tenders	×	✓
Procurement entity must handle complaints internally	×	✓
Complaints should be handled by an impartial administrative or judicial authority that is independent of the procurement entity	✓	×

✓ Denotes express requirement
× Denotes silence on requirement

The major impact of the TPP on Australian central procurement entities will be the requirement that complaints regarding the procurement process are handled by an impartial administrative or judicial authority which is independent of the procurement entity. In comparison, the CPRs provide that these complaints are handled internally.

In most other areas, it is Australia that has a high benchmark for procurement, with the CPRs raising the bar in terms of value for money, efficient management of public resources, risk management and costs of procurement.

TRADE LIBERALISATION

The infrastructure and construction sector is now subject to the "faster, safer, better, cheaper" mentality that has gripped manufacturing and services sectors. Clients and governments award contracts on the basis of cost, speed, reliability and innovation; demands which are often conflicting.

Companies must innovate and regularly review their internal processes, structures and ambitions in order to strike the right balance between these factors and remain competitive.

To facilitate this the TPP reduces pecuniary, regulatory and policy based barriers that currently affect trade in goods and services. The TPP also mobilises skills and personnel through its Entry For Business Persons Chapter, allowing business persons to provide professional services more readily across jurisdictions.

MARKET ACCESS FOR GOODS

The Trade Liberalisation provisions in the TPP will impact the supply of materials in construction projects.

The first impact will be due to tariff reductions. Exporters of construction materials, such as iron ore, copper and nickel, can expect increased exposure to new markets as a result of lower tariffs. Lower tariffs will also benefit developers of domestic construction projects because project companies will have easier and cheaper access to foreign-supplied construction materials.

The second impact will be due to the market access provisions. The TPP contains mechanisms designed to protect market access and competitiveness of goods and exports. Each TPP Party is required to accord the goods of other TPP Parties the same treatment as any like, directly competitive, or substitutable domestic goods. TPP Parties are also restricted from adopting or maintaining any fees, charges or formalities that represent an indirect protection of domestic goods.

This means that for a construction project, materials will theoretically be given equal treatment regardless of origin.

ENTRY FOR BUSINESS PERSONS

International construction and engineering firms are set to benefit greatly from the TPP's entry for business persons provisions. The TPP allows for skilled business persons to temporarily visit TPP Party countries, to oversee the management of their business, take advantage of international placements with their company, attend meetings or trade fairs, provide services negotiated under a contract, or set up a business or investment.

The TPP promotes harmonisation of rules across TPP Parties, and also includes mechanisms for inquiry and review, more transparent entry requirements, reasonable fees, and timely and efficient processing of applications.

These advantages align with commitments from TPP Parties to improve market access to construction, architecture and engineering services, as identified in our section on Cross-Border Trade in Services on page 8. For example, contractual service suppliers can more easily obtain guaranteed lengths of stay in various TPP Party countries including Malaysia, Brunei, Japan and Vietnam.

Foreign workers coming into Australia will do so in accordance with the 457 visa programme. Employers will be required to sponsor foreign workers and otherwise comply with Australian employment law standards. Foreign workers will also have to meet qualification requirements.

CROSS-BORDER TRADE IN SERVICES

The TPP reduces key barriers to trade for Australian service exports, including engineering, environmental and other consultative services.

TPP Parties are required to afford foreign services and service suppliers with no less favourable treatment than domestic equivalents, or than those of another TPP Party. For example, Australia will have guaranteed market access for engineers, urban planners and architects in TPP Party countries including Malaysia, which historically has imposed major restrictions in this space.

The TPP will also promote equal treatment of foreign services by prohibiting the following:

- The requirement of a local presence for suppliers. The result is that cross-border service suppliers will not need to maintain an enterprise or a representative office in a TPP Party country to which it is supplying services;
- Particular limitations on services, such as limiting the number of service suppliers in a sector; and
- Restrictions on the type of legal entity of the service supplier.

CASE STUDY: MINING

No other industry is quite as affected by trade as mining. Fuelling the construction industry with materials, and heavily reliant on infrastructure, the mining industry will benefit from a range of different trade initiatives under the TPP.

In-depth – Mining Equipment Technologies and Services (**METS**) and oilfield service providers will see new opportunities for investment and business under the TPP. This is partly attributable to TPP provisions requiring the introduction of laws prohibiting TPP Parties from providing financial support to State-owned enterprises (**SOEs**). The TPP's efforts to address likely anti-competitive behaviour that may arise with respect to SOEs means that Australian METS and oilfield service providers can compete fairly with large SOEs, such as Vinacomin and Petrovietnam. Again, however, METS and oilfield service providers will be in the same markets as other service providers from leading exploration and extraction nations, such as Canada and the US.

CASE STUDY: ENERGY

The resources and energy sector is a big focus of the TPP. The TPP has liberalised markets that are presently highly protective of their energy sectors from incoming investments, such as Vietnam, Brunei Darussalam and Mexico. New opportunities for the export of minerals and energy commodities are likely to come from this, including the elimination of tariffs on the export of petroleum and natural gas to Vietnam.

In-depth – Foreign companies will be allowed to participate in the Mexican energy industry for the very first time. This is expected to attract up to $30 billion of additional foreign investment per year. The exploration, extraction and production opportunities that currently exist in Mexico will be open to Australian and other TPP Party companies. Being at the forefront of this action and benefiting from the same will require commercial and technical preparedness, and the ability to show this in any bid for participation. Opportunities will canvas oil, gas and geothermal resources. Additionally, Australian companies will have the opportunity to bid for government procurement projects with PEMEX, Mexico's State-owned petroleum company.

HARMONISING REGULATIONS

The TPP facilitates a single set of trading rules, standards and procedures, providing for transparency and accessibility in cross-border trade and transactions. The harmonising of inconsistent regulatory regimes among TPP Parties will have a positive impact on all industries by facilitating the connection of domestic industries to global supply chains.

Companies are expected to see a reduction in compliance costs when a TPP Party agrees to recognise another TPP Party's standard as equivalent to its own. This will also provide more predictable market access which will incentivise Australian construction companies to invest in TPP Party countries.

Some of the key measures of harmonisation relevant to infrastructure and construction, particularly in respect of the shipping of materials and equipment, are discussed below:

- **Import and export licensing:** requirement for all TPP Parties to adopt or maintain import licensing procedures that are consistent with the World Trade Organisation Agreement on Import Licensing Procedures.
- **Accessibility of information:** requirement to enhance the accessibility of information for small and medium-sized enterprises by publishing a range of information relating to trade, including information concerning procedures for importation, exportation and transit, any restrictions or prohibitions, penalty provisions for breaches of import, export or transit formalities, appeals processes, and laws, regulations and administrative rulings of general application relating to rules of origin.
- **Customs administration and trade facilitation:** promoting cooperation in respect of customs issues affecting goods traded between TPP Parties. The provisions on trade facilitation enhance conditions for businesses and persons involved in cross-border trade among TPP Parties, including by:
  - **Review:** ensuring the availability of administrative and judicial review of determinations on custom matters in accordance with a TPP Party's domestic law;
  - **Expedited procedures:** providing for expedited customs procedures for express shipments; and
  - **Transparency and simplification:** creating transparent and efficient customs procedures for the release of goods.

The TPP preserves the ability for authorities to enforce domestic laws and regulations relating to customs.

PROTECTION FROM DISCRIMINATION AND STATE ACTION

Projects don't always go to plan, and State action can often lead to financial loss for contracting parties in jurisdictions with a less stable political backdrop.

The TPP's investment provisions protect the "investment" of a party from one TPP nation into the territory of another. This applies to investments in existence as at the date the TPP comes into force, or thereafter.

The definition of "investment" includes construction contracts such as "turnkey, construction, management, production, concession, revenue-sharing and other similar contracts".

The ISDS provisions protect investments such as construction contracts where there is an investment agreement that grants rights with respect to:

- **Infrastructure projects not for predominant use and benefit of the government:** including the construction of roads, bridges, canals, dams or pipelines or other similar projects. This is provided that the infrastructure is not for the exclusive or predominant use and benefit of the government;
- **Public utilities:** power generation or distribution, water treatment or distribution, telecommunications, or other similar services supplied on behalf of the TPP Party for consumption by the general public; and
- **Natural resources:** oil, natural gas, rare earth minerals, timber, gold, iron ore and other similar resources (controlled by a TPP Party), including for their exploration, extraction, refining, transportation, distribution or sale.

A contracting party may make a claim where a government has legislated in a manner that causes a loss, such as by direct means of nationalising or seizing an investment and indirect means (noting the exceptions in the TPP in respect of public health, safety and the environment). Such regulations can indirectly affect entities involved by destroying the economic value of an investment.

For a more in-depth look at the investment protections and the ISDS mechanism under the TPP, see Part I of our TPP series, which can be accessed here.

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