THE RISKS OF DISCIPLINES ON STATE-OWNED ENTERPRISES IN THE PROPOSED TRANS-PACIFIC PARTNERSHIP AGREEMENT[1]

The proposal for 'disciplines' on state-owned enterprises (SOEs) in a Trans-Pacific Partnership free trade and investment agreement appears to be a purely United States initiative that has limited support from other negotiating parties. This paper examines the common elements of the state-owned enterprise model that is being promoted by developed countries through the OECD; the main practices that are targeted through the concept of competitive neutrality; the downsides of the model, drawing on lessons from New Zealand where it was first systematically implemented; and the rationale for the US in advancing the text in the TPPA.

This analysis is necessarily speculative. While the text itself appears to have been drafted and redrafted with intimate involvement of US stakeholders, critics of the proposed agreement are again left to shadow box with a text that remains secret.[2]

The 'Best Practice' SOE Model

The current model for fully commercial and competitively neutral state-owned enterprises (SOE) was developed in New Zealand in 1986[3] and adopted in Australia following the Hillmer Review of National Competition Policy in 1993.[4] It has since been applied across federal, state and local governments. The core concept of 'competitive neutrality', as described by the Australian Productivity Commission, aims 'to promote efficient competition between public and private businesses', specifically 'to ensure that government businesses do not enjoy competitive advantages over their private sector competitors simply by virtue of their public sector ownership.'[5]

In practice, this requires the fundamental restructuring of government agencies that have a combination of policy, regulatory and delivery functions that are *or could be made* commercial, or existing state enterprises that serve commercial or mixed functions. The model requires the separation of commercial, policy and regulatory activities into different agencies. This may result in the creation of one or more new commercial state owned enterprises or the transfer of commercial activities to an existing SOE. Regulatory activities and policy responsibilities are allocated to other agencies and ministries.

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[1] Professor Jane Kelsey, School of Law, University of Auckland, paper prepared for the stakeholder programme at the 11th round of Trans-Pacific Partnership Agreement negotiations in Melbourne, 4 March 2012. For comments or further information please contact me at j.kelsey@auckland.ac.nz

[2] According to Senate Majority Leader Harry Reid six trade associations had input into the text in addition to the US Chamber of Commerce and Coalition of Services industries, 'Reid Urges White House To Seek Strong SOE Limits In TPP Talks', *Inside US Trade,* 26 May 2011

[3] Outlined by the New Zealand Treasury in *Economic Management: Briefing Papers to the Incoming* Government', Treasury, 1984 and implemented through the State-Owned Enterprise Act 1986 that originally created nine state-owned enterprises.

[4] The State of Victoria replicated the New Zealand model during the late 1980s. The Hillmer Review recommended competitive neutrality as one of six competition principles. See F. Hillmer, M. Rayner and G. Taperrell, *National Competition* Policy, 25 August 1993. Matthew Rennie and Fiona Lindsay, *Competitive Neutrality and State-owned Enterprises in Australia: Review of Practices and their Relevance for Other Countries*, OECD Corporate Governance Papers, No. 4, August 2011

[5] http://www.pc.gov.au/agcnco/competitive-neutrality

SOEs are **structured** under law as if they were private corporations:

- ministerial shareholders (usually the portfolio minister and the minister of finance or SOEs), who set the performance indicators and appoint the board of directors;
- a board of directors drawn from the private sector, paid at private sector rates;
- a chief executive appointed by and accountable to the board, usually drawn from the private sector and paid at private sector rates;
- the chief executive is the employer of all other staff, who are treated as private (nor public) sector workers; and
- SOEs report annually, a central monitoring unit oversees financial and non-financial performance and parliamentary committees can seek testimony.

The **statutory framework** sets out:

- the overriding objective to act as a commercial business;
- responsibilities to employees and communities, which are subordinated to the commercial objective;
- provision of non-commercial activities required by shareholding ministers to be separately contracted and funded on a full cost recovery basis;
- the governance structure;
- reporting obligations; and
- terms for raising debt.

Their **commercial operation**s are maintained at arms length from government:

- Ministers and the Board agree an annual statement of intent including the required dividend;
- the Board provides periodic reports and can be required to appear before a parliamentary committee;
- the Board and the CEO determine how to operate the business and deliver the dividend; and
- the CEO's employment package is linked to performance.

The **benefits** of the model are said to be:

- improved efficiency of government commercial operations by facing private sector disciplines;
- efficiency and fiscal benefits from delivering a commercial return on public funds held as SOE assets;
- restructuring and cutting the public sector workforce, and subjecting them to private sector employment conditions;
- preparing SOEs for privatisation (at government expense);

- rationalising government's social obligations through explicit subsidies and rules against cross-subsidisation;
- encouraging private sector competitors by creating a level playing field;
- stronger public sector accountability for use of taxpayer funds;
- more transparent relationships between ministers and SOEs and less opportunity for hidden political interference; and
- a more consumer focused approach by state-entities.

It seems likely this model will be proposed as best practice for all TPPA parties and others that might later accede to the agreement. The authors of an OECD paper on the Australian model in late 2011 made it clear that this kind of corporatisation assumes a much more fundamental transformation:

> success can probably only be copied by other countries if these are willing to undertake similarly profound reforms as were engendered as part of the Australian competition reforms in the 1990s with the active participation of the Productivity Commission.[6]

Practices targeted by 'competitive neutrality'

The SOE text in the TPPA traces back to a joint report from the US Chamber of Commerce and Coalition of Services Industries that seeks to 'level the playing field' to US standards in SOE's home markets, third countries and the US itself. That paper, and various speeches and submissions, notably submissions the US-China Economic and Security Review Commission in February 2012, target a range of commercial practices:

- low cost of capital through subsidised loans, low interest rates and other forms of below market-rate financing, government bonds with implicit guarantees, grants, equity infusions, non-commercial relationships with state-owned banks, preferred access to private bank capital, debt forgiveness;
- favourable tax treatment, including through lower transaction costs;
- protection from bankruptcy and bailout support for stressed enterprises;
- exemption from payment of full dividends and requirements for full reinvestment in the enterprise;
- preferential access to resources, such as land, and other raw materials;
- preferential rates for utilities, such as electricity and water;
- targeted infrastructure development, such as road and rail lines;
- concessional export credits and export credit guarantees (although these are covered by the WTO's Agreement on Subsidies and Countervailing Measures)
- government procurement from SOEs and by SOEs from other state enterprises or

[6] Rennie and Lindsay, 2011, 3

local suppliers;

- links to domestic technology research facilities, and preferential R&D and technology transfer arrangements;
- favourable regulatory treatment and standard setting;
- differential financial reporting and other transparency requirements;
- differential licensing requirements and oversight through separate regulatory bodies or reporting regimes;
- exemptions from competition, consumer and fair trade practice rules, company law, other general laws and regulations;
- lack of redress for competitors to challenge uncompetitive practices; and
- subsidies for operations, including universal service obligations, which are not based on actual cost or enable for cross-subsidisation, are not open to competitive tender, provide beneficial or preferential access to networks and infrastructure, or increase market opportunities.

These could be challenged through an escalating compliance, reporting and enforcement regime that might include:

- Requiring parties to submit comprehensive annual notifications listing: all SOEs in which they have an ownership or control interest; markets in which they operate and their market shares; all forms of government support, including guarantees and the rates, terms of loans from state-owned banks, land concessions and similar information; supply contracts with state-owned suppliers; terms of major procurement and supply contracts they enter into; material transactions with related entities; and material risk factors;
- Failure to comply could result in requests for expedited information;
- Notifications could be reviewed by a standing working group and subject to questions, as per notifications at the WTO;
- Enforcement for non-compliance could follow a SCM-style assessment – a market-based proxy rate would be used to adjust tariffs on exports from a SOE according to its expected subsidy rate, or a 'snap-back' provision to suspend tariff concessions; and
- Adjudication as a final option.[7]

Some Reflections from New Zealand's Experience with SOEs

Commentaries on corporatisation commonly extoll their success in terms of efficiency, transparency of their performance indicators and returning dividends to government. Those are often achieved thorough short-term reductions in costs, staff

[7] Sabina Dewan, 'CAP Presents Recommendations For SOE Disciplines Within TPP
Getting State-Owned Enterprises Right in the Trans-Pacific Partnership', Director of Globalization and International Employment at the Center for American Progress, 23 February 2012

and services whose immediate and longer-term impacts are not included in such assessments. Because corporatisation is often a precursor to privatisation, most evaluations of SOEs also fail to assess the broader success or failure of that continuum. The disciplines of an SOE chapter reach much further than commercial concerns, as the New Zealand experience shows. Yet even less is heard about the impact of corporations on those social, employment and public service infrastructure of the country.

A core objective of competitive neutrality is to strip state enterprises of their integral public good functions and render them discretionary add-ons. The New Zealand and Australian approach, endorsed by the OECD guidelines, eliminates the social functions of government enterprises and prevents them being performed if they are not profitable. If such activities are to continue they must be separately and transparently funded. In practice, that makes it increasingly unlikely they will occur. The New Zealand legislation provides for the government to contract SOEs to provide services that would not be commercially viable. It was used in 1988 for a short-term contract to keep several hundred post offices open for a year; that was quietly terminated early once the political furore over the closures died down. It has remained dormant since. These gaps may become normalized, and hence invisible, but they are still problematic, especially when they most affect those with the least political voice.

A second public role that disappears is the contribution of SOEs to building social capital. In New Zealand, government departments responsible for the railways, electricity, public works, forestry and telecommunications conducted most of trade training of the next generation of skilled workers. That function also disappeared with corporatisation, and was largely responsible for a skills shortage that was not compensated by market-based training mechanisms. As a result of that and declining relative pay, conditions and job opportunities, New Zealand has a serious skills deficit and depends on immigrant labour to fill the skill gap.

The SOE model has another detrimental impact for workers. One of the first steps usually taken by fully commercial SOE boards is to strip the labour force through redundancies. That often occurs at the time the SOE is created, with the costs borne equally by the government and the workers, leaving the SOE with a misleadingly healthy balance sheet. Ongoing cost cutting means further redundancies, contracting out and union-busting operations in the name of increasing productivity and efficiencies. Particular workforces that are affected by these tactics – in New Zealand's case Maori workers in provincial areas – tend never to recover their place as productive workers in the privatised economy. Meanwhile, private sector employment practices ensure that management are rewarded on private sector pay scales, with incentives linked to performance indicators that are often crudely commercial and short term.

Corporatisation in New Zealand directly challenged indigenous rights under the Treaty of Waitangi between indigenous leaders on behalf of their people and the British Crown in 1840. Maori challenged the further alienation of natural resources that had been subject of long and unresolved disputes, which they had been promised would be resolved through a new Tribunal process. At the last minute the government inserted a provision that required those exercising power under the SOE Act to comply with the principles of the Treaty. Subsequent litigation on state-

owned enterprises, forestry, coal, geothermal and other resources means this remains a constitutional, political, moral and social dilemma. Just last month the government conducted a fraught round of consultations on its proposal to privatise a number of assets where indigenous rights remain unresolved.

A further serious risk is the application of the model to social services in which private providers have growing commercial interest and demand competitive neutrality. In the 1990s the New Zealand government applied the SOE model to public hospitals, the state housing operation, and the public research institutes.[8] That saw the appointment of private sector boards of directors who, to avoid vested interest capture, excluded directors with hands-on experience of the sector. Social entities were required to operate on a competitively neutral basis and return dividends to the government, which required either introduction of user charges or cuts to services. Functions that were not fully cost recoverable or funded by explicit contractual arrangements could not be delivered. All three of these experiments were dismal failures. Each has been undone, some more rapidly than others and using different alternatives. Their ongoing problems can be sheeted home to this ideologically driven experiment of the kind being proposed in the TPPA.

A final point (of many that could be raised) is the damage caused to the fabric of the nation itself by requiring state entities that serve democratic and nation building roles, but have a commercial dimension and private sector competitors, to pursue a purely commercial model. During the time that state-owned Television New Zealand operated as an SOE and was required to operate on a competitively neutral basis with the private broadcasters, New Zealand's local content plummeted to the lowest of any OECD country. A Labour government elected in 1999 sought to address that and restore a public role to the state broadcaster. It was unable to introduce compulsory local content quotas because of GATS commitments the previous government entered into.[9]

The government created a diluted form of the SOE model called a Crown Entity with a dual remit to pursue both commercial objectives, including payment of dividends to the Crown, and implement a new public service charter. The hybrid still failed to provide New Zealand with an effective public broadcaster as most other TPPA countries currently enjoy, but it did improve the amount of public service content. The current government has reversed that arrangement and seems intent on creating obligations to private broadcasters that will be difficult to undo, especially if they enjoy investor rights and enhanced lobbying power under the transparency and regulatory coherence provisions of a TPPA.

Why is this SOE text on the TPPA table?

As several US commentators have observed, the SOE issue has never before been addressed in a trade agreement.[10] So why it is on the table in these TPPA

[8] Jane Kelsey, *The New Zealand Experiment. A World Model for Structural Adjustment?* Bridget Williams Books, Wellington, 1997

[9] Jane Kelsey, *Serving Whose Interests? The Political Economy of Trade in Services Agreements*, Routledge, UK, 2008, 232-3.

[10] Source cited in 'US Fixes Future-SOE 'Loophole', Sends TPP Partners Proposed Text', *Inside US Trade,* 20 October 2011

negotiations? Background documents circulating in the US over the past year indicate four motivations:

> (a) as part of the US strategy directed to neutralise the economic and security challenge perceived from China;
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> (b) to stem the ascent of state-capitalist economies and the decline of countries whose economies are organized on the free market model of capitalism by forcing the former to adopt the latter model; in the immediate TPPA context that means Singapore, Malaysia, Vietnam and Brunei, but again it ultimately targets China;
>
> (c) to find an avenue to apply the work of the US and its corporate lobbies such as the USCOC and USCSI to advance these agendas through the Doha round at the WTO and at the OECD, and to extend the precedent established in the US Singapore Free Trade Agreement (FTA); and
>
> (d) to ensure that the design of the chapter advances US offensive interests, whilst shielding its own policy autonomy from the disciplines.

(a) **The US's anti-China strategy**

It became abundantly clear during the APEC meeting in Honolulu last November, with repeated expositions on 'America's Pacific Century', that the US is preoccupied with its decline vis-a-vis China.[11] The inclusion of the SOE chapter is explicitly seen as a means to rein in China's economic expansion domestically, in the US and third countries through its expansive network of state-related entities.

The genesis of the TPPA chapter, according to Senate Majority Leader Harry Reid[12] – a Democrat – was the in-depth paper on SOEs/State Supported Enterprises circulated by the US Chamber of Commerce and Coalition of Services industries.[13] Two of its three main targets – China and India – were not participants in the TPPA negotiations; Vietnam was the third. Other recent statements to that effect include:

> Although China is not a party to those talks, the TPP is viewed by a range of business and labor groups as an opportunity to establish strong SOE rules that could eventually form the basis for negotiation on the same issues with China.[14]
>
> On-going negotiations over competition rules in the Trans-Pacific Partnership (TPP) Agreement also offer an opportunity to establish a high standard that would set the baseline for new rules to discipline subsidies to Chinese SOEs.[15]

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[11] See my analysis of this in 'Trans-Pacific Partnership as a Lynchpin of US Anti-China Strategy', http://web.me.com/jane_kelsey/Jane/TPPA.html

[12] 'Reid Urges', May 2011

[13] '"21st Century" Trade Issues: The challenges to services trade and investment from state owned/assisted enterprises, restrictions on data flows, and forced localization', 2011 Global Services Summit; Engaging with Dynamic Asian Economies, Washington DC, 20 July 2011

[14] 'Expert: China's push to Invest Abroad May Aid Effort to Discipline SOEs', *Inside US Trade,* 21 July 2011

[15] Elisabeth Drake, 'Chinese State-Owned and State-Controlled Enterprises: Policy Options for Addressing Chinese State-Owned Enterprises', Testimony before the US-China Economic Security review Commission, 15 February 2012

> While application of such rules to the Chinese marketplace would requirement agreement with the Government of China, the TPP Agreement again offers an important opportunity to develop model rules that could form the starting point for such negotiations.[16]

Back in May 2011, US Under-Secretary of State Bob Hormats made the same point indirectly, noting the TPPA was an important forum to introduce higher competitive neutrality standards to which the US could hold others that wish to join.[17]

The China issue is of pivotal importance in how other countries approach the TPPA. As US Secretary of State Hilary Clinton made clear in Honolulu, and reiterated subsequently, the US concern is not simply over the commercial ramifications of China's dominance of its own domestic markets and growing international presence, but that it is shaping these markets 'to build and exercise power on behalf of the state'.[18] It is no surprise that the US seeks to protect its hegemonic interests; that is to be expected. However, its use of the TPPA as the vehicle to do so makes the TPPA a foreign policy issue. That raises important additional considerations when addressing the SOE chapter, as one of the spearheads for the US strategy.

First, the US appears to have no concern about negative implications of the chapter in our countries; those effects are collateral damage in a struggle between the ascendant and declining superpowers of China and the US.

Second, the use of the TPPA as a weapon against China can seriously compromise relationships between other TPPA parties and China. New Zealand's Trade Minister Tim Groser expressed concern on Radio New Zealand last month about the increasingly virulent anti-China rhetoric from the US, which he attributed to think tanks and some academics. He stated unequivocally that New Zealand would pull out of the TPPA talks if politicians in the United States used them as a vehicle to try to contain the rise of China.[19] As that is unequivocally stated goal of the SOE text tabled by the USTR, New Zealand has presumably drawn a red line under the proposal. Other states will doubtless share that concern on a mixture of commercial and foreign policy grounds.

(b) Paradigm conflict between free market and state capitalist models

There is a broader paradigm conflict that has long infused APEC, and is evident in US discussions on the TPPA, between free market models that centre on trade and investment liberalisation and state-supported models of capitalism. Several US commentaries explicitly acknowledge this conflict in relation to TPPA members Vietnam, Malaysia and Singapore,[20] although the model of state-supported capitalism is different from that operating in China. In particular, those promoting the OECD guidelines on SOEs as the best practice framework for SOE disciplines describe them as a set of policy recommendations to address the trade, investment

[16] Drake, February 2012

[17] 'Hormats Says US Will Use BIT Talks To Address SOE Issues With China', *Inside US Trade*, 5 May 2011

[18] 'US Fixes Future-SOE 'Loophole', October 2011

[19] Nigel Stirling, China, the US and New Zealand', Radio NZ Insight, 12 February 2012, http://www.radionz.co.nz/national/programmes/insight/20120212

[20] Dewan, 2012.

and competition issues posed by state capitalism.[21]

The US's SOE text is directly targeting three of the TPPA countries in ways that will have serious consequences for them. This is not a 'partnership'. The impact will clearly also extend to Japan, if it ever passes the test for entry to the negotiations or seeks to accede to the final text. The government-owned Japan Post has been the subject of repeated attacks by the USTR and US banking, insurance and express delivery firms.[22]

(c) Extending the agenda of the Doha round, OECD and US-Singapore FTA

US corporate interests have identified the TPPA as a vehicle through which they can push further with an agenda they have already seeded in other international fora with mixed success.

In the Doha round the US proposed tougher subsidy rules, with specific rules for SOEs that would prohibit certain government financing on non-commercial terms. That sunk with the Doha round. The US also proposed similar positions with China bilaterally, but it has made little progress.

Deputy USTR Demetrios Marantis told the Global Services Summit in mid-2011 how the US had been working with other countries in the OECD and G20 to develop disciplines on SOEs, again making specific reference to China.[23] The principle of 'competitive neutrality' between SOEs and private firms, which is central to the US text, was drawn from the OECD, building on its work on corporate governance. It is clear from the US commentaries that the OECD Guidelines on SOEs will be touted as best practice, if they are not explicitly referred to in the text (which of course I don't know).

Importing external 'best practice' documents into a TPPA should cause particular concern to developing countries that do not have any role in the international organisations that generate them. Developing countries were rightly outraged when the Multilateral Agreement on Investment was being negotiated in the OECD, with the spectre that rich capital exporting countries would construct an agreement that served their interests and present it to the global South as a fait accompli.

Already the regulatory coherence chapter in the TPPA cites as 'best practice' the APEC Information Notes on Good Practices for Technical Regulation 2000 and their expansion through the APEC/OECD Integrated Checklist on Regulatory Reform, which are the work primarily of Australia, New Zealand, the US and the United Kingdom.

The international standards recognised in the Agreement on Technical Barriers to Trade are explicitly required to derive from international organisations that all WTO members can join. Why should, or would, developing countries that are part of the TPPA negotiations, or other countries that are not even at the table, accept these partisan 'disciplines' as the way they should organise their state enterprises?

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[21] 'Hormats Says US Will Use BIT Talks', May 2011

[22] http://www.ustr.gov/countries-regions/japan-korea-apec/japan/regulatory-reform-and-competition-policy-initiative

[23] 'USTR using OECD Work As Guide For TPP Proposals On SOE Disciplines', *Inside US Trade*, 21 July 2011

The third source cited by the US is Chapter 12 of the US Singapore FTA 'Anti-Competitive Business, Designated Monopolies and Government Enterprises'. The chapter requires any Singaporean – *but not any US* – government enterprise to act 'solely in accordance with commercial considerations'. Singapore is required to

> take no action or attempt in any way, directly or indirectly, to influence or direct decisions of its government enterprises, including through the exercise of any rights or interests conferring effective influence over such enterprises, except on a manner consistent with FTA provisions.

Singapore must also 'continue reducing, with a goal of substantially eliminating its aggregate ownership and other interests that confer effective influence in entities organized under the laws of Singapore'.[24] SOEs themselves must refrain from anti-competitive conduct, such as restraints on price, outputs, allocations of customers or exclusionary practices that substantially lessen competition.

The term 'commercial considerations', used in Article XVII GATT and the US-Singapore FTA was considered to be too weak. So the term 'competitive neutrality', used in Australia's competition policy, was preferred but packaged in a text that apparently extends beyond the Australian law.

(d) US exceptionalism

The US's SOE text is a brazen move by domestic US interests to use the TPPA to pursue their own agenda. There is no pretense of some kind of 'partnership'. The original draft of the text, influenced by the US Treasury, reflected concerns to maintain the US own capacity to respond to crises, as it had done post-2007. That was honed back to a peculiar style of US exceptionalism.

Assistant USTR Marantis said in October 2011, around the time of the Chicago round, that the US government was seeking to preserve US practices and its flexibility in future policy making, which could involve government backing for private companies that de facto created new SOEs.[25] Likewise, Deputy USTR Michael Punke said the proposal had to strike a balance between US offensive and defensive interests. The problem was that the flexibility would have been available to other countries as well. Hence the intervention from the US industry lobby to ensure the balance of US offensive and defensive interests gave precedence to their demands.

The appearance that US labour groups are on the same page has muddied the water. They are responding to a quite different imperative. As they face the loss of jobs through bankruptcies, redundancies and offshoring as the US model fails they are seeking to hold ground. Their objective was apparently a text that would prevent Chinese SOEs undercutting US standards within the US. That is a quite different scenario from the deal that is on the TPPA table now.

The US commentaries identify a range of entities that could be affected by an SOE

[24] 'US Business Groups Push for New SOE Disciplines in TPP Negotiations', *Inside US Trade,* 24 March 2011

[25] 'Marantis: USTR To Table SOE Proposal At Lima TPP Round, But Not Labor', *Inside US Trade*, 14 Oct 2011

chapter.[26] These include nationalised industrial and financial entities such as General Motors, Chrysler and AIG; government-sponsored enterprises Fannie Mae and Freddie Mac that received capital injections from the US Treasury in 2008; quasi-governmental agencies like US Postal Service, Amtrak (a Congressional Research Report 2008 said it had been classified as a quasi official agency), Tennessee Valley Authority, Pension Guarantee Benefit Corporation. One commentator speculated that Buy US provisions might also run foul of the disciplines.

Even without access to the text is it clear that there are exemptions for the measures the US took in response to the global financial crisis. It also appears that the disciplines only to central government levels, which protects the US states and those in other federal countries from coverage, but leaves unitary states with much smaller enterprises subject to the disciplines. It is suggested that other states may be able to take exemptions, but these will be limited and temporary. In practice, the US approach is an indirect form of the unilateralism that it applied to Singapore in the US Singapore FTA.[27]

The link to privatisation

The SOE model the US proposes that all TPPA parties (except itself?) should apply has serious flaws. In New Zealand's experience corporatisation has been used to strip away the social, regional development, skills training and other functions and ready enterprises for sale at the expense of taxpayers, workers and communities. If governments choose to pursue this model, they need to have the capacity to tailor it to their particular context and priorities and have the flexibility to undo it if it fails. Secretly negotiated constraints that tie their hands and limit their options to temporary measures in certain exceptional circumstances are irresponsible. They are also fundamentally undemocratic, depriving future citizens of the right to decide how to respond to social and market failure by abandoning that model of SOEs.

Corporatisation is the precursor to privatisation. There is an inexorable logic among champions of a limited state role in the economy that a competitively neutral state-owned enterprise that operates as if it is a private sector business belongs in private ownership. This ignores many relevant factors, including foregoing the income stream from SOEs, permanent loss of the value of the assets, and the permanent abandoning of non-commercial interests served by SOEs.

Significantly, the OECD work on SOEs arose in the context of privatisation. One US commentator suggested that criteria for showing an SOE is investing and operating for commercial and not political purposes (talking in the China context) is moving towards market-based financing of investment deals and towards a 'pathway to privatisation'.[28]

Government will, in turn, be constrained by other chapters of the TPPA from reversing failed privatisations. New Zealand has had a litany of such failures. We had to buy back the Railways, when asset and profit stripping by foreign owners left it

[26] USTR Under the Gun to Generate Draft TPP Language Dealing with SOEs', *Inside US Trade*, 14 July 2011

[27] One commentator observed that the US would not be able to get away with this kind of unilateralism in a TPPA. 'US Business Groups', March 2011

[28] 'USTR using OECD Code', July 2011

barely functional. The national airline, Air New Zealand, was privatised and then nationalised to safeguard the internal passenger and freight transport networks; the current government is privatising it again. After privatization of all our banks left us at the mercy of foreign owners that did not want to service unprofitable poor customers or small town and rural communities, another government has to establish another state-owned Kiwi Bank. In another roundabout, one government put parts of the world-leading no-fault Accident Compensation scheme in private hands, another renationalised them, and the current government is privatising them again, along with electricity companies and coal SOEs, even though 80% of New Zealanders oppose further asset sales.

These are all highly political decisions. Decisions to privatise are problematic enough when they domestic decisions. That autonomy must not become subject to direct and indirect influence by other states and their corporations through the inter-locking SOE, competition, investment, transparency and regulatory coherence chapters of a TPPA. Equally, future governments need the political and regulatory autonomy to reverse nationalisations in forms other than SOEs, if and when they need to.

In conclusion, TPPA negotiators are invited to consider the following questions:

- What is the difference between a state enterprise and a state commercial enterprise?
- What threshold of shareholding will be used: 51%, any residual control over certain strategic decisions, including a golden share?
- Will disciplines extend to entities that receive preferences but are not actually government owned?
- Will they extend to SOEs from third countries operating in the party?
- What activities will the rules cover?
- Will they refer to best practice and if so, whose best practice?
- Will there be an explicit link to the OECD guidelines?
- How will exceptions be identified and according to what criteria?
- Will exceptions be time limited?
- Will exceptions be linked to criteria?
- Will exceptions be permitted only in times of crises and will the deficiencies of the 'prudential' test be repeated?
- Will there be a necessity or least burdensome test?
- Will transparency provisions entitle foreign commercial interests to be consulted or involved in such decisions?
- What reporting requirements will be imposed, how onerous will they be and what is their purpose (US commentators suggest they are the basis for bringing a dispute)?

- What review mechanisms will exist and how far could the disciplines ultimately extend?
- What enforcement mechanisms will there be?
- How reversible will this be if the SOE fails?
- What are the social, skills training, regional development and other social roles that these enterprises currently play?
- What provision is made for these functions to be performed by SOEs?
- If SOEs no longer perform them, who will?
- What will happen to the nation if those essential public goods are no longer performed?