SACU Workshop, 26-27 April, Cape Town, South Africa

On 26 & 27 April 2018, tralac hosted a High-Level Dialogue on SACU, with a focus on the SACU Work Programme and Future Developments. Participants came from the private and public sector across the region.

Discussions centred around three key areas: SACU revenue sharing, SACU's external relations and the future of SACU.

Updates were provided by the SACU Secretariat and member states.

The future of SACU

SACU is the world's oldest customs union, and one of the most integrated regions in Africa. Notwithstanding, or perhaps despite of the SACU Agreement, the SACU region is a well-integrated commercial space and members are inter-dependent. In addition to the being a customs and excise union, four of the five member states (excluding Botswana) belong to the Common Monetary Area, bringing monetary policy into the integration space.

The relationship between the five member states – South Africa, Botswana, Lesotho, Namibia and Swaziland is based on the SACU Agreement, the most recent iteration being completed in 2002.

The Agreement provides for the distribution of the pool of customs and excise revenue, and for the development of common policies in key areas, including competition, industrial development, agriculture and unfair trading.

The Agreement establishes the Commission of Senior Officials and the supreme decision-making body, the Council of Ministers, where decisions are taken by consensus. A Tariff Board and Tribunal are also provided for, but they have not been established. The Agreement has been amended to institutionalise a Summit of Heads of State and Government.

There are many flaws in the way SACU is designed (some resulting from the inclusion of parts of the 1969 SACU Agreement), and in the way it operates. As well as the failure to implement many of the SACU Agreement provisions – the institutions and the common policies – there are elements of the Agreement itself that cause problems. For example, the consensus decision-making model of SACU is problematic, particularly given differing levels of development and size among the members.

SACU in many ways epitomises the challenges in integration across the continent, in particular, the challenge of integrating unequal partners and the challenge of regional integration in the 21^{st} century political and economic environment.

It is in this context that he SACU Council of Ministers decided in 2017 that SACU's work going forward would focus on three areas:

- Tariff management and institutional architecture
- Industrial development
- Revenue sharing

The import tariff features prominently in all three work areas – in SACU there has been a disproportionate focus on the use of the import tariff as the key tool for industrial development, and the smaller member states remain significantly dependent on this source of revenue.

We identified four potential options for SACU's future:

1. **Implementation**: the 2002 SACU Agreement is implemented in full and therefore disquiet around the financial aspects of the agreement, and the common policy-making should be resolved through the institutions that would be established.
2. **Status quo:** Current practice continues – a reality aside from what the SACU Agreement provides
3. **Incremental change:** specific provisions in the SACU arrangement are amended, but there is no wholesale review of the agreement.
4. **Renegotiation of the SACU Agreement:** this could start with a renegotiation of the revenue sharing arrangement

There is an increasing acknowledgement among member states that many provisions of the 2002 agreement are unlikely to come into effect and that incremental change is the most likely course of events, however it will be important to keep reconsidering the value of SACU and its underlying instruments as this process is undertaken.

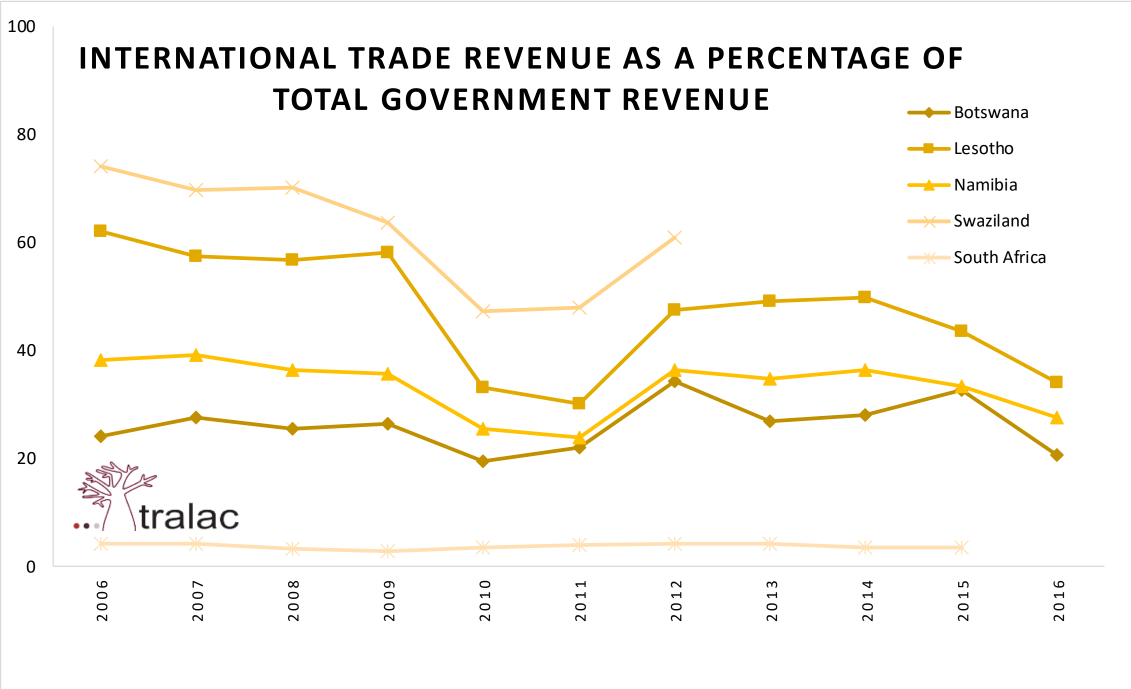
Continuing with the status quo is not supported by most members, but there is a risk that this will be the result, particularly given some of the flaws in the arrangements – for example, the absence of dispute resolution, the failure of member states to institute competition authorities and the absence of supra-national governance.

Members, particularly South Africa, are now speaking of SACU as needing to transform into a 'developmental region' – but it is unclear what this means in practice.

Sovereignty and policy space can dominate discussions around the future of SACU, and conflict with the idea of an integrated trading region. Member states need to focus on what the task is – what they want from SACU. In the 21st century, this should not be merely a customs union, but rather should acknowledge the integration of goods and services, the integration of the financial, monetary and fiscal areas, that is a result of the integration of goods trade and industrial development. In a future SACU, ideally, there would more emphasis on development, and less on the import tariff. More emphasis on competition policy and less on trade remedies. More focus on building value-chains in the region, rather than rebates.

SACU revenue sharing

Revenue is key to the continuation of SACU – it is the glue that holds the union together. Particularly for the BLNS countries, SACU revenue is critical source of income.



Part 6 (articles 32 to 37) of the SACU Agreement provides for a Common Revenue Pool which comprises all customs, excise and additional duties collected in SACU. Part 6 also covers the management of this pool and Part 7 provides a formula to determine each Member State's share of the pool.

The revenue sharing formula has three components. The Customs Component is allocated based on each country's share of intra-SACU imports.

The Excise Component, which constitutes 85 percent of the excise revenue, is distributed based on each country's share of total SACU GDP, a proxy for the value of excisable goods consumed.

The Development Component, fixed at 15 percent of total excise revenue, is distributed according to the inverse of each country's GDP per capita. The deviation in GDP/capita from the SACU average is reduced by a factor 10 to reduce disparity in the distribution of shares for the Development Component.

Revenue sharing is also a significant source of conflict between members. The revenue can be volatile, and the formula results in delayed adjustments. There are concerns from the BLNS about South Africa's management of the Common Revenue Pool and use of rebates, while there is some disquiet on the South African side about *perceived* subsidisation by South Africa of the other member states.

These are issues that are expected to be on the table for discussion in the current SACU work programme. South Africa's Minister of Finance has confirmed that the revenue sharing formula is to be reviewed.

As it is a customs union, the Common External Tariff (CET) applies to all goods entering any of the SACU countries. This CET, which generally provides most of the income to the common revenue pool, is also a source of tension. BLNS states are aggrieved at a lack of influence in setting tariffs, and in accessing rebates – seen as a key policy tool for industrial development.

A Stabilisation Fund for the region is under consideration, but the technical parameters of this are difficult, and unprecedented at a regional level. Member States are also considering a regional financing mechanism to support regional infrastructure development. There are many complications associated with this, such as how to fund it and what projects to fund, but there is a sense that this might be more desirable and more achievable than the proposed stabilisation fund, and may also contribute to BLNS countries relying less on the SACU distributions to support their fiscus.

The management of rebates – a customs duty waiver for industrial and agricultural inputs allowed under the SACU agreement – continues to cause issues for the BLNS states. This is in part due to the institutional infrastructure, which has defaulted to South Africa's International Trade Commission (ITAC), which is legislatively bound to only consider South Africa's interests; in part due to a perception of opacity from ITAC; and in part due to the nature of the SACU market, with one dominant economy, different levels of development and differing industrial policy agendas. There are also complaints about how these rebates are accounted for in the Common Revenue Pool – i.e. should they be withdrawn from the share of the member state whose businesses benefit from any particular rebate. Of course, this would also bring its own complexities.

SACU's external relations

While SACU battles its internal problems, its external relations continue to move forward. SACU negotiates as a bloc and has concluded several trade agreements, although the annex on common negotiation has not been concluded.

Going forward, trade disputes may arise, SACU member states are engaged in the Tripartite Free Trade Agreement (TFTA) negotiations and will have to prepare for the African Free Trade Agreement (AfCFTA) negotiations. Countries, and traders are becoming fatigued with the long list of African regional negotiations and promises and the lack of implementation.

Looking further afield, the United States may well seek a reciprocal agreement and Brexit will impact trading relations with the United Kingdom and European Union.

All the while, issues with existing agreements continue to cause problems.

Southern African Development Community (SADC)

SACU is fully liberalised within SADC, except for sugar, however, rules of origin provisions remain contentious, and for wheat are still not agreed so, wheat trade takes place on MFN rules.

Bilateral agreements remain important, complicating the trading environment in SADC.

Some countries, such as Zimbabwe are requesting special dispensations – to actually increase tariffs. And non-tariff barriers are increasing.

SADC also links industrialisation to the import tariff, which is a very narrow focus – the import tariff is not capable of delivering on the developmental agenda.

Given the demise of the SADC Tribunal, there is nowhere to resolve disputes in SADC.

Tripartite Free Trade Area

The TFTA has been a challenging negotiation as only the SACU countries had experience in negotiating FTAs. There have been diverging views on scope and coverage, the role of RECs, overlapping membership, and the role of secretariats. Rules of origin are an issue, and although countries have agreed to liberalise 85% of tariff lines, tariff schedules have not yet been finalised. At this stage, negotiations between SACU and East African Community (EAC) and between SACU and Egypt are ongoing.

Phase II negotiations, including on services have not commenced, and there is no consensus on how to address these issues, or whether to abandon them given the AfCFTA.

African Continental Free Trade Area

The AfCFTA has been signed, but before the content of the agreement has been finalised.

Member states have agreed to liberalise 90% of tariffs on implementation, there is no phasing in of commitments, and there will be an anti-concentration clause. The AfCFTA is more ambitious on tariffs than the TFTA and so may subsume the TFTA, depending on the modalities. There is a group of seven LDCs who will be allowed to liberalise only 85% of tariff lines.

SACU EFTA – FTA

SACU's Free Trade Agreement with the European Free Trade Association (EFTA) States (Norway, Switzerland, Lichtenstein and Iceland), which includes bilateral side agreements with all the EFTA states except Lichtenstein on agriculture, entered into force in May 2008.

There is an ongoing review process for this agreement. It remains important as the BLNS countries have a big stake in this trade.

SADC-EU Economic Partnership Agreement

The SADC-EU EPA has been implemented after a long gestation period, however there are already some controversial issues on areas such as tariff rate quotas, the creation of institutions and selection of arbitrators, the base trade data for agricultural safeguards, among other things.

This sounds daunting, but these processes and controversies are important in a rules-based trade environment.

SACU-MERCOSUR PTA

SACU's Preferential Trade Agreement with the Common Market of the South (MERCOSUR) entered into force in April 2016. It has a limited scope, and only covers a limited range of products, and so it has a low impact on trade.

SACU India-PTA

The last negotiating round on this agreement was in 2008 and the parties could not agree on a way forward. The Indian side wants a reduction of 70% on average, on 1015 lines, while SACU offered 10%, on 748 lines. It is difficult to see how a compromise could be reached, however, negotiations continue.

SACU – United States.

Free trade agreement negotiations collapsed in early 200s, largely due to new generation issues where SACU has no common positions and was not ready to engage, and US farming subsidies.

Instead, SACU and the US signed a Trade, Investment and Development Cooperation Agreement to promote investment and expand and diversify trade, this does not include any legally binding obligations.

SACU countries are also eligible beneficiaries of the African Growth and Opportunity Act (AGOA), a US law that enhances US market access for sub-Saharan African countries.

SACU is starting discussions again on ongoing engagements with the United States, particularly as AGOA will expire in 2025.

Brexit

The UK is an extremely important trading partner for SACU.

Although the contours of Brexit are not yet clear, and the UK is not yet able to negotiate, SACU and the UK have been in dialogue to safeguard the post-Brexit trading relationship. The aim is to have no disruption in trade. There will be some provisions from the SADC-EU EPA that will be able to be directly rolled over, but in many areas the shape of the ongoing relationship will still be influenced by the EU – for example, quotas, cumulation, non-tariff measures. The built-in agenda of the EPA cannot be rolled over so SACU and the UK will need to also consider areas such as services and investment.

There are also implications for non-trade issues, such as development assistance, including under the Cotonou Agreement, which the UK will exit.