



Occasional Paper

Inter-Jurisdictional Regulatory Collaboration Committee

Performance-Based Codes Impact on International Trade

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There have been many discussions on issues of public policy related to performance-based codes, including their impact on international trade. The following paper is part of a broader IRCC Guidance Document created to explore the major issues pursuant to a performance-based regulatory system.

INTRODUCTION:

The influence of a building code is now no longer confined within national borders. Governments and industry are increasingly seeing the relationship between their internal regulatory framework and the impact that such regulations have upon their industries' ability to operate within the global economy. In part, this is a response to the General Agreement on Tariffs and Trade (GATT) and the World Trade Organization (WTO) – such international trade agreements require all trade barriers to be dropped, which demands transparency of requirements. With purely prescriptive codes, when a country attempts to export their construction products, which conform to their own code requirements, into another country, it is difficult for the recipient country to understand what level of performance the exporting country's products actually provide. In contrast, using a performance-based code with clearly defined criteria, there should not be any ambiguity concerning the performance that is expected. During the last five to ten years, there has been a growing global trend for countries to develop and adopt a performance-based approach to the establishment of building codes and related standards. The global marketplace is going to increasingly apply pressure for more countries to move towards the adoption of verifiable performance codes. Following is a discussion of the impact of performance-based codes on trade in the new globalized economy.

BACKGROUND/ENVIRONMENT:

▪ **Trends**

Globalization/border-less economy, emergence of regional trade blocs, rapid advance of technology

Over the past twenty years the world has experienced a fundamental transformation in the nature of the international economy. In the first three post-war decades, international trade, investment and other cross-border transactions took place largely between firms and individuals in one country and unrelated firms and individuals in another. International transactions largely involved sales of primary goods, machinery and luxury goods, exports of excess production, establishment of foreign affiliates through foreign direct investment, transfers of technology through affiliates and licensing arrangements. Over the past two decades, as a result of globalization, that type of international exchange has given way to a much more integrated kind, with a growing share of cross-border transactions taking place within firms or among related parties. International exchange now involves a much more complex and sophisticated range of economic interactions. Production is being geared to a much wider market, and the range of goods and services that are exchanged internationally is widening considerably.

Global forces are significantly changing the dynamics of global competition. The effects of these forces include:

- borders have been largely erased as a commercial factor. Consequently, the nation-state is no longer the key element in the organization of production or the exchange of goods. The principal organizer of economic activity, the firm, is more likely to have global rather than national interests.
- the rapid implementation of new technology - advances in communications and transportation technology have erased borders and shrunk distances, leading to fundamental changes in business organization and techniques. Revolutionary changes in the organization and technology of production (including faster product cycles) are further hastening the transformation of domestic economies.
- more industries are dependent on trade, and there is growing involvement by other participants (e.g. developing countries) in the trading system. Trade is representing a significant and growing proportion of economic activity.
- the proliferation of trading blocs and associated regional organizations and agreements could be a defensive manoeuvre in response to globalization, leading to increased harmonization of regulations within blocs, and increased discrepancies in regulations between blocs.
- there has been a dramatic growth in the number of international standards and the scope of international standards development activity over the last two decades: as recently as 1957, there were only a few dozen ISO standards. By the end of 1997, there were almost 12,000 ISO standards. In addition, there is growing national as well as sector involvement in international standards development activities. These trends impel the adoption of a global approach to national regulatory systems.

Historically, national regulatory structures developed on the assumption that most economic activity takes place within the borders of the nation-state. Governments assumed that the limited activity that crossed national frontiers could be addressed adequately through their border regimes. The global economy has evolved to the point, however, at which an increasing share of national economic activity is conditioned by global transactions and influences.

As a result, national regulatory structures developed over the past century and a half to address issues of health, safety and more now serve as one of the greatest impediments to trade and further economic development. With the rapid globalization of trade and markets, and the rapid pace of technological change regionally and internationally, compatible regulations are increasingly important factors in establishing the ground rules for market access.

▪ **WTO Agreement**

The WTO regime is beginning to reflect the new reality of the globalization of markets and the fact that trade now represents a significant and growing proportion of economic activity for most of the principal players. From the outset, the General Agreement on Tariffs and Trade (GATT) has included rules to restrain the use of standards and technical regulations as major non-tariff barriers to trade. These principles continue to be the basis for the approach to technical barriers in international trade agreements. During the Tokyo Round of GATT negotiations (1973-79), concern over the growth of technical barriers to trade led to the conclusion of a voluntary Code on Technical Barriers to Trade (TBT). This voluntary code was strengthened and made binding on all WTO members during the Uruguay Round of GATT negotiations. The 1994 agreements require member countries to regulate products in the least-trade-restrictive manner possible in an effort to minimize the burden on international trade and reduce the potential for discrimination in this area. There are now 132 signatories to the WTO Agreement. This expansion has meant that most of the fastest growing economies are signatories and has resulted in a significant increase in the global scale of coverage by the agreement.

The trend towards performance-based codes is consistent with WTO TBT obligations. WTO TBT requires that, for technical regulations affecting trade, technical regulatory requirements must be specified, where possible in terms of performance rather than design or descriptive characteristics. Member economies that are signatories to the WTO General Agreement on Tariffs and Trade have therefore committed themselves to the use of performance requirements in evaluating a products' fitness for purpose and in accepting new and/or innovative products in their market.

▪ Regulatory Reform

The trend to globalization is setting new rules for building construction, largely as a result of trade fora such as the GATT, the European Common Market (EC) and the WTO. This trend has coincided with a similar domestic trend in many countries to reduce the regulatory burden of building codes, make regulations clearer and reduce the overall cost impact to regulators. These developments collectively are causing pressures for changes to the codes and standards for buildings and construction.

In many cases around the world, the change to a performance approach has been undertaken in order to rectify the problems associated with the current system, which has grown both in scope and level of technical complexity over a number of years. The code-using community has been pushing for a variety of reforms to the code documents and the vast majority have been undertaken within the move to performance-based codes.

CONSTRAINTS TO TRADE OF PRESENT PRESCRIPTIVE SYSTEM:

With the success of the GATT/WTO system in reducing global tariff barriers to trade, new trade obstacles have arisen. Amongst these non-tariff barriers, standards and technical regulations have assumed an increasingly important role as impediments to trade, with the result that they have developed into a major item on the trade agenda. Specifically, the present, relatively inflexible, prescriptive building codes are increasingly criticized as being non-tariff barriers to trade, which inhibit the creation of a truly global market. In many cases, difficulties in understanding the regulatory regime in a particular market operates as a *de facto* discriminatory barrier against imports (resulting in increased costs, creation of barriers to innovation, suppression of international competition, etc). To reduce these regulatory barriers to trade would require increased transparency as well as greater reliance on functional, performance-based rather than designed-based specifications.

HOW PERFORMANCE-BASED CODES ARE SUPPORTIVE OF GLOBAL TRADE POLICIES:

In light of the above discussion, the attributes of a performance-based regulatory system are conducive to the global trade environment in the following manner:

- **Performance-based codes will provide international credibility**

The need to open regulatory systems to foreign scrutiny in order to participate in trade agreements requires a building code that is flexible and transparent, and compatible with the regulations in other countries (i.e the same technical basis of requirements, but not necessarily the same level of performance). By providing a clear indication of the intent and performance requirements that a product must meet, performance-based regulations will make it easier for exporters to convince other countries of the level of performance that can be expected of a product, facilitating recognition by trading partners and helping to legitimize products both at home and abroad.

- **Performance-based codes will provide a common basis upon which products and solutions can be compared and assessed - can be used to create a common market**

As the “Global Village” concept develops between countries, the adoption of universal terms and formats can facilitate consistency of regulations in international trade and serve as a primary means of eliminating misunderstanding between countries. Consequently, those countries that adopt performance-based regulations should have an easier time exporting products and professional services to other countries that have also conformed to a performance-based system. This creation of a common market will create more efficient economic interactions and economies of scale that would flow from producing to satisfy a single globally accepted regulation. It should be noted that, in addition to common performance criteria for products and systems, a common regulatory structure (i.e. standardized building terminology), as well as common performance evaluation systems and assessment methods need to be established among trading partners, in order for this outcome to be significant.

- **Performance-based codes can be used as a marketing device to expand trade opportunities**

In an increasingly competitive international trading environment, other advanced countries use technical regulations as an important marketing tool in developing their trade relations. A performance-based system provides the means to communicate the attributes of a product more compellingly. By focusing on the performance attributes of a particular product, performance-based codes can be trade-promoting and facilitating. In addition, performance-based codes promote international competitiveness; firms operating in a performance-based system are exposed to global trading conditions, and are compelled to becoming more outward-oriented and competitive on a global scale.

- **Performance-based codes preclude countries from using regional regulatory systems to restrict trade**

Currently, international trade in building and construction products and services tends to be relatively segmented and insulated by national markets. This is largely a result of prescriptive regulatory regimes, which have been used (intentionally or unwittingly) as non-tariff barriers to trade. Under the performance-based approach, even if each region adopts its own unique, regional based system due to differing societal values, the resulting transparency and clarity of intent will prove to be less restrictive to trade.

- **Support of innovative products/new technologies will provide new export opportunities**

The current prescriptive system is based on process (how the product is made) or physical attributes (product composition) and favor existing manufacturers who have access to specific types of material or machinery and are skilled in a particular manufacturing process. Performance regulations on the other hand, favor new entrants who may have new techniques or innovative products and production processes. Moreover, the rapid technological change and faster product cycles of today's business environment require a flexible system that is responsive to change – requirements which can be met by a performance-based system.

- **Performance-based codes can simplify conformity assessment procedures**

This can occur when exporting to countries with a performance-based system with a common regulatory structure, which concurrently adopt universal verification methods. Given, for a specific requirement the use of a uniform performance measure, it will provide for a common basis upon which construction products and systems can be compared and assessed.

OTHER ISSUES:

▪ **Can performance-based codes be barriers to trade?**

This discussion has focussed primarily on the trade-facilitating nature of a performance-based regulatory regime. However, in certain situations, performance-based codes can also potentially be regarded as barriers to trade:

- the use of performance criteria, on their own, would likely increase the level of technical sophistication required for development, enforcement and verification; this can serve as a barrier to entry and to the adoption of such a system by less developed countries and less skilled, small scale business, effectively barring them from the trade arena
- no single regulation can fully balance the special structural, legal, cultural, environmental and historical conditions that exist in each country, resulting in the possible development of unique, regional performance systems without common basis; this may secure transparency of regulatory requirements, but fail to provide favorable conditions for trade
- when performance-based codes refer to different performance requirements for the same regulatory objective; also if the performance assessment and evaluation methods are different or refer to different standards for assessment/evaluation in each jurisdiction; this can create confusion and difficulties among trade partners
- support structures of a performance-based system, such as performance approval/accreditation systems, liability concern, and insurance policy, may differ among different jurisdictions and serve as a trade barrier

These are all issues, which must be considered in the establishment of a performance-based system, in order to preclude this potential outcome.

SUMMARY:

With the globalization of trade and markets and the rapid pace of technological change, the influence of building codes on international trade has become significant. The WTO Agreement, reflecting the reality of globalization, requires that for technical regulations affecting trade, requirements must be specified in terms of performance rather than prescriptive characteristics. In addition, the trend towards regulatory reform is causing pressures for changes to the current prescriptive-based system, which has been identified as perpetuating non-tariff barriers to trade.

These developments have influenced a growing global trend for countries to develop and adopt a performance-based approach to building regulatory systems. A performance-based system is conducive to today's global trade environment by creating conditions favorable to trade - performance codes remove ambiguity and provide a clear indication of intent and performance requirements, providing a common basis upon which products can be compared and assessed. These attributes can provide international credibility for building product exports, making them more easily accepted in foreign markets, ultimately lowering trade barriers.

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