

# The WTO negotiations on services: The regulatory state up for grabs

## SETTING THE STAGE FOR NEGOTIATIONS

At present, WTO members are negotiating to further liberalize international trade in services. Services cover activities ranging from financial and telecommunications services over health and education to energy services and the provision of water. In the context of the General Agreement on Trade in Services (GATS), trade-policy makers currently design new rules to more comprehensively govern worldwide trade in such services. In June 2003, they will start a new phase of negotiations—the request/offer phase—aimed at rendering each other’s domestic services markets more open by requiring their trading partners to enter into additional liberal commitments under the GATS market access and national treatment provisions. Together, these negotiations bring about a series of challenges for trade-policy makers, domestic regulators, and civil society.

## THE THREAT TO DOMESTIC REGULATORY FLEXIBILITY

Most prominent among these challenges is the fear that further liberalization of international trade in services may inappropriately constrain domestic regulatory prerogatives. Domestic regulatory activities are crucial to attain legitimate policy goals intertwined with the provision of services. There are important public goods aspects to many service sectors, such as telecommunications, education, health, or the provision of water, with a corresponding need for extensive regulation. Even where there are justifications for demonopolization and regulatory reform, new regulations are needed to address access to “networks,” consumer protection, and equitable access to basic services.

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**Flexibility and diversity in domestic regulation are at risk from future liberalization of trade in services.**

Flexibility and diversity in domestic regulation are at risk from future liberalization of trade in services. Services liberalization aims to increase international trade by reducing obstacles to trade. As is obvious from even a cursory glance at the manual on services trade regulation produced by the WTO Secretariat, many domestic regulations of a generally applicable character are considered as possible “obstacles to trade” to be eliminated through commitments negotiated at the WTO, even where the measures in question contain no explicit element of discrimination against trading partners.

## LACK OF CLARITY IN GATS

Here it is important to note that the existing agreement on services trade at the WTO, the GATS, doesn’t clearly limit or define the scope and coverage of obligations that WTO members may undertake within the framework for serv-

ices trade liberalization. One apparent exception is GATS article I:3(b), which excludes “services supplied in the exercise of governmental authority.” However, a closer look reveals that the exact scope of this governmental/public services exception is far from clear. In order to be exempt from the GATS, a service has to be provided “neither on commercial basis” nor “in competition with one or more services suppliers.”

To date, the precise meaning of these provisions remains unclear. In the case of basic health services, for example, it remains unclear whether user fees or even insurance premiums charged for public health care would result in these services being found to be provided on a “commercial basis,” and thereby subject to general GATS disciplines. The wording of article I:3(b) creates uncertainty for governments seeking to experiment with public/private partnerships, or with regulatory reform of a services sector that combines a role for government in the provision of public goods with a role for the private sector in assuring competitiveness and efficiency in non-monopoly aspects of the service.

Similar lack of clarity surrounds some of the rules based upon which members enter into specific commitments for individual services subsectors and modes of supply. For example, the GATS national treatment obligation (article XVII) establishes that a member, once it has accepted that one of its subsectors and modes of supply is bound by this provision, may not discriminate between domestic and foreign “like” services and service suppliers. In that case, the scope of permissible regulatory action depends upon whether two services or service suppli-

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ers are considered to be “like” or “unlike.” However, neither the GATS nor any other WTO agreement provides guidance on how to determine the “likeness” of services and service providers. Such a determination is crucial from an environmental perspective, where different production methods might warrant different regulatory treatments. In the case of energy services for example, different energy sources—that is, solar versus carbon—might require different regulatory frameworks. With respect to energy, the situation is even more complex because some WTO members view electricity as a good, falling under the GATT, while others view the generation of electricity and the operation of power plants as a service. Consequently, before entering into further commitments under the GATS, WTO members may wish to clarify the breadth of its basic obligations. Also, members may wish to carefully design their specific commitments to carve out policies they wish to preserve.

## NEW RULES AND DISCIPLINES

Another source of concern is linked to the design of new rules and disciplines in the ongoing negotiations. To ensure that the GATS framework more comprehensively governs international trade in services, members are currently negotiating new rules in the areas of subsidies (article XV), government procurement (article XIII), and domestic regulation (article VI.4). Future disciplines on domestic regulation would either apply across the board to all services sectors, to certain commonly agreed upon sectors, or at a minimum to all sectors with respect to which members have made specific commitments in their schedules.

## THE NECESSITY TEST

A central concern in that context is the proposal to apply a necessity test to non-discriminatory domestic regulations. If in the future, a necessity test would be applied “horizontally,” that is for all services sectors and in the form

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of “general disciplines” without granting members the possibility to decide whether their individual services sectors and modes of supply should be bound—such rules would indeed significantly constrain domestic regulatory prerogatives. Affected regulations would be those relating to qualification requirements, for professions such as doctors or teachers; technical standards and licensing requirements, which most likely would also cover zoning restrictions designed to monitor planning permission—for example, in the retail sector. Thus, a great deal of domestic regulations would have to be “not more trade restrictive than necessary.” What, it has to be asked, are the consequences of applying a “necessity test” to such a broad array of domestic regulations?

Here the intrusiveness of the proposed disciplines is far greater than those of the GATT in the case of trade in goods. Under the GATT, generally speaking, only if domestic regulations are found to constitute trade-protective discrimination, in other words to be in violation of the obligation of national treatment, are they subject to scrutiny under a necessity test.

The role of the necessity test proposed in the GATS framework would, however, be quite different. Its purpose would not be to grant a government the

possibility to justify domestic regulations that have been found, *prima facie*, to contain elements of trade-protective discrimination, as is the case where the necessity test is applied in relation to certain exceptions in article XX of GATT. Rather in the GATS concept, the meaning of the necessity test would be that the WTO dispute settlement organs would become something like a global regulatory review agency, second-guessing domestic regulatory trade-offs in services regulations, regardless of whether there is any element of protectionism.

## TRADE EXPANSION VERSUS THE REGULATORY RIGHTS OF GOVERNMENTS

The fundamental purpose of a necessity test, as explained by the WTO Secretariat, is that of a “means by which an effort is made to balance between two potentially conflicting priorities: promoting trade expansion versus protecting the regulatory rights of governments.” How, if at all, should such a balancing take place and are WTO tribunals the right organs to carry out such a balancing exercise? In the current negotiations WTO members have further elaborated on how this “balance” between promoting free trade and preserving governments’ regulatory rights to achieve legitimate policy objectives may look. The EC, for example, has made a proposal that suggests that “[a] measure should be considered not more trade-restrictive/not more burdensome than necessary if it is not *disproportionate* to the objective[s] pursued.”

Again, a fundamental concern is that this could lead to a WTO tribunal deciding whether a domestic measure aimed at achieving a legitimate policy objective “*disproportionately*” restricts trade. Similarly, it is highly questionable whether it should rest with a WTO tribunal to make value judgments about the *importance* of a domestic policy objective. Many believe that the WTO is ill equipped and the wrong forum to make

these sorts of decisions, because such a balancing exercise would involve judgments weighing fundamental societal values. Given these serious concerns, WTO members may wish to refrain from designing rules that give overly broad decision-making powers to WTO tribunals.

### **THE LACK OF A SAFEGUARDS MECHANISM**

The above concerns about loss of domestic regulatory flexibility are aggravated by the difficulties surrounding export changes of the relevant GATS disciplines and individual specific commitments. Most importantly, unlike the regulatory framework covering trade in goods, the current GATS framework does not yet contain a safeguards agreement. Safeguard provisions usually aim to allow the importing trading partner to take back obligations that cause serious injury to domestic industries producing a good or service, which is “like” or in competition with those goods or services whose importation is increasing, due to the acceptance of market-opening obligations.

In the GATS context, members cannot currently resort to any safeguards mechanism. Thus, if a member’s services market is being swamped by foreign imports and if its industry is negatively affected by such imports, the importing member to date has no means to unilaterally impose temporary measures to allow its domestic industry to adjust. Yet, such a safeguards mechanism would be of fundamental importance for developing country WTO members because, in most cases, their services industries are still at an early stage of development and, therefore, most vulnerable to increasing imports from highly competitive service providers.

The need for a safeguards mechanism is even recognized in the GATS agreement, which mandated members to adopt such a mechanism by January 1998. Unfortunately, although members have spent the last years negotiating such a mechanism, the adoption of any

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respective instrument has been postponed several times, most recently from March 2002 to March 2004. With the request/offer phase coming closer, the ongoing lack of safeguards is likely to become particularly detrimental for developing countries, many of which will be pressured into opening up their services markets to foreign competition, without being granted any possibility to impose temporary safeguards measures.

### **THE LOCK-IN EFFECT**

In addition to the lack of safeguards, undue constraints for domestic regulatory flexibility may also arise from the GATS’s “lock-in” effect for specific commitments. Indeed, many hail it as one of

the positive features of the GATS in that its specific commitments provide services exporters with the type of legal security and predictability necessary to conduct international business. Although feasible in theory, it is virtually impossible for a WTO member to reverse specific commitments: the “modification of schedule” process may start only three years after a commitment has been taken and it entails lengthy and difficult negotiations about the level of compensation for affected trading partners. Again, this bargaining process promises to be particularly difficult for developing country members, which, because of their lack of negotiating expertise and their difficult economic situations, might be those countries most in need of quick and easy modification processes. In addition, the GATS “lock-in” effect may also bring about ramifications for citizens’ democratic right to decide how services are regulated in the future. Citizens having elected a government upon its promise to reverse or adapt certain steps toward economic liberalization in the services sector will realize that the latter may have virtually no means of taking back measures if preceding governments had enshrined them as binding GATS commitments.

### **FUTURE CONSIDERATIONS**

Beside the area of specific commitments, similar issues might also arise with respect to current rule-making processes under the GATS. As explained above, there are concerns that certain rules and negotiating proposals might not be adequate for the services sector. Yet it is most likely that members will go ahead and agree on a set of disciplines, possibly without the foresight and experience required to design adequate and well-balanced disciplines. Also, to not endanger the conclusion of any agreement, the highly political nature of multilateral trade negotiations might induce members to agree upon ambiguous language. In both cases, modification or clarification of the provision in question might

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be needed. However, experience with the TRIPS agreement has shown how hard it is to change agreed rules in order to re-balance a once agreed upon WTO agreement. Likewise, experience with GATS article I:3 has shown how difficult it is for members to acknowledge the need to clarify a highly ambiguous provision.

### **A THOROUGH AND COMPREHENSIVE ASSESSMENT AND EVALUATION PROCESS IS CRITICAL**

Thus, WTO members should not rush blindfolded into accepting binding specific commitments or agreeing upon new rules and disciplines. Rather, members should precede any negotiations with a thorough and comprehensive assessment and evaluation process, reviewing both positive and negative effects of services liberalization with a view to promoting key environmental, social, and development goals. Only such an assessment will provide negotiators with the much-needed information to achieve a sustainable and well-balanced outcome of negotiations. The need for such an assessment is already acknowledged in the GATS agreement itself, which states in article XIX:3, that for the purpose of establishing negotiating guidelines and procedures, members "shall carry out an assessment of trade in services."


Unfortunately, members have not succeeded in carrying out a satisfactory assessment before the establishment of the negotiating guidelines and, therefore, paragraph 14 of the March 2001 guidelines makes assessment an ongoing activity of the council. More importantly, the guidelines also state that negotiations shall be adjusted in light of the result of the assessment. Indeed, when comprehensively looking at the pros and cons of services trade liberalization as well as at the regulatory challenges arising in that context, GATS assessment could provide valuable input into the negotiating process and assist negotiators to avoid some of the pitfalls and dangers described above. Assessment will become even more crucial with the request/offer phase rapidly approaching.

### **OPEN, TRANSPARENT NEGOTIATIONS**

In addition, both the assessment as well as the negotiating processes should be conducted in an open and transparent way. Unfortunately, this is not yet the case. Both a recent two-day WTO symposium on services trade assessment as well as the ongoing negotiating and working sessions of the CTS (Council for Trade in Services) and its subsidiary bodies are closed to the public. Also, while the WTO Secretariat appears to increase transparency by regularly up-

dating a list of most recent negotiating documents on the WTO web site, many of the equally important background documents, informal "job-" or "non-papers" and the minutes of the relevant meetings remain largely inaccessible for the interested public.

Even greater transparency issues are likely to arise once the next phase of the bilateral request/offer negotiations start. Up until now, many WTO members have agreed to make their initial expressions of interest for the request/offer phase public. However, to date, several WTO members have also indicated that the more detailed requests and offers, as well as initial agreements among negotiating partners will remain secret.

Given the broad implications that a country's GATS commitments have upon its regulatory freedom to enact policies aimed at attaining legitimate objectives, depriving the public of access to a country's negotiating position seems fundamentally undemocratic and thereby raises serious concerns. In that vein, it is crucial that both the June 2002 request and March 2003 offers, as well as any intermediary conclusions, agreements, or changes of negotiating positions are readily communicated and available to the interested public and that WTO members' negotiating positions reflect the concerns of all affected constituencies. 

## What is the WTO for? continued from page 1

Many of the criticisms are based on the mistaken notion that the WTO has autonomous authority that overrides that of its individual members. Of course, in reality, it is a voluntary arrangement for negotiating and implementing contracts between sovereign powers. The WTO as such has no mechanisms of its own to coerce or impose outcomes on governments. It is up to the individual member nations to join, and they are free to pull out—though so far none has done so.

Behind many of the attacks lies resentment at the WTO's binding dispute procedures. Many recent dispute rulings have been castigated as undemocratic intrusions into national sovereignty. However, critics are divided about solutions. Some simply want to demolish the organization. For others, undoubtedly the majority, the problem is less with binding rules as such, than the purposes they are intended to serve. Their chief interest appears to be in getting the rules re-written and interpreted

to uphold priorities other than trade. Indeed, some that assail the WTO as unaccountable and dictatorial appear eager to appropriate its machinery to promote diverse and sometimes conflicting alternative agendas.

At the same time, the role of WTO rules has recently aroused growing controversy among its members. First, there are developing countries' complaints about implementation, above all of the TRIPS (Trade-Related Aspects of Intellectual Property Rights) agree-