The GATS, democratic governance, and public interest regulation

BY SCOTT SINCLAIR

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THE MOST IMPORTANT SINGLE DEVELOPMENT IN THE MULTILATERAL TRADING SYSTEM

The General Agreement on Trade in Services (GATS) has been described as "perhaps the most important single development in the multilateral trading system since the GATT (General Agreement on Tariffs and Trade) itself came into effect in 1948." Despite its importance, the GATS was hardly known when the Uruguay Round of international trade negotiations concluded in 1994. It has only recently begun to attract the public scrutiny that it deserves. This broadly worded treaty to enhance the rights of international commercial service providers has potentially far-reaching public policy impacts. These impacts merit serious attention and debate.

FROM THE GATT TO THE WTO

The GATS was created under the umbrella of the WTO, which came into being on January 1, 1995 after eight years of complex and difficult negotiations. The WTO agreements subsumed and ranged far beyond the GATT, which had regulated international trade since 1948. While the GATT system had gradually been amended and elaborated throughout the post-war period, the advent of the WTO profoundly transformed the multilateral trading regime in several respects.

The most important of these fundamental changes were:

- While the GATT was simply an international agreement among "contracting parties," the WTO is a full-fledged multilateral institution with "member governments." It now takes a place alongside the International Monetary Fund, the World Bank, and other elite international economic institutions.
- While GATT rules primarily covered tariffs and trade in goods, the WTO rules cover not only trade in goods, but agriculture, standards-setting, intellectual property, and services.
- While the GATT focused primarily on reducing tariffs and other "at-the-border" trade restrictions, the far broader scope of the WTO means that it intrudes into many "behind-the-border" regulatory matters.
- While the GATT agreements had gradually expanded to cover new matters such as procurement or standards-setting, adhering to these side codes was optional. By contrast, the WTO agreements are a "single undertaking," meaning that member governments have no choice but to be bound by all WTO agreements.

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rangements." This is the pragmatic and constructive way of the WTO's future.

INTERNATIONAL FINANCIAL SUPPORT

In the end, there is no escape from the fact that poverty eradication and developmental objectives will require more finance. At present, the United States lacks the political will to increase significantly its official development assistance, except to those countries in which it has a security interest. But other countries, even some G7 members, do. Any Kananaskis consensus will have to incorporate US foot dragging on foreign aid. More progress in global poverty eradication and development objectives is therefore likely to be made in forums and cooperative arrangements other than the G7. If the government of Canada were serious about its stated objectives in Africa, it would do better aligning itself with Europe and increase its support for development significantly.

Among the reasons why the UN Conference on Finance for Development (March 2002 in Monterrey) is potentially significant is that it marks the first time that the more representative procedures of the UN have been permitted to "intrude upon" the procedures and practices of the international financial institutions. Because of pressure from the United States and others, this "intrusion" has not been permitted to travel very far. Some would even argue that the UN has been co-opted into the world of the Bretton Woods institutions. Yet finance ministers are forced, by this event, to talk about major financial issues with their "more political" counterparts in ministries of foreign affairs, not only in international circles but also at home. Despite the best efforts of the IMF, World Bank, and G7 officials to keep such matters off the agenda, global governance issues cannot help but surface at this UN conference.

Little of significance is likely to be achieved at this UN conference on international financial policies or governance, or even on development finance. This event, nevertheless, marks a small step toward more legitimacy because it consists of a slightly more representative process for the discussion of global economic governance. However small a step it may appear, its long-run significance, as a precedent, may prove to be profound.

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- Perhaps most significantly, while the GATT dispute settlement system was essentially "diplomatic" (panel rulings had to be adopted by consensus, including the agreement of the defendant government), the WTO dispute system is "legally binding" (the adoption of panel rulings can be blocked only by consensus, including the agreement of the complaining government).

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A CONSTITUTIONAL SHIFT

These changes qualitatively transformed not only the GATT regime, but the entire multilateral system. Taken together, they amount to a constitutional shift: a fundamental reworking of the basic legal precepts of the multilateral trading regime and of its role in the international system. Multilateral rule making, and especially enforcement, to protect commercial trading interests surged ahead of international rule making in other vital areas such as environmental protection, human rights, public health, and cultural diversity. These changes, relatively unnoticed and undebated at the time, are now proving both controversial and destabilizing.

THE SCOPE OF THE GATS

First, a few undisputed facts. The GATS was concluded in 1994 as part of the Uruguay Round. It took effect on January 1, 1995. It is part of the WTO's single undertaking and therefore binds all WTO member governments. It is subject to legally binding dispute settlement. The GATS consists of a "top-down" framework of rules that cover all services, measures, and ways (or "modes") of supplying services internationally. This framework is combined with more intrusive rules that apply only to services that governments explicitly agree to cover. Further negotiations to expand GATS rules and to increase its coverage are built into the agreement. The first of these successive rounds to broaden and deepen the GATS is currently underway in Geneva.

GATS critics and proponents agree on at least one critical point. The scope of the GATS is very broad—far broader than traditional rules governing trade in goods. Indeed, the subject matter of the GATS—services—is immense. These range from birth (midwifery) to death (burial); the trivial (shoe shining) to the critical (heart surgery); the personal (haircutting) to the social (primary education); low-tech (household help) to high-tech (satellite communications); and from our wants (retail sales of toys) to our needs (water distribution).

Moreover, the GATS applies to all measures affecting services taken by any level of government, including central, regional, and local governments. Therefore, no government action, whatever its purpose, is, in principle, beyond GATS scrutiny and potential challenge. As noted, all service sectors are also on the table in ongoing, continuous negotiations.

For the critics, this breadth and the GATS novel restrictions set off alarm bells. As a former director general of the WTO, Renato Ruggiero, has admitted the GATS extends "into areas never before recognized as trade policy." Not limited to cross-border trade, it extends to every possible means of providing a service internationally, including investment. While this broad application does not, of course, mean that all services-related measures violate the treaty, it does mean that any regulatory or legislative initiative in any WTO-member country must now be vetted for GATS consistency or risk possible challenge.

HOW FLEXIBLE IS THE GATS?

The proponents, however, while acknowledging the treaty's universal scope, stress its "remarkable flexibility." They also point to its controversial exclusion for governmental services and the range of exceptions available to protect otherwise non-conforming measures from successful challenge.

Proponents sometimes refer to the GATS as a "bottom-up" agreement. This refers to a treaty that applies only to those specific government measures and sectors that individual governments explicitly agree to cover. By contrast, "top-down" treaties automatically apply to all measures and sectors unless governments explicitly exclude them by negotiating them off the table. The GATS, however, is not a purely bottom-up agreement. It is, in fact, a hybrid agreement that combines both bottom-up and top-down approaches.

Certain GATS obligations, most notably the most-favoured-nation rule, already apply unconditionally across all service sectors. And, while it is true that the most forceful GATS obligations apply only to sectors that governments explicitly agree to cover, there are serious limits to this flexibility:

- Most governments have already given up much flexibility by not

making full use of their one-time chance to specify limitations to their initial GATS commitments.
- Members remain under intense pressure to cede flexibility in successive rounds of negotiations to expand GATS coverage.
- The GATS requires governments that withdraw previously made commitments to compensate other governments whose service suppliers are allegedly adversely affected.
- Protective country-specific limitations will endure only if all future governments are committed to maintaining them.

The GATS vaunted flexibility is, therefore, considerably less than is sometimes claimed.

THE GATS GOVERNMENTAL SERVICES EXCLUSION

The GATS covers all services, except those "supplied in the exercise of governmental authority." At first glance, this controversial exclusion is potentially broad, but it is highly qualified. GATS article I:3 excludes services provided "in the exercise of governmental authority," but it goes on to define these as services provided on neither a commercial nor a competitive basis. These terms are not further defined and, if left to the dispute settlement process, will most likely be, according to the rules of treaty interpretation, interpreted narrowly.

"Public services" are rarely delivered exclusively by government. They are complex, mixed systems that combine a continually shifting combination of public and private funding, and public, private not-for-profit, and private for-profit delivery. A truly effective exclusion for public services should safeguard government's ability to shift this mix and to regulate all aspects of these mixed systems. Where the GATS exclusion is most needed, when governments want to expand or restore the public, not-for-profit character of the system, it is least effective. This controversial exclusion is, therefore, ambiguous at best and ineffective at worst.

A common refrain in every official rejoinder to GATS critics is that the GATS specifically recognizes governments' right to regulate. Regrettably, it is terribly misleading to suggest that the mere affirmation of the right to regulate, contained in the treaty preamble, fully protects the right to regulate. It does not.

THE GATS PREAMBLE AND THE "RIGHT TO REGULATE"

A common refrain in every official rejoinder to GATS critics is that the GATS specifically recognizes governments' right to regulate. Regrettably, it is terribly misleading to suggest that the mere affirmation of the right to regulate, contained in the treaty preamble, fully protects the right to regulate. It does not. While the preamble does contain a clause that "recognizes the right of Members to regulate," this language has strictly limited legal effect. It would have some interpretive value in a dispute but should not be construed as providing legal cover for regulations that would otherwise be inconsistent with the substantive provisions of the treaty. In short, governments retain their freedom to regulate only to the extent that the regulations they adopt are compatible with the GATS.

THE MFN RULE

The GATS most-favoured-nation treatment (MFN) rule, which applies to all service sectors, has proven to be a surprisingly powerful obligation in two recent GATS-related disputes. This rule (GATS article II) is best understood as a most-favoured-foreign *company* rule, because it requires that any regulatory or funding advantage gained by a single foreign commercial provider must be extended, immediately and unconditionally, to all. The MFN obligation has the practical effect of consolidating commercialization wherever it occurs. While not legally precluding a new policy direction, this rule makes it far more difficult for governments to reverse failed privatization and commercialization.

THE NATIONAL TREATMENT AND MARKET ACCESS RULES

The hard core of the GATS comprises restrictions that apply only to the sectors, or subsectors, where governments have made specific commitments. These commitments, together with any country-specific limitations, are listed in each government's GATS schedule.

The GATS national treatment rule (GATS article XVII) requires governments to extend the best treatment given to domestic services (or service providers) to like foreign services (or service providers). In the GATS, this rule is quite intrusive, because it explicitly requires government measures to pass a very tough test of *de facto* nondiscrimination. That is, measures that on their face are impartial can still be found inconsistent if they modify the conditions of competition in favour of domestic services or service providers. This gives dispute panels wide latitude to find measures GATS-illegal even when they are, on their face, nondiscriminatory or when such measures alter the conditions of competi-

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tion merely as an unintended consequence in the legitimate pursuit of other vital policy goals. The GATS stiff national treatment requirement thus opens the door for non-discriminatory public policy to be frustrated for reasons that are unrelated to international trade.

The GATS market access rule (GATS article XVI) is one of the treaty's most novel, and troublesome, provisions. There is nothing quite like this rule in other international commercial treaties. Framed in absolute rather than relative terms, it precludes certain types of policies whether or not they are discriminatory. A government intent on maintaining otherwise inconsistent measures is forced to inscribe them in its country schedules when it makes its specific commitments. This rule prohibits governments from placing restrictions on the number of service suppliers or operations; the value of service transactions; the number of persons that may be employed in a sector; and, significantly, the types of legal entities through which suppliers may supply a service.

Such prohibitions call into question, for example, the GATS-consistency of limits imposed to conserve resources or protect the environment. Also, many governments restrict the private delivery of certain social services such as childcare to non-profit agencies. Many also confine certain basic services such as rail transportation, water distribution, or energy transmission to private, not-for-profit providers. Such public policies certainly restrict the market access of commercial providers, whether domestic or foreign. But they have never before been subject to binding international treaty obligations. Now, whether this was intended or not, these vital policies are exposed to GATS challenge.

GATS RESTRICTIONS ON MONOPOLIES AND EXCLUSIVE SERVICE SUPPLIERS

The GATS restrictions on monopolies and exclusive service suppliers (GATS article VIII) impose new burdens on monopolies and exclusive service supplier arrangements. In fact, monopolies and exclusive service suppliers are GATS-inconsistent and must be listed as country-specific exceptions in committed sectors. Any government wishing to designate a new monopoly in a listed sector is required to negotiate compensation with other member governments or face retaliation.

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Monopolies, while not so prevalent as they once were, are still relied upon to provide basic services in many countries. Postal services, the distribution and sale of alcoholic beverages, electrical generation and transmission, rail transportation, health insurance, water distribution, and waste disposal are just some of the more widespread examples. Exclusive supplier arrangements are commonplace in post-secondary education, health care, and other social services. The consequences of these GATS rules, which so far have gone largely unexamined, are likely to be significant in all of these important areas.

GATS RESTRICTIONS ON DOMESTIC REGULATION

If proposed GATS restrictions on domestic regulation (GATS article VI.4), now being negotiated in Geneva, were ever agreed to, they would constitute an extraordinary intrusion into democratic policy making. At issue is the development of "disciplines" on member country's domestic regulation, explicitly non-discriminatory regulations that treat local and foreign services and service providers evenhandedly. The subject matter of these proposed restrictions is very broad, covering measures relating to qualification requirements and procedures, technical standards, and licensing procedures; a wide swath of vital government regulatory measures.

Critically, these proposed restrictions are intended to apply some form of "necessity test"—that is, that regulations must not be more trade restrictive than necessary and that measures must be necessary to achieve a specified legitimate objective. Perversely, the proposed GATS restrictions would turn the logic of the long-established GATT necessity test on its head. It would transform it from a shield to save clearly discriminatory measures from challenge into a sword to attack clearly non-discriminatory measures. The proposed GATS restrictions on domestic regulation are a recipe for regulatory chill; they are among the most excessive restrictions ever contemplated in a binding international commercial treaty. This excess is concrete evidence of the hazards of leaving the ambitions of commercial ministries, and the corporate lobbyists driving them on, unchecked by broader public scrutiny and debate.

A CONTROVERSIAL AGREEMENT

The GATS is a deservedly controversial agreement. Its broadly worded provisions give too much weight to commercial interests, constraining legitimate public interest regulation and democratic decision making.

As GATS proponents frequently insist, the treaty does not *force* governments to privatize public services. But this is somewhat beside the point, because

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TRIPS: Controversies and potential reform

BY KEITH E. MASKUS

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The WTO Ministerial Conferences in Seattle in 1999 and Doha in 2001 may have marked a new era in global trade negotiations. In particular, governments of developing countries are becoming increasingly assertive in criticizing the structure of the trading system and presenting their own positions. The Seattle meeting failed in part because developing countries pushed for changes in the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) and were unwilling to countenance strengthening its standards as advocated by the United States. At Doha, the WTO members agreed to relaxed interpretations of the obligations many of the least-developed countries found onerous or impossible to meet, most significantly in the treatment of patents for essential medicines.

FROM SEATTLE TO DOHA

The road from Seattle to Doha was not travelled by trade ministers alone. As it became clear that TRIPS standards could restrain government policies in health care, agriculture, environmental protection, education, and technology supports, wider official interests questioned the utility of these standards. Numerous NGOs made their views known about how TRIPS might make more costly the provision of global collective goods in such areas as medicines, food security, and biodiversity. In turn, media interest has mushroomed with regard to the implications of global protection of intellectual property rights (IPRs). Official organizations, such as the WTO, the World Health Organization, the World Bank, and UNCTAD (UN Conference on Trade and Development), now devote increasing resources to conceptualizing IPRs as a development issue.

TRIPS raises a number of controversies, ranging from concerns over costs and availability of medicines, agricultural chemicals, new seed varieties, and software, to the implications of asserting private ownership rights over life forms, genetic resources, and biotechnological inventions. For such reasons, there are numerous proposals to scale back, alter, or clarify the provisions of TRIPS.

At the same time, developing countries wonder if there might be gains

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- through continuous negotiations it exerts constant pressure to open services to foreign commercial providers;
- the GATS MFN rule helps consolidate commercialization;
- the GATS monopoly provisions make it more difficult for governments to maintain public services by hamstringing their ability to compete;
- where GATS commitments are made, the GATS restricts the ability of governments to restore, revitalize or expand public services; and
- in such cases, compensation must be negotiated or retaliatory sanctions faced.

Similarly, the GATS does not *eliminate* governments' ability to regulate, however,

- the recognition of the right to regulate in the preamble has little legal effect;
- the GATS clearly applies to government regulatory measures, whatever their form or purpose;
- the GATS applies a very tough test of non-discrimination when considering the possible adverse effects of domestic governmental measures on foreigners;
- the GATS prohibits certain types of measures, whether they are discriminatory or not; and
- negotiations to apply a necessity test to non-discriminatory domestic regulation pose a very serious threat to crucial regulatory instruments.

Apparently, the GATS strongest proponents would prefer to keep these threats out of public view. But they are unlikely to succeed in this. The negotiations to broaden and deepen GATS coverage will make services one of the centrepieces of the new round of WTO negotiations launched recently in Doha. The existing GATS and the negotiation to expand it raise such serious challenges to democratic governance that they are certain to stimulate even greater public interest and controversy.

With only modest effort, non-governmental organizations, elected officials, and ordinary citizens are more than capable of understanding the GATS and its critical implications for public policy. When they do, they are likely to react with disapproval at how far this, nominally, *trade* agreement intrudes into the crucial regulatory prerogatives of democratic *governance*. Hopefully, this will result in greater public mobilization to bring citizens' considerable influence to bear on their respective governments, both to change the nature of GATS negotiations now underway in Geneva and to chart a more balanced future for the multilateral system.