Chapter 5

Preparing for the year 2000

Members have agreed, in Article XIX, to resume liberalization negotiations on trade in services by 1January 2000. These negotiations will be launched during the Seattle Ministerial Conference.

Since the conclusion of the Uruguay Round, the rapid changes in information technology and telecommunications have resulted in a virtually borderless global economy in which any service that can be digitized and transmitted electronically can be produced and delivered anywhere in the world. Electronic commerce's potential as the great equalizer will influence the new round as it begins.

Building on the progress made

In preparation for a new round of negotiations, several preliminary tasks have already begun:

- *The Exchange of Information Programme.* GATS negotiators need to be familiar with the way in which different services industries operate and how various services are traded, and not only with negotiating rules and principles. The WTO Secretariat has been preparing a series of background sectoral papers in order to stimulate policy thinking, as well as to facilitate the ongoing exchange of information on regulatory environments in member countries.

- *Assessment of trade.* Members naturally want to know what effect liberalization commitments have had in increasing trade in services, changing laws and regulations that impede trade in services, and promoting the growth of developing countries. The continuing lack of accurate services statistics is an obstacle to doing this effectively.

- *Guidelines for future negotiations.* WTO has started to prepare suggestions on the negotiating structure and procedures, including objectives for the next round with particular reference to securing benefits for developing and transition countries.

- *Committee on Specific Commitments.* This committee is examining options for modifying the schedule of commitments in a number of ways, including:

  - Ensuring a better match between the Central Product Classification (CPC) system used by statistical agencies, the list of services used by the WTO Secretariat for scheduling commitments, and the way in which Members describe their services in their schedules.

  - Re-examining the way in which new services are defined.

  - Determining a way to consolidate and update the schedules electronically.

Issues for the next round

For the next round, there is already a rather full list of potential agenda items:

- *Completing the outstanding work programme.* Several issues that were to have been resolved remain outstanding and create a built-in agenda, such as:

  - *Maritime transportation.* Negotiations that were to have been concluded by 1996 stalled in 1995 and have been postponed until the new round.

- *Professional services.* While guidelines have been developed for the transparent regulation of accountancy, they fall short of what the accountancy profession and WTO had hoped for. A decision will need to be taken on how to move forward on disciplines for domestic regulation, including whether to continue on a sectoral basis or to revert to a horizontal approach in order to address the matter to the satisfaction of the private sector, industry regulators and trade negotiators alike.

- *Ongoing issues.* Work has been underway on emergency safeguards, subsidies and government procurement. The status of the discussions on each issue is described in greater detail further below.

❑ *Consolidating and advancing the liberalization process.* GATS is the first multilateral undertaking on trade in services, and much has been learned since its signing. To achieve its main purpose of placing disciplines on governments so that they cannot act in an arbitrary or discriminatory manner, there are several types of discussions that need to occur:

- *Completing the initial sectoral scheduling.* The schedules originally filed by Members are far from complete. Even if a number of limitations are listed, it would be a major advance to have all services scheduled by all Members and hence subject to transparency. One of the challenges in broadening the coverage will be to determine how to liberalize sectors like energy or postal services that have traditionally been subject to monopoly or exclusive rights.

- *Strengthening the scheduling process.* Without changing the architecture of the schedules, there are several possible improvements to be considered: harmonizing regulations at the federal and subfederal levels; withdrawing MFN exemptions, at least for developed economies; and developing a competition code.

There has also been some discussion of making national treatment a general rather than a sector-specific obligation.

- *Further liberalization in financial services and telecommunications.* It seems likely that Members will want to register the advances they have made in liberalizing these two traditionally heavily regulated sectors, if only to increase their attractiveness to investors.

- *Re-examining GATS and the issue of the movement of natural persons supplying services.* Many developing and transition countries were unaware during the Uruguay Round of how many of their services firms were already exporting. Instead, there developed a presumption that one of the few ways in which these countries export services is embodied in the movement of labour. As a result, Mode 4 has become for some synonymous with the movement of individuals seeking temporary employment abroad. This concerned both high-skill (e.g. doctors, nurses) and low-skill (e.g. construction workers) personnel. Strongly held feelings about the issuing of work permits to foreign workers have obscured the pressing issue of temporary business travel for the staff of services firms.

  Because many services are not produced until the customer has agreed to their purchase, potential customers typically want to meet the persons who will produce those services. This means that services exporters must be able to travel in order to develop business, not just in order to execute a given project. Services providers from many developing countries, however, face stringent visa requirements, often including the need to produce a letter of invitation in order to be given permission to enter the foreign country. Such requirements, varying as they do on a bilateral basis, clearly contradict the concepts of most-favoured-nation status and equitable market access.

For most developing and transition economies, the contribution of worker remittances to the balance of payments is substantially less than their foreign exchange earnings from 'other services' or tourism (*see* table 20). What has not entered the debate to date is the economic cost of barriers to visa-less business travel. At a conservative estimate, services firms from developing and transition countries average 12 hours of staff time for visa-related formalities for each business trip abroad. Reducing such opportunity costs (i.e. the costs that arise because of the lost opportunity for carrying out a potentially revenue-generating activity) could have substantial benefits for these countries.

Table 20 Developing countries: sources of foreign exchange earnings, 1997

	Export earnings (US$ million)			Worker remittances as % of export earnings from:	
	Travel	Other services	Worker remittances	Travel	Other services
Africa	9 138	4 300	6 410	70.1	149.1
Asia	61 285	103 400	20 929	34.2	20.2
Europe	32 533	26 493	5 521	17.0	20.8
Middle East	9 330	17 610	6 560	70.3	37.3
Americas	25 213	13 583	9 748	38.7	71.8

Source: Calculated from IMF balance-of-payments data.

By not reaching a clear agreement on temporary business travel, developing countries have handicapped their services exporters in a critical way. In order to move this issue forward, government officials responsible for immigration policy would need to be included at the negotiating table. Further, those officials would need to be willing to shift focus from screening access to their own economies to facilitating access by their citizens to foreign markets.

– *Continued requests and offers.* In the new round, there will be the usual requests and offers to secure further liberalization of each other's schedules. Developing and transition countries will do well to bear in mind the commitment of developed Members to make concessions in the services sectors and modes of trade of greatest interest to them.

- *Addressing structural issues*. In addition to the definitional and administrative issues already under discussion in the Committee on Specific Commitments, there are more fundamental factors to be considered. The private sector has complained that the schedules are cumbersome to use and that the modal approach does not reflect commercial reality (where firms often use all four modes in their design and delivery of services). To be competitive, services firms must be able to select strategically among all four modes if they are to increase market share.

  Further, the distinctions allowed in the degree of liberalization among sectors create problems for private firms which operate in a more integrated environment. To capitalize on market opportunities, there often needs to be collaboration and cooperation among sectors as what is possible in one sector can significantly constrain what is possible in another sector. For example, while cross-border delivery of health services (tele-health) is technically feasible and well received by consumers, restrictions on insurance payments for out-of-jurisdiction health care can drastically reduce the viability of such trade.

  While the objections raised are cogent, the present structure does at least have the virtue of familiarity. From a practical perspective, negotiators may find it more constructive to press for full scheduling and the withdrawal of limitations on market access or national treatment than to spend time on the architecture of the schedules itself.

- *Addressing new substantive issues.* In addition to the outstanding work from the Uruguay Round, there are several new issues that cannot be ignored. At a minimum, these are likely to include:

- *Civil aviation.* Aviation is a service that has been negotiated largely bilaterally in the past on the basis of the Chicago Convention 'freedoms'. There is already evidence that open-skies policies have expanded the number of airline carriers to a given destination and have also led to an increase in tourism and business travel to the markets following such policies. At present, GATS covers only equipment repair, ticketing and sales, and computer reservation systems. At a minimum, charter airlines and air cargo companies want to begin a discussion on multilateral disciplines. Hopefully, there can also be a full discussion of landing rights for commercial airlines.

- *Electronic commerce.* The maturing of the Internet has raised a range of issues affecting trade in services. It remains to be seen how effectively the use of the Internet, as an infrastructure through which goods and services are marketed and delivered, can be regulated within the current GATS context. A more detailed examination of this issue is given further below.

- *Trade and competition policy.* The matter of competition policy is one of interest to the General Council, not just to the Council on Trade in Services. The guidelines in the *Reference Paper* on telecommunications have provided a starting point for such discussion (*see* Appendix IV to this Guide).

Ongoing issues

At the conclusion of the Uruguay Round, there were several outstanding issues on which Members agreed to undertake further work: subsidies, emergency safeguards and government procurement practices. All three remain have unresolved; however, negotiations are underway and will run on into the new round.

Subsidies

A transition economy has been reviewing the incentives it offers to the offshore data companies established in its export processing zone. It is wondering whether these incentives would be considered trade-distorting subsidies and thus come under GATS discipline.

Subsidies are financial contributions by a government or any public body within the territory of a Member or any form of income or price support which confer a benefit (i.e. lower operating costs). As a matter of course, governments often provide subsidies in specific sectors – e.g. utilities, transportation, financial services, health, education, and cultural or entertainment industries. Governments may also allow or encourage cross-subsidization among different services or types of consumers. GATS is concerned only with trade-distorting subsidies (Article XV) that are specific – i.e. that are provided to an enterprise or industry or group of enterprises or industries.

While there is a WTO Agreement on Subsidies and Countervailing Measures, that Agreement has been developed for the goods trade. A number of challenges arise in trying to set for services the boundaries of what is or is not trade-distorting. To help with the ongoing discussion, four general types of subsidies have been identified, each of which has its own definitional challenges and could have trade-distorting effects:

- *Production subsidies*. Subsidization of production costs for one mode of supply generally results in distortion from one mode to another. For example, subsidizing domestic producers of certain services (e.g. education) could result in domestic consumers taking advantage of local education rather than importing education services from another Member through Mode 2. In this case, the injured party could potentially be any other Member that exports education services through Mode 2.

- *Investment subsidies.* Since such subsidies apply only to Mode 3 (commercial presence), the foreign entities being subsidized could be more cost competitive than domestic suppliers of the same service. If a Member has committed itself to providing national treatment in the sector, then the injured party would be the domestic providers (as well as any foreign investors who did not receive the subsidy).

- *Export subsidies.* Subsidies that are contingent on export performance would qualify as export subsidies. If a Member has committed itself to providing national treatment but restricted the export subsidy to national exporters, the injured party would be foreign services suppliers with affiliates (commercial presence) in its territory which engage in export activities.

- *Consumption subsidies.* Subsidies contingent upon purchasing from a national source (i.e. partial or complete health-care costs underwritten by the government) are classified as consumption subsidies. If a Member has made a commitment in regard to national treatment, then the injured party would be foreign services suppliers active in its territory which also supply the subsidized service.

The rationale for subsidies is usually that of advancing social objectives such as local capacity building, regional development, providing equitable access to basic services, protection of the cultural heritage, or ensuring the viability of infrastructure services. In the example above, although the foreign firms are exporters and do not compete in the domestic market, such subsidies would serve as an export subsidy to these firms and could limit the export potential of domestic firms.

Even though the definitional issues have not yet been resolved, any subsidies that alter the conditions of competition in favour of either domestic or foreign firms could be in violation of national treatment obligations (unless the limitation is scheduled).

Emergency safeguards

A resource management firm from the Middle East with offices in an Asian country has been reviewing the measures taken by that country's government in the face of its financial crisis.

Emergency safeguards refer to temporary measures that Members may take to limit market access (i.e. suspend their scheduled commitments) in cases of market disruption. Article X of GATS provided for multilateral negotiations on disciplines for emergency safeguards to be completed by the end of 1997 and to come into force no later than the beginning of 1998. However, agreement has not yet been reached.

Members already have two mechanisms under Article XII with which to address serious balance-of-payments problems: restricting the extent of commitments, and restricting trade-related payments, transfers and capital movements. Such actions must be temporary, not excessive, non-discriminatory and avoid unnecessary damage to other Members. If a Member does invoke such a restriction, the WTO General Council must be notified. In the example above, the foreign exchange crisis faced by the Asian government would qualify as a circumstance under which suspending commitments could apply.

The challenge in developing disciplines on safeguards is to define what constitutes an injury (e.g. a decline in domestic share?). Among the issues are whether or not all modes of supply should be included, and whether safeguards are needed at all since the scheduling of commitments is so flexible.

Government procurement practices

An accounting firm from the Republic of Korea would like to be able to bid for audit contracts with major government-owned enterprises in Japan and is wondering if it can be excluded from bidding under GATS.

Governments are major purchasers of services. If government contracts are not open to services suppliers from other Members, the impact on trade in services could be considerable. At present, GATS does not apply to government procurement practices; however, there does exist a renegotiated Agreement on Government Procurement signed mainly by developed countries and a handful of developing countries/territories. The Agreement calls for transparency and non-discrimination in both the calls for tender and the award process, and operates on the basis of reciprocity. The Agreement uses the WTO dispute settlement mechanism and prohibits cross-retaliation between the Agreement and GATS. In the example given above, since both the Republic of Korea and Japan are signatories to the Agreement, it is likely that the Republic of Korea firm could bid for the audit contracts. Further negotiations to improve the Agreement and achieve better coverage on the basis of mutual reciprocity have been scheduled to begin in 1999.

Links with the Agreements on TRIPS and TRIMs

The Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) provides minimum standards for the protection of intellectual property rights as well as the procedures and remedies for their enforcement. Built on the existing relevant international conventions (e.g. the Berne Convention), its provisions apply to patents, copyright and related rights, trademarks, industrial designs, layout designs of integrated circuits, undisclosed information, and geographical indications. The Agreement on TRIPS should have a harmonizing effect on standards for intellectual property rights among Members. The Agreement provides for a transition period of five years (i.e. up to January 2000) for developing countries to bring their IPR legislation into conformance with the provisions of the Agreement, with the period extended to 11years (i.e. to January 2006) for least developed countries. The Agreement on

TRIPS is administered by the WTO's Council for TRIPS; a review of the Agreement is scheduled to begin on 1 January 2000.

A critical feature of globalization is the complementary activities of trade and investment, with at least half of FDI flows being in the services industries. Mode 3 under GATS already covers the terms and conditions on which a foreign investor may enter a market and the conditions under which its commercial establishment may operate. The Agreement on Trade-Related Investment Measures (TRIMs) prohibits certain types of requirements imposed on investors, namely local content and trade-balancing requirements. If such requirements exist, signatories are to phase them out by 2000. The operation of the Agreement on TRIMs is to be reviewed by the year 2000; the review will also consider whether or not provisions on investment policy and competition policy should be included in the Agreement.

Services statistics

It has been clear since early in the Uruguay Round that officially published statistics do not provide an accurate picture of the services being traded. Efforts to improve services statistics continue, with discussion covering the following issues:

- *Classification.* Since domestic regulations play such a large role in facilitating or limiting access to markets, comparable domestic services data are as important as accurate and comparable trade statistics. The United Nations Statistical Division has led the development of a provisional Central Product Classification (CPC) system for national accounts; however, there remain unresolved issues both in the grouping and enumeration of service activities and in the distinction between services industries and service commodities. Services suppliers in a particular industry (e.g. accountancy) may well produce several different kinds of services (e.g. accounting, auditing, computer systems consultation, management consulting). On the trade statistics side, the International Monetary Fund has issued the fifth edition of its *Balance of Payments Manual*, which provides for greater detail in disaggregating traded services, especially 'other services'.

In order for any classification system to be useful, it must be used consistently by all parties. At present, there are inconsistencies between CPC (the classification system used in GATS) and the classifications used by Members in their schedules. All Members should be required to use a common classification system such as CPC.

- *Linking trade statistics to modes of supply.* Traditional methods of collecting trade statistics assume that products move across borders (Mode 1). The services trade is underestimated as there are no mechanisms for measuring trade volumes in the other modes of supply, and even in Mode 1 the electronic transfer of services is not well captured. In regard to Mode 3, the United States has estimated that affiliate services trade may be equivalent to at least 84% of the cross-border services trade of parent companies (*see* table 21).

- *Capturing 'other services'.* Although the highest trade growth is occurring in 'other services', only the transportation and travel accounts typically have adequate data collection methodologies. OECD has estimated that the growing discrepancy between global services exports and imports is due in large part to an under-reporting of exports of 'other services' by as much as 40%. As an example of services not being correctly captured, the United States has estimated that at least 9% of reported goods trade actually consists of embedded services (such as maintenance and training contracts, financing).

- *Bilateral trade flows.* In order to study the effects of market opening and determine the importance of various export markets, data on bilateral trade flows are essential. At present, there are few publicly available statistics on bilateral services trade. Where they exist, they are typically disaggregated only for the highest-volume markets.

Table 21 United States: exports of selected services, 1994 (in millions of United States dollars)

Services	Exports		MOFA as % of BOP
	BOP a/	MOFA b/	
Accounting/management	1 792	5 678	316.9
Computer services	3 837	16 714	435.6
Insurance	4 944	30 941	625.8
Total commercial services	182 704	153 541	84.0

Source: Coalition of Service Industries, United States.

a/ Exports by firms established in the United States whose exports are reported in the balance of payments (BOP).
b/ Majority-owned foreign affiliates (MOFA) of United States companies located outside the United States.

Electronic commerce

The newest structural change affecting services exporters is the explosion in Internet use, with the number of Internet users said to be doubling every year. In contrast to the 4.5 million Internet users in 1991, WTO estimates that there will be as many as 300 million by the end of 1999. Encryption technologies have advanced sufficiently for sales to take place electronically, though electronic commerce is most likely to be used for services viewed as low risk. Estimates indicate that at least US$ 18 billion in sales is already taking place via the Internet, with 2002 estimates placed at US$ 330 billion.

Although already over 10% of all consumer shopping is taking place electronically, business-to-business transactions on the Internet are 10 times the volume of consumer purchases. Web site researchers report that the majority of site visitors are looking for information to help with a purchase decision, or to comparison shop, rather than wanting to purchase electronically. But there are already firms whose sales over the Internet exceed a billion dollars a year. Countries with a telecommunications infrastructure that is open to competition have five times the number of Internet hosts and less than half the connection charges than countries whose infrastructures are closed to competition.

Electronic commerce may radically alter industry structures, eliminating the need for distributors, wholesalers and even retailers in some instances. For financial and telecommunications services in particular, there are likely to be dramatic consequences. Many financial transactions are already being done on-line, making intermediary personnel redundant. Internet telephony is already a reality, providing international telephone and fax services at the cost of a local call (owing to better use of bandwidth). Electronic commerce will also make the tracking of international trade infinitely more difficult, and has led to proposals such as a tax-free zone for electronic commerce.

For countries without Internet access, priority attention to going on-line can make the difference between operating from a level playing field and being marginalized. The Internet provides a low-cost, highly efficient way to approach potential customers worldwide, in support of which the UNCTAD GTPNet (Global Trade Point Net) is gradually being transformed from a pre-transactional electronic trading network to a transactional tool for electronic commerce.

The second WTO Ministerial Conference adopted a Declaration on Global Electronic Commerce "to establish a comprehensive work programme to examine all trade-related issues relating to global electronic commerce, taking into account the economic, financial, and development needs of developing countries." The Council for Trade in Services was directed to report on the treatment of electronic commerce in the GATS legal framework by July 1999, addressing the following issues: scope (including modes of supply); MFN treatment; transparency; increasing the participation of developing countries; domestic regulation, standards and recognition; competition; protection of privacy and public morals and the prevention of fraud; market-access commitments on the electronic supply of services (including basic and value-added telecommunications); national treatment; access to and use of public telecommunications networks and services; customs duties; and classification issues.

The emerging use of the Internet for telephony is an illustration of some of the challenges lying ahead for GATS.