

## **Towards a More Balanced and Comprehensive Services Agreement\***

Bernard Hoekman  
World Bank and CEPR

November 3, 1999

\* A preliminary draft of this paper was presented at the conference Preparing for the Seattle Ministerial, Institute for International Economics, Washington DC, October 26, 1999. I am grateful to Patrick Messerlin, Jeff Schott, Sherry Stephenson and Jayashree Watal for helpful comments and discussions. The views expressed in this paper are personal and should not be attributed to the World Bank

## **Introduction**

The establishment of a General Agreement on Trade in Services (GATS) was one of the major outcomes of the Uruguay Round. The GATS broke new ground in a number of areas. Not only did it cover measures affecting trade in services—a product group that was mostly not subject to the General Agreement on Tariffs and Trade (GATT)—but it defined trade in a novel way. Trade under the GATS includes not just cross border exchange, but also sales by affiliates of foreign companies that have established a long-term commercial presence in a host country, purchases of services made by non-residents who have moved to the location of their provider, and the sale of services by natural persons made possible by a temporary presence in a host country. The potential reach of the GATS therefore extends beyond that of the GATT, which deals only with cross border trade in merchandise. One consequence of this broader domain was that governments insisted on being able to maintain national derogations and limitations on the reach of multilateral disciplines. A rather complicated scheduling technology was adopted—each WTO member may list exceptions to the national treatment principle or market access for individual service sectors for any or all of the four modes of supply through which trade can occur. They may also refrain from making any commitment for specific services.

During the Uruguay Round negotiations on services most attention centered on conceptual and “architectural” issues—how to define trade, what rules and principles should apply to measures affecting this trade, and devising mechanisms to determine the coverage of the agreement. What was created was a framework under which

liberalization could be pursued in the future.<sup>1</sup> Article XIX GATS calls on members to engage in negotiations to liberalize trade in services five years after the entry into force of the agreement, and periodically thereafter. New negotiations on services therefore are to commence in 2000.

This paper discusses the agenda of the services talks, taking an economic and systemic perspective. Three broad topics are discussed: (i) modalities for expanding the coverage and increasing the relevance of the GATS; (ii) achieving reciprocity—attaining a balance “concessions” made by participants; and (iii) improving the multilateral rules of the game that are embodied in the GATS. The premise is that the GATS must become more balanced in terms of the magnitude and distribution of the benefits of the agreement for different groups of countries. This will require a more comprehensive coverage of sectors and modes of supply. Achieving a substantial expansion in the coverage of the GATS is of great importance not only in its own right but also to ensure that multilateral negotiations more generally will be successful. In the run-up to the Seattle Ministerial it has become clear that many developing countries are of the view that the costs of implementing Uruguay Round agreements in various areas—e.g., TRIPs, customs valuation—were much greater than was realized when these agreements were signed (Finger and Schuler, 1999). Moreover, the benefits from market access agreements in other areas of importance to developing countries are perceived to be disappointing due to continued use of highly distorting policies in major markets (agriculture), and/or the back loaded nature of the liberalization process (textiles and clothing). The services negotiations offer the opportunity for significant market access gains for developing

---

<sup>1</sup> See Hoekman (1996) for a description and assessment of the GATS.

countries, while at the same time improving the regulatory environment for services and the efficiency of domestic industries.

The major challenge confronting negotiators is to create incentives for developing countries to expand their commitments under the GATS. Given ongoing efforts in many countries to adopt a more market and pro-competitive policy stance, the focus of attention can be expected to center on increasing the extent to which both the status quo and future (autonomous) reforms are scheduled in the GATS. This depends importantly on the value that is placed on such scheduling by reforming economies themselves and the “demandeur” countries that want governments to lock-in reforms in the GATS.

Arguments by economists that the WTO can be used as a valuable credibility-bolstering device have proven to be less than compelling to policymakers (e.g., Francois, 1997). In practice, the mercantilist logic of multilateral negotiations is likely to require that industrialized countries improve export market access opportunities for developing countries. Absent such a quid pro quo it may prove difficult to greatly expand the coverage of the GATS in areas where the economic payoffs are highest—sectors where entry restrictions are most severe or the perceived probability of policy reversal is high.

## **1. The Status Quo**

The situation that prevails in the GATS is well known.<sup>2</sup> The sectoral coverage of the specific commitments (on national treatment and market access) is limited for many countries. The majority of country schedules list a variety of measures that continue to restrict or limit either market access or national treatment. As of the end of the Uruguay

---

<sup>2</sup> Feketekuty (1998) and Mattoo (1999b) discuss the status quo and the weaknesses of the GATS, and provide references to the rapidly expanding literature.

Round, high-income countries had made specific commitments on about half of their services, of which only one-half entailed “free access.” Thus, ignoring horizontal restrictions for modes of supply, only 25 percent of all service activities have no limitations on market access or national treatment. In the case of major developing countries, on average “free access” commitments were made for only 15 percent of the service sector; smaller countries generally do not attain even this low level (Hoekman, 1996). Subsequent to the Uruguay Round, successful negotiations on basic telecoms and financial services expanded the coverage of specific commitments.<sup>3</sup> These negotiations were important both for keeping momentum going and inducing the U.S. not to invoke an MFN exception. They were important from an economic perspective because the services involved are vital intermediate inputs.<sup>4</sup>

Not only is the coverage of specific commitments limited for many countries, in many cases the commitments are less liberal than the status quo policies that are actually applied. That is, many governments have refrained from binding the status quo. Examples in the financial services area are well documented, with a number of countries scheduling foreign ownership limits that are more restrictive than those currently enforced (Mattoo, 1999a). One interesting feature that was been remarked upon by a number of observers immediately following the Uruguay Round was that more commitments tended to be made with respect to FDI (“mode 3”) than cross-border trade (“mode 1”) (Hoekman, 1996). A number of countries’ commitments also favor infusions of foreign equity into existing firms and limit the ability of entry by new firms. Such

---

<sup>3</sup> Cowhey and Klimenko (1999) assess the telecom agreement; Mattoo (1999a) analyzes the financial services agreement.

<sup>4</sup> These agreements did not lead to a major expansion in the coverage of the GATS relative to the Hoekman (1996) assessment, as his compilation included commitments made as of 1994 for financial services.

protection of existing market structure is difficult to rationalize in economic terms, as it can easily result in a transfer of rents to foreign firms rather than a socially desirable increase in competition and lower prices/higher quality output.<sup>5</sup> Differences in the treatment of modes of supply have the potential to distort incentives to contest or service markets through the most cost-effective means available, and may impede the ability of suppliers to sell their services. This can be particularly important for e-commerce (Mann, 1999).

## **2. Expanding the Coverage of the GATS**

In principle, efforts to expand the coverage of the GATS should focus on those sectors and policies where reforms will have the highest payoff in terms of enhancing efficiency and bolstering economic growth potential. Doing so will be difficult. Available data on barriers and international services transactions remain substantially weaker and less complete than those for merchandise trade. The lack of data on the restrictiveness of current policies is particularly troublesome. Efforts undertaken during the last decade to improve trade statistics, including data on sales of services by local affiliates of foreign multinationals, have been successful in improving our knowledge of the flows involved, especially with respect to “foreign affiliate trade in services”—local sales achieved through establishment (Whichard, 1999). Data on trade flows are needed for analytical purposes. But much more important from an economic policy and negotiating perspective are data on the barriers that restrict international competition. Relatively little progress

---

<sup>5</sup> This is a phenomenon that occurs not infrequently. All other things equal, many foreign investors are unlikely to be averse to earning rents and limiting competition once established in a market. The pattern of commitments observed in the GATS has also characterized liberalization episodes that predate the GATS. See, e.g., Cho (1988), on the approach used by Korea to open access to the insurance market. For

has been achieved in compiling quantitative measures of the barriers restricting trade and investment flows that are comparable across sectors and across countries. Instead, the focus of attention largely remains sectoral, as was the case during the Uruguay Round.<sup>6</sup>

Some progress is beginning to be made in measuring the restrictiveness of services markets across countries and sectors, using frequency indicators of the prevalence of different types of measures, enterprise-level panel data and US bilateral trade flow data to generate estimates of tariff equivalents.<sup>7</sup> This work suggests that barriers to trade in services are higher than barriers to merchandise trade—although perhaps not as high as is sometimes thought; that the barriers in major “backbone” services such as transport, financial and telecom services are higher than in business or distribution services; and that barriers are higher in developing countries. A major problem affecting much of this work is that it is based on indirect indicators of openness of sectors or countries and does not rely on direct measures of specific policies. From a national perspective, especially for developing countries, greater efforts are needed to generate information on the level and effects of policies that restrict international competition.

Although the data situation remains far from ideal, seeking a more balanced and comprehensive coverage of services sectors and modes of supply is the most obvious

---

discussions of the economics of alternative instruments that are used to restrict access to service markets, see Hindley (1988) and Hoekman and Primo Braga (1997).

<sup>6</sup> The launching of the Uruguay Round services negotiations led to a spate of sector-specific research, much of which remains relevant. Examples were a series of monographs prepared for the American Enterprise Institute (see, e.g., Aronson and Cowhey, 1988; Kaspar, 1988; Walter, 1988 and White, 1988) and numerous papers commissioned by UNCTAD focusing on developing country interests—e.g., UNCTAD (1989). Since then the focus of attention has centered in particular on telecoms and financial services. For recent research output, see [www.worldbank.org/trade](http://www.worldbank.org/trade), [www.worldservicescongress.com](http://www.worldservicescongress.com), and [www.cid.harvard.edu/cidtrade](http://www.cid.harvard.edu/cidtrade).

<sup>7</sup> For recent work in this area see Findlay and Warren (1999) and Francois and Hoekman (1999). The former uses frequency indices to describe the status quo for a number of important sectors in countries for which data is available, and to assess the possible impact of liberalization. The latter use trade and financial

priority for negotiations. There is no a priori reason why national specific commitments should not cover *all* services and *all* modes of supply. Setting targets for expanded coverage to be achieved in the next round would help signal that governments are serious about strengthening the GATS, and provide a focal point for policy makers. Two types of targets or focal points can be envisaged, quantitative and qualitative.

Quantitative indicators that could be considered include: (i) sectoral coverage ratios—the “quantity” of national treatment and market access commitments; (ii) the degree of liberalization that has been achieved by WTO members, using some agreed characterization of the restrictiveness of applied policies; and/or (iii) the extent to which applied policies are bound in the GATS. From an economic and a market access (business) point of view what matters most is the restrictiveness of applied policy. In GATS negotiations, this has not been the primary focus of attention; however, perhaps in part because there is no simple metric that can be applied to determine the restrictiveness of the set of policy measures that apply to a sector. Instead, efforts have centered on inclusion of sectors in national schedules. This has led to situations where a country may be relatively liberal in terms of applying national treatment or limiting market access, but has not locked this in, i.e., either has not scheduled anything at all, or, if commitments are made, has not bound the status quo in the GATS.

In terms of designing possible quantitative focal points for GATS coverage in the next set of negotiations, it is very difficult to focus on the degree of liberalization that has been attained by countries. Doing so would require a *de facto* move to a negative list approach to scheduling, something that was rejected during the Uruguay Round, and agreement on a method to determine the level of intervention that is implied by policy

---

data to construct measures of openness across countries and sectors.

(analogous to the aggregate measure of support used in the GATT Agreement on Agriculture). In principle such measures could be developed, but it is very unlikely that agreement could be obtained from WTO members on the acceptability of any index. More practical focal points are the share of sectors that have been scheduled, and the share of commitments that involve a bound promise not to apply any national treatment of market access violating measures. These two indicators are objective in the sense that do not require any judgement regarding the importance of actual policies that restrict national treatment or market access, whether or not scheduled.

Various qualitative “formula” approaches can also be envisaged. One simple qualitative coverage target would be to prohibit specific commitments for sectors or modes of supply that do not convey information and do not constrain governments: the so-called ‘unbound’ commitments that some WTO members have included (see Hoekman, 1996). Another would be to extend the national treatment principle to all instances where a nation decides to make a commitment on mode 3 (commercial presence) for a sector.

A problem with a formula approach to expanding coverage is that sectors that are important inputs into production and sectors where the barriers to trade are currently highest may remain excluded. Inconsistent treatment of interdependent service activities may also result. Consequently, request-offer negotiations cannot and should not be avoided. Priority attention should be given to key “backbone” sectors such as transport, telecoms, and financial services, as well as clusters of interdependent services that are vital to economic development and participation in the world economy (e.g., multi-modal

transport and express courier services).<sup>8</sup> Increasing the efficiency of such service sectors will have major payoffs for developing countries in terms of lower prices, higher quality, and greater product differentiation.

From a mercantilist perspective, these backbone services are sectors where enterprises in industrialized countries can be expected to dominate the supply side. Traditional negotiating balance imperatives then requires that services and modes of supply where developing countries have an export interest also be put on the table. Without reciprocal concessions, developing countries are unlikely to want to bind the status quo or to use the GATS as a pre-commitment device for planned future reforms. Even though many countries have been and can be expected to continue undertaking domestic pro-competitive reforms in their services sectors, a major challenge for WTO members is to increase the incentives to bind these reforms. Despite the compelling economic arguments that can be made in favor of using international agreements as a vehicle to reduce investor uncertainty—the argument being that making binding commitments can signal a willingness on the part of governments to “lock-in” reforms—in practice negotiating dynamics often impede the use of agreements for this purpose. The situation that arises is similar to what occurred in the Uruguay Round, during which developing countries sought—rather unsuccessfully—to obtain “negotiating credit” for autonomous liberalization of import barriers that had been implemented in the period leading up to the launch of negotiations, as well as thereafter.

---

<sup>8</sup> As illustrated by recent theoretical research—Deardorff (1999) and Markusen, Rutherford and Tarr (1999)—there are strong reasons to believe that liberalization of such services deserve priority in the negotiations because they are crucial in terms of both increasing the gains from trade in goods and reducing the costs of international fragmentation of the value chain and production sharing.

Art. XIX:3 GATS requires that negotiations to expand the GATS include guidelines or modalities for the treatment of autonomous liberalization that has occurred in the period after the last multilateral round (in this case 1994). It is unclear what should be done in this connection, i.e., how “credit” should be defined, nor is it obvious that 1994-2000 is the appropriate base period given the discrepancy between applied policies and many country schedules (Fung and Stone, 1999). Credit that involves developing countries obtaining the right to “do less” than other countries is unlikely to be in their own interest. It appears more productive to think of credit in terms of the *quid pro quo* to be put on the table by high income countries and major middle income emerging markets in return for a significant increase in bindings by developing countries. Existing market access commitments by OECD countries, while much more comprehensive than those made by developing countries, are not of great export interest to many developing countries. Relevant in this connection is also Art. IV:3 GATS, which calls for special treatment of least developed countries—if taken seriously, this could involve an explicit focus on improving access to markets that are interest to such countries.

Potential tradeoffs (gains from trade in policies) within the ambit of the services negotiations can be identified relatively easily. For example, developing countries have an interest in seeking commitments in the area of national social and medical insurance regimes, to allow patients to undergo treatment abroad. Perhaps the most obvious “big” area for tradeoffs is liberalization of mode 4—temporary entry of service providers. Although undoubtedly highly sensitive, it is an area where incremental progress can be made, as one of the key instruments used to restrict trade through this mode are quotas (for visas). These can be expanded over time, with within quota visas not being subject to

economic needs tests, with liberalization facilitated by a mode 4-specific safeguard procedure (see below).<sup>9</sup> It is also an area where opposition within OECD countries is not monolithic—there are many industries that would benefit from a more liberal temporary access regime, and development of coalitions with such industries could help change the status quo.<sup>10</sup> Of course, at the end of the day a key factor determining the willingness of OECD countries to provide concessions in areas of interest to developing countries is the value that is attached to binding domestic reforms, be it on a sector-by-sector basis, or by mode of supply (e.g., agreeing to national treatment for mode 3).

### **3. Strengthening and Simplifying the Rules**

The primary disciplines embodied in the GATS are MFN, market access and national treatment. The latter two apply only on a sector-mode basis, and are subject to exceptions: governments may schedule (grandfather) measures that are inconsistent with either principle. The distinction between national treatment and market access is not clear cut, as some market access exceptions also violate national treatment. Removing such inconsistencies would clarify what a country is committed to (Feketekuty, 1998).

The current approach to scheduling distinguishes between the four modes of supply that define trade. As a result, national schedules may distort incentives to use the most efficient mode, while also creating uncertainty what rules prevail in instances where more than one mode is used to service a market. Such uncertainty can also impede dispute settlement. It creates difficulties in predicting how a panel will interpret the

---

<sup>9</sup> For detailed proposals by developing country scholars in this area, see Mukherjee (1999) and Chanda (1999).

<sup>10</sup> Liberalization of mode 4 is not solely a North-South issue. Hodge (1999) notes that South African firms frequently run into human capital constraints and have an interest in enhancing their ability to rely on

schedules, and thus reduces the perceived benefits from initiating dispute settlement procedures. One way to reduce potential inconsistencies in commitments across modes within a specific sector is to require one-to-one mappings between commitments on modes (“non-discrimination across modes”).<sup>11</sup> Such a technological neutrality principle was embodied in Agreement on Basic Telecommunications. Modal neutrality is an objective worth pursuing because, as is often emphasized in the literature, trade and investment have increasingly become complementary. It is also frequently noted that it will become more difficult to maintain a clear distinction between trade in goods and trade in services, as technology may give producers the choice of delivering their products in tangible or in disembodied (digitized) form. A priori, it would appear that any multilateral disciplines should apply equally to international transactions regardless of the mode of supply. The rapid growth in e-commerce illustrates the danger of mode-specific disciplines, as it is unclear whether transactions should be defined under modes 1 or 2 (Barfield and Groombridge, 1999; Mann, 1999).

There are some fundamental “architectural” issues here. For example, a case can be made that WTO members should consider developing disciplines that distinguish between trade and investment, with trade in goods or services being subject to a set of common rules, and movement of factors of production being subject to another set of rules. This in effect has been the approach taken in the NAFTA, which includes a separate chapter on investment (in goods or services), which is distinct from the rules relating to cross-border trade (in goods and services). This approach results in much greater consistency and clarity of the applicable rules and disciplines than the current

---

temporary service providers.

<sup>11</sup> See, e.g., Hoekman (1996), Feketekuty (1998), Mann (1999) and Mattoo (1999b).

WTO structure. These are longer run questions that must be addressed at some point. For the time being, within the GATS setting a focus on modal neutrality can be a useful halfway house.

Efforts to attain greater neutrality could be complemented by efforts to expand the ambit of horizontal, pro-competitive principles, that apply to all sectors. This would help make the GATS both more transparent and more relevant to investors, by allowing negotiating efforts to center more on developing disciplines that make sense from a long-term growth and economic development perspective. As far as network services are concerned a start was made in this direction in the Agreement on Basic Telecommunications, which included the development of a so-called “Reference Paper” on regulatory principles in telecoms. The Reference Paper includes concepts such as “affecting the terms of participation” and “essential facilities” which could usefully be extended to all network services, even those without any background of monopoly or public ownership or control.

Care must be taken to avoid attempts at imposing a one size fits all approach to pro-competitive regulatory principles, as different service sectors will in general have different requirements and characteristics. Countries may also differ in terms of the weight that is accorded to competition policy (antitrust law) compared to direct regulatory oversight by specialized regulatory agencies. As is the case with competition law, harmonization across countries is unlikely to be first best, and any disciplines, whether sector-specific or horizontal, should be limited to procedural norms that aim at increasing transparency and accountability of regulations and regulators. One dimension that is particularly important in this connection concerns multi-jurisdictional situations,

where central and local governments share responsibility for enforcing regulatory regimes. Quite frequently, the “action” occurs at the state or provincial level, implying that local regulators must be involved in the development and implementation of procedural rules at the WTO level. Improving communications and dialogue between the trade and regulatory policy communities *within* countries, and between regulators *across* countries are preconditions for achieving progress in this area.<sup>12</sup>

Similar caution should apply to efforts to “regulate domestic regulation” in sectors where access to a network is not at issue. It has been proposed that one way to address domestic regulation is to adopt a “necessity test”—putting the burden of proof on governments to show that a particular regulation that has detrimental effects on foreign providers is necessary to achieve an objective (Mattoo, 1999b). Although this has proven a powerful pro-competitive instrument in the EU context, it likely to be much more difficult to apply in the WTO, given the much lower integration ambitions that prevail among WTO members and the substantially weaker institutions that will be asked to rule on claims that a regulation is not necessary. Attention could more productively focus in the next round on expanding the reach of the national treatment and market access principles.

One area deserving attention in the next round is strengthening the reach of MFN. In the Uruguay Round countries were permitted to schedule MFN exemptions, in part reflecting a concern by regulators that MFN might impede their ability to intervene, or a desire by governments to discriminate on a sectoral basis (e.g., culture). Existing provisions in the GATS already give regulators the ability to pursue actions that discriminate across firms to achieve regulatory objectives, and provide scope for entering

---

<sup>12</sup> Improved communication and “understanding” between trade and competition authorities was arguably the primary positive result of the working group on trade and competition policy that was created at the

into regional economic integration agreements. Now that some experience has been obtained with the GATS, negotiations should seek to abolish the grandfathering of policies that allow countries to discriminate against certain WTO members. Efforts should also be made to ensure that MFN applies in the area of standards and mutual recognition, with non-recognition being made easier to contest through dispute settlement. Multilateral cooperation may be required to mitigate the competition-reducing effect of domestic regulations, especially in the area of mandatory standards—for product safety, professional certification, prudential regulation, etc. All WTO members should be treated equally in terms of having access to mechanisms that are created by countries to achieve mutual recognition. Ensuring that initiatives to achieve “deeper integration” among subsets of WTO members do not result in *de facto* discrimination in areas where this is not inherent in the design of such agreements is an important area for future rule-making efforts.

#### *Outstanding Issues: Subsidies, Procurement and Safeguards*

A number of “outstanding” rule-making issues were left open after the Uruguay Round for further work and discussion: subsidies, procurement and safeguards. The economic case for GATS-specific disciplines in any of these areas is weak. There is nothing services-specific about procurement: any multilateral disciplines should cover goods and services. Of primary importance for foreign firms is to have access to procurement markets, and frequently this can only be achieved if they have a commercial presence in a country. What matters in economic welfare terms is therefore not so much policies of discrimination, but the ability of foreign firms to establish. If the sectoral

---

1996 WTO Ministerial meeting.

coverage of the GATS is expanded and foreign providers become able to access markets, the contestability of procurement markets will be enhanced at the same time, independent of whatever discriminatory policies are in place (Evenett and Hoekman, 1999).<sup>13</sup>

Multilateral disciplines on subsidies might help avoid mutually destructive policies from the viewpoint of developing countries—e.g., seeking to attract FDI via the use of incentives—and eliminate important sources of distortion in OECD markets for some services and modes (e.g., FDI incentives designed to divert investment away from developing countries, or operating subsidies for transportation activities). In the services context any disciplines will have to focus primarily on domestic production or operating subsidies—the distinction between export and production subsidies found in the GATT is much harder, if not impossible, to make in practice. It is also much harder to envisage emulation of the main GATT discipline—countervailing duties—increasing the need to agree to substantive rules (harmonization). Difficulties will immediately arise in distinguishing between what is “legitimate” and what is not. While there are clearly potential sources of gain for WTO members associated with a set of subsidy disciplines, subsidies will frequently be the most efficient instrument to pursue non-economic objectives—e.g., to ensure universal service; promote regional development; offset income inequalities; and so forth. Cross-subsidies of the type that are often regarded as inefficient and nontransparent mechanisms to achieve an objective may sometimes be the best available second best instruments for developing country governments.<sup>14</sup>

---

<sup>13</sup> It should be noted this is not the majority view, which focuses more on market access opportunities and not on the welfare effects of procurement policies.

<sup>14</sup> See Joskow (1998) and Laffont (1998) for general discussions of these issues from a developing country perspective.

The GATT/WTO negotiating and implementation history illustrates that agreement on subsidy and related disciplines is difficult to obtain, and that any disciplines may easily be circumvented. Even the EU—which goes much further than the WTO in this area—has encountered recurrent difficulties associated with government policies intended to attract FDI and enforcing its restrictions on the use of State aids. NAFTA does not even try to tackle this issue. Given the rationale for subsidies in many contexts and the revealed preference of many governments to use subsidies, it would appear more effective to seek to extend the reach of the national treatment principle to subsidy policies, especially when the subsidy is aimed at firms that have established a commercial presence (FDI). Given national treatment, there should be less concern about the impact of subsidy policies, allowing the principle of “subsidy freedom” to prevail. As in the procurement case, what matters most is market access and national treatment.<sup>15</sup>

The economic case for safeguards instruments is also weak. Insofar as governments are under pressure to (re-)impose protection (discrimination), they already have the opportunity to invoke the re-negotiation modalities that are built into the GATS. GATT-type safeguards (emergency protection) is difficult to rationalize in the services context because in many cases it will require taking action against foreign firms that have established a commercial presence (Hoekman, 1993). Why a government would want to do this is unclear, as it can have a major chilling effect on FDI, and will affect negatively the national employees of the targeted foreign-owned firms. If safeguards are to be considered, it would therefore most likely exempt mode 3. But then it must be considered

---

<sup>15</sup> There are other problems that arise in contemplating subsidy rules in the GATS. Given that much of the action relates to investment incentives and analogous measures, it can again be asked what is services-specific here. Any disciplines that are regarded as beneficial should presumably also apply to investment in manufacturing, mining or agriculture. It seems inappropriate to pursue multilateral disciplines in the GATS,

that any safeguards instrument that exempts mode 3 can easily act to induce investment, rather than trade (mode 1), thus distorting incentives (leading away from the modal neutrality objective).

There is, however, one potentially compelling argument for seeking to develop a safeguard instrument. A case could be made that the extremely limited nature of liberalization commitments to date on movement of service providers (mode 4) is in part due to the non-existence of safeguards instruments. As this is a mode of supply that is of major interest to developing countries and one on which almost all countries maintain stringent restrictions, one could envisage a safeguard instrument that is limited to mode 4 liberalization commitments, and is explicitly aimed at providing OECD country governments with an insurance mechanism that can be invoked if liberalization has unexpected detrimental impacts on their societies.

#### **4. Achieving Greater Transparency**

It is widely recognized that the “scheduling technology” used in the GATS does not greatly promote transparency. A fundamental need is to improve the available information on status quo policies. This will facilitate national reform efforts and help identify where the multilateral process can support such efforts. Unfortunately, there is nothing in the GATS or the WTO that encourages and assists countries in generating comprehensive information on applied policies and evaluating the impact of these policies. Some progress was made in the Uruguay Round with the creation of the Trade Policy Review Mechanism, but more can and should be done. Priority should be given to

---

as opposed to a more general set of investment-related disciplines, if there is a consensus that the issue is important enough to attempt rule-making.

greatly improving statistics and data on trade barriers and entry-cum-operating restrictions in services. Analogous to the role played by the OECD Secretariat in compiling information on agricultural policies in the 1980s, international organizations and multinational business should devote the resources required to document the status quo and to put this information in the public domain.

The importance of strengthening capacity to collect and analyze information cannot be over emphasized. A common mistake made by governments involved in regulatory reform is to reduce the ability of agencies to compile the information needed to monitor the impact of reforms. Better information on status quo policies, their effects, and the impact of GATS-based liberalization agreements will assist governments make policy and provide stakeholders (business, civil society) with the information needed to engage in the domestic policy formation process.<sup>16</sup> The private sector—both the business community and NGOs—must play a prominent role in collection, dissemination and analysis of information on applied policies and their effects. The private sector also has a crucial role to play in the enforcement of multilateral obligations. Without active participation by business, WTO dispute settlement will have no relevance as an enforcement device (Hoekman and Mavroidis, 1999). Available information and data should be put into the public domain, including all statistics, databases and documentation on policy measures that is collected by the WTO. One option that deserves serious consideration in this connection is to resurrect an Australian proposal made at the 1996 WTO Ministerial meeting to engage in a negative list *reporting* exercise

---

<sup>16</sup> Analysis and research by developing country scholars is very important in this connection, in order to increase ownership and local capacity to develop negotiating positions. Examples of the type of work that is required is emerging—see, for example, Chadha (1999), Hodge (1998, 1999), Naude (1998), and Tohamy (1999).

of prevailing policies in services for transparency purposes. This should be accompanied with adequate technical and financial assistance to help developing countries, in particular least developed countries, participate in the transparency exercise.

## **5. Concluding Remarks**

Opposition by domestic firms to the prospect of increased competition from foreign firms may not be as strong in services as in goods. The political economy of services liberalization is different from goods: the gross negative impact on labor employed in services is likely to be lower (given that foreign entrants will often use mode 3 and employ mostly nationals), the net impact on labor more likely to be perceived to be positive (as total employment opportunities can be expected to expand),<sup>17</sup> and support for reform by businesses that would benefit from higher quality and lower-prices services more likely to be stronger.<sup>18</sup> Indeed, those that liberalize first may have a strategic advantage—creating further incentives to pursue domestic reforms. Narrow reciprocity, i.e., “equivalent” concessions being offered by trading partners, is therefore less of a priority for developing countries than was the case for merchandise trade liberalization by OECD countries (Hoekman and Messerlin, 1999). In order to benefit most from GATS talks, the multilateral process should be used to support the implementation of a national reform agenda that has been developed through domestic consultations.

There is widespread recognition among governments and civil society that pursuit of regulatory reforms in the services area can have very large payoffs. In this respect the political context going into the GATS 2000 talks is quite different from that prevailing in

---

<sup>17</sup> And not just for relatively unskilled labor—see Markusen, Rutherford and Tarr (1999).

<sup>18</sup> For recent numerical assessments of the gains from liberalization of trade in services see Chadha (1999),

1986 when the Uruguay Round was launched. Opposition to liberalization certainly does exist in developing countries, and countries differ regarding the desirable modalities and speed with which to pursue reforms. There are also valid concerns regarding the need to put in place the appropriate regulatory policies and strengthen regulatory institutions before certain types of liberalization are undertaken. But the thrust of policy in the majority of nations is towards a more market-oriented policy stance, as is reflected in widespread privatization of utilities, telecom operators, airlines, etc. The success of the financial and basic telecom sectoral talks was largely a reflection of the fact that most of the governments involved were convinced of the need to pursue regulatory reforms in these sectors, including liberalization and elimination of entry barriers. This was a precondition for the agreements to materialize—it was clear that the associated regulatory reforms did not go beyond what had already been accomplished or decided in the national (unilateral) context.

A key factor for the next round will be expanding the extent of “lock-in” of reforms through the GATS, as this remains quite limited for many countries. Ideally, the GATS should be regarded as a valuable instrument for anchoring expectations and pre-committing to a future reform path (Francois, 1997). In practice it is not used to this effect. Greater specific commitments and binding of applied policies is unlikely to emerge without a quid pro quo. The potential scope for tradeoffs in the GATS context is quite large, and there should be no need to rely on cross-issue linkages—although those can certainly be envisaged as well. An obvious linkage strategy *within* services would be a mode 3—mode 4 exchange, with developing countries making bound national

---

Dee and Hanslow(1999), Brown and Stern (1999), and Robinson, Wang and Martin (1999).

treatment and market access commitments on mode 3 across a wide range of sectors, in return for significant expansion of access to high-income markets through mode 4.

Independent of what can be achieved in terms of binding of the status quo, the next round of services negotiations should seek to significantly expand the coverage of national treatment and market access commitments. These constitute the core of the GATS, and there is still an immense scope for expanding coverage. A formula approach might be considered to establish a benchmark or focal point for negotiations. Such a formula could center on the share of commitments that involve full bindings and the share that implies “free trade”, defined as the absence of limitations on national treatment or market access. But any formula must be complemented by guidelines that ensure that the key sectors that are vital from an economic development perspective are included—financial services, telecoms, transport, and the “trade services” sector—the cluster of activities that revolve around trade logistics and facilitation. The latter includes government services such as customs and conformity assessment procedures. While not regarded as “services” and dealt with in GATT fora, these are important activities that have a direct bearing on the ability of countries to participate in the world economy.

## References

- Aronson, Jonathan and Peter Cowhey. 1988. *When Nations Talk: International Trade in Telecommunications Services*. Cambridge, MA: Ballinger Press.
- Barfield, Claude E. and Mark A. Groombridge, "Breaking Down Barriers in Electronic Commerce," American Enterprise Institute, mimeo.
- Brown, Drusilla and Robert M. Stern. 1999. "Measurement and Modeling of the Economic Effects of Trade and Investment Barriers in Services," mimeo.
- Chadha, Rajesh. 1999. "GATS and Developing Countries: A Case Study of India," National Center for Advanced Economic Research, New Delhi, mimeo.
- Chanda, Rupa. 1999. "Movement of Natural Persons and Trade in Services: Liberalizing Temporary Movement of Labour under the GATS," Indian Council for Research on International Economic Relations, New Delhi, mimeo.
- Cho, Yoon-Je. 1988. "Some Policy Lessons from the Opening of the Korean Insurance Market," *World Bank Economic Review*, 2:239-54.
- Cowhey, Peter and Mikhail Klimenko. 1999. "The WTO Agreement and Telecommunications Policy Reform," World Bank, mimeo.
- Deardorff, Alan. 1999. "International Provision of Trade Services, Trade and Fragmentation," University of Michigan, mimeo.
- Dee, Philippa and Kevin Hanslow. 1999. "Multilateral Liberalization of Services Trade," Productivity Commission Australia, mimeo.
- Evenett, Simon and Bernard Hoekman. 1999. "Government Procurement of Services: Assessing the Case for Multilateral Disciplines," in Pierre Sauvé and Robert Stern (eds.), *Services 2000: New Directions in Services Trade Liberalization*, Washington D.C.: Brookings Institution, forthcoming.
- Feketekey, Geza. 1998. "Setting the Agenda for the Next Round of Negotiations on Trade in Services," in Jeffrey Schott (ed.), *Launching New Global Trade Talks: An Action Agenda*. Washington DC: Institute for International Economics.
- Findlay, Christopher and Tony Warren (eds.) 2000. *Impediments to Trade in Services: Measurement and Policy Implications*, Routledge, Sydney, forthcoming.
- Francois, Joseph. 1997. "External Bindings and the Credibility of Reform," in A. Galal and B. Hoekman, eds., *Regional Partners in Global Markets*, London: Centre for Economic Policy Research.
- Francois, Joseph and Bernard Hoekman. 1999. "Market Access in the Services Sectors," mimeo.
- Fung, Betty and Michael Stone. 1999. "Focus and Priorities of the New Round of Services Negotiations," World Services Congress 99, mimeo.
- Hodge, James. 1998. "Developing a Trade and Industrial Policy Agenda for Service Sectors in South Africa," TIPS Working Paper, Johannesburg (September).
- Hodge, James. 1999. "Examining the Cost of Services Protection in a Developing Country: The Case of South Africa," prepared for the World Services Congress 99, mimeo.
- Hoekman, Bernard. 1993. "Safeguard Provisions and International Trade Agreements Involving Services," *The World Economy*, 16:29-49.

- Hoekman, Bernard. 1996. "Assessing the General Agreement on Trade in Services," in Will Martin and L. Alan Winters (eds.), *The Uruguay Round and the Developing Countries*. Cambridge: Cambridge University Press.
- Hoekman, Bernard, and Carlos A. Primo Braga. 1997. "Protection and Trade in Services: A Survey." *Open Economies Review* 8 (3): 285–308.
- Hoekman, Bernard and Petros C. Mavroidis. 1999. "Enforcing Multilateral Commitments: Dispute Settlement and Developing Countries," World Bank, mimeo.
- Hoekman, Bernard and Patrick Messerlin. 1999. "Liberalizing Trade in Services: Reciprocal Negotiations and Regulatory Reform," in Pierre Sauvé and Robert Stern (eds.), *Services 2000: New Directions in Services Trade Liberalization*, Washington D.C.: Brookings Institution, forthcoming.
- Hindley, Brian. 1988. "Service Sector Protection: Considerations for Developing Countries," *World Bank Economic Review*, 2:205-24.
- Joskow, Paul. 1998. "Regulatory Priorities for Reforming Infrastructure Sectors in Developing Countries," Annual Bank Conference on Development Economics, World Bank, mimeo.
- Kaspar, Daniel. 1988. *Deregulation and Globalization: Liberalizing International Trade in Air Services*. Cambridge, MA: Ballinger.
- Laffont, Jean-Jacques. 1998. "Competition, Information and Development," World Bank Annual Conference on Development Economics, mimeo.
- Mann, Catherine. 1999. "E-Commerce", this volume.
- Markusen, Jim. Thomas Rutherford, and David Tarr. 1999. "Foreign Direct Investment in Services and the Domestic Market for Expertise," World Bank, mimeo.
- Mukherjee, Neela. 1999. "Market Access Commitments Under GATS: An Analysis from Developing Countries' Perspective," World Services Congress 99, mimeo.
- Mattoo, Aaditya. 1999a. "Financial Services and the WTO: Liberalization Commitments of the Developing and Transition Economies," Policy Research Working Paper 2184, World Bank (downloadable from [www.worldbank.org/trade](http://www.worldbank.org/trade)).
- Mattoo, Aaditya. 1999b. "Developing Countries in the New Round of GATS Negotiations: From a Defensive to a Proactive Role," World Bank, mimeo.
- Naude, W. 1999. "Trade in Transport Services: South Africa and the GATS," TIPS Working Paper, Johannesburg (August).
- Robinson, Sherman, Zhi Wang and Will Martin. 1999. "Capturing the Implications of Services Trade Liberalization," World Bank, mimeo.
- Tohamy, Sahar. 1999. "A Case Study of Egypt's Services Liberalization, Services Barriers and Implementation of the GATS", Egyptian Center for Economic Studies, mimeo (presented at the World Services Congress 99).
- UNCTAD. 1989. *Trade in Services: Sectoral Issues*. New York: United Nations.
- Walter, Ingo. 1988. *Global Competition in Financial Services: Market Structure, Protection, and Trade Liberalization*. Cambridge, MA.: Ballinger Press.
- Whichard, Obie. 1999. "Measurement, Classification and Reporting of Services Activities: An International Perspective," mimeo (downloadable from [www.worldbank.org/trade](http://www.worldbank.org/trade)).
- White, Lawrence. 1988. *International Trade in Ocean Shipping Services*. Cambridge, MA: Ballinger.