UNITED NATIONS

TD

United Nations Conference on Trade and Development

Distr.
GENERAL

TD/B/COM.1/EM.30/2
18 September 2006

Original: ENGLISH

TRADE AND DEVELOPMENT BOARD
Commission on International Trade in Goods and Services, and Commodities
Expert Meeting on Universal Access to Services
Geneva, 14–16 November 2006
Item 3 of the provisional agenda

UNIVERSAL ACCESS TO SERVICES

Note by the UNCTAD secretariat*

Executive summary

Many services are essential for human life or have important infrastructural characteristics and play a key role in achieving the MDGs. Telecommunications, health and education, or the provision of energy and water services are cases in point. In these sectors, governments face the challenge of ensuring that services are adequately provided, including to the poor and marginalized. National policies and regulations aimed at ensuring universal access to services (UA) are determined by a series of factors, including a country's specific economic and social situation, its national policy objectives and international commitments. This note analyses characteristics of key essential services sectors, how national policies to ensure UA differ across sectors and countries, and what can be done at the international level to promote access. It places particular emphasis on how to harness services trade and trade liberalization as a tool for improving UA to essential services.

* This document was submitted on the above-mentioned date as a result of processing delays.

I. INTRODUCTION

1. The tenth session of the Commission on Trade in Goods and Services, and Commodities (6–10 February 2006) agreed to hold an Expert Meeting on Universal Access to Services. Services, particularly universal access (UA) to essential services, can be an important contributor to human and economic development. Governments use various regulatory/policy tools to ensure UA for their citizens. Issues arising include: i) which services are critical for UA policies; ii) the spectrum of policy options available to advance UA objectives; iii) supportive financial and other mechanisms for UA; and iv) factors relevant in assessing whether public or private sector provision, or a combination thereof, is better placed to advance UA objectives in specific essential services sectors. This note focuses on policy and regulatory frameworks for ensuring UA to essential services, linking this debate to WTO negotiations to liberalize services trade, including negotiations for future disciplines on domestic regulation.

II. THE CASE FOR REGULATING SERVICES AND UNIVERSAL ACCESS

2. While there is broad agreement on the importance of ensuring UA to essential services, less agreement exists on what are the best approaches and means to do so. Options range from public to private provision, as well as community-based and other systems. Proper regulation, targeted pro-poor policies and active monitoring of services sectors' UA performance are critical requirements, particularly when relying on market forces and on the private sector to achieve UA.

3. Regulation involves the process of influencing, controlling and guiding economic or other private activities with impact on others through various governmental policies and measures. Regulation helps ensure numerous public policy objectives by, *inter alia*, protecting consumers, ensuring competition, developing domestic supply capacity, maintaining cultural diversity, protecting the environment, and ensuring UA to essential services for all, particularly the poor, vulnerable and marginalized segments of society.

4. The rationale for state-intervention to ensure UA stems from two different types of considerations: addressing market failures (e.g. information asymmetry, monopolies and externalities) and providing "merit goods", where the socially desirable level of services supply is not offered because of, among other reasons, profit considerations, public-good characteristics and the potential for free riding.[†] Various schools of thought (e.g. liberal theory of economic regulation, regulations based on distributive and other social policy objectives and rights-based approaches) suggest carefully designing regulatory frameworks for the services sector. The ultimate objective of regulation is to address issues of equity, accessibility, availability, adaptability and quality/safety as well as ethical issues beyond their manifestation as market failures and the pursuit of economic efficiency. A smooth functioning regulatory framework can contribute to government efforts to discharge their obligations and allow them to channel private sector engagement towards the achievement of UA goals.

[†] Merit goods/services are intrinsically desirable or socially valuable, with citizens being entitled to such goods and services, irrespective of whether they can afford them and of actual desires and preference.

5. Agreement exists on the positive role of regulation in ensuring UA to essential services and in infrastructural reform. Recently, regulatory failures have drawn attention to the importance of establishing an effective regulatory framework to ensure that social objectives are met and to raise levels of economic efficiency and quality achieved by private sector service providers. Examples include rail transport (UK), electricity (California), Enron, WorldCom, or various experiments with health-related user-fees and voucher systems (Ghana, Kenya, Nigeria), and private sector engagement in the provision of water (Bolivia).

6. This sparked analytical work on effective regulation in relation to identifying the most critical enabling conditions for proper infrastructure reform,[‡] one of the objectives of which is to attract the capital-investment required for a more satisfactory provision of services. Issues raised include: the need for regulatory agencies to be free of political interference in their decision-making; subjecting their decisions to review by the judiciary or oversight by another entity; competition and transparency, and the proper pacing and sequencing of reform, with suitable regulatory frameworks being established before the launching of privatization and liberalization processes. For UA policies to be sustainable for both governments and operators, appropriate pricing policies have to be in place. In the context of proposals for better managing and regulating transition processes (including privatization and liberalization), the more fundamental question may be whether or not the involvement of the private sector and foreign operators is the most suitable option in the first place. The need for government intervention to ensure UA is widely recognized and considered legitimate.

III. DEFINING UNIVERSAL ACCESS

7. Many services (e.g. health, education, water, communication, transport) are deeply embedded in a country's social, cultural or political context. Some are essential for human life, while others serve central infrastructural functions. Widespread recognition of the importance of certain services emanates from the benefits their consumption creates for society (e.g. their nature as a public or merit good) and from the positive impact they can have on a country's competitiveness and efficiency. While there is no universally agreed definition for essential services – and even less so an exhaustive catalogue – the centrality of many services has been recognized by the international community (e.g. in the Universal Declaration of Human Rights and the MDGs).

Universal Service – Universal Access

Universal service means that the service is provided to each person or household individually. *UA*, in turn, refers to the objective of providing everyone with access to a particular service, whether through individual or collective access. Universality is central to both concepts. In itself, it is a broad term, based on three fundamental principles: availability, access and affordability. In the case of telecommunications, the goal to achieve universal service is used in circumstances where there is already relatively good network coverage and high teledensity, with the focus therefore being on affordability. When there is poor network development and low teledensity, the objective is to ensure every citizen has reasonable public access at affordable rates. UA may be provided through pay phones, community telephone centres, teleboutiques or community internet access (e.g. a phone for every settlement with over 500 people in Ghana). While developed countries generally use the concept of universal service, for many developing countries the primary target is UA.

[‡] Ioannis N. Kessides (2004). *Reforming Infrastructure, Privatisation, Regulation and Competition, A World Bank Policy Research Report, 2004*, Washington D.C.

8. Policymakers use different concepts and definitions, e.g. essential or basic services, public services, merit goods, basic infrastructure services or services of general interest. Concepts vary depending on the type of service, the country's level of development and the policy discourse from which they emanate. Variations in the UA concept and definition also exist across sectors.

9. Poverty, ill-health and inadequate *health care* access are closely related, and it follows that economic progress depends on healthy citizens. Governments recognize the importance of human health as a human right, as reflected in MDGs 4, 5 and 6. They also set specific health targets, e.g. the '3-by-5' target of reaching 3 million people in developing countries with combination antiretroviral therapy for HIV/AIDS (by the end of 2005). Primary health care is the focus of most UA policies. While there is no uniform definition of primary health care, an approach to the development of health-care systems driven by primary health care must aim at UA to quality services. Primary health care varies according to the level of development.

10. The importance of *education* stems from its central contribution to poverty eradication, productivity/earnings, human resources capacity-building, technology development and sustained economic growth, including through integration into the global economy. No country has achieved economic growth without reaching the critical adult literacy rate of 40 per cent. However, education targets are far from being met, with an estimated 100 million children out of school (58 million of whom were girls) in 2005. UA goals relate to the achievement of universal primary education; higher literacy levels, including adult literacy; good quality education and gender parity; simultaneously developing secondary and tertiary education, as well as specific skills required in the global economy. This is closely linked to MDGs 2 (universal primary education) and 3 (gender parity in both primary and secondary education by 2015).

11. Access to clean, sufficient and affordable *water* is essential to poverty alleviation, sustainable development and human health and well-being. It is also an essential input to numerous production processes. However, to date, more than 1.1 billion people do not have access to clean water and about 4.2 billion lack access to sanitation facilities. UA goals in water are defined as access to an improved water source as the percentage of the population that can obtain at least 20 litres per person per day from a source that is within one kilometre of the user's home (UNICEF, WHO).

12. The essential nature of *telecommunication services* stems from their importance for economic growth and for the wider benefits associated with information and communication technologies (ICT). Telecommunication services can facilitate citizens' participation in information society initiatives, promote national cohesion and reduce disparities in rural and urban areas. In many countries, there is a growing trend to consider access to ICT as a basic right of all citizens. However, in many developing countries this infrastructure is lacking, particularly in rural areas. The goal of achieving UA was defined as access (whether individual or shared) to telephone services for every population centre above a certain size, and within a given distance. With technological evolutions, the UA aspect of telecommunication services changes from basic telephone services to Internet usage, possibly even broadband.

13. Reliable *energy supply, particularly through electricity* is essential for numerous activities in an economy, including the production of goods and services. It is also essential for socioeconomic development as it provides lighting (e.g. for literacy and greater chances

of employment); use of ICT; heating and cooking; and broadly supports income and employment generation; and affects sustainable development.

14. People in all income groups and all firms require access to *financial services* for their welfare and future economic prospects. However, the use of basic financial services in developing countries is far from universal. Even in developed countries, lack of access to financial services by certain segments of the population and firms is considered a serious problem; policies aimed at closing the financial divide (e.g. microcredit, microfinance) are discussed and implemented. While UA to financial services has not traditionally been a clearly stated public policy, the strong links between access to financial services, economic growth and poverty alleviation are modifying perceptions. Linkages between financial and other services (e.g. health and insurance) and the negative impact which not having access to financial services has on the achievement of key social objectives (e.g. the ability of patients to access health services) are widely recognized. UA to financial services has become a target of government policy.

15. Essential services and UA goals exhibit certain cross-cutting features. One relates to their *fundamental and essential nature,* economically and socially, including the fact that they are both a result of growth/development and a driver of it.

16. UA goals have *central common equity-related aspects*. While essential services and UA tend to be closely related to human dignity and sustainable development, they are *unequally and inequitably provided*.[§] One overriding principle across UA goals is to expand the availability of services to the public at large, so that inability to pay does not result in exclusion from the service, paying particular attention to the needs of consumers in lower-income and disadvantaged groups, including those in rural and remote areas. UA goals are to be developed in line with a number of *domestic factors* (e.g., national income; geographic distribution of the population; existing infrastructure; market/demand structure; security matters; and financial means). UA goals need to be carefully designed to allow for *accurate targeting* to specific segments of society and *adequate pricing* of services for sustainability of the policies.

17. *Essential services are closely interrelated*. Lack of progress in one can effectively impede progress in the other; this suggests an *integrated and holistic approach* towards designing and implementing policies to achieve UA in essential services.

18. *Flexibility* of UA goals to accommodate the different levels of *economic/social development within societies* and *to adjust to technological developments* is crucial. For example, the energy sector has seen new technological developments, (e.g. generation of renewable energies or photovoltaic technology), which have become internationally accepted as a valuable option for electrification in rural areas. As one target is met, UA must be redefined.

19. Another feature of many essential services is the *widely recognized importance of the role the public sector should play in their provision* – either as a regulator, provider or both. Public responsibilities for providing or regulating certain essential services arise as they are prone to market failures and because they may be considered human rights. In education,

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[§] UN Habitat and UNITAR, *Access to Basic Services for All, Towards an International Declaration on Partnerships*, a UN Habitat and UNITAR Joint Working Document, available at: http://dcp.unitar.org/spip/IMG/pdf/Access_to_Basic_Services-2.pdf.

health, water and electricity, the public sector is a major provider and funder of services. *Increasing reliance on private provision of services* is leading to a new paradigm in which the role of the government is shifting from providing services to monitoring and regulating to ensure UA.

IV. POLICIES FOR UNIVERSAL ACCESS

20. UA policies are diverse, with no universally accepted categorization. The spectrum ranges from public to private provision with many variations in between.

Diversity of UA Policies

Public services provision occurs at various levels of governance, frequently through hierarchical bureaucracies, where service providers are civil servants. *Publicly-funded services provision* includes the participation of private sector actors, receiving governmental support. *Universal Services Obligations (USOs)* are minimum performance requirements, which the State imposes on service providers. Sometimes taking the form of non-commercial service obligations (NCSO) they are used in combination with other policy tools, e.g. incentive mechanisms. *Subsidies* can be provided to different beneficiaries (households, operators) and have different sources of financing (government budget, UA-fund and cross-subsidization). *Microfinance, community-based* and other systems are attempts to ensure UA through innovative options, building on technological developments and local societal structures. The multiplicity of solutions proposed in response to public sector failures include: contracting out; participatory methods; social funds; user associations; community-driven civil services reform; privatization; democratization; decentralization; and empowerment − each of them is implemented through various policies/instruments.

21. Differences in UA policies exist depending on whether UA is ensured through monopolies, minimum social policy obligations or competitive services provision subject to government intervention. The latter category would contain different policy tools, broadly categorized according to whether they are supply-side interventions (e.g. domestic regulations, financial incentives/sanctions, and regulated prices), or demand-side interventions (consumer subsidies, e.g. scholarships, tax rebates and low interest loans).

22. It is important to realize that none of these solutions is a panacea and that “no one size fits all”. There is broad consensus that regulatory intervention is needed to ensure UA to essential services. At the same time, there is a wide diversity of options and each government needs to identify the "best fit solution" for it to implement, in accordance with its particular needs. The decision about which option to implement depends on a series of complex trade-offs, i.e. between promoting equitable and affordable access to a basic set of services; ensuring efficiencies; and meeting the constraints in government and household budgets, with trade-offs depending on economic/social circumstances, and the UA goal. Solutions have to be country and sector-specific. Frequently, regulatory tools are used in combination and modified over time to achieve optimal results.

23. The following survey of public and private sector approaches to UA and the different policy tools available (e.g. USOs, subsidies and UAFs), and the sectors in which they are commonly applied permits some preliminary lessons to be drawn on their usefulness and success for achieving UA to essential services.

Public Sector Involvement

24. Public provision of essential services is widespread. Throughout much of the twentieth century, most countries considered the provision of formal network infrastructure services (e.g. water, electricity) and other essential services (e.g. education, health), as the main prerogative and obligation of the State. In many of these services markets the public sector has traditionally been − and still is − a major provider (if not monopoly provider), as well as funder of the service. Governments contribute a large share of the financing for schools and clinics, and many teachers and health workers are civil service employees. Public services provision is different from publicly-funded services provision. While both are implemented at the state and municipal levels, the latter relies on private actors for services provision, but receives considerable government support to offset market failures. Conversely, publicly-owned services providers can draw on private funding (e.g. through fees or private donors/sponsors). Thus, the borders are becoming increasingly blurred.

25. In *education services* governments are directly involved in every aspect of schooling. UA policies are diverse (e.g. free/subsidized primary education, integrated food and health programmes; programmes targeted at the disadvantaged (e.g. women, minorities, working children, nomadic tribes); incentives to students/teachers; ensuring a specified number of schools per village; scholarships; education vouchers and user-fees). Experience from countries such as Kenya, Mexico and India indicates that the use of such programmes impacts on school participation, particularly by reducing the cost of schooling (including subsidies conditional on school attendance). While public education in some countries is controlled by individual states, in others there is a highly centralized public education system at the national level.

26. Frequently, public education co-exists with private education, which is sometimes publicly funded. Compared to some developed countries, in developing countries, private schools make up a larger share of educational providers, partly due to the public sector's inability to meet the demand for public schools. In developing countries the financial effort made by governments tends to be mainly directed towards primary education, followed by secondary education. Public spending increases in some developing countries have focused on tertiary education.

27. Some governments have tried to recover education expenditures by charging user fees, or through cost-sharing. These policies, implemented *inter alia* under the guidance of the international financial institutions (IFIs), aim at allowing market forces to set an economically efficient level of services; improving efficiency and equity in service delivery (reducing frivolous demand); increasing revenues; improving quality/coverage; and reducing the need for State funding. User fees would enable cost-sharing of expenses between governments. However, it has also been argued that user fees are not be appropriate to finance core government services, particularly social services and education programmes where services and benefits should be provided based on social objectives.

Education User Fees: The African Experience

Previously, education services may have been provided for free or at nominal cost, but user fees were advocated as an alternate form of funding education expenditure. However, the use of such fees has been criticized; the criticism has been levelled at the assumption that users can afford to pay, a specifically relevant issue for developing countries. Another argument against user fees is the unlikelihood of freed-up resources being significant in terms of their relevance to the provision of other capital-intensive basic services. The track record on user fees, particularly in sub-Saharan Africa, was not universally successful. Prior to the abolition of school fees in Uganda, the cost of educating a child for one year at the primary level was equivalent to 20 per cent of per capita income. The elimination of primary school fees in 2002 is reported to have resulted in an increase of students. Kenya, Malawi, Tanzania and Uganda serve as examples.

28. The public sector's inability to meet educational needs (including in rural areas) has sometimes been addressed by increasing private sector activity (e.g. NGOs, philanthropic or religious institutions) and supported by government contributions (e.g. free electricity, water, education funds, voucher systems, etc.). However, this can also result in private education being government-dependent. African governments have experimented with various public sector approaches to address specific educational challenges, including those in rural communities where the opportunity cost of school enrolment is significant and negatively affects household, livelihoods and potential earnings.

29. Effective public provision (and financing) of *health services* can be an important tool, particularly if governments lack the resources to prevent undesirable market failures and sufficient institutional frameworks to regulate private provision and protect consumers. Public money and public provision is maybe most important for interventions, where treating one case may prevent many others from arising (e.g. communicable diseases control). However, the public sector faces challenges (e.g. changing needs of consumers, new medical technologies, expectations of health professionals) and is often seen as uncompetitive. While some suggest that private provision of health services tends to be larger where countries' income levels are lower, most developed countries have publicly funded health systems, covering the majority of the population and with public hospitals frequently maintained under the State and centralized managements. Moreover, almost every country with a publicly-funded heath care system also has a parallel private system, which usually tends to serve private insurance holders. Publicly-funded healthcare can be provided by public sector practitioners (public agencies responsible for the delivery of healthcare) or by private agencies. Funding can come from different sources (e.g. general government revenues and social security systems).

30. Many low and middle-income countries have established State-funded healthcare systems with services produced by public bureaucracies. Many public systems now see developments towards greater flexibility, with attempts to increase market exposure of hospitals by "outsourcing" or "unbundling" some hospital activities, or by giving them autonomy over management decisions. However, experiences are mixed. Recently, also evidence on the potential impact of user-fees in terms of reduced access is becoming increasingly clear. A 2001 WHO report stated that user-fees have been found to decrease the utilisation of health services in most cases, and that the poor are the ones most discouraged

from health service use by fees.[**] A 2004 World Bank study found that the abolition of user fees improved access to health services.[††]

Private Sector Involvement

31. Private sector engagement and market-based policies can be an option for improving UA, particularly for sectors where significant investments are required and where financing from the public sector is lacking. While privatization was once considered the best available means to render infrastructure services efficient, experience has been mixed, with some privatizations producing efficiency gains and others failing. Privatization could end government support, with the result that (even though the sector becomes more efficient and average prices decline) the price for certain end users may increase, or geographical availability declines.[‡‡] In basic telecommunication services evidence points to a positive relationship between competitive market structures and wider access to services. In terms of financial services liberalization some evidence indicates adverse effects on access to credit for rural areas and the poor.

32. The success of private sector engagement for improving UA depends on a series of factors, including the type of essential service; the competitive situation in the industry; the type of private sector engagement (e.g. privatization, concessions, joint-ventures and build-operate-transfer); the manner in which private (including foreign) participation is introduced (e.g. public consultation, transparent decision-making); and the design and implementation of complementary policies. Besides economic justifications, the political feasibility, regulatory considerations and more broadly, social issues play major roles in the success or failure of privatization and trade liberalization efforts.

33. In most countries, the *supply and management of water* has traditionally been the domain of public entities at the national, regional or local levels. Yet, countries have employed different regulatory models and governments have often played multiple roles in the water sector (e.g. as a natural resource manager, service provider and regulator). During the late 1990s, public debate focused on the private sector and its potential to play an important role in building water infrastructure. Potential benefits could arise because of the highly capital intensive nature of water services, where financing for infrastructure development is crucial and higher payments from consumers could be an incentive for suppliers to extend pipes to those relying on water trucks or unclean sources. Accordingly, policies encouraging private (often foreign) investment in water services and privatization (including outsourcing and public-private partnerships) have been on the increase in recent years. While many of these policy shifts were based on autonomous national decisions, IFIs have also advocated a greater involvement of the private sector. However, full-fledged privatization is rare in the water sector, with governments preferring solutions which allow them to retain the ownership of the facility and contracting out certain tasks to private operators.

34. Privatization may well be a viable option for improving access to water for people without safe drinking water or sanitation systems. Indeed, there are examples where

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[**] England, S. et al. (2001), *Practice and Policies on User Fees for Immunization in Developing Countries*. WHO/V&B/01.07, available. Available at http://www.who.int/vaccines-documents.

[††] Deininger, K. and P. Mpuga (2004), *Economic and Welfare Impact of the Abolition of Health User Fees: Evidence from Uganda*. World Bank working paper 3276, April 2004, World Bank, Washington D.C.

[‡‡] World Bank (2002). *Global Economic Prospects and the Developing Countries, Making Trade Work for the World's Poor*, World Bank, Washington D.C.

privatization has proved successful in delivering water services to those in need. However, numerous questions have also arisen about the scope and extent of the role given to the public-good nature of water services. Studies point to mixed results following privatization. While benefits have occurred through an increased connectivity of households to distribution networks, there has also sometimes been a surge in water prices, which has affected the affordability of water services. It has been felt that private businesses may put too much emphasis on profits and costs-recovery and that services to vulnerable groups may be inadequate and of poor quality, and lastly that private operators may not be accountable to the public. Pressure on communal water schemes and the emergence of multinational companies specializing in water supply, with some − much publicized − privatizations failing to meet UA goals, has spurred a debate on the issue. Recent empirical evidence shows that there is no significant difference between public and private operators in terms of efficiency or other performance measures.

35. Public sector provision of services is widespread and central for economic development. However, it does not always translate into increased access due to inefficiencies. Responses to improve performance include: public/private partnerships in market and quasi-market relationships; far-reaching privatization programmes; greater accountability; and reducing corruption and rent-seeking. While the two extremes have been contrasted in public debates, a variety of options lie in-between. The level of private sector involvement partly determines the scope of foreign participation (or international trade) in essential services. Foreign providers can improve access to services, bringing new capital/expertise to domestic markets. However, foreign providers may seek to serve only high-income groups.

Universal Services Obligations

36. Universal services obligations (USOs) are central for pursuing UA objectives. They are performance requirements which the State imposes on the service provider (e.g. to expand service delivery to previously unserved areas, or to provide the particular service at an affordable price). Some USOs are general, applicable to all service providers, while others are specific, applicable to selected ones. Frequently, USOs are used in the context of licensing and they can be placed on both public (frequently the incumbent) and private operators. Some USOs are non-commercial (non-commercial service obligations, NCSOs), as they involve provision of a service to certain identifiable consumers for whom the costs of providing services exceeds anticipated revenues. Sometimes, USOs are used in combination with other policy tools (e.g. incentive mechanisms or licensing, including competitive bidding).[§§]

37. When using USOs, there is a need to ensure that they are realistic and clearly defined and that there are sufficient incentives for implementation. Other concerns include: their potential to impede competition in the market; their impact on the company's financial viability; consumer protection; and the need to account for technological changes. The most important challenges, however, arise with regard to their funding (e.g. appropriately estimating funding needs and meeting them), and how they should be targeted and monitored.

[§§] This involves licensing, with operators bidding against each other. The contract is awarded to the supplier with the lowest bid or to the supplier requiring the least amount of subsidy. The USO is inscribed in the operator's licence or concession contract.

38. *Telecommunications* is a sector where USOs have been most widely used, both in developed countries and developing countries. In developing countries USOs were one of the main mechanisms for expanding networks. Telecommunications USOs generally describe the geographical areas; the categories of services that service suppliers should provide; and the timeframes for implementation. In Europe, the scope of the USO is derived from the EC Universal Service Directive, with implementation at the national level. In the United Kingdom, for example, USOs included: special tariff schemes for low-income consumers; a connection to the fixed network (with functional internet access); reasonable access to public call-boxes; and several services for customers with disabilities.

Telecommunications in Kenya

Kenya's telecommunications sector has undergone numerous transformations with a series of challenges remaining today. Kenya's fixed lines are characterized by poor access. The situation is more promising in the mobile sector. The government guides the sector through its broader strategy for telecom reform, with the key objective to ensure that services reach poorly served areas of the country at affordable rates. When gradually liberalizing, the government applies licensing procedures to ensure compliance, including with UA targets. This includes targets to facilitate countrywide roll-out; improving service penetration in rural (from 0.16 lines to 5 per 100 people (2015) and in urban areas (from 4 to 20 lines per 100 people (2015)). This is complemented by the government's broader framework for investment, competition and growth aiming at encouraging investors/operators to participate in the provision of UA; and to provide quality service and choice. This resulted in the installation of 1.5 million fixed lines in rural and 2.4 million fixed lines in urban areas.

Source: UNCTAD Assessment Studies in Trade in Services and Development Implications, TD/B/COM1/77.

39. Many developing countries have used USOs to expand UA to telecommunications services, examples include countries such as India, China and Mexico. When India moved from a monopoly system to private participation, private firms were required to provide 10 per cent of their coverage in rural area as part of their licence conditions. However, while USO targets were stipulated in licence agreements, operators did not meet them and regulatory authorities could not enforce them. Under China's "village-to-village project", six telecommunications operators were each assigned responsibility for providing UA (two public pay phones) to each village in a number of designated provinces. Targets were set in accordance with the company's size and financial capacity. The 2005 short-term goal was for a certain per cent of villages to be provided with telephone services; the 2010 medium-term goal is for all villages, hospitals and other organizations to be connected to public telecommunications network; and the 2020 long-term goal is for all organizations and families to be connected to the public telecommunications network. In Mexico, the incumbent operator (Telmex) was required as part of its privatization, to install pay phones in 20,000 rural areas over a five-year period to ensure access in all villages with at least 500 inhabitants.

40. Key USO-related questions concern their funding, implementation and enforcement. Inadequate enforcement mechanisms and overly ambitious targets are among the reasons for failure. Policies for funding include: general taxation; interconnection charges; access charge mechanisms, or access deficit charges (long-distance operators paying interconnection charges when accessing the local loop, in addition to termination charges); cross-subsidies; Universal Access Funds (UAFs) (operators in the industry contribute to a fund, used to cover

the net cost of UA); or competitive bidding (where the provider is compensated after the specified targets have been reached).

Subsidies

41. Subsidies are widely used for UA. They can target households (e.g. vouchers directly benefiting disadvantaged consumers), or service providers (e.g. cross-subsidies and UA fund). Sources of financing include: government budgets, UA funds and cross-subsidization. Subsidies can take various forms, either by being transferred directly, through vouchers or cost free, or below-cost provision of services. The specific types of subsidies used vary depending on the UA goal and on the country's level of development. Subsidies also give rise to numerous challenges, e.g. the unavailability of financial resources for providing subsidies, or the difficulties related to the proper targeting of subsidies. This is particularly the case in developing countries, where institutional and regulatory frameworks tend to be weak. More broadly, some subsidies are criticized for the distortions they create in market mechanisms (including trade distortions).[***]

42. For some services the purchasing power of poor people remains insufficient to overcome price barriers, suggesting direct transfers to households (demand-side subsidies) as a possible policy response. This may be particularly important for services which serve the needs of vulnerable people, e.g. low-income consumers, disabled or those living in remote areas. The main problem lies with targeting. While targeting criteria are established (on the basis of certain attributes of households, consumers, different geographical jurisdictions or areas) implementation remains difficult. Another challenge relates to the choice of focusing subsidies (i.e. whether to concentrate on increasing access for unconnected or reducing prices for those already connected).

43. The voucher system in education takes various forms involving both public and private schools. Some countries have started subsidizing private schools in order to increase supply. While education vouchers have been frequently used, doubts have been expressed on whether this system has been successfully implemented and whether they have performed well. The system has seen successes (e.g. Sweden), but also less satisfactory performances (e.g. Colombia). Proponents claim that vouchers will increase competition between schools and raise performance across schools; furthermore, critics argue that vouchers can lead to additional funding problems and may siphon the best students away from public schools.

44. In the 1990s Chile introduced a nationwide system of quasi-vouchers, directed to all municipal schools and non-charging private schools. Enrolment increased considerably, particularly in private schools. In Mexico's *Progresa* system children over seven were eligible for education vouchers, with financial transfers increasing by grade, to account for the family’s opportunity costs of sending children to school. Benefits were also higher for girls in middle school to encourage their enrolment. The subsidy is dependant on children’s attendance record and performance. Transfers went to mothers to ensure rational spending. The system was considered successful.

[***] For example, over the years WTO Members have discussed the potential for subsidies to have trade distorting effects. See the Annual Report of the Working Party on GATS Rules to the Council for Trade in Services (2005), 12 September 2005, S/WPGR /W/53. Discussions are undertaken in line with the GATS Article XV mandate to negotiate "with a view to developing the necessary multilateral disciplines to avoid such trade-distortive effects".

45. Colombia's PACES programme (1991) offered vouchers aiming to increase the number of poor students continuing to secondary education (in private and public schools). Most elite private schools refused to participate and the voucher value was not indexed to price rises (requiring out-of-pocket payments). While the system provided some degree of higher enrolment, many argued that it failed to meet its objective, and in 1998 it was discontinued and replaced by another more successful programme. India has recently announced a voucher system with the goal to universalize secondary education; the India education voucher scheme would be a tax-funded payment, enabling beneficiaries to choose the school, thereby allowing for greater competition among public and private schools.

46. Some countries refined their subsidies programmes by making support dependent on certain development enhancing actions by beneficiary families. In Nicaragua the condition for certain financial stipends is the use of certain preventive health services. Under the Mexican *Progres* programme, families could receive additional monthly stipends if they undertook medical checkups and attended nutrition/hygiene sessions.

47. Direct subsidies are also used in the *water sector*, the main problems being targeting and choosing whether to support connection or consumption. Water subsidies can take different forms and can either be paid in kind (e.g. free water per households or head), in cash (e.g. managed through the billing system, with government-funded subsidies deducted from the consumers' bills), or through social tariffs which cross-subsidize poorer households. Regarding targeting, subsidies tend to benefit the middle classes, sometimes excluding the poor. A study revealed that for most of the water programmes studied, the poorest 40 per cent of the population received only 5-20 per cent of the subsidy benefits. In La Paz, Bolivia, water is subsidized but those benefiting the most were higher-income households.

48. While good monitoring and metering, together with data and general administrative capacities, is essential, communities can play a leading role in improving targeting. Also, the type of target has an impact on leakages, with targeting by geographical area risking high rates of errors and rendering testing administratively costly. According to some, the most effective form of targeting in developing countries would be to focus subsidies on connection rather than consumption, with the additional benefit of avoiding missing-out on those who are still excluded from the network – usually the poorest. In Nairobi the cost per litre is 10 times more for customers of vendors compared to those connected to the network. Nevertheless, emphasis is frequently put on keeping prices down for existing users, while maintaining connection fees for new users.

49. Targeting water subsidies raises additional questions, e.g. about managing the interface between private/individual and industrial/agricultural consumption, and about water being supplied below the cost of supply (e.g. 40 per cent of utilities charge tariffs that do not cover operation and maintenance). Average water tariffs in low-income countries are about a tenth of those in high-income countries, while costs are roughly the same.

50. Challenges similar to those in the water sector also arise in power/energy, where connection subsidies constitute an important tool for improving the electrification of developing countries (particularly given high costs of grid connection). Consumption subsidies are also used. In the Philippines, "lifeline rates" are given to low-income captive end-users who cannot afford to pay at full cost. However, some of the mechanisms may have increased inequality, as benefits were captured by the already well-off rather than the poor.

51. UAFs collect revenues from various sources and disburse them to achieve UA targets/goals. For certain essential services UAFs are considered one of, if not the best, option for achieving universality, with sources for funding varying between direct funding from government; proportional contributions from all service providers; proceeds from auctions or licence payments; levies on subscribers or funding from international development agencies. Also, the financing of universal service obligations is frequently done through UAFs.

52. UAFs have proven to be successful in *telecommunications,* where they were generally financed by a tax on telecommunication operators, general tax funds, industry levies, the sale of resources (e.g. privatization) or the sale of licences. In developing countries, USFs are often financed through government subsidies, frequently in combination with other sources. Besides operator levies, minimum-subsidy auctions have proved a smart form of subsidization, including for USFs. In several countries auctions resulted in meeting – partly even exceeding − the targets set by governments. In some cases (Chile, Peru), competitive bidding processes even led to issuing licences with zero subsidies, with no need to subsidize the winning bidder at all. Competitive bidding for telecommunications has also been considered successful in other countries, including Argentina, Australia and New Zealand.

V. UA AND TRADE IN SERVICES

53. The extent to which privatization and trade liberalization of services can deliver more efficient services provision, while maintaining access to essential services by the poor, must be evaluated within national contexts. The selection of specific services sectors for liberalization, generation of synergies between liberalized sectors and those remaining in the public realm, the structure and degree of market opening, and the timing and sequencing of related market reforms are critical considerations in the liberalization process. UA gains from liberalizing and trading services can arise through the positive economic impact of reducing barriers to foreign services supplier (including by increasing efficiencies in services sectors); the use of openness to attract FDI (one mode of services trade) to expand infrastructure; or the re-allocation of funds, where access to lower-priced and privately-provided services can free up government funding to be used for enhancing access for those unable to pay.

54. Concerns were voiced that liberalization may negatively affect access/equity (e.g. liberalization creating situations where benefits arise predominantly for those who do not face most access-related difficulties); that liberalization might generate structural changes leading to a two-tier system and "cream-skimming"; and that it might render specific services more expensive and impossible to access, particularly for the poor and marginalized (even if the overall impacts of liberalisation are positive). In such scenarios, openness will exacerbate the underlying challenges of a country's UA system.

55. As evidence and analysis is limited and − when available − points to mixed results, this suggests caution, as well as careful pacing and sequencing of liberalization and regulation. It also highlights the importance of building appropriate institutional and regulatory frameworks, ensuring that certain preconditions are in place before opening services markets. This raises broader questions about the impacts which trade can have on governments' abilities to take such a careful/sequential approach, including for UA policies. Together with the potential for constraints on policy space, this made governments reluctant to accept binding liberalization commitments for certain essential services sectors (e.g. health).

GATS and UA Policies

56. The relationship between the GATS and UA in services is multifaceted, with several GATS provisions relating to UA policies. Article I:3(b) of the GATS contains a carve-out for services "provided in the exercise of governmental authority". This reflects Members' desire to leave certain services activities (and policies regulating them) outside multilateral rules, including because they are considered governmental prerogatives. However, uncertainties exist about the exact scope of Article I:3(b). Some argue that the provision establishes quite stringent criteria: for a service to be covered by the exemption, it must neither be provided on a commercial basis, nor be in competition with another service. Many of the systems through which governments ensure UA in essential services sectors do not directly match the criteria for exemption contained in Article I:3(b). Given the potentially narrow coverage of Article I:3(b), uncertainties surrounding its interpretation, and the fact that UA frameworks only partially correspond to the Article I:3(b) criteria, several Members introduced additional "public services carve-outs" in their commitments, including to manage the public-private interface.

57. In their schedules, Members adopted different methods for such carve-outs, either by limiting the sectoral coverage (e.g. not covering all of the sewage sector, but only related advisory services); limiting the scope of the commitment to private provision (e.g. only provision of private education/health services; excluding public works function); carving-out public services; or retaining the space to use certain policy tools to be used in sectors considered public utilities. Some schedules specifically refer to the various levels of governance or the contractual arrangements for private sector engagement.

58. UA-related provisions cover telecommunications. Paragraph 3 of the Telecommunications Reference Paper (RP)[†††] states that "any Member has the right to define the kind of universal service obligation it wishes to maintain. Such obligations will not be regarded as anti-competitive *per se*, provided they are administered in a transparent, non-discriminatory and competitively neutral manner and are not more burdensome than necessary for the kind of universal service defined by the Member". The RP also requires Members to put in place appropriate measures for the purpose of preventing major suppliers from engaging in or continuing anti-competitive practices, with anti-competitive cross-subsidization possibly falling into this category. A 2004 dispute settlement case demonstrated the limits of these provisions: in *Mexico − Telecommunications*, Mexico, the defending party argued that "… countries – especially developing countries such as Mexico – have wide latitude to allow rates that would permit the continued development of needed infrastructure and the achievement of universal service", an argument developed in the context of paragraph 2.2(b) of the RP.[‡‡‡] Ultimately, however, the Panel found "an inconsistency with Mexico's obligations under Section 2.2(b) of the Reference Paper". India adopted the RP with modifications, essentially aiming to make it more flexible. India's RP uses language specifying that it retains the right to define the kind of USOs it wishes to maintain. India deleted the RP template's language that a USO will not be regarded as anti-competitive *per se*, if it is "administered in a … competitively neutral manner and [is not] more burdensome than necessary for the kind of universal service defined by the Member".

[†††] Negotiating Group on Basic Telecommunications, 24 April 1996. Available at: http://www.wto.org/english/news_e/pres97_e/refpap-e.htm.
[‡‡‡] *Mexico − Measures Affecting Telecommunications Services*, WT/DS204/R, para. 4.180.

59. GATS also contains − albeit limited − rules for subsidies. While governments appear to have some leeway to use financial incentives, the negotiating mandate (Article XV mandating negotiations on trade distortive subsidies); the general MFN obligation (Article II); the specific national treatment provision (Article XVII) and the above-mentioned language in the RP are all relevant for subsidies. In their schedules several Members made reservations to retain policy space for implementing certain subsidy-related policies. Examples include schedules noting that the supply of a service or its subsidization, within the public sector, is not in breach of the relevant commitment; schedules noting that scholarships/grants may be limited to relevant nationals; schedules making the eligibility for subsidies dependant on participation of nationals on company boards; or schedules keeping modal entries unbound, either for all subsidies or for specific subsidies (e.g. R&D).

60. Article XIII provides that "Articles II, XVI and XVII[§§§] shall not apply to laws, regulations or requirements governing the procurement by governmental agencies of services purchased for governmental purposes…". It also establishes a negotiating mandate, the scope of which, however, is disputed. Article XIII has given rise to complex UA-related questions, e.g. whether concession contracts, build-operate-transfer (BOT) arrangements, or management contracts are considered as government procurement, and therefore excluded from the GATS. There appears to be some convergence on the view that concession contracts are not seen as government procurement, but the issue is even more complex when it comes to BOT- management contracts. Also Article VI on domestic regulations (DR) and current negotiations to establish future disciplines on DR raise questions on UA policies, highlighting the need to preserve the right to regulate, as enshrined in the GATS.

Uruguay Round Commitments

61. GATS impact on a country's UA policies depends, amongst others, on the extent/depth of commitments made in UA-related sectors. Schedules tend to reflect considerations about constraints for governments' right to regulate (including for UA goals) and about the long-term effects of commitments, possibly locking in certain policy choices or limiting flexibility.

62. The number of Members with commitments in UA-related sectors ranges from a few to a relatively high number, depending on the sector in question; related sensitivities and social/cultural policy objectives; and the country's level of development. While in primary education, less than one quarter of WTO Members made commitments, in telecommunications over 60 per cent of Members made (albeit limited) commitments (e.g. voice telephony).

63. For education, wide-ranging sectoral coverage is more prevalent in schedules of developed and transition countries (many of which recently acceded to WTO), *vis-à-vis* those of developing countries, with some Members carefully limiting the sectoral scope of their commitments (e.g. focusing on private tertiary education). No Member made any commitments on the provision of water, but 42 Members made binding commitments in related essential services, e.g. sewage. Also energy has drawn relatively few commitments, mostly because of the generally public nature of energy services during the Uruguay Round negotiations and the absence of a separate energy sector in the WTO's classification list. Health services (covered under health and professional services) attracted relatively few commitments, medical and dental services have the most commitments, followed by hospital

[§§§] Articles II, XVI and XVII address MFN, national treatment and market access respectively.

and midwives/nurses services. The country pattern of commitments is diffuse with some not undertaking commitments in any of the four core health-related subsectors. Telecommunications commitments are in turn, frequent, with many countries, including accession countries, adopting the RP. This may reflect the sector's transition from a monopoly, over oligopolistic structures, to open regimes and all the benefits accruing from this.

Doha Negotiations

64. The Doha negotiations to liberalize services trade are conducted along two tracks: one track consists of negotiations to increase market access; and the other track is on GATS rules/domestic regulation. The WTO's sixth Ministerial Meeting in Hong Kong raised the profile and provided impetus into services negotiations, with Annex C of the Ministerial Declaration setting important targets and timelines for future work. Regarding *market access*, 71 initial offers were submitted (by 95 Members), and 30 revised offers (by 54 Members) by August 2006. However, Members offered limited improvements (e.g. regarding number of subsectors and depth of commitments). Besides the overall limited nature of offers, sectoral offers broadly follow the pattern of UR[UU1] commitments. While telecommunications (similar to business/financial) attracted numerous offers, education, environmental or health services show comparably fewer offers/improvements. No Member made an offer for the provision of water and − apart from a minor change in one offer − no developed country offered anything in certain health services. With several essential services subject to plurilateral negotiations, Members may wish to consider innovative options. Combining GATS commitments with flexibility to review − and roll back − commitments in light of their impacts on UA goals may offer a safety-valve, making it easier for Members to offer commitments in the first place.

65. Plurilateral negotiations − while falling short of achieving concrete market access − were considered useful for clarifying technical issues and outlining the contours of a possible services package. Several requests, mainly submitted by developed countries, dealt with sectors in which governments pursue UA goals (education, postal, environmental, telecommunications, energy), sometimes specifically addressing UA policies. This is illustrated by the request on education which: seeks new/improved commitments in private higher education and/or private "other" education; does not request commitments in public education; and states that a commitment (especially in private education) does not necessarily mean committing government resources to private institutions. It suggests a sector coverage that excludes that part of a member’s sector which it considers to be a public good and a limitation for government funding available to students/institutions.

66. On domestic regulation, the Chairperson of the Working Party of Domestic Regulation (WPDR) issued a consolidated working paper based on proposals, covering licensing requirements/procedures, qualifications requirements procedures, technical standards and transparency. The paper suggests disciplines to apply across all services sectors where a Member has binding liberalization commitments. It clarifies that disciplines do not apply to measures which constitute limitations subject to scheduling under Articles XVI and XVIII. It states that the disciplines shall not be construed to prevent Members from exercizing the right to regulate and from introducing new regulations, nor to prescribe or impose any particular regulatory approach in domestic regulations. While the paper refers to "necessity", it also acknowledges that many delegations have made no proposals on this concept and are reluctant to include it. It also states that future disciplines shall not be

construed to prevent a Member from exercising the right to introduce or maintain regulations to ensure provision of a universal service, in a manner consistent with its obligations and commitments under the GATS.

67. Several fundamental issues remain unresolved and there are concerns that future disciplines could affect countries' abilities to implement UA policies suited to national contexts. Outstanding issues include: scope/coverage of future disciplines (e.g. the extent to which future disciplines would cover UA policies, particularly given that USOs, e.g. minimum capacity/service requirements for social, regional and similar policy reasons, tend to be enshrined in licensing contracts); and the "necessity test", e.g. whether it could make it difficult for regulators to accommodate and balance the interests of various stakeholders. For developing countries the main challenge is striking a balance between preserving the right to regulate and achieving clear and specific international disciplines, including for Mode 4.

VI. CONCLUSIONS

68. Ensuring UA is central for human and economic development, and governments use a series of policies to achieve these goals. There is widespread agreement on the importance of UA goals, but less convergence on how to best achieve them. Governments use a range of UA policies. Options include public provision and financing or private sector engagement, used in combination with each other and/or with other UA policies (e.g. USOs and subsidies). The main challenges faced by governments are to determine UA goals and the most appropriate policy to pursue them; to improve the accessibility and affordability of a service; to increase the efficiency of supplying the service; to limit the expenses arising for governments/ taxpayers; to properly price the service; and to monitor and target specific policies and their implications.

69. With good regulations in place, private engagement, including by foreign providers, may contribute to the achievement of UA. Policymakers need to carefully consider those instances where opening to foreign providers extends access to disadvantaged and marginalized groups in society. For certain sectors, and in certain countries, the government rather than the private sector may be best placed to provide essential services, and vice versa. Or, in cases where privatization is pursued, the national objective might be better met by limiting participation to domestic firms (e.g. without or with limited trade-liberalization commitments). However, evidence on the impacts of various UA policies remains limited and − where available − results have been mixed. Therefore, caution is warranted and more research is needed to improve the knowledge and evidence base available to governments when making their policy choices. Research could shed light on innovative approaches for pursuing UA goals.

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