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Services, development and trade: The regulatory and institutional dimension

Note by the UNCTAD secretariat

Executive summary

Services, particularly infrastructure services sectors (ISS), foster economic growth and development, contributing to the achievement of the Millennium Development Goals, and will eventually contribute to future post-2015 sustainable development goals. Despite the outcome of the World Trade Organization (WTO) Ministerial Conference in Bali, Indonesia, the multilateral trading system continues to face challenges in delivering negotiated results including in services. Regional trade agreements (RTAs) have proliferated worldwide to become a defining feature of today's international trading system and trade policy landscape. New-generation RTAs have extended the frontier of international trade rules and market access to services. Many developing countries have embarked on regional integration and cooperation to harness the potential of ISS. Adequate design, pacing and sequencing between domestic reform and regional and multilateral liberalization is important in achieving a coherent and integrated policy and regulatory mix that is best fit to national circumstances and development priorities. Developmental regionalism that combines liberalization and cooperative frameworks is providing a promising avenue for ISS development.

Introduction

1. ISS – transport, energy, communications and financial services – are essential to the efficient functioning of all modern economies and to strengthened productive capabilities. They are fundamental inputs to all economic activities, both goods and services, and facilitate development, trade and investment. Their importance has been further accentuated by the rising prominence of trade within global value chains. Firms today depend on access to high-quality and adequately priced services for their competitive positions. Existing research strongly suggests a positive association between infrastructure quality and economy-wide competitiveness and income levels. Access to some essential ISS are also fundamental to achieving the Millennium Development Goals, including universal access to water, energy, finance and technology and eradicating poverty, and will also be essential to achieving post-2015 sustainable development goals.

2. Regulations strongly matter in harnessing the benefits of ISS as they are prone to a series of market failures. Devising adequate regulatory and institutional frameworks that are best fit to national circumstances and priorities in an increasingly open trading environment has emerged as a critical challenge to Governments. The national regulatory landscape has evolved as regulators seek to adapt regulatory tools to better respond to technology advancement and new business models (telecommunications, information and communications technology (ICT)), enhance macroprudential regulations to pre-empt financial crisis (financial) and address climate change and energy efficiency (energy, transport). As RTAs have become a key driver of market opening with an important bearing on national regulatory regimes, the issue that arises is ensuring a coherent approach to multilateral and regional trade liberalization and national regulatory processes.

I. Trends in trade in infrastructure services sectors

3. The value of global cross-border exports in ISS reached $1.4 trillion in 2012, equivalent to 32 per cent of world total services exports (table 1).[1] ISS were estimated to account for some 14 per cent of global services outputs in 2010, absorbing about 10 per cent of the global work force. Transport is by far the single most important ISS with its 20 per cent share in total services exports, and largely outweighs financial services (9.1 per cent) and communications (2.5 per cent).[2] Apart from sheer market size, this reflects the fact that cross-border provision of services (mode 1) is the dominant form of trade in the transport sector associated with merchandise trade and movement of people.

Table 1
Share of infrastructure support services in total services exports by region, 2012
(Percentage)

	Transport	*Communications*	*Financial*	*ISS total*	*Travel*	*Other business services*
World	20.2	2.5	9.1	31.8	25.1	25.5
Developing countries	22.4	2.0	5.3	29.8	33.0	24.5
Transition economies	32.8	3.1	2.1	38.1	29.1	20.4

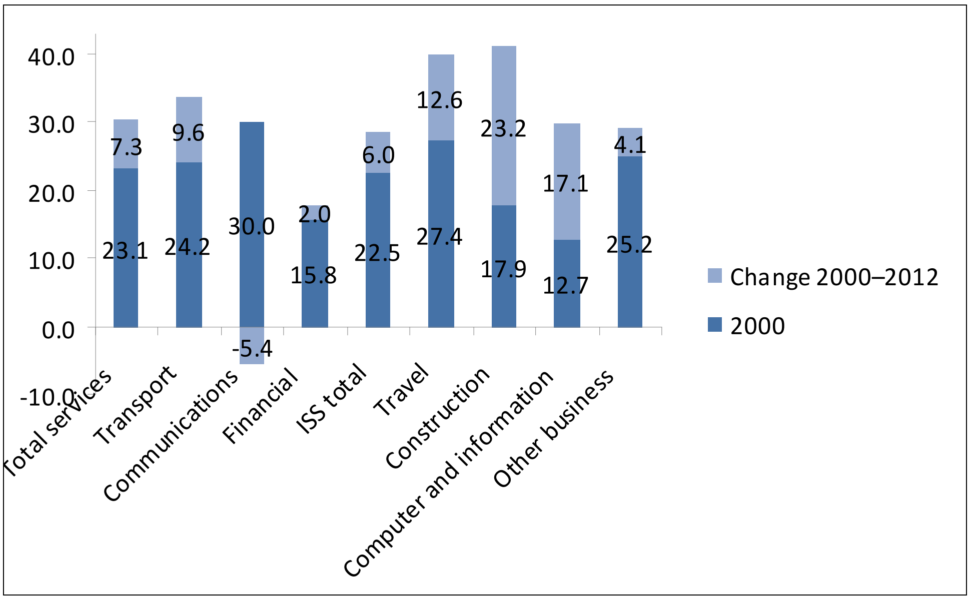
[1] Data are not available for energy services.
[2] Financial services referred to in this paper include insurance unless otherwise noted.

	Transport	*Communications*	*Financial*	*ISS total*	*Travel*	*Other business services*
Developed countries	18.6	2.7	11.1	32.4	21.3	26.1
Developing Africa	27.2	4.5	3.4	35.1	43.9	10.7
Developing America	18.3	2.7	5.9	27.0	38.2	27.3
Developing Asia	22.6	1.7	5.4	29.8	31.2	25.4

Source: UNCTADstat.

4. For developing countries, cross-border exports in ISS stood at $401 billion or 29.8 per cent of their total services exports in 2012. Their share in world exports in ISS rose from 22.5 per cent in 2000 to 28.5 per cent in 2012 (figure 1). This points to the improved competitiveness of developing countries in these sectors. There is significant sectoral variation in the dynamic competitive position of developing countries. In 2012, the share of developing countries in world exports was highest in transport services (33.8 per cent) and lowest in financial services (17.8 per cent), and the share increased by 9.6 percentage points in transport between 2000 and 2012 and decreased by 5.4 percentage points for communications.

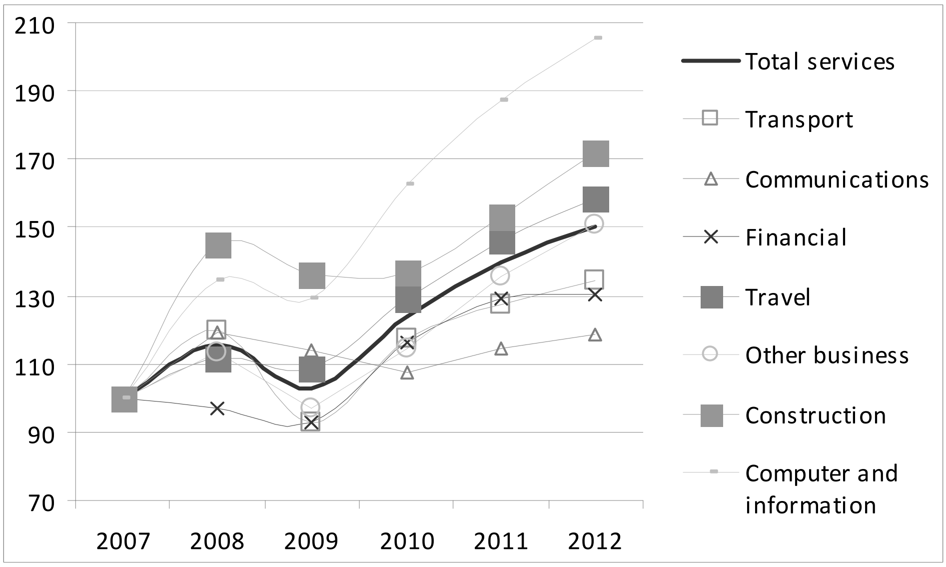
Figure 1
Share of developing countries in world services exports by sector, 2000 and 2012
(Percentage)



Source: UNCTADstat.

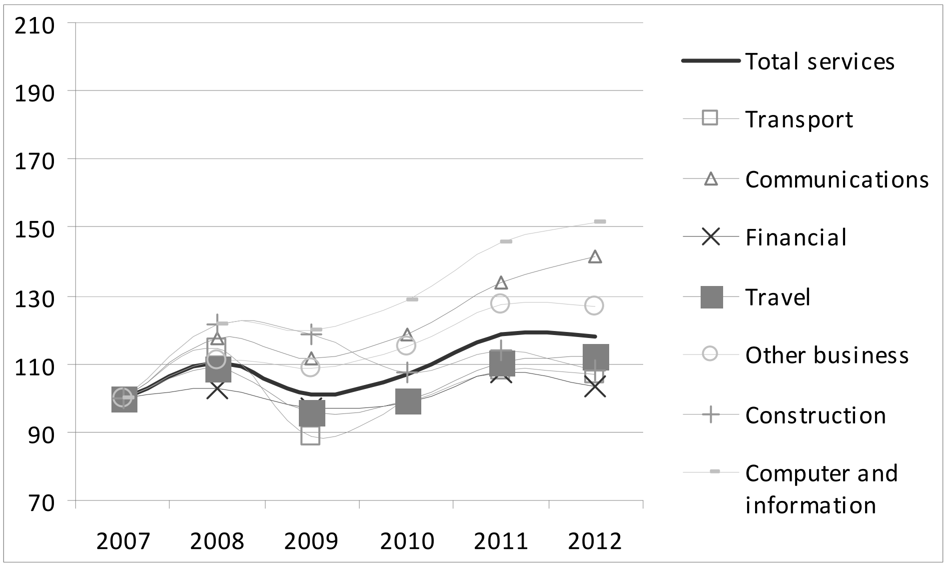
5. Cross-border exports in ISS generally underperformed compared with other more dynamic services sectors in recent years (figure 2). The three areas of ISS for which data are available demonstrated a slower recovery since the global financial crisis, in part coinciding with slow growth in trade in manufactures and continued fragility in financial markets. This is sharply contrasted with the more dynamic export expansion of computer and information, construction and travel services. Among developing regions, Asia remains a dominant player and represent over 80 per cent of total developing countries' exports in transport and financial services. Developed countries exhibited an even slower export recovery in all sectors, but particularly in transport and financial services (figure 3).

Figure 2
Developing countries' exports of selected services categories, 2007–2012
(2007=100)



Source: UNCTADstat.

Figure 3
Developed countries' exports of selected services categories, 2007–2012
(2007=100)



Source: UNCTADstat.

6. Cross-border trade captures only one dimension of services trade. A different picture emerges if one takes into account trade through mode 3 (commercial presence). In the United States of America, affiliate transactions (i.e. services supplied by majority-owned foreign affiliates of United States firms) accounted for the majority of United States trade in ISS, with foreign affiliates supplying $641 billion of such services, five times greater than cross-border services exports.[3] This indicates that the bulk of services exports takes place through foreign direct investment (FDI).

7. World FDI outflows amounted to $1.4 trillion in 2009–2011, 69 per cent of which were directed at services. ISS as a group represented 31 per cent of total FDI outflows. Developing countries accounted for 12.5 per cent of FDI outflows into ISS. This share represents a remarkable increase from 1990–1992 when the share was a marginal 0.4 per cent. The vast majority of developing country FDI was directed at financial services (15.4 per cent), and the shares of electricity, gas and water (1.0 per cent) and transport, storage and communications (3.9 per cent) were small.

8. Some industry-level revenue trends are informative of the market forces behind country-level trade performance. The size of the telecommunications market is increasing dynamically in line with developments in ICT access and uptake. From 2007 to 2011, total telecommunications revenues grew by 12 per cent, climbing to $1.8 trillion or 2.6 per cent of world gross domestic product (GDP).[4] The developing country share of total telecommunications revenues increased from 26 to 30 per cent. In financial services, commercial banking industry revenue increased at a modest 1.3 per cent average annual rate, to about $3.5 trillion over the five years to 2013. It was estimated that the industry's revenue would grow at 4.2 per cent in 2013. As regards transport, international seaborne trade volumes increased an estimated 4.3 per cent in 2012.[5] Continued overcapacity kept overall freight rates low in 2012, which reduced the earnings of carriers to close to operating costs, thereby casting uncertainty over their future revenue prospects.

9. While no data are available on trade though temporary movement of natural persons (mode 4), mode 4 is potentially important in the provision of ISS and related professional and business services. Global remittance flows to developing countries are estimated to have increased by 6.3 per cent in 2013 to $414 billion, while global flows are estimated at $550 billion.[6] Hence, about 75 per cent of total global remittance flows goes to developing countries. Flows to developing countries are expected to increase to $540 billion by 2016. Facilitating labour mobility, including through mode 4, could further contribute to increased remittance flows.

10. Data paucity in services, including trade in modes 3 and 4, highlights the importance of improved data collection to facilitate impact assessment analysis, informed policymaking and regulatory reform, and multilateral and regional trade negotiations. Brazil's Siscoserv initiative is an example of a national initiative to improve firm-level data collection on services.

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3 United States, International Trade Commission, 2012, *Recent Trends in United States Services Trade: 2012 Annual Report* (Washington, D.C.).

4 International Telecommunication Union, 2013, *Measuring the Information Society 2013* (Geneva).

5 UNCTAD, 2013, *Review of Maritime Transport 2013* (New York and Geneva, Sales no. E. 13.II.D.9, United Nations publication).

6 World Bank, 2013, Migration and remittance flows: Recent trends and outlook, 2013–2016, Migration and Development Brief No. 21, available at http://siteresources.worldbank.org/INTPROSPECTS/Resources/334934-1288990760745/MigrationandDevelopmentBrief21.pdf .

II. Overview of services regional trade agreements

11. Progressive liberalization of services has been pursued at the multilateral level under the WTO Doha Round. Priority attention failed to be given to services although services were a built-in agenda issue left from the Uruguay Round, and progress in services negotiations was largely conditioned upon that in agriculture and non-agricultural market access negotiations. This remains the case despite the outcome of the recent WTO Ninth Ministerial Conference, including the trade facilitation agreement and the ministerial decision on operationalization of the waiver concerning preferential treatment to services and service suppliers of least developed countries. The ministerial decision, inter alia, provides for the Council for Trade in Services to initiate a process for the expeditious operationalization of the waiver.

12. It is against this backdrop that plurilateral and regional initiatives have intensified. Twenty-three WTO members representing 70 per cent of global services trade have launched negotiations for a plurilateral trade in services agreement (TISA). The TISA is said to be comprehensive in scope and built upon the General Agreement on Trade in Services (GATS) approach to promote subsequent multilateralization and participation of new members and capture autonomous and preferential liberalization. There is a possibility that national treatment would be applied on a horizontal basis to all sectors and modes. Automatic multilateralization of TISA based on the most-favoured nation principle is envisaged to be temporarily pushed back as long as there is no critical mass of WTO members joining TISA. This implies that the future TISA may be a preferential agreement covered under article V of GATS. Another option that has been discussed is a plurilateral agreement in WTO.

Box 1. The trade in services agreement and regional trade agreements

Development implications of TISA provisions on market access and rules for both participants and non-participants, and for the multilateral trading system, need careful assessment. While existing estimates suggest that TISA would lead to a potential increase in bilateral exports of $78 billion, such an assessment would need to factor in the existence of RTAs among TISA participants. Chile has services RTAs with 17 of the 23 TISA participants, and Colombia, Mexico, Peru, the United States and the European Union each have RTAs with at least 9 TISA participants. The weight of TISA in total exports of individual countries would decrease accordingly if trade between the county pairs that already have services RTAs were excluded. While TISA participants accounted for 74 per cent of Canada’s total services exports, for instance, this could decrease to 19 per cent, and for the United States, the share would decrease to 42 per cent from 61 per cent. Further, plurilateral requests under the Doha Round suggest that the overall export interests of TISA participants may lie primarily with non-TISA participants.

Source: J Marchetti and M Roy (2013). The TISA initiative: An overview of market access issues. Staff Working Paper ERSD-2013-11. WTO.

13. Services have become a major feature of twenty-first century RTAs that are oriented towards deeper and comprehensive integration with a strong regulatory focus, in part to facilitate trade through global value chains. These RTAs address behind-the-border measures encompassing services, investment, competition policy, capital movement, intellectual property rights, government procurement, standards, labour and environment. As of July 2013, 575 RTAs were notified to WTO; of these, 379 were in force and 129 had been notified under article V of GATS. Of the RTAs notified since 1985, some 60 per cent of those formed by developed countries and 55 per cent of those formed by developing

countries contain services (table 2). While only six services RTAs had been notified to WTO before 2000, over 100 additional agreements have been notified since then.

Table 2
Services in post-1985 regional trade agreements

	With developed countries			*With developing countries*			
	Yes	*No*	*Share*	*Yes*	*No*	*Share*	*Total share*
Developed countries	7	5	58%	55	35	61%	60%
Developing countries							
Latin America	22	2	92%	39	5	89%	90%
Asia	17	1	94%	27	14	66%	75%
Africa and Middle East	2	13	13%	0	21	0%	6%
Transition economies	0	0	-	0	31	0%	0%
Total	**41**	**16**	**72%**	**66**	**70**	**49%**	**55%**

Source: UNCTAD based on WTO data.

14. Particularly notable is the emergence of two “mega” RTAs – the Trans-Pacific Partnership Agreement (TPP) and the Transatlantic Trade and Investment Partnership between the European Union and the United States (TTIP). Given their sheer size and ambition, they are seen as a “game changer” in the quest by countries for greater economic integration. The proposed TPP among 12 countries would create a regional market with 40 per cent of world GDP and 24 per cent of world exports and might pave the way towards a region-wide Asia–Pacific free trade agreement (FTA), together with a regional comprehensive economic partnership under negotiation between the Association of Southeast Asian Nations (ASEAN) and its six trading partners. The future TTIP would create the world’s largest market, representing about half of world GDP and one-third of global trade. Consequently, RTAs are expected to cover 60–70 per cent of total services exports for the United States.

15. Developing countries have also embarked on regional services liberalization. A growing number of North–South RTAs, often bilateral in scope, have extended the reach of liberalization to services for developing countries. Of note are ongoing negotiations towards economic partnership agreements (EPAs) between African, Caribbean and Pacific countries and the European Union that replace previous unilateral preference-based relationships with reciprocal preferences (e.g. the Caribbean Forum of African, Caribbean and Pacific States–European Union EPA).

16. Consolidation and expansion of existing South–South regional initiatives, including by linking up with larger or developed country partners, are being pursued often based upon the notion of developmental integration by combining market opening with building productive capacity and infrastructure. ASEAN is headed towards the formation of an ASEAN economic community by 2015. The China–ASEAN FTA has emerged as the world largest RTA, comprising one-third of the world’s population and 13 per cent of world GDP. Africa now aims at boosting intra-African trade by fast-tracking the establishment of a continental pan-African FTA by 2017. The continental FTA builds upon the existing tripartite FTA initiative among the East African Community (EAC), the Common Market for Eastern and Southern Africa (COMESA) and the Southern African Development Community (SADC) through which advanced efforts are ongoing to deepen services integration. The Greater Arab Free Trade Area provides a platform for services liberalization, and the Gulf Cooperation Council has advanced in establishing a common

regulatory framework. In Latin America, the Common Market of the South (MERCOSUR), the Andean Community and the Caribbean Common Market have moved towards deeper integration.

III. Liberalization of infrastructure services sectors under regional trade agreements

Regional liberalization of infrastructure services sectors

17. ISS are subject to a series of regulatory measures that could have a trade restrictive effect from an exporter’s perspective. Any trade-restrictive effect, however, needs to be weighed against the legitimate public policy goals the measures are expected to address. Many countries have anchored their development strategies upon progressive liberalization of services, including on an autonomous basis, to such a degree that the applied regime is often more open than the formal regime “bound” in GATS or even RTAs. The recent initiative by China to substantially liberalize services trade in the China (Shanghai) Pilot Free Trade Zone using a negative list approach, covering 18 subsectors in six key sectors excluding banking and ICT services, is a case in point. Regional liberalization of services attempts to reduce gaps between bound and applied levels of trade policy regimes for services and go further to induce liberalization of applied services trade barriers.

Box 2. Relative restrictiveness of applied services measures

Recent research efforts have explored methods to quantify the perceived restrictiveness of measures applied to services sectors. Table 3 reports the relative restrictiveness of measures affecting ISS and professional services based on the World Bank’s Services Trade Restrictions Index. Overall, the highest restrictiveness is typically found in professional services. This arises from the fact that the provision of professional services depends on mode 4, which is subject to both immigration-related regulations and licensing and qualifications. Indeed, mode 4-related barriers appear to drive the higher restrictiveness in professional services.

Table 3
Average services trade restrictions index

	Overall	Mode 1	Mode 3	Mode4
Financial	22.3	32.4	21.5	na
Professional	48.3	28.3	40.1	60.3
Telecom	26.7	na	26.7	na
Transport	31	28.6	31.8	na

Source. UNCTAD calculation based on the Services Trade Restrictions Index.

In contrast, it is counter-intuitive that financial services appear to be the least-restrictive sector with regard to foreign competition. On average, countries restrict mode 1 more stringently than mode 3. This may reflect the concern of regulators that openness to cross-border trade in banking services implies allowing capital mobility.

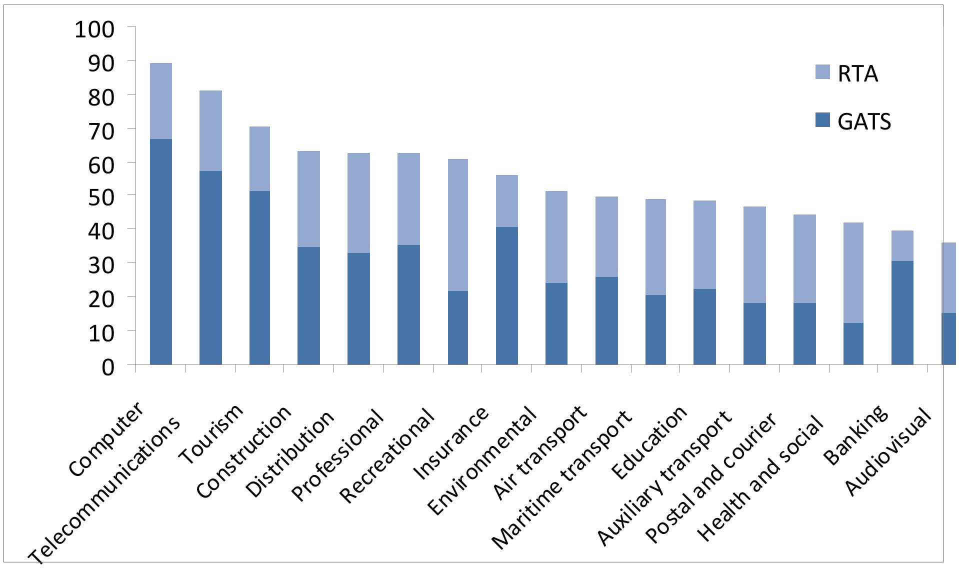
18. At the multilateral level, the extent of trade openness differs across sectors, reflecting competition in domestic markets. GATS commitments on ISS are high in telecommunications, with 108 countries having made commitments, and low in the energy sector. Transport services are in the middle, with 38 countries having made commitments in

international maritime freight transport. Under the Doha Round, improvements were proposed in the 71 initial and 31 revised offers as well as at the Signalling Conference. RTA commitments on services generally go beyond the commitments made under GATS and Doha Round offers.

19. The level of GATS and RTA commitments varies across sectors (figure 5). The computer and telecommunications sectors appear as the most open of all services sectors under GATS and continue to see further liberalization under RTAs. Three transport subsectors (maritime, air and auxiliary) generally receive a particularly low level of GATS commitments among all ISS, but see relatively significant improvements under RTAs. In contrast, financial services exhibit a relatively high level of GATS commitments but see the least improvements in an RTA context, particularly in banking. This may be because the scope for preferential treatment is greater in transport services, for which geographical proximity or special bilateral relationships matter, than in financial services for which preferential treatment might give rise to regulatory arbitrage.

Figure 4

Average indices of commitments under the General Agreement on Trade in Services and regional trade agreements for all countries

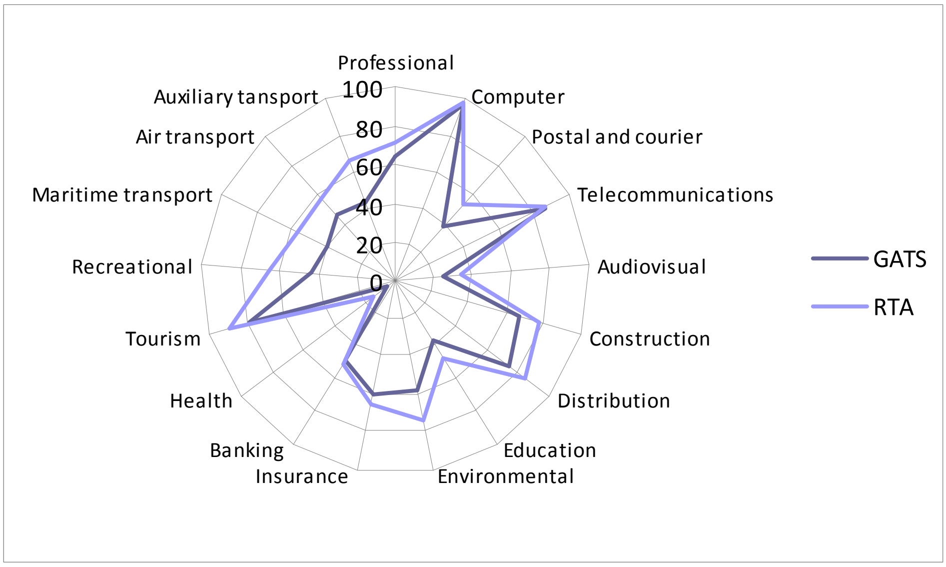


Source. UNCTAD calculation based on WTO data set of services commitments in RTAs.

20. For developed countries, RTA commitments represent only limited improvements from their GATS commitments although these countries generally register a higher level of GATS commitments than developing countries (figure 6). Virtually no GATS-plus commitments are registered in the computer, telecommunications and financial (banking) sectors while modest improvements are notable in transport.

Figure 5

Average indices of commitments under the General Agreement on Trade in Services and regional trade agreements for developed countries

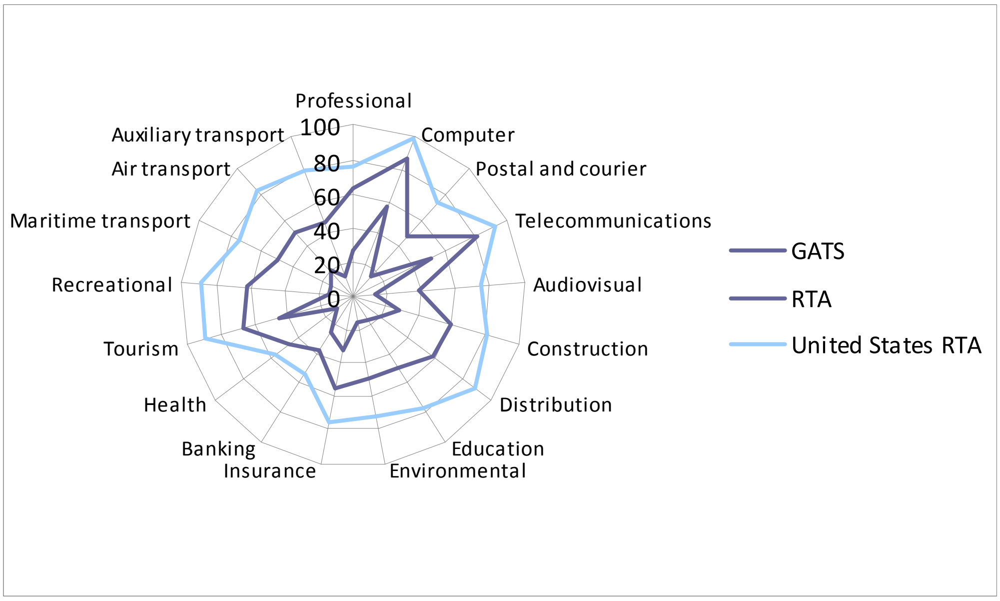


Source: UNCTAD calculation based on WTO data set of services commitments in RTAs.

21. In contrast, in developing countries RTAs appear to have exercised a stronger effect in inducing liberalization. The level of RTA commitments is significantly higher than GATS commitments in all sectors (figure 7). This is partly owing to the fact that developing countries' initial GATS commitments are relatively low, although some have inscribed deep commitments, especially WTO-acceding countries. However, this may also be explained by the asymmetric bargaining structure of North–South RTAs. Figure 7 shows a particularly high level of openness achieved in all sectors for those developing countries that have concluded RTAs with the United States, including in those often considered sensitive, such as postal and courier, transport, professional and financial services.

Figure 6

Average indices of commitments under the General Agreement on Trade in Services and regional trade agreements for developing countries



Source: UNCTAD calculation based on WTO data set of services commitments in RTAs.

Note: The United States RTA includes Bahrain, Chile, Colombia, Costa Rica, the Dominican Republic, El Salvador, Guatemala, Honduras, Jordan, Morocco, Nicaragua, Oman, Panama, Peru, the Republic of Korea and Singapore.

22. Going beyond formal commitments, whether and to what extent GATS and RTA commitments have led to the liberalization of applied levels of services barriers is difficult to gauge quantitatively. An alternative is to examine the implementing legislation that countries enact for their RTAs. For instance, research has found that under the United States–Central American FTA, whereas Guatemalan implementing legislation made 16 amendments to the country's services laws (especially in telecommunications), United States implementing legislation did not amend any laws, implying that the United States services commitments amounted to removal of the difference between bound and applied levels of services measures while the Guatemalan commitments required real liberalization.

Examples of regional trade agreement commitments

23. Specific commitments of individual countries appear to corroborate broad patterns of RTA liberalization of ISS as observed above. Under the Morocco–United States FTA, for instance, Morocco has made bindings in mode 1 in 94 subsectors (66 per cent of the total) and 80 subsectors in mode 3 (53 per cent). In telecommunications, Morocco made full commitments while its GATS commitments excluded private leased circuits. On insurance, United States life and non-life insurance companies were allowed to establish branches within four years and to supply marine, aviation and transport insurance on a cross-border basis within two years. Under the Bahrain–United States FTA, Bahrain made full commitments although its GATS commitments were limited to telecommunications. On financial services, Bahrain committed to phasing out local presence requirements for mode 1 within seven years and allowed United States insurers to acquire new non-life insurance licences without restrictions.

24. The Republic of Korea and European Union FTA and the Republic of Korea and United States FTA are often regarded as prototypes of emerging twenty-first century high-standard RTAs. Both agreements improved market access conditions on legal, financial, transportation and telecommunications services. In telecommunications, the Republic of Korea allowed European Union and United States providers to own, in principle, 100 per cent of the voting shares of Korean-based providers of facility-based public telecommunications services within two years. In insurance, the Republic of Korea agreed to open its markets for direct insurance in maritime shipping, commercial aviation and international transport of goods. In banking, the Republic of Korea allowed European Union and United States financial institutions to provide and transfer financial information and data across their borders and provide advisory services. Unique to the Republic of Korea and United States FTA, financial service providers are allowed to provide through mode 3 all existing financial services and any new ones, while mode 1 service providers are limited to pre-selected financial services. In legal services, European Union and United States law firms will be allowed to open representative offices and later to form joint ventures with Korean law firms.

25. South–South RTAs have achieved significant GATS-plus commitments in ISS. Under the ASEAN Framework Agreement on Services, GATS-plus commitments were made on transport, especially on air, rail and road transport, whereas ASEAN members had made limited or no GATS commitments. The negotiations led to improvements on six air transport subsectors (e.g. aircraft repair and maintenance, selling and marketing of air transport services) with a foreign equity ceiling of 40–51 per cent. In the energy sector, GATS-plus commitments were made in services related to energy manufacturing, including electricity, and services incidental to energy distribution with equity limitations of 40–70 per cent. In telecommunications, improvements were made by raising the equity limit to 49–70 per cent.

26. In Africa, ongoing regional integration processes – COMESA, EAC and SADC – have generally identified ISS as priority areas for liberalization. For instance, EAC negotiations have led to a substantial GATS-plus opening while the level of initial GATS commitments by EAC countries was relatively modest (table 4). In communications, Kenya streamlined its GATS commitments with a 30 per cent equity limitation. In financial services, all EAC countries took commitments on both banking and insurance services with only a few limitations listed (e.g. a residence requirement for bank managers). In transport, substantial improvements were made with subsector coverage extended, including to services auxiliary to all modes of transport. Kenya deepened its GATS commitments by fully liberalizing mode 3 for air and road transport.

Table 4
Liberalization under the East African Community and the General Agreement on Trade in Services

Countries	*Sectors committed in EAC (out of 7)*	*Subsectors committed in EAC (out of 140)*	*Percentage of liberalized commitments in EAC*	*Percentage of liberalized commitments in GATS*
Burundi	7	89	59 %	18 %
Kenya	7	67	42 %	31 %
Rwanda	7	105	74 %	6 %

Countries	*Sectors committed in EAC (out of 7)*	*Subsectors committed in EAC (out of 140)*	*Percentage of liberalized commitments in EAC*	*Percentage of liberalized commitments in GATS*
United Republic of Tanzania	7	56	37 %	≤ 1%
Uganda	7	102	72 %	7%

Source: P Kruger (2011). Services negotiations under the tripartite agreement: Issues to consider. Working Papers, 15 June. Trade Law Centre. Stellenbosch, South Africa.

27. SADC's ongoing services negotiations under its Protocol on Trade in Services, to be completed by 2015, focus on six priority sectors (communications, construction, energy, financial services, tourism and transport). The negotiations seek to address asymmetries in the level of development of diverse SADC countries. Among the key issues are measures to facilitate mode 4 trade and mode 3, including ownership forms, rules of origin and competition issues. Parallel EPA negotiations with the European Union have raised the issue of how intra-SADC liberalization focusing on six sectors will compare with the possible EPA, where liberalization in "substantially all" services sectors would be required under article V of GATS, and how preferential services treatment under SADC will relate to that under the EPA.

28. In Latin America, MERCOSUR seeks to further deepen services liberalization based on a positive list by 2015. GATS-plus commitments have been made on telecommunications; the remaining restrictions include limitations on the number of providers, ownership limitations and economic needs tests. Commitments on maritime, air, road and railroad transport also went beyond GATS with some limitations remaining on short-sea shipping, ownership restrictions and nationality limitations. The Andean Community has adopted a negative list approach. The remaining non-conforming measures often pertain to nationality requirements, ownership restrictions and monopolies in transport and energy services.

Issues in regional trade agreements

29. Different liberalization approaches used under RTAs could have different implications for the extent of liberalization and regulations in ISS. The negative list approach is often associated with the United States' North American Free Trade Agreement model. This model deals with cross-border services (i.e. modes 1 and 2 and some aspects of mode 4) in one chapter, while dealing with investment in both services (i.e. mode 3) and goods in a distinct chapter on investment. The negative list differs from the positive list approach used in the GATS model in that all sectors are assumed to be covered unless they are explicitly restricted through some exemption. Restrictions in all sectors are assumed to be removed unless a reservation is explicitly listed. It thus requires full knowledge of the measures in place in all sectors and detailed scheduling of existing non-conforming measures that limit market access or national treatment. Any measures not scheduled could result in inadvertent liberalization.

30. In contrast, with the positive list approach, liberalization commitments only apply to sectors that countries decide to schedule and are subject to any limitations and conditions that may be attached. It thus allows more flexibility, especially for those countries that face constraints in devising sectoral regulations and identifying applicable non-conformity measures. Once full market access commitments are made, however, countries cannot maintain restrictions, including number of suppliers, ownership restrictions and forms of establishment. Therefore, it is possible that both positive and negative approaches lead to

the same degree of liberalization, and the ability of RTAs to achieve an ambitious outcome does not necessarily depend on a specific scheduling approach, but rather on the parties' commitment to that goal within a specific time frame.

31. Recent RTAs have introduced innovations for triggering deeper liberalization. For instance, commitments may be based on applied levels of market access conditions, including through standstill requirements, i.e. not allowing countries to decrease the conformity of the measure with respective obligations, and a "ratchet" clause that provides for automatic incorporation of further future liberalization measures. National treatment may be applied on a horizontal basis to all sectors and modes. A "(third-party) most-favoured nation" clause increasingly incorporated in recent RTAs, as opposed to the GATS most-favoured nation principle, has the objective of ensuring that an RTA party obtains the best possible preferential treatment available from other RTA partners. Applied under North–South RTAs, this has raised concern that the clause could dissuade a party from engaging in ambitious market opening with a third party, including under South–South RTAs. The development implications of such liberalization instruments warrant careful assessment.

32. Sector-specific regulatory disciplines and liberalization modalities, often targeting ISS, feature prominently in recent RTAs such as those on telecommunications. The disciplines are often based on the GATS Reference Paper on basic telecommunications. The Republic of Korea and European Union FTA provides for commitments on non-discriminatory access to basic telecommunication networks and communication platforms for value added services. The ASEAN, Australia and New Zealand FTA extended the GATS Reference Paper on basic telecommunications to add new definitions and disciplines, including a definition of facilities-based suppliers and the obligations of major domestic suppliers to provide least-circuit services and co-location of equipment. The European Union and the United States agreed in 2011 on the Trade Principles for Information and Communication Technology Services, including on network access and use, cross-border information flows, use of spectrum and interconnection, which may inform TTIP negotiations.

Box 3. Regulatory issues in telecommunications

Some emerging regulatory issues for telecommunications are relevant to future liberalization and regulatory cooperation. The network neutrality issue arises as broadband access providers may discriminate against certain services, applications or content, when they manage data traffic to avoid congestion. Increased demand for broadband applications has accentuated the scarcity of spectrum. Regulators seek to sustain growth in mobile data traffic and manage spectrum more effectively. The high prices of international mobile roaming arise from high wholesale prices under the responsibility of regulatory authorities in countries visited by users and point to the need for international cooperation. Ensuring privacy and data security is a critical challenge for cloud computing as company data are no longer stored on company property and may be in a different country.

Source: International Telecommunication Union (2013). *Trends in Telecommunication Reform 2013.* Geneva.

33. RTAs deepen regulatory disciplines in financial services, often building upon the GATS Understanding on Commitments in Financial Services and addressing such issues as prudential carve-out, standstill, new financial services and anti-competitive practices. Concerns exist that "standstill obligations" may effectively lock in an existing level of regulations and limit future re-regulations as they pertain to commitments. The obligation to allow new financial services by any foreign suppliers through mode 3 may run counter to

the increased regulatory attention given to financial product safety, unless adequately designed.

34. Developing countries have proved to be cautious in making commitments in banking through mode 1. This may reflect the concern of regulators that, first, mode 1 liberalization may create more risks as it is easier to exercise regulatory control over banks established within their jurisdiction. This also explains recent trends of regulators requiring commercial establishment through subsidiaries, rather than branching, as allowing branching would imply accepting home-country regulations, including on capital adequacy requirements. Second, mode 1 commitments require an open capital account as capital should be permitted to flow freely to the extent that such capital is essential to the provision of the services concerned (e.g. cross-border deposit taking). For example, India and China have not made commitments for mode 1 trade in most banking services.

Box 4. Financial regulatory reform

Ongoing financial regulatory reforms are aimed at reducing the probability of a future crisis and mitigating costs by shifting the regulatory focus to macroprudential objectives. The central reform agenda is to strengthen bank capital and liquidity standards under Basel III, scheduled to be introduced between 2013 and 2019, and improve the ability of banks to cover losses. A recent major development is the approval in December 2013 of the "Volcker rule" in the United States which prohibits deposit-taking banks from engaging in most forms of proprietary trading, in order to curtail the perceived implicit government guarantee on deposits from being applied to proprietary trading. The United Kingdom of Great Britain and Northern Ireland is introducing a more restrictive "ring-fencing" of retail banking from investment banking by requiring that all investment banking be conducted by a separate subsidiary with independent governance and its own extra capital. In the European Union, steps have been taken towards a Banking Union, including a Single Resolution Mechanism which aims at mitigating the impact of bank failures on the financial system and Capital Requirements Directive IV, applicable as of 1 January 2014, which has transposed the Basel III capital requirements.

35. Sector-specific regulatory disciplines of RTAs on international maritime transport, postal and courier services and express delivery have sought to ensure free and fair competition by guaranteeing access to essential facilities (ports), pre-empting cargo-sharing arrangements and prohibiting cross-subsidization that may arise from a national postal monopoly when they compete with private suppliers such as express delivery services. National maritime cabotage and air traffic rights in air transport are usually excluded from RTAs as well as under GATS.

Box 5. World Trade Organization Agreement on Trade Facilitation

The new WTO Agreement on Trade Facilitation is likely to affect trade in transport and logistics services, particularly express delivery. The Agreement clarified existing disciplines on customs procedures regarding transit, fees and formalities, and administration of trade regulations. It introduced new binding commitments including on pre-arrival processing, authorized operators and expedited shipments. Freedom of transit through pipelines (oil) and road freight transport (trucks) were proposed but not included in the Agreement. Developing countries were provided with flexibility to self-designate and implement different commitments either immediately or subject to pre-determined transition periods or subject to the provision of capacity-building support and capacity acquisition.

36. Mode 4 commitments under North–South RTAs tend to be closely associated with mode 3 in that enhanced commitments typically apply to “key personnel” (business visitors, intra-corporate transferees, managers), graduate trainees and business services sellers associated with commercial presence and not to contractual services suppliers and independent professionals delinked from mode 3. This was the case with the Republic of Korea and European Union FTA and the ASEAN, Australia and New Zealand FTA. A key stumbling block in liberalization in mode 4 has been its linkage with immigration and labour market policies. Regulatory cooperation, including to facilitate temporary movement of labour, has been pursued under some RTAs. ASEAN, for instance, addresses temporary entry and stay and recognition of qualifications. The United States and Chile and the United States and Singapore FTAs provided for numerical limits on the annual allocation of temporary entry visas for business persons (e.g. 5,400 annual applications for Singapore), which however were envisaged within established United States visa programmes and led to concern over their relationship with GATS commitments.

37. Regulatory harmonization and mutual recognition could remove barriers arising from diverse licence and qualification requirements. Such regulatory cooperation is more feasible among countries with similar levels of development and regulatory preferences. RTAs typically seek to reduce regulatory discretion by requiring that such measures not be more trade restrictive than necessary (“necessity test”). Recent RTAs have often set up an institutional framework through which relevant professional bodies are encouraged to develop criteria for mutual recognition for the authorization, licensing, operation and certification of services suppliers and to negotiate mutual recognition agreements.

Box 6. Mutual recognition agreement on professional services

In the European Union, the 2013 Professional Qualifications Directive created a “European professional card”, an electronic certificate issued by a professional’s home country to facilitate automatic recognition in the country of destination. ASEAN has signed 7 mutual recognition agreements covering, inter alia, architectural, accountancy and engineering services. The agreements on engineering and architectural services create the concept of “registered ASEAN professionals” to whom recognition is provided in participating countries. The Asia–Pacific Economic Cooperation forum has created its own Business Travel Card to facilitate the movement of business people and allow pre-cleared, facilitated short-term entry to participating member economies.

38. Beyond liberalization, emerging twenty-first century RTAs are shifting their focus towards regulatory harmonization to reduce divergence in national standards. Proposed disciplines under the TPP include regulatory coherence, whereby each member will be required to have a mechanism to facilitate central coordination and review new “covered regulatory measures” so as to promote convergence towards good regulatory practice, including impact assessments of a regulatory measure.

39. International disciplining of national regulatory processes and frameworks through essentially trade-liberalizing processes under RTAs has prompted concern over the possible adverse effect on national regulatory autonomy. Investor–State disputes being increasingly incorporated into RTAs is a case in point. Investor–State disputes might confer greater rights to foreign investors and lead to “regulatory chill” as regulators might refrain from taking certain regulatory actions (e.g. environmental regulations) for fear of a legal challenge under Investor–State dispute mechanisms, given that many disputes have concerned ISS (e.g. telecommunications, energy). Another example concerns proposed disciplines on the potentially anti-competitive effect of State-owned enterprises that tend to

receive some preferential treatment including preferential finance. Some regional disciplines have sought to establish “competitive neutrality” between State-owned enterprises and private companies by eliminating such structural advantages. Developing countries have stressed the importance of State-owned enterprises in delivering public policy goals, including in energy, telecommunications, postal and courier and financial services.

40. The asymmetric bargaining structure of North–South RTAs, especially in services where developing countries face particularly significant productive and regulatory capacity constraints, points to the importance of equipping such RTAs with operational special and differential treatment provisions, productive capacity-building commitments and cooperative facilities.

IV. Regional regulatory and economic cooperative schemes

41. Liberalization is only one aspect of regional integration processes. It is often accompanied by various forms of regulatory cooperation. Such cooperation, including harmonization and mutual recognition, has proved to be more feasible among neighbouring countries with similar levels of development. Regional regulatory institutions and coordination mechanisms – such as the Eastern Caribbean Telecommunications Authority, South Asian Telecommunication Regulators’ Council and Southern Africa Telecommunications Association – have been instrumental in such cooperative schemes.

42. RTAs have also acted as platforms for the development of regional transport and infrastructure networks and the connectivity essential for provision of ISS. Such cooperative initiatives, along with liberalization, have proved to be essential components of developmental regionalism.

Energy

43. Regional cooperation in the energy sector typically aims at optimizing regional provisions of energy, including by creating common regional infrastructure and facilities essential for the provision of electricity and gas. ASEAN adopted the ASEAN Plan of Action for Energy Cooperation 2010–2015 to harmonize regulatory frameworks regionally and expedite the implementation of cross-border power interconnection and trade, to harmonize technical specifications for the ASEAN Power Grid and to promote renewable energy and energy efficiency. The ASEAN Power Grid project seeks to meet the increasing demand for electricity and enhance access to energy services by facilitating cross-border trade in electricity, enhance generation capacity and stimulate reserve sharing schemes. The Trans-ASEAN Gas Pipeline is another example of joint infrastructure building to ensure energy security.

44. In Latin America, regional development institutions have prioritized infrastructure building, including energy and transport. For instance, the South American Infrastructure and Planning Council, under the Union of South American Nations, implements projects focused on electrical interconnection and transmission lines. Similarly, ongoing projects of the Fund for Structural Convergence of MERCOSUR support electrical interconnections, transmission lines and substations in the subregion. The Andean Community has set up a regulatory framework for regional interconnections with a view to the future Andean Electrical Interconnection System.

Box 7. The Central American Electrical Interconnection System

The energy sector in Central America is marked by asymmetries in size and resource endowment. Central American countries face the challenge of oil supply whereas Mexico and Colombia have larger energy reserves. There is therefore great potential for energy integration to optimize the regional energy supply. The Central American Electrical Interconnection System introduced a transmission line that covers all Central American countries providing an interconnection with Mexico and Colombia. The 230 kV transmission line is 1,800 km long, with 15 substations, and will allow for 300 MW exchanges among the countries. It will allow for energy flows in a regional electricity market, and transactions will include contract and spot markets.

45. The energy sector presents a major challenge for sub-Saharan Africa. The average price of power is double that in other developing regions, and less than 30 per cent of the population has access to electricity. The formulation of regional energy policy and harmonized regulatory frameworks has been found essential to overcoming such bottlenecks. SADC seeks to enhance interconnection for cross-border transmission (e.g. the Angola–Namibia interconnector) to implement the SADC Protocol on Energy. The Southern African Power Pool has been created to provide reliable and economical electricity by promoting regional multi-country competitive electricity trade to foster regional integration.

Transport

46. In the transport sector, cooperation has centred on extending regional transport networks and cross-border connectivity. ASEAN is making sustained efforts to facilitate cross-border road transport. The ASEAN Framework Agreement on the Facilitation of Inter-State Transport (2009) further advanced this objective. The Agreement expanded market access by setting the maximum number of vehicles to be used by transport operators established in an ASEAN country for inter-State transport (500 vehicles per party) and sets out regional regulations, including on inter-State transport routes, harmonized road transport permit requirements and mutual recognition of vehicle inspection certificates.

Box 8. China–ASEAN cooperative scheme

The Greater Mekong Subregion Economic Cooperation Programme launched in 1992 places ISS among its five strategic areas and is now considered an important complement to the Framework Agreement on Comprehensive Economic Cooperation between ASEAN and China. Under the programme, six member countries share the costs of building hard infrastructures. The bridge straddling the Mekong River between Thailand and the Lao People’s Democratic Republic, operational since December 2013, signalled the completion of physical work along the Greater Mekong Subregion North–South Economic Corridor and connects China, the Lao People’s Democratic Republic, Myanmar and Thailand. As regards energy, power grid connectivity and power trading among neighbouring countries are the focus of cooperation. To utilize river water resources in Myanmar, China supported the country’s building of the Shweli River Hydropower Station through a build-operate-transfer project and connected it to the China Southern Power Grid, which enabled Myanmar to export power to China.

47. In Latin America, the Andean Community has developed regional initiatives on transport (road, maritime and air). Ongoing transport projects implemented by the South

American Infrastructure and Planning Council focus on road infrastructure and border crossings, while the Fund for Structural Convergence of MERCOSUR supports road and railroad infrastructure. In Central America, the Mesoamerica Project has supported the development of road transport and connection through the International Mesoamerican Road Network.

48. In Africa, the COMESA-EAC-SADC Tripartite Initiative is having a notable effect on inducing convergence of subregional transport policies and institutional frameworks. Such convergence may be observed in the development of subregional transport policies and strategies in COMESA, EAC and SADC. COMESA's transport policy, developed in 2010 under the COMESA Transport and Communications Strategy and Priority Investment Plan, encouraged its members to incorporate regional dimensions in their national policies. The EAC Transport Strategy developed later in 2011 incorporated the COMESA Strategy and Plan, adopting same regulatory principles in respect of physical infrastructure and harmonized regulatory regimes.

49. Regional transport corridors have occupied a central place in transport cooperative schemes in Africa. The recent economic corridor approach has enlarged the scope of operation to cover construction, maintenance and rehabilitation projects and trade facilitation measures by tackling regional transport routes as a means of stimulating social and economic development in the areas surrounding the route (e.g. the North–South Corridor Aid for Trade Programme). Studies have found that quality-driven logistics services are particularly important for the effective functioning of regional corridors. Furthermore, several regional economic communities have adopted the model of the one-stop border post as a key trade and transport facilitation measure to reduce the time spent, and costs involved in, border crossings.

Telecommunications

50. In telecommunications, particular emphasis has been placed on regional interconnection, spectrum management and broadband infrastructure building. ASEAN is working on seamless provision of telecommunication services through the implementation of the ASEAN ICT Master Plan 2015. Recognizing the importance of universal access to ICT, ASEAN has enhanced ICT cooperation on broadband, information security and ICT adoption by small and medium-sized enterprises to bridge the ICT development gap across the region, for example through efficient spectrum management.

51. In Latin America, the Andean Committee of Telecommunications Authorities and the Andean Community promote the integration of telecommunications, including roaming services in border areas and broadband development. Ongoing development projects in the Andean hub have aimed at building synergies between existing infrastructure and new fibre optical investments. In Central America, the Mesoamerican Information Highway is being developed as a technological platform to improve broadband connectivity. The Highway includes an optical fibre backbone and supplementary optical fibre networks that connect the backbone with the subregion's main cities.

52. In Africa, the New Partnership for Africa's Development e-Africa Programme has supported policies and projects since 2001 at the continental level for ICT development. Among the key projects are the ICT Broadband Infrastructure Network for Africa and the e-Schools Initiative which help African countries to connect internationally through existing and planned submarine and terrestrial cable systems and enable trade, social and cultural interchange to take place with ease and affordability. The East Africa Submarine System has developed a submarine cable along the East Coast of Africa and is expected to provide better connectivity to the region.

Financial services

53. Regional cooperation in financial services has centred on the creation of regional financial infrastructure and institutions to support regional regulation and integration of financial systems and development finance. In Africa, efforts are being made to establish a West African Monetary Zone payment system to prepare for a single currency for West African countries. In Europe, the Single Euro Payments Area (2010) is intended to increase efficiency in handling cross-border electronic euro payments for its 33 members.

54. In Asia, ASEAN together with China, Japan and the Republic of Korea have set up the Chiang Mai Initiative Multilateralization, a liquidity risk-sharing arrangement through $120 billion swap agreements, to reduce the risk of financial crisis. Another initiative – the Credit Guarantee and Investment Facility – seeks to strengthen regional capital markets to provide credit guarantees for local currency denominated bonds. Latin America has created a major institution, the Bank of the South. Together with the Common Reserve Fund of the South and the creation of a monetary unit of the South, the Bank is expected to channel resources towards economic development.

V. Conclusion

55. RTAs have become a key driver of market opening. Services RTAs have been driven by developed countries with the export capacity of competitive services, and emerging large RTAs will soon encompass the majority of world trade with important implications for the multilateral trading system. A growing number of developing countries have joined RTAs while many others, especially those with lower per capita income and weak services capacity, continue to view ambitious RTAs with apprehension. Such a transformation of the international trading system warrants careful analysis to identify how developing country participation in these processes can be best coordinated with their national regulatory frameworks to maximize development benefits of ISS. Assessing the development impact of RTAs is however complex, including owing to the paucity of services data. The pervasive importance of ISS throughout modern economies also makes it difficult to measure precise ways in which RTA liberalization might be reflected in economic outcomes.

56. Reconciling deep liberalization under RTAs and national regulatory processes remains a key policy challenge. New approaches to deep liberalization and regulatory harmonization would have an important bearing on national regulatory regimes and the domestic services industry. Conversely, the extent of regional liberalization has been conditioned by regulatory frameworks. Adequate special and differential treatment under RTAs is particularly important to help developing countries to build competitive services, participate in global value chains and strengthen regulatory and institutional capacities. Regional cooperation in ISS can go a long way to facilitating intraregional trade and accessing markets, as well as enhancing regional infrastructure networks.

57. Taken together, regional liberalization and cooperation in ISS that is adequately coordinated and coherent with national policy and regulatory processes can serve as a catalyst for developmental integration transmitting the benefits of trade integration for inclusive and sustainable development. UNCTAD’s comprehensive work on services, including this multi-year expert meeting, Services Policy Reviews and the Global Services Forum, serves as a knowledge platform that can support developing country efforts in furthering developmental integration through services development and trade.

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Note by the UNCTAD secretariat

Corrigendum

Paragraph 32, line 9

For least-circuit services *read* leased-circuit services