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TRADE IN SERVICES AND DEVELOPMENT IMPLICATIONS

Note by the UNCTAD secretariat*

Executive summary

The services economy and trade in services are becoming more important for the growth and development prospects of developing countries (DCs). The contribution of services to income generation, employment creation, competitiveness, and foreign exchange earnings has significantly increased over the last two decades across countries. Services exports are, however, concentrated in a relatively small number of DCs. The potential of services and services trade is yet to be fully realized by many DCs, particularly African ones and LDCs. Recent research indicates that intraregional services trade accounts for the vast majority of DCs' South–South services trade. Regional trade agreements (RTAs) have proliferated worldwide to become a defining feature of today's international trade policy landscape. Provisions on services, investment and temporary movement of labour are now common in many RTAs. Given the nascent state of the services sector in DCs, the implications of North–South reciprocal market opening in services for DCs' services sectors need to be carefully assessed. Adequate pacing and sequencing between domestic reform, and regional and multilateral liberalization are also important. Support is needed in strengthening analytical, regulatory and institutional capacities of DCs to allow them to benefit from trade in services.

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

I. TRENDS IN THE GLOBAL SERVICES ECONOMY

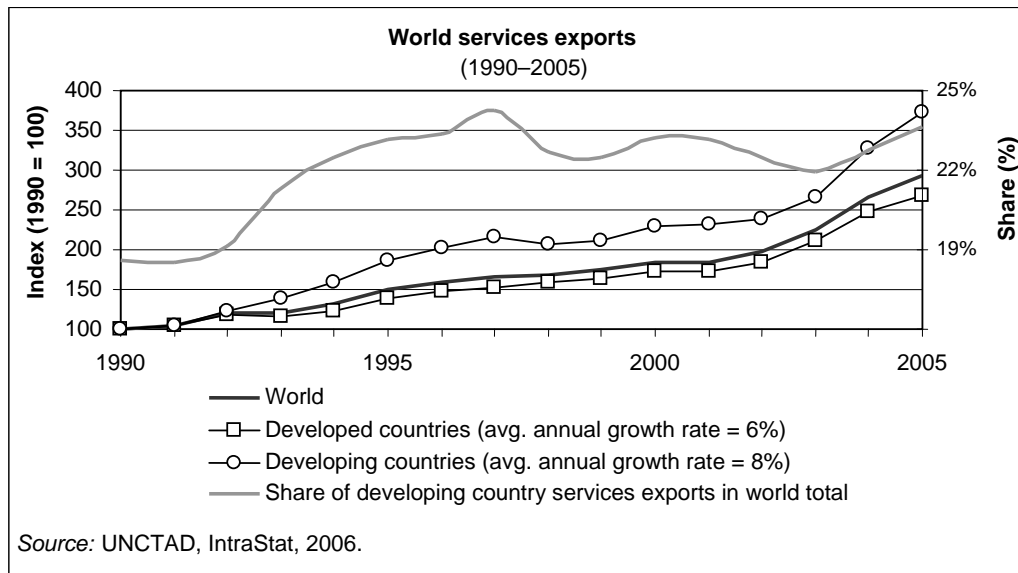
1. The services economy and trade in services are becoming more important for the growth and development prospects of DCs, including in attaining the Millennium Development Goals. Since services are essential inputs into various economic activities, they directly contribute to infrastructure building, greater productivity and the increased competitiveness of an economy. They also have an important social dimension through provision of essential services and universal access. The services economy is still at an early stage in many DCs, while some DCs are already successful in exporting services such as tourism, transport, construction, audiovisual, computer and information services, and business and professional services, particularly through mode 1 (cross-border supply of services) and mode 4 (temporary movement of natural persons).

2. One of the aims of the Doha Round of multilateral trade negotiations is progressive liberalization of trade in services. The slow pace of progress in the Doha negotiations seems to have further strengthened interests in regional approaches, including with regard to services. RTAs have proliferated worldwide to become a defining feature of today's international trade policy landscape. The trend has been particularly pronounced over the past decade. Existing RTAs are reinvigorated and expanded, and new ones, on a bilateral, subregional, regional and interregional scale, are negotiated and concluded on a North–North, North–South and South–South scale, including between RTAs. The number of RTAs notified to the WTO has reached 211. Over half of world trade in goods is conducted under RTAs. As for services, a significant share is estimated now to occur regionally, but the contribution of RTAs to this remains to be assessed.

3. “New regionalism” has wider coverage and scope, and involves deeper commitments relating to behind-the-border measures, of which the liberalization of services is a major component. Of 153 RTAs operational today, some 43 are economic integration agreements in services under Article V of GATS. Liberalization and greater cooperation in trade in services are a driver of regional dynamics. Against this backdrop, the integration of DCs into service trade requires the designing and implementing of appropriate policies and regulatory frameworks, and the building of competitive services supply capacities. Both multilateral and regional negotiations should enable DCs to benefit from fast-growing services trade and contribute to their overall national development. Adequate pacing and sequencing between domestic reform, and regional and multilateral liberalization are also important.

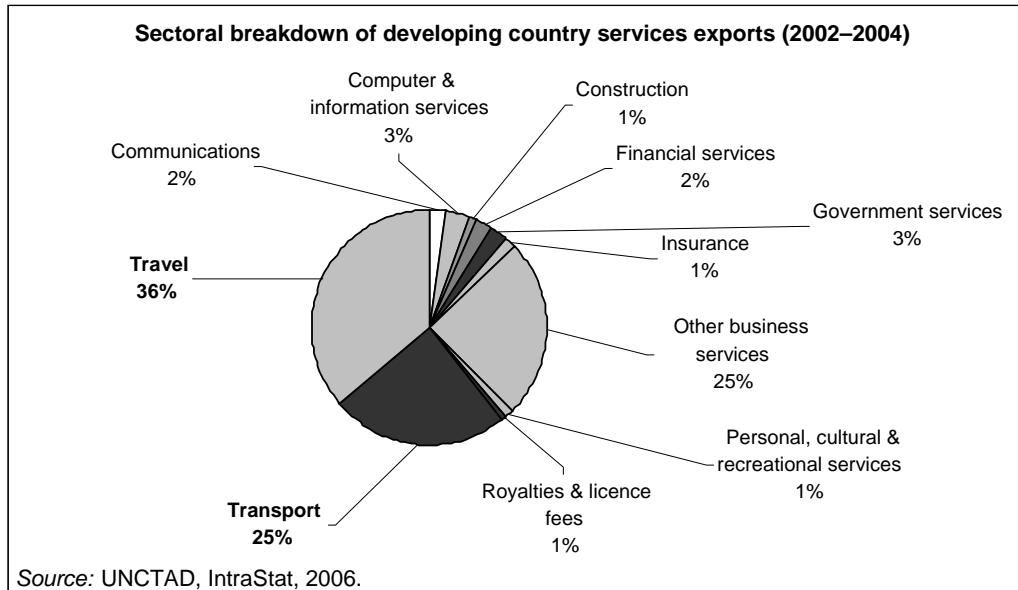
Economic trends

4. Services' contribution to income generation, employment creation and foreign exchange earnings has significantly increased over the last two decades across countries. Since 1990, the share of services in GDP has grown from 65 to 72 per cent in developed countries and from 45 to 52 per cent in DCs. Services now account for over 70 per cent of employment in developed countries and about 35 per cent in DCs. Since 1990, world services trade has nearly tripled to reach \$2.4 trillion, while the FDI inward stock has quadrupled to nearly \$10 trillion against the backdrop of globalized production of goods and services. DCs have outperformed those global trends – Since 1990 services exports from DCs have grown at an average annual rate of 8 per cent compared with 6 per cent for developed countries — and their share of world services exports has increased from 19 to 24 per cent. Annual growth in world services exports has further accelerated over the past five years, with an annual average growth rate of 12 per cent and 13 per cent for developed and DCs respectively.

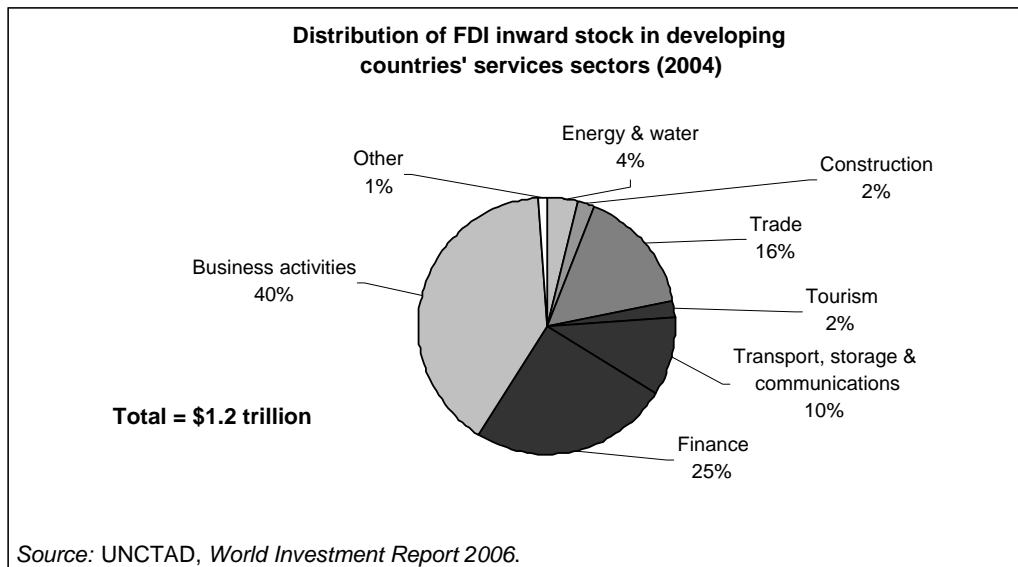


Note: The growth in services exports is indexed to 1990 on the left-hand vertical axis. The share of DCs' exports in total world services exports is plotted along the right-hand vertical axis.

5. Services exports are concentrated in a small number of DCs. DCs in Asia account for 75 per cent of all DCs' services trade, while 10 per cent and 15 per cent are attributable to Africa and to Latin America and the Caribbean, respectively. Over half of developing country services exports originate in only six countries, and the top 15 developing country services exporters account for 80 per cent of all DC services exports. The potential of services trade is yet to be realized by Africa and LDCs. LDCs continue to be marginalized from international flows of services, with their share in world service exports being about 0.8 per cent. Travel and transport continue to represent the major proportion of developing country services exports, while business services, including ICT, financial and insurance services, now account for one third.



6. FDI inflows into DCs increasingly target the services sector. The share of FDI inflows into the services sector in DCs rose from 35 per cent in 1990 to nearly 50 per cent in 2004. Currently at about \$1.2 trillion, FDI inward stock in DCs' services sector is now twice the value of FDI inward stock in their manufacturing sector, and represent 20 per cent of total world FDI inward stock in the services sector.

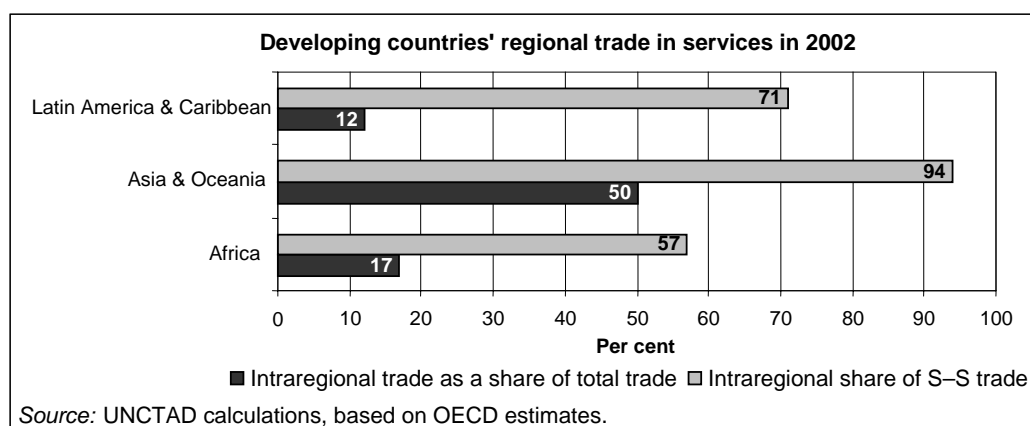


7. DCs themselves have become a major source of those investments. Their total FDI outflows to DC's services sectors rose from only \$2 billion in 1990 to nearly \$30 billion in 2004. A major share of those outflows is at the regional level, including through mergers and acquisitions. DCs' firms were the purchasers in over 40 per cent of DC services firm

acquisitions between 2000 and 2003. Notwithstanding these trends, developed countries remain the dominant source of FDI outflows to DCs.

Regional trends

8. During the period 1994–2004, growth in intra-RTA merchandise exports in most South–South RTAs has consistently exceeded growth in their merchandise exports to the rest of the world. For instance, for ASEAN, the average growth rate of intraregional exports was 12 per cent compared with 10 per cent for exports to the rest of the world. The same figures for SADC were 18 per cent and 5 per cent, and for MERCOSUR 11 per cent and 8 per cent. Through the extension of the coverage to services, RTAs are expected to generate increased intraregional services trade. A recent study by the OECD indicates that intraregional services trade accounts for most of DCs' South–South services trade, and intraregional services trade accounts for 57 per cent, 71 per cent and 94 per cent of South–South services trade for Africa, Latin America and the Caribbean, and Asia and Oceania respectively. Intraregional services trade is particularly significant in Asia and Oceania, since as much as half of its total services trade is directed to the region. This figure remains below 20 per cent in other DC regions.



9. For DCs, much of regional trade reflects trade in commercial services such as freight transportation, tourism, construction and business services. However, the scope of traded services, and correspondingly the magnitude of services trade flows, is expanding rapidly as countries progressively privatize and liberalize those services traditionally performed as a government function.

II. POLICY ISSUES AND APPROACHES TO SERVICES IN RTAs

10. While motivations for engagement in services RTAs vary across countries, several factors may be identified. First, in cases where regional merchandise trade liberalization is considered successful, countries may be encouraged to extend liberalization to services. Second, services liberalization may be more easily negotiated between a limited set of participants, particularly with economies at similar levels of development with geographical proximity and cultural ties, as they enable a greater degree of reciprocity between regional partners, thus reducing the free-rider problem, than would be possible through multilateral negotiations. Third, recognizing the critical importance of services trade for growth and

development, many countries accelerated regional initiatives in the search for services export opportunities and greater investment attraction.

11. Existing literature suggests a greater likelihood of static and dynamic gains from preferential liberalization of services than would be the case with preferential liberalization in the goods area. The potential of RTAs in promoting liberalization of the temporary movement of services suppliers is particularly significant. Regulatory cooperation on mutual recognition or harmonization of professional qualifications and licensing certification and technical standards, competition, and provisions for labour mobility, could further improve welfare. Furthermore, regional services trade offers a supportive environment for national firms by accelerating learning curves, building supply capacities and enhancing international competitiveness. Regional services trade also plays a catalytic role in generating employment and furthering the development of growing regional services industries and firms. By allowing for economies of scale in the production of services, RTAs may support the development of regional infrastructure in key sectors such as transportation, communications and energy.

12. Gains are expected to be greater from non-preferential than from preferential liberalization, because, among other reasons, the former allows consumers to import from the most competitive sources. Regional liberalization is often sequenced as a transition to multilateral liberalization as it can help strengthen indigenous supply capacities and regulatory effectiveness before they face competition at the global level. Adequate sequencing in the opening of services market could provide long-term dynamic gains. In this sense, RTAs can serve as a “building block” for multilateral liberalization. The sequencing of liberalization particularly matters in those sectors where sunk costs and the incumbent advantages associated with some capital-intensive services are significant, for example infrastructure services, as temporary privileges granted under a preferential RTA may result in preventing the market entry of more efficient suppliers after eventual non-preferential market opening on an MFN basis.

13. Harnessing the potential of RTAs, particularly South-South RTAs, is of interest to DCs as a means to increase national services exports, and to support the broader objectives of stimulating regional growth dynamics and the development of regional supply capacities and infrastructure development, including through cooperative mechanisms aimed at promoting shared regional infrastructure, policy and regulatory cooperation, and skill-sharing and capacity-building. In some North-South RTAs, developed countries provide support through cooperative mechanisms. There is a need to ensure that supportive mechanisms are made effective, particularly in respect of building supply capacities. Instituting effective cooperative mechanisms, and securing resources for such mechanisms, continues to be at the forefront of regional discussions in developing regions.

14. Different RTAs have adopted different approaches to services liberalization. For an assessment of the extent to which RTAs have effectively liberalized trade between partners, it is necessary to examine both the services regime and other commitments under agreements, including provisions on investment, integration of labour markets, government procurement, and recognition of licences, certifications and qualifications. Furthermore, various sectoral regulations are also relevant to services trade liberalization. The combined effect of all those disciplines will define the extent of services trade liberalization.

15. RTAs have adopted distinct approaches in respect of (i) scope; (ii) modalities for liberalization; (iii) depth of commitments; (iv) regulatory cooperation; and (v) other areas of

cooperation. On (i) sectoral and modal coverage, existing RTAs tend to provide for universal sectoral coverage, with the exclusion of sensitive sectors such as air and maritime transport and audiovisual services. Liberalization may be based on a progressive approach with an implementation period, especially for DCs (10 years in MERCOSUR). Some agreements provide for separate treatment of investment (NAFTA-type RTAs, MERCOSUR, EU) and movement of persons (NAFTA). Some sector-specific provisions can also contain a liberalization element, including financial services, air, maritime and land transport, telecommunications, professional services and mode-4-type movement.

16. With regard to (ii) liberalization modalities, RTAs generally follow either a negative or a positive list approach. In the negative list approach, countries list those sectors and modes of supply that they wish to be excluded from the general obligation of not restricting services imports, and remaining restrictions may be subject to negotiated elimination (in some cases with the “ratchet mechanism”, which automatically binds unilateral liberalization of new services under the agreement). The positive list approach consists in listing those sectors and modes of supply to whose liberalization countries commit themselves. This approach can, in theory, provide the same level of liberalization as the negative list approach but provides greater flexibility in designing the scope and pace of liberalization commitments. The negative list approach was adopted in NAFTA-type RTAs (CAN, CARICOM), Europe Agreements and EU–Mexico, while the positive list approach was adopted in EU–Chile, ASEAN, MERCOSUR, CACM, Japan–Singapore and United States–Jordan. The definition of rules of origin for services providers is important in determining the level and depth of regional services liberalization vis-à-vis third country services/suppliers.

17. As regards (iii) the depth of commitments, countries’ regional commitment as well as general and sectoral disciplines provided under an RTA would affect the extent to which RTAs can generate effective services liberalization. Liberalization commitment may result either in standstill or rollback of restrictive measures. This is important, since RTAs can go beyond GATS commitment to provide “preferential” market access conditions for regional partners. A series of measures are included to promote effective market access, including improved transparency obligations. Regarding (iv) regulatory cooperation, domestic regulation measures such as qualification requirements also determine the level of liberalization, since such requirements often constitute important market entry barriers to services trade, for example trade in professional services. Harmonization and mutual recognition are pursued under some RTAs (MERCOSUR, NAFTA (accountancy, architecture, engineering), CARICOM), but often on a best-endeavour basis. RTAs can contain market access commitments in government procurement in services and disciplines regarding ESM, monopoly and competition policy.

III. EXPERIENCES WITH RTAS’ SERVICES LIBERALIZATION

North–North RTAs

18. The EU is the example of deep and far-reaching economic integration. The EEC Treaty of 1957 provided for services trade liberalization as part of the four freedoms (free movement of goods, persons and capital, as well as freedom of establishment). The progress towards a single market for services has been slow compared with trade in goods. Liberalization of services has been pursued progressively through specific sectoral directives (e.g. financial services, telecommunications, liberal professions, transport services, postal services, port and dock services, and energy) and the case law of the European Court of

Justice (ECJ), but numerous barriers remained in some sectors. Implementation has encountered difficulties, for instance in energy and financial services. In 2000, the EU Lisbon Summit called for a removal of cross-border barriers to services trade to achieve a single market in services. Liberalization of services would be expected to increase regional GDP by between 0.3 and 1.8 per cent, and to result in a 0.7 per cent increase in employment, or 2.5 million new jobs created.

19. Trade liberalization in EU is accompanied by regulatory cooperation (sometimes harmonization) in various areas of public policy. EU acknowledges member States' prerogative to pursue legitimate public policy objectives even if they interfere with the four freedoms.

20. The EC treaty does not distinguish between market access and national treatment, which are cornerstones of the GATS legal architecture. All "restrictions", regardless of whether they are discriminatory (such as additional costs or delays), are prohibited. The Services Directive also goes beyond GATS in the requirement for single contact points and in issues related to recognition.

21. "Mode-4-type" movement of services suppliers is provided for as "temporary provision of services without setting up business", and other directives regarding the posting of workers, who usually do not have to apply for recognition of qualifications. Member States must ensure that the employer grants the posted workers core mandatory protections required in the member States where the work is undertaken (e.g. minimum wage, holidays and maximum working periods). Implementation has proved to be difficult, with discriminatory requirements remaining (for example, several EU-15 States employ de facto discriminatory measures or a transition period for the movement of workers from new member States), partly because of concerns about local jobs as a result of the possible inflow of services providers from new member States.

Towards an EU internal market for services

In January 2004, the European Commission presented a draft Services Directive aimed at creating an internal market for services. However, the draft faced criticism spurred by concerns that it would lead to "social dumping" and commercialization of key services (e.g. social services, culture, education, health) and restrict members' capacity to regulate. Moreover, there were fears that the draft Directive would put downward pressure on wage and labour conditions. There was controversy about the "country of origin" principle, under which service providers would be subject to the laws of their country of origin rather than of the country where the service would be provided. Concerns were raised about a "race to the bottom" in social and environmental policies resulting in relocation, increased unemployment and, erosion of social protection. The revised Directive was adopted in autumn 2006, to enter into force in 2010. The most controversial aspect — the "country of origin" principle — was replaced by a provision on the "freedom to provide services". Moreover, provisions on the posting of workers were eliminated; liberalization would not affect national labour law, criminal law or social services; and member States would be free to maintain restrictions on public policy grounds (e.g. public security, social policy, consumer protection, environmental protection and public health), provided that these were "non-discriminatory, necessary and proportional". While the revised Directive would cover services of general *economic* interest, business services, and services provided to businesses and consumers, a number of services areas would remain excluded (e.g., financial, telecommunications, transport, port, health care and certain social services, activities connected with the exercise of official authority, temporary work agencies, gambling and audio-visual services).

South–South agreements

22. South–South RTAs are an important element in developing countries' development strategy regarding their gradual and strategic integration into the world economy. The impetus to include services in South–South RTAs has been growing. UNCTAD is providing technical assistance for such negotiations.

23. In Asia, the impetus to include services in RTAs has been growing, some Asian countries being a global powerhouse in the manufacturing and services. The significant development of regional services capacities to support manufacturing has led to an increase in exports of services. One estimate points to a \$68 billion gain resulting from a 50 per cent reduction in barriers to trade in services, double that from a similar reduction in protection in manufactures and about one fourth more than that from agricultural liberalization. ASEAN was among the first to embark on services liberalization in Asia, with the signing of the ASEAN Framework Agreement on Services (AFAS) in 1995. The South Asia Free Trade Agreement (SAFTA) integrated services liberalization in 2006. Asian countries have become active recently in concluding bilateral RTAs with partners within and outside the region.

ASEAN

The AFAS is modelled on a positive list approach, and commitments have so far focused on the air and maritime transport, business services, construction, financial services, telecommunications and tourism sectors. Commitments in these sectors could be characterized as "GATS plus". The long-term objective of the AFAS is the elimination of restrictions on trade in services among members in all the four modes of service supply. It is built through a three-year cycle of negotiating rounds. By June 2005, four ASEAN packages of commitments had been concluded. Liberalization commitments are complemented by mutual recognition agreements (MRAs) (for professional services, including engineering, accountancy, architecture, surveying and nursing) and cooperative mechanisms, such as for infrastructure development. Among the priority sectors for advanced liberalization are "e-ASEAN" and health-care services; both envisage facilitation of professional mobility in those sectors. Achievements in the liberalization of Mode 4 remain rather limited. Commitments are mostly at the level of GATS. The next step in AFAS liberalization is the establishment of the ASEAN Economic Community (AEC) by 2020 — that is, the free flow of goods and services as provided for in the 2003 Bali Concord II. A High Level Task Force has recommended that (i) clear targets and schedules for services liberalization be set for each sector and round; (ii) services liberalization in specific sectors be accelerated earlier than the 2020 end date through the ASEAN minus X formula; (iii) MRAs for qualifications in major professional services be concluded by 2008; and (iv) capacity-building be undertaken.

24. Most Asian RTAs adopt a GATS approach, which contains provisions on national treatment, market access, modes of delivery and domestic regulation. However, there are notable differences from a GATS approach. For instance, while the schedules of country-specific commitments in most Asian RTAs, such as ASEAN, follow a positive list approach, some Asian FTAs follow a negative list approach (FTAs between the Republic of Korea and Singapore, and the Republic of Korea and Chile). Most bilateral agreements contain well-defined services provisions, including separate chapters for key services sectors. The India–Singapore agreement has separate investment and services chapters with extensive coverage of the movement of professionals, air services and e-commerce. In view of the Philippines' and India's skilled English-speaking workforces, both the India–Singapore FTA and the Japan–Philippines EPA have extensive provisions for the movement of natural persons.

25. After the Uruguay Round, RTAs in *Latin America and the Caribbean* — CARICOM, the Andean Community and MERCOSUR, but not CACM — adopted disciplines for services trade liberalization. Bilateral NAFTA-type agreements (currently 12) have spread throughout the region.

26. The *Andean Community* and *CARICOM* have achieved notable progress in services. In the Andean Community, the regime for the liberalization of trade in services, with a negative list, adopted in 1998, established a standstill obligation and an inventory of restrictive measures that members could maintain during a transition period to full liberalization, to be achieved in 2005. The adoption of the inventory implied significant initial liberalization commitments. Bolivia inscribed only 46 measures, Colombia 75, Ecuador 74 and Peru 20. In 2006, full liberalization of services was adopted. The Andean countries have lifted all measures registered in the inventory except national content in audio-visual services, and the requirement for incorporation under type of company for public services. Bolivia has been granted special treatment until 2009. The Andean experience reveals a process of integration at the subregional level that is deeper than the one so far achieved at the bilateral and multilateral levels. The initial commitments at the subregional level are deeper than the GATS commitments and the offers in the GATS negotiations; and in the case of national treatment they exceed the commitments of Colombia and Peru in the bilateral FTAs with the United States.

27. *MERCOSUR* adopted a staged positive list approach. A framework agreement on trade in services, the Protocol of Montevideo, entered into force on 7 December 2005. Initial commitments were adopted in July 1998, and since then six rounds of negotiations have been conducted on specific commitments, with new commitments being progressively incorporated into national schedules. *MERCOSUR* has made progress both in terms of the increased number of commitments and in providing enhanced transparency, as commitments now specify with more precision the restrictive measures in market access and national treatment. Commitments adopted under the Montevideo Protocol have gone beyond *MERCOSUR* members' commitments under the GATS. However, only the initial commitments have entered into force. The *MERCOSUR* government procurement regime covers both goods and services, using a positive list approach.

28. *CARICOM* has made considerable progress in creating a single market for services, in liberalizing capital movements and in ensuring the right of establishment of business within the region. Members are in the process of removing existing restrictions that impede the rights of *CARICOM* nationals to establish business enterprises, move capital and provide services. All services sectors without restrictions in national schedules were completely liberalized in 2002. The number of restrictions has been reduced significantly, and this has resulted in significant liberalization in services and capital movements, and in advancing the right of establishment. Intraregional liberalization of services trade has thus advanced beyond the level of GATS commitments adopted by *CARICOM* members and the levels of liberalization of most North–South agreements entered into by a number of Latin American countries.

29. African countries have embarked on a strategy of regional integration to overcome difficulty in integrating into the global economy. Major agreements include ECOWAS, WAEMU, CEMAC, SACU, COMESA and SADC. These regional economic communities (RECs) are expected to serve as building blocks for the formation by 2025 of a continental African Economic Community. Subregional RTAs are proliferating, and the consolidation and rationalization of these initiatives are an important challenge for the continent. Six of the

53 African countries are members of one REC, 26 are members of two RECs and 20 are members of three RECs, while one country belongs to four RECs.

30. Most African RTAs aim at strong economic integration to stimulate economic growth by enlarging regional markets, generating economies of scale and facilitating trade and investment through regional cooperation. Despite the stated objective of the removal of obstacles to the free movement of persons, goods, services and capital, and to the right of residence and establishment, African RTAs are yet to embark on a services liberalization agenda. COMESA has established a Working Group to spearhead the development of this framework for trade in services. The mandate for services liberalization in SADC stems from Article 23 of the SADC Trade Protocol, which refers to the importance of trade in services for the development of the economies of SADC countries and adopting policies and implementing measures with a view to liberalizing their services sector within the Community. The article also indicates that this will be done in accordance with SADC countries' obligations under the GATS. A Draft Annex (to the Trade Protocol) on Trade in Services is currently being considered by SADC member States, using a positive list approach. The target for SADC is to achieve substantial liberalization of trade in services no later than 2015.

North–South RTAs

31. North–South RTAs increasingly integrate services. Some bilateral agreements involving the United States and the EU have an important services component. Their accelerated proliferation has led to widespread use of deeper liberalization approaches to services under bilateral RTAs. Broader economic partnership agreements such as ACP–EU EPAs can potentially help DCs develop regional supply capacities building and investment promotion in infrastructure and modern technologies in the services sectors. North–South RTAs need to be designed in such a way that they serve as real instruments for development and for poverty eradication in the South. Given the nascent character of the services sector in DCs, the implications of North–South reciprocal market opening for DCs' services sectors need to be carefully assessed.

32. *NAFTA* has become a model for services trade liberalization that has been replicated elsewhere, including through US bilateral RTAs. The *NAFTA* model incorporates comprehensive provisions dealing with cross-border trade in services, and a separate chapter on investment covering both goods and services, government procurement and the mobility of business persons, with a negative list approach often with the “ratchet mechanism”. It adopts a broad definition of investors and investments, sets out high standards for the right of establishment (i.e. the provision of substantial pre-establishment rights), and deals with national treatment, the prohibition of performance standards, the freedom to transfer funds, an expropriation clause and investor-to-State dispute settlement. Most *NAFTA*-type agreements contain specific chapters on financial services, telecommunications and electronic commerce, incorporating various obligations both in goods and in services. *NAFTA*-type agreements have resulted in a *standstill* and GATS-plus commitment. Reservations are set out for specific measures and liberalization commitments; exemptions from MFN treatment; activities reserved to the State; quantitative restrictions; and reservations to commitments in financial services. Also, reservations are contemplated in respect of the provisions in the government procurement chapter. *NAFTA*-type agreements have led to a considerable opening of developing country markets.

33. A number of bilateral RTAs exist or are being negotiated between the EU and DCs, for example Euro-Mediterranean Agreements. These are modelled on the GATS, and include positive list approach without a separate investment chapter. The Trade, Development and Cooperation Agreement between South Africa and the EU provides for the fostering of cooperation in the services sector in general and in the area of banking, insurance and other financial services in particular.

34. *ACP States* are engaged in negotiations aimed at concluding economic partnership agreements (EPAs) with the EU no later than the end of 2007, with the possibility of liberalization of trade in services being foreseen. Services account for one third of all ACP exports of goods and services to the EU. It is estimated that some three quarters of recorded African ACP exports are destined for the EU. This indicates the importance of the EU for ACP services exports. In the negotiations on EPAs, ACP States identified the tourism sector and Mode 4 as crucial for their trade and development prospects. Trade in services is dealt with in the Cotonou Partnership Agreement (CPA) in terms of eliminating restrictive measures affecting trade in services in the signatory countries with the objective of reciprocal market opening, and in terms of strengthening regulatory and development cooperation in the sector. While there is no firm obligation under the CPA to liberalize trade in services, the parties have agreed on the objective of extending their partnership to encompass liberalization of services (Article 41(4)) in accordance with the provisions of the GATS. Services liberalization would be progressive, in principle based on the positive list approach, adapted to the level of development of the ACP countries and regions concerned in overall terms and in terms of their services sectors and subsectors, and to their specific constraints, and underpinned by the principles of SDT, asymmetry and positive regional discrimination. A sound regulatory framework is considered important. Parties would retain the right to regulate, and to introduce new regulations on the supply of services within their territories in order to meet national policy objectives. The negotiations would address special safeguard mechanisms.

35. Improvement in Mode 4 will be discussed in the context of the EPA negotiations. This may constitute an area where greater market access opportunities may arise for ACP States through the EPA negotiations. It should be noted that additional market access opportunities may be limited in the goods area owing to long-standing unilateral preferences. In this respect, an approach suggested by the EU limits the scope of temporary movement of natural persons to “business natural persons”, including key personnel, business visitors and intra-corporate transfers (managers, specialists, graduate trainees, business services sellers). In respect of contractual services suppliers and independent professionals, the proposed provisions are limited to the reaffirmation of the parties’ obligations and commitments under the GATS. This may limit the potential benefit of future EPAs. The form and content of liberalization commitments, sequencing and support for ACP services supply capacity-building are key issues for consideration.

IV. RTAS AND MOVEMENT OF SERVICES SUPPLIERS

36. RTAs can provide a promising avenue for service-related temporary movement of persons and workers. They could be relevant for the promotion of movement of workers at all skill levels. This is important, as the existing Mode 4 commitments in the WTO are limited in scope and depth, generally focusing on skilled workers. The existing offers in the ongoing GATS negotiations are largely seen by developing countries as insufficient in respect of

contractual services suppliers, independent professionals and semi- and less-skilled service providers. While half of the 70 offers under GATS negotiations have introduced Mode-4-related changes, they often attach professional and educational requirements or sectoral carve-outs.

37. Some RTAs reflect existing commitments under the GATS while others have moved beyond the GATS in this area, as they have provided for general access for certain categories of personnel and offered additional liberalization. The way in which RTAs treat labour movement varies across regions, ranging from full labour mobility to no effective provision at all. However, many RTAs are yet to achieve their full potential through increased Mode 4 commitments facilitating labour mobility. Even in the most liberal agreement, the transition period and economic assistance to disadvantaged regions are used to mitigate the impact of flow of workers. Most RTAs still focus on facilitating the movement of higher-skilled workers and do not go very much beyond the GATS Mode 4 commitments or unilateral programmes to attract skilled workers. Facilitated movement of people does not always lead to the right to provide services. This will depend on the actual liberalization of particular sectors. Moreover, most RTAs stipulate that the provisions covering labour mobility do not override countries' general migration laws and their right to use residence requirements and related permits and visas.

Treatment of Mode 4 in RTAs

Most RTAs contain some provisions on labour mobility. They fall into the following five categories:

(i) Agreements providing full mobility of labour with very limited exceptions (e.g. for public services, public security and/or public health works) (EU, EEA, EFTA, COMESA, ANZCERTA);

(ii) Agreements providing market access for certain groups (university graduates, professionals, highly skilled persons or workers from selected occupations), including service suppliers and/or grouping all movement of natural persons/temporary business entry in a separate chapter (CARICOM, NAFTA, Europe Agreements, Canada–Chile, United States–Singapore, United States–Chile, Japan–Singapore);

(iii) Agreements using the GATS model with some additional elements (e.g. common regulations for work and labour conditions) (AFTA, MERCOSUR, Euro-Med Association agreements, New Zealand–Singapore, EU–Mexico, EU–Chile, United States–Jordan);

(iv) Agreements providing no market access but facilitated entry (e.g. facilitated travel for business travel and visa waivers for certain categories of persons) (APEC, SAARC);

(v) Agreements without provisions on labour mobility or services (CEFTA).

38. Regional cooperation in the related field of the labour market, including through visa and migration policy, has also been pursued to promote the provision of services through Mode 4. For instance, the Japan–Philippines Economic Partnership Agreement (2006) has incorporated a commitment regarding visa allocation/quota for the movements of health-care workers.

39. Some regional groupings have specific initiatives relating to services workers — for example, the *SADC* regional framework aims at developing policy guidelines to attract and retain health professionals in the public sector in order to reverse brain drain in the health sector in the region. Other cooperative processes cover migration-related issues generally,

including regular migration and highly skilled migrants. Related mechanisms include COMESA's protocol on the gradual relaxation and eventual elimination of visa requirements and protocol on the free movement of persons, labour, services and the right of establishment and residence, as well as cooperation under the *Thailand–Australia FTA* in facilitating the temporary entry of business people, for example by granting applications offshore. ECOWAS introduced the ECOWAS Passport, thereby eliminating barriers to the cross-border movement of citizens.

40. *NAFTA* facilitates the cross-border movement of four categories of persons: business visitors, 63 professions, intra-corporate transferees, and traders and investors. No party may impose numerical limits or labour market tests as a condition for the entry of intra-corporate transferees, and no limits are imposed on *NAFTA* visas (TN) issued for one year with an unlimited number of extensions. *NAFTA* does not alter a member country's general immigration provisions or the requirement for temporary visitors to meet licensing or certification requirements with respect to the exercise of a profession or the delivery of after-sale services. There has been a sharp increase in entries under the *NAFTA* regime since 1995, when 20,000 persons were admitted to the United States on a TN visa. In 2004, 133,000 Mexican nationals, belonging to those categories of persons set out in *NAFTA*, entered the United States for work on temporary non-immigrant visas.

41. The *Andean* services regime provides that member countries shall facilitate the free transit and presence of natural persons supplying services, including professional services, and employees of services firms of other member countries in relation to the activities covered by the regime. The *Andean Labour Migration Instrument* has already introduced significant commitments regarding the free movement of workers, including in the services sector, within the subregion. Any *Andean* national has the right to enter, reside and work in any *Andean* country. Therefore, employment in the services sector has been fully opened up to *Andean* nationals in all member countries. The *Andean Community* is currently working on a regime for the recognition of licences and certifications in order to make the free movement of natural persons also a reality for accredited occupations and professions.

42. In *MERCOSUR*, the mechanism for the temporary exercise of professions, which includes the directives for the conclusion of framework agreements for reciprocal recognition between professional bodies adopted in 2003, is expected to promote free trade in professional services. In addition, the elimination of visa requirements for *MERCOSUR* nationals, and the *MERCOSUR* Visa for temporary services suppliers, are important developments. The *MERCOSUR* Visa allows natural persons to enter, and stay for up to four years, for the purpose of providing services. It applies to managers and directors, administrators, legal representatives, scientists, researchers, professors, artists, sportspersons, newspersons, highly qualified technicians, and specialists and professionals. The granting of the *MERCOSUR* Visa is not subject to any economic needs test and is exempt from any requirement for proportionality regarding nationality or wage parity.

V. COOPERATIVE MECHANISMS UNDER RTAS

43. Among the arguments for a regional approach to services trade liberalization is the greater viability of cooperative mechanisms. Cooperation can take various forms, including regulatory cooperation, financial, human and institutional capacity- building, trade facilitation and infrastructure-building. Cooperation leading to deeper integration may be more feasible

among countries with similar levels of development, social preferences and cultural affinity. The benefits of regulatory cooperation may be particularly great for sectors where trade is impeded by differences in qualification requirements, licences and standards (e.g. professional services) or by visa-related issues. However, there may also be costs, for example those arising from sub-optimal harmonization, which do not properly reflect social preferences and local economic conditions.

44. Numerous cooperative initiatives focus on *recognition and harmonization of qualifications and standards*, with mutual recognition agreements (MRAs) being a central component. In Europe, mutual recognition of qualifications has been a central pillar for a single services-market. The recognition of qualifications was enshrined in the EEC Treaty and subsequently implemented through 15 directives pertaining to the transfer of qualifications and skills for academic and professional purposes. In 2007, this sectoral approach is expected to be replaced by a single directive for more automatic recognition of qualifications, simplified administrative procedures and enhanced cooperation.

45. The recognition of professional qualifications and registration procedures for services suppliers also figures prominently in South–South RTAs. ASEAN is in the process of concluding MRAs for professional services (e.g. engineering, accountancy, architecture, surveying, nursing). MERCOSUR has a mechanism for the temporary exercise of professions, including directives for reciprocal recognition between professional bodies. The Andean Community is working on a regime for the recognition of licences and certifications for accredited occupations. African RTAs have had some success with harmonization programmes: the 1999 SADC Driver's Licence harmonizes the training, examination and licensing of drivers across the region and has facilitated transport services.

46. Amongst *North–South RTAs*, the *Singapore–Australia FTA* envisages cooperation in the form of academic credits transfer and mutual recognition of academic and vocational qualifications between recognized institutions of higher learning. It also contains a separate chapter on cooperation in education, focusing on quality assurance processes; online and distance education; primary, secondary and higher education systems; technical education and vocational training; industry collaboration for technical and vocational training; and teacher training and development.

47. Cooperation covers *infrastructure sectors*, including financial services (COMESA Bond Guarantee Scheme, COMESA Yellow Card Scheme, PTA-Reinsurance Company (ZEP-RE)); *energy* (e.g. SADC's Southern African Power Pool, aimed at sound economic, environmental and social practices, coordinating and enforcing regional quality supply standards; measuring systems performance); and *research and development* (including human resource development, e.g. Thailand–Australia FTA). ASEAN, for example, covers the strengthening and integration of infrastructure in transportation, energy and telecommunications (e.g. cooperation for an ASEAN highway, the Singapore–Kunming Rail Link, an ASEAN action plan for open-sky arrangement and a Trans-ASEAN Gas Pipeline Network). COMESA has a number of programmes aimed at facilitating services trade, which focus on transport (i.e. air transport liberalization, the COMESA Carriers' Licence, harmonized axle loading and maximum vehicle dimension, harmonized road transit charges). Other African RTAs also focus on cooperation in transport (e.g. the Yamoussoukro Decision to gradually liberalize air transport, an Africa-wide initiative) and business services, including insurance and logistics services, to facilitate trade within the region.

48. Many cooperative initiatives also focus on *institution-building*. SADC, through its protocols, aims to enhance more institutionalized sharing of information, and has created a number of new institutions — for example, the Telecommunications Regulators Association of Southern Africa (regulatory cooperation on telecommunications), the Regional Tourism Organization of Southern Africa and the Southern African Power Pool.

49. Some cooperative mechanisms aim at building *supply capacity*. Amongst North–South agreements, the ACP–EU Cotonou Partnership Agreement (CPA) provides for (and future EPAs will provide for) cooperation regarding labour, business, distribution, finance, tourism, culture, and construction and related engineering services with a view to enhancing their suppliers' competitiveness and increasing trade. The measures envisaged aim at providing ACP residents/citizens with easy access to information and communication technologies. The CPA's “Development Strategies” aim at improving the competitive position, especially of SMEs, including through cooperation in private sector development; product development; sector development (e.g. sustainable tourism development or, in the case of SADC, marketing of the SADC region in close cooperation with the private sector). The Thailand–Australia Agreement aims at investment support and promotion.

50. The EU implements a *broader cooperative mechanism*, including at a sectoral level (e.g. transport, audiovisual, telecommunications). Programmes have been implemented to support new and potential member States in adopting the *acquis communautaire* in the accession process. The Phare programme, which currently applies to acceding and candidate countries, covers areas relating to services trade, including human resources and institution-building (in part with accompanying investment), and measures designed to promote economic and social cohesion. Phare aims at promoting the functioning of the market economy and helps in building the capacity to cope with competitive pressures and market forces within the EU.

VI. INTERFACE BETWEEN REGIONALISM AND MULTILATERALISM IN TRADE IN SERVICES

51. There is an intrinsic linkage between RTAs and the multilateral trading system, and DCs face the particular challenge of maximizing benefits from their parallel engagement in multilateral and regional processes. Various dimensions of the interface and coherence need to be taken into account when approaching GATS and RTA negotiations. This is important for DCs, given their limited administrative/institutional capacity to conduct a multitude of negotiations simultaneously and to ensure a coherent framework of rules across agreements; their limited negotiating capacities and bargaining power vis-à-vis economically stronger countries; and their limited capacity to implement international rules. There is a risk that the multiplicity of RTA negotiations may divert human and institutional resources away from multilateral efforts.

52. *WTO rules on RTAs* determine conditions under which RTAs in services are allowed to exist and operate. GATS Article V (“Economic integration”) establishes an exception to the general MFN principle, with two key requirements to be met: first, services RTAs must have “substantial sectoral coverage” in terms of “number of sectors, volume of trade affected and modes of supply” (no “a priori exclusion of any mode of supply”); and second, RTAs must provide for “the absence or elimination of substantially all discrimination” in terms of national treatment (GATS Article XVII) either through (i) “elimination of existing

discriminatory measures” “and/or” (ii) “prohibition of new or more discriminatory measures”. This has to be achieved “on the basis of a reasonable time-frame”. Moreover, RTAs must be designed to facilitate trade between member States and must not raise the overall level of barriers to services trade against third countries. Different views exist about the key requirements of Article V.

53. Unlike GATT Article XXIV, GATS Article V contains special and differential treatment (SDT). When DCs are party to an RTA, flexibility is to be provided in accordance with the level of development of the countries concerned regarding the two key conditions noted above. In the case of South–South RTAs, “more favourable treatment” may be granted to juridical persons owned or controlled by natural persons of the parties in respect of the requirement to engage in “substantive business operations” in the territory of a party to an agreement. Various interpretations have been put forward as to what constitutes “flexibility” and “more favourable treatment” in Article V:3(b).

54. Doha negotiations on RTA rules are aimed at “clarifying and improving” rules on RTAs, including Article V, while taking “into account the developmental aspects of regional trade agreements”. The outcome may affect regional negotiations and the terms of agreements. A Transparency Mechanism for Regional Trade Agreements was adopted in December 2006. It aims at improving procedures for early announcement, notification, examination and reporting of the regional trade agreements on goods and services.

55. *MFN market access conditions* determine the level of preferences that may be provided in the regional context since preferential treatment is a function of restrictions applied on an MFN basis. Thus, as in the case of goods, MFN liberalization in services could affect the level of such “preferences” or the “GATS plus” element in an RTA. The ongoing GATS negotiations could thus affect the scope of such preferential treatment applied to regional partners in services. Indeed, as noted, several RTAs go beyond GATS commitments. Some RTAs even go further than offers submitted in GATS negotiations (e.g., in financial, express delivery, distribution and audiovisual services). Sometimes, the depth of commitments across sectors is comparable with (or goes beyond) commitments envisaged in plurilateral requests. However, it is also notable that RTAs preserve limitations and sensitivities (for example, in respect of audio-visual services in the EC; maritime and certain professional services in the United States; and cross-border trade in financial services in many countries).

56. Negotiations are under way regarding *GATS disciplines on domestic regulation*, where DCs face the challenge of striking the right balance between the need to preserve domestic policy flexibility and the need to achieve specific disciplines to underpin their export market access opportunities, including in Mode 4. In this regard, some RTAs incorporate provisions ensuring compliance with future GATS disciplines, for example the Singapore–US FTA services chapter.

57. Particularly relevant to RTAs are disciplines on recognition under Article VII of GATS. The article governs terms and conditions of recognition agreements and thus affects RTAs' ability in instituting and implementing mutual recognition and harmonization of qualifications and standards. In this regard, there arises the question of how this rule will affect RTAs' regulatory cooperation aimed at mutual recognition of qualifications and standards. GATS Article VII requires parties to MRAs “to afford adequate opportunity for interested members to negotiate their accession” and not to “accord recognition in a manner which would constitute a means of discrimination between countries in the application of its

standards or criteria for the authorization". Such conditions need to be factored in when designing and implementing MRAs in the regional context.

58. Regarding subsidies, government procurement and emergency safeguard measures, no GATS disciplines exist in this respect; negotiations are ongoing, but to date have made only limited progress. Thus, RTAs' members have greater leeway in adopting disciplines and commitments which they deem to be appropriate in the regional context, and RTAs appear to have advanced as regards rule-making in some of these areas. Singapore issues dropped in the Doha negotiations are increasingly being pursued in North-South RTAs, entailing disciplines on the right of establishment, investment or government procurement. Thus, some proposals in the GATS negotiations on government procurement, for instance, draw on provisions on government procurement in existing RTAs to open services procurement to international competition. Various RTAs have embarked on regional commitments in those areas, and they may have a bearing on future WTO disciplines.

VII. CONCLUSIONS

59. RTAs, coherent with the MTS, can harness development gains from trade in services by allowing for greater and deeper liberalization while creating viable mechanisms for cooperation for institutional, regulatory and supply capacity-building, competitiveness enhancement and infrastructure development. RTAs can, however, complicate the trading environment through their "spaghetti bowl" effect. South-South RTAs can provide a platform for boosting regional service trade and addressing bottlenecks in trade and production, build up supply capacity and develop trade and transport infrastructure and networks. North-South RTAs can potentially improve market access opportunities for DCs in sectors and modes of supply of export interest to DCs, and incorporate cooperation packages. Effectively implementing such packages can generate substantial development gains. Given the nascent state of the services sector in DCs, the implications of North-South reciprocal market opening in services for DCs' services sectors need to be carefully assessed.

60. Ensuring development gains from services liberalization and cooperation in the regional context requires DCs to design and implement a judicious domestic regulatory framework and institutions, while carefully approaching international commitments so as to serve their overall development objectives. Adequate impact assessment of trade in services is thus important in identifying strategies and priorities for enhancing developing country competitiveness in services trade and benefiting from the combination of RTAs and the MTS.

61. Additional research is needed on the experience of DCs in configuring an optimal, mutually supportive balance of regional and multilateral services trade liberalization so as to identify ways and means of maximizing development gains through their joint participation in global and regional trade agreements and through judicious sequencing of commitments at those levels. Support is needed in strengthening analytical, regulatory and institutional capacities of DCs at the regional level, including strengthened regional integration secretariats, and improvement of data and information regarding services. In addition, DCs need to be supported in their efforts to assess trade in services and design appropriate regulatory frameworks and institutions supportive of their national development objectives, as well as to build up competitive services supply capacities.

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