

**NEGOTIATIONS ON "TRADE IN SERVICES" :  
DEVELOPMENTAL IMPLICATIONS  
FOR THE SOUTH**

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country

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CERTIFICATE

This is to certify that this dissertation entitled "NEGOTIATIONS ON 'TRADE IN SERVICES' : DEVELOPMENTAL IMPLICATIONS FOR THE SOUTH" submitted by Pamela Seth in partial fulfilment of six credits out of a total requirement of twenty four credits for the award of the degree of Master of Philosophy of this university. This dissertation has not been submitted for the award of any other degree of this university or any other university. This is her original work.

We recommend that this dissertation be placed before the examiners for evaluation.

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## ABBREVIATIONS

ACTN	: Advisory Committee on Trade Negotiations, United States.
ASEAN	: Association of South East Asian Nations.
EC	: European Community.
GAS	: General Agreement for Services.
GATT	: General Agreement on Tariffs and Trade.
LDC	: Less Developed Country.
MFN	: Most Favored Nation.
MTN	: Multilateral Trade Negotiations.
NIC	: Newly Industrialised Country.
NTB	: Non-tariff Barrier.
OECD	: Organisation for Economic Cooperation and Development.
SPAC	: Services Policy Advisory Committee of the US Trade Representative.
UNCTAD	: United Nations Conference on Trade and Development.
USTR	: United States Trade Representative.
WIPO	: World Intellectual Property Organisation.

## PREFACE

The Uruguay Round of Multilateral Trade Negotiations under the auspices of the GATT has occupied centre-stage in the international political arena for the last five years. They have assumed as much importance as the arms talks in recent years, and moved from low foreign policy to "high" policy. This dissertation provides an insight into the national objectives, constraints and strategies for these new trade talks and examines the stake in the outcome of these talks for different countries.

The international community has realised that the trading system under the (GATT) is at a critical juncture. Worldwide economic nationalism that threatens to destroy the world trading system is on the rise; some of the reasons being sluggish world economic growth, oil shocks of the 70's and debt crises in some less developed countries.

Nations have adopted domestic industrial and economic policies, such as subsidies that give unfair favorable edge to their exports in world markets. On the other hand they have increased barriers to their domestic markets to protect or encourage their own industries. It is clear to most nations that the rules governing the world market place must be improved to maintain fair and equitable access to international market. Recognizing the great danger faced by the world trading



system, the United States has led the industrialised nations in calling for a new round of multilateral trade negotiations under the GATT and insisted on extending GATT disciplines to new areas such as services, high technology, investment and intellectual property.

↗ This study deals with 'Trade in Services' for it has become a focus of attention in the 80's since they form a highly significant portion of the international trade. Services have in recent years been intensely debated and have become a bone of contention between the North and South. An effort has been made in this dissertation to analyse the divergent viewpoints and explore the possibility of an agreement in the area. ↗

The first chapter explores the question of definition in order to develop a conceptual understanding of services which would shed some light on the nature of international "trade in services". It deals with the dimensions of the phenomenon; analyses the data collection problems and examines the existing data thereby discovering the distribution of this trade between the industrialised countries and the developing countries, and highlights the developing world concerns and emerging significance of Trans National Corporations in the services sectors. Restrictions and barriers

have been examined in order to understand the reasons for the push for liberalisation and cry against protectionism. This exercise establishes the importance of trade in services in the production process and international economic interaction thereby providing the reason for this sudden interest in freer services trade.

The second chapter analyses the views of the industrialised countries on this subject; their motives, stakes and strategies in these negotiations; they are "bargaining for gains" in an area where they already have a comparative advantage.

The developing countries concerns and apprehensions and the developmental implications for these countries is dealt with in the IIIrd chapter. This section examines the strategies employed by the initially reluctant developing countries of the South in dealing with the North keeping their vulnerable and comparatively disadvantageous position in mind.

The last section i.e. Chapter IV deals with some concluding suggestions and observations about the issue of services as it stands today. Certain alternative models for negotiations have been suggested and a compromise solution presented which could benefit both the North and South.

The method used in this dissertation is descriptive, and analytical. In writing this dissertation, I mostly relied on secondary sources.

CHAPTER I

TRADE LIBERALISATION IN SERVICES:  
AN INTRODUCTION

General Agreement on Tariff and Trade (GATT):

X The (GATT) General Agreement on Tariff and Trade is a multilateral trade agreement or treaty entered into force in 1948 to promote freer trade among member countries.<sup>1</sup> It provides a forum for negotiating trade issues and a framework of principles guiding the conduct of trade. 107 countries are at present a party to this agreement. Of these 96 have signed this agreement as contracting parties while 31 others apply GATT rules on a defacto basis. GATT is neither an organisation or a court of justice. The GATT has a permanent Council of Representatives with its headquarters at Geneva; its main function is to call international conferences to decide on trade liberalisation on a multilateral basis. This treaty covers over 74 percent of the world trade.

Objectives and Framework:<sup>2</sup>

X The declared objective of the GATT is "to raise living standards, ensure full employment through a steadily growing effective demand and real income, develop fully the resources of the world and expand the production and exchange of goods on a global level.

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1. GATT "Trade Policies for a better future".  
Journal of World Trade Law, 19(3); May-June 85; 301-04.
  2. Lenore Sek: Trade Negotiations; the Uruguay Round, CRS Issue Brief, The Library of Congress:Updated, April 16, 1990, pp. CRS 2.

The guiding philosophy behind this treaty is bilateral agreements are more vulnerable and discriminatory practices and high tariffs hamper trade, hence its endeavours are directed towards liberalisation on a multilateral basis.

Central features of the GATT framework are:

- (a) non discriminatory trade treatment (unconditional most favoured nation principle);
- (b) to carry on trade on the principle of reciprocity and transparency;
- (c) reliance on tariffs rather than non-tariff barriers when protecting domestic producers;
- (d) adherence to negotiated tariff rates at fixed maximum levels;
- (e) settlement of disputes through consultation and conciliation;
- (f) to liberalise tariff and non-tariff measures through multilateral negotiations.

↙ To achieve these objectives, the Agreement provides for:

- (a) multilateral trade negotiations.
- (b) consultation, conciliation and settlement of disputes.
- (c) waivers to be granted in exceptional cases.

Previous Rounds of the GATT: <sup>3</sup>

The GATT has completed seven rounds of multi-lateral trade negotiations (MTN) and the eighth round was launched in 1986 at Punta del Este (Uruguay). The first conference was held at Geneva in 1947, the second at Annecy (France) in 1949, the third at Torquay (England) in 1950-51, the fourth at Geneva in 1955-56, the fifth at Geneva (Dillon Round) between 1954-62, the sixth at Geneva (Kennedy Round) between 1963-67 and the seventh at Tokyo between 1973-79.

The first five rounds, completed between 1947 and 1962, concentrated on reducing tariff rates and eliminating quantitative restrictions on trade in manufactured products. The sixth Round, the Kennedy Round, focussed on tariff cuts but it also addressed for the first time certain non-tariff barriers to trade. The seventh round, the Tokyo Round, lasted from 1973 to 1979 and was the most ambitious attempt undertaken in the GATT to reduce or eliminate barriers to trade. In addition to agreeing to further cuts in tariff rates, negotiators developed a series of agreements or codes of conduct, setting rules for non-tariff barriers to trade. The agreement on tariffs reduced rates on trade in manufactured goods among

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3. *ibid* pp. CRS 2.

major developed countries by an average of about 34 percent. The cuts, which were to be phased in between 1980 and 1987 have reduced the average tariff on manufactured goods in the major developed countries from 7.0% to 4.7%. Negotiators in the Tokyo Round also agreed to six codes of conduct, setting new rules for subsidies and counter-vailing measures, technical barriers to trade (standards), import licensing procedures, government procurement, customs valuation, and antidumping measures. Other agreements in the Tokyo Round covered trade in specific product categories

meat, diary products, tropical products, and civil aircraft.

URUGUAY ROUND<sup>4</sup> : Despite the significant accomplishments of past GATT negotiations in removing barriers to trade, many observers maintained that important reforms were needed to improve GATT rules and procedures, to strengthen the codes negotiated in the Tokyo Round, and to expand the coverage of GATT to new areas of international trade. In September 1986 a new round of multilateral trade negotiations subsequently called Uruguay Round was launched with the conclusion of a conference of trade ministers in

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4. "Old Rules and New Players: GATT in the World Trading System," Paper given at the 25th Anniversary of the Centre for International Affairs, Harvard University, March 29, 1983.



TABLEKey LDC participants in the Growth Round

Countries	1983 Trade (billion dollars)	
	Exports	Imports
Heavily indebted LDCs:		
Argentina	7.8	4.5
Brazil	21.9	16.8
Colombia	3.0	5.0
Indonesia	21.2	16.4
Jamaica	0.7	1.4
Mexico <sup>a</sup> .	21.1	8.2
Philippines	4.9	8.2
Yugoslavia	9.9	12.2
More creditworthy LDCs:		
Algeria <sup>a</sup> .	11.2	10.3
China <sup>a</sup> .	22.2	21.3
Egypt	3.1	10.0
Hong Kong <sup>a</sup> .	22.0	24.0
India	8.5	13.3
Malaysia	14.1	13.2
Singapore	21.8	28.2
South Korea	24.5	26.9

Source: GATT, International Trade 1983/84, table A5.

a. Countries that are not contracting parties to the GATT.

Uruguay (Punta del Este). ~~X~~ The Ministerial declaration<sup>5</sup> signed at the end of the conference set a comprehensive agenda.

The key objectives<sup>6</sup> of the United States were taken care of since it is the US that has led the industrialised nations in calling for a new round of multilateral trade negotiations under the GATT. The US has been rallying for the inclusion of new issues and demanding -

increased GATT discipline for trade in agricultural products; extension of GATT rules to cover trade in services and trade related to foreign investment; greater protection for intellectual property; and improvement of the GATT dispute settlement mechanism.

A major US objective in the Uruguay Round was to establish rules for trade in services that are similar to rules for trade in goods. The United States was the first to push for liberalisation in the services sector and the first impetus for inclusion of this issue in the eighth round of multilateral negotiations came

~~by~~ from the United States, the reason being:

1. it is the world's largest exporter of services.

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5. For details of the Ministerial declaration, see *Launching the Uruguay Round, Focus*, GATT Newsletter, No. 41, October 1986, pp. 1-5.

6. Lenore Sek; n.2, pp. CRS 2.

2. it has the highest percentage of its population engaged in services.
3. the most important reason in this context was that it was the earliest and furthest in its data collection.

Most of the GATT members particularly the developing countries have been reluctant to extend GATT coverage to services and have expressed concern over the adverse economic and cultural consequences of foreign competition in service industries. India and Brazil as leaders of the developing World have expressed concern regarding concessions on services trade return for greater access to goods markets of industrial countries.

An agreement was finally arrived at Punta del Este in 1986 and is reflected in the Ministerial Declaration.

The Ministerial Declaration called for the completion of the Uruguay Round in 4 years. It provided that agreements readied at an early stage may be implemented prior to the formal conclusion of negotiations.

The Declaration instituted a structure for the negotiations. It established a trade negotiating

committee (TNC) that would have oversight of the negotiations. It established two Groups that would report to the TNC: a Group of Negotiations on Goods and a Group of Negotiations on Services.

The Group of Negotiations on Goods covers 14 key issues:

- a) agriculture.
- b) trade related aspects of intellectual property, including counterfeit goods.
- c) trade related investment measures.
- d) dispute settlement.
- e) tropical products.
- f) textiles and clothing.
- g) natural resource-based products.
- h) tariffs.
- i) Non-tariff measures.
- j) safeguards.
- k) subsidies and countervailing measures.
- l) Tokyo Round Agreements.
- m) articles of the GATT.
- n) functioning of the GATT system.

The Group of Negotiations on Services was to deal with the trade in services exclusively.

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Trade in Services:

The Uruguay Round for the first time<sup>7</sup> dealt with trade in services though during the 1970's the traditional focus on the worldwide trade of merchandise goods began to give way to a more comprehensive approach which recognised the importance of trade in services<sup>8</sup> as well as goods.

This has occurred because of the growing realisation that services comprise a highly significant portion of international trade. Earlier few policy makers have recognised that the world market for services has expanded dramatically in the past decade. Trade in services has been left relatively untouched by international negotiating forums i.e. there is no regulatory

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7. In the Tokyo Round of Multilateral Trade Negotiations, attention was given to services pertaining to goods i.e. the sets of codes applicable to non-tariff barriers covered certain service sectors as well.
- a) services related to goods trade included in the provisions of the Government procurement code.
  - b) the subsidies code includes several services on the illustrative list of export subsidies to goods trade.
  - c) the Agreement on Trade in Civil Aircraft contains references to repair and maintenance services.
8. Raymond Vernon, "International Trade Policies in the 1980's: Prospects and Problems", in International Studies Quarterly (December 1982), pp. 483-510.

framework for world trade in services and hardly any rules have been developed for regulating services trade, as a result of this theoretical and regulatory void restrictions have mushroomed and many governments have created barriers restricting the access of foreign service industries to their markets.

The expansion of existing GATT framework into services has some advantages. First of all, it is contractually binding. Secondly, it applies to a large number of developed and developing nations. Third, as a conceptual framework, the GATT has existing structures which are accepted and could with some difficulty be extended to services.

'Trade in Services' such as insurance, transportation, banking and construction form a large part of the world trade. In 1987 the total world export of commercial services exceeded US \$ 500 billion - almost one fourth the value of world merchandise exports.<sup>9</sup> Trade in global services amounted to about 85 billion dollars in early 1970's<sup>10</sup> and according to OECD statistics, easily exceeded 350 billion dollars in

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9. Stephen F. Benz: Trade Liberalisation and the Global Service Economy, Journal of World Trade Law, vol. 19, no. 2, March-April 1985, pp. 95-120.
  10. US Trade Representative: US National Study on Trade in Services: A submission by United States Government to the General Agreement on Tariffs & Trade, (Washington, 1983), p.13.

1980 compared with a value of 1650 billion dollars for merchandise trade. Its volume doubled between 1960 and 1970 and again between 1970 and 1975. Services account for the largest share of GDP in most countries ranging in 1979 from around 40 percent in the least developed countries to almost 67 percent in the developed market economy countries. The size of the service sector is large and growing in all countries, what differs is their composition.<sup>11</sup>

The value of Exports of Services<sup>12</sup> minus investment income in 1980 was 271.5 billion SDRs of which the United States accounted for 9.8 percent, the United Kingdom 9.4, France 9.3, West Germany 9.1, Italy 6.3, Japan 5.3, Netherlands 5.0.

Despite the importance of services in international trade,<sup>13</sup> the GATT is virtually silent on issues related to services. GATT rules cover trade in goods and pertain to services only when they are incidental to goods trade.

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11. J.J. Schott, "Protectionist threat to trade and investment in services" The World Economy, vol.6, No.2, pp. 198 and 200.
  12. CF Gary Clyde Hufbauer and Jefferey J. Schott, Trading for Growth: The next round of Trade Negotiations, (Washington: Institute for International Economics, 1985) esp. chapter I.
  13. Jagdish N. Bhagwati, "GATT and Trade in Services: How we can resolve the North-South Debate" Financial Times, 27 November 1985, pg. 25.

~~The~~ The text agreed by Ministers<sup>14</sup> and not the contracting parties in September 1986 essentially identified seven objectives for the negotiations on services:<sup>15</sup>

- (a) a multilateral framework of rules and principles.
- (b) possible disciplines for individual sectors.
- (c) expansion of trade in services.
- (d) transparency.
- (e) progressive liberalisation.
- (f) economic growth of all trading partners, and
- (g) the development of developing countries.

It was agreed that while negotiations on services will be carried out by a separate group, the negotiators would use the procedures and practices of the GATT and operate under the aegis of the Single Trade Negotiating Committee.

By early December, 1988, a ministerial level<sup>16</sup> mid-term review of progress began in Montreal. An Agreement on basic principles to cover services trade was reached. These principles included transparency

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14. P.S. Randhawa; Punta del Este and After: Negotiations on Trade in Services and the Uruguay Round, Journal of World Trade Law; 21(4); Aug.87; 163-171.

15. *ibid.*

16. Frances Williams: World Trade in Services; Hope for Montreal and After; European Trends, London, No.3, 1988.



(availability of information and government measures effecting services trade); national treatment (equal treatment for foreign and domestic service providers); and non-discrimination (equal treatment for foreign service providers). The mid term framework agreement also provided for:

- (a) progressive liberalisation of services trade.
- (b) freedom to service providers to deliver their services by preferred means.

After the mid-term review in December 1988, the negotiating group on services began discussions on how the rules and principles might apply to various sectors.<sup>17</sup> In June 90 they discussed telecommunications and construction; in July transportation and tourism; and in September, professional services and the financial sector. In October, the United States presented a proposal for a General Agreement on Trade in Services (GATS). The proposed GATS outlined broad rules for services trade and allowed annexes for specific service sectors.

In further talks negotiators have discussed how broad the initial commitments under a services agreement might be. The US position is that the principles should apply broadly and automatically. Some countries,

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17. *ibid.*

including the EEC want a freeze<sup>18</sup> on the level of market access for services, followed by negotiations. The developing countries want to negotiate on a sector by sector basis.

Definitional and Statistical Issues:

In order to understand the importance of trade in services in the production process and international economic interaction one must examine the definitional problems and analyse the statistical data on share of services in the global trade.


It is very difficult to define services - One definition is based on the output of the production process and the intangible or "invisible" nature of the service product. This, however, is too limited for some services do produce tangible goods, such as construction and engineering services.

Services can be defined as any activity other than manufacturing, mining or agriculture. But this is a negative definition for according to this services are defined by what they are not.<sup>19</sup>

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18. For a comparison of differing US and European views, see Andrew Pierre, ed., Unemployment and Growth in Western Economies (New York: Council on Foreign Relations, 1984).
19. Shelp, Ronald K. - Beyond Industrialisation: Ascendancy of the Global Service Economy (New York; Praeger Publishers, 1981), p.10.

The first attempt to study services as a distinct economic activity was made by Colin Clark and Allan Fisher in their endeavour to analyse the role of the services sector in the process of economic growth and structural change.

The services sector has become more varied and complex with the passage of time. The term services is used to describe a phenomenal range of heterogenous economic activities some of which have nothing in common with each other.

 The services sector includes:<sup>20</sup>

- (a) infrastructural services: such as transport, communications, electricity and water supply.
- (b) social services: such as health and<sup>21</sup> education.
- (c) financial services: such as banking, insurance, accounting and brokerage.
- (d) technological services: such as construction, engineering and consultancy.
- (e) marketing services: such as advertising, wholesaling and retailing.

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20. Stephen F. Benz, n.9, pp. 96-97.

21. *ibid.*

- (f) commercial services: such as chartering, leasing and franchising.
- (g) professional services: those provided by lawyers, doctors and architects.
- (h) government services: such as those in public administration and defence.
- (i) personal services: such as hotels, restaurants, hair dressers, beauty parlours and domestic help.

The classification and sets of examples is not exhaustive and in the parallel economy there are other services like smuggling, prostitution and organised crime and black marketeering.

According to Hill -- A service may be defined as a change in the condition of person, or of a good belonging to some economic unit, which is brought about as a result of the activity of some other economic unit, with the prior agreement of the former person or economic unit.....

Trade in services may also be defined as international transactions in services between the residents of one country and the residents of another country irrespective of where the transaction takes place. International trade in services, so defined

can be divided into four categories.<sup>22</sup>

- (a) those in which the producer moves to the consumer;
- (b) those in which the consumer moves to the producer;
- (c) those in which either the producer or the consumer moves to the other; and
- (d) those in which neither the producer nor consumer move to each other.

In the first three categories,<sup>23</sup> physical proximity of the producer and the consumer is essential, if the international service transaction is to take place. In the fourth category, however, physical proximity is not necessary.

One common characteristic of service industries is that they deal in "intangibles". Motion picture and Computer software industries, where a service is embodied in a tangible good is an exception to the rules.

Most services operate on a contractual basis<sup>24</sup> and therefore focus on fees, royalty, premiums and

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22. Deepak Nayyar, Some reflections on the Uruguay Round and Trade in Services; Journal of World Trade Law; Vol. 22(5): 1988

23. *ibid.*

24. Benz, n.9, pp. 96-97.

margins. Some, such as tourism provide output inside their respective nations to non-residents. Others offer parts of their services from their home country. Most depend on establishment of overseas presence, since by their very nature many services cannot be shipped or transported across national boundaries.

A number of service industries have well defined international markets such as shipping, airtransportation, banking and motion pictures. Others such as consulting services do not.



~~Government~~ Government regulations<sup>25</sup> also varies greatly among service industries being strongest in the area of banking and insurance. But in most cases government regulations of services activities are greater than in the merchandise goods trade; the reason being sensitivity. National Security is another major consideration (transportation, telecommunications), financial stability (banking) or cultural identity (motion pictures) and television programming are other areas where government control is exercised.

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25. Philippe Brusick, Murray Gibbs and Mina Mashayekhi: Anti Competitive Practices in the Services Sector, Uruguay Round: Further Papers on Selected Issues; New York, UNCTAD, UNDP, 1990.

Although service industries are generally regarded as being labour intensive there is substantial variation within the groups. Accounting, Management consulting, architectural and engineering services are all labour intensive. In contrast insurance is a capital intensive industry not because of investments in plant and machinery but because of its very nature it must have adequate capital stocks present.

Any attempt to measure international trade in services is confronted by a range of serious statistical difficulties which need to be recognised. It is the greatest obstacle facing the liberalisation of trade in services as well as the understanding of service economies. There has to be an adequate theoretical and numerical framework of international services trade and investment for negotiators and policy makers to do some constructive work. They cannot work or make decisions in the dark. The essential pre-requisite for decision makers is that data must be collected, restrictions must be catalogued, comparative advantage must be found i.e. for liberalisation to occur, an undertaking of the flows of modern complex service economies is required.

 The Europeans have also been wary of granting any concessions without first having an adequate database, which is why upto the present time most of the activity in international forums on services has consisted of submission of country studies. 

In most of the countries there is an apparent bias shown in the collection of data i.e. the manufacturing sector has a relatively higher level and more detailed statistics than services transactions.

Limited Services data on trade in services is available for most countries.<sup>27</sup> Four broad groups of services have been studied and statistics collected on receipts and payments for these through balance of payments reports published annually by International Monetary Fund.

The four groups are:<sup>28</sup>

- (i) shipment (freight costs and merchandise, insurance charges).
- (ii) other transportation (passanger fares and port charges).

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27. International Monetary Fund, Balance of Payments Statistics, Yearbook; Part II (1982; cited in Jeffrey J. Schott and Jacqueline 1985) Mazza, Journal of World Trade Law, Vol. 20/3; May-June 86; pp. 253-76.

28. *ibid.*



- (iii) travel (tourism).
- (iv) other private services (which include banking, construction, engineering, consulting, data processing etc.).

Figures on the preceding groups of trade are available for most countries. From here, both the quality and quantity of services trade data vary considerably. But it is evident that the data collected even in these four important groups is far from satisfying.

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 In the light of this limitation and problems regarding data collection it is easy to see that a true picture of modern service economy is difficult to construct.<sup>29</sup> Part of this problem can be blamed on a changing economy and an antiquated data collection system. Another factor lies in the inherent nature of services. Services have no natural location such as a customs point of entry or exit at which data can be gathered as they can be in the case of merchandise trade. The result of this is that the growth industries such as electronics in the last decade is consistently understated while declining industries like steel are continually overstated.



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29. *ibid.*

Many service transactions occur by way of electronic media making it more difficult to gather information and statistics.

Trade in Services have assumed immense importance in the past decade and inspite of all the definitional and statistical problems it has become an established fact that services are growing in scope and activity and services trade has to be liberalised, for achieving the objectives of development of all developing countries, economic growth of all trading partners and expansion of trade.

Restrictions on Trade in Services:

In order to understand the concerns and apprehensions of the countries of the South and the interests of the North in pushing these negotiations one has to examine the existing restrictions<sup>30</sup> on "Trade in Services".

Protectionism<sup>31</sup> has been growing in the international services trade. Traditionally restrictions for reasons of national interest and security were limited to financial services and communications. US is by far the leader in world services exports.

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30. Schott, n.11.

31. Brusick, Gibbs; n.25; Mashayekhi.

INCIDENCE OF RESTRICTIONS ENCOUNTERED BY  
AMERICAN SERVICE INDUSTRIES IN INTERNATIONAL MARKETS

Industry	Investment					Trade/Investment					
	Remittance and Repatriation Restrictions	Ownership Requirements	Personnel and Employment Restrictions	Taxes	Intellectual Property	Government Subsidies	Government Controlled Facilities	Licensing	Duties and Quotas	Standards	Restrictive Government Procurement
Accounting	x		x		x					x	
Advertising	x	x	x	x			x	x	x		
Auto/Truck Leasing		x		x	x			x			
Banking	x	x	x	x				x		x	
Communications		x	x			x				x	
Computer Services	x					x	x			x	x
Construction/Engineering		x	x	x	x	x		x		x	x
Education Services					x				x		
Employment Services							x				
Equipment Leasing	x	x									
Franchising	x	x	x	x	x			x	x		
Health Services	x	x	x			x			x		
Hotels/Notels	x		x		x	x			x		
Insurance	x	x		x		x		x			x
Legal			x					x		x	
Motion Pictures	x	x		x	x	x	x		x		
Civil Aviation				x		x	x				x
Shipping				x		x	x		x		x

SOURCE: Task Force on Services and the Multilateral Trade Negotiations, US Service Industries in World Markets, (Washington: US Department of Commerce, 1977), p.32.

Other nations placed barriers on the services trade in order to develop their own infrastructures as well as to protect their "infant" service sector. Analysis by the International Trade Administration and the US Trade Representative indicates a number of significant trends in this direction.<sup>32</sup>

- barriers to trade in services are growing in scope and severity.
- barriers in the developing and industrial countries are similar though more frequent and severe in less developed countries. Restrictions in developed nations, however, tend to have a greater trade impact.
- new barriers are beginning to arise over some previously unrestricted national service markets in area of electronic communications and information transmittal.

The same non-tariff barriers exist in services trade as in merchandise trade. Services trade is used by many countries to counter short term balance of payments difficulties and in recent years service restrictions have noticeably increased.

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32. Centre for Strategic and International Studies, George Town University, Services and the US Trade Policy, (Washington, 1982), p.15.  
 Also, J. Aronson & P. Crowley; Trade in Services: A Case for open markets cited in Terence G. Berg, Harvard International Law Journal, vo. 28, 1987, pg 2

In the first major study on non-tariff barriers to trade in physical goods, Baldwin<sup>33</sup> divided the major types of non-tariff barriers into twelve groupings:

- (i) quotas and restrictive trade policies;
- (ii) export subsidies and taxes;
- (iii) discriminatory government and private procurement policies;
- (iv) selective indirect taxes;
- (v) selective domestic subsidies and aids;
- (vi) restrictive customs procedures;
- (vii) antidumping regulations;
- (viii) restrictive business practices;
- (ix) controls over foreign investment;
- (x) restrictive immigration policies;<sup>34</sup>
- (xi) selective monetary controls and discriminatory exchange rate policies.

Services trade, though inherently different from goods in many respects encounters the same non-tariff barriers. The only above restrictions that might not apply to services trade are restrictive customs procedures and perhaps antidumping regulations. A study by the International Trade Administration

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33. First listed in R. Baldwin, Non-tariff Distortions of International Trade, (Washington: Brookings Institute, 1970).

34. US Department of Commerce, US Service Industries in World Markets: Current Problems and Future Policy Development, (Washington 1976), pp. 33-34.

substantiates this. According to this study problems of service industries were not exclusive ones and affected goods industries as well or plagued a specific sector and there were no service industries problem as such.

The first comprehensive analysis of services trade issues was done in 1976<sup>35</sup> by US Department of Commerce, entitled "U.S. Service Industries in World Markets". Although a distinct US bias is reflected most studies that have followed have merely restated the conclusions drawn from the original study.

The major conclusion drawn from analysis of the problems faced by service industries in international commerce is that their problems are predominantly investment oriented. Many service industries encounter obstacles or difficulties in establishing and operating affiliate abroad, particularly in LDCs. Generally these concern rights of establishment and ownership, foreign taxation, nationality restrictions on the employment of personnel, exchange restrictions, profit repatriation restrictions, protection of intellectual property, and means of international arbitration.<sup>36</sup>

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35.     ibid.

36.     Benz, n.9.

The eleven Baldwin restrictions<sup>37</sup> applying to services can be grouped into two major categories, for there is a thin line between investment and trade in services.

Investment/ownership problems:

1. restrictions on remittances and repatriation of profits, fees and royalties;
2. ownership restrictions that require full or partial local ownership or control of establishments and that may completely prevent market access by a foreign firm;
3. personnel restrictions, such as local labour requirements, licensing of professionals, visas and work permits;
4. discriminatory taxes, i.e. taxes placed solely or inequitably on foreign business income, profits or royalties.
5. inadequate protection of intellectual property, trademarks, copyrights and theft of technology.

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37. Baldwin, n.33.

## Trade/investment problems: 38

- vi. government subsidies to locally owned firms to aid their competition in the home market or in third country markets;
- vii. government controlled facilities, frequently having objectives other than earning a profit;
- viii. difficult or discriminatory licensing regulations licensing fees and taxes;
- ix. excessively high duties on imports of materials.
- x. absense of international standards and procedures for services;
- xi. restrictive or discriminatory government procurement requirement.

In 1976 using this format, US Department of Commerce study grouped and analysed its service industries according to whether the barriers they encountered were predominantly investment oriented (such as accounting, advertising, equipment leasing), banking, employment agencies, equipment leasing, hotels

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38. The description of the prominent restrictions facing the various sectors are adapted from the National Study, Shelp, Andre Sapir & Ernst Lutz, Trade in non-factor Services Past Trends and Current Issues (Washington: World Bank Staff Working Paper No. 410/1980).



and motels and legal services), trade and investment oriented (such as communications, computer services, construction and engineering services, education services franchising, insurance etc.) or predominantly trade oriented (such as air and maritime transportation).

Restrictions on services vary in different countries. Here in a list of the nature of restrictions facing the 18 groups of service industries as compiled by the US Department of Commerce is given.

Predominantly investment restrictions:<sup>39</sup>

In accounting, obstacles usually involve various means of restricting the establishment of foreign firms (Denmark, France, Germany), or government procurement practices (Brazil, Mexico). Other barriers lie in requirements that foreigners practice accounting only following a national exam (Belgium, Britain, Germany). Some international firms are also required to list with the firm's name the names of those associates who are titled accountants of that nation.

Advertising restrictions are usually in the form of licenses (Dominican Republic, Iraq), quotas (Canada), discriminatory taxes (Costa Rica, Surinam), embargoes on radio or television commercials (Canada, India, Italy, Korea), or restrictive technical agreements (Greece,

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39. *ibid.*

Indonesia, Mexico). Some countries require that foreign controlled advertising firms divest themselves partially or totally, and many firms have had difficulty in repatriating funds.

Auto and truck leasing forms the largest category of U.S. franchising in foreign countries, with more than 2,250 locations abroad. They are principally subjected to remittance of profit restrictions (Greece, Norway, Spain), and restrictions on foreign investments (Jamaica, New Zealand, South Africa).

Equipment leasing is a new phenomenon which is rapidly expanding at the international level, lessors being manufacturing companies, independent leasing companies, lease brokers and commercial banks.

The explosion of international banking services over the past few decades is probably the best example of the increasing interdependence of the international financial system. Banking activities internationally are restricted by the prohibition on establishment of foreign branches (Australia, India, Malaysia), limitations on the financial activities of foreign banks (Ghana, Japan, Korea, Nigeria), work permit requirements for foreigners which are issued infrequently or are subject to a quota (Australia, New Zealand, Singapore, Switzerland, Zaire), or the imposition of restrictions on remittances abroad (Brazil, Ghana, Italy, Korea, Zambia).



The international trade of legal services is somewhat smaller than might be expected, but similar to the accounting operations, they generally consist of regulations and requirements that disallow practice by foreign attorneys (Austria, France, Netherlands), or laws which limit the activities of foreign attorneys (Belgium, Switzerland).

Trade and investment restrictions: 40

In communications, exports tend primarily to be in foreign telephone operations, telex, and communications satellites, as well as the exports of consulting and managerial know how. This in turn often leads to direct export of US telecommunication equipment, another example of the close ties between the goods and services trade. The field also includes the radio and television industry.

One of the most common types of barriers involves restrictions on the use of privately owned communications lines, such as telephone lines or satellite circuits. Government controlled telecommunications authorities (France, Germany, Japan) have put limits on the use of leased lines, thus forcing multinationals to use more expensive volume sensitive public networks. American Express now spends \$ 10m. per year on leased lines.

Barriers facing the export of computer services are akin to those faced in the telecommunications field, and range from the establishment of foreign firms (Brazil, Israel, Italy, Japan), licensing (Belgium, France, Mexico, Netherlands), lack of patent and copyright protection for software (Australia, Austria, Canada, Greece, Hong Kong, Switzerland), and foreign investment income (Chile, Denmark, Iran, Norway, Portugal, Venezuela). Brazil even prohibits the importation of most data processing equipment and software that can be obtained domestically.

Construction and engineering services such as consulting, management and know how are finding themselves hampered by legal requirements that a majority of employees must be nationals (Brazil, India, Peru, Saudi Arabia, Tunisia), that foreign engineers have work permits (Finland, Iceland, Jamaica, Malaysia), government procurement policies (Argentina, India, Mexico, Nigeria), export subsidies (Britain, France, Japan, Korea), or difficulties in remitting earnings (Kenya, Senegal, Tunisia).

Exports of consulting services on school system design, operation and management are classified as educational services. Restrictions in this area include the appropriation of curriculum materials resulting from inadequate copyright laws (the pirating of school

materials), as well as the foreign bias against private educational expertise in favour of non-profit institutions.

Franchising is a method of operation of overseas sales common to auto and truck leasing, lodging, soft drink bottlers and fast food outlets, typically encountering such problems as restrictions on foreign ownership, lack of sufficient trademark protection, and limitations of royalty payments.

The export of health services, such as health care consulting services, hospital and clinical management, has at present a small presence. Some hospital management companies are established in a number of markets. Yet in many cases trade in health services is suffering from increased competition from government owned or financed operations and local ownership requirements, as well as other complications with the importation of foreign medical equipment and local ownership requirements.

Investments overseas by motion picture industries are primarily in marketing and distribution facilities. Trade in motion pictures is subject to quantitative restrictions (Australia, Egypt, India, Switzerland, Canada, Italy, Portugal), screen quotas in favour of domestic movies (Australia, Denmark, Greece), or

government subsidies. Some nations also put restrictions on investment income remittances for foreign distribution companies (Algeria, France, India, Israael, Pakistan).

Insurance companies operations overseas are often hampered by restrictions on ownership by foreign companies. These include nationalization (Australia, Canada, Morocco, Pakistan, Sweden), limitations on the scope of permissible activities (Korea, Thailand), requirements that all resident companies co-insure a portion of the business with state owned reinsurance companies (Italy, Singapore), or government procurement (Argentina, Indonesia, Jordan).

Predominantly trade restrictions:

Air transportation services international operations as a whole experienced a loss of \$ 2.53 billion in 1980. Industry investments are predominantly in marketing and ground support facilities to support the international operations. The industry is diffused with complex government regulation and subsidies, treaties, and national favouritism. Common problems include marketing and sales practices that favour national carriers like illegitimate discounts, overrides, rebates (Argentina, Belgium, Germany, India), discriminatory taxes (Guatemala, Indonesia, Thailand) or discriminatory landing fees (Britain, Haiti, Italy, Mexico).

In the field of maritime services, there is probably no one who is an expert. It is without a doubt the most complex service field, restrictions vary from such bilateral agreements as 50/50 clauses (Brazil, Chile, India, Singapore), special tax treatment in favor of national vessels (Argentina, Brazil, India, Phillipines), government procurement (Phillippines, Sri Lanka), or cargo preference schemes reserving all or part of a country's trade for transport in its own vessels (Australia, Egypt, France, Germany, India, Venezuela).

Negotiations at the UNCTAD Liner Conference came up with a fairly concise classification of shipping restrictions.

- direct subsidies for the construction, purchase, and improvement of ships.
- scrap and build schemes to renovate fleets.
- loans at low rates of interest.
- accelerated depreciation provisions on investment allowance or grants.
- exemption from income tax and other tax privileges.
- reimbursement of harbor dues, pilotage expenses and canal fees.
- financing out of tax revenue the deficits of state owned fleets or shipyards.
- contracts for the carriage of mail on favorable terms.



payments of freight at rates above world charter rates for government cargoes carried in national ships.

Talwar

The Negotiations in the GATT began with discussions on definition and statistical issues related to Trade in Services. In the Group of Negotiations on Services, Developing Countries like India and Brazil insisted on factual examination of service sectors which any eventual package for negotiations would cover. Seeing the variety and diversity of the services sector this approach was suggested. The French National Study on Services begins with a section devoted to definitions and statistics and states that "it is not easy to grasp clearly what is actually meant by the heterogenous aggregate of disparate activities that are covered by the term "Services" for the sake of convenience rather than because of their common economic characteristics.

These negotiations examined the existing international disciplines and arrangements for individual service sectors, and tried to build various negotiating alternative for modalities to achieve expansion of trade in services. These negotiations have dealt with definitional and statistical issues, conceptual framework and sectoral arrangements.

The debate has focussed on not only the US Transnational Corporations motive for liberalisation and push for open markets but also on the development concerns of developing countries thereby visualising the whole process of trade expansion through the adoption of multilateral framework as a means of development and growth.

The three basic considerations that developing countries have towards trade in services viz. the desire to protect infant industries, balance of payments difficulties; and the crucial role of services in infrastructure and their desire for a more favourable and differential treatment<sup>41</sup> are the major issues in negotiations between the developed and the developing world specially when the countries of the North are insisting on "transparency" and progressive liberalisation of the services trade.

The developed countries have realised the growing importance of services in their domestic economies and desire liberalisation in the area for they have a comparative advantage. The developing countries interests differ and they fear that western

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41. Andre Sapir - North South Issues in Trade in Services "The World Economy", March 1985.

emphasis on improved market access would permit powerful multinationals to muscle in on building indigenous service industries including those that are expected to play a crucial role in the developmental process.

The issue of trade in services involves a lot of complexities and bargaining in this area can proceed only after the initial hurdles of defining the term services, computing statistical data on services, identifying the various restrictions and barriers on services can be overcome.

In order to reach an agreement an effective consensus has to be evolved and the differences in opinion of the developed and developing world have to be carefully examined to see if there is a meeting ground. The countries of the North and the South must fully realise their rights and obligations in order to reach an agreement and must put whole hearted faith in GATT for this is the only forum that can effectively deal with an issue of such importance.

CHAPTER II

'MOTIVES, ATTITUDE AND STRATEGY' OF THE  
NORTH - 'BARGAINING FOR GAINS'

The Uruguay Round has involved scores of countries and dozens of issues. This chapter analyses the negotiating concerns, objectives, constraints and strategies, of the Key players on the issue of 'trade in services'. The American perspective is emphasised because United States most actively campaigned for negotiations and because its commitment is essential to launching and successful completion of any multi-lateral negotiations on political or economic issues. The interests of other industrial countries specially the European Community and Japan which together with the United States form the three pillars of the international trading system have been examined. With Canada, they compose the Quadrilateral which has met periodically since 1983 to discuss trade issues and have been urging that the GATT agenda should include 'trade in services' (known as 'trade in invisibles').

Service industries such as banking, insurance, telecommunications, data processing, construction and transportation are growing increasingly important in the World Economy. Services imports are restricted and discriminated against by a plethora of government regulations designed to protect domestic services.

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1. Aho (Michael C) and Aronson (Jonathan D): Trade Talks: America better listen; Council on Foreign Relations, USA, 1985.

The United States, Canada and Japan advocated in the Uruguay Round that an attempt to develop new rules, principles and procedures to manage trade in services should be made. The European Community joined them in March 1985 and officially added its support. These industrialised countries of the North have been pushing for liberalisation in and outside the GATT ever since. In September 1986, seventy four signatories of the General Agreement on Tariffs and Trade (GATT) adopted the agenda for the new round of multilateral trade negotiations which began in 1987, this agenda included services alongwith investment, agriculture, greater protection for intellectual property and improvement of the GATT dispute settlement mechanism on the insistence of US and its economic allies with the former threatening to abandon the GATT process if services were not put on the table<sup>3</sup> and the others showing

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2. In 1991, 107 countries are engaged in trade talks; Uruguay Round, The Times of India, New Delhi, July 13, 1991, p.11.
  3. In testimony before the Senate Finance Committee on November 14, 1985, shortly before a meeting of GATT Ministers, US Trade Representative Clayton Yeutter suggested that the United States "could, for example, convene a Conference here in Washington to negotiate trade matters of interest to the participants only... Non participants would not any benefits of such international agreements". 'Hints of new Round outside GATT', Financial Times, Nov. 15, 1985, at 7, Col. 2.

varying degrees of enthusiasm. The desire of industrial countries for an accord rests on the growing importance of services in their domestic economies. The bulk of employment in the West is now provided by public and private services and they account for a quarter of the World Trade.

The Role of Services in the Economies of the Developed States:

Service industries in the industrialised states have accounted for an increasing percentage of economic activity since the end of World War II. In the United States, the share of services in the (GDP) Gross Domestic Product rose from 48 percent in 1950 to nearly 70 percent today.<sup>4</sup> Similarly over 70 percent of available US jobs are found in the service industries.<sup>5</sup> Some 86 percent

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4. Magnet, Special Report: The Service 500, Fortune, June 10, 1985; p. 166.

5. See United States Trade Representative, National Study on Trade in Services, 75-101 (1983).

The study also points out that US service industries appear to be "recession-proof" by comparison with manufacturing industries.

During periods of recession, the Service economy has shown remarkable resilience while the goods producing sector has borne the brunt of the economic declines. Service employment has advanced by an average of 2.1 percent during contractions and 4.8 percent during times of economic expansion, while employment in the goods producing sector declined by 8.3 percent in recessions and increased by an average of 3.8 percent during recovery periods.

of the job growth in the United States economy during the past twenty years has occurred in the service producing sector.<sup>6</sup> The bulk of these jobs has been created in the high technology field.

The push for rules to govern services is consistent with the long term restructuring within countries and in the world economy as a whole. Goods production requires the use of services increasingly. Services which could never be traded before (eg. consulting, legal, data processing, design services) are being traded now signaling the emergence of a, 'World Information Economy'.<sup>7</sup> In essence services are the infrastructure on which future growth will depend. Unless countries extend the trading system to cover services and other related items such as international flows of information protection with regard to services could significantly hamper future trade in goods and services.

Service industries have become increasingly important in the economies of other industrial states as well. As a percentage of GDP, services have climbed from 51.8 percent in 1964 to 53.6 percent in 1981 in the United Kingdom during the same period, from 45.2 percent to 49.7 percent during the same period in West

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6. Terence G. Berg "Trade in Services": Toward a "Development Round" of GATT Negotiations Benefitting Both Developing and Industrialised States" - Harvard International Law Journal, Vol. 28, No.1, Winter 1987.

7. ibid.



Germany, and from 51.6 percent to 53.7 percent in France.<sup>8</sup> Although in Japan services declined as a percentage of GDP from 1964 to 1982, they rose as a percentage of total employment.<sup>9</sup> Such growth in the service sector corroborates economists predictions over the last forty years that industrialised countries would enter a tertiary stage (after agriculture and manufacturing) of economic development.<sup>10</sup>

The post war period has witnessed the fall of US from the position of the worlds largest exporter of services. In 1973, the United States exports accounted for 14.6 percent of the world market for proprietary rights and other business services, the largest single national share. In 1980, the United States was still the largest exporter by value of services (\$ 34.9 billion). The United Kingdom (\$ 34.2 billion), France (\$ 33.0 billion), West Germany (\$ 31.9 billion) followed closely. By 1983, however, the United States share had fallen to only 7.8 percent of world market. France, West Germany and the United Kingdom each exported more services by value than the United States. As the total value of trade in services increased, the United States Commerce

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8. See Spellman, "Services: US, EC Prepare for Talks; Stakes are High for the Fastest Growing Sector in Industrial Economies", Europe, Jan-Feb 1986, pp. 16, p.18.

9. Shelp R.K. : Beyond Industrialisation: Ascendancy of the Global Service Economy, New York, Praeger Publishers, 1981.

10. *ibid.*

Department<sup>11</sup> figures indicate that "the principal beneficiaries of the decline in the US market share are France, the East Asian NIC's newly industrialised countries Brazil and Mexico".

Statistics collected during the post world War II period shows a relatively consistent trade surplus in the services sector in United States while deficits in traded goods mounted. Due to an increase in import of services US trade surplus in services has fallen for three consecutive years. Absolute accuracy in measuring trade in services cannot be attained due to lack of data,<sup>12</sup> a disaggregation of the data that do exist and a lack of consensus about how to classify the data. The figures however, sufficiently demonstrate that service industries are a substantial and growing force in the economies of developed countries. Figures<sup>13</sup> on US service industries sufficiently demonstrate the growing share of services in the country's economy.

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11. Bureau of Economic Analysis, US Department of Commerce, US International Trade and Investment in Services: DATA NEEDS AND AVAILABILITY, 41 (1984).

12. *ibid.*

13. US Department of Commerce, US Service Industries in World Markets: Current Problems and Future Policy development, (Washington, 1976), pp. 33-34.

Accounting - The 1977 foreign revenues of the US 'big eight' accounting firms was \$ 1,374 m.

Advertising - In 1983 top 25 US firms earned revenues worth \$ 11,953 m. from overseas operations.

Auto and Truck Leasing, Equipment Leasing - In 1981, the foreign revenues of US equipment, auto and truck leasing, and service firms was \$ 13.4 billion.

Banking - In 1982, there were 900 foreign branches of US banks, with the assets of these branches exceeding \$ 341 billion.

The United States:

The United States has championed every post war multilateral trade round. The Regan Administration<sup>14</sup> addressed issues such as services, high technology products, intellectual property, dispute settlement safeguard, and agriculture where it felt that it had something to gain and hence called for a new round of trade negotiations.<sup>15</sup> The purpose was to halt the further disintegration of the trading system and distract attention from the growing trade imbalance.

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14. Gibbs M., Continuing the International debate on Services, 20, Journal of World Trade Law, 199-211 (1985).

15. See Brock, A Simple Plan for Negotiating on Trade in Services; World Economy, Nov. 1982, p. 235.

In 1982, the Global recession, the debt problem and the hesitation of some and opposition of other major trading nations prevented the Reagan administration from getting agreement to launch a new round at the 1982 Ministerial Meeting. In 1985, the timing was better and with the consent of other major industrial countries new trade negotiations were launched.

The administration had to decide on the issues to be tackled in consultation with the congress and with the private sector and develop a domestic consensus necessary to complete a successful negotiation. It was seen that successful trade negotiations would increase the worldwide growth and would help restore confidence in the trading system; failure would further undermine the system.

The most explicit expression of United States goals for Trade in Services is attached as an appendix to the United States Trade Representatives Annual Report to the President of the United States on the Trade Agreement Program 1984-85.<sup>16</sup>

The Trade Representatives Report states that services must be included in the GATT because advances in technology make services increasingly tradeable and because the services sector of the world economy

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16. Appendix II.

continues to grow without any uniform international norms for its treatment. The Report identifies GATT as the most appropriate forum to deal comprehensively with services because trade in services is closely linked with trade in goods in the world economy.<sup>17</sup>

The general goal of the United States,<sup>18</sup> according to the Trade Representative, should be:

1. the establishment of a legal framework of rules and procedures that would
  - (i) make trade in services as open as possible through a commitment to transparency of practices and the resolution of problems through consultation, and
  - (ii) negotiate commitments of a sectoral or functional character dealing with problems unique to individual service industries.

In addition to these overriding goals, the US Trade Representative (USTR) mentions specific elements that should be included in any agreement to liberalise trade in services. This is an implicit recognition of the fact that no service agreement can resolve all service trade issues simultaneously. The USTR advocates

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17. Appendix I, US Trade Representative Annual Report to the President of the United States on the Trade Agreements Program, 1984-1985.

18. *ibid.*

including in any initial accord agreements on specific procedures for addressing, unresolved problems.

According to the USTR any services agreement should include a commitment to transparent practices which would require that all parties to the agreement notify each other of specific laws and regulations intended to protect domestic service industries. Such notification is seen unnecessary because barriers to trade in services often take the form of domestic regulations and practices that act as non-tariff barriers. In the United States view, regulations not specifically identified as protectionist must be intended solely to advance national sovereignty. The trade representatives<sup>19</sup> (STR) argument assumes that, "transparency, ideally would distinguish autonomy consensus from protectionist ones." Transparency would at least favour an explicit regulatory regime of subsidies or market restrictions over a system in which government agencies use vague, unpublished standards to grant or deny foreign firms Licenses to trade.

The USTR also favours a rule requiring that foreign service companies be treated in the same way as domestic service companies.<sup>20</sup> Regulatory procedures

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19. *ibid.*

20. The United States recognised that such a rule would have to be applied flexibly since certain regulations applied equally to foreign and domestic service firms, would deny foreign firms access to domestic markets for eg. in the case where a government prohibited both foreign and domestic firms, on an equal basis from competing in certain government controlled sectors of the economy.

should be open, as in the "notice and comment" approach to rule making practiced by US administrative agencies, to allow foreign service providers a voice in the rule making process. This "due process" goal goes beyond mere transparency in that it allows foreign service providers to participate in rule making.

Further, the United States seeks rules to prevent domestic public monopolies from competing unfairly with foreign firms. Many service industries, particularly in developing countries, are carried on exclusively by publicly owned enterprises. Public monopolies, accordingly can achieve a comparative advantage by dealing with the home markets on terms that allow the public sector to absorb costs. In effect the public sectors subsidizes the monopolys operations in the less regulated markets of other States. The USTR proposes a rule that proposes an arms length relationship between the monopolistic service industry's monopoly activities and its activities as an international competitor.

In addition to its specific proposals - transparency, national treatment, the process rule making and curbing unfair competition by monopolies, the United States would in any agreement to liberalise services trade a general legal framework to govern future negotiations and the settlement of disputes. The USTR<sup>21</sup> recommends that the

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21. Gibb, n.14.

United States bargain in any initial agreement on services trade for a commitment by all parties to future negotiations on specific issues. The legal framework would specify the commitments already undertaken, as well as the rights and obligations of the parties to the agreement. Subsequently negotiations would be designed to create a series of supplemental agreements addressing problems specific to individual service sectors. Subsequent talks moreover could focus upon issues of a functional nature - such as intellectual property rights that pertains to all service sectors. The general framework would also provide, in the event of a dispute under the initial agreement on services, for consultation procedures akin to those currently mandated under GATT for problems relevant to trade of goods. The consultation mechanism would include an independent panel to resolve disputes and procedures allowing for compensation to parties injured by government practices inconsistent with the agreement.

Finally the USTR favours<sup>22</sup> including at least a partial resolution of issue of service related investment in any initial agreement. This aspect of the US position derives from a perception that barriers to service related foreign investment deny commercial opportunities to US service firms.

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22. Gibbs, n.14.



The US proposes that, at a minimum, a service trade agreement should guarantee the right of foreign service companies to establish a commercial presence in host countries to market the imported service. US position on investment is vague and ill defined.

The United States has important stakes and economic incentives involved in negotiations on services. Their negotiation position is designed with a view to retain their former position of largest exporter of services. There has been a recent shift in emphasis from liberalisation of trade in goods to trade in services for it is realised that US would have a comparative advantage since its economy has become more service oriented. The US National Study submitted to the GATT argues that the removal of barriers to trade in services would be consistent with "the generally accepted principle that trade based on comparative advantage promoted economic efficiency and benefits all trading partners....."<sup>23</sup>

A shift of comparative advantage to the area of services would explain the strong interest of the United States in liberalising service trade. Even if it is too soon to tell whether such a shift has occurred the dominant role of services in production and employment in the US economy provides a sufficient explanation for

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23. Murray Gibbs and Mina Mashayekhi, Services: Cooperation for Development, Journal of World Trade Law, No.2, Vol. 22; 1988, pp. 81-107.

the push for freer trade in services. The diminishing US share of the world market for services provides added motivation for liberalisation.

United States Trade Representative Clayton Yeutter had conditioned US participation in the next round of GATT talks on the inclusion of services in the agenda.<sup>24</sup> He said that the next round would determine whether the GATT "lives or dies".<sup>25</sup> Yeutter suggested in a congressional Committee that the United States could convene a non-GATT multilateral trade negotiation session for those parties interested in discussing services, if developing countries continued to oppose even putting service talks on the GATT agenda. He added that the developing countries that refuse participation should be excluded from whatever benefits might arise out of the non-GATT talks and the US should withdraw its special tariff concessions from developing nations that refuse to participate in the new round.

These policy statements were delivered just weeks before the compromise on services was reached at a GATT meeting and clearly indicate the significance of the services issue to the United States. But it also demonstrates the importance that participation and acquiescence of the developing countries holds for the

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24. See Yeutter Cites Preconditions on Trade Talks, Journal of Commerce, Dec. 9, 1985, 3A.

25. Ibid.

United States on the issue of trade in services. The emphasis in the Trade Representative Report on perceived barriers in less developed countries provides some explanation for the industrialised states desire to include LDC's in the negotiations.

The President of the US and the Congress<sup>26</sup> share the authority to negotiate trade agreements. The President has powers to negotiate on trade matters under the constitutional authority to regulate foreign commerce. The President may negotiate trade agreements but if the agreements require a change in the law, which multilateral trade agreements generally require the Congress must approve the statutory changes.

For past rounds of multilateral trade negotiations, the Congress has delegated some of its authority to the President. The Trade Act of 1974 has authorised the President to agree to and implement by proclamation 40 percent tariff cuts. It also directed the President to negotiate on non-tariff matters in the Tokyo Round and provides for fast track consideration. The Government implemented the Tokyo Round non-tariff agreements by enacting the Trade Agreements Act of 1979.

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26. Lenore Sek; Trade Negotiations: The Uruguay Round, CRS Issue Brief, April 16, 1990, p. CRS 10.

The President began negotiations in the Uruguay Round without congressionally delegated authority. At the time, however, Congress was considering legislation to extend negotiating authority to the President and subsequently approved authority under the Omnibus Trade and Competitiveness Act of 1988 (1988 Trade Act). This Act extended the authority for the President to enter and proclaim tariff agreements if the agreements are reached by May 31, 1993<sup>27</sup> and also extended the President's authority to negotiate non-tariff agreements. The 1988 Act designated negotiating objectives which gave congressional direction to US negotiators. It listed specific objectives on 16 subjects such as agriculture, dispute settlement, unfair trade practices, services and intellectual property. Many of these objectives were those just has been announced by US negotiators before the start of the Uruguay Round.

The issue of trade in services was taken up in 1984<sup>28</sup> with the passage of the Trade and Tariff Act (1984) that provided the United States Administration with a mandate to negotiate on services and identified the issues to be raised. Among its stated purposes are to "improve the ability of the President to identify

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27. *ibid.*

28. Murray Gibbs and Mina Mashayekhi - Services: Cooperation for Development. Journal of World Trade Law, No.2; Vol.22; 1988; pp. 81-87.

and analyse barriers to and restriction on US trade and investment and to achieve their elimination, as well as that of encouraging the expansion of international trade in services through the negotiation of bilateral and multilateral agreements which reduce or eliminate barriers to trade in services.

The first step in this process as provided by the Act is - identification of barriers, second step is to take action to achieve the stated objectives -

- (a) by negotiations and consultations,
- (b) by leverage of unilateral retaliation by the United States under Section 301 of the Trade Act of 1974.

With regard to the latter approach the 1974 Act has been amended to increase its effectiveness with respect to services, investment and high technology.

Retaliation under Super 301<sup>29</sup> of the US Omnibus Trade and Competitiveness Act of 1988 implies that the President could impose discriminatory restrictions on imports of goods from an individual country in order to retaliate for its denying right of establishment or national treatment to US service Trans National Corporations. In fact, the US has actually threatened

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29. *ibid.*

to do so in certain cases. The professed aim of the United States in implementing Super 301 was to put an end to unfair trade practices and trade barriers and trade distorting practices through bilateral and multi-lateral negotiations.

A 301 investigation<sup>30</sup> includes such finding, consultations with the affected domestic industry, consultations with the foreign government involved, and where applicable, use of dispute settlement procedures under existing trade agreements. In investigations initiated as a result of Super 301 process, the statute requires the United States Trade Representative seek to negotiate agreements which provide for the elimination of, or compensation for the practice within three years. It is provided that if agreement is reached, the investigation shall be suspended and annual reports shall be submitted to the Congress during the next three years of progress made towards eliminating the practice. If non-compliance with the agreement is later found, the USTR must continue the investigation as though it had not been suspended. If no agreement is reached the USTR makes the "unfairness determination" and also determines the retaliatory action. Retaliatory measures may include increased

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30. Times Research Bureau, Times of India, New Delhi, 1990.

tariffs quotas on imports, restrictions or fees on services, withdrawal from a trade agreement or other appropriate action. If retaliatory measures are imposed under Section 301 they may be modified or terminated at any time and they automatically expire after four years if not renewed. This Act gives the United States Trade Representative the right to identify trade liberalisation priorities including priority countries and priority practices. Priority practices are defined as "those the elimination of which is likely to have the most significant potential to increase United States exports either directly or through the establishment of a beneficial precedent."

The European Community: <sup>31</sup>

The European Community nations have been plagued by High Unemployment rates and a stagnant economic outlook. The number one European priority is jobs. Between 1973 and 1985 no new net jobs were created in the Community and the unemployment rates have increased monotonically. In the best growth years of 1960's and 1970's West European employment only expanded by 300,000. There is not much hope in the future, for the labour market is highly inflexible. On account of strict jobs protection laws and generous unemployment insurance

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31. Philip Hayes, "Trade and Adjustment Policies in the European Community" (London : Trade Policy Research Centre, July 1984).

benefits. Between 1970 and 1980 both the United States and Japan generated nine jobs for every ten entrants into the labour force while the West European economies<sup>32</sup> created only about four new jobs for each ten new entrants. The community economy<sup>33</sup> has been beset by many problems resulting in Eurapessimism. Since it is easier politically to blame these failings on scapegoats beyond the border than to change deeply embedded social policies the community has been less than keen on maintaining open markets and further liberalising trade.<sup>34</sup> It has advantages in certain services sectors and has been enthusiastic in getting maximum gains out of liberalisation in those sectors and hence progress has been made to forge EC-wide policies on trade in services. On the other hand external talks are seen to provide Brussels a stronger mandate to carry out internal rationalisation and spur comparative action within the European Community.

Trade negotiations if it is realised can also yield important new export opportunities for European firms. European businessmen are highly impatient with the one way street in trade relations with successful

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32. OECD, Employment Report (Paris: OECD, 1984).

33. Hayes, n. 31.

34. Miles Kahler, "European Protectionism in theory and Practice", "World Politics", Vol. 37, No. 4 (July 1985), pp. 475-502.



developing countries, that is the "easy" access to Europe as against the "hard" access to South Korea, India, Brazil and other LDC markets. Joint US-EC-Japanese pressure could help persuade these countries that reciprocal concessions are a good idea.

Like the US, Europe has pressed Japan to liberalise trade in areas that would benefit EC exporters i.e. selected services, such as insurance, finance and management consulting. The EC ran an average surplus with Japan on services of almost 2 billion E.C.U. per year from 1979 to 1982 while its merchandise trade was in deficit by more than 8 billion E.C.U.<sup>35</sup>

The EEC initially appeared sceptical of the United States initiatives to include services in multilateral trade negotiations. However, it subsequently favoured services negotiations and currently supports a multilateral framework of principles and rules to govern international trade in services.<sup>36</sup> The EEC is not in favour of all regulations being liberalised and insists on a distribution between appropriate and inappropriate regulations. The EEC also considers that different

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35. The figures are from Eurostat as cited in 1984 EC submission to the GATT on Trade in Services.

36. The EEC Service Exports are three times higher than the United States cited in Eurostat (1984).

service sectors have their own characteristics and that a future multilateral framework should take these into account. The EEC also considers that progress in the Group of Negotiations on Services should not be quantitatively linked with other areas of the Uruguay Round although the results of the negotiations would have to be examined as a "single political undertaking".<sup>37</sup> The EEC has already adopted extensive regulations governing liberalisation of the services sectors in traditional and new technologically advanced areas.

In contrast to the United States which was pushing the pace of negotiations to complete an overall framework in services by mid 1988 the EEC pursued progressive liberalisation based on a set of principles for determining "appropriate regulations", and believes that a final agreement would be possible only through "mutual advantage" for industrial and third world nations.

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JAPAN:

In recent years, Japan has successfully pursued a policy of export-led growth and amassed huge trade

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37. C. Michael Aho and Jonathan David Aronson; Trade Talks; America Better Listen, Council on Foreign Relations USA, 1985, pp.

38. Gary Saxonhouse, "The Micro and Macro Economics of Foreign Sales to Japan", in William Cline, ed. Trade Policy in the 1980's (Washington: Institute for International Economics, 1983), pp. 259-85.

surpluses with most of its major trading partners. After recovering from the second oil shock by the end of 1980, Japan's cumulative current account surplus exploded from 4.8 billion dollars in 1981 to 45 billion dollars in 1985.<sup>39</sup> As befits the sweepstakes winner in the world trade race, Japan helped orchestrate the Bonn Summit call for a new round of trade negotiations. Japan has no bilateral agenda and is not aggressively pursuing negotiations. In fact, its main goal is to avoid a protectionist backlash. Japan has more to gain from the negotiating process than from the actual conclusion of agreements - agreements that would likely require Japan to make substantial concessions.

Indeed many governments and business leaders in the US and Europe believe that the "Japan Problem" is the key issue on the trade agenda opening the Japanese markets to imports and redressing Japan's bargaining trade and current account surpluses are regarded as the sine qua non for successful negotiations. On the subject of multilateral negotiations including the extension of the GATT to new areas such as services, the Japanese were early and consistent supporters of US efforts. Prime Minister Nakasone was the first head of State publicly to call for a new round of

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39. C. Fred Bergsten and William R. Cline, *Policy Analysis in International Economics* (Washington: Institute for International Economics: 1985).

talks. This was a clever diplomatic move of the Japanese, made them appear as cooperative actors in the trading system and cost them nothing in terms of concessions. Japan realises that they can continue to open their markets without worry for cultural, linguistic and other invisible barriers will prevent the flooding of their markets with foreign imports.

The Other Developed Countries:<sup>40</sup>

Canada, Sweden and Switzerland are the only ones worth mention amongst the other industrial countries for they have internationally competitive high technology and service industries. Sweden and Switzerland are particularly sensitive to restrictions- especially export controls on access to new technologies in electronics, telecommunication and robotics. Large markets are needed to afford economies of scale in production and to recoup massive R&D costs over a short period of time. To stay abreast these countries would benefit from multilateral rules:

- (1) to discipline extra territorial national controls, often enacted and enforced in the

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40. Jeffrey J. Schott and Hufbauer; Trading for growth: the next round of trade negotiations: Washington, DC: September, 1985.

overly broad search for national security and perhaps masking protectionist intentions.

- (2) to promote national treatment and establishment rights, which would help further the activities of Swedish and Swiss firms in foreign markets, and
- (3) to extend GATT rules to cover trade in services, particularly banking, insurance and telecommunication services.

A major Nordic strategy<sup>41</sup> with the larger multilateral talks, will involve closer EFTA-EC trade. Many of the concessions that the Nordic countries and Switzerland would be called on to make would fall in the agriculture area. Swiss agriculture is even more protected than EC agriculture. An other protected area is textile and apparels and these highly successful trading countries still have valuable bargaining chips to play in the Growth Round.

CANADA: 42

Canada has been a strong supporter of GATT since its very inception. In the new round Canada, like

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41. According to some studies, Swiss farm subsidies total between SF 3 billion and SF 5 billion a year: Financial Times; 1 August 1985, p.4

42. Schott and Hufbauer, n.40.

United States, wants progress on services. Canada is far more enthusiastic about the need for negotiations than the Europeans are.

Industrial Countries broadly agree on few fundamental principles that would be part of any framework accord for trade in services. These include non-discrimination between a trading partners, national treatment (giving foreigners the same rights and obligations as domestic service providers, including rights of establishment markets access and regulatory restrictions) and transparency (publication of rules and regulations affecting trade in services).

These countries disagree on how such a framework accord would operate and on how the general principles would be translated into practice. The USA wants a tough multilateral framework which would apply directly to most if not all of the 150 service sectors it has identified. Agreement on the framework would be followed by negotiations on sectoral coverage during which countries could place markers on rules or restrictions they would not wish to immediately bring into conformity with the framework contract. At the same time, a detailed list of service industries would be established to which the framework contract would apply in all countries. The USA has suggested that, if governments do not want openly to state which industries they regard as candidates for liberalisation,

they could notify the GATT Secretariat anonymously.

The EC and others argue that it is simply not practical to agree to a set of general rules without knowing how these might apply in individual sectors. This is a view strongly endorsed by developing countries which are even more unwilling to sign a "blank cheque" on services, especially since they see no benefit for themselves.

Behind these differences of approach<sup>43</sup> lie obvious differences of interest. For countries with a wide range of well developed service industries a comprehensive overall framework is a good deal more attractive than for countries with a few or no strong service sectors.

It is possible that the USA could change track once some of its own highly protected service industries, such as shipping and airlines, wake up to the implications of trade liberalisation.

Even the EC, which is the biggest exporter of services in the world, does not want to liberalise trade in all sectors. The Community wants the freedom, for eg. to protect its cultural industries

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43. William S. Zartman (ed.) Positive Sum: Improving North-South Negotiations, New Jersey, USA, Transaction Books, 1987.

like broadcasting and films from foreign domination and is not yet ready to accept free competition in telecommunications.

The North led by the United States has fostered since the GATT ministerial session in 1982 the idea of inclusion of services in the GATT. The US objectives are:

- (a) create a legal framework of rules and an international regime of discipline;
- (b) provide national treatment, market access, transparency, open regulatory procedures and dispute settlement for service firms located abroad, and
- (c) wherever foreign investment is a prerequisite for trade in services, the service firms should have the right of presence in overseas markets.

The declared aim is to make trade in services as open as possible, through a progressive dismantling of all prevailing barriers to such trade.

The proposed US model<sup>44</sup> visualises: a) minimisation of the role of state in economic activities; b) freezing the so called barriers to trade in services at the present level (restrictions on entry of foreign

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44. Raghavan Chakravarthy: Recolonisation; GATT, the Uruguay Round and the Illid World, Penang, Malaysia: Third World Network, 1990.



enterprises, including practices such as performance criteria, restrictions on repatriation of profits etc.)

- c) preventing introduction of new barriers; and
- d) securing for Transnational corporations (TNCs) the maximum freedom of operation. Armed with this new international framework US and her allies in the industrial world visualise exchanging concessions in goods against services.

The motives are clear, the developed countries want to make a concerted effort to reshape the existing international trading system that would promote maximum freedom for TNCs to operate in the developing countries; and through that they would like to impound the autonomy of developing countries to pursue independent economic policies.

On analysing these objectives, one question that emerges is, Will liberalisation help developing countries i.e. what would be the implications and subsequently what should be the strategy of the developing countries in dealing with this issue of "trade in services", so that they can benefit from these liberalisation efforts of the North.

CHAPTER III

TRADE IN SERVICES AND THE DEVELOPING COUNTRIES :  
IMPLICATIONS AND STRATEGIES

Within the developing world there is a great divergence of interests. While dealing with the industrial world on economic issues, developing countries try to maintain a united front, using solidarity as a strategy to achieve their objectives. With regard to planned trade negotiations, it is always the largest, and most influential of the developing countries<sup>1</sup> that dominate the stage. Brazil, Argentina, India, Indonesia and a few other middle level powers tend to be most influential. Even though many smaller countries do not agree completely with India and Brazil on critical issues and their true interests are not clearly reflected in the presentation made by these top developing countries, they have so far not threatened the Developing Countries' united front. So long as Less Developed Countries group themselves as a bloc,<sup>2</sup> the industrial countries treat them as one. Most of the LDCs have exhibited little enthusiasm for new trade negotiations. Disappointed by the results of the Tokyo Round, the LDCs are more

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1. Henry R Nau, "The NICs in a new Trade Round" in Ernest H Preeg, ed, Hard Bargaining Ahead: US Trade Policy and Developing Countries (New Brunswick) NJ: 1985; pp. 63-83.
  2. J. Aronson, Trade Talks; America Better Listen; New York, 95 (1985). Also see Karl Sauvant; The Group of 77: Evolution, Structure and Organisation (New York: Oceana Press, 1981); Gerald nelleriner, ed., International Economic Disorder: Essays on North South relations (Toronto 1981).

interested in parallel negotiations<sup>3</sup> on development finance and debt than in trade talks. Brazil and India, the two most active LDC participants in the Tokyo Round, have been the most vocal opponents of launching a new round. Their concerns are two fold - they see little evidence that developed countries will commit themselves to significant trade liberalisation in LDC sectors of comparative advantage, such as labour services; and India & Brazil hesitate to negotiate more liberal rules for services trade in the face of strong political opposition from their own highly protected firms.

#### The Role of Services in the Economies of Developing States:

Services account for a large share of economic activity in both developed and developing countries.<sup>4</sup> In the United States for instance, almost 67 percent of GNP and 74 percent of civilian, non agricultural employment is in services. On the other hand the share of services in GNP in LDC range from 29 percent

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3. Anne O Krueger, Foreign Trade Regimes and Economic Development : Liberalisation Attempts and Consequences (Cambridge: Ballinger, 1978).

4. Terrence G. Berg, Trade in Services: Towards a "developmental round" of GATT negotiations benefitting both developing and industrialised states. Harvard International Law Journal. 28(1); Winter 87; 1-30.

for low income economies, to 49 percent for medium income, and to 52 percent for upper-middle income LDCs. Employment in services<sup>5</sup> varies from 5 percent of the work force in Nepal to 64 percent in Kuwait. But services have been growing at a faster rate in LDCs than in industrial economies. Between 1973 and 1983 the average annual growth rate for services was 2.1 percent in the industrial nations, 1.3 percent in the high income LDCs and 5.3 percent and 5.0 percent respectively in the middle and low income LDCs.

Data on the role of services in developing States are less than complete.<sup>6</sup> Existing data indicate that services industries are large and growing. National account statistics do not give a clear picture of what is at stake in international trade negotiations. They include out employment by national and local governments. They exclude services that are provided in the production of manufactured goods and workers performing service jobs in non-service sectors. As a result they both exaggerate the scope of activities that could be affected by trade negotiations and underestimate the impact of services in the national economy.

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5. Editorial - Trade in Services: Issues and Policy Options. Mainstream Annual, 1986 reproduced from World Economy in the mid-eighties, (RIS) New Delhi.

6. *ibid.*

In 1979, services represented approximately 40 percent of the gross domestic production (GDP) of developing countries. The trade and finance service sector is the largest service activity in both the developed and developing countries. During the 1970s, this sector grew in developing countries from 44.6 percent to 50.6 percent of total services while maintaining a relatively constant share of total services in developed countries. Other categories of services, including educational health, legal, business and hotel services, declined from 26.4 percent as a share of services in developing countries to 19.2 percent while growing in developed countries. Growing service sectors in LDCs do not produce international trading strength. While several developing states were listed among the twenty five largest service exporters in the 1980 many other LDCs registered trade deficits in services during the years 1977-82. Though services account for close to 20 percent, by value, of the total export of goods and services from industrialised states to developing states, they represent only seven percent of the total trade flows in the opposite direction.<sup>7</sup>

Developing nations vary markedly as to the size

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7. Sapir, North-South Issues in Trade in Services, World Economy, 27, 34 (1985).

and composition of their services accounts and the international competitiveness of their service sectors. Analysis of the services accounts of six major LDCs in the 1980s show sharp differences between those with high debt burdens and those whose foreign debt is relatively low. For instance, High debt<sup>8</sup> LDCs (Brazil, Mexico, Argentina) have large invisible deficits due primarily to payments on factor services (i.e. debt servicing). Trade negotiations<sup>9</sup> can have an indirect effect on this problem but only if the debt issues are given priority in multilateral talks. On the other hand low debt LDCs (Korea, Singapore and India) have strong services accounts and traditionally run surpluses (Korea runs a small net deficit when factor payments are included).

#### Development and Services:<sup>10</sup>

The developing countries have recognised the importance of 'services' in development. The basic economic "infrastructure" of a nation is comprised of services mainly transportation, banking, insurance and communication services are a critical requirement

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8. William Brock, "Trade and Debt: The Vital Linkage", Foreign Affairs. Vol. 62, no. 5 (Summer 1984), pp. 1037-58.

9. Krueger, n.3.

10. Cf Gary Clyde Hufbauer and Jeffrey J. Schott (ed.) Trading for Growth: The Next Round of Trade Negotiations, (Washington: Institute for International Economics, 1985)...

for the furtherance of many developmental objectives-like better health care, education, and food distribution. Services are seen to be integrally involved in the production and distribution of manufactured goods and commodities and provide an important channel for transfer of technology. It is a recognised fact that "services dramatically effect the over-all development performance of countries".

While the LDCs recognise the importance of services to development they are apprehensive about liberalising of services trade. They fear that liberalisation may hinder economic growth<sup>11</sup> and their ability to manage development policies. They see little to gain and much to loose and their concerns are based on three perceptions:

- (i) LDCs do not have a comparative advantage in traded services;
- (ii) their infant service industries need protection; and
- (iii) liberalisation would impinge on national security and sovereignty.

#### Comparitive Advantage:

The developing countries believe that since they have comparitive disadvantage in services they would

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11. United Nations Conference on Trade and Development, Services and the Development Process, Summary and Conclusions, Report by the UNCTAD Secretariat, 2 August 1984, p.1.



not gain from the liberalisation of services trade. These countries fear that liberalisation would lead to an increase in imports giving unfair competition and hampering the development of indigenous service industries leading to increased current account deficits, and condemning the third world to being "permanent importers of services and high technology goods".<sup>12</sup>

Recent studies have established that the principle of comparative advantage can be applied to trade in services. The theory of comparative advantage suggests that merchandise trade patterns are determined by relative factor endowments. Brian Hindley and Alasdair Smith have concluded that "services are different from goods in ways that are significant and that deserve careful attention but the powerful logic of the theory of comparative advantage transcends these differences".<sup>13</sup> Andre Sapir and Erust Lutz found that countries with abundant physical and human capital were most likely to be services exporters.<sup>14</sup> Their findings confirm the notion that comparative advantage in services lies with the developed world. But it does not mean that LDCs

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12. Paulo Nogueira Batista, Brazilian Ambassador in Geneva, as cited in the New York Times, 2 October 1985, p.D19.
  13. Brian Hindley and Alasdair Smith, "Comparative Advantage and Trade in Services", The World Economy, December 1984, p. 389.
  14. Andre Sapir & Erust Lutz, Trade in Services: Economic Determinants and Development Related Issues, World Bank Staff Working Paper No. 480, Washington, 1981, p. 31.

have little to gain from liberalised trade in services. As in goods trade, the gains from international trade in services come from improved efficiency from specialisation and increased trade flows. Though a country may have absolute disadvantage in services trade it can have a comparative advantage in the export of certain services. A number of LDCs have proven to be successful exporters : Korea and India in construction services, Singapore in transport and financial services.

LDC firms are using the experiences gained in building roads, bridges and waterways at home to export construction services. The Hyundai Engineering and Construction Company Limited of South Korea ranks among the top five contractors in the world, building ports, shipyards, industrial plants and commercial and residential facilities primarily in the Middle East, and South East Asia. The Brazilian construction and engineering firm of Construtora Mendes Junior SA has over 12000 workers abroad, with total contracts valued at \$ 2 billion, through Latin America, the Middle East (Iraq) and Africa (Tanzania, Nigeria).<sup>15</sup> Advances in technology are making it easier for the LDCs to capitalise on the advantages of low cost, skilled

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15. Bancodo Brasil, S.A. - Cacex "Uma Opcao de Crescimento", Information Sen and Cacex, Rio de Janeiro, 5 November 1984 cited in Schott (Jeffrey J) and Mazza (Jacqueline) Trade in Services and Developing Countries, Journal of World Trade law, 20(3); May/June 1986, 253-73.

labour. Data processing centres and engineering design units, linked to foreign corporations through international telecommunications networks, already are flourishing in countries such as India and South Korea. LDCs can profit from their comparative advantage in labour even in a capital intensive industry such as airlines. Singapore Airlines is one of the most efficient in the world, not because it holds a capital advantage but because of its low labour costs and better service.

#### Infant Industries Protection and Liberalisation:

The LDCs are concerned about protecting their infant service industries for they feel that opening their economies would bring in competition from highly developed services specially in sectors like banking, telecommunications and insurance which are dominated by multinational firms. They also feel that their firms lack the capital resources and the experienced personnel to compete effectively. LDCs need to consider whether protection may lead to obsolete technologies and economic structures, tie up scarce capital resources, and inhibit growth. In fact protection may be the very road block which prevents the development of a competitive industrial and service economy.

#### Infringement of National Security & Sovereignty and Cultural Consequences:16

LDCs fear that opening up their services sectors

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16. *ibid.*

to foreign competition could infringe their national security and sovereignty in three ways. First greater liberalisation would allow powerful multinationals to muscle in and dominate the traditionally domestic sectors. These firms would be difficult to regulate and could make decisions detrimental to the national interest (eg. exporting capital; retaining technology in-house). Foreign participation in the media, arts and entertainment industries has social and cultural consequences as well.

Secondly free services trade could involve removal of certain controls on foreign investment which could infringe on national sovereignty and economic ambitions.<sup>17</sup> LDC skepticism about foreign investments is based on the fear that it could result in misapplication of technology, can stifle local initiatives and can side track domestic borrowers in local capital markets.

#### State Ownership and Services Trade:

Third, state controlled or owned firms would be subjected to greater international competition, which could drive them out of business or reduce their influence. LDC policy makers want to retain political

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17. Prem Kumar, Indian Commerce Secretary as cited in the New York Times, 2 October 1985, p.7.

and economic control that comes with state ownership,<sup>18</sup> particularly in new, high technology sectors, Brazil in the informatics sector, and want to insulate defence, transportation and infrastructure services.

MNC's and the Developing Countries:

On analysing the developing countries concerns and opposition to freer trade in services one can clearly discern their motives and understand their policy position. Third World nations, in general, want to preserve autonomy over development of their service economies. The fear of transnational corporations strengthening their influence in LDC markets and economies and unfair competition to their infant industries in the services sector are issues of concern. The LDCs want a separation of the issue of foreign direct investment from the issue of trade in services. Third World Nations do not want to discuss services under GATT auspices, since such a discussion could imply that the GATT principles developed in the context of trade in goods would apply equally to services. Some developing countries have fundamental differences of opinion with the North over the efficacy of commercial competition as the most equitable means of development.<sup>19</sup>

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18. C. Diaz - Alejandro & G. Helleiner, "Hand Maiden in Distress: Worldtrade in the 1980s" (Washington: Overseas Development Council, September, 1982).
19. Malmgren, Negotiating International Rules for Trade in Services, World Economy, 11, 21 (1985).

They fear the potential loss of sovereignty and freedom of action to guide the services domestically according to their own political objectives.<sup>20</sup> National Security interests particularly in computer-telecommunications systems, transport, and shipping, also motivate the developing countries reluctance to grant market access to foreign service industries.<sup>21</sup>

Protection vs. Liberalisation: weighing the alternatives:

LDCs have deep rooted concerns about the implications of services trade liberalisation for their economic development and therefore tend to impose protectionist regulations on their services industries.

The LDCs viewpoint is that regulation of service industries safeguards important national interests ranging from the area of monetary policy to defence. But in many cases regulation masks protectionism, creating distortions and impediments to growth. In particular it serves as a disincentive to technology transfer and inflows of foreign direct investment needed to spur economic development.

LDCs thus face a series of conflicting policy choices. It is questioned whether LDCs would be better

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20. *ibid.*

21. Sapir, Trade in Services: Policy Issues for the Eighties, 17. Columbian Journal of World Business, 1982, 77-81.

off if they had access to via trade and investment to advanced technologies? Are the LDC concerns regarding development and sovereignty justified. The most pressing need for LDCs, is additional sources of development finance, and protectionism creates a disincentive to inflows of foreign, official and private capital. It can be argued that an improved investment climate, devoid of protectionist measures that prove as disincentives to trade and investment could prompt new flows of equity and debt finance needed to spur development.


LDCs feel that they have little to gain from liberalised trade in services for the comparative advantage in services lies with the developed world, but this is a wrong notion for the gains from International trade in services would depend on improved efficiency from specialisation and increased trade flows.i.e.

LDCs argue that the protection of emerging "infrastructure" services is necessary for the development of an internationally competitive economy, i.e. the long term benefits of a strong, indigenous service sector outweigh the short term costs of protection.

Although complete and sweeping liberalisation should not be adopted by LDCs, a sectoral approach

for instance in labour intensive services could be to their advantage.

LDCs stand to gain from services liberalisation in important ways: (1) it would facilitate technology transfer from the developed to the developing countries; (2) inflow of development finance crucial for growth.

 Indian Motives & Stakes in Services Negotiations:

India has taken, alongwith nine other countries (G-10)<sup>22</sup> a joint leadership role with Brazil on the question of trade in services. And this position is in direct contrast to the position of the developed world, led by the United States, as well as in contrast to the developing world excluding the G-10.

At the Ministerial Meeting in Punta del Este (Uruguay) in 1986, India with Brazil assumed the leadership of developing countries and opposed the introduction of services within the framework of GATT. The opposition was based on several apprehensions which are as follows:

- i) The introduction of services within GATT will deflect GATT's attention from other more pressing issues like agricultural subsidies etc.

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22. G-10 consists of India, Brazil, Argentina, Cuba, Egypt, Nicaragua, Nigeria, Peru, Tanzania and Yugoslavia. *Ind.* *AP* *LA* *\**



- ii) GATT itself had not been effective in "protecting" and/or advancing developing countries interests in the area of trade in goods; hence it would be irrational to expect it to help LDCs in the area of services.
- iii) Services trade is seen as a form of neo imperialism since service industries are dominated by multinationals and opening of trade barriers would mean an invitation to be gobbled up.
- iv) The services area was seen to be such a new sector that even the economists (including GATT's own) had difficulty in defining it; hence it would be of no consequence to speculate on what would happen if services trade were to be liberalised.
- v) Another factor is that the developing countries realised that liberalisation of trade in services may not result in comparative advantage and protection of infant service industries in LDCs. Besides it may infringe on national sovereignty and economic ambitions.

In order to understand the real reasons for India's leadership role<sup>23</sup> in opposing the introduction of services

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23. Surjit S. Bhalla: Trade in Services (I): Assessment of Indias Position. Times of India, 22 March, 1990.

into GATT one must analyse the above factors. India's position needs to be examined to see whether it is representative of genuine economic concerns or meant for political consumption.

1. The first factor cited by India is "No services in GATT because agenda for GATT is already full"<sup>24</sup> - This argument is based on the fact that there are diseconomies of scale to a beaurocracy but India already has one of the largest burocracy in the world. A comparative study by Hellien and Tait of the IMF reported that among the 60 odd countries considered India had the largest share of government employees in formal non-agricultural employment - 54 percent. Indian stand has been that services cannot be handled by GATT but since the distinction between goods and services is getting blurred, it would not have been rational to have two different organisations arguing about what would come under each others.

The Indian stand has been motivated by the belief that if you do not want something to happen set up a committee to study the problem plus setting up a new organisation is a stupendous task.

2. GATT had not been effective in protecting developing country interests - Indian position has been "the foreign

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24. Editorial, Mainstream, n.5,

hand position" i.e. the outside world is largely responsible for domestic problems. The following explanation is given for India's bad export performance until the mid-eighties - the increasing incidence of protectionism in the industrialised countries, embodied in the escalated tariff structures and a range of unquantifiable non-tariff barriers.<sup>25</sup> Amiya Bagchi in her article on economic policy for the new government opines "Rising Protectionism in the OECD block has made the situation even more adverse to a pure strategy of export-led growth".<sup>26</sup>

Nayyars and Bagchis argument is not fully acceptable for Indian exports have consistently declined in market share since the 1980s. Domestic policy certainly has to be blamed for this export debacle rather than the entire blame being put on GATT or the policies of the developed world. Seeing the progress made by countries like Korea, Taiwan and other countries like China during the same period the GATT cannot be held guilty of not protecting developing country interests.

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Though barriers like Textile quotas are against

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25. Deepak Nayyar "India's export performance, 1970-85, Underlying Factors and Constraints, Economic and Political Weekly, May 1987.
26. Amiya Bagchi - Economic and Political Weekly, Feb. 10, 1990.
27. Bhalla, n.23.

the interests of textile producing countries like India; India cannot complain for its interests have not been hampered since "the only year in which textile quotas were fully utilised was 1987, while for the remaining years, quotas were grossly underutilised, especially the European quotas. Even in 1987, quotas for Indian commodities like bed-linen and made ups were under-utilised. Hence it is not absolutely right on the part of Indians to blame the GATT for not protecting and furthering developing countries interests.

3. Services trade as neo imperialism - the Developing countries led by India believe that opening up the world market for goods or services would lead to domination by multinational, self reliance being the only course left.

4. Trade will not protect infant industries - Indian policy makers and industrialists have been crying themselves hoarse for 40 years about their need for protection now and competition later. And though so many years have gone by Indian industrialists are still not competitive internationally. During the years of infant industry protection from independence in 1948 to the present, Indian share in world trade has declined from approximately 2.5 percent in the early fifties to barely 0.5 percent at present. Indians therefore have no ground to argue for protection for infant industries. The industrialists are not keen on giving up protection

for it benefits them and infact suggest that the deficit problems can be solved by raising import tariffs, already estimated at 125 to 175 percent, the highest in the world.

Indian position is therefore affected not so much by the factors mentioned above; which simply amount to political rhetoric but is an outcome of domestic economic policies.

The most convincing political explanation for India's membership and leadership of this club<sup>29</sup> is that India has always prided itself on being a leader of the Third World. It is a hangover from the heady days of non-alignment and Nehru, Nasser and Tito - and that is the reason why Egypt and Yugoslavia are also members of the G-10. The economic performance of India over the last 40 years has been disappointing and the leadership of the Third World is considered a worthy substitute for the lack of domestic growth and glory.

LDCs have deep rooted concerns about the implications of services trade liberalisation for their economic development. National interests can be safeguarded if service industries are regulated

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29. For Indian and Brazilian statements at the Group of Negotiations on services on February 25, 1987, see C. Raghavan, Trade Services Negotiations start, Special United Nations Service No. 1664, 3 March 1987.

and government autonomy maintained. In many cases regulations masks protectionism creating distortions and impediments to growth. In particular, this works against technology transfer and inflows of foreign direct investment needed to spur economic development.

LDCs recognise the importance of technology<sup>30</sup> to development, but are constrained in their ability to obtain or develop it. Most of the channels of technology transfer (eg. foreign direct investment; technology - embodied imports) have been blocked by trade and investment controls imposed by LDCs to protect infant industries and national sovereignty. New technologies cannot be acquired directly because of financial constraints. The speed of technological change has led many companies to hold their patents closely to maximise sales in order to recoup quickly R and D expenditure. Competition between the various technologically developed countries lowers the price of outdated technology thus enabling the LDCs to buy, thus putting them at a competitive disadvantage in both export and home markets. LDCs could benefit from freer trade and investment for it would give them greater access to advanced technologies. The question remains

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30. Jeffrey J. Schott and Jacqueline Mazza, Trade in Services and Developing Countries, Journal of World Trade Law. 20(3); May/June 86; 253-73.

whether the advantage outweighs the perceived concerns regarding development and sovereignty.<sup>31</sup> Liberalisation would facilitate the import of technology - embodied goods and services. Other than this liberalisation could lead to additional sources of development finance. Protectionism creates a disincentive to inflows of foreign official and private capital whereas an improved investment climate could prompt new flows of equity and debt finance needed to spur development.

Free trade in services would benefit developing countries for three important reasons:<sup>32</sup>

1. Third World Countries would benefit from the opportunity to obtain benefit of high quality modern services at the cheapest world market price increasing the productivity of other sectors. Professor Ronald K. Shelp gives the example of agricultural insurance and its subsequent effect on introduction of new methods and technology.
2. Developing countries can combine innovations in communications with cheap domestic labour to export some services such as finance, engineering and computer programming at costs low enough to compete globally.

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31. C. Michael Aho and Jonathan David Aronson: Trade Talks America Better Listen, Council on Foreign Relations (USA), 1985.

32. *ibid.*

3. Developing countries can benefit from the changing comparative advantages in the conventional sectors of agriculture, manufacturing and services like the developed countries have.

Negotiating Strategy:

The developing countries have developed a negotiating strategy that serves their interest. This strategy is based on three perceptions:

- i) united they benefit and as a bloc have better bargaining leverage.

Individual bargaining positions and capacity to retaliate on the part of the developing countries are necessarily weak. But collectively they become a force to be reckoned with, particularly since an enlarged market is vitally important for the dynamic expansion of all the new areas. The developed countries would not want to ignore the growing market in the developing world and would therefore be prepared to make "reasonable" concessions.

- ii) developing states must clearly examine and conduct a study on which sectors can be opened up and would serve their long-term



economic interests. If the US agenda for liberalisation of service trade presents opportunities to developing countries, these must be thoroughly tested and explored.

The developing countries have realised that an expanded GATT is not to their advantage. It will increase the Souths dependence on the North, take away the Souths autonomy as far as the choice of economic policies are concerned and will be a threat to national sovereignty.

The GATT scenario is to benefit the US and its economic allies and further worsen the global trade share of the South.

Another matter considered by the South is the asymmetry prevailing in the agenda for liberalisation. The current proposals are by and large limited to capital-related services (banking, telematics etc.) where the North has a comparative advantage. Labour related services where developing countries can hope to have advantage are not part of the agenda. Hence the developing nations should endeavour to get concessions in sectors that benefit their economy by insisting on sector specific arrangements.

On the insistence of India and other developing countries, labour intensive industries are now treated on par with technology intensive ones.

Developing countries can insist on temporary migration of labour from developing countries to developed countries for the purpose of providing services to the users abroad. India, South Korea, Phillipines and Pakistan were allowed to do so in West Asia, they could benefit, if allowed in the industrial countries as well.

- iii) If liberalisation of service trade threatens LDC interests, counter proposals must be developed to compensate for negative effects of free trade in services.

It is imperative to impress upon the developed countries to recognise the special social and developmental needs of the LDCs. Science based technology has become a crucial factor for development and control of international markets and stringent measures to block its diffusion would condemn the LDCs permanently to the status of "cultural slaves", which would be untimately detrimental to everybody's interests.

The developing countries have to formulate a careful strategy<sup>33</sup> to counter the proposals of the

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33. Bhalla, n.23

developed world for the latter aims at and would benefit by maintaining and perpetuating the dominance-dependence relationship between North and the South.

The developing countries have not been softened by the tough stand of the U.S.A. They argue that the concept of economic development should be integral to any services agreement and insist on number of issues that any agreement must tackle. These include provisions to facilitate transfer of technology, encourage service exports of developing countries and control restrictive business practices.

CHAPTER IV

BEYOND THE URUGUAY ROUND

"PROSPECTS FOR FUTURE AREAS OF COOPERATION"

The World Trading System is under severe strain. Most countries are not content with the way it works and feel the urgent need for reform and restructuring.<sup>1</sup>

Trade Rules are vague and weakly enforced. Trade Protection has increased, prompting imitation or retaliation. Massive trade and current account imbalances threaten a further increase in protection. The LDC debt problem has assumed alarming proportion and if this continues it will erode the trading system and undermine economic growth in developed and developing countries alike.

While trade negotiations are not a panacea for the ills of the economy, trade reforms can alongwith appropriate monetary and fiscal policies contribute to economic growth and employment. Trade negotiations can stop the growing tide of protectionism and restore momentum for liberalisation.

Trade talks can succeed, if countries cooperate. No country will sacrifice its own growth prospects for the insubstantial benefit of stronger trade rules.

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1. GATT Wisemen's Report, Trade Policies for a Better Future: Proposals for Action, GATT, March 1985. The GATT Wisemen's group made several recommendations designed to strengthen discipline and to reduce frictions in trade policy. The recommendations by this group of eminent, practical people from outside trade policy circles imply a great deal for institutional reform of the trading system. The report contains a detailed framework for evaluating the costs and benefits of trade restrictions in an Appendix.

At the same time, national and international growth prospects will suffer unless the trading rules are overhauled and made relevant to fast changing world economy. Hence trade talks are essential for the achievement of higher growth and greater discipline in international trade, that would benefit all trading partners.

The Uruguay Round of multilateral trade negotiations is dealing with the issue of services and a compromise formulae is being worked on.

For an agreement to take place, each must gain, and all must sacrifice the interests of protected, inefficient domestic producers and/or agree to limits on national sovereignty. In case a trade pact is worked out with these issues in mind, the United States and Canada would get improved access to Japan and the Asian NICs and the promise of better access in other developing countries when conditions permit. The development of codes, framework and general principles for services has been reached though immediate liberalisation in these realms is elusive. Various countries will have to make important sacrifices so that the objective of development of all trading partners can be realised.

United States in order to move closer to an agreement should reaffirm its commitment to special

and differential treatment for the least developed countries and to the concept of unconditional most favoured nation treatment. The United States would also need to promise that in the future it will apply and adhere to GATT rules and principles when they went against the US interests as well as when they supported them. In addition the United States will have to accept the high cost of continued internal adjustment and permit greater access to LDC products in the US market.

European gains in any package will come at the margins. It can benefit to some extent from progress on trade in services, though it would be difficult for the Europeans to agree to liberalisation in insurance and telecommunications. The EEC<sup>2</sup> opposition to a stronger legalistic GATT system is well known though some countries in the EC, would approve of an extension of GATT.

Since it is better to negotiate from a position of strength, negotiations on high technology sectors or services depends on how successful these industries are at the time of negotiations and thus different countries are motivated to call for liberalisation or protection depending on their industrial position at the time of negotiations.

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2. Philip Hayes: Trade and Adjustment Policies in the European Community (London - Trade Policy Research Centre, July 1984).

Japan has been sitting on the sidelines supporting the negotiations buying time seeking a stronger trading system and continued access for its products in return for further steps to internationalise its markets. The Japanese will have to accommodate other countries interest in order to prevent them from ganging up against them.

The NICs and other developing countries have a greater interest in stronger system. If discipline is strengthened and market access in industrial countries is increased the NICs benefit. To obtain this the NICs will have to join the bargaining process whole heartedly accepting more GATT discipline and will have to give up some market access both to industrial countries in capital intensive goods, as well as to other developing countries in traditional products. For an agreement to work out the NICs have to agree on general framework for trade in services.

Talking about rights and obligations and about making and receiving concessions is not enough. On new issues like services negotiations have been complex and difficult. A general framework was agreed upon in the mid-term review in Montreal Negotiations in order to be successful should proceed through three stages:-

In the first stage, negotiators could agree to a general commitment not to increase barriers to



trade while negotiations define the scope and objectives to be addressed.

In the second stage, work would focus on horizontal issues. It should be aimed at developing codes, rules, procedures and principles parallel to those in the GATT Articles for goods. This could include dispute settlement, surveillance and complaint procedures.

In the third and final stage, after agreement on definitions and objectives and the negotiations of general principles, rules and procedures, negotiators can try to reduce trade barriers.

The bulk of the trade in services is between industrial countries. Therefore, industrial countries are keen to deal with services issues even if the LDCs refuse to participate.

Services is a complex issue and much progress has not been achieved in the Uruguay Round; if multilateral talks fail<sup>3</sup> bilateral and regional negotiations can be used as substitutes; the greatest gains from negotiations could be gained by conducting cross sector bargains involving as many countries as possible.

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3. The more heterogeneous the participants, the less lively are successful negotiations to result.

Cross Sector bargains can be described as second best solutions because relative to a global bargain, with wide participation, they are not optimal. But all issues are not conducive to wider participation.<sup>4</sup> Some, like trade distorting investment practices, may be handled better among smaller groups of countries. On certain other issues, some countries or group of countries may be reluctant to contribute their shares or to follow disciplines. These countries should not be allowed the benefits of these negotiations and the guiding principle should be reciprocity.

When prospects for broad negotiations seemed remote, the United States and some other industrial countries became interested in trade liberalising agreements among smaller groups of countries. Various plans for a "GATT-Plus",<sup>5</sup> a Super-GATT, or a "GATT of the likeminded" differ in detail but have three common features.

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4. H. Peter Gray: Negotiating Strategy for Trade in Services. Journal of World Trade Law. Vol.17(1983).
  5. There might be a "GATT-Plus" embracing nations prepared to trade on a freer basis than that agreed in the GATT. Second, a 'Super-GATT' to unite a group of nations which would exercise trade leadership towards a more liberal system. Third, a '&'GATT of like minded' where some countries would lower barriers and invite other nations to join them. "United Kingdom Doubtful over plans to reform GATT", Financial Times, March 18-19, 1985, p.6.

First they are viewed as second-best alternatives<sup>6</sup> to multilateral negotiations within GATT that produce the same agreement or terms.

Second, they are built on the premise that if some countries mostly in the industrial world want to go further to liberalise trade among themselves than others, they should do so.

Third, the benefits from such liberalisation would only be extended to countries which participated in negotiations and accepted the discipline that emerged. Initial holdouts might join agreements after they were negotiated by contributing their fair share.

Countries desiring progress will seek it in smaller negotiations or in bilateral agreements, the principle being that limited negotiations<sup>7</sup> can either substitute for or complement multilateral talks. Such negotiations would be less subject to ideological disputes because only countries that believe they would benefit would participate. The only danger is

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6. C. Michael Aho and Jonathan David Aronson : Trade Talks, America Better Listen, Council on Foreign Relations (USA) : 1985.

7. Northern nations have a better record of successful bargaining and therefore may be more likely to achieve some possible agreement. Moreover, the similarity of concerns of the participating nations is likely to be a positive factor.

that unless key countries eventually joined, negotiations in smaller groups could fragment the trading system into regional groupings and undermine whatever existing authority GATT retained countries might leave GATT in large numbers.

Another possibility is that trade negotiations move forward in the GATT and in the other fora simultaneously<sup>8</sup> and could complement GATT negotiations. On certain issues countries could proceed outside the GATT because GATT negotiations could not deal with them or they get bogged down. For instance, on the issue of services if, the LDCs refuse to consider in the GATT, the industrial countries could work on these among themselves, in the OECD or some other forum. Similarly, countries might choose to negotiate on issues of specific interest if the progress in GATT does not satisfy them. Countries wishing to go further or faster than in GATT, might conduct parallel talks. Discussions of a free trade agreement between the United States and Canada fall into this category.

Regional negotiations<sup>9</sup> offer another possibility. EC is trying to create a unified market among its members

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8. William Clive (Ed.): Trade Policy in the 1980s, Washington DC, 1983.

9. East African, Arab and Latin American efforts to promote regional free trade groupings in the 1960s did not fare as well as Europe's attempts. The most promising grouping today is among the Asian NICs.

and has long extended special benefits to other European countries and to many African and Asian Development countries. In case of failure of GATT negotiations such efforts could get more attention. Similarly Japan, Australia, and the NIC's are seeking ways to improve Pacific trade cooperation. The United States is also seeking to improve hemispheric trade relations. Improved trade relations with Canada or Mexico are on the agenda, whether or not GATT negotiations proceed. Even the LDCs are trying once again to improve trade relations among themselves.

Regional arrangements<sup>10</sup> would have important foreign policy implications and is an inferior alternative to multilateral liberalisation on a non-discriminatory basis. Trade policy could be raised from "low level" to "high level" foreign policy. Major pillars of the trading system cannot afford to be in rival blocs, for instance Western Cooperation remains important for strategic and security reasons and must not be undermined. The best message of security cohesion could be a flourishing unified non-discriminatory system.

Another alternative is Bilateral Free Trade agreements and these can be compatible with the GATT. EC members

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10. Cline, n. 8.

extend to each other more liberal trade opportunities than they do to the United States. Other free trade agreements may or may not be compatible with the GATT, Former Colonies and other European Countries also enjoy more liberal access to European markets than is extended to United States or Japan. The 1984, Trade & Tariff Act gives the president the authority to negotiate bilateral free trade arrangements with other countries.

In 1985 Congress approved a free trade agreement<sup>11</sup> on services between Isreal and the United States thus demonstrating that trade liberalisation in the area could be negotiated. It was also meant as a warning that unless progress was made towards new trade talks, the United States will go elsewhere for agreements. The United States could not support the multilateral trading system alone and others would have to contribute their fair share.

Bilateral agreements would lead to regionalisation of world trade and create rigid regional trading blocs. It is difficult to integrate the developing countries with their differential and special treatment into the world trading system , therefore, bilateralism would

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11. US Officials regard the "Declaration on Trade in Services" annexed to the US-Isreal Free Trade Agreement as a model for what could be negotiated multilaterally.

lead to the emergence of four or five rival trading blocs. The experience of the 1930's shows that bilateral agreements cannot provide a stable consistent and expanding trading system and would lead to unhealthy competition and hostility. If large number of countries try to offer mutually incompatible privileges in order to gain liberalisation, predictability and stability will be destroyed for everyone. Discriminatory bilateral arrangements cannot combine to form a globally consistent stable system of national trade policies. Such a system requires effective equality of rights and obligations among countries, which can only be ensured by general acceptance of the principle of unconditional most favoured nation treatment, for this principle mobilises large nations to support the aspirations of small ones to be treated equally. In no other way can the sovereign equality of nations be realised or even approximated.

When considering regional arrangements,<sup>12</sup> a few questions should be kept in mind. Could South Korea, Hong-Kong, Taiwan and Singapore show the same dynamism in economic terms in a fragmented trading system. Could the heavily indebted countries generate sufficient export earnings to service their debts in a fragmented

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12. Gary Clyde Hufbauer, Jeffrey J. Schott: Trading for Growth: The Next Round of Trade Negotiations.

trading system. The answers to these would in the negative.

Limited agreements<sup>13</sup> should be building blocs which allow for further liberalisation either by broadening the country coverage of functional agreements or merging regional arrangements otherwise, the limited deals would further heighten trade tensions and undermine the system and the goal of integrating the LDCs more fully into the trading system cannot be achieved. But before considering any other arrangements nations should consider a global, multilateral bargain which definitely offers a lot of advantages.

A study of the issue of Trade in Services gives a fairly good idea of the problem and its various dimensions. To deal with this problem negotiators should try various permutations and combinations.

The best solution for a prospective agreement would be if a significant number of countries make a joint declaration that the principles of GATT were to apply to services as well as goods. If not all at least some of the GATT codes, notably those regarding subsidies and public procurement could be applied. This would

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13. Gray, n.5



cover atleast some of the practices being complained of and would establish a complaint and disputes settlement procedure for certain activities.

Another alternative could be adoption of an Umbrella<sup>14</sup> Code:

New codes could be established like (1) a code for services; (2) Codes for individual services or groups of services; (3) a code for codes.

The Tokyo Round Codes represent understandings between signatories on how they will interpret and implement existing GATT articles. Since there is no general body of rules on services in the GATT and the possibility of an agreement by all members on amendment is unlikely services code can be outside the GATT framework. It could be linked, however, to basic GATT notification, consultation, and enforcement provisions, and it should be open to all members on a conditional MFN basis.

A services code should focus on three broad principles that would serve as guide posts for national policies.

First is transparency: services trade barriers need to be notified and exposed to consultation and dispute settlement procedures.

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14. Clive, n.8

Second is non-discrimination as between domestic and foreign firms, or the extension of national treatment principle to the services sector.

Third is the right to transact business : foreign firms should be free to establish ventures on the same footing as local firms.

Governments should commit themselves to these three principles with exceptions for narrowly defined national security health and safety concerns.

The scope of these principles has to be well defined for it would raise problems in certain areas. In the civil aviation and maritime sectors, the right of establishment would translate into an "open skies" regime and permission for all vessels to ply, the coastal trades. In some cases rendering the service is closely linked to immigration for instance contract construction and coastal maritime services, in other instances right of establishment would intrude on Government monopolies (Civil aviation and health care). To deal with these problems, Government could negotiate in the first instance which sectors would be subject to code obligations, with a commitment to expand coverage after a review period.

Many services trade problems can be addressed

directly in a GATT context.<sup>15</sup> There is ample scope to extend the Tokyo Round codes to deal with practices that distort services trade in particular, subsidies, licensing controls, technical standards and restrictive Government procurement policies.

Another option could be a pledge to impose no new barriers to international transactions in services for a given period of time or while negotiations were proceeding i.e. a standstill agreement.<sup>16</sup>

A complaints centre established in the GATT where impediments to transactions in services could be registered would help in rectifying these to the benefit of all.

Most countries have come to realise the growing importance of services, in their domestic economies and are, in favour of establishing a framework of rules that would further their interests and lead to development and progress for all. The developing countries though hesitant and sceptical to liberalise all areas are in favour of a sector by sector approach. The developed nations want to safeguard their weaker sectors also,

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15. Jagdish N. Bhagwati, "GATT and Trade in Services: How we can resolve the North South Debate", Financial Times, 27 November 1985, p. 25.

16. Hufbauer, n. 12.

but since they enjoy a comparative advantage in services exports; are pushing for liberalisation more seriously.

This study has examined the reasons why negotiations are needed and has proposed strategies for them to succeed. It has explored the objectives of the major trading countries, the issues that need to be addressed and possible approaches for pursuing negotiations.

These negotiations would indirectly benefit the LDCs. Their concerns and apprehension regarding liberalisation is justified but many of the developing countries have come to realise that these negotiations can benefit them without hindering their development and growth plans.

The inclusion of services will bolster the effectiveness of GATT and the LDCs being the weakest partners in the multilateral system will benefit from the strengthening of the multilateral discipline.

In addition services liberalisation would complement several reforms of primary interest to the LDCs, because of the growing interlinkages between manufacturing and services a standstill on new services trade barriers would reinforce the proposed standstill and eventual roll back of merchandise trade barriers.

LDC objectives can be realised through meaningful participation in the Uruguay Round and in negotiations on services LDCs desire.

1. revival of third world growth.
2. resolution of the debt crisis.
3. removal of barriers to the merchandise exports.

Service trade liberalisation is critical to the development objectives of a few LDCs, holds the prospects of new trade opportunities for some others and threatens the protective barriers of selective service industries in a few others.

Blanket liberalisation<sup>17</sup> of the economy is not a miracle solution to the problems faced by developing economies a crucial step before liberalisation in India would be privatisation and relinquishing of state control from most of the sectors so that domestic industry can develop into a competitive industry and meet international standards. There is a significant difference between US approach prior to the start of the round when it was threatening to leave GATT and its approach now, after five years of negotiations. Services have receded to the background and US and its OECD partners have clashed over the question of agricultural subsidies that has presently become the focus of attention.

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17. -- Liberalisation of all sectors of the economy.

Liberalisation can be used by the developing countries to achieve important developmental objectives but the LDCs must follow a sectoral approach and first liberalise only those areas where it has a comparative advantage. Developing nations can use these negotiations to their advantage.

APPENDIX I

## MINISTERIAL DECLARATION ON THE URUGUAY ROUND

Ministers, meeting on the occasion of the Special Session of CONTRACTING PARTIES at Punta del Este, have decided to launch Multilateral Trade Negotiations (The Uruguay Round). To this end, they have adopted the following Declaration. The Multilateral Trade Negotiations (MTN) will be open to the participation of countries as indicated in Parts I and II of this Declaration. A Trade Negotiations Committee (TNC) is established to carry out the Negotiations. The Trade Negotiations Committee shall hold its first meeting not later than 31 October 1986. It shall meet as appropriate at Ministerial level. The Multilateral Trade Negotiations will be concluded within four years.

**Part II: Negotiations on Trade in Services:**

Ministers also decided, as part of the Multilateral Trade Negotiations, to launch negotiations on trade in Services.

Negotiations in this area shall aim to establish a multilateral framework of principles and rules for trade in services, including elaboration of possible disciplines for individual sectors, with a view to expansion to such trade under conditions of transparency and progressive liberalisation and as a means of promoting economic growth of all trading partners and the development of

developing countries. Such framework shall respect the policy objectives of national laws and regulations applying to services and shall take into account the work or relevant international organisations.

GATT procedures and practices shall apply to these negotiations. A Group of Negotiations on Services is established to deal with these matters. Participation in the negotiations under this Part of the Declaration will be open to the same countries as under Part I. GATT Secretariat support will be provided, with technical support from other organisations as decided by the Group on Negotiations on Services.

The Group of Negotiations on Services shall report to the Trade Negotiations Committee.



APPENDIX IIUS GOALS FOR NEW MULTILATERAL TRADE NEGOTIATIONS,  
UNITED STATES TRADE REPRESENTATIVE, JULY 9, 1985

The United States believes that there is an urgent need for action to improve and strengthen the international trading system, which is under severe strain pressures on governments to restrict imports are increasing partly as a result of serious adjustment problems in key industries but also in large part due to the absence of any effective dispute settlement mechanism and the lack of meaningful international discipline over import restraints and export subsidies. These pressures give rise to trade distortive actions that prejudice the interests of trading partners and cause them, in turn, to take similar restrictive measures. This current trend needs to be reversed to secure the expansion of world trade, support global economic growth and continue the improvement of worldwide living standards. Maintenance of open markets also would assist developing countries in meeting their debt obligations and supporting their development efforts.

The GATT work program initiated in 1982 covers most of the pressing issues. This work programme is reaching a stage where further progress will depend on the initiation of negotiations. These negotiations, to be conducted under the auspices of the GATT, would be open to any contractual party wishing to participate. In the US view, the negotiations should aim to:

- strengthen and develop trading rules to better attune them to current and future trading environment;
- expand the exchange of goods through the reduction of trade barriers to raise standards living; and
- develop a set of rules applicable to trade in services.

This paper lays out the initial view of the United States on the first set of issues to be dealt with in the negotiations. It is based on preliminary consultations with our private sector. We expect to consult further with them, and with Congress, in the months ahead.

Additional or modified proposals for negotiations may emerge out of this process.

US Objectives for Negotiations Dealing with  
Trade in Services:

Trade in services accounts for a growing share of global trade. This trade has taken on increased significance for all countries as a result of its critical role in fastening the application of new technology which is central to economic growth. However, there are few international rules for services trade and no established procedure for negotiations that could lead to the liberalisation of barriers limiting this trade. The United States seeks the development of a general agreement of principles and procedures to ensure that trade in services is as open as possible. Negotiations should be carried out by as many interested contracting parties as possible under the aegis of the GATT, using its administrative facilities and Secretariat staff.

Negotiations on Services under the auspices of the GATT should aim at an agreement on a set of rules and principles for conducting trade in services. The agreement would be based on a commitment to transparency of practices and the resolution of problems through consultation. Procedures also would be established for the negotiations of commitments dealing with the

reduction of trade barriers, including provisions laying out the nature of these commitments.

The General Agreement on services should be complemented by negotiations aimed at the removal of barriers in individual service industries. We also foresee negotiations in functional areas, such as standards as well as the development of an undertaking dealing with investment issues in services. The United States also believes that priority should be given to developing a multi-lateral agreement on international information flows.

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