# The Challenge of the GATS for Transition Economies Seeking to Join the WTO*

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ABSTRACT. Transition economies seeking to join the World Trade Organization (*WTO*) face a variety of distinctive challenges relating to their prospective obligations under the General Agreement on Trade in Services (*GATS*). Transition economies are characterized by changing market and industry structures on the one hand, and ongoing reforms to their regulatory structures on the other. Both make it extremely difficult for transition economies to develop a position on what WTO services commitments they should undertake in their national schedules of specific commitments. Accession negotiations are further complicated by the evolving nature of GATS rules themselves and the tough negotiating stance taken by existing Members. Based on evidence from recent accessions, the effective minimum requirements relating to services for transition economies seeking to join the WTO are increasing.

KEY WORDS. WTO; transition economies; GATS; modes of supply; Most Favoured Nation; sector specific obligations; market access; national treatment; transparency; post-Uruguay Round negotiations; evolving nature of GATS rules; dispute settlement; regional integration

All countries seeking to accede to the WTO face substantial challenges. In the main areas where country specific commitments are negotiated, tariffs and services, terms must be settled which strike a delicate balance between liberalizing market access and protecting domestic industry. As well, domestic legal regimes must be reformed, sometimes substantially, to comply with the disciplines of

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the WTO. For transition economies these challenges are especially great in the area of services for two reasons. First, the General Agreement on Trade in Services (GATS),[1] which imposes general trade disciplines applying to services, is continually evolving.[2] Second, dramatic changes continue to take place in countries in transition as they transform into market-based economies, making it difficult to undertake the commitments that GATS requires.

Indeed, GATS obligations have been far from static since coming into force in 1995. There were negotiations continuing beyond the end of the Uruguay Round resulting in higher levels of commitments in financial services,[3] telecommunications[4] and the movement of natural persons.[5] GATS also mandated negotiations to develop disciplines in relation to subsidies, safeguards, government procurement and domestic regulation in the area of services trade. These negotiations are ongoing. Along with agriculture, services is one of the two areas where future negotiations were part of the built-in agenda of the Uruguay Round. A new round of services negotiations commenced in February 2000.

But these are only the most obvious ways in which the services commitments of the Members of the WTO are evolving. The impact of the GATS obligations is beginning to be fleshed out in the still small number of WTO dispute settlement cases dealing with trade in services. Even in the relative absence of authoritative interpretation, WTO Members are developing a more sophisticated understanding of GATS commitments through the research and analysis carried out by the governments of Members, academics and, significantly, the staff of the WTO Secretariat.[6] Given the novelty of the

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[1] Annex 1B to the Marrakesh Agreement establishing the World Trade Organization, (1994) 33 I.L.M. 81 [*GATS*].

[2] GATT rules, particularly those relating to national treatment, covered services to the extent that services were incidental to trade in goods. For example, GATT Art. III:4 refers to transportation and distribution services. A GATT dispute settlement case involving Canadian liquor distribution revolved around the use of government-owned monopoly retailers providing less than national treatment (and even imposing quantitative restrictions in the sense of GATT Art. XI) (*Canada-Imports, Distribution and Sale of Certain Alcoholic Drinks by Provincial Marketing Agencies*, BISD, 39th Supp. 27 (1992) (*US* v. *Canada*). Moreover, GATT Article IV permitting governments to retain screen quotas which would otherwise be contrary to their Art. III obligations is arguably a measure that allows denial of national treatment for a cultural service as much as for a good (exposed film). See the discussion below of the dispute settlement cases involving GATS.

[3] New commitments were annexed to the Fifth Protocol to the General Agreement on Trade in Services. The protocol entered into force in March 1999. A previous set of enhanced commitments had been annexed to the Second Protocol to the General Agreement on Trade in Services, adopted July 2, 1995 and in force on September 1, 1996.

[4] New commitments were made in the Fourth Protocol to the General Agreement on Trade in Services adopted April 30, 1996, in force January 1, 1998.

[5] Members recorded their additional commitments in this area in annexes to the Third Protocol to the General Agreement on Trade in Services adopted 24 July 1995.

[6] This is discussed below. For a general discussion see GATS 2000: NEW DIRECTIONS IN SERVICES TRADE LIBERALIZATION, P. Sauvй & R. Stern, eds. (Washington: Brookings Institution Press, 2000) [*GATS 2000*].

obligations in the GATS, the customized nature of national schedules of commitments and the rush to conclude negotiations in the final months leading up to the end of the Uruguay Round, undoubtedly, Members did not fully appreciate the scope of their own commitments, much less those of all other Members. Now that more than seven years have passed since the agreement came into force, Members have begun to develop a better understanding of the nature of problems associated with the poor and inconsistent scheduling practices followed by different Members, as well as a range of difficult interpretive issues related to the complex provisions of the GATS. Armed with this new understanding Members have required countries seeking to accede to make services commitments that are more precise and much less qualified than they themselves have made.[7] The Kyrgyz Republic, Latvia, Georgia and Armenia, for example, have all made less qualified commitments in relation to more services sectors than major trading countries like Canada and the European Union. The evolving nature of the GATS creates challenges for countries in the process of acceding to the WTO as they seek to adjust to changing expectations and demands from the existing Members.

There are a variety of other challenges faced by transition economies in the accession queue. Legislation in the services area is often new, incomplete and uncertain, typically reflecting both the relatively short time that these countries have been seeking to implement market based reform and continuing evolution in national policies and laws in step with the process of economic transition. Various factors impede the development of strong legal rules, including a small cadre of government officials with relevant experience, weak rule of law traditions, the absence of a structured policy development process providing for effective stakeholder input, budgetary constraints on the types of realistically available policy instruments and the need to ensure the delivery of basic services to large numbers of poor citizens. Change and uncertainty in services laws and policies makes it hard for transition economies to develop their services offers as well as to make and implement services commitments.

The extensive reach of the GATS to measures of regional and local levels of government poses an additional barrier to efforts to join the WTO. In many transition economies, the need to engage and ensure compliance by regional and local governments has made the development of market-based services rules and a coherent, and com-

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[7] G. Feketekuty. «Assessing and Improving the Architecture of the GATS» in GATS 2000 [*Feketekuty*], *ibid.*, at 99.

prehensive negotiating position on services commitments difficult. At the same time, one of the legacies of the Soviet Union is a complex and evolving web of international agreements among the countries in the Commonwealth of Independent States (CIS). These various special relationships must be accommodated in some manner for CIS Members to join the WTO.

This combination of the internally dynamic nature of the GATS and the continuing changes taking place in transition economies and the regulatory regimes related to services makes entering into GATS commitments an ever shifting and increasingly difficult undertaking. This article explores the challenges for transition economies in making credible services commitments sufficient to gain admission to the WTO.

## General Overview

The GATS is a complex agreement. It comprises both a general framework of obligations that apply to all services and a negotiated set of specific commitments regarding the treatment of identified services activities that each country lists in a national schedule. Although GATS incorporates key GATT principles, including most favoured nation (MFN), national treatment and transparency, the application of these principles to services trade is substantially attenuated.

The most important general rule is the obligation to grant MFN treatment to foreign services and services suppliers. This means that Members must treat services suppliers from other Member states no less favourably than those from any other country. Members can negotiate to list specified exceptions to their MFN obligation at the time they join the WTO.

For sectors listed in its national schedule, a Member becomes subject to a higher level of obligation. Members must grant foreign services suppliers national treatment (meaning treatment equivalent to the treatment of domestic businesses) and cannot impose certain restrictions on market access, such as limiting the total number of service providers in a sector and limiting the percentage of foreign ownership. For listed sectors, the Member's regulatory scheme must meet specified standards, including a requirement that measures affecting trade in services be administered in a reasonable, objective and impartial manner.

Listing a sector does not necessarily mean that foreign services suppliers from WTO Members have an unrestricted right to enter the national market. The national treatment and market access obligations for listed sectors can and in many cases are circumscribed by limitations inscribed in the schedule itself.

## Scope of Application: Modes of Supply

GATS applies to all internationally traded services, however delivered. Service is not defined.[8] Instead, GATS simply states that it applies to the four modes of supply set out below. With its application to the establishment of a commercial presence by foreign services suppliers within a Member state and the presence of natural persons in the state to supply services, the GATS moves well beyond the scope of the GATT which is limited essentially to cross-border supply of goods from a supplier in one state to a consumer in another.

- *Cross-border supply* (mode 1) — A service is supplied from the territory of one Member into the territory of any other Member (e.g. a doctor in Ukraine gives advice over the telephone to a patient in Georgia).
- *Consumption abroad* (mode 2) — A service is supplied in the territory of one Member to a service consumer of any other Member (e.g. a Russian goes to Armenia to attend university).
- *Commercial presence* (mode 3) — A service is supplied by a service supplier of one Member, through a commercial presence in the territory of any other Member (e.g. a Russian computer training business sets up a campus and delivers courses in Azerbaijan).
- *Presence of natural persons* (mode 4) — A service is supplied by a service supplier of one Member, through the presence of natural persons of a Member in the territory of any other Member (e.g. an individual Ukrainian computer programmer enters Georgia on a temporary basis to deliver seminars on his or her own behalf or to work at the Russian computer training business referred to above).

GATS obligations apply to the measures of central, regional and local governments and to those of non-governmental bodies in the exercise of powers delegated by central, regional or local governments.[9] For this purpose, non-governmental bodies include independent agencies and commissions exercising powers delegated from the state.

The provision of services «supplied in the exercise of governmental authority» is excluded from the disciplines of GATS provided two conditions are met: the service is non-commercial and is not provided in competition with other services providers.[10] While it may be rela-

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[8] Although early in the negotiations attempts were made to develop a definition, these were abandoned when it became apparent that no single useful definition was possible. See GATS 2000, above note 6.

[9] M. Trebilcock and R. Howse, THE REGULATION OF INTERNATIONAL TRADE 2d. ed. (London: Routledge, 1999), at 229-230. The text leaves unclear whether obligations apply to private enterprises exercising regulatory powers without any formal delegation from the state. In some countries, private monopolies (*e.g.*, basic telecommunications carriers in Canada) exercise *de facto* powers of regulation that, in other countries, would be under taken by the state or publicly owned utilities.

[10] GATS Art. I:3(c).

tively easy to determine whether the second condition is met, it is not at all clear what services are non-commercial. It may be that a service would be considered to be provided on a non-commercial basis if, over time, the costs of service delivery exceeded any revenue received. The scope of the exemption will be extremely important for transition economies where many services continue to be supplied by the state.

## Obligations Applying to All Sectors

### *Most Favoured Nation*

GATS Article II obliges Members to provide MFN treatment: a Member must not discriminate between services or services suppliers of other Members; it must accord to the services and service suppliers of each Member treatment no less favourable than the best treatment it accords to like services and service suppliers of any country.[11] GATS MFN obligation has been interpreted by the WTO Appellate Body as requiring that measures not discriminate in their express terms (*de jure* discrimination) or in the way they operate in practice (*de facto* discrimination), even if, on its face, measures are not discriminatory.[12]

Under GATS, Members can record one-time exemptions from the MFN obligation in their national schedules. Many exemptions filed list existing bilateral and regional preferential arrangements. Some Members have listed exemptions which appear to extend to future preferential arrangements, as well.[13] Exemptions are intended to be temporary and normally should not exceed ten years.[14] The Council for Trade in Services established under the GATS,[15] must review exemptions granted for a period of more than five years to determine if the conditions which created the need for the exemption still exist. Nevertheless, it seems unlikely that Members invoking Article II exemptions expect that such exemptions will disappear.[16] The scheduling country proposes exemptions and, unless these are objections from other Members, they are included

[11] This obligation replicates for services the GATT Article I obligation for goods.

[12] *European Union — Certain Measures Concerning the Importation of Bananas* AB-1997-3 (WT/DS27)[*EU — Bananas*].

[13] The MFN exemption list filed by Mauritius, for example, may be interpreted in this way. By permitting Members to list possible future discriminatory measures, the provisions of GATS Art. II are thus weaker than those of GATT Article I, which provided for the continuation, but no increase in existing preferences.

[14] GATS Annex on Article II Exemptions, paragraph 6.

[15] GATS Art. XXIV.

[16] In lists of MFN exemptions in national schedules there is a column headed «intended duration.» Many, if not most entries in this column read «indefinite». Art. II exemptions must be reviewed in 2004. It is unclear, however, whether this will lead to any diminution in the capacity of Members with Article II exemptions to enter bilateral preferential arrangements.

in its schedule. It does not appear that this negotiating process has led to the cancellation of any existing preferential arrangements.

The GATS MFN requirement is also qualified by the Agreement's Article V, which permits Member countries to enter regional agreements to liberalize trade in services under prescribed conditions. To qualify for the Article V exemption, regional agreements have to meet conditions analogous to those in GATT Article XXIV which provides a similar exemption in relation to trade in goods. Qualifying agreements must have «substantial» sectoral coverage, in terms of the number of services sectors, volume of trade and modes of supply covered[17] and provide for the elimination of substantially all discrimination in the trade of the parties, meaning measures providing for less than national treatment or less than MFN treatment. To be exempt an agreement must be designed to facilitate trade between the parties to the agreement and not raise the overall level of barriers to trade in services involving Members not party to the agreement.[18] Like those of GATT Article XXIV, the conditions of GATS Article V may be interpreted very differently by parties to a regional arrangement and the other WTO Members.

## *Transparency*

In language similar to that of Article X of GATT, Article III of GATS requires Members promptly to publish all relevant measures of general application that pertain to or would affect the operation of GATS. Bilateral or plurilateral agreements on services must also be published. Members are obliged, as well, to respond to requests for information regarding their measures and agreements. There are enhanced transparency obligations for sectors in relation to which a Member has undertaken specific commitments, as discussed below.

## *Judicial Review*

Article VI:2 of GATS requires Members to «maintain or institute judicial, arbitral or administrative tribunals or procedures» which provide for the prompt review of administrative decisions affecting trade in services by objective and impartial decision makers with the power to award appropriate remedies where justified. This require-

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[17] In order to meet this condition, agreements should not provide for the *a priori* exclusion of any mode of supply. The fact that the fourth mode of supply, «presence of natural persons,» is largely absent from even such deeply integrationist agreements as NAFTA suggest that the conditions will have to applied without undue rigor.

[18] GATS Art. V*bis* permits Members to enter into preferential agreements for the full integration of labour markets notwithstanding the MFN obligation.

ment is qualified by a provision that tribunals or procedures need not be introduced if doing so would be «inconsistent» with a Member's «constitutional structure or the nature of its legal system.»

## *Recognition*

Bilateral agreements between governments and other arrangements relating to the recognition of educational and other qualifications, such as, for example, the licensing or certification of service suppliers, should be open to other Members who wish to accede or to negotiate comparable agreements or arrangements. As well, GATS requires that recognition not be accorded in a discriminatory manner, or operate as a disguised restriction on trade. Recognition should be based on multilaterally agreed rules where possible.[19]

## *Monopolies and Exclusive Service Suppliers*

In accordance with GATS Article VIII, Members commit to ensuring that any monopoly service supplier, such as a provider of basic telecommunications services or postal services, observes the MFN requirement, as well as any specific commitment undertaken. This obligation extends to exclusive suppliers of services if a Member formally or effectively authorizes or establishes a small number of services suppliers and substantially prevents competition among suppliers.

## *Restrictive Business Practices*

Unlike GATT, GATS addresses restrictive business practices by services suppliers, though the concrete obligations are minimal. Article X imposes a loose requirement for each Member to consult on the request of another Member in relation to domestic restrictive practices by a service supplier of the Member with a view to eliminating such practices. A Member receiving a request must cooperate through providing non-confidential information. Confidential information must be provided where a satisfactory agreement safeguarding confidentiality is concluded.

## *Exceptions*

GATS Articles XIV and XIV(bis) allow Members to impose measures otherwise inconsistent with the GATS that are necessary to

[19] GATS Art. VII.

protect important national interests: national security, public morals, public order and health.[20] GATS goes on to provide that measures necessary to ensure compliance with laws protecting privacy of personal data and safety and to prevent deceptive and fraudulent practices or the effects of defaults in services contracts are also exempt, so long as the laws themselves are not inconsistent with the GATS. Certain tax measures are also exempt.

## Sector Specific Obligations

### *Structure of Market Access and National Treatment Commitments*

By listing a service sector or activity in its national schedule a Member commits itself to a higher range of obligation under GATS, including commitments on market access and national treatment.[21] Each Member may customize the precise level of market access and national treatment to which it is committed by recording limitations in its national schedule. Limitations are listed separately in relation to each of the four modes of services supply. Limitations may take the form of a total exclusion of any obligation for one or more modes of supply, in which case the notation would read «unbound». Alternatively, limitations may describe discrete conditions qualifying the extent of the Member's commitment regarding a particular mode of delivery in specific ways.[22] Limitations are recorded as «horizontal» where they apply to a particular mode of supply for *all* listed activities.[23] When a limitation applies only to a specific activity, the limitation is recorded only for that activity. In sum, the listing of a service activity in its schedule commits a Member to accord in relation to that services activity and to suppliers of that service both market access and national treatment, with respect to each of the four modes of service supply, but subject to any limitation recorded in the schedule itself.

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[20] These exemptions are analogous to those found in GATT Articles XXI and XX.

[21] GATS schedules are based on a sectoral classification developed by the WTO Secretariat which divides services into 12 sectors, which are broken down into 54 sub-sectors. Sub-sectors are further disaggregated into 161 activities. GATT Secretariat, *Services Sectoral Classification List: Note by the Secretariat* (MTN.GNS/W/120, 10 July 1991) which is based on the United Nations *Statistical Paper Series M No. 77, Provisional Central Product Classification* (New York: Department of International Economic and Social Affairs, Statistical Office of the United Nations, 1991). The UN classification system has been revised.

[22] For example, a common limitation on commitments relating to commercial presence (mode 3) is a requirement for a joint venture with a prescribed minimal level of participation by nationals.

[23] Thus, for example, bindings of commercial presence (mode 3) under market access might be qualified by a horizontal note to the effect that all foreign investment is subject to official review and authorization.

## *National Treatment*

In GATS, the national treatment obligation requires that a WTO Member treat services and service suppliers of other Members no less favourably than its own like services and service suppliers.[24] But whereas in GATT the national treatment provisions are powerful, applying to virtually all goods without exception,[25] the GATS national treatment principle applies only to those services listed in national schedules. As well, national treatment commitments are frequently qualified by general or sector specific limitations.

Because most governments participating in the Uruguay Round had well-entrenched systems of internal regulations that precluded or inhibited imports by the denial of national treatment and because widespread dismantling of these barriers was not politically feasible, it was impossible to include in the GATS any national treatment obligation that would apply across the board to all services.[26] Rather it was decided that any «national treatment» commitments should be negotiated and included, with reference to identified services activities, in national schedules of commitments.

## *Market Access Commitments*

For services sectors listed in national schedules, Members must satisfy each of the requirements for market access set out below, but subject to any limitation inscribed in their schedule.[27] In other words, where a Member wishes to maintain or be able to adopt a domestic measure inconsistent with these market access obligations in relation to a listed sector or activity, the Member had to describe the measure or use other language preserving this flexibility.

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[24] GATS Art. XVII. Art. XVII.2 reflects the fact that national treatment need not necessarily require formally identical treatment. Paragraph 3 of the article establishes that the real test of national treatment, whether or not formally identical, is equality in «conditions of competition.» GATT Art. III refers only to «like» rather than «competing». This seemingly narrower definition is not itself unambiguous, as is evident from GATT dispute settlement cases, many of which have revolved around alleged differences in treatment of «like» imported and domestic products.

[25] GATT Art. IV exempts screen quotas from the national treatment obligation. However, interestingly, such quotas might be considered a limitation on trade in a service (entertainment) rather than a good (exposed film).

[26] In contrast, in NAFTA there is a general «national treatment» obligation with a voluminous list of «grand fathered» exceptions. The NAFTA approach freezes the existing degree of liberalization whereas under GATS Members may introduce new discriminatory measures for any unlisted or service on any service which has been listed but with respect to which no obligations are being accepted because the schedule describes the commitment as «unbound» for a particular mode of delivery.

[27] GATS Art. XVI:1.

In relation to listed services activities, Members commit to not impose restrictions of the following kinds, except as identified in their schedules:

- Limitations on the number of service suppliers, whether by quota, monopoly, exclusive service supply or on the basis of an economic needs test.
- Limitations on the total value of service transactions or assets in the form of numerical quotas or the requirement of an economic needs test.
- Limitations on the total number of service operations or on the total quantity of service output expressed in terms of designated numerical units whether in the form of quotas or the requirement for an economic needs test.
- Limitations on the number of natural persons that may be employed in a particular specified sector or activity or that a service supplier may employ who are necessary for, and directly related to, the supply of specific service whether in the form of numerical quotas or the requirement of an economic needs test.
- Requirements as to the type of legal entity or joint venture through which a service supplier may supply a service.
- Quantitative limits on the participation of foreign capital in terms of a maximum percentage of foreign share holding or a maximum total value of individual or aggregate foreign investment.

Members' market access commitments for services under GATS are analogous to those found in national goods schedules with respect to bindings of maximum tariff rates. However, whereas national schedules on goods frequently contain bound levels of duty at rates below previously applied rates,[28] most bindings of market access in services schedules negotiated in the Uruguay Round simply freeze the *status quo*. This, in itself, enhances the transparency and predictability of rules regarding services trade, but does little to promote liberalization directly. Scheduled commitments form the starting point for subsequent rounds of negotiations on services trade liberalization.

## Other Obligations Relating to Listed Services Sectors and Activities

**International Transfers and Payments.** In sectors listed in their national schedules, Members may not frustrate the implementation of their obligations and commitments by imposing restrictions on the

[28] This observation is true only for developed countries. Developing country schedules rarely contain bindings that result in a lowering of applied duties. Developing countries' schedules frequently contain bound rates well in excess of current applied rates.

international transfers of funds and payments to settle current transactions. However, in a situation of balance-of-payments emergency temporary payments restrictions may be instituted. Article XII envisages that balance of payments restrictions on services would be subject to the same conditions and multilateral monitoring as those imposed on goods.[29]

**Enhanced Transparency Obligations.** In addition to the general publication obligation referred to above, Article III requires each Member promptly and at least once every year to inform the WTO of the introduction of any new law, regulation or administrative guideline which significantly affects trade in a services sector listed in its national schedule as well as changes to existing laws, regulations and administrative guidelines. Each Member must also establish one or more enquiry points to provide specific information to other Members regarding its services regime in relation to the sectors the Member has listed in its national schedule. GATS does not oblige Members to disclose confidential information the publication of which would impede law enforcement or otherwise conflict with the public interest or which would prejudice legitimate commercial interests.[30]

**Domestic Regulation.** For sectors in which specific commitments are undertaken, each Member must ensure that all measures of general application are administered in a reasonable, objective and impartial manner. Measures relating to qualification requirements and procedures, technical standards and licensing requirements cannot nullify or impair specific commitments by imposing requirements or standards not based on objective and transparent criteria, such as competence and ability to provide the service, or that are more burdensome than necessary to ensure the quality of the service. In the case of licensing procedures, the procedures themselves must not be restrictions on the supply of a service. Where authorization is required to provide a service, each Member must inform applicants regarding whether authorization has been granted within a reasonable time.[31]

**Monopoly Service Suppliers.** Where a Member's monopoly service supplier competes in the supply of a service which is outside the scope of its monopoly rights and in a sector listed in the Member's schedule, the Member must ensure that the monopoly supplier

[29] GATS Articles XI and XII. These provisions mirror GATT Article XII. Only the GATS provisions, however, specifically recognize that particular pressures on the balance of payments of a Member in the process of economic transition may necessitate the use of restrictions to ensure the maintenance of a level of financial reserves adequate for the implementation of its program of economic transition.

[30] GATS Art. III*bis*.

[31] GATS Art. VI.5.

does not abuse its monopoly position. Abuse would include, for example, subsidizing its activities in the competitive market from its monopoly profits.[32]

## Post Uruguay Round Agreements in Specific Sectors[33]

Members agreed to continue negotiations after the close of the Uruguay Round in four areas where it was felt that insufficient progress had been made: movement of natural persons, financial services, basic telecommunications and maritime transport.

At the end of the Uruguay Round, many developed and some developing country Members made specific commitments to provide access to intra-corporate transferees who are needed to manage a service supplier's commercial presence and to business visitors seeking to enter temporarily to market and negotiate contracts. Negotiations were kept open until the end of 1995 in the hope that offers in this area might be improved. There were only marginal improvements in the package of commitments finally agreed to.[34]

Negotiations on financial services were not concluded by the end of the Uruguay Round. Largely, this was due to American unwillingness to enter into access commitments on an MFN basis. The United States felt that granting MFN would permit very liberal access for financial services suppliers of all other Members, while the access that American financial services suppliers would be getting in return from some Members, especially those in South East Asia, would remain limited. Negotiations resumed in 1996 and ultimately, in December 1997, a new agreement was reached on financial services under which 102 Members, including the United States made additional commitments.[35] Significantly, the US dropped its broad MFN exemption in relation to financial services.

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[32] Members are also obliged (Art. VIII.1) to ensure that monopoly service suppliers do not undermine access commitments undertaken in national schedules of concessions.

[33] One such topic related Annex is that on Article II exemptions, described under «Most Favoured Nation» above.

[34] Members recorded their additional commitments in this area in annexes to the Third Protocol to the General Agreement on Trade in Services adopted 24 July 1995.

[35] These new commitments were annexed to the Fifth Protocol to the General Agreement on Trade in Services. The protocol is entered into force in March 1999. A previous set of enhanced commitments had been annexed to the Second Protocol to the General Agreement on Trade in Services, adopted July 2, 1995 and in force on September 1, 1996. The new commitments on financial services are discussed in R. Dattu, J. Boscariol, «WTO Pact Revolutionizes Financial Services Trade» (1998) 17 National Banking Law Review 25.

Many developed country Members based their commitments regarding financial services on the Understanding on Commitments on Financial Services.[36] This non-binding understanding provides a scheme for improved access which may be incorporated in national schedules of commitments. It is likely to form the benchmark for future liberalization commitments.Telecommunications is both a distinct services sector, as well as an essential means of delivery of many other services. An Annex to GATS addresses the failure to reach agreement on commitments regarding the provision of basic telecommunications services.[37] As in the case of financial services, failure to reach a broad based agreement was attributable to the unwillingness of the US and others to enter into liberalization commitments on an MFN basis in circumstances where they were denied reciprocity in a significant number of national markets. Negotiations recommenced in 1996 and, after some additional offers had been made, resulted in an agreement to include basic telecommunications in the services schedules of 71 Members.[38]

Maritime transportation services is the subject of various kinds of protectionist measures including rules which restrict access to ports or provide access on a discriminatory basis. At the end of the Uruguay Round, there was no agreement among Members to make commitments to remove these measures. Other countries pressed the US to forego protection of its domestic shipping achieved through the notorious *Jones Act* which requires that all maritime carriage between US ports be on US flag vessels built in the US and crewed by US citizens. Negotiations were scheduled to be completed in June 1996, but have been suspended in the absence of any movement from the US.[39]

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[36] The Understanding is reprinted in GATT Secretariat, THE RESULTS OF THE URUGUAY ROUND OF MULTILATERAL TRADE NEGOTIATIONS: THE LEGAL TEXTS (Geneva: GATT Secretariat, 1994)[*THE RESULTS OF THE URUGUAY ROUND OF MULTILATERAL TRADE NEGOTIATIONS: THE LEGAL TEXTS*], at 477.

[37] Negotiators were not successful in defining «basic telecommunications». Negotiations encompassed all public and private end-to-end transportation of customer-supplied information (*i.e.*, simple transmission of voice or data from sender to receiver).

[38] National commitments were annexed to the Fourth Protocol to the General Agreement on Trade in Services, adopted April 30, 1996, in force January 1, 1998. The negotiators had elaborated a set of principles on such matters as competition safeguards, interconnection guarantees, transparent licensing processes and the independence of regulators in a reference paper. Most Members committed to the reference paper in whole or in part.

[39] The sensitivity regarding the *Jones Act* in US domestic politics is vividly under scored by Art. 3(a) of the Introduction to the General Agreement on Tariffs and Trade 1994 which, in effect, retains for the *Jones Act* the exemption from the application of GATT for prior legislation contained in GATT 1947. Under the Protocol of Provisional application (and all subsequent accession protocols), GATT Contracting Parties were obliged to apply the provision of the Agreement's Part II only to the extent that they did not conflict with mandatory legislation in place before accession. This exclusion was dropped from GATT 1994 for all prior legislation, other than the *Jones Act* and similar maritime transport legislation.

## Modification of Schedules

Under GATS Article XXI, after three years have elapsed from its entry into force, a Member may withdraw concessions in its national schedule at any time on three months notice.[40] Such withdrawals are to be accompanied by negotiated compensation to Members whose services exports may be affected. In the event of failed compensation negotiations, an affected exporting country may seek arbitration.[41] Where arbitration has been requested, the Member seeking to modify its schedule cannot make the modification until it has given compensation in accordance with the arbitration award. If it does not, any Member who participated in the arbitration may withdraw concessions in retaliation. If arbitration is not requested by an exporting Member, the Member seeking to make the change is free to do so.

The following section describes the various ways in which GATS rules have evolved from the basic framework of rules described above since the conclusion of the Uruguay Round. The continually changing rules of the GATS make the services agreement a rolling target for transition economies seeking to accede to the WTO.

## Accession Challenges I: The Evolving Nature of GATS Rules

GATS requires successive rounds of further negotiations on services trade liberalization, the first of which began in February 2000, to increase levels of commitments in schedules and to reduce adverse effects of government measures on services trade. Reducing adverse effects includes more than eliminating discriminatory measures, potentially extending to the removal of all forms of barriers to market access. Although there is a requirement to negotiate further liberalization, there is no obligation on individual Members to ensure that the process of negotiation does in fact lead to liberalization. Indeed the requirement itself is qualified by language of Article XIX:2 which stipulates that «the process of liberalization shall take place with due respect for national policy objectives and the level of development of individual Members …»

In March 2001, the Services Council established the negotiating guidelines and procedures for the new round. All Members of the WTO were to have tabled requests for improved market access by 30 June 2002. Initial offers of market access were to have been ta-

[40] These provisions are analogous to GATT Art. XXVIII.
[41] There is no parallel provision in GATT Art. XXVIII.

bled by 31 March 2003. Not all Members met these deadlines. Negotiations are ongoing with a view to concluding an agreement as part of the Doha Round in 2005.[42]

In addition to providing for negotiations on liberalization of market access, GATS provides for negotiations in four specific areas of GATS rules where progress was not possible during the Uruguay Round: safeguards, government procurement, subsidies and domestic regulation. The status of these negotiations is summarized below.

**Safeguards.** Under GATT Article XIX, and the WTO Agreement relating to Safeguards,[43] Members are permitted, subject to certain conditions, to suspend obligations and to withdraw tariff concessions on a temporary basis, to contain or forestall serious damage to a domestic industry. GATS Article X provides for the negotiation of similar provisions for services by 1998. This deadline was recently extended to March 15, 2004. The fundamental desirability and feasibility of «safeguards» provisions for services is an issue which is still being discussed. While there are some proposals on the table, no consensus is emerging on disciplines in this area.

**Government Procurement.** GATS Article XIII explicitly excludes government procurement from the general MFN obligation as well as any specific market access and national treatment commitments entered into in national schedules.[44] However, the Article commits Members to negotiations on procurement which began in January 1997. The need for separate procurement rules in services is not at all clear. The plurilateral Government Procurement Agreement[45] (GPA) covers services. The interest of Western countries in a services procurement agreement can presumably be explained by their failure to «multilateralize» the GPA at the end of the Uruguay Round.[46] It seems unlikely that Article XIII negotiations will achieve a better result. The negotiating group is still working on developing a work plan and little progress has been made.[47]

**Subsidies.** Under GATS Article XV, Members are obliged to negotiate disciplines to avoid trade-distorting effects of subsidies. Such disciplines could be modeled on the rules in the Agreement on Sub-

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[42] Ministerial Declaration of 14 November 2001 (WT/MIN(01)/DEC/1), para. 15.

[43] The rules regarding safeguard actions were elaborated significantly in the Agreement on Safeguards forming part of Annex 1A to the Marrakesh Agreement establishing the World Trade Organization.

[44] Notwithstanding this «blanket» exception, some schedules show «horizontal limitations» on national treatment and market access for procurement. Presumably such limitations are inserted for greater clarity and, perhaps, to allay the concerns of domestic interests.

[45] Forming part of Annex 4 to the Marrakesh Agreement establishing the World Trade Organization.

[46] At the end of the Uruguay Round there were only 15 parties to the GPA. Now there are 27.

[47] See Council for Trade in Services: Special Session, Report of Meeting held on 9 December 2002-13 January 2003, 21 February 2003 (TN/S/M/5) at 15.

sidies and Countervailing Measures dealing with subsidies that affect trade in goods, but little progress has been made to date. The negotiating group is still working on developing a work plan.[48]

**Domestic Regulation.** The development of disciplines in this area has been under discussion since the close of the Uruguay Round. Some specific disciplines were agreed on for accountancy, but there has been little progress on the development of further general disciplines applicable to all services sectors. Currently the Council on Trade in Services is continuing to collect examples of national practices.[49] If new disciplines on domestic regulation were agreed to for all services sectors, this would mark a substantial increase in the burden of GATS compliance for transition economies.

If the current round of negotiations concludes before a country joins the WTO, both the substantive rules and the expectations for market access will have expanded, raising the bar for accession. Even prior to the conclusion of the round, the market access positions taken by the Members in the round are likely to inform their positions in accession discussions. While acceding countries have observer status, and may be aware of changes in Members' expectations regarding market access, they will not be able to influence them. They will have to adjust the level of commitments they are prepared to make to a rising set of expectations from the Members.

Similarly, developments during the round with respect to new rules for safeguards, subsidies, government procurement and domestic regulation will affect the burden of the package of commitments that acceding countries will have to shoulder to become Members. Again, these disciplines will be set without the direct participation of acceding countries.

## *Accessions by Other Countries*

From the end of the Uruguay Round in 1994 to early 2003, nineteen countries, including China and thirteen other transition economies, have acceded to the WTO. Twenty-seven other countries have sought to join the WTO, eleven of them transition economies, so far without success. A review of the protocols of accession reveals that the level of commitments being negotiated and committed to by new Members is higher than that undertaken by many WTO Members at the close of the Uruguay Round and appears to be climbing.[50]

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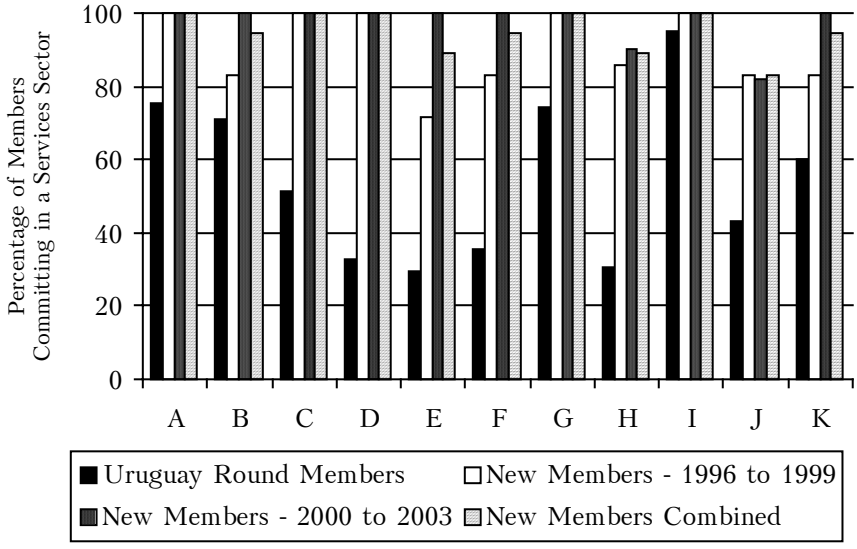
[48] *Ibid.*

[49] *Ibid.*

[50] P. Nary, RUSSIA AND THE WORLD TRADE ORGANIZATION (Houndmills, U.K. and New York: Palgrave 2001) [*Nary*] at 91, 110-120, 139-140. The higher standard being imposed on acceding countries has been the subject of concerns expressed in the WTO General Council (WT/GC/M/32, 9 February 1999).

The individualized nature of national schedules of commitments makes generalizations about the level of obligation undertaken difficult. Nevertheless, some measures may be used to assess the extent to which the bar for WTO accession has been raised.[51] The figure below shows that a much higher percentage of new WTO Members have made specific commitments in each of the twelve major sectors of services activities than those countries who became WTO Members at the end of the Uruguay Round. In Distribution Services, for example, 100 percent of post Uruguay Round acceding countries have made commitments, while only 33 percent of Uruguay Round Members did so.

**Comparison of Percentage of WTO Members Making Commitments in Major Service Sectors**




**Legend:**

A. Business/Professional
B. Communication
C. Construction
D. Distribution
E. Education
F. Environment
G. Financial
H. Health
I. Tourism
J. Recreation
K. Transport

There is also some evidence that the bar is continuing to go up. In every sector but one, a higher percentage of the countries acceding since

[51] Concern that new Members are being required to meet higher standards has also been expressed by some existing developing country Members who fear that these higher commitments will be used to try to negotiate higher levels of commitments from other countries in the context of the current negotiations.

1999 have made commitments as compared to the countries that joined between 1995 and 1999. Apart from China,[52] all countries acceding since 1999 have accepted some commitments in all 12 major services sectors. The only sector excluded by China was health, a sector attracting commitments by only 30.5 percent of Uruguay Round Members.

The structure of the GATS means that the quality of commitments must be examined to determine the effective extent of market access agreed to by each Member. Here again, there is some evidence that acceding countries are making stronger commitments than those countries that joined at the end of the Uruguay Round.[53] Mode 3, commercial presence, is arguably the most important mode of entry for foreign service providers in many sectors. For some services, like construction services, it is the only technically feasible mode of entry. The quality of commitments in mode 3 demonstrates the same pattern noted above. Again, ignoring China, of the ten other countries acceding since 1999 only Jordan (five) and Macedonia (three) have listed more than two services sectors in which they are unbound with respect to whether they permit market access by commercial presence or are free to restrict foreign ownership. Again, by comparison, the group of seven countries acceding between 1995 and 1999 made weaker commitments. Four of the seven had these kinds of limitations in more than three services sectors. Nevertheless, overall, the group of all acceding countries tended to have fewer restrictions than even the major developed countries.[54] Four acceding countries imposed no restrictions at all on mode 3.

There are several other ways in which it is possible to show that the bar for acceding countries has been raised. In their protocols of accession, many countries have been required to give undertakings in excess of what is required by GATS itself — obligations to which Uruguay Round Members are not subject. For example, as a condition of their accession, Albania, Armenia, Bulgaria, China, Georgia, Estonia, Jordan, the Kyrgyz Republic, Latvia, Panama, and Chinese Taipei were all required to commence negotiations to join the Government Procurement Agreement.[55] Several countries have had to make commitments to provide reports on the progress of privatization programs[56] and to ensure compliance by local governments with WTO obligations.[57]

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[52] Given the economic and political weight of China, it is unlikely that Chinese commitments are representative of the kinds of commitments that will be imposed on other acceding countries.

[53] This analysis is based on the information presented in the charts in Schedule 2 annexed to this paper.

[54] As shown in Schedule 2, the EU imposed such limitations on commercial presence in 8 sectors, Canada in 5 and the United States in 4.

[55] A review of protocols of accession reveals similar WTO-plus obligations in other areas as well.

[56] Armenia, Estonia, Georgia, Latvia, Lithuania, Macedonia and Moldova.

[57] Albania, Armenia, China, Croatia, Estonia, Georgia, Kyrgyz Republic, Latvia, Lithuania and Moldova.

## *WTO Dispute Settlement Related to GATS*

The GATS, together with the various trade in goods agreements, and the Agreement on Trade Related Intellectual Property Rights, is an integral part of the WTO's legal instruments and is subject to the WTO's dispute settlement procedures under the Dispute Settlement Understanding (DSU).[58] Uncompensated breaches in obligations under GATS can lead to retaliation («compensatory withdrawals»).[59]

Dispute settlement cases are an important way in which the application of the rules of the WTO is progressively clarified. Each successive case defines the way in which the rules apply to the particular government measure at issue and provides guidance regarding how the rules will be applied in future cases. Though WTO panel and Appellate Body decisions in particular cases are not binding on future panels, consistency of decision-making is essential to ensuring the predictability of trade rules. In practice, panels and the Appellate Body try to ensure that there decisions are consistent with earlier ones.

At this early stage, it is not clear how dispute settlement panels and the Appellate Body will deal with disputes under GATS. Such disputes present different challenges because of the untested and customized nature of the obligations imposed under GATS. One issue, which has arisen, is the relationship between the GATS and the other agreements forming part of the Uruguay Round Final Act. The approach taken to date is to treat each agreement as applying in accordance with its own terms, meaning that, where there is an overlap in the application of two or more agreements in relation to a particular measure, panels should try to give effect to all agreements which apply. In the *Periodicals Case* for example, Canada argued that a measure related to advertising services in periodicals and that it was not obliged to provide national treatment in this sector because Canada had not listed such services in its national schedule of commitments. The measures included a tax on magazines with foreign advertising directed to the Canadian market. The panel and Appellate Body determined that the measures were contrary to Can-

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[58] GATS Art. XXII. Under the WTO, disputes are governed under the Dispute Settlement Understanding forming Annex 2 to the Marrakesh Agreement establishing the World Trade Organization. Disputes relating to GATS are also subject to the Decision on Certain Dispute Settlement Procedures for the General Agreement on Trade in Services which provides for the establishment of a special roster of panellists with expertise relating to trade in services or GATS. The Decision is reprinted in THE RESULTS OF THE URUGUAY ROUND OF MULTILATERAL TRADE NEGOTIATIONS: THE LEGAL TEXTS, above note 36, at 457.

[59] GATS Art. XXII. With respect to disputes relating to obligations under GATS, however, the Dispute Settlement Body, must only permit the removal of concessions where it thinks the breach was sufficiently serious. Such a requirement is only applicable for disputes under GATS. Members are also obliged to consult with other Members with respect to any matter affecting the operation of GATS in accordance with the process set out in the DSU.

ada's obligation to provide national treatment in relation to magazines as goods under GATT.[60]

In the other significant case dealing with services obligations, the challenge to the European Union's import preferences for bananas from certain countries under the Lomй Convention,[61] GATS MFN obligation was interpreted by the WTO Appellate Body as requiring that measures not discriminate in their express terms (*de jure* discrimination) or in the way they operate in practice (*de facto* discrimination).[62] In the same case, the Appellate Body determined that in assessing whether services were «like» for the purposes of the GATS national treatment obligation, it is only necessary to have regard to the nature and characteristics of the services transactions themselves and not the origin of the bananas being provided by the services providers.[63]

While dispute settlement panels cannot change GATS obligations, in clarifying how they apply in particular situations, panel decisions can interpret the obligations in ways which may be different from what the Members themselves expected. As the increasing number of cases on GATS work their way through the dispute settlement system, the meaning of GATS will evolve, changing the overall burden of assuming GATS obligations for acceding countries.

## *The Evolving Understanding of GATS Commitments*

Our understanding of GATS rules is evolving in other ways as well. The GATS represents a significant innovation in international trade rules. Prior to the close of the Uruguay Round, there were no multilateral rules relating to services. Consequently, it is not sur-

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[60] *Canada – Certain Measures Concerning Periodicals* AB-1997-2 (1997) (WT/DS31/AB/R)[*Canada- Periodicals*]. This approach was also applied in *EU – Bananas*, above note 12.

[61] This obligation replicates for services the GATT Article I obligation for goods.

[62] *EU – Bananas*, above note 12. This finding is discussed in H.A. Milan Smitmans, «Dispute Settlement in the Services Area under GATS,» in SERVICES TRADE IN THE WESTERN HEMISPHERE: LIBERALIZATION, INTEGRATION AND REFORM, Sherry M. Stephenson, ed. (Washington, D.C.: Brookings Institution Press, 2001) at 112-115.

[63] *Ibid.*, at para. 7.322. The following cases have been brought in relation to GATS provisions: *EU – Bananas*, above note 12, *Canada – Periodicals*, above note 60; *Canada – Certain Measures Affecting the Automobile Industry* (139 brought by Japan, 142 brought by EC) (2000)(WT/DS139, WT/DS142)[*Canada – Autopact*]; *Japan – Distribution Services* (1996)(WT/DS45); *Belgium – Commercial Telephone Directory Services*, (1996)(WT/DS80); *Canada – Film Distribution Services* (1998)(WT/DS117); *Mexico – Telecommunication Services* (2000)(WT/DS204); *United States – Cross-Border Supply of Gambling and Betting Services* (2003)(WT/DS285); *United States – Cuban Liberty and Democratic Solidarity Act* (1996) (WT/DS38); *Nicaragua – Imports from Honduras and Colombia* (2000)(WT/DS201); *Turkey – Fresh Fruit* (2001)(WT/DS237); *United States – Softwood Lumber* (2003)(WT/DS277). Of these only *EU – Bananas*, *Canada – Periodicals* and the *Canada – Autopact* cases have resulted in final decisions to date.

prising that there has been some uncertainty regarding the scope of GATS application and the precise nature of the obligations it imposes. The interpretive challenges have been identified in the secondary literature[64] and include some fundamental questions regarding how the various obligations relate to each other. There is some uncertainty, for example, regarding whether transactions over the Internet are within mode one (cross-border supply) or mode two (consumption abroad). Perhaps the best evidence of the shortcomings of the structure, however, has been the need to develop special instruments embodying a customized set of commitments for financial services and telecommunications.[65]

Uncertainty is compounded in the commitments listed in national schedules. Member countries use inconsistent and frequently opaque language[66] to define the scope of their obligations in listed sectors, and, in some cases, use different approaches to the classification of services activities. As well, it is common for countries to provide additional information regarding their national regimes for the ostensible purpose of explaining the basis for the restrictions or in the interests of transparency. Where such information is not required by GATS, however, its legal impact is questionable and adds to the uncertainty of commitments.

In some cases inconsistent scheduling is caused by uncertainty regarding the requirements of the GATS. Consider the following example. There is some uncertainty regarding the need to list restrictions on market access other than those mentioned in Article XVI.2 and set out above, such as licensing. The WTO Secretariat takes the position that it is not necessary to do so.[67] Nevertheless, many countries have listed such limitations in their national schedules. This approach may have been adopted in the interests of transparency or to address concerns of domestic interests. It is possible as well that market access, for the purposes of the GATS, is not exhaustively defined by the absence of the specific kinds of limitations on market

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[64] Some of the basic problems are discussed in P. Low & A. Mattoo, «Is there a better way? Alternative Approaches to Liberalization under GATS,» in GATS 2000, above note 6, at 449-457. They include, for example, questions such as what is the relationship between market access and national treatment limitations and between Article VI (domestic regulation) and Article XVI (market access)? and is it possible to schedule a limitation inconsistent with the domestic regulation obligations?

[65] Understanding on Financial Services and Reference Paper in Telecommunications.

[66] For example, some countries stipulate that market access is subject to compliance with an «economic needs test.» This wording, taken from GATS Article XVI, provides little information regarding the nature of the limitation, and could be interpreted in such a way as to nullify any commitment. Art. XX.3 provides that national schedules of commitments are integral parts of the GATS. As a result, it is possible that the different approaches to scheduling and the different interpretations of GATS substantive obligations that they reflect may affect how those substantive obligations are interpreted.

[67] GATT Secretariat, Scheduling of Initial Commitments in Trade in Services: Explanatory Note (1993) and Revision of Scheduling Guidelines, Note by the Secretariat, 5 March 1999 (S/CSC/W/19). The Note indicates that the interpretation in the Guidelines is not binding (at 1).

access mentioned in GATS Article XVI.2. Article XX.1 requires Members to list the «terms, limitations and conditions on market access» in relation to listed sectors. Consistently, Article XVI requires Members to provide «market access on terms no less favorable that provided for under the terms, limitations and conditions agreed and specified in its Schedule.» Because market access in not defined, it could be argued that *any* restriction on market access must be listed if it is to be maintained. The difficulty with such an interpretation is that it converts a concrete set of commitments defined by the absence of the specific types of restrictions mentioned above into an uncertain and open-ended obligation to provide «market access.» One would have expected that, if the drafters of the GATS had intended such a significant result, they would have expressed themselves in much clearer language. Also, why would it be necessary to have a list of discrete commitments, if market access was to be defined more broadly? The correct interpretation of these provisions of the GATS will be determined, ultimately, through the dispute settlement process, as Members challenge restrictions on market access. Nevertheless, the ambiguity surrounding this basic obligation illustrates the uncertainty shrouding many provisions of the agreement.

Lack of certainty with regard to GATS rules means that it is difficult for acceding countries to determine the precise practical impact of the obligations that they are being asked to undertake and how to schedule properly the commitments they are prepared to make. As well, uncertainty impairs the ability of acceding countries to determine what market access they can expect from the other Members based on those Members' schedules of commitments.

At first glance, the problems associated with uncertainty and lack of clarity of GATS obligations may appear common to all WTO Members. In fact, the challenge for acceding countries is greater. The level of scrutiny that the national schedules of commitments in protocols of accession are subject to is far more exacting than the review undertaken of Members' commitments at the end of the Uruguay Round. The inconsistent and unclear language which characterizes the national schedules of Members that joined at the end of the Uruguay Round reflects the relatively light review which national schedules received at the close of the round in the rush to complete it. Such a relaxed approach to scheduling is not applied to offers of services commitments by acceding countries.[68]

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[68] Feketekuty, above note 7, at 99. At the end of the Uruguay round, Western countries were above all pre-occupied with obtaining a critical mass of GATT contracting parties to convert to WTO Membership. In the four months between December 1993 and the Marrakesh meeting in April 1994, there was little time for true negotiations and developed countries were forced to accept exiguous services offers from the developing countries.

Since the close of the round, existing Members and the WTO Secretariat have advocated an interpretive approach that seeks to minimize the content of limitations included in national schedules. The Secretariat has said that half the limitations inscribed in national schedules at the end of the round are unnecessary.[69] In seeking to ensure that acceding countries schedule their commitments based on a relatively narrow and untested reading of what may be inscribed, however, these countries are being asked to accept the risk of future challenges to their national rules in ways that existing Members are not. This poses a particularly difficult challenge to newcomers to the WTO system who will understandably not have the same degree of understanding and confidence in the fairness of its operation.

A related challenge is that the wide variety in the form and substance of national schedules of commitments means that there is no standard yardstick for admission.[70] In most other areas, WTO disciplines must be accepted in full. In tariffs, each country must negotiate its level of commitment but expectations are easier to predict based on more extensive past practice and the ready comparability of tariff bindings. In services, the customized nature of each national schedule of commitments, and the complexity and diversity of national approaches to services regulation means that each country must develop its services offer with few such reference points. The practice of many founding Members of the WTO was to describe their existing regime in their national schedules, resulting in little actual liberalization providing instead a commitment not to make national rules more restrictive of services trade. As discussed below, largely because of the rapid evolution of domestic policy this option is not realistically available to transition economies in the accession process. In any case, it would not likely be acceptable to WTO Members, given the rising standard being set for WTO accession.

## Accession Challenges II: Changing Conditions in Transition Economies

### *Policy Development and Legislative Uncertainty*

Compliance with GATS disciplines, especially GATS rules on domestic regulation and market access, involves the implementation of transparent and effective regulatory structures. This poses particular challenges for countries in transition that, historically, have

[69] GATS 2000, above note 6.
[70] Nary, above note 50 at 93.

had weak legal systems and institutions.[71] Often the legal regime is obscure, either because there is no current law or regulation or because laws and regulations conflict or are not implemented in practice.[72] This was especially true in the services area because services was regarded as an «unproductive sector» during the Soviet era.[73]

During the 1990s, as countries in transition moved from a command to a market economy, the rules governing services trade changed in dramatic fashion because as privatization and other aspects of economic transition proceeded, different kinds of regulatory structures were needed.[74] In some cases, reforms were too rapid, such that a second round of reform was required to eliminate problems created by initial changes.[75] Since the process of transition will continue for some time, regulatory regimes will continue to change with it.

Substantial progress has been made in the enactment of legal rules, but progress in the development of the institutions and expertise necessary to ensure that legal rules are effectively implemented and enforced has not kept pace.[76] Enhancing implementation and enforcement, while critical, is a much larger, slower and more expensive task than simply pushing new laws through the legislature. The institutions charged with implementation and enforcement must be properly organized and adequately funded. Officials must develop required expertise. Compliance with the law will be facilitated where legal rules are perceived as legitimate by those who must are subject to them. Historically, however, legal rules in transition economies have suffered from a lack of legitimacy due to weak, or worse, selective, enforcement. Legitimacy may be enhanced by ensuring that stakeholders have a greater opportunity to participate in the policy development process as well as through other means.

It was only in the late 1990s that international assistance agencies began to provide money for implementation and enforcement to

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[71] OECD ECONOMIC SURVEYS: RUSSIAN FEDERATION (Paris: OECD, 2002) at 10. Nary discusses the historical basis for the lack of a strong legal tradition in Russia (at 24-29, 72-74). Nary describes post-Soviet Russia, for example as a «legal and institutional wasteland» and quotes Mikhail Gorbachev as saying that «Russia is not ready for the procedures of a law-based state» in 1990 (at 29).

[72] *Ibid.*, at 65, 82, 90.

[73] *Ibid.*, at 140.

[74] LAW IN TRANSITION: TEN YEARS OF LEGAL TRANSITION, G. Sanders & D. Bernstein, eds (EBRD, 2002)[*Law in Transition*] at 15, 25; EBRD, TRANSITION REPORT, 2001 (EBRD, 2002) at 33; EBRD, TRANSITION REPORT, 2000 (EBRD, 2001) at 39.

[75] LAW DRAFTING AND REGULATORY MANAGEMENT IN CENTRAL AND EASTERN EUROPE, SUPPORT FOR IMPROVEMENT AND MANAGEMENT IN CENTRAL AND EASTERN EUROPEAN COUNTRIES (Paris: OECD Center for Cooperation with Economies in Transition, 1997) at 18.

[76] This has been responsible for a large but diminishing gap between what the European Bank for Reconstruction and Development calls legal extensiveness and legal effectiveness (*Law in Transition*, above note 74, at 19-20).

complement their support for other aspects of legal reform. The cumulative consequences of underdeveloped and frequently changing services policies and laws in transition economies constrain their capacity to make binding commitments relating to how their services regimes will operate. It is hard to decide what liberalization commitments to offer and difficult to implement them once the accession process has been completed. The practice of scheduling commitments that mirrored their existing regime followed by many developed countries with stable regulatory regimes and mature market economies that joined at the end of the Uruguay Round is simply not feasible for transition economies now in the accession process.

Changing services regimes in transition economies affect the prospects for successful services negotiations in another way as well. In many countries in the accession queue, domestic policy changes involve liberalization of foreign market access.[77] In the context of the current negotiations, the Members have just agreed on a process to give credit to existing Members who have engaged in trade liberalization since the end of the Uruguay Round.[78] To the extent that Members have liberalized, other Members must take such liberalization into account in making their demands for improved market access. There is, however, no corresponding agreement on how or, indeed, whether there should be credit for such «autonomous liberalization» engaged in by countries during the accession period. This leaves acceding countries in a dilemma. They face the prospect that domestic reform initiatives may reduce their bargaining leverage in accession negotiations by reducing their ability to make concessions at the bargaining table.

## *Federal States and Local Governments*

A problem related to institutional weakness is the ability of the national government to make commitments which involve areas which are legally or practically within the power of regional and local governments. GATS applies to measures of all levels of government.[79] But, GATS obligations fall most heavily on national governments which are obliged to «take such reasonable measures as may be available to it to ensure observance» by sub-national bodies. In the case of Russia, for example, the national government would

[77] It is also true, however, that constrained budgets in transition economies may preclude resort to policy instruments that are available to others states, such as subsidies. In such a case, discrimination and market access become more attractive as ways to protect domestic interests.

[78] Agreed rules on the modalities for giving credit for such «autonomous liberalization» were adopted at a Special Session of the Council on Trade in Services on 6 March 2003.

[79] GATS Art. I:3(a).

be responsible under the WTO's dispute settlement machinery for any allegations of violations of GATS obligations by any of Russia's 89 sub-federal jurisdictions, as well as all lower levels of government and their respective agencies.[80] The ability of the state to make credible commitments with respect to matters within the jurisdiction of sub-national governments has been identified as a concern in the Protocols of Accession of other, less complex states such as Latvia, Estonia, the Kyrgyz Republic and Georgia. Most protocols of accession for transition economies have contained express guarantees of compliance by sub-national levels of government, going beyond what is required in GATS itself.[81]

Difficulties associated with making commitments in relation to measures of sub-national governments have a variety of sources. Some sub-national governments have jurisdiction over aspects of services supply in their geographic regions, such the power to impose licensing requirements or to approve direct investment. Regions that are very diverse in their level and kind of economic development as well as in their orientation to market reform, may adopt very different policies from those favoured by national governments that may undermine GATS commitments.[82] In the new constitutions in transition economies, the division of powers between levels of government is often unclear. This may permit sub-national governments to exercise powers in relation to services that are beyond what the constitution permits. For a host of political, economic and fiscal reasons, national governments maybe unable or unwilling to assert control over sub-national governments acting outside their jurisdiction in ways that affect services trade.[83]

In the course of time, practice, negotiation between national and sub-national governments, increased political and economic stability and domestic jurisprudence may combine to clarify and fix the re-

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[83] As noted above, «[services] measures by Members,» means measures taken by: «central, regional or local governments» (GATS Art. I:3(a)). As defined in the Federal Treaty of 1992, the Russian Federation consists of the following 89 subjects of the federation: 21 republics, six territories, 49 oblasts, one autonomous oblast, 10 autonomous okrugs and two cities of federal importance (Moscow and St. Petersburg).

[81] Albania, Armenia, China, Estonia, Georgia, Kyrgyz Republic, Latvia, Lithuania and Moldova.

[82] This is particularly true in Russia (See also OECD Secretariat, *The Role of Russia's Regions in Trade Policy* (Paris: OECD, 2003)[*OECD on Role of Regions*], at 8, 52).

[83] For example, during the Yeltsin era, sub-federal units effectively obtained exclusive jurisdiction when the federal state could not act because of a deadlock between the Duma and the President. This has happened in relation to various important economic reform packages, such as land reform (*OECD on Role of Regions*, *ibid.*, at 7). Since he took power in June 2000, President Putin has taken various other steps to ensure that the actions of the regions are consistent with federal law and the constitution. These reforms are discussed in M. Hyde, «Putin's Federal Reforms and their Implications for Presidential Power in Russia» (2001) 53 Europe-Asia Studies 719. One of the impediments to clarifying which level of government is responsible for different aspects of services regulation may be that an application to a constitutional court is not a feasible option.

spective roles of different levels of government. However, considerable uncertainty regarding who has the power to do what is likely to persist in the period of accession for most transition economies.

The actions of sub-national governments raise significant challenges not just in terms of fulfilling GATS obligations following accession, but also in developing an offer on services commitments as part of the accession negotiations. Offers of services commitments must reflect the priorities and existing restrictions of all sub-national bodies with effective responsibility in areas affected by GATS obligations, including, in particular, rules relating to licensing and investment.[84] This will force national governments to engage what may be politically difficult discussions regarding the respective jurisdictions of the various levels of government. As a precondition to such discussions, it will be necessary to provide training for local governments regarding unfamiliar GATS obligations.

WTO Members are of course aware of the negotiating complications arising from strong sub-national governments. Nevertheless, they will need to be assured that in entering into their GATS obligations countries in transition can provide a reasonable degree of assurance that sub-national governments are cognizant of GATS obligations and scheduled commitments and are willing to ensure their observance. In order to be able to do so transition economies will have to develop an efficient mechanism to coordinate trade policy development and implementation between the national government and relevant sub-national governments.

## *Regional Integration in CIS[85]*

The GATS MFN requirement is qualified by the Agreement's Article V, which permits Member countries to enter regional agreements to liberalize trade in services under prescribed conditions. To qualify for the Article V exemption, regional agreements have to meet conditions analogous to those present in GATT Article XXIV which provides a similar exemption in relation to trade in goods. Qualifying agreements must have «substantial» sectoral coverage, in terms of the number of sectors, volume of trade and modes of supply covered and provide for the elimination of substantially all discrimination in the trade of the parties, meaning measures providing for less than national treatment or less than MFN treatment. To be exempt, an agreement must be designed to facilitate trade between the parties to the agreement and not

[84] Nary, above note 50, at 100.

[85] The Members of the CIS are Azerbaijan, Armenia, Belarus, Georgia, Kazakhstan, Kyrgyz Republic, Moldova, Russia, Tajikistan, Turkmenistan, Uzbekistan and Ukraine.

raise the overall level of barriers to trade in services involving Members not party to the agreement.[86] Like those of GATT Article XXIV, the conditions of GATS Article V may be interpreted very differently by parties to a regional arrangement and the other WTO Members. Many WTO Member countries have entered into bilateral arrangements which confer mutual preferential treatment in agreements which could not, by any interpretation, meet the conditions of Article V.

At the beginning of Russia's accession in 1993, it declared that it had international trade agreements with 138 countries.[87] Significantly these included bilateral free trade agreements with former soviet republics making up the Members of the CIS. In September 1993, the CIS countries entered into an economic union agreement which provided for the gradual implementation of a free trade zone, followed by a customs union and then a common market for goods, services, capital and labour. A number of coordinating institutions were set up, including the Council of Heads of State and an Interstate Bank.[88] A multilateral agreement on a free trade area was entered into in 1994. In 1995, a customs union was agreed to between Russia, Belarus, Kazakhstan, and the Kyrgyz Republic. By 1998, Tajikistan had joined the customs union. These major agreements only define the broad outlines of the continually evolving relationships among the CIS countries.[89] By 1995, there were over 300 agreements between the Members of the CIS relating to different aspects of their economic relationship, though many of the obligations have never been implemented.[90]

Many of the treaties between the Members of CIS may not meet the requirements of Article V. For acceding countries, therefore, there would seem to be only two options: to include in their services offers a list of Article II exemptions which refers to existing preferential arrangements with Members of the CIS not meeting the requirements of Article V or to terminate these relationships. In light of the evolving nature of the relationships between the CIS countries it may be desirable to provide for the future mutual exchange of preferential treatment with CIS countries.[91] It is not likely, how-

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[86] GATS Art. V*bis* permits Members to enter into preferential agreements for the full integration of labour markets notwithstanding the MFN obligation.

[87] Nary, above note 50, at 142.

[88] Markiyan Malsky, Mykhailo Mykievych, Liana Kovtun, Roman Moskalyk, REGIONAL TRADING AGREEMENTS IN INTERNATIONAL ECONOMIC RELATIONS (Lviv: Ivan Franko National University of Lviv Press, 2003)[*Malsky*], at 38-39.

[89] By 2001, this customs union had been transformed into the Eurasian Economic Community (see Malsky, *ibid*., at 59-62)

[90] WTO Document WT/ACC/RUS/2, 2 June 1995, at 144. See generally Nary, *ibid*., at 143-145; Malsky, *ibid*., at 36-63.

[91] GATS Art. V.2 specifically provides that, in considering whether the requirements of Art. V are met, consideration may be given to the relationship of the agreement to a wider process of economic integration or trade liberalization among the countries concerned.

ever, that such an open-ended exemption would be acceptable to the Members of the WTO.[92] How to deal with the uncertain future of economic relationships within the CIS remains an additional challenge for transition economies seeking to accede to the WTO.

## Conclusion

The development of the market in transition economies on the one hand, and the concomitant reforms to their regulatory structures on the other make it extremely difficult for transition economies to develop a position on what services commitments they should make in their schedules of specific commitments. The approach taken by many developed countries was to schedule obligations reflecting the existing legal regime domestically. In light of the fast paced changes in countries in transition, this is not feasible. The alternative adopted by many developing countries that were original Members of the WTO was to schedule highly qualified commitments in a small number of sectors to preserve maximum flexibility. The Members of the WTO will not accept such weak commitments from acceding countries. Indeed, the bar to accession is going up. Acceding countries are being forced to take on progressively higher levels of commitments, higher even than those of developed country Members, as each year passes. The bar will continue to rise as new market access and GATS rules are being negotiated. Fundamentally, the rising bar means that transition economies are being required to commit to higher levels of liberalization. At the same time, accession is putting pressure on transition economies to find solutions to the often complex internal challenges associated with the relationships between national and sub-national levels of government and to plot the course for their evolving external relations within the CIS. Overall, the challenges relating to GATS for transition economies seeking to join the WTO are daunting.

[92] The practice to date has not consistently followed either option. The Kyrgyz Republic, for example, did not file a list of MFN exemptions or otherwise seek to reflect its commitments to other CIS states in its schedule of commitments (Nary, above note 50 at 144).

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