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Sectoral and plurilateral approaches in services negotiations: Before and after TISA

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INTRODUCTION

WITH THE STAGNATION of services negotiations under the WTO, TISA is the only framework that possesses the potential to advance direct global liberalisation and rulemaking. The use of a plurilateral format, in which all the major developed nations are participating as the next-best alternative, opens up the possibility of rulemaking and liberalisation in the services sector that would have great potential to offer a foundation for the creation of overseas business opportunities at a level that would be impossible for any of its participants to achieve in isolation.

TISA also shifts the focus from exclusively working on mega free trade agreements (FTAs) to utilisation of both mega-FTAs and plurilaterals as indispensable forums for services negotiations. It is of particular importance that both the EU and the US participate in TISA, in addition to Trans-Pacific Partnership (TPP) and the Japan-EU FTA. Between these fierce rivals (especially in the area of regulations), the TISA will reduce the risk of other countries being sandwiched between them, in a similar way that Japan was in the past. Indeed, both the US and the EU have already initiated pro-

EXECUTIVE SUMMARY

With the stagnation of services negotiations under the World Trade Organisation (WTO), the Trade in Services Agreement (TISA) is currently the only framework that possesses the potential to advance direct global liberalisation and rulemaking. The plurilateral format, used as the next-best alternative, opens up new possibilities that would be impossible for any of its participants to achieve in isolation.

This policy brief looks at the circumstances that led to the shortcomings of the General Agreement on Trade in Services (GATS), which in turn led to the inception of TISA. It also looks at the options that were available (in particular with regard to its legal form) before the negotiations took place as a free trade agreement outside the WTO. Moreover, it looks to how the TISA can eventually be multilateralised through

sectoral agreements such as the GATS Annex approach (i.e. sector by sector, or issue by issue).

If a universal agreement, based on reaching critical mass and extending the benefits according to the most-favoured nation (MFN) principle can be reached in individual sectors, there is potential to advance global services liberalisation from the TISA framework.

posals that take both mega-FTAs (in particular the TPP and the Transatlantic Trade and Investment Partnership (TTIP)) and TISA into consideration.

The major trading blocs will introduce the contents of TISA into their mega-FTAs and force Japan and other third countries to accept them, stressing the fact that they are international rules – unless they grasp the movement towards the TISA and become part of that movement. It can be assumed therefore, that the TISA will function as an “insurance policy”, providing significant leverage to protect Japan’s national interests in its mega-FTAs. Given the importance of the services sector, both the government and the private sector have recently displayed increased interest in the agreement.¹ In the view of various service industries, TISA is a framework worthy of the great effort required to achieve it.

THE NECESSITY OF AN ALTERNATIVE APPROACH TO GATS

Trade in services now occupies an important position in international trade alongside trade in goods. It represents 70% or more of the GDP of developed nations and its volume is increasing annually. Although the WTO General Agreement on Trade in Services (GATS) was a groundbreaking framework, merely by expanding the WTO scope into services (including domestic regulations for investments), the agreement’s scope, depth, and commitments do not come close to those for goods.² GATS divided services into four means of delivery, Modes 1 to 4, and stipulated the disciplines on MFN status, national treatment (NT), and market access (MA), as well as appending Schedules of Commitments clarifying the specific commitments of each signatory nation. Generally speaking, however, GATS merely presents a ‘snapshot’ of the existing level of liberalisation in each country at the time of its conclusion.

It cannot be said that GATS has evolved steadily as foreseen at its conception – with the exception of the Agreement on Financial Services and the Agreement on Basic Telecommunications in 1997. With the failure to conclude the Doha Round in summer 2008, any progress (including the 2008 Signaling Conference) should be regarded as no longer relevant today. In order to break the deadlock in the WTO, the WTO Ministerial Conference in 2011 made efforts towards seeking separate resolutions for each agenda on the table, each within separate timeframes. This approach has opened up the possibility of sectoral or issues-based plurilateral agreements amongst interested WTO members only, as opposed to the multilateral approach based on an agreement between all WTO members. TISA is indicative of this trend.³

The Doha Round in regards to services was bogged down due to three factors. Firstly, the WTO negotiation was based on parallel negotiations in multiple fields, which would incentivise a deal but let them maintain their sensitivities, as they may become valuable bargaining chips in settling large packages.

Secondly, there was an excessive fear of free riding on the outcomes of liberalisation. The agreements on Financial Services and Basic Telecommunications are founded on the concept of extending the benefits to non-members based on the MFN principle. With an increasing concern towards the free rider problem in developed countries including the US, a strong sense of caution has also developed in the services field given the rapid growth of developing countries, leading to an increasingly mercantilist approach of seeking the necessary leverage to open the services

¹ See Keidanren Proposal (2013).

² For the relationship between disciplines on goods and services, see Reference Materials 1 (Comparison of Goods and Services Disciplines).

³ See Nakatomi (2013c).

market in BRICS countries. It is often pointed out that the severity of this problem differs in market access vis-à-vis rules. The argument goes that the extension of benefits to non-members based on MFN had a significant impact on firm-level competition in the area of market access (through e.g. tariffs), but only a minor and indirect effect in the area of rules,⁴ an argument that could also be made with regard to services negotiations.⁵

Lastly, and closely related to the prior points, is the recent deployment of FTAs as a means of services liberalisation and rulemaking – culminating in the creation of TISA.

THE IMPORTANCE OF TISA

Recognising that progress was not being made using traditional negotiating methods, the 2011 WTO Ministerial Conference acknowledged the possibility of advancing negotiations in different areas at different speeds in order to overcome the stagnation of the Doha Development Agenda (DDA),⁶ and the idea of a Trade in Services Agreement (TISA) was introduced, with the US as its driving force. TISA is an initiative for services liberalisation and rulemaking being discussed by 23 members,⁷ amongst a coalition called ‘Really Good Friends of Services’ (RGF). Preliminary discussions between participating members commenced in 2012, and on 28 June 2013, the RGF issued a joint declaration to the effect that discussions concerning TISA had advanced, and that the participating members had now moved to the stage of full-fledged negotiations. It is necessary to bear in mind the fact that TISA is not an initiative involving all the WTO members, but a plurilateral initiative outside the WTO framework. As expected, TISA was viewed critically by non-participating WTO members, especially the developing countries, because it was not a WTO initiative.

A European Commission memo⁸ has provided an outline of the structure of TISA, and the main features are expected to be comprehensive in scope and no modes will be excluded at the onset;⁹ like the DDA negotiations, all sectors can potentially be covered by the negotiations. Each participating nation, however, will decide on the sectors in which, and the extent to which, services can be provided by foreign businesses. Initially, the agreement will only be binding on participating nations. The EU has ensured that the structure of the agreement allows a path towards its future multilateralisation by adding an accession clause for interested WTO members. Naturally, the inclusion of developing countries (in particular China and other major economies) is an essential condition for the TISA to become a meaningful global framework in the future, and

⁴ See Van Grassek and Sauvé (2006), pp. 857-8.

⁵ See Elsig (2010). With regard to MFN, Elsig claims that we should not adopt a dichotomous perspective, but for each field focus on the benefits of cooperation and the incentives for free riding, which differ for the opening of markets and the formulation of rules. Elsig indicates the importance of creating incentives for participation by non-participating nations.

⁶ The agreements concerning trade facilitation, LDC, and food security realised at the 2013 Bali WTO Ministerial Conference can be understood as an extension of this accord at the 2011 Ministerial Conference.

⁷ Countries and regions participating in TISA negotiations (23 countries and regions (49 countries and regions if the individual countries of the EU are included)): Japan, the US, the EU, Canada, Australia, South Korea, Hong Kong, Taiwan, Pakistan, New Zealand, Israel, Turkey, Mexico, Chile, Colombia, Peru, Costa Rica, Panama, Paraguay, Norway, Switzerland, Iceland, and Liechtenstein.

⁸ See European Commission (2013).

⁹ For detailed information regarding the purpose of the TISA, see Hufbauer, et al. (2012) and the testimony of Samuel A. Di Piazza, Jr. and Peter Allgeier (both of the Coalition of Services Industries (CSI)) to the Inter-agency Trade Policy Staff Committee (Di Piazza, Jr. and Allgeier (2013)).

thus, the further expansion of the membership of the agreement will be essential.¹⁰ To incorporate TISA in the WTO system, the EU also stresses the importance of the obligations specified by the agreement being the same type as those specified by GATS.

Although it has been agreed that national treatment will in principle be applied across the board, in order to prevent free riding, automatic multilateralisation based on the MFN principle will be temporarily suspended unless a critical mass of WTO members joins the agreement.¹¹

THE STRUCTURAL ISSUES OF TISA

It is essential to ensure that TISA becomes a truly global services trade framework. Its legal form – in particular whether or not it is an FTA – took on significant importance. Marchetti and Roy (2013ab) considered that there were four possibilities in terms of the legal structure of TISA:

- 1) A GATS Protocol approach, on an MFN basis, like the previous agreements on Financial Services and Basic Telecommunications.
- 2) A method in which the members participating in the negotiations would voluntarily improve their commitments on an MFN basis.
- 3) A plurilateral agreement within the WTO, on the basis of consensus among all members.
- 4) A plurilateral agreement outside the WTO, or in other words a services FTA based on Article V of GATS.

Marchetti and Roy did not discuss which of the above options should be chosen, but realistically, the discussions could only proceed on options 1 or 4.¹² Option 2 had little chance of realisation because there is no guarantee that all participants would improve their commitments (also referred to as a ‘prisoner’s dilemma’).¹³ In the case of option 3, the agreement would be subject to consensus among WTO members, which was unrealistic.

TISA was proposed by the US as an FTA based on GATS Article V, and the negotiations are now taking place as such. It is understandable that TISA is being pursued as an FTA – the negotiation strategy is to encourage participation as a stick, rather than a carrot. There are suggestions that the strategy might be working, as China is considering participating in TISA.

¹⁰ Critical mass was not discussed as a numerical benchmark in the cases of the agreements on Financial Services and Basic Telecommunications either. On this point these agreements differ from the ITA, for which the condition for critical mass was the participation of nations representing approximately 90% of trade volume. If the TISA is constituted as an FTA, then the concept of critical mass will be irrelevant, but if it is not constituted as an FTA, sufficient coverage by participating nations will be an important element in the formation of the agreement. Low (2011) takes critical mass to refer to the intention among participating nations to reach an agreement, irrespective of the existence of non-participating free riders.

¹¹ European Commission (2013) is unclear as to what form this suspension of multilateralisation through MFN will take, and which conditions should be fulfilled for multilateralisation through MFN.

¹² See Reference Materials 3: Perspectives on the Legal Form of the TISA. Here, the author provides an evaluation of the options discussed above.

¹³ Marchetti and Roy (2013a).

The FTA approach based on GATS Article V, however, also involves considerable risks.¹⁴ There is a risk of an arbitrary interpretation of requirements such as ‘substantial sectoral coverage’ under GATS Article V – surprisingly, there has been almost no discussion concerning the interpretation of these exceptions to the MFN principle. Taking into consideration its importance, a careful and sufficiently detailed discussion of the requirements for these exceptions is essential.¹⁵ In the absence of such, there is a strong possibility that the article will no longer act as a check on future discriminatory treatment amongst WTO members.

Even assuming that new non-participating members would join the TISA framework, reaching critical mass would require a long period of time.¹⁶ Since FTAs are fundamentally structured around discrimination between participants and non-participants, they are not conducive to being integral to global rulemaking. The business community has a preference for rules on a global level, given the importance of developing countries in the world economy and the market in services. The fact that TISA is an FTA makes its path towards global rules a non-transparent process.

Another concern is related to economic welfare. The non-MFN approach may offer preferential treatment to some inefficient services industries, which is a significant issue.¹⁷ There are doubts as to the extent to which a non-MFN approach is actually feasible, given the horizontal nature of services regulations.¹⁸ In fact, in many cases services regulations are implemented domestically on an MFN basis. Also, many FTAs stipulate the sharing of benefits with its members on an MFN basis, that stipulate the sharing of benefits to other countries who have already concluded FTAs with the parties in question. It is no exaggeration to say that clauses that deny MFN treatment are being eroded and there is no rationality in introducing a discriminatory system.^{19,20} Japan, for example, does not withhold any of the services sectors from MFN treatment, and has made a principle out of sharing all its services liberalisation in future FTAs with its present FTA partners, meaning that it is applying MFN treatment at a high level.

¹⁴ See Bosworth (2014). Like the author, Bosworth expresses strong concern regarding the constitution of the TISA as an FTA.

¹⁵ See Materials 4: Legal Structure of Exceptions to MFN Treatment, concerning the legal structure of exceptions to MFN treatment in GATT and GATS. It will be clear to the reader that the GATS disciplines are particularly vague with regard to exceptions to MFN treatment, and that there has been insufficient discussion of their details.

¹⁶ Until then, the TISA would be a framework for the liberalisation of services among the RGF (centring on the developed nations). A scenario in which proceeding with the TISA as an FTA invites a backlash from developing nations, resulting in a suspension of global rulemaking, is another concern.

¹⁷ Miroudot et al. (2010).

¹⁸ In the case of market access, discriminatory application is possible (licences, etc.), and is sometimes necessary.

¹⁹ This argument is taken by supporters of the concept of the TISA as an FTA (Hufbauer et al. (2012)) as providing a rationale for the constitution of the TISA as an FTA. The argument goes that because regulations are after all normally implemented on an MFN basis, it makes no difference whether or not the TISA is an FTA.

Assuming that the benefits of the FTA for participants were multilateralised through MFN, opposition to the constitution of the TISA as an FTA would be eased, and the danger of GATS taking on a bipartite structure – surely a grave situation – would be reduced.

However, assuming that multilateralisation of benefits through MFN was possible, given the flexible character of the GATS Schedules of Commitments, it would be enough for countries to simply modify their Schedules of Commitments, and there would be no reason to adopt an FTA structure predicated on discrimination between participants and non-participants.

²⁰ As indicated by Miroudot et al. (2010), the issue of multilateralisation through MFN is an issue of political will, and in the case of services FTA also, the correct course of action is to move ahead with extending benefits of the FTA through MFN as a fundamental principle.

A GATS ANNEX MODEL

Since the GATS has produced no other significant outcomes on services, its annexes – the agreements on Financial Services and Basic Telecommunications – are still relevant today, and are trailblazing examples for future negotiations.

The GATS Annexes were indeed part of a ‘built-in agenda’, but other elements were eliminated from that agenda, or suffered severe setbacks (for example the work to harmonise non-preferential rules of origin).²¹ Instead, the rapid changes and globalisation of the economic environment, induced by the internet and the global financial architecture, were the main factors behind their conclusion. The countries involved (and their business communities) sought a systematic legal structure to facilitate these developments, similar to how the parties of the Information Technology Agreement (ITA) shared the recognition that free trade is a fundamental structure for the information and communication technology (ICT) sector.²² All major economies participated to create a global public good in a specific sector – a shared political will was a significant element in negotiating the GATS Annexes – rather than seeking reciprocity, or other forms of negotiation dynamics.

The agreements on Financial Services and Basic Telecommunications have several unique and distinguishing features. One such feature, worthy of special note, is the support and assistance of the related business communities in the major nations in realising the agreements on Financial Services and Basic Telecommunications, as in the case of the ITA, an initiative to eliminate tariffs in the ICT sector.²³

Another significant distinguishing feature of both agreements is the fact that their basis is the formation of critical mass by the major nations and extension of their benefits based on the MFN principle, which is also represented in the basic framework of the ITA. The cases of the agreements on Financial Services and Basic Telecommunications (and similarly the ITA) represent an approach in which all major economies participated to create a global public good in some specific sectors at a time (1997) when the adverse effect on competitiveness from the free ride problem did not attract a great deal of attention.

Yet another distinctive feature of the agreements on Financial Services and Basic Telecommunications is that these agreements adhered to sectoral characteristics. They added disciplines on issues that were not covered by the market access and national treatment disciplines in GATS, and significantly advanced the basic structure of GATS through sectoral negotiations. The evolution of a legal framework suited to the characteristics of specific sectors is an important outcome of both agreements, and such a framework had not yet been achieved by GATS.²⁴ A sectoral approach is able not only to expand market access and national treatment disciplines, but can

²¹ However, the fact that the negotiations were held after the expiry of fast track negotiating authority and that the US possessed residual negotiating authority are important points.

²² Negotiations towards the expansion of the products subject to the ITA commenced in 2012 and are ongoing, and continuous efforts are being made to formulate an agreement.

²³ In the case of the ITA, close cooperation between the business communities of Japan, the US, the EU and Canada (the Japan Electronic Industry Development Association (JEIDA), the ITI (Information Technology Industry Council), the European Association of Manufacturers of Business Machines and Information Technology (EUROBIT), and the Information Technology Association of Canada (ITAC)) provided a powerful impetus for the realisation of the agreement. See Nakatomi (2012a).

²⁴ For a comparison of goods and services disciplines, see Reference Materials 1: A Comparison of Goods and Services Disciplines. These materials make clear the significant progress in disciplines in the goods sectors, compared with services.

also dramatically increase the potential for the introduction of additional disciplines in response to the characteristics of specific sectors.²⁵

SECTORAL APPROACH IN TISA

Unfortunately, similar sectoral approaches on an MFN basis have not borne fruit in the services sector since the GATS Annex. Meanwhile, TISA is being pursued as a non-MFN FTA, although services disciplines are in most cases applied on an MFN basis within each jurisdiction. The issue of free riders is in many cases nothing more than a mere conceptual concern. The great value of TISA is its potential to enable global rulemaking in the future, but there will be a long period of numerous complications before the agreement becomes part of the GATS system.

Against this background, disaggregated agendas in each services sector (i.e. sector by sector, or issue by issue) represents extremely important and powerful tools for liberalising and establishing disciplines in the services sector.²⁶ TISA is an excellent platform for launching such initiatives. If a universal agreement, based on reaching critical mass and extending the benefits according to the MFN principle, following the precedents of the agreements on Financial Services and Basic Telecommunications, can be reached in individual sectors, there is the potential to advance global services liberalisation and rulemaking in sectors of particular importance from the TISA framework.²⁷ Through adoption by all WTO members, sector agreements could become part of GATS, and *ipso facto* global agreements.

As the discussion above suggests, whether or not TISA takes the form of an FTA will have a powerful impact on the GATS system and its future developments. Hopefully, the issues will be discussed seriously in the future.²⁸ It is essential for TISA to not compete with mega-FTAs, and instead secure the participation of a larger number of countries and develop a negotiation framework that will lay the foundation for future GATS rules.

The potential of TISA represents a valuable opportunity – and presently, the only one available in services. As the critical mass approach cannot be pursued across all sectors within TISA as a whole, an approach in which critical mass is sought in a few, important sectors where it can be reached would be a practical and meaningful alternative. As the benefits of the agreement are shared with non-participating nations, the possibility of securing approval from the developing

²⁵ In the case of the ITA, in 1996 the EU stressed that not only tariff but non-tariff measures should form a part of the negotiations; it is possible that the majority of the associated issues were issues of services negotiations, centring on the telecommunications sector. See Nakatomi (2012a).

²⁶ Naturally, the existence or non-existence of NT and MA disciplines are also extremely important factors, but in a situation in which there is inadequate provision of horizontal disciplines in the services sector (e.g. disciplines related to domestic regulations based on Article VI (corresponding to TBT in goods) have not yet been established), it will be more efficient to conduct focused discussion of disciplines by limiting the scope to important sectors of concern.

²⁷ Because the inclusion of the major developing nations would form the basis for critical mass for sectoral proposals of this type, the mounting of initiatives to explain the benefits of the agreement to the developing nations and the presentation of frameworks that sufficiently address the concerns of the developing nations would be important factors.

²⁸ The idea of constituting the TISA as an FTA and applying the MFN principle conditionally (the concept is to multilateralise commitments if the participation of sufficient nations to constitute critical mass is obtained (Hufbauer et al. (2012))) puts the cart before the horse. The European Commission (2013) also indicates that multilateralisation of the agreement will be suspended until critical mass is reached, but is unclear on the legal constitution of the agreement (FTA, waiver, etc.) or its details (e.g. conditions for introduction of multilateralisation based on MFN).

country members and producing a global agreement would increase.²⁹ In addition, if several agreements were pursued in this form, a global solution would be formed within GATS, producing international standards – in both a substantive and a legal sense – creating powerful incentives to participate in the framework.

CONCRETE SECTORAL PROPOSALS

Such a sector-by-sector approach would create an atmosphere of working towards the ‘global public good’ similar to the agreements on Finance and Basic Telecommunication, and thus should be pursued more wholeheartedly.³⁰ It will be necessary to concretely examine each service sector under the progress of mega-FTAs and TISA in parallel. Past examples of success in sectoral agreements, and in particular the plurilaterals, provide a reference for future sectoral proposals. Although the details are sector specific, they include the elements detailed below.

- 1) Creation of clusters that closely match policy goals in the sector in question. It is no exaggeration to say that cluster design is essential and will decide the success or failure of sectoral proposals.³¹
- 2) Market access, national treatment and MFN disciplines are pillars of liberalisation in services and, therefore, are assumed to be central elements in sectoral agreements in the services field.
- 3) Identification of additional horizontal commitments allowed in GATS, other than market access and national treatment, responding to the characteristics of the sector.
- 4) Support measures to enable the realisation of the above, in particular capacity building and technical assistance for developing economies, as the participation of the major developing economies is essential for critical mass. To ease the burden and avoid a sense of caution, it may also be necessary to consider granting exemptions on disputes.
- 5) Adequate verification and explanation of the economic benefits of participation will be essential. Cooperation with academia will be important in addition to the involvement of industry and government.³²
- 6) An examination of each individual sector by the industry, the government and trade experts is essential, thereafter concrete sectoral proposals should be made.

It would be essential to respond prudently, for example by selecting sectors in which there will be little conflict of interest with partner countries (e.g. setting standards for scale) or proposing frameworks that bring benefits to partner countries, (e.g. rationalisation of domestic industry, support for supply chains).

²⁹ See Warwick Commission (2007).

³⁰ See Nakatomi (2012a, 2013a) and Nakatomi (2013c).

³¹ See OECD (2000).

³² The further development of indicators of openness in services fields, such as the Services Trade Restrictiveness Index (STRI) by the OECD will be important in providing proof of the economic benefits of liberalisation of services.

A diverse range of internal regulations in numerous countries characterises the retail and distribution sector, cultural services and cross-border data flows. These are sectors wrapped up in domestic regulations but at the same time they offer a variety of business opportunities, though their liberalisation may present difficulties.

It would also be necessary to examine the potential for clustering. If it was possible to cluster services that are integral and closely associated with the overseas expansion of manufacturing industry, or 884 and 885 under the United Nations Central Product Classification (CPC), this sector would contribute to the promotion of investment and the expansion of value chains in developing economies, making the explanation of economic benefits a relatively easy task. In addition, attempts should be made to include a portion of telecommunications (e.g. CPC 842 to 844), data services (CPC 84) and other business services, e.g., management consulting services (CPC 865, 866), packaging services (CPC 876), and conference services (CPC 87909).

Given that most nations support the development of environmental protection and environmental industries, sectoral proposals concerning environmental services in cooperation with *inter alia* the APEC countries, represent another possibility. A possible clustering with CPC environmental services (9401-3) as the core therefore should be examined.

CONCLUSION

Focusing on plurilateral initiatives within the services sector, this paper has discussed the importance and the problems of TISA, the direction that it should move in, and the value of pursuing negotiations on a sectoral basis. In addition to being an important framework in terms of the international development of Japan's service industry, TISA is also important from the perspective of the provision of global rules within GATS. It is highly desirable that negotiations proceed on a sectoral basis within this framework, and that Japan offers its contributions. The author hopes that this paper will serve as a reference in advancing both TISA and sectoral negotiations.

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