TOWARD A REGIONAL AGREEMENT ON TRADE IN SERVICES:

A CRITICAL ASSESSMENT

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TOWARD A CONSENSUS ON FREE TRADE IN THE AMERICAS

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Toward a Regional Agreement on Trade in Services: Issues and Perspectives

Introduction

Trade in services no longer excites the minds of negotiators and policy decision-makers as it once did when it first appeared on the international agenda. At the end of 2002, fully sixteen years after the beginning of the Uruguay Round and almost eight years since the entry into force of the WTO, trade in services has become an integral part of the international trading regime, its activities being now covered by a multilateral general agreement as well as by a number of regional or sub-regional, whether plurilateral or bilateral, agreements. Attesting to that evolution, the issue at present in the FTAA negotiations is not *whether* to include or not

disciplines on trade in services: the issue is rather *how* to do it so as to reflect the realities of a sector responsible for over 50% of the world's GDP while providing for an attractive balance of rights and obligations for all countries involved.

The issue of how to include services in a future FTAA is not, however, as simple as might be presumed from a cursory look at the mosaic of existing agreements around the Americas and the world. In fact, the existence of various instruments that deal with services has in and of itself become an issue in the region, as different blocks view their own set of disciplines as preferable to anything else on the negotiating table. The classic example of this in the FTAA context is the Mercosul-NAFTA dichotomy. Much of the stalemate in the negotiations has to do with the differing conceptual and methodological approaches between the two blocks and the insistence of either side on the merits of its own disciplines. In that sense, a negotiation that is already "blessed" with enough technical complexities runs very quickly into political difficulties. Needless to say, the preference for one or the other paradigm reflects a host of reasons on either side, of the sort which do not render themselves easily to negotiating simplifications or compromises.

A successful negotiation has to be the result of technical creativity alongside political will. The two ingredients are indispensable and must feed on each other if an agreement in a matter as complex as trade in services, and in a region as *sui generis* as the Americas, is to be concluded. It would be an illusion to think that either ingredient could alone provide for a good agreement on services. It is widely known that there are a number of technical issues whose outcome in the FTAA could be seen as an improvement on existing agreements on services, including the WTO's own General Agreement on Trade in Services (GATS). In what follows, technicalities will be addressed, not as an end in itself, but as the possible means to facilitate dealing with real policy issues facing services markets and regulations around the hemisphere.

Hemispheric State of the Art in Services

Since the entry into force of NAFTA in 1994, the world's first free trade agreement to include provisions on the liberalization of trade in services, fourteen other agreements have been concluded in the Americas following in some measure that example and extending the scope

of trade to include activities in the traditionally-known tertiary sector. As such, all thirty-four countries participating in the FTAA negotiations are parties to at least one agreement on trade in services in the hemisphere while all are also members of the WTO and parties to the GATS.

The advent of free trade agreements including services in the hemisphere was concomitant with a considerable freeing of markets in the region – primarily as a result of diversified privatization and public concession processes. It would be, however, naïve to assume that the opening up of markets to trade and investment in services in the Americas had much to do with the agreements that have been concluded in the meantime. Most of the stimulus for opening up services sectors was self-induced, as countries increasingly viewed their competitiveness and integration with world markets to depend on access to world-class services. Trade agreements have for the most part locked-in levels of openness that resulted from autonomous liberalization, as opposed to actually forcing the pace of liberalization in those countries. That is a very important point since it can help in gauging the level of ambition that FTAA architects may want to favor, given past relevant experience.

The NAFTA

The NAFTA is the oldest agreement covering trade in services in the hemisphere. As early as August 1992, the governments of Canada, Mexico and the U.S. would announce the conclusion of negotiations, which, as in the case of NAFTA's predecessor, the U.S.-Canada FTA, included provisions on trade in services in a number of its chapters. Thus, Chapter XI deals with the issue of investment, Chapter XII with cross-border trade in services, Chapter XIII with telecommunications, Chapter XIV with financial services and Chapter XVI with the temporary entry of business persons. Other chapters of the agreement, notably those relating to standards, government procurement, intellectual property and competition policy, monopolies and state companies, also cover crucial aspects of services transactions in their provisions.

The provisions on services trade in NAFTA broke new ground in terms of structure and mechanics of liberalization. One of the most distinct characteristics of the NAFTA provisions is, for example, that the issue of commercial presence and/or investment in services is dealt

with alongside commercial presence and/or investment in goods: the Chapter on Investment (Chapter XI) deals with the matter without making a distinction between goods and services – something that has not yet been possible at the WTO.[1]

NAFTA permits reservations and exceptions relating to national treatment, m.f.n. treatment, local presence, performance requirements and senior management and boards of directors on a host of items (such as existing *and future* measures, quantitative restrictions, etc.) with respect to Chapter XI (Investment), Chapter XII (Cross-Border Trade in Services) and Chapter XIV (Financial Services). Countries can lodge reservations regarding specific sectors; all sectors have to be specified in a country's schedule in a method known as that of a "negative list approach". The agreement also sets out sectoral exclusions, as is the case with some activities in air transport, basic telecommunications and maritime transport. The movement of natural persons is limited to business persons by virtue of specific provisions in the agreement.

Mercosul: The Montevideo Protocol

In the case of Mercosul, services are covered by means of the Montevideo Protocol on Trade in Services, concluded in December 1997 as the result of negotiations conducted by the "*Ad Hoc* Group on Services", forum created by the Mercosul Council in December 1994. It should be noted, however, that discussions on issues relating to services in Mercosul had taken place since the entry into force of the Assuncion Treaty in 1991, by means of sectoral sub-groups created by the Treaty itself (financial, communications, transport). The novelty in the Montevideo Protocol was in bringing all services sectors together under one set of common disciplines of general and specific application whose main objective was to promote the intra-zone liberalization of these sectors – an objective which was not present in the case of the Assuncion Treaty sub-groups.

The Montevideo Protocol took as its starting point the rules and principles of the GATS Agreement – most notably, the definition of trade in services on the basis of four modes of

[1] Investment in the WTO is only covered in the GATS agreement, by virtue of the so-called "mode of supply 3" – commercial presence, and in the Trade-Related Investment Measures agreement (TRIMs) – a partial agreement on some investment measures that relates only to trade in goods.

supply, the scheduling of specific commitments on market access and national treatment, and the positive list approach to the listing of committed sectors and activities. By the time the negotiations had been concluded, the Protocol had innovated on a number of aspects of its multilateral mentor, providing for a framework for the negotiation of one of the key objectives of the Assuncion Treaty: the free movement of services, alongside goods and factors of production, among member countries.[2] Perhaps the strongest feature of the Montevideo Protocol is the commitment for the achievement of a full-fledged free trade area in services in Mercosul within ten years from its entry into force.

Other Agreements

In addition to NAFTA and Mercosul, countries all over the region have concluded agreements on trade in services. Thus, the Andean Community countries apply Decision 439 since June 1998 with a view to achieving intra-zone liberalization while Mexico has perhaps been the most active proponent of free trade agreements that include services among other matters.[3] Chile has an agreement with Canada and Central America (presently negotiating with the United States), the Dominican Republic has an agreement with Central America and CARICOM, and CARICOM itself has a Protocol devoted to Establishment, Services and Capital since 1997.

The FTAA: Commonalities and Differences

There is therefore a lot to go on, insofar as disciplines for trade in services are concerned. It could be said that the experience is still shallow and that the WTO itself continues to move up on the learning curve in the area of services. The fact is, however, that the FTAA negotiations are far from being conducted in a vacuum. There is plenty of technical information (albeit statistics continue to be a problem across countries), some relevant experience in the conclusion and implementation of free trade agreements and quite a bit of autonomous reform so as to allow countries in the hemisphere to put together consensual provisions on trade in services. In fact, there is also a good common ground that pervades all existing agreements

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[2] Article I of the Treaty of Assuncion of 26 March 1991.

and may do much to assist negotiators to move forward. The differences in agreements and negotiating positions and the way to attenuate them will, nevertheless, determine the fate of the FTAA in services.

The Common Ground

All existing agreements in the hemisphere have rules and principles based on the traditional notion of non-discrimination – as set out in the GATS and, even before that, in the GATT: most-favored-nation treatment and national treatment. All agreements also include some definition of market access in services, often on the basis of the provisions of Article XVI of the GATS. The application of these principles can be, however, quite differentiated across agreements. Both the Montevideo Protocol and the relevant provisions of the Andean Community tend to be more ambitious in their application of non-discrimination, committing member countries not to discriminate among themselves from the outset: in other words, neither agreement permits m.f.n. exemptions as was the case with the GATS and NAFTA.[4]

Another common element to all agreements in the hemisphere is the understanding that the principles of market access and national treatment needed to be accompanied by provisions on measures which are essentially of a domestic nature but may affect, all the same, international trade in services. All agreements recognize that measures taken by countries on the pursuit of national policy objectives are not *a priori* to be considered restrictions or violations, but that, depending on their application, they may become limitations on services trade. This recognition extends to the commitment to pursue further negotiations with a view to diminishing discretionary behavior when regulating or applying regulations.[5]

The principle of transparency is another common feature of all agreements in the hemisphere. In all cases it sets out the obligation to publish relevant measures affecting trade in services and to notify changes in the existing regulation. All agreements call for the establishment of contact points for the supply of information requested by interested parties. NAFTA goes

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[3] The G-3 (with Colombia and Venezuela), Bolivia, Chile, Costa Rica, Nicaragua and the North Triangle Group (with El Salvador, Guatemala and Honduras).

[4] Mercosul follows the GATS approach, permitting countries to enter non-conforming measures to market access and national treatment in their schedules of commitments. There are no exceptions permitted for m.f.n. treatment, all discrimination being thus eliminated at the entry into force of the agreement.

beyond Mercosul in that it gives the right to Member countries to comment on proposals for change in the regulation in any Member country.

Various other elements permeate the agreements in the hemisphere, most of them somehow inherited from the GATS. Provisions on domestic regulation, mutual recognition of licenses, professional certificates, quantitative restrictions, general and security exceptions, are very common throughout the region. Some important distinctions remain, however, with respect to some concepts. On professional services, for example, while the NAFTA sets out an obligation to eliminate nationality and/or residency requirements within a fixed time period, other agreements such as the Montevideo Protocol only call on governments to stimulate and accept mutual recognition agreements. A most important difference between the two most prominent agreements in the hemisphere relates to the issue of subsidies. As in the GATS, Mercosul countries committed themselves to elaborate disciplines on subsidies while the NAFTA is silent on any such commitment.

Bridging the Gap

It would be naïve to think that resolving technical imperfections apparent in the existing agreements covering trade in services, starting with the GATS itself, would somehow make an FTAA package or agreement on the subject more palatable to participating countries. Whether a measure is considered a restriction on market access, on national treatment or on both, or whether a common definition is feasible or not for all services activities across the hemisphere are important questions but not of the sort that will make or break the agreement.

To adopt a "correctional" mode when dealing with a possible FTAA package on services, as if it is relevant that there is a technically-correct agreement somewhere in the horizon, is useful but definitely not sufficient. Most of the issues on the negotiating table cannot be resolved only by "improving" on technicalities that could clarify the liberalizing intent of existing agreements. Resolving the issues requires a good understanding of where the balance is going to be between competing interests across countries, across sectors and across national

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[5] The "mother-principle" is Article VI of the GATS.

policy objectives (for example, the interest of engaging in domestic reform *versus* the interest of liberalizing trade).

Objectivity: Domestic Reform versus Trade Liberalization

One of the most important characteristics of the regulation affecting trade in services is the fact that a great deal of it is motivated by domestic concerns such as the preservation of quality levels in the supply of services or the protection of the consumer, the guarantee of access to services essential to the general well-being, the guarantee of access to information regarding specific services, and the preservation of civic and/or cultural values. Protection in the traditional economic sense is in and of itself becoming less common than it once used to be, as governments come to realize that competitiveness requires integration and partnerships and not protectionism and self-sufficiency.

As mentioned before, the international rules-based regime for services has understood that fact and acted on it. Starting with the GATS, all trade in services agreements in existence have recognized that a host of essentially domestic measures can affect international transactions in services and have attempted to discipline the recourse governments may have to them. Even measures which do not discriminate between national and foreign services or service providers have been included in the purview of these agreements, expanding considerably the scope of measures considered to affect trade in services.[6] By doing so, agreements have blurred the all-important distinction for governments between domestic reform and trade liberalization. That is not *a priori* a problem, except of course when there is the risk of one objective outstripping the other of its effectiveness.

Domestic reform is something that may take time, be undertaken in stages and require both de-regulation as well as re-regulation. All of those features of a reform process may not be in tune with the expediency with which trade liberalization may take place – autonomously or as a result, for example, of a free trade agreement. Reform requires taking action, monitoring developments and a constant re-evaluation of results. Depending on the rigidity of the

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[6] While Article VI of the GATS deals with domestic regulations that are not necessarily considered restrictions or violations, Article XVI of the GATS deals with domestic measures which do not discriminate between

mechanism adopted in a particular agreement, it may be difficult to re-visit measures already taken.

In the entire hemisphere, many countries have undergone significant domestic reforms of their services sectors (in telecommunications, for example). In many cases, the initial furor with which markets were opened to private and foreign participation has given way to the need for re-evaluating and perhaps re-regulating. Instruments such as an FTAA may need to permit some flexibility in the way countries commit themselves on such matters. The issue here is whether the regulation is good or bad, whether good governance is being achieved or by-passed – it is not about the merits of trade liberalization *per se*. Ways out of this dilemma include the possibility of reservations, flexibility on phasing-out periods or even exclusions of aspects of a particular sector.[7]

Predictability: Positive versus Negative

One of the main differences among existing trade in services agreements and provisions relates to the mechanism of liberalization – in other words, the approach adopted with respect to the freeing of markets itself. Given that all such agreements adhere to the possibility of member countries lodging reservations with respect to specific sectors or sub-sectors, the centerpiece of the issue has become the type of listing set out in a possible FTAA for committed sectors or sub-sectors – whether the lists or schedules where countries commit themselves on crucial matters such as market access and national treatment should be *positive* or *negative* in nature.

In a positive list approach, countries include only sectors and sub-sectors where they actually are committing to bind, at least partially, an existing situation. Whatever is not included in the list is free from any liberalization commitment. The opposite is true for the negative list approach: only what countries include in their lists is free from the liberalization provisions of a particular agreement. Thus, if a country includes the financial services sector in a positive

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national and foreign services and services suppliers but which are deemed to be restrictions on market access – one of the three most important operative principles of the Agreement as a whole.

[7] As NAFTA has done, for example, with basic telecommunications.

list, that country will be committing that sector in terms of the liberalization principles of the agreement in question: whatever is included *is indeed* subjected to the liberalization process. Conversely, if a country includes the telecommunications sector in a negative list, that country will be freeing that sector from liberalization commitments: whatever is included *is not* subjected to the liberalization process.

In the FTAA, positions are polarized between NAFTA and Mercosul countries since the former favor a negative list approach while the latter favor exactly the opposite. The issue may seem to be of no consequence, merely an "optical" illusion of sorts. However, given the variable levels of regulatory capacity across countries in the hemisphere and the fact that many of them have not yet regulated "adequately" their services sectors, or are in the process of doing so pursuant to reform efforts, it is likely to be difficult for many countries to accept binding existing national situations that are clearly incomplete, insufficient or plainly inexistent in schedules of a trade agreement. For governments that may seem equivalent to giving up the prerogative to regulate one's own economy in accordance with one's own national policy objectives, in effect transferring it to the disciplines of an agreement whose objective is not equally multi-fold.

It should be noted, however, that whether the lists are positive or negative may be much less important than whether the agreement in question has overall deadlines or partial deadlines for specific phasing-out procedures or the attainment of agreed goals, aims or objectives. In addition, all agreements covering trade in services may benefit from greater clarity in the manner commitments are described in country schedules, lists or annexes. Whether committing through a positive or a negative list, countries in all agreements have to enter (describe) the limitations or restrictions that are applicable to committed sectors or sub-sectors. It is widely known that these entries could undergo considerable improvement. The clearer the commitments entered, the more transparent becomes the trade agreement, the more attractive to real world investors, services suppliers, governments and the business community at large, the more predictable becomes the instrument as a whole.

Clarity: Services versus Investment

Once again, the issue pits NAFTA countries against Mercosul countries. Once again, the issue emanates from different approaches adopted in each of the two relevant sets of provisions – namely, the fact that in the NAFTA investment in services is dealt with alongside investment in goods in a separate chapter fully devoted to investment *per se*, while in Mercosul the Montevideo Protocol adopts the GATS approach of subsuming investment in services under one of the four modes of supply defined in the agreement: namely, mode 3, that of commercial presence. In essence, the Montevideo Protocol manages to keep all services transactions and forms of commercialization under one set of common disciplines while NAFTA separates investment in services from other matters relating to services trade.

There is no question that in the real world investment and trade in services go hand in hand. It is not clear, however, whether in the world of trade and integration agreements there is an overriding reason to collapse or separate provisions on the two matters. NAFTA and Mercosul seem to have staked out tactical positions on the issue, following their natural instinct to preserve their approaches to negotiating mechanisms. Ultimately, the choice between one or the other alternative will hinge on the appreciation each country or block will make on the effect that choice could have on two competing objectives: that of providing for a friendly environment for foreign investment *versus* that of preserving a certain capacity to intervene and control the nature of incoming investment in accordance with national objectives. Even though the latter objective has been much less common than in the past, the fact remains that in certain crucial sectors governments may deem necessary to maintain some leverage in the matter of investment. The case of telecommunications comes to mind in that context, as countries are increasingly finding out that global conditions in the industry alongside first and sometimes second-generation liberalization through privatization, public concessions and the like, may require more caution in the future.

The issue is very delicate. No country in its right policy mind-set can afford to scare away world-class foreign investment, especially in services sectors that can make an enormous difference in the global competitiveness race. If blocking the separation of investment in services from trade in services is perceived as obstructionist, countries may have to think twice before doing it. After all, one of the purported benefits of concluding trade agreements is precisely to get the image across to investors and other economic operators of a discipline- and predictability-friendly country, ready to welcome foreign interests that may contribute to national development.

Tactics should not be underestimated, however. If conceding on the separation of investment and trade in services is perceived to make more difficult the achievement of an overall balanced package of results across all negotiating items, that will be the end of that concession. If, for example, conceding in this matter for Mercosul makes it easier for NAFTA countries to avoid committing on agricultural liberalization, no deal will be had here. It may just as well be that this issue makes more of a difference at the systemic level of the FTAA deliberations as opposed to within the self-contained universe of the services-related negotiations. At the end of the day, from the perspective of a good trade agreement, what matters most is clarity of purpose and application.

Autonomy: Cooperation versus Market Access

Services activities could well be characterized as "regulation-intensive". As mentioned before, regulations on services span the full gamut of possibilities, from economic measures to measures relating to consumer protection, national security or cultural values. Regulators have therefore traditionally had a prominent role in services in most countries, drawing regulatory boundaries around the myriad of activities that together account for the sector.

It should not be advisable that trade agreements run roughshod over regulations, regulators and regulatory agencies. As a matter of fact, regulators and their agencies can be especially instrumental in making things work in free trade agreements and that for a simple reason: liberalization of some services simply cannot take place without a certain "paving-of-the-way" process that only regulators can achieve across countries. Paving the way in this context can take many forms but they all amount to regulatory cooperation of some sort. Key among those forms are the processes known as harmonization and mutual recognition.

The GATS, NAFTA and Mercosul, alongside other agreements in the hemisphere, acknowledge implicitly or explicitly the value of cooperation in regulatory matters. GATS invented, at the multilateral level, the notion of stimulating governments to mutually recognize their regulatory regimes and, whenever possible, to harmonize them. There could be no better way to advance the cause of free trade in services than to permit and even stimulate countries to move forward in regulatory cooperation. The fact is that national

regulatory regimes are complex and different across countries and that efforts aimed directly at acceding a market may be frustrated in the absence of cooperation efforts. Acceding a market such as insurance across borders, for example, may be made much simpler through harmonization or mutual recognition negotiations than it would be the case in a market access bargain which eliminated a few measures but did not manage to change a particular host country's regulatory approach so as to ensure effective negotiated benefits.

The world has been accumulating considerable experience on de-regulating, regulating and re-regulating. Sectors such as telecommunications, financial services, aviation and professional services have had to adapt and re-adapt repeatedly to changing national and international conditions. As an objective, liberalization has with time become less important internationally than regulatory supervision. Good governance seems to be more urgent than additional bouts of market opening. There seems to be no need or trend to backlash from liberalization but there is no evidence either that freeing markets continues to take priority over avoiding systemic risk or revamping regulatory regimes.

At a time like this, it may not be unlikely that FTAA countries favor greater focus on regulatory cooperation over the market access objectives of the negotiations. Past experience with harmonization and mutual recognition agreements may be relevant here, as may be the negotiations on Article VI (domestic regulation) of the GATS and the development of model instruments such as the provisional agreement on accounting, also at the WTO.

Realism: General versus Sectoral

An issue that has not yet been adequately dealt with in the FTAA negotiations on services relates to the inclusion in an agreement of disciplines of a sectoral nature. It is widely known that good candidates for specific provisions are always the financial, telecommunications and transport sectors. These have been sectors usually seen as complex and important enough to warrant special attention. The issues surrounding this question should, however, be similar to those addressed in a pioneering fashion during the Uruguay Round when the GATS Agreement was concluded: whether there is any reason to replace general disciplines that apply to all sectors with sectoral disciplines which apply only to specific sectors; or, whether

sectoral provisions should only clarify the application of general provisions and thus avoid ambiguity in the application of what could become competing sets of operative disciplines.

The history of creating specific provisions or disciplines that detract from general rules and principles in the multilateral trading system has not been successful from a liberalizing standpoint. The Multi-Fiber Agreement (MFA), for example, managed to get textiles and clothing fully outside the scope of the GATT Agreement and, effectively, to create the antithesis of GATT: an agreement based on strict bilateral reciprocity, discrimination and quantitative restrictions. In services, there may always be the risk of a similar plight for delicate sectors where the liberalization drive is much lesser than other policy objectives.[8] Where such a "solution" is the result of a consensus, there may not be much damage inflicted on the system as a whole; where it is the result of power politics and the preservation of the interest of a country or a few countries, the overall systemic effect can be nefarious.

There are a few problems also if the interest in having sectoral provisions is to create liberalization disciplines which go further than the general liberalization disciplines of a particular agreement. Having a different set of operative provisions on market access or national treatment, for example, may do away with the possibility of reaching an acceptable balance across sectors at the end of the negotiations. Assuming that the wider the scope of a particular agreement the greater is the chance that meaningful trade-offs be found among participating countries, the basic interest might be to keep as many sectors as possible in the same negotiating context. In principle, focusing on further liberalizing a sector such as financial services, for example, might not be interesting to all countries: those not interested might be put at a disadvantage since they may need to make concessions without the guarantee of comparable concessions elsewhere in the agreement; a trade-off that is limited to the confines of a particular sector itself is not interesting to countries that hardly have an export interest in that sector – as is clearly the case in financial services for many countries in the FTAA.

Admittedly, certain services sectors may warrant some special attention but not necessarily of the sort that achieves either an exclusion from the scope of the agreement or, alternatively, a replacement from general obligations. Experience has shown that sectoral provisions can be

useful in clarifying and adapting features of a particular sector to the overall objectives of a particular agreement. Financial services clearly comes to mind in that context as it is a sector like no other in terms of its relationship to the economic system as a whole and of the consequent system risks associated with unfettered competition. Telecommunications is another candidate, in this case for technical reasons.

In financial services, the balance between further opening and the need to exert systemic caution should continue to be crucial in the FTAA (as elsewhere as well). Now that the sector has been effectively included in the multilateral and regional trading system and that the issue is no longer whether including it would make things overly complex, thought should be given as to how to strike that balance in the face of new and renewed conditions in the world financial markets. During the Uruguay Round, participating countries avoided having to negotiate and reach consensus on prudential measures, choosing instead to permit countries to exert their own discretion when it came to those matters. NAFTA went further, still coming short of a common agreement on prudential measures, but moving forward on matters such as transitional periods, safeguards, individual and aggregate market share caps while clearly providing for increasing market access levels. Perhaps in financial services, more than anywhere else, starting from regulatory cooperation and evolving through harmonization or mutual recognition efforts might be the best means to aim at fluid but safe international markets.

Creativity: Approaches versus Targets

As mentioned before, liberalization mechanisms may be less important than actual deadlines in the FTAA negotiations. In other words, it may be more important to know by when a country or a group of countries is willing to commit to opening up its market or granting treatment no less favorable than that accorded to national services and service providers, than whether schedules of commitments follow a positive or a negative list approach. It is difficult to tell at this particular juncture in the negotiations whether there could be consensus on setting down specific deadlines or targets. Clearly, much will depend on the content of possible specific targets. Admittedly, there might be a greater chance of reaching consensus

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[8] Two cases in point: maritime transport services for the United States and audiovisual services for Canada or the

on partial targets than on overly ambitious targets. For example, agreeing to review the economic needs tests, so common in a number of sectors, for a particular sector during a certain time-period might be more palatable than choosing to provide for full national treatment across a group of sectors within a certain deadline.

An alternative that actually might go hand-in-hand with the establishment of negotiating targets is the formulation of negotiating approaches to specific issues, sectors or regulations. As services sectors are regulation-driven and countries often differ in the manner in which they regulate their services markets, it might make good sense to stimulate FTAA participants to reach side agreements which, while not replacing the operative part of the overall package of results, may be flexible (not mandatory to all participants, for example) but conducive to agreed common objectives.

Harmonization and mutual recognition agreements of the sort usually associated with professional services could fit this category but there may be more that can be done as demonstrated by the telecommunications reference paper negotiated in the aftermath of the Uruguay Round, in the extended basic telecommunications negotiations. Identifying specific issues that may have a strong bearing on the question of liberalization and reform in the services sector and provide the means to address them without threatening the main objectives of a future FTAA agreement on services trade may facilitate, and not complicate, the achievement of overall consensus. Negotiating on approaches may make possible to reconcile the overall interest in trade liberalization, which is the principal objective of any future agreement, with the need to be realistic about market conditions and systemic issues.

Conclusion

To negotiate on services trade is no longer a novelty and should not scare countries away from the negotiating table. In addition to being the object of intense regulatory purview, services activities have a crucial relationship to the rest of a country's economy, contributing directly to its competitiveness and integration with the rest of the world. The FTAA is a great opportunity for services. It can represent a meaningful support for reform around the

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European Union.

hemisphere, in particular if it succeeds in reconciling liberalization objectives with equally legitimate regulatory aims of the sectors and the countries involved in the negotiations. It should also be kept in mind that the success of the FTAA in services will also hinge on whether it can become a reliable vehicle not only for the integration of the services economies of the Americas but also for the integration of the region into the world services economy as a whole.

LINDA SCHMID: Thank you very much for having me here, today. I am with the Coalition of Service Industries and I am going to approach this from a private sector perspective and having recently returned from Quito from the Business Forum of the Americas.
As many of you know, the ministerial concluded with the eruption of a volcano, the Reventador volcano, and we are hoping that that does not foreshadow the future volatility of the FTAA negotiations.

What I wanted to look at was, really, three issues that we are dealing with in the FTAA and also in the multilateral negotiations. They are those issues of concern to negotiators, the issues or the charges that trade opponents have put forth having to do with services and, also, regulatory reform, or the importance of efficient regulation. And I think some of my remarks will reflect what Mario has said.

First, on the issues that face negotiators. Now, we know some talk of this very technical issue of the positive or negative list approach. It is U.S. industry's position that it should be a negative list approach. And, principally, because we believe that with the negative list approach, where you are only listing your exceptions, you leave very little to the imagination, and everything is covered except what is excepted. And in that case we will end up with a much more comprehensive agreement.

At the same time, this avoids some of the classification issues of new services. So that could be of concern. But having read Mario's paper, I recognize that the precedent of other agreements will have a strong bearing on how this issue is decided.

Also, with respect to whether establishment is dealt with in the investment chapter or whether it is dealt with in the services chapter, we prefer, industry prefers that it is dealt with in the investment chapter so that there are no gaps between goods and services, so that the chapter is comprehensive. And we also recognize that, in this case, other agreements will set a precedent on how this is determined.

One thing of note is that the ministers said both of these issues have to be decided by December 15th of this year. And we will see how that turns out.

Now, with respect to transparency, this is a very high priority for service industries. Now, if you look at the services chapter, there is a very limited transparency provision requiring governments to publish measures with a caveat for feasibility. Our interpretation is that this provision is very weak and that it would have to be augmented with stronger domestic regulation requirements. Because most services barriers are found in domestic regulations, and these domestic regulations are many times opaque and ad hoc, this is where much work has to be done. At the same time, we recognize that reforming domestic regulation really cuts very close to the bone of sovereignty. So what FTAA negotiators come out with will have to be balanced, so that it sufficiently disciplines regulations so that they are effective without eliminating or diluting domestic regulations developed to achieve public policy objectives.

Ideally, we are hoping that the FTAA would include cross-cutting domestic regulation for all sectors and then, in particular sectors, for example, in insurance, there would be supplementary disciplines.

This raises the question, well, you don't want different disciplines in the FTAA that you end up with in the WTO. So we would hope that there would be some consistency between these two things. But with respect to insurance, for example, what we would be looking for is something along the lines of regulatory best practices that address solvency and prudential issues, regulation of monopolies, and that you have disciplines to ensure the independence of regulatory authorities.

Now, this is somewhat consistent with the Telecom reference paper. So this is what we are looking for there.

Now, another issue for the negotiators is subsidies and safeguards. The previous panel, I think, demonstrates that for industry we don't want any disciplines on safeguards or subsidies. So I will just skip that.

With respect to trade opponents, we are hearing a lot of verbal criticisms of services negotiations in general. What we are hearing, and I remember hearing this in Ecuador, is there is a fear that services liberalization absolutely means privatization of governmental services. There is a fear that there will be an expectation that services liberalization will eliminate essential services to the poor and that they will raise the cost of those services. There is also a fear that services liberalization will eviscerate domestic regulations. And I think this is a task for trade ministers. I think trade ministers will have to communicate how the negotiations can be carried out so that there is an articulation of how new market entrants would come in and what the limitations of those new entrants would be.

The strength of services negotiations is that there is a great degree of flexibility. Governments have a lot of room to carve out how they want foreign service operators to function in their market. So I think it is incumbent upon trade ministers to communicate this to trade opponents who think that what we are trying to do in the negotiations is privatize all water supply, for example.

These criticisms are getting much more press coverage. For us in the U.S. it is problematic because not only is it coming from labor, it is coming from the environment. State representatives are starting to echo these same criticisms. So it is really incumbent on trade ministers and the U.S. Government to do some educating on this aspect of it.

I think, finally, I would conclude with the importance of effective regulation. In Quito ministers agreed on a cooperation program, and I think that the cooperation program is designed to assist countries in the negotiations and implementation of those negotiations, and then a very general effort to achieve the benefits from the negotiations. And I think here, if we have an opportunity to specify where this trade capacity assistance should go, it should go to ensuring that different countries have capability of designing and implementing effective prudential regulation, that these regulations ensure that there are not anticompetitive practices. And that not

only that institutionally they are capable of doing this but, also, that they have the people who are trained to do this.

This might be a real issue for some of the smaller economies. Some small economies, for example, have already put together regional regulatory authorities because they realize that they don't have the national capacity to deal with, let's say, telecommunications regulations. So, for example, in the Eastern Caribbean there is a regional authority.

So I think, in concluding, these are the issues at play in the negotiations, in the public debate, and, finally, how ministers will address regulatory reform after the negotiations are concluded.

One last point. In the ministerial declaration they talk a great deal about the western hemisphere cooperation program. But there is no explanation of how it will be financed. So that question must be dealt with.

SHERMAN ROBINSON: I would like to raise a number of issues. I will draw on the results of a large amount of work analyzing the FTAA from a variety of different perspectives. Some of it is joint work between the International Food Policy Research Institute (IFPRI), where I work, and the Economic Research Service (ERS) at the U.S. Department of Agriculture, and some other places.

The team at IFPRI includes: Eugenio Diaz-Bonilla, who leads the team working on global trade issues, Lucio Reca, Xinshen Diao, and Karen Thierfelder. We have collaborated a lot with Mary Burfisher and others at the ERS.

The proposed FTAA is really, part of a trend in Latin America. There has been a rapid growth in the number of subregional trade pacts in the region, which is part of a worldwide phenomenon. Alongside global negotiations, there has been a proliferation of regional trade agreements (RTAs).

An alternative to an RTA is a "hub and spoke" agreements, where one country does pairwise deals with a number of countries, becoming the hub. This hub-and-spoke approach looked like it might be a U.S. strategy after NAFTA, but then the Clinton administration was not able to negotiate anything in trade after the Uruguay Round, so it did not happen. But the U.S. has announced that it is seeking to make agreements with individual countries, and is negotiating agreements with Singapore and Chile. It certainly now seems to be part of the U.S. strategy under the Bush Administration.

Based on a lot of research, I would argue that a hub-and-spoke arrangement is a bad idea for the "spoke" countries. It would be a great pity if Latin America allowed itself to be Balkanized by a series of pairwise agreements with the U.S. There is an enormous incentive for the countries in the region, and for the region as a whole, to negotiate as a group. The gains are larger, no one is left out, and a group can negotiate on more even terms with the U.S. Research also indicates that it important to have the negotiations be as wide as possible. It is in the interest of the participants to include agriculture in a wider negotiation, and also not to try to do agriculture separately.

We also see, as Carla Hills and others have pointed out, enormous potential for dynamic gains from expanded trade among developing countries in the region. There are links between trade expansion and total factor productivity growth and employment growth. There are certainly gains to be achieved from successful negotiations.

But also in Latin America the countries vary widely in initial conditions. Led by Eugenio Diaz-Bonilla, we have done work looking across the world at food insecure countries; countries in which food security is a major issue. At least ten countries in Latin America that are very poor, so poor that basic food security issues dominate their policy debate.

In this environment, an approach to the FTAA negotiations assuming that "one size fits all" is probably a mistake. I would tend to agree with Alejandro Foxley that seeking an agreement that only achieves a "least common denominator" result would be a bad mistake, missing an opportunity for making real progress.

I also fully agree with the arguments made earlier about transparency. A major issue in the Uruguay Round was recognition of the need to develop standard measures of the size and nature of domestic agricultural programs. After much discussion, much of it technical, the OECD countries agreed to produce measures of "producer subsidy equivalents" and "consumer subsidy equivalents" (later renamed "producer support estimates" and "consumer support estimates").

These measures are now being assembled by the OECD, but only for a narrow range of countries.

This kind of data on domestic agricultural support (and tax) programs needs to be developed for a wider range of countries, particularly developing countries. Advancing the current WTO Round negotiations in agriculture, including market access issues, will require that the negotiators know about the size and impact of government programs supporting and taxing agriculture, both domestic policies and border policies.

Existing research indicates that a Free Trade Area of the Americas would be net trade creating. It would be a good thing for the region, with gains for all participants. It would also be net trade creating for agriculture, alone. With an FTAA, trade expansion within the region would greatly exceed any diversion of trade away from nonmember countries.

Also, studies indicate that participants benefit despite erosion of preferences for some of the countries under existing subregional trade agreements. For example, does Mexico want to have a FTAA, since it already has NAFTA? Why should Mexico let anybody else play in this patch? The answer from various studies is that Mexico would gain further from a wider FTAA agreement.

As Alejandro Foxley pointed out, however, macro issues are as important as trade issues. It is very important for the countries in Latin America to achieve and maintain macro stability. Swings in real exchange rates among the countries in this region arising from macro crises have been enormous. They have a much larger impact on domestic prices of tradable goods than any of the kind of numbers we are talking about arising from tariff reduction or removal of non-tariff trade barriers. A macro crisis wipes out or completely dominates the impact of any liberalization of tariffs or trade barriers.

Regarding the objectives of a free trade agreement in agriculture, I think the previous speaker gave you a pretty good list and talked about some of them. The argument is to progressively eliminate tariffs. Basically, all forms of protection are on the agenda, at least in the proposals tabled so far. For example, SPS issues are very important in agriculture, and it is important to ensure that SPS measures are not applied arbitrarily or as hidden protection. Achieving science based transparency as part of a rules based system is a major issue for Latin America.

Another important issue is eliminating agricultural export subsidies in the hemisphere. The U.S. position in both FTAA and the WTO negotiations is that agricultural export subsidies should be eliminated. However, the U.S. is less clear on the issue of market access for

agricultural goods and is unwilling to discuss domestic agricultural programs as part of the FTAA negotiations.

These issues are really left over from the Uruguay Round. The issue is how to bring other trade distorting practices in agriculture, including domestic support programs, under greater discipline. There is a trade-off between the WTO negotiations and the FTAA negotiations on these issues.

One argument is to leave agriculture out of the FTAA negotiations, and leave it to the WTO Round. Globally, agricultural policies raise many politically messy and complicated issues. In this view, discussing domestic agricultural policies under the FTAA is difficult for the U.S., so let's just leave it out.

The Brazil counterproposal is to argue that if agricultural access is not going to be addressed in the FTAA, then we should delay the FTAA until after the WTO Round, which will address agriculture. After that, we can return to an FTAA on nonagricultural trade.

Both views seriously impede the FTAA negotiations and are unfortunate. For example, agriculture was essentially left out of the U.S.-Canada free trade agreement (CUSTA) on the argument that those issues would be settled in the Uruguay Round. But the final Uruguay Round agreement left many unresolved issues, and they were not addressed in NAFTA. The result has been a series of agricultural trade disputes with Canada that have been irritants in U.S.-Canada relations, and have slowed progress toward deeper integration of the North American economies under NAFTA.

A number of studies argue that there are trade-offs between agricultural and nonagricultural market access. These trade-offs need to be part of the negotiation, so it is important that the negotiations be as broad as possible in order to build a coalition to support the final agreement.

The Uruguay Round was definitely a mixed success. One speaker at a conference years ago put it well. He said that the initial U.S. position was to eliminate all distorting agricultural policies by 20 percent a year for five years. As he put it, the French counteroffer was one percent a year for ten years. The final result was a mix, but far from the goal of eliminating distortions in international agricultural markets.

I would argue that the Uruguay Round did succeed in bringing more transparency into the system and in bringing domestic agricultural policies into the negotiations. I would strongly agree with the previous speaker that transparency has got to be part of the process, and domestic programs must be brought into the system of trade negotiations. We didn't get as far as we hoped under the Uruguay Round. Indeed, the position of the Cairns group today is to simply finish doing what the countries agreed in the Uruguay Round.

The data indicate that there is enormous diversity in Latin America with regard to the role of trade in agriculture. The share of the Western Hemisphere in the agricultural trade of

potential members in the FTAA varies enormously for both exports and imports. Looking at the big players, particularly the U.S. and Brazil, their dependence on FTAA markets is not very high. In addition, the FTAA negotiation is complicated by the fact that there are numerous existing trade agreements in the region. We counted 39 subregional pacts including NAFTA and Mercosur, and then there are a number of special preference arrangements such as GSP, the Caribbean Basin Initiative, European's Lome convention and its successor the Cotonou arrangements. Under these arrangements, a significant amount of Latin American agricultural exports to the U.S., and some to Europe, are already basically tariff free.

These existing preferential agreements have important implications for the developing countries. For example, if you have preferential access to the U.S. for, say, sugar, it is certainly not obvious that you want sugar liberalized in the U.S. You get restricted access to a market that gives you two or three times the world price, which is a pretty good deal.

The Europeans have been using this kind of argument to garner support from the developing countries in the WTO Round. They argue that developing countries get preferential access under Cotonou and the "Everything but Arms" initiative, but that if European markets are liberalized, this preferential access is worthless. Preferential access to a level playing field is not worth anything.

In order to make progress on regional and global trade liberalization, it is important to compensate the poor countries who are potential losers from liberalization, given the erosion of the value of their existing preferred access in selected commodities. Again, it is important to recognize the heterogeneity of the interests and needs of the various countries involved in the FTAA negotiations.

U.S. agricultural programs, especially the new farm bill, have engendered a great deal of criticism, especially from developing countries. However, recent studies indicate that the U.S. program may not be as distorting as we thought when farm bill was first passed. There is a certain amount of subsidy envy in many countries, and the U.S. certainly has incredibly well supported farmers.

One of my jobs when I worked for the Council of Economic Advisors was to brief Alan Blinder on agricultural support programs. Alan finally came out of one meeting with the USDA and said, "You know, Sherman, the problem is that the U.S. Department of Agriculture has never met a subsidy it didn't like." But the current support program is probably less distorting than the programs in place at the beginning of the Uruguay Round. However, the current situation is reminiscent of the late 1980s, with costly agricultural programs in both the EU and the U.S., and a real danger of a "subsidy war" breaking out. And the new farm bill has certainly caused the U.S. to lose the moral high ground in the negotiations.

Finally, just to sum up, we do see from various scenarios of the FTAA, that there would significant trade diversion, especially for the NAFTA countries. Not very large for the other countries. And if you assume that there are productivity links between trade expansion and the creation of the FTAA, then, then there is virtually no trade diversion—a rising tide lifts all boats.

From the perspective of the Latin American countries, it is important to look at more than agriculture. Their trade interests range all the way up the food chain and the value-added chain. A broad FTAA would lead to major trade increases in food manufacturing, a lot of specialty crops (e.g., fruits, vegetables, horticulture).

Indeed, the most rapid increase in agricultural exports in value terms from Latin America over the past decade is in all kinds of specialty crops. This trend is certainly consistent with what economic trade theory would predict. Developing countries should have a comparative advantage labor-intensive, high value exports moving up the value-added chain.

But the developed countries have tended to protect the processed good sectors. For example, in the European Union, under Cotonou, they let in your cocoa but they protect chocolate bars. Such restrictions are especially onerous for the Latin American countries. Finally, a lot of studies indicate that the FTAA is good for the member countries, but they also indicate that global liberalization is better still. In fact, in some of the studies focusing on Latin America, the FTAA region gains the most of any region from global liberalization, after an FTAA is implemented.

The results of empirical studies tend to support the view of "open regionalism" put forth by Carla Hills earlier. Fred Bergsten at the Institute for International Economics has argued over the years that regional trade agreements can be building blocks towards further global liberalization, and the empirical work supports him.