

Domestic Regulation and the GATS: Challenges for Developing Countries

I. Introduction

The GATS, in its preamble, explicitly recognizes the right of Members to regulate, and to introduce new regulation, on the supply of services within their territories in order to meet national policy objectives, and given the asymmetries existing with respect to the degree of development of services regulation, the particular need of developing countries to exercise this right. Furthermore, the process of progressive liberalization of trade in services, as provided by Article XIX.2, has to take place with due respect of national policy objectives; and the right of Members to regulate the supply of services in their territories has been further reaffirmed by the Negotiating Guidelines and Procedures adopted for the GATS 2000 negotiations, endorsed by the Doha Ministerial Declaration.¹ Nevertheless, the possible impact of the GATS on the regulatory autonomy of the nation state is perhaps one of the issues that have given rise to greater concern among, negotiators, national policy makers, and civil society institutions alike. The growing interest on domestic regulation in the context of services trade liberalization is also highlighted by the blossoming literature dealing with this topic.²

Existing concerns reflect the preoccupation surrounding the possible outcome of current negotiations on domestic regulation taking place in the Working Party on Domestic Regulation (WPDR) under GATS Article VI.4. This Article calls for negotiations to develop any necessary disciplines in the agreement with a view to ensuring that measures relating to qualification requirements and procedures, technical standards and licensing requirements do not constitute unnecessary barriers to trade in services. As provided by paragraph 7 of the Guidelines for the Negotiations, negotiations under Article VI:4 should conclude prior to the conclusion of negotiations on specific commitments under GATS Article XIX. Because trade rules are primarily designed to ensure markets access and not directly defined to promote efficiency or social welfare, there is growing preoccupation concerning the potential adoption of disciplines, highly intrusive in the domestic domain, requiring trade considerations to prevail over other legitimate policy objectives of domestic regulation. This could seriously constrain the capacity of states to effectively regulate services activities when pursuing such

¹ Guidelines and Procedures for the Negotiations on Trade in Services. Adopted by the Special Session of the Council for Trade in Services on 28 March, 2001. S/L/93 29 March 2001.

² On this issue, among other publications see: Krajweski, Marcus (2003). National Regulation and Trade Liberalization in Services: The Legal Impact of the General Agreement on Trade in Services (GATS) on National Regulatory Autonomy; Kluwer Law International, The Hague-London-New York; Mattoo Aaditya and Sauvè, Pierre, Editors (2004). Domestic Regulation and Services Trade liberalization, World Bank and Oxford University Press; Djordjevic M (2002) Domestic Regulation and Free Trade in Services - A Balancing Act. Legal issues on Economic Integration, vol 29, no 3; and Lang, Andrew (2004) The GATS and Regulatory Autonomy: A Case Study of Social regulation of the Water Industry, Journal of international Economic Law, 7(4). Scott Sinclair and Jim Grieshaber-Otto (2002) Facing the Facts: A guide to the GATS Debate, Canadian Centre for Policy Alternatives, Ottawa.

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goals. Also, the outcome in the recent Gambling case has generated further uncertainty with respect to interpretations, in the context of dispute settlement procedures, of domestic regulation measures in the light of Members specific commitments under the GATS, and regarding their potential effects on the regulatory autonomy of the states.³

Article VI Domestic Regulation

1. In sectors where specific commitments are undertaken, each Member shall ensure that all measures of general application affecting trade in services are administered in a reasonable, objective and impartial manner.
2. (a) Each Member shall maintain or institute as soon as practicable judicial, arbitral or administrative tribunals or procedures which provide, at the request of an affected service supplier, for the prompt review of, and where justified, appropriate remedies for, administrative decisions affecting trade in services. Where such procedures are not independent of the agency entrusted with the administrative decision concerned, the Member shall ensure that the procedures in fact provide for an objective and impartial review.

(b) The provisions of subparagraph (a) shall not be construed to require a Member to institute such tribunals or procedures where this would be inconsistent with its constitutional structure or the nature of its legal system.
3. Where authorization is required for the supply of a service on which a specific commitment has been made, the competent authorities of a Member shall, within a reasonable period of time after the submission of an application considered complete under domestic laws and regulations, inform the applicant of the decision concerning the application. At the request of the applicant, the competent authorities of the Member shall provide, without undue delay, information concerning the status of the application.
4. With a view to ensuring that measures relating to qualification requirements and procedures, technical standards and licensing requirements do not constitute unnecessary barriers to trade in services, the Council for Trade in Services shall, through appropriate bodies it may establish, develop any necessary disciplines. Such disciplines shall aim to ensure that such requirements are, *inter alia*:
 - (a) based on objective and transparent criteria, such as competence and the ability to supply the service;
 - (b) not more burdensome than necessary to ensure the quality of the service;
 - (c) in the case of licensing procedures, not in themselves a restriction on the supply of the service.
5. (a) In sectors in which a Member has undertaken specific commitments, pending the entry into force of disciplines developed in these sectors pursuant to paragraph 4, the Member shall not apply licensing and qualification requirements and technical standards that nullify or impair such specific commitments in a manner which:
 - (i) does not comply with the criteria outlined in subparagraphs 4(a), (b) or (c); and
 - (ii) could not reasonably have been expected of that Member at the time the specific commitments in those sectors were made.
(b) In determining whether a Member is in conformity with the obligation under paragraph 5(a), account shall be taken of international standards of relevant international organizations¹ applied by that Member.
6. In sectors where specific commitments regarding professional services are undertaken, each Member shall provide for adequate procedures to verify the competence of professionals of any other Member.

Evidently there is a real risk of WTO intrusion into the regulatory freedom of Members beyond what was originally intended in the GATS. Therefore, there are contending views about the treatment to be accorded to domestic regulation under the GATS. The following statement exemplifies one extreme position: "there should be no role for the WTO

³ Panel Report on United States - Measures Affecting the Cross-Border Supply of Gambling and Betting Services (challenger Antigua and Barbuda) WT/DS 285/R, circulated November 10, 2004, available at http://www.wto.org/english/tratop_e/dispu_e/285_e.pdf Also, Appellate Body Report on US - Measures Affecting the Cross-Border Supply of Gambling and Betting services, WT/DS285/AB/R circulated 7 April 2005.

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in over-seeing non-discriminatory regulation. This exercise represents a wholly unwarranted intrusion of trade law into important domestic public safety laws."⁴ It has also been stated that the GATS by intruding into the regulatory domain even threatens democratic governance.⁵ On the other hand, there are those of the view that disciplines on domestic regulation in the GATS, while they have to respect the right to regulate as mandated by the agreement, are a necessary, even an indispensable, complement to market access commitments in order to assure that those commitments will not be nullified by regulation being applied solely for protectionist purposes. The development of multilateral disciplines on domestic regulation is further promoted on the basis that they can play a significant role in promoting and consolidating domestic reform in developing countries, and also on the basis that disciplines on domestic regulation would help developing countries exporters addressing regulatory barriers to their exports faced in foreign markets. (Mattoo and Sauve 2004)

Even if the desirability and necessity of disciplines on domestic regulation in the GATS is accepted, the issue of how to curtail protectionism without infringing the recognized right of countries to regulate the supply of services in their territories still constitutes a formidable challenge for WTO Members. It is extremely difficult to develop effective multilateral disciplines in the area of domestic regulation of services without seeming to encroach upon national sovereignty and unduly limiting regulatory freedom. How to solve the tension between trade liberalization and regulatory autonomy constitutes a core issue in the current negotiations on domestic regulation taking place in the Working Party on Domestic Regulation (WPDR).

Negotiations on domestic regulation of services were launched in the WTO in 1995, on the basis of the Marrakech Ministerial Decision on Professional Services of 15 April 1994. After the entry into force of the WTO Agreement, the Council for Trade in Services (CTS) established the Working Party on Professional Services (WPPS) and entrusted it with the mandate of GATS Article VI:4 in the field of professional services, requiring to first develop disciplines in the accountancy sector.⁶ The WPPS agreed on guidelines for mutual recognition or arrangements, and on disciplines governing domestic regulation in the accounting sector by 1998. The Decision on disciplines relating to the accounting sector is still not binding. The CTS indicated the intention to formally integrate the disciplines it into the GATS no later than the conclusion of GATS 2000 negotiations.⁷ The CTS abolished the WPPS and established the Working Party on Domestic Regulation (WPDR) on April 1999, with the mandate to develop any necessary disciplines to ensure that measures relating to licensing requirements

⁴ Canadian Environmental Law Association. CELA Report 397 (2000). General Agreement on Trade in Services: Negotiations Concerning Domestic Regulation under GATS Article VI(4): Submitted to the Department of Foreign Affairs and International Trade and to Industry Canada, November.

⁵ Sinclair & Grieshaber-Otto (2002)

⁶ Decision on Professional Services. Adopted March 1, 1995. S/L/3.

⁷ Guidelines for Mutual Recognition Agreements or Arrangements in the Accountancy Sector, S/L/38, 27 May 1997; Decision on Disciplines Relating to The accountancy Sector, Adopted by the Council for Trade in Services on 14 December 1998, S/L/63, 15 December 1998. The CTS did not clarify what should be understood by "formal integration into the GATS". While this happens, Members shall "to the fullest extent consistent with the existing legislation, not take measures which would be inconsistent with these disciplines". Therefore the CTS's Decision has introduced a sort of stand still obligation, however with a doubtful legal standing.

and procedures, technical standards and qualification requirements do not constitute unnecessary barriers to trade in services. The WPDR was also entrusted to continue with the work of the WPPS, including the development of disciplines for professional services. According to its mandate, the WPDR in fulfilling its tasks shall develop generally applicable disciplines and may also develop, as appropriate, disciplines for individual sectors or groups of sectors.⁸

As it can be observed from the evolution of the work program on domestic regulation in the WTO, there has been a significant shift from the original task aiming at developing disciplines exclusively for professional services, to the current attempts to devise disciplines governing domestic regulation affecting all services sectors. One could even wonder if the original intention of the GATS drafters, and what was their main concern when incorporating Article VI:4 into the agreement, was only to deal with trade restrictive domestic regulation affecting accredited professional services. The content and wording of Article VI:4 is obviously more suitable to the case of accredited professions than to all imaginable existing or future services. In effect some of the problems being confronted in current negotiations derive to some extent from the need to adapt the exclusive list of measures of Article VI:4 to all possible circumstances.

Negotiations in the WPDR, after more than ten years, have not achieved substantial progress. There are still many basic issues to solve, and consensus seems elusive. However, in the last two years negotiations seem to have reached a different level on the basis of some more specific proposals touching, *inter alia*: on horizontal disciplines on transparency, technical standards, and qualification requirements and procedures. Momentum seems to be building in the process, and as the Chairman of the WPDR indicated, Members appear willing to build on the purposeful progress made to date.⁹ This Chapter discusses some of the main issues being addressed in the negotiations in the WPDR. The second section attempts to place the issues arising from the interface between domestic regulation and trade liberalization in services in the broader context of the ongoing analysis and debate surrounding regulation in general. The third section discusses current GATS Article VI provisions on domestic regulation and their potential impact on the regulatory freedom of states. The fourth section addresses the main issues being considered in the negotiations in the WPDR. Finally, some preliminary thoughts are presented as concluding remarks.

II. Some General Issues on Regulation and Disciplines on Trade in Services

Regulation has become a prominent issue in scholarly analysis, across various disciplines, due to what has been termed the rise of the "regulatory state" and the emergence of the age of regulatory governance; and considerable efforts are being undertaken to understand the politics and dynamics of regulation and in the analysis of regulatory "best practices".¹⁰ The GATS does not provide a definition of the concept 'domestic regulation' as

⁸ Decision on Domestic Regulation, adopted by the Council for Trade in Services on 26 April 1999, S/L/ 70, 28 April 1999.

⁹ Special Session of the Council for Trade in Services; Report by the Chairman to the Trade Negotiations Committee. TN/S/19/Suppl.1, 9 May 2005.

¹⁰ Among many other publications for a comprehensive review of the issues under consideration refer to: Jordana Jacint and Levi-Faur David (eds) (2004) *The Politics of Regulation: Institutions and Regulatory Reforms in*

utilized in Article VI; and there is no universally agreed definition of the term "regulation". This term used without distinction both to refer to different acts of governance, covering a wide variety of forms of state intervention in the economy, and other means of influencing behaviour, of firms and individuals in society, not necessarily only in the economic realm. In the literature, as highlighted by Baldwin et al. (1998), the term regulation appears with various meanings. In its wider sense regulation refers to all mechanisms of social control, including those, which are not necessarily product of state activity. A narrower meaning refers to regulation as all modes of state intervention in the economy; and in its narrowest and simplest sense regulation refers to a specific form of governance through targeted authoritative rules that are often accompanied by some regulatory body or agency entrusted with monitoring and enforcing compliance.¹¹

The concept of domestic regulation incorporated in the GATS would seem closest to the narrowest meaning of the term, referring in general to the state directly prescribing and proscribing what private agents have to do, and what they can and cannot do. Defined in this way, regulation is distinguishable from other forms of state intervention in the economy, such as the provision of public goods or essential services, and also from intervention that intends to affect the behaviour of private agents by modifying price signals, as for example through taxes or subsidies. However, the issue of whether the GATS provisions on domestic regulation are confined to the narrowest meaning of the term is not clear-cut, and there is room for interpretation in respect to the scope of measures on falling under Article VI.¹²

The pure economic case for regulation is essentially that regulatory measures are necessary to offset market failure stemming primarily from three kinds of problems: natural monopoly or oligopoly, asymmetric information and externalities. When market failure exists, it is commonly accepted in economics that optimally timed and executed state intervention can lead to higher economic welfare than unregulated private markets. In this context and as it relate to trade in services, it is considered that given the limited scope of GATS Article VIII and the fact that the incumbents can impede access to markets in the absence of appropriate regulation, multilateral disciplines might be necessary to address directly the problem generated by lack of competition in the markets. When market failure is attributable to asymmetric information or externalities, then multilateral disciplines might be needed only to ensure that domestic regulation put into effect to deal with the problem does not unduly restrict trade. However, it should be borne in mind that, in the real world, states regulate a number of economic activities, and other human endeavours for that matter, in pursuing a variety of policy objectives and not only with the view of offsetting perceived market failure. Many regulations are motivated, for example, by distributional considerations arising from the concern with fairness in society, or with the view of providing a variety of "merit goods" in

the Age of Governance. Centre on Regulation and Competition (CRC) Series on Competition, Regulation and development. Edward Elgar UK, USA. Also, to Cook, Kirkpatrick, Minogue and Parker (2004); Leading Issues in Competition, Regulation and Development. CRC Series on Competition, Regulation and Development. Edward Elgar Cheltenham UK, and Northampton USA.

¹¹ Baldwin, R, Scott, C and Hood, C (1998) *A Reader on Regulation*, Oxford: Oxford University Press. For a suggestive discussion of different meanings of regulation and definitional issues refer to: Black, Julia, *Critical Reflections on Regulation*, mimeo.

¹² For example, Krajewski (2003) seems to be of the view that regulation in the context of GATS could cover a wider range of measures than those that will fall under the narrowest and simplest definition.

line with societal preferences. Also, overall developmental objectives could be guiding the definition and implementation of a wide range of regulatory measures.¹³ Furthermore, some regulation is essential for the very existence, and not only for an effective functioning, of many markets (Chang 2003).

In general, regulation has flourished worldwide aiming to address a wide variety of social concerns, not exclusively limited to the economic realm, in searching for what is perceived as being the "public interest". In particular, in developing countries the regulatory structures appear to serve a wider range of objectives than pure economic efficiency. Therefore, even though economic analysis can provide interesting and valuable insights for the work in the WPDR, an exclusive economic approach should be avoided, as much as possible, while considering future disciplines on domestic regulation under the GATS. Other type of considerations should also be equally brought on board.

There are a number of issues arising from the current analysis and the debate on regulation in general that might be appropriate to take into account in the context of devising multilateral disciplines aiming to discipline states when applying domestic regulation, as is the case of the work being done in the WPGR. The societal mechanisms through which domestic regulation comes into being in the national domain, and the related issue of the appropriateness and viability of policy transfer across countries in the realm of domestic regulation constitute central themes that should be factored in the work of the WPDR, and also taken into account in any future disciplines to be adopted in the GATS. Even though there are different approaches providing diverse explanations on the emergence of regulation, a common denominator amongst most of them is that in a democratic setting overall societal preferences and the interests of particular groups in society are expressed through the indigenous political process generating a policy outcome that, to some extent, reflects a balance of the interests of all those involved in promoting, or be case in opposing, such regulation. Nevertheless, it is also recognized that due to the differentiated capabilities of different groups to influence decision-making processes there are many cases that deviate from this norm, and regulation tend to be skewed favouring a particular collective group. Also, the issue of the differences in regulatory processes and the diverse policy responses across policy areas at the national level has been highlighted in the literature. Therefore, regulatory outcomes tend to be country and in most cases issue specific. More importantly for our purposes is the growing consensus that the policy outcome equally reflects the system of values and beliefs of a society, its particular institutional setting, its legal system and practice, and also its own ways of doing things.

The country -and issue-specificity of most regulatory responses leads us to a basic question related to attempts, as the one intended in the WPDR, to adopt universally applicable regulatory frameworks or principles, or international standards, which may be based at the end of the day mainly in the experience and practice of developed countries. What is the level

¹³ This issue was raised, for example, by Johnson (1982) MITI and the Japanese Miracle, Standford, Standford University Press. When distinguishing the objectives of regulation between the US and other developed countries in their "catching-up" stages, Johnson highlights the fact that while regulation in the US was mainly shaped by the concern for productive and allocative efficiency, in countries like Western Europe and Japan the regulatory regime put emphasis on developmental objectives, such as improving productivity, upgrading technology and achieving efficient structural change.

of generality needed in multilateral disciplines on domestic regulation, as to allow accommodating the national, and diverse sectoral, particularities of all Members in such a way as making their implementation viable without unwarrantedly conflicting with domestic values, institutions and practices? This is a particularly pertinent issue for developing countries. As it has been noted, "transferred best practice models demonstrate clear adaptive variations in different countries, and is likely that the blind importing of these models from developed countries will be counterproductive where no account is taken of differences in legal infrastructure, bureaucratic culture, market realities and political values"¹⁴ Any multilateral disciplines on domestic regulation of services should be therefore have to be general enough to accommodate a wide variety of national circumstances, but at the same time they could not be as general as to render them for all practical purposes ineffective. A careful balance will need to be achieved between national applicability and the effectiveness of any future multilateral disciplines on domestic regulation under the GATS. Also, the *issue specificity* of most regulation should be taken into consideration when assessing whether horizontal or sectoral disciplines would be more appropriate to achieve the intended objectives of multilateral disciplines on domestic regulation.

Another relevant issue for developing countries are the possible consequences of internationalizing domestic rule-making processes allowing for the intervention of foreign governments and firms in those processes. Proposals have been made to mandate the justification of the rationale of domestic regulation and also to allow prior comment on proposed regulation. These requirements will effectively open domestic legislative and administrative procedures to foreign intervention. It would be expected then that in such a setting the policy outcome would not only reflect the interests of domestic stakeholders, but also foreign interests. Besides the administrative burden that would be imposed by these type of requirements and also its potential effects on prevailing legislative and administrative practices, an issue that has to be carefully assessed is the fact, widely recognized in the literature on domestic regulation, that those interest groups that are more cohesive, that can best formulate their interests, and that have the resources available to be invested in influencing decision-making are the ones that will see their interest prevail. In the light of the uneven distribution of resources; to what extent the internationalization of decision-making processes in developing countries might play more in favour of foreign interests in detriment of national ones? Enhanced transparency in defining and administering domestic regulation is predicated as an antidote to regulatory capture or rent-seeking influence (OECD). However, it might as well be that these requirements will effectively open the door for this type of behaviour and problem. This is not just an issue of merely academic concern. It can have strong implications in the nature of domestic regulation and in the extent to which it will effectively respond to legitimate national concerns.

It is widely accepted that in many cases domestic regulation might not be established solely in the pursuit of the public interest, but as explained in the literature by "rent-seeking" and "regulatory capture" type of arguments, its ultimate objective being to provide a benefit to certain groups in society having the power to influence and to skew the regulation setting process and its outcome in their favour. In these cases regulation is implemented and administered in such a way as to generate effective set up entry barriers deterring new entrants

¹⁴ Cook, Kirkpatrick, et al. (2004) "Competition, regulation and regulatory governance: an overview". In Cook P, Kirkpatrick C, (2004) op.cit page 20.

to those markets, and/or guaranteeing higher income or profitability to services suppliers in comparison with the situation what would have prevailed in the absence of the regulation. The benefit is the reward that organized interests groups get, justifying the rent-seeking costs they incur in bringing up the desired regulation. If the objective of disciplines on domestic regulation under the GATS is to support services trade liberalization, this is the type of regulation that should be the primary target, addressing its trade distorting effects.

If domestic regulation emerging from any kind of regulatory appropriation benefiting particular interests groups favours only domestic services or services suppliers to the detriment of foreign services and services suppliers, as discussed in the next section of this chapter, it would be covered by GATS Article XVII and the Members specific commitments regarding national treatment. However, regulatory measures of this kind could be benefiting all incumbents irrespective of their origin, being therefore non-discriminatory. If these regulatory measures contain any of the limitations explicitly defined in Article XVI, they would be prohibited market access limitations unless explicitly inscribed in a Members national schedule. What would need to be disciplined under Article VI are non-discriminatory, non-quantitative regulatory measures that are conferring some type of benefits to the incumbent service suppliers and as a consequence restricting trade in services. Therefore, the basic test to identify these kinds of regulatory measures, and to assess if they constitute unnecessary barriers to trade in services, should focus on determining if these measures are conferring an unwarranted benefit to services suppliers, and if as a consequence of such benefits the regulatory measures are in effect restricting trade in services.

The issue of the costs of regulation has also been highlighted in the literature. Domestic regulation imposes two types of costs on society, namely: *administration costs* and *compliance costs*. The first refers to costs of administering the regulation that is borne directly by the state or the regulatory agency, and financed either through fees imposed on the regulated industry, or through general budgetary financing. Compliance costs refer to the overall transaction costs imposed on the regulated agents by domestic regulation, not limited to direct monetary costs. Compliance costs can be brought about simply by wrongly defined and applied domestic regulation. This kind of cost might be relevant in the context of the discussions on disciplines under GATS Article VI. These costs would be covered by the notion incorporated in Article VI that domestic regulation should be "not more burdensome than necessary" Optimum regulation would be that which minimizes administrative and compliance costs while maximizing the positive effects on welfare. However, the objective of the GAT is not to promote good governance as such in the field of domestic regulation, but instead to promote the progressive liberalization of trade in services. Therefore, the requirement that domestic regulation be not more burdensome than necessary should be assessed solely in the light of the real, or potential, trade effects of compliance costs, and not in terms if the measure constitutes efficient or "sound regulation" or not, or if it is just an inconvenience to services providers.

Overall efficient regulation is of course an objective that every country should pursue, but this is an issue that needs to be addressed at the national level. However, some of the arguments in favour of strong multilateral disciplines on domestic regulation on services, as well as some of the proposals that have been advanced to date, tend to focus more on how the GATS could promote "sound regulation" and pro-competitive and market-friendly regulatory reform at the national level, than on what should be the only objective of multilateral

disciplines on domestic regulation as mandated by Article VI: 4, i.e. how to ensure that domestic regulation does not raise unnecessary barriers to trade in services. In order to challenge a regulatory measure the case would have to be made that the compliance costs related directly to that particular regulatory measure are in effect imposing an unnecessary barrier to trade in services, and not just that it is a needlessly burdensome or a high compliance cost regulation. Achieving social objectives in an economically efficient manner is of course a mayor challenge to national policy-makers. But this is certainly an issue that goes far beyond the objectives that should be pursued by multilateral disciplines on domestic regulation under the GATS.

Multilateral disciplines on domestic regulation of services, as derived from the above brief discussion, should aim to address the restrictive effect on trade of measures that might emerge, at least conceptually, from two different situations. On one hand, "protectionist" non-discriminatory, non-quantitative domestic regulation conferring unwarranted benefits to incumbent services or services providers that have the effect of restricting trade; on the other, from domestic regulatory measures, not intended to discriminate or restrict trade, but imposing compliance costs, directly associated with the measure, that have a demonstrable trade restrictive effect. In practice, however, the identification of regulatory measures and of the primary intention behind them along this line is not by any means an easy task. High compliance costs are usually associated with protectionist regulation, but the intention of the measure cannot be directly derived from the magnitude of those costs. However, differentiating measures according to whether they provide, or not, a particular benefit to services or services providers could be a useful device contributing to the reflection concerning future disciplines on domestic regulation under the GATS. Following this approach would approximate the discussion on domestic regulation to the treatment accorded to another form of state intervention in the economy in the WTO agreements, that of subsidies, where the defining element constitutes the extent to which a measure effectively confers a benefit to producers.

A basic proposition of those who actively promote multilateral disciplines on domestic regulation under the GATS as a means for encouraging developing countries to undertake good governance and efficient regulation of services, is that the measures employed should as a general rule be the least trade restrictive alternative available, or in a somehow different but closely linked formulation "no more trade-restrictive than necessary", as incorporated on the disciplines on accountancy. Only in this way would regulatory efficiency be assured. In GATT jurisprudence a measure is deemed necessary to the extent that there is no less trade-restrictive alternative reasonably available to achieve the regulatory goal. Determining what alternatives are available in a particular country and concerning a particular policy area is a highly complex issue, necessarily tainted with many subjective considerations. The issue of the "burdensomeness" and "trade restrictiveness" of domestic regulatory measures, terms that some times are indistinctively used, has to be assessed in the light of the existing regulatory capabilities of a particular state, the specific policy area, and also on the basis of the compliance capabilities of firms or individuals subjected to regulation. The institutional weaknesses and low regulatory capabilities of the state in most countries, the fragility of the private sector institutions, and as the compliance limitations of SME's, are recurrent themes in the literature addressing the issue of regulation in developing countries. The recognition of the difficulties and of the complexities involved in institution building and in enhancing

regulatory capabilities is also well entrenched on the literature.¹⁵ But these issues seem to be, unacknowledged by many proponents of tidily disciplining domestic regulation through multilateral enforceable commitments.

In the case of many developing countries, in particular, LDC's, because of the above mentioned limitations there might very limited regulatory options available that could assure the achievement of the legitimate social and economic objectives being sought by society. Therefore, any assessment of whether a regulatory measure in effect the least trade restrictive option available has to take into account the overall setting in which such regulation is being applied. It might be more an issue of what is actually possible under the prevailing circumstances in order to achieve what is perceived as being in the public interest, rather than a matter of choice. It may be that a regulatory measure is indeed trade restrictive, but its objectives are justifiable beyond pure concerns with economic efficiency. Self-regulation though voluntary industry standards or a code of conduct, for example, might be less trade restrictive in a certain policy area than mandatory regulation that generates high compliance costs. But in the absence of private sector institutions capable to defining and enforcing self-regulation, there might be not other choice.

Finally, regulations are formed at a particular point in time to address issues in a particular market, technological and social context. Regulation needs to adapt constantly to changing circumstances, in particular to rapid technological developments that could be hampered by applying inflexible regulation. Also, regulation has to be adjusted to preference shifts in society, and also when addressing emerging situations that represents, or are perceived, as new threats to society. A clear example of this last issue is the regulatory earthquake brought about in the accounting and auditing sectors by the series of corporate scandals that shook the foundations of the existing regulatory frameworks and of the industry alike in developed countries, with worldwide spillovers. Lack of flexibility and adaptability would render regulation either irrelevant or harmful in time. Binding domestic regulatory frameworks in multilateral enforceable commitments could introduce a degree of rigidity to required regulatory adaptation. Therefore, besides taking into account national and sectoral particularities, disciplines on domestic regulation should provide for the necessary flexibility in their implementation in such a way that domestic regulation can be adapted, within the framework of such disciplines, to changing national circumstances and requirements. Multilateral disciplines themselves should also incorporate the mechanisms that would allow them to be quickly modified in order to adapt them to any new developments, guaranteeing its effectiveness and national applicability. In this regard it should be borne in mind that deciding on multilateral disciplines has taken more than a decade. Usually technology, markets and societal needs cannot wait that long.

III. Domestic regulation in the GATS

It has been noted that one of the ironies of GATS is that among its weakest provisions are those dealing with domestic regulation, which has an obvious and powerful effect on international trade in services (Mattoo.). But perhaps, and we cannot discard this possibility, this might have been the explicit intention of those who negotiated the GATS. Also, some of the provisions of Article VI, as is the case with other provisions in the GATS, could be

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subjected to different interpretations, as it is already the case, and that the more substantive obligations disciplining domestic regulation are still in the making under an uncertain prognosis. This section briefly analyses Article VI, assessing its main provisions and highlighting some areas where different interpretations have become already evident, and discussing their potential implication for regulatory autonomy.

As it stands Article VI only applies to sectors in which Members have adopted specific commitments. Articles VI:1, VI: 3, VI: 5 and VI: 6 explicitly contain obligations only in sectors with specific commitments. If the rationale, and objective, for developing disciplines on domestic regulation under Article VI: 4, as highlighted by their main promoters, is to guarantee that specific commitment undertaken by Members would not be rendered meaningless by "protectionist" or unwarranted regulation, then any future disciplines in this regard should only be applicable to sectors in which Members have adopted specific commitments. This is the approach taken in the case of the Accountancy Disciplines, which is consistent with what seems to have been the original intention of those who negotiated the GATS. Being that the liberalization of trade in services is the main objective of the GATS, it would not make much sense disciplining domestic regulation in sectors in which Members can maintain and even introduce new trade restrictive measures in the sense of Articles XVI and XVII.¹⁶ The objective of GATS, as already highlighted, is not to discipline domestic regulation as such.

It should be noted that Article VI: 4, unlike GATS Article II which refers to "any measure covered by this agreement" or Article III applying to "all relevant measures of general application", is silent about the scope of future disciplines to be developed. Therefore, it should be interpreted in the immediate context of Article VI as a whole, which mainly refers to obligations in sectors in which specific commitments have been undertaken. Explicitly limiting the scope of future disciplines on domestic regulation under Article VI: 4 only to cover the specific commitments undertaken by Members will certainly eliminate uncertainty, allowing Members at the same time to assess their existing and future specific commitments also in the light of the parallel obligations they will be assuming with respect to domestic regulatory measures. This would assure the necessary flexibility, in particular for developing countries, in adopting commitments with respect to domestic regulation, together with their specific commitments, in line with national development objectives and their regulatory and institutional capabilities.

In the framework of the GATS, and for the ongoing negotiations on domestic regulation in the WPDR, a correct classification of policy instruments or domestic regulation measures, and their respective relation with trade restrictive measures, constitutes critical issues. To date the boundaries between them remains largely unsettled. In this regard the WPGR has devoted considerable time and efforts in discussing the type of measures to be

¹⁶ The issue of the applicability of future disciplines has been discussed in the WPDR. While most Members favour the view that future disciplines should only apply to sectors with specific commitments, there are some Members that have proposed that disciplines should be applicable regardless of commitments. Also, the possibility that some disciplines would apply to all sectors and other only to those with specific commitments has been suggested.

addressed by future disciplines under Article VI.4.¹⁷ A clear definition of the scope of Article VI, and clarity regarding the type of measure subjected to its different provisions is necessary.

The GATS as a whole applies to measures by Members, in any form¹⁸, emanating from any level of government or taken by non-governmental bodies in exercise of powers delegated by any level of government, affecting trade in services. As interpreted in the Bananas Case, the scope of the GATS encompasses any measure of a Member to the extent that it affects the supply of a service, regardless of whether such measure directly governs the supply of a service or whether it regulates other matters but nevertheless affects trade in services.¹⁹ Therefore, the GATS is far reaching and almost any type of state intervention, to the extent it affects trade in services, falls under it. The GATS provides for a first order distinction between measures. One set comprises measures that are defined, in its context as trade restrictive, being subject to scheduling under Article XVI (*Market access*), or Article XVII (*National treatment*). Article XVI provides an exhaustive list of five types of quantitative limitations to market access, and any requirement of a particular legal form of firm. It covers both discriminatory and non-discriminatory measures. Any measure that discriminates against foreign services or services suppliers, to the extent that modifies the conditions of competition in favour of domestic services or services suppliers, falls under Article XVII. All other measures covered by the GATS belong to another and distinct set of measures.

This second set of measures encompasses all non-quantitative-non-discriminatory measures affecting trade in services. This is the realm of domestic regulation. In principle there should be no overlap between this set and the one encompassing trade restrictive measures, each one being exclusive. All quantitative limitations, discriminatory or not, covered by one of the specific limitations defined by Article XVI; and all measures that discriminates against foreign services or services suppliers in the sense of Article XVII, belongs to the first set of trade restrictive measures. All other measures pertain to domestic regulation. This distinction between measures belonging to the different sets is also highlighted by the fact that Article XVIII, allowing for commitments in a wide range of areas, can only cover measures affecting trade in services not subject to scheduling under Articles XVI and XVII.²⁰

Even though the domains of trade restrictive measures and that of domestic regulation might seem a clear-cut case based on the exclusiveness of each set of measures, there are nevertheless some crucial issues blurring the boundary between these two sets of measures. How these issues are defined and interpreted in the context of the Members specific commitments may have significant implications for the regulatory autonomy of the states. In the case of *de jure* national treatment discrimination, which is brought by formally different

¹⁷ WTO (2003). "Examples of Measures to be Addressed by Disciplines Under GATS Article VI:4", Informal Note by the Secretariat., 22 September 2003. This note prepared on the basis of submissions by Members has been further updated.

¹⁸ As provided by article XXVIII (a) measure means any measure by a Member, whether in the form of a law, regulation, rule, procedure, decision, administrative action, or any other form.

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treatment, the distinction between trade restrictive measures and domestic regulation might be almost self-evident, being all these measures nevertheless subjected to the test of Article XVII:3. However, in the case of *de facto* discrimination arising from formally identical treatment of foreign services and services providers as the one provided to like domestic services or services suppliers, the relationship between trade restrictive measures and domestic regulation measures becomes could become more complex. Full commitments on national treatment would preclude any *de facto* discriminatory measure. However, the extent to which formally identical treatment discriminates in fact against foreign services, which could probably account for significant proportion of trade fiction cases, is not easy to identify and empirically assess. If identifiable, Members making national treatment commitments while wishing to maintain the measure should explicitly inscribe it as a limitation in their national schedules. There have been some such cases. However, due to the above-mentioned difficulties many Members, in particular developing countries, have not inscribed *de facto* discriminatory measures as such in their national schedules.

Cases concerning *de facto* discrimination are likely to emerge in dispute settlement procedures. In the context of such cases, domestic regulatory measures which seem non-discriminatory, and that being the regulators' primary intention, will have to be audited to empirically determine in each instance the extent they imply a less favourable treatment of foreign services or services suppliers modifying the conditions of competition in their detriment. Domestic regulation, which is non-discriminatory in intent and pursuing legitimate national policy objectives could be challenged on those grounds. The critical test would be if the measure modifies the conditions of competition against foreign like services or like services suppliers. It is obvious that such a test would not be an easy task to undertake, and would provide a wide discretionary margin to panels, and if it comes to that, to the Appellate Body, in determining if the contested regulatory measure is in fact discriminating against foreign services or services suppliers. Therefore, even without specific disciplines on domestic regulation, the enforcement of Members obligations when assuming specific commitments on national treatment could have by itself significant implications on the regulatory autonomy of the states.

In the case of market access commitments the relationship between Article XVI and Article VI is also a complex one. The GATS does not provide any guidance concerning their relationship. It should be presumed that domestic regulation falls under Article VI, and not as a market access limitation, unless it is clearly covered by one of the specific definitions in Article XVI. However, as the Gambling Case indicates a domestic regulatory measure can have the unintended consequence of restricting the number of services or services suppliers that can access the market, producing an effect that overlaps between the two sets of measures. Should domestic regulation, not covered by one of the market access limitations explicitly defined by Article XVI, be considered as violating specific commitments on markets access adopted by a Member? The decision in the Gambling case might have opened a troublesome route, even a *Pandora Box*, as there may be many state measures, and not only among those directly governing services, that have the unintended effect of restricting the number of services or services suppliers than can access a certain market. In this case, the decision of the Appellate Body has considerably expanded the reach of GATS prohibitions,

beyond explicitly numerical quantitative restrictions to include also substantive qualitative regulations applied indistinctly to foreign and domestic services suppliers.²¹

Article VI introduces a distinction between two types of domestic regulatory measures. On the one hand those "*measures of general application*" affecting trade in services being subjected to provisions of Article VI:1. On the other, a particular set of measures relating to qualification requirements and procedures, technical standards and licensing requirements that are dealt transitorily by VI:5, and for which negotiations of disciplines are called for in Article VI:4. Article VI.1 generates certain obligations in the case of measures of general application. In sectors where specific commitments are undertaken countries shall ensure that these measures are administered in a reasonable, objective and impartial manner. As it has been stated, "it is possible that this requirement, especially its reasonableness prong may be employed and developed in WTO dispute settlement to impose substantive obligations of proportionality in connection with domestic regulation."²² It should be noted that Article VI:1 disciplines the administration of regulation rather than regulation itself. Measures of general application are also subjected to the provisions of Article VI:2 and 3, providing for the availability of procedures and prompt review, and if necessary remedy of administrative decisions. Also, when authorization is required to supply a service, it requires that the status of the application to be informed to the services supplier on a reasonable timeframe, and also to adequately respond to inquiries by the applicant.

Article VI does not give any guidance on how to determine which domestic regulation measures should be considered, for all purposes, as measures of general application subjected to the provisions of Article VI:1; and no much effort has been spent in clarifying the reach of Article VI.1 either in the context of the deliberations in the WPGR, or in the specialized literature. Subjecting all measures covered by the GATS, when specific commitments are undertaken, to the requirements of Article VI.1 will certainly impose an extremely high administrative and procedural burden on Members.²³ Obviously, Article VI.1 seems to refer to a narrower set of measures than all those covered by the GATS, but clearly a wider range of measures than those explicitly listed in Article VI:4. What types of domestic regulatory measures are governed by it? This is a highly relevant question that needs to be addressed. Are visa procedures, that is an issue of special interest for developing countries, for example, covered by the requirements of Article VI:1?

Pending the adoption of disciplines on measures relating to qualification requirements and procedures, technical standards and licensing requirements, in sectors in which specific commitments has been made, these measures are subjected to the requirements

²¹ For a very suggestive analysis of the Gambling case refer to: Pauwelyn, Joost (2005) Rien ne Va Plus? Distinguishing Domestic Regulation from Market access in GATT and GATS; forthcoming in World Trade Review, July.

²² Trachtman, Joel (2002). Lessons for the GATS Article VI from SPS, TBT and GATT Treatment of Domestic Regulation. OECD-World Bank Services Expert Meeting, OECD Paris, 4-5 March.

²³ According to Krajewski, measures of general application, under Article III, are "any laws, regulations, decrees, administrative decisions or other measures if they apply to a large number of situations and not only to a single case", (page 125): and that "Article VI.1 applies to the same types of measures as Article III:1" (page 126). This would tend to equate obligations related specifically to domestic regulatory measures to obligations on all measures of general application covered by the GATS.

of Article VI:5; providing already some indication of what the GATS drafters envisioned as the direction of future disciplines in this area. Article VI:5 establishes that Members may not apply domestic regulatory measures of these types, if these measures nullify and impair their specific commitments. Therefore, domestic regulation measures can not be applied in a manner which does not comply with the criteria of Article VI:4 That is they must be: (a) based on objective and transparent criteria, such as competence and the ability to supply the service; (b) not more burdensome than necessary to ensure the quality of the service; and, (c) in the case of licensing procedures, not in themselves a restriction on the supply of the service. However, Article VI:5 only covers nullification or impairment, which could not have been reasonably expected at the time the specific commitments were undertaken by a Member.

Therefore, Article VI:5(a)(ii) suggests the grandfathering pre-existing domestic regulatory measures. It would mean that those measures could be maintained even if they are not in conformity to the above mentioned requirements. This provision might had already introduced a strong bias in favour of those Members in which there is profuse regulation on services, against those Members, like most developing countries, that are characterize to a large extent by the absence of regulation in many services activities. The future of Article VI:5 once that domestic regulation disciplines are adopted under Article VI:4, is an issue that is being debated in the WPDR. On the one hand there is the issue that specific commitments where undertaken by Members under this set of rules and if those rules are not maintained at least for those commitments, changing the rules would perhaps modify the reach of the commitments beyond the original intention of Members. On the other hand, if this element of Article VI:5 is incorporated into the VI:4 disciplines, and existing regulatory measures can be grandfathered, then a situation of blatant uneven application of the new disciplines could emerge in detriment of new specific commitments, and also of some Members, in particular those that have adopted less specific commitments..

In determining whether a Member when applying licensing and qualification requirements and technical standards, is in conformity with its obligations under Article VI:5(a), Article VI:5 (b) introduces some sort of a presumption in favour of international standards, establishing that account shall be taken of international standards of relevant international organizations applied by that Member. It should be understood that if a Member is applying international standards in its domestic regulation is more likely that it is fulfilling its obligations, than will be the case if it is not applying such standards, or domestic standards are not based on international standards. This raises two main issues. One that is common to all cases in the WTO Agreements in which presumption is made in favour of international standards, and relates to the effective participation and involvement of most developing countries is setting such standards. The case is made that even if the standard setting body is formally open to the participation of all WTO Members, in practice, due to the limited resources available and lack of specialized knowledge, the rate of involvement and degree of influence of developing countries in setting such standards is at the best very limited. Therefore, international standards tend to reflect in most cases the interests and concerns of developed countries, and in many cases mainly the interests of the private sector stakeholders who end up determining international standards to suit their particular interests.

A second issue, and closely related to the dynamics of international setting of regulation or standards, that has been correctly highlighted by some observers is, that if

conformity with international standards is to be used as the justification for the necessity of a particular element of domestic regulation, or in order to generally assume presumption in their favour, then it would be essential for the international standards themselves to have adequate regard for transparency, necessity and proportionality.²⁴ As it stands Article VI:5(b) does not require any conditions to be met by international standards, other than the standard setting body be opened to the participation of all WTO Members. Future disciplines on domestic regulation under the GATS should require international regulation or standards, if they are to be used as benchmarks, to be subjected to the same type of conditions imposed on domestic regulatory measures, and also on domestic rule-making procedures. It should not be a priori presumed that rent-seeking behaviour does not, or could not, take place equally at the international level.

Finally, Article VI:6 incorporates the obligation, only in sectors where specific commitments regarding professional services are undertaken, to provide adequate procedures to verify the competences of professionals of any other Member. This obligation does not seem to imply a major burden for developing countries. If a certain profession is an accredited one, in the majority of cases such procedures are in place. However, what should be understood as adequate procedures? That is something that is left to be assessed on a case by case basis as no benchmarks, or guidance is provided in this regard.

IV. Main Issues in Current Negotiations under Article VI: 4

Negotiations on domestic regulation are evolving around four core themes: (i) the applicability of future disciplines; (ii) the appropriate nature of those disciplines, i.e. horizontal vs. sectoral disciplines, and in this context if the disciplines on accountancy can be extended to other sectors; (iii) the assessment of the trade effect of domestic regulatory measures, i.e. the necessity test; and, (iv) the reach of transparency obligations in the context of the disciplines on domestic regulation.

Applicability

A main issue regarding the applicability of future disciplines on domestic regulation is if these disciplines should apply regardless of whether specific commitments had been undertaken, or they should only applied to sectors in which a Member has undertaken specific commitments. This issue has been briefly discussed in the preceding section. Nevertheless, is important to stress the fact that disciplines on domestic regulation of generic application would undermine the "bottom-up" approach of the GATS. They would curtail the necessary flexibility that should be provided, in particular to developing countries, for adopting whatever commitment they wish to undertake in line with their development needs and institutional capabilities. The overall logic that underlines the GATS should be dully respected when establishing disciplines on domestic regulation. A closely related issue, briefly discussed in the previous section, is the need to explicitly define the relationship of domestic regulation disciplines with Articles XVI and XVII. This issue has been correctly highlighted by Krawjeski, and also by Pauwelyn, who suggest that in order provide legal certainty and to maintain the balance of rights and obligations of Members any future

²⁴ John Cooke: Head of International Relations, Association of British Insurers, Domestic regulation, IAIS Observer Panel Presentation. Mimeo, nd.

disciplines on domestic regulation needs to regulate their relationship to Articles XVI and XVII, in line with the accountancy disciplines which excluded measures subject to scheduling from their application.²⁵

Another issues related to the applicability of future disciplines concerns the level of government to be covered by those disciplines, how to treat measures emanating from non-governmental bodies in the exercise of powers delegated by central, regional and local governments, and the type of measure that should be governed by future disciplines. The issue of the significant administrative burden for local and regional authorities, in particular in developing countries, that the compliance with future disciplines may impose has been highlighted in the literature, as well as in the debate in the WPDR. Also, the issue has been raised that because of the different weight of different levels of government in regulating services across countries, limiting the applicability of disciplines only to certain levels of government, as some Members and analysts have proposed as a way of addressing this potential problem, may lead to an uneven application of obligations on domestic regulation.

In order to achieve a balance of obligations for all Members in this area, it would be appropriate for any future disciplines on domestic regulation to respect in principle the GATS basic structure covering all measures independently from the level of government they emanate. The problems that developing countries may confront in complying with disciplines can be addressed by linking the applicability of any new obligations on domestic regulation for these countries with the development of regulatory and institutional capacities at the local and regional levels of government. The type of formulation adopted for the negotiations of trade facilitation could provide some insights on how this issue could be addressed in future disciplines on domestic regulation under the GATS. In that case, WTO Members agreed that the results of the negotiations shall take fully into account the principle of special and differential treatment for developing and least-developed countries. This principle should extend beyond the granting of traditional transition periods for implementing commitments. In particular, the extent and the timing of entering into commitments shall be related to the implementation capacities of developing and least-developed Members. It was also agreed that those countries would not be obliged to undertake investments in infrastructure projects beyond their means.²⁶

Treatment of regulatory measures emanating from non-governmental bodies constitute a very complex issue to be address in the WPDR, as the exact meaning of "in exercise of powers delegated by government or authorities" is not at all clear. It should be taken into account that a literary interpretation of the term would not necessarily cover all the possibilities through which private entities might end up regulating the provision of services. As it has been noted there are different motivations and means through which non-governmental actors end up regulating a variety of services. There is *mandated self-regulation*, in which a collective group is required or designated by the state to formulate and enforce norms within a broad framework set by the state. There is also *sanctioned self-regulation* in which the collective group formulates rules, which are then approved by the

²⁵ Krajewski, Markus (2005). Domestic regulation for services: Presentation at the South Centre Workshop in Services. 28 February to 4 of March, Geneva, Switzerland. Pauwlyn (2005).

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government. There is also the case of *coerced self-regulation*, in which the collective group formulates and imposes regulation only in response to the treat of statutory regulation, and in addition government may have taken backstop statutory powers to impose such regulation, what is described as 'regulation in the shadow of the law', or 'co-regulation'.²⁷

All the above mention cases differ from *voluntary self-regulation* where there is no state involvement at all in promoting or mandating regulation. It should be presumed that the first case of state involvement would clearly qualify under the definition of GATS Article I:3(a)(ii). What about the other cases where there is also deep state involvement but not necessarily there are powers directly delegated by local, regional or central governments and authorities? There is also the issue concerning the fact that voluntary self-regulation in services, as for example the case of private standards, or accreditation and recognition of qualifications, can have even a greater restrictive effect on trade than any state mandatory regulation. Self-regulatory bodies are frequently much more complex regulators, in the sense that they combine rule-making, monitoring, and sanctioning powers within a single organization, something that is not usual for state regulatory agencies.²⁸ It has also to be taken into account that the concept of voluntary self-regulation itself might be even questionable, due to the multiplicity of actors usually involved in defining and setting regulation, and in particular because the indirect non-coercive state influence that may be exerted in promoting the adoption and shaping self-regulation by different collective groups, through what has been label as *quasi-regulation*.

Developing countries tend to rely for the most on statutory regulation, while developed countries are increasingly utilizing different forms of self-regulation by private bodies or entities to achieve their regulatory objectives. If future disciplines on domestic regulation will confine themselves to disciplining statutory regulation and that emerging from private entities in exercise of powers delegated by government or authorities, understood this later case in its narrowest sense, the final outcome could be greatly unbalanced. Practices of developing countries will clearly fall under the new disciplines, while many of those of developed countries, that might even have a greater effect on trade, may be fully sheltered from any obligation on domestic regulation. The incorporation of voluntary self-regulation under the reach of multilateral disciplines, as some Members have already suggested, raises a number of complex legal issues that the WPDR would have to assess and deal with.²⁹

A final issue with respect to the applicability of disciplines on domestic regulation refers to the type of measures to be governed by those disciplines. There has been some debate in the WPDR if the list of regulatory instruments incorporated in Article VI:4 could be extended to include other regulatory measures. However, VI:4 suggest that the list is exhaustive, and it seems that the prevailing mood in the WPDR until this moment is to stick to the negotiating mandate. Extending the list of measures to be covered by disciplines on

²⁷ Black Julia (2003). "Mapping the Contours of Contemporary Financial Services Regulation". ESRC Centre for Analysis of Risk and Regulation, London School of Economics and Political Science, Discussion Paper No 17, October

²⁸ Scott, Colin (2002) "Private Regulation of the Public Sector: A Neglected facet of Contemporary Governance": Journal of law and Society, No 29.

²⁹ Swiss Proposal

domestic regulation would certainly increase the intrusiveness of the GATS into the domestic regulatory domain.

Horizontal vs. Sectoral Disciplines

An issue under discussion in the WPDR is whether a set of common disciplines on domestic regulation should be developed for all services, or if it would be more appropriate to device disciplines for particular services sectors. The pros and cons of the different approaches have been debated in the negotiations and in the literature alike. The main concern of Members should be which approach would be more effective in achieving the explicit objective set for Article VI:4 disciplines, that is avoiding unnecessary barriers to trade in services that could arise from the application of the list of measures contemplated in it. That goal should be achieved without compromising the Member's necessary flexibility for regulatory adaptation, or their right to regulate the provision of services in their territories. These are the benchmarks against which the different proposals should be assessed.

Discussion in the WPDR has to date mainly focused on horizontal disciplines, and some of the proposals presented to the WGDR aim at establishing disciplines on domestic regulation applicable to all sectors.³⁰ Benefits of the horizontal approach to disciplines on domestic regulation have been presented in terms of political economy type arguments. It has been suggested that a horizontal approach will economize negotiating efforts, would lead to the creation of disciplines for all services sectors rather than only for politically important ones, and would also reduce the likelihood that negotiations will be captured by powerful sectoral interests groups (Mattoo 2000)³¹. The economic case for horizontal disciplines is made on the grounds that such an approach will promote rules based on economic efficiency considerations, incorporating at the same time technological neutrality and will allow automatic application to new sectors.

In connection horizontal disciplines it is argued that, to the extent that the type of market failure needed to be addressed by domestic regulation is the same irrespective of the sector, generic disciplines could be applied to govern domestic regulation implemented for similar purposes. Nevertheless, it is acknowledged that it might be needed to incorporate certain provisions to account for the different type of market failure being addressed by the variety of domestic regulatory measures. Issues arising from monopoly or oligopoly command a different policy response, than those arising from asymmetric information or externalities. Taking into account these issues, it is asserted that it could be possible to construct viable horizontal disciplines covering all services sectors; or at least some generic disciplines on domestic regulation in line with the different problems associated with the kind of market failure that they are intended to deal with.³²

³⁰ Japan, Developing countries

³¹ Mattoo, Aaditya (2000) Developing Countries in the New Round of GATS Negotiations: Towards a Pro-Active Role, *The World Economy*, Vol 23, No 4 (April)

³² In this regard for example it has been proposed that the pro-competitive provisions incorporated in the Telecommunication Reference Paper could be applied to all network services, and also be extended to embrace all forms of internal distribution.

A horizontal approach, in order to be applicable to diverse sectoral specificities, might need to be very broad and to a large extent highly abstract. Therefore, its effectiveness could be significantly jeopardized; and its provisions at the end of the day, being interpreted case by case in the context of dispute settlement procedures. This certainly would not provide the necessary predictability concerning the potential effect of multilateral rules on regulatory autonomy. Also, specific industry features may limit the scope of a horizontal approach. With respect to adopting horizontal disciplines, it should be borne in mind that even within more similar services, as is the case of professional services in which asymmetric information is reputed to be the main problem to be addressed by domestic regulation, still there is no certainty if disciplines adopted for a particular profession, as the case of accountancy, could be extended as they are to all other professions.³³ Sectoral disciplines may be more appropriate because they can be tailored to fit the particular needs and circumstances of regulation in a particular sector and will provide higher predictability. However, what seems to be evolving in the work in the WPDR is a hybrid approach aiming at incorporating horizontal disciplines to govern certain areas, to be complemented by a sectoral approximation to ensure the presence of specific features to meet particular requirements of different services industries. A truly horizontal regime might evolve in time through the experience with the application of sector specific disciplines.

Necessity Test

GATS impact on domestic regulation will greatly depend on the nature of the necessity test that would be developed in the context of Article VI:4 disciplines. The more appropriate design for a necessity test in the disciplines on domestic regulation has been widely analyzed in the literature, and the WPDR has devoted significant efforts to address this issue. The basic objective of disciplines on domestic regulation is to ensure that measures applied by countries "do not constitute unnecessary barriers to trade in services". Article VI:4 makes the presumption that in order for a measure not to constitute an unnecessary barrier to trade it should be based on objective and transparent criteria, to be not more burdensome than necessary, and in the case of licensing procedures not in themselves being a restriction to trade. Multilateral disciplines on domestic regulation shall ensure that domestic regulatory measures fit these requirements. However, as already mentioned the objective of article VI:4 is not to discipline domestic regulation as such. Some of the proposals regarding the implementation of Article VI:4 tend to emphasize more on assuring that domestic regulation conforms to the requirements set in this Article, than on achieving its explicit objective. Some of the proposals, in particular on transparency have significantly departed from the original intention of Article VI:4.

As provided by the objective of Article VI:4 the basic test should be determining first if a certain regulatory measure is in effect restricting trade, and then if there is the need to restrict trade in order to achieve the national policy objectives. Among the requirements set by Article VI:4 the notion of burdensomeness, or compliance costs, as discussed in the second section, becomes crucial in the context of such a necessity test. To assess a particular measure it would not be enough to demonstrate that a measure is more burdensome, or costly, than necessary and directly deriving from that fact that it is a trade restrictive measure, as some tend to suggest. A measure can be burdensome but not necessarily trade restrictive. The notion of

³³ Case of lawyers.

more burdensome than necessary should be understood in the context of Article VI:4 as referring to "more trade restrictive than necessary".³⁴ Once that a measure is found to be trade restrictive, the following test would be to determine if it is more restrictive than necessary to achieve the policy objective. Determining necessity in this context is certainly a very complex issue.

Different possibilities have been suggested for assessing if a measure is more trade restrictive than necessary. One alternative, following GATT jurisprudence, would be to consider the measure as necessary to the extent that there is no other less trade-restrictive alternative reasonably available to achieve the same policy goal. The practical complexities in determining the availability of alternative measures, and if those alternatives can effectively achieve the goals being pursued, has been briefly discussed in the second section. Presumably this formulation will provide a wide margin of discretion in identifying available alternatives in DSB procedures. Other alternative that has been proposed is to incorporate the benchmark of proportionality in the test. A measure will not be more trade restrictive than necessary if it is proportional to the objective pursued. This formulation would also introduce significant complexities in assessing the proportionality of a measure and in its practical application. A measure can be proportional to the objective pursued, but that does not guarantee that it is the least trade-restrictive possible measure. An important issue is that either alternative would demand, at the end of the day, an assessment of the objectives being pursued by domestic regulation, as they will require evaluating the balance between policy objectives and the level of trade restrictiveness imposed by a domestic regulatory measure. Whatever form it takes the necessity test call for Article VI:4 will obviously has the potential, through its application, of being highly intrusive into the regulatory autonomy of the states.

Article VI:4(b) establishes that a regulatory measure should be no more burdensome, that is no more trade restrictive, than necessary "to ensure the quality of the services". Regulatory measures pursued a wide variety of objectives besides assuring the quality of a service. The fact that only one objective is explicitly mentioned in Article VI has led Members to discuss on the convenience of incorporating a list of legitimate objectives into multilateral disciplines on domestic regulation, as was done in the case of the accountancy disciplines. In that case, consumer protection, the quality of the service, professional competence, and the integrity of the profession were incorporated as legitimate objectives. The definition of which should be considered legitimate objectives of domestic regulation is a highly sensitive issue. What might be considered a legitimate objective by society varies across countries and across time. Any criteria of legitimacy, necessity and proportionality therefore would only be satisfied if domestic regulatory measures were subject to periodical review to test whether they continue to meet the criteria.

The debate in the WPDR seems to have moved away from seeking some sort of agreement on the issue of legitimate regulatory objectives. However, when assessing the balance between regulatory objectives and the restrictiveness of a measure, is probable that this issue would be brought into consideration. Therefore, in the absence of clarity in this regard in future disciplines, the objectives been pursued by a country through a regulatory measure could be challenged. This would effectively curtail the regulatory freedom of

³⁴ Krajewski (2005)

Members. Multilateral disciplines on domestic regulation should leave no room for challenging the objectives being pursued by regulatory measures.

Contrary to the case of GATS Articles XIV and XIV bis, in which the necessity test has been introduced in order to allow Member to justify a measure that violates an specific commitment when necessary to achieve the objectives considered in those Articles; in the case of the necessity test in Article VI:4, it will be more for justifying the application of legitimate regulatory measures. Therefore, as it has been noted it could transform the necessity test from a shield to save clearly discriminatory measures from challenge into a sword to attack clearly non-discriminatory measures.³⁵

Transparency

Article VI:4(a) provides that measures should be based on objective and transparent criteria, such as the competence and the ability to supply the service. In the context of the Article it is presumed that non-objective and non-transparent criteria could create unnecessary barriers to trade. In the first case, requirements beyond those needed to assess the competences and the abilities of the services provider, or other not justifiable in the light of the specific nature of the service, could turn the measure into more burdensome than necessary. In this case this issue blends with the necessity test discussed above. The issue of international standards is relevant in this context. Criteria and requirements based on such standards could be presumed to be objective. Nevertheless, as discussed supra those standards would have to be subjected to the same tests as those proposed for domestic regulatory measures.

Regarding transparency, lack of easily accessible information on regulatory measures could have a trade effect. Therefore, disciplines should assure that all required information be available to services providers in order that trade would not be unnecessarily restricted. Article VI:4 deals with ex post transparency, whereby regulations are made public once taken. That is precisely the objective of GATS Article III. The central issue in the debate in the WPDR should be what else is needed in top of Article III and beyond what is already covered by Article VI:2 and VI:3 requirements, to avoid lack of information emerging as an unnecessary barrier to trade in services. However, some proposals on this issue have gone far beyond this objective, suggesting disciplines on ex ante transparency. In particular this is the case of those suggesting the inclusion of "prior comment" and "prior publication" of intended regulation in disciplines on domestic regulation that would require members to explain the objectives and the rationality of the regulatory measures. The possible effect on domestic decision-making processes of these types of requirement, which have been introduced in the accountancy disciplines already, have been already discussed. Nevertheless, in order to consider this kind of requirement in future disciplines, a clear case would need to be made that the absence of prior comment or prior publication effectively restricts trade beyond what is necessary. That has not yet been the case.

Proposals presented to the WPDR on transparency aiming to significantly strengthening obligations by including prior comment and prior publication requirements,

³⁵ Scott Sinclair, *The GAS, Democratic Governance and Public Interest Regulation*, mimeo

among others, are based, not on trade considerations, but in different type of arguments. It is argued that transparency and openness in decision-making is an essential part of public governance under any democratic setting. Lack of transparency reduces the information available to interested parties and undermines their ability to participate meaningfully in policy processes. Also, it is argued that open processes can lead regulatory authorities to reflect carefully on the full range of alternatives before introducing or modifying regulations, resulting in better regulation, greater compliance and ultimately greater political legitimacy.³⁶ These are very laudable goals, but not the objectives of Article VI:4. Due to their intrusive nature national regulatory autonomy could be significantly curtailed by the incorporation of these requirements in multilateral disciplines on domestic regulation.

V. Conclusions

The GATS as it is could already be highly intrusive in the domestic regulatory domain limiting the autonomy of the state. In particular issues arising from the relationship of measures falling under Article VI:4 and Members specific commitments under Articles XVI and XVII could bring legitimate regulatory measures under challenge. This requires Members to carefully analyse the requirements of the regulatory system before any specific commitment is scheduled. The lack of clarity regarding the reach of future disciplines on domestic regulation calls for caution in adopting commitments that might compromise in the future domestic regulation and the state's autonomy in this area. The extent of the encroachment of the GATS in the regulatory domain of the national state will depend on the final reach of the disciplines being negotiated in the WPDR. The final outcome of the negotiations is still unclear at this moment. To avoid unwarranted intrusion into domestic regulation these disciplines should strictly be limited to promoting the explicit objective of Article VI:4, and disciplines should be crystalline clear to provide predictability as to its effects on domestic regulatory decision-making, and to avoid in the future rule-making by adjudication. Multilateral disciplines on domestic regulation need to incorporate meaningful special and differential treatment for developing countries taking into consideration its development needs and their institutional and regulatory capabilities.

³⁶ OECD

Policy Paper on Trade in Services and Sustainable Development: Domestic Regulation

Prepared by Luis Abugattas Majluf, UNCTAD

Draft – Not to be Quoted
