

Appendix 2. Overview of the *General Agreement on Trade in Services*

General introduction

The General Agreement on Trade in Services (GATS)¹ is one of the agreements entered into as part of the Uruguay Round of multilateral trade negotiations that resulted in the formation of the WTO. It was the first multilateral agreement on trade in services, though services are dealt with in many regional and bilateral trade and investment agreements. GATS applies to all measures of a WTO member that affect trade in services, including services supplied through a commercial presence, which includes some forms of investment.

GATS comprises both a general framework of obligations for WTO members that apply to all services and a negotiated set of additional specific commitments regarding the treatment of identified services activities that each member lists in a national schedule of commitments. GATS incorporates key principles from the General Agreement on Tariffs and Trade (GATT),² including most favoured nation (MFN) treatment, national treatment and transparency, though the application of these principles to services trade is substantially attenuated.

The most important general rule is the obligation to grant MFN treatment to foreign services and services suppliers. This means that members must treat services suppliers from other member states no less favourably than those from any other country. Members were permitted to list specified exceptions to their MFN obligation at the time they joined the WTO (GATS Art. II.2; Annex on Article II Exemptions).

For sectors listed in its national schedule, a member becomes subject to a higher level of obligation. Members must grant foreign services suppliers in these sectors national treatment (meaning treatment no less favourable than the treatment of domestic suppliers) (GATS, Art. XVII) and cannot impose certain restrictions on market access, such as limiting the total number of service providers in a sector and limiting the percentage of foreign ownership of a service supplier (GATS, Art. XVI). For listed sectors, the member's regulatory scheme must meet specified standards, including a requirement that measures affecting trade in services be administered in a reasonable, objective and impartial manner (GATS, Art. VI.I).

1 *General Agreement on Trade in Services*, signed 15 April 1994, in force 1 January 1995, Marrakesh Agreement Establishing the World Trade Organization, Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations, GATT Doc. MTN/FA, Annex 1B, 1869 *United Nations Treaty Series* 183, 33 *International Legal Materials* 1167.

2 *General Agreement on Tariffs and Trade 1994*, signed 15 April 1994, in force 1 January 1995, Marrakesh Agreement Establishing the World Trade Organization, Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations, GATT Doc. MTN/FA, Annex 1A, 1867 *United Nations Treaty Series* 187, 33 *International Legal Materials* 1153.

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

GATS commitments for the WTO's 159 member states interact with their IIA obligations in a variety of complex ways. Because each member's obligations are customised in its national schedule of commitments and MFN exemption list, IIAs and GATS do not interact in the same way for every country. This note on GATS provides a general overview of the provisions in GATS that are most relevant in relation to investment and IIA obligations.

Scope of application

Introduction

GATS applies to all measures taken by WTO member states that affect trade in services. Services are not defined. Instead, GATS simply states that trade in services means services supplied through any of four modes of supply:

- Mode 1: Cross-border supply – a service is supplied by a service supplier of a WTO member in the territory of the WTO member to a service consumer in the territory of any other member such as over the telephone or the internet;
- Mode 2: Consumption abroad – a service is supplied by a service supplier of a WTO member in the territory of the member to a service consumer of any other member where the service consumer travels to the supplier's country to consume the service;
- Mode 3: Commercial presence – a service is supplied by a service supplier of one member through a commercial presence in the territory of any other member; and
- Mode 4: Presence of natural persons – a service is supplied by a service supplier of one member through the presence of natural persons of that member in the territory of any other member (GATS, Art. 1.2).

GATS obligations apply to the measures of central, regional and local governments and to those of non-governmental bodies in the exercise of powers delegated by central, regional or local governments (GATS Art. 1.3(a)). For this purpose, non-governmental bodies include independent agencies and commissions exercising powers delegated by the state.

Services 'supplied in the exercise of governmental authority' are excluded from the disciplines of GATS provided two conditions are met: the service is not supplied on a commercial basis or in competition with other services providers (GATS, Art. 1.3(c)).³

3 The scope of the exclusion is extensively discussed in J A VanDuzer (2004), 'Health, Education and Social Services in Canada: The Impact of the GATS', in J M Curtis and D Curiak (eds), *Trade Policy Research 2004*, International Trade Canada, Ottawa, 287 at 367–407.

Supply of services through a commercial presence – a form of investment

Mode 3, commercial presence, includes some kinds of investments. In general, a service supplier of one WTO member is supplying a service through a commercial presence in the territory of another WTO member if:

- The supplier has a subsidiary (usually a corporation) or an unincorporated branch of its operation within the territory of that other member for the purpose of supplying the service; and
- The subsidiary or branch is owned or controlled by natural persons that are nationals of the first member or legal persons (usually corporations) organised under the laws of the first member.

A bank incorporated in the UK that is supplying banking services through a locally incorporated subsidiary in South Africa that it controls is an example of a UK service supplier supplying services in South Africa through a commercial presence.

Commercial presence under GATS does not include all of the forms of investor and investment that are eligible for protection under existing IIAs. Most obviously, commercial presence for the purposes of GATS does not include investments that do not involve the supply of a service, such as an investment to operate a local mine. Even in relation to services businesses, such as accounting or construction services, commercial presence does not include many forms of investment protected under an IIA. For instance, it does not include investments that do not give the foreign investor control over the local business such as a minority shareholding in a business. This kind of investment is often protected in IIAs.

Supply of services through the presence of natural persons

Mode 4, the presence of natural persons, can also be relevant with respect to the activities of foreign investors. In general, the obligations of the GATS apply to the supply of services by individuals, though the obligations are very limited. GATS obligations do not apply to natural persons seeking access to the employment market in a member state or measures regarding citizenship, residence, or employment on a permanent basis. Members are not obliged to give up measures to regulate entry, such as visas. However, each member can make commitments in its national schedule of commitments relating to the movement of natural persons. Many developed countries but few developing countries did so.⁴ In some cases, these commitments relate to individuals who work at the operations of foreign investors in the host state.

Members who made commitments for mode 4 typically grant rights of temporary entry into their territory for specific categories of persons who have technical or managerial expertise subject to requirements set out in their national schedules. In its national schedule, for example, Canada committed to granting temporary entry into Canada

4 GATS Annex on Movement of Natural Persons Supplying Services under the Agreement.

to a number of categories of individuals, including ‘Intra-corporate transferees’, who are individuals of one member who go to work at an investment in another member. Intra-corporate transferees are granted entry for up to three years. In Canada’s national schedule of commitments, intra-corporate transferees include senior executives and managers of a foreign service supplier, and specialists with some particular expertise related to the business of the supplier.⁵

Key obligations applying to all sectors

Most favoured nation

As noted, *GATS* Article II obliges members to provide MFN treatment. Under *GATS*, members can record one-time exemptions from the MFN obligation in their national schedules of commitments. Exemptions listed by members include existing bilateral and regional preferential arrangements of various kinds. Some members have listed exemptions that appear to extend to future preferential arrangements as well.⁶

The *GATS* MFN requirement is qualified by the agreement’s Article V, which permits member countries to enter preferential regional and bilateral agreements to liberalise trade in services under prescribed conditions. Such agreements do not have to be set out in a member’s MFN exemption list. To qualify for the Article V exemption, regional and bilateral agreements must meet conditions analogous to those in *GATT* Article XXIV, which provides a similar exemption in relation to trade in goods. Qualifying agreements must have ‘substantial’ sectoral coverage, in terms of the number of services sectors, volume of trade and modes of supply covered⁷ and must provide for the elimination of substantially all discrimination in the trade of the parties. Few IIAs, apart from some comprehensive PTIAs, will meet these requirements. Consequently, the *GATS* MFN obligation could apply to preferences to particular countries granted under IIAs.

Transparency

Some of the transparency requirements in IIA models can be found in the *GATS* and other WTO Agreements. Article III of *GATS* requires WTO members to publish promptly all relevant measures of general application that pertain to, or would affect the operation of, *GATS*. A ‘measure’ is defined as ‘any measure by a Member, whether in the form of a law, regulation, rule, procedure, decision, administrative action or any other form’ (*GATS* Art. XXVIII(a)). Bilateral or plurilateral agreements on services must also be published. WTO members are obliged to respond to requests for information regarding their measures and agreements.⁸

5 See Box 5.18 for more details on Canada’s commitments.

6 The MFN exemption list filed by Mauritius, for example, may be interpreted in this way (*GATS/SC/55*), available at: <http://docsonline.wto.org> (accessed 8 January 2013).

7 In order to meet this condition, agreements should not provide for the a priori exclusion of any mode of supply.

8 See Box 5.15 for more details on *GATS* transparency obligations.

Key sector-specific obligations

Structure of market access and national treatment commitments

As discussed above, by listing a service sector or activity in its national schedule, a member commits itself to another set of obligations under GATS, including commitments to provide market access and national treatment.⁹ Market access has a specific meaning under GATS. For services sectors listed in national schedules, market access means that members must not impose the following specific market access restrictions (GATS Art. XVI:1):

- Limitations on the number of service suppliers, whether in the form of numerical quotas, monopolies, exclusive service suppliers or the requirement for an economic needs test;
- Limitations on the total value of service transactions or assets in the form of numerical quotas or the requirement for an economic needs test;
- Limitations on the total number of service operations or on the total quantity of service output expressed in terms of designated numerical units, whether in the form of quotas or the requirement for an economic needs test;
- Limitations on the number of natural persons that may be employed in a particular specified sector or activity or that a service supplier may employ who are necessary for, and directly related to, the supply of a specific service, whether in the form of numerical quotas or the requirement for an economic needs test;
- Measures which restrict or require specific types of legal entity or joint venture through which a service supplier may supply a service; and
- Limitations on the participation of foreign capital in terms of a maximum percentage limit on foreign shareholding or the total value of individual or aggregate foreign investment.

Each member may customise the precise level of market access and national treatment to which it is committed. Where a member wishes to maintain or be able to adopt a domestic measure inconsistent with the market access or national treatment obligations in relation to a listed sector or activity, the member must describe the measure or use other language preserving this flexibility in its national schedule of commitments. Limitations are listed separately in relation to each of the four modes of services supply. Limitations may take the form of a total exclusion of any obligation for one or more modes of supply. Alternatively, limitations may describe discrete conditions qualifying the extent of the member's commitment regarding a particular

⁹ GATS schedules are based on a sectoral classification developed by the WTO Secretariat, which divides services into 12 sectors, which, in turn, are broken down into 54 sub-sectors. Sub-sectors are further disaggregated into 161 activities. GATT Secretariat (1991), *Services Sectoral Classification List: Note by the Secretariat*, MTN.GNS/W/120, 10 July, available at: <http://docsonline.wto.org> (accessed 8 January 2013), which is based on United Nations (1991), *Statistical Paper Series M No. 77, Provisional Central Product Classification*, Department of International Economic and Social Affairs, Statistical Office of the United Nations, New York. Subsequently, the UN classification system has been revised.

mode of delivery in specific ways. In sum, the listing of a service activity in its schedule commits a member to accord in relation to that activity, and to suppliers of that service, both market access and national treatment with respect to each of the four modes of service supply, but subject to any limitation recorded in the schedule itself.

Most states, other than those that have joined the WTO since it was formed in 1994, have made weak commitments in their services schedules that, at most, oblige them to maintain the degree of openness that they provided to their domestic markets when GATS came into force in 1995. Negotiations are ongoing, however, and it is possible that stronger liberalising commitments will be a feature of a successful conclusion of the current Doha round of negotiations.

Domestic regulation requirements

GATS imposes a variety of additional obligations on members in relation to sectors listed in their national schedules. As noted, each member must ensure that all measures of general application are administered in a reasonable, objective and impartial manner. More importantly, under Art. V.5, measures relating to licensing and qualification requirements and technical standards cannot nullify or impair any specific commitment undertaken by a member in its national schedule of commitments by imposing requirements or standards not based on objective and transparent criteria, such as competence and ability to provide the service, or that are more burdensome than necessary to ensure the quality of the service. In the case of licensing procedures, the procedures themselves must not be restrictions on the supply of a service. These obligations are qualified by the caveat that the nullification and impairment 'could not reasonably have been expected of that member at the time the specific commitments in those sectors were made' (GATS, Art. VI.5(a)(ii)). In effect, this means that these domestic regulation commitments are 'standstill' obligations. Nullification or impairment can occur only as a result of new measures adopted after GATS came into force.¹⁰ Also, where authorisation is required to provide a service in an activity subject to a member's specific commitments, each member must inform applicants regarding whether authorisation has been granted within a reasonable time (GATS, Art. VI.3).

Transfer of funds

GATS contains a transfer of funds obligation for all members. GATS prohibits members from restricting international transfers and payments for current transactions related to services that are listed in its national schedule of specific commitments and from restricting capital transactions in a manner that would be inconsistent with its commitments in its schedule (GATS, Art. XI). This obligation is, however, subject to an exception that permits a member to restrict trade in services and any related

¹⁰ GATS, Art. VI.4, 5. See J Trachtman (2005), 'Negotiations on Domestic Regulation and Trade in Services: (GATS Art. VI): A Legal Analysis of Selected Issues', in E U Petersmann (ed.), *Reforming the World Trading System: Legitimacy, Efficiency and Democratic Governance*, Oxford University Press, Oxford, at 205.

payment, even in sectors that it has listed in its national schedule of commitments, ‘[i]n the event of serious balance-of-payments and external financial difficulties or threat thereof’ (GATS, Art. XII). GATS specifically recognises that ‘particular pressures on the balance of payments’ of a member that is a developing country or a transition economy may require the use of restrictions to ensure the maintenance of a level of financial reserves adequate for the implementation of its programme of economic development or economic transition.

Any restrictions on transfers under this exception must meet certain requirements. They:

- (a) Shall not discriminate among members;
- (b) Shall be consistent with the Articles of Agreement of the International Monetary Fund;
- (c) Shall avoid unnecessary damage to the commercial, economic and financial interests of any other member;
- (d) Shall not exceed those necessary to deal with [serious balance-of-payments and external financial difficulties or the threat thereof]; and
- (e) Shall be temporary and be phased out progressively as the [serious balance-of-payments and external financial difficulties or the threat thereof] improves.

Any restrictions adopted by a member must be promptly notified to the WTO General Council. Any member applying restrictions must consult promptly with the Committee on Balance-of-Payments Restrictions on restrictions established under GATS.

Enhanced transparency obligations

There are enhanced transparency obligations for sectors in relation to which a member has undertaken specific commitments, which means that the member has listed the sector in the member’s national schedule of commitments. In addition to the general publication obligation described above, each member must establish one or more enquiry points to provide specific information to other members regarding its services regime (GATS, Art. III.4). GATS does not oblige members to disclose confidential information the publication of which would impede law enforcement or otherwise conflict with the public interest, or which would prejudice legitimate commercial interests (GATS, Art. III*bis*).¹¹

Monopoly services suppliers

Where a member authorises a monopoly service supplier to operate, such as a single provider of telecommunications services, and the services supplier competes in the

11 A similar proviso regarding confidential information is contained in the India–Singapore CECA (Art. 6.14(2)), the ASEAN Agreement (Art. 21.2) and the COMESA Investment Agreement (Art. 4.4). See Box 5.15 for more details on GATS transparency obligations.

supply of a service that is outside the scope of its monopoly rights and in a sector listed in the member's schedule, the member must ensure that the monopoly supplier does not abuse its monopoly position (GATS, Art. VIII). Abuse would include, for example, subsidising its activities in the competitive market with its monopoly profits.¹²

Exceptions

GATS Article XIV allow members to impose measures otherwise inconsistent with the GATS that are necessary to protect important national interests, including measures necessary to protect public morals, public order and human, plant or animal health. These exemptions are analogous to those found in GATT Article XX. GATS goes on to provide that measures necessary to ensure compliance with laws protecting privacy of personal data and safety and to prevent deceptive and fraudulent practices or the effects of defaults in services contracts are also exempt from the obligations in the agreement, so long as the laws themselves are not inconsistent with the GATS. Certain tax measures are exempt from national treatment, and measures related to international agreements on the avoidance of double taxation are exempt from MFN. All of these obligations are subject to a chapeau requirement, which provides that to qualify for the exception, a measure must not be 'applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where like conditions prevail, or a disguised restriction on trade in services'.

GATS Article XIV(bis) contains a national security exception that is similar to that contained in GATT XXI. Nothing in GATS can be construed:

- a. To require any member to furnish any information, the disclosure of which it considers contrary to its essential security interests; or
- b. To prevent any member from taking any action which it considers necessary for the protection of its essential security interests:
 - i. relating to the supply of services as carried out directly or indirectly for the purpose of provisioning a military establishment;
 - ii. relating to fissionable and fusionable materials or the materials from which they are derived;
 - iii. taken in time of war or other emergency in international relations; or
- c. To prevent any member from taking any action in pursuance of its obligations under the United Nations Charter for the maintenance of international peace and security.

Because the exception is available any time a member 'considers' that its essential security interests are at risk, each member has a broad discretion to determine when it will rely on the exception. It is not clear to what extent it is possible to challenge the availability of the exception if a member claims to rely on it. If a member takes

¹² Members are also obliged (GATS Art. VIII.1) to ensure that monopoly service suppliers do not undermine access commitments undertaken in national schedules of concessions.

a measure in reliance on the exception, the member is obliged to give notice to the WTO Council on Trade in Services.

GATS also excludes prudential measures in its Annex on Financial Services (s. 2). A member can take measures for prudential reasons, which are defined to include the protection of investors, depositors, policy holders or persons to whom a fiduciary duty is owed by a financial service supplier, or to ensure the integrity and stability of the financial system.

To the extent that such prudential measures do not conform with GATS, they are not to be used as a means of avoiding the member's obligations under the Agreement. The Annex goes on to provide that a member is not obliged to disclose any information relating to the affairs and accounts of individual customers or any confidential or proprietary information in the possession of public entities.

GATS built-in agenda

GATS requires WTO members to recommence negotiations on a number of aspects of the treaty with a view to increasing the level of members' commitments. Article XIX requires new negotiations with a view to achieving greater liberalisation of obligations in national schedules of commitments. These negotiations are now incorporated into the Doha Round of multilateral trade negotiations, which are ongoing.

Also, as part the built-in agenda of the GATS, members are required to negotiate rules to avoid trade-distorting effects caused by subsidies in services (GATS, Art. XV). GATS' MFN, national treatment and market access obligations do not apply to government procurement, but GATS requires that the members engage in negotiations on procurement commitments (Art. XIII). GATS also commits members to negotiate disciplines on the use emergency safeguard measures to address the effects of services liberalisation (GATS, Art. X). Finally GATS obliges members to negotiate rules that will ensure that measures relating to qualification requirements and procedures, technical standards and licensing requirements relating to services do not constitute unnecessary barriers to trade in services (GATS, Art. V.4). All of these negotiations are ongoing as part of the Doha Round.