

Service Trade and the OECD

By Serge A. Devos

This article is essentially devoted to a description of the work carried out within OECD (the Organization for Economic Cooperation and Development) on trade in services. This involves considering basic questions concerning ways to deal with trade in services at the international level, as well as substantive issues that efforts toward liberalization raise in this field. This article, however, does not pretend to be comprehensive in this respect. The subject matter is very complex and while substantial progress has been achieved, in the examination of the issues within OECD, much remains to be done.

The OECD concern with trade in services and its competence in this field is not new. The Convention under which the OECD was established in 1960 provides that member countries will "pursue their efforts to reduce or abolish obstacles to the exchange of goods and services and current payments, and maintain and extend the liberalization of capital movements." This commitment was further developed in two Codes of Liberalization, one for Current Invisible Operations (which covers most service sector activities) and one for Capital Movements. Since its inception OECD activities have covered a wide range of service sectors (insurance, banking, tourism, shipping, etc.) through specialized committees. Work on trade in services, however, has taken a new dimension and a new perspective in recent years. In 1979, a more global and more systematic approach was adopted which included initially a vast program of factual analysis. It coincided with a decision to undertake a review of certain OECD instruments, notably the Invisible Code. A political impulse was given by the OECD Council to the new work undertaken when, in 1982, ministers encouraged the competent committees of the organization "to progress as soon as possible in their analytical and fact finding work on the complex issues involved so as to be able, in the light of the results, to begin examining ways of removing unjustified impediments to international trade in services and of improving international cooperation in this area."



OECD Deputy Director for Trade Serge A. Devos

Before turning to the work being pursued under this broad political mandate, a few preliminary observations should be made as they help to explain the nature of the work and the way it is progressing. The importance attached to the service sector is linked to the fact that, in all developed countries, its economic significance is growing relative to the manufacturing sector. As to international trade in services, though it is already substantial, there is not a definite perception of its overall economic significance. While it is assumed that liberalization of trade in services would bring with it advantages similar, though not necessarily identical, to those of freer trade in goods, it must be recognized that, with some exceptions, this represents more of an intellectual extrapolation than the result of analytical research. The uncertainty about the effects of liberalization of trade in services in general, is one of the causes of the uneasiness and of the cautious attitude of some in this little known field. The situation is complicated by the differences which exist among the various services sectors. An additional and perhaps more trivial reason is that, in most if not all countries, the various service sectors had up to now been considered on their own merits, with less attention to the service industry as a whole. In this respect the

work launched in OECD in 1979 has already had one major result, having led national administrations to adopt a new and global vision of the services sector. At the same time it is probably true that various member countries' approach to the OECD exercise remains influenced by the importance they attach to one or another sector, which may vary from one country to another, or by their focusing on the implications of liberalization in a given sector. Telecommunications, data processing and information services represent one sector that may be at stake here, because of its promising developments and its high technology component, and because of its interconnection with industrial structure, and more generally with economic growth.

These are among the reasons why the choice between vertical, or sectoral, and horizontal approaches has been much debated. The two-track approach which has been adopted, though there may still be differences of emphasis, reflects the recognition that the sectoral and horizontal approaches are in fact complementary and mutually supporting. Their combination may well be indispensable to achieve fruitful results in dealing with international trade in services. A solely vertical approach entails the risk of getting bogged down in technicalities. A broader approach can provide the necessary political impetus and could ensure a balanced policy response to the issues, as between the sectors and also as between the interests of the various countries. On the other hand, though there are issues which are common to all service sectors, and common principles that could apply to all of them, account may have to be taken of the specificities of each sector, including the differences in regulations. Beyond a general and common policy framework, additional provisions may be required to address specific issues or specific aspects of general issues.

In summary, the OECD activities follow a comprehensive approach including both in-depth studies of the specific service sectors, and horizontal studies devoted to problems which are common to all or a number of services industries, examining

Serge A. Devos is deputy director for Trade at the Organization for Economic Cooperation and Development (OECD). Devos joined the Organization for European Economic Cooperation (OEEC), predecessor of OECD, in 1954 after serving in a Belgian economic research institute and in the Belgian chemical firm Solvay & Cie.

concepts which might be applied to such problems. Without prejudice to political decisions to be taken at the appropriate time and place, this latter part of the work is intended to elaborate a general framework of international cooperation in trade in services. For convenience, the OECD activities will be described under four titles: identification of problems and obstacles; OECD existing instruments; examination of concepts applicable to trade in services; other horizontal studies.

Identification of problems and obstacles

The normal course of action was to start by trying to identify and analyze problems and obstacles in international trade in services. Both "across-the-border trade" and "establishment trade" were covered in recognition of the fact that often the supply of a service by a foreign firm necessitates, even when not required by regulations, the presence of the firm in the consuming country. This identification exercise was based on inquiries addressed to national administrations which have generally responded with the help of the service industry of their respective countries. To determine which, among identified problems, could be considered obstacles to trade, and therefore subject to international cooperation, four criteria have generally been used as a working hypothesis: (a) discrimination against services provided by foreign firms, including discriminatory restrictions on market access, investment, and the right of establishment; (b) discriminatory treatment of foreign-controlled service firms already established in the country in question; (c) internal regulations which have an excessively inhibiting effect; and (d) a lack of transparency of regulations or arbitrary administrative practices. A preliminary attempt was also made to evaluate whether such obstacles are of major or minor im-

portance, whether they can be reasonably justified or not and whether they are relevant only to the specific sector in question or are of more general relevance.

Studies have been carried out so far for insurance, banking, tourism, maritime transport and construction-engineering consultancy. Studies are underway on the telecommunications, computers and information services, and audiovisual and professional services. Other sectors to be included or being considered for study include advertising and auditing. Generally, these studies focus on obstacles within the OECD area, but in some cases, such as maritime transport and construction-engineering consultancy, they also covered obstacles in non-OECD members, in particular in developing countries. This is rather important, in view of the fact that, at least in some sectors, problems are felt to be already or potentially acute in trade with those countries.

A few general points emerged from the studies. First, though there are obstacles common to various sectors, they may be of varying significance according to the sectors. However, the right of establishment seems to be a question which is relevant in a number of sectors. This may also be the case for other questions such as outright limitations to market access, government procurement, etc. Second, when it comes to tackling identified impediments to trade in services, the underlying motivations of the regulations will have to be considered. This is particularly important in the case of the service sector because it is highly regulated and the regulations can create impediments for international trade even when they do not constitute an obstacle according to the criteria mentioned above. In certain cases, diversity of regulation, or in other words lack of harmonization, has been identified as a problem.

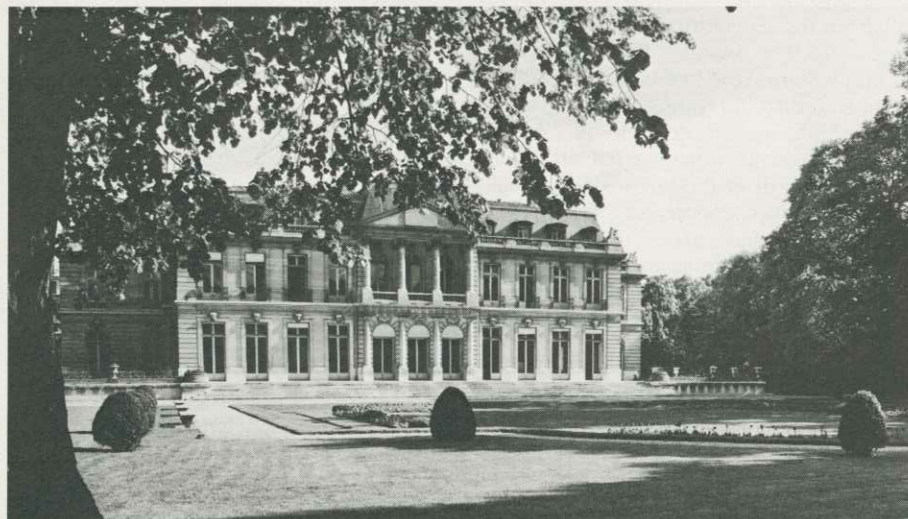
Following the identification of impediments to trade in services, a number of

questions have to be considered more systematically. They include the importance of the obstacles in terms of their effect; whether they are specific or general; the motivations for them; the negotiability of solutions. That kind of work has already been done or started in some sectors.

OECD existing instruments

As already mentioned, there have been in OECD since 1961 various instruments concerned with liberalization of trade in services, i.e. service transactions and transfers, and international investment. These instruments have the merit of being operative and of combining the horizontal and sectoral approaches. It was quite normal, in the context of the new impetus given by ministers toward improved cooperation and removal of obstacles in the field of trade in services, to draw on the experience gained through the existing instruments and see how they could be used to promote liberalization. This work is carried out mainly by the Committee on Capital Movements and Invisible Transactions (CMIT) in close cooperation with specialized committees in charge of various service sectors. It consists in examining the instruments with a view to improving their capability to address the identified obstacles to trade in services by strengthening their implementation and, where necessary, by amending the instruments themselves. As one of the results of that work, the OECD Council has just decided to extend the liberalization obligations of the Capital Movements Code, to cover certain important aspects of the right of establishment. The Code will henceforth cover not only restrictions on foreign direct investment but also discriminatory restrictions in the granting of licences or authorization to carry out business related to direct investment. Another expected result concerns the National Treatment instrument of 1976, revised in 1979, which covers goods and service sectors, and calls for foreign-controlled firms already established to be accorded treatment within the country no less favorable than that accorded to domestically-controlled firms in like situations. Ministers decided, at the meeting in May, to strengthen the implementation procedures of the instrument, aiming at a reduction of the number of exceptions to the national treatment principle.

The Code of Liberalization of Current Invisible Operations deserves special mention because it is directly related to international trade in services. The Code contains general obligations covering notably liberalization, non-discrimination, transparency, which apply to a list of service transactions, and transfer. More specific obligations are included for individual



OECD headquarters in Paris

service sectors, notably insurance and maritime transport. It was generally felt that this Code has been too static, that it has not evolved to adapt to important changes which have taken place over the last twenty years in the service industry. The CMIT has been asked therefore by the OECD Council to work toward its updating and revision. On the basis of that work, the existing provisions could be re-drafted and strengthened, and the coverage could be extended to additional sectors and to include additional obligations.

It is fair to say that some basic features of the Codes are seen, at least in some quarters, as limiting the possibility of making real progress toward the reduction of impediments to trade in services. It is claimed, in particular, that the binding character of the obligations and the effective scope of the Codes are affected by the possibility, for any member country, not to eliminate immediately all measures contrary to the obligation, but to lodge reservations when adhering to the Code and when new obligations are entered. These reservations (and temporary and justified derogations) are submitted to a process of periodic in-depth examinations. There is no way, however, to ensure that the recommendations which are addressed to the country, as a result of the examination, concerning its specific non-complying measures, are implemented. It is one aspect of a more general question which is that of the basic process of liberalization on which the OECD Codes rest, i.e. consensus-building rather than negotiations. This question will be taken up later, in somewhat more detail. That there has been until recently little evolution in the Code on Invisibles reflects the fact that further liberalization of trade in services was just not contemplated. That the situation is now changing should normally open better prospects. Moreover changes could be made in the OECD codes systems. Some may feel that such changes, without going as far as adopting the traditional negotiating process, would imply more than mere adaptation and would need to be substantial. The work being done presently on the Codes constitutes, in any case, a major contribution to international cooperation in trade in services.

Examination of concepts applicable to trade in services

In parallel to the work based on the existing OECD instruments another more general path is being followed within OECD and notably by its Trade Committee. The approach adopted consists in an in-depth examination of general concepts drawn basically from those already applicable to trade in services, those exist-

ing for trade in goods, to the extent that they are relevant, and from other possible notions. This exercise contributes to bringing about a better understanding of the issues of liberalization involved and is part of a process aimed at coordinating views on how to bring about trade liberalization. Following a first general examination of concepts their validity is now being tested in individual sectors. Summarizing the work achieved up to now is difficult, particularly because views still differ at least on certain points. The replies given to the various questions raised may depend on the final objective and scope of international cooperation, and are likely to be of a political nature. Some of the highlights of the discussion, however, are presented below.

Market access and right of establishment

In any effort to liberalize trade in services, the concept of market access is fundamental. What does this concept mean and what does it imply in the case of services? Though an answer to these questions, with possible variations from one sector to another, may be given at the theoretical level, it will in the end depend also on political decisions, concerning the accepted scope of liberalization. It is clear that market access includes the reduction or removal of "obstacles" to transborder trade in the classical sense. But beyond this traditional aspect the question is whether and to what extent market access should encompass the right of establishment. It is a fact that the supply of services often requires the foreign supplier to be established through a subsidiary, a branch or an agency. Beyond the fact that it may be required by the regulations of the consuming country (even if the service could be in theory supplied directly from abroad), the necessity to operate locally may be intrinsically linked to the nature of the service. Local operation may also be an "economic" condition to make the supply of services competitive, or to substantially increase business possibilities. What, in those conditions, can be considered effective market access? Where should we draw the line between trade in services and local production of the same service? The approaches here may differ. On the one hand, it may be felt that what matters is to offer the opportunity to sell on the market concerned, which may imply, for instance, access to local distribution/marketing infrastructures and the right to use a brand name. On the other hand, at least in certain instances, the question at stake would be the right of establishment. A more general question thus concerns the relation between trade in services and foreign direct investment in services. It may be noted that issues such as the movement of persons (not to mention transfers and payments) may also be relevant. It has to be seen in further

discussions whether the specific components of market access—and in particular, where necessary, elements of the right of establishment—can be defined across-the-board, or would have to be determined on a sectoral basis (or a combination of both).

Non-discrimination: This concept has been examined in the light of Article I of GATT, which refers to non-discrimination among foreign suppliers (and not between foreign and home suppliers). This principle is embodied also in the OECD codes of liberalization applicable to services. It is a central feature of the multilateral trading system for goods, and it may be felt that it should also apply to trade in services. A number of issues are, however, being discussed. The first concerns bilateral reciprocity as distinct from the general reciprocity, in terms of overall balance of advantages and concessions, used traditionally in negotiations. Reciprocity in the bilateral sense is frequently found to exist in countries' regulations and in agreements in the investment field. The question is whether this kind of reciprocity is incompatible with a multilateral approach to liberalization, or on the contrary whether it might be seen, in this complex area of trade in services, as a means to foster liberalization, and as a transitional mechanism in the move from a restricted to a more open and subsequently to a multilateral system. The second point discussed concerns the possibility of a conditional application of the non-discrimination principle. The conditional non-discrimination approach preserves a multilateral character, as in this case the benefit resulting from an agreement negotiated in advance multilaterally, would automatically be extended to any country prepared to accept the underlying obligations of that agreement. This approach might be considered suitable in the field of trade in services, because liberalization measures may often require important and intricate changes in internal regulations. Countries may more readily accept to make such concessions if they are ensured that partners will contribute to the same extent. The conditional approach may leave some flexibility and create less resistance to agreement on the principle of substantive liberalization measures.

National treatment: This concept is embodied in a number of agreements, notably for imported goods in Article III of GATT; for foreign goods and suppliers, in the Code on Government Procurement; and, in the context of foreign direct investment, for already established foreign controlled firms, in the OECD instrument on National Treatment. The OECD codes contain provisions which indirectly convey similar notions. In a broader approach, it seems this concept would have to be redefined, for

services, in a way that covers both trans-frontier trade and "establishment" trade. This raises some important questions; for example, as a counterpart to the granting of full national treatment, it would be necessary to be able to ensure that foreign firms comply with the domestic regulations of the country where they sell services. Another question is whether limitations to the extent of national treatment granted, could be used as a means to afford protection to domestic industry with a role similar to that of custom duties for instance.

Transparency: It is generally acknowledged that this concept, which is almost a prerequisite of liberalization, is also relevant to trade in services. It is in fact embodied in a number of agreements or instruments, including those directly related to services. The problem is to define in precise terms what would be needed to achieve the necessary transparency, as part of a set of obligations or an agreement on trade in services. A precondition is that the regulations and other necessary information should be readily available. Beyond that, a notification procedure constitutes one of the major tools to achieve transparency. The question is, however, to determine what has to be notified. One suggestion discussed is that governments should notify measures which, at the border or as part of internal regulations, are protectionist in their intent. This may still leave a wide margin of interpretation unless related to a well-defined "liberalization commitment," or to an agreed list of restrictive measures and practices. Provisions for cross notification might thus also be added.

In the context of discussions of relevant concepts other issues of significance are being examined. One stems from the fact that regulations in the service sector, often if not always, correspond to some special needs or objectives. One typical example are regulations deemed necessary to protect consumers' interests (for instance in insurance or banking). But regulations to meet these objectives may differ from one country to another and views may differ as to what is necessary, and what is excessive, considering the possible unintended restrictive effects. The possibility has been raised of seeking a consensus on what constitutes a reasonable regulation or a reasonable level of regulation. Other issues relate to the consideration that, as in the case of goods, liberalization of trade in services should, realistically, be a progressive process.

Other studies

The concepts briefly examined above are only a first approach and the list may have to be extended to include, for instance, the notions of distortions, excep-

tions, derogations and safeguards. Besides this kind of work, other studies are being undertaken or are already planned. Issues to which a number attach special importance from the point of view of further liberalization efforts include: the problems of regulation in federal states; the problem of private regulations; the problem of competition arising in the service sector with state or private monopolies. It has also been suggested that a closer examination of the economic and structural characteristics of trade in services would be useful. Finally, efforts to improve statistics of trade in services are greatly needed. Balance-of-payment figures probably very much underestimate actual trade. This work is beginning, based on an inquiry into the availability and lacunae of balance-of-payments data. But there is also the broader problem of collecting economically more significant and comprehensive data on trade in services.

Perspectives

The longer term prospects for OECD activities on trade in services are intrinsically linked to some fundamental issues concerning international cooperation in that field, not only in OECD but also in a broader context. One of the main questions concerns the choice between two basic approaches: consensus-building or negotiations. In the former case, the aim is to reach a broad consensus on the principles, commitments and action required to achieve the accepted objective. Progress also depends on the political pressure that can be put on any country to join the majority view on general principles or commitments, and to take the necessary steps to conform to the obligations. This is generally the approach to international cooperation used in OECD. But there are cases where negotiations take place in OECD and lead to agreements with explicit obligations. Even the consensus approach may be seen as including a certain element of negotiation.

On the other hand, the traditional negotiations leading to contractual agreement, as used in GATT for trade in goods, are based on the principle of reciprocity. Such negotiations consists in an exchange of concessions which are deemed to produce a balanced result taking account of various interests in liberalization measures. Whether such a negotiating process could and should be used in the case of trade in services is still a debated question. The possibility of undertaking such negotiations in GATT may also depend on the attitude of developing countries. For various reasons, these countries have been reluctant or hesitant about GATT activities in the field of services. There are recent signs that this attitude may be changing, at least in some cases. Such countries'

final stand may depend on what they could expect from multilateral negotiations including services, in areas where they feel they have a greater interest, in particular in terms of improved and more secured access for their exports of manufactures.

For OECD countries, the heart of the matter at this stage does not seem to be institutional. Trading partners are still in a phase of preparation including efforts toward a better and common understanding of the issues and the progressive elaboration of individual positions on them. This analytical phase is long, not only because of the complexity of the issues, but also because of policy implications. In this phase, OECD has a number of advantages. First, it has long experience in dealing with trade in services, both horizontally and in specific service sectors; it already has a number of instruments, which are being and can be further developed and improved in their operation. Second, the normal method of work, characterised by a large degree of informality, allows for open and extensive discussions. Third, there is a process of cross-fertilization between the various studies on the concepts, the existing instruments, other horizontal issues, and in a wide range of sectors.

The work carried out within OECD is indispensable to the development of international cooperation in the field of trade in services. For the future, there is considerable scope for complementary activities in OECD and GATT, and there are several ways to combine their efforts. It is too early to develop these possibilities, however, as the final approach and mechanisms of a process of liberalization have yet to be formulated, in particular as regards possible use of a combination of bilateral and multilateral, generic and sector-specific approaches, or as to the role of reciprocity, etc. Whatever the final decisions, it is clear that OECD will remain active in this field. There are several reasons, in addition to the organization's long-standing competence and activities, to support this assumption. A formal agreement may not initially be all-encompassing. It may need progressive strengthening of obligations or extension to additional commitments, either general or specific. As the field is very wide and expanding, there will probably be a need for continuous work on new or additional sectors, based on technical and even more general expertise. ●

The views expressed in this article are solely those of the author and do not necessarily represent the views of the organization. The author expresses his thanks for the contributions and comments of members of the secretariat, in particular Mr. William Witherell, deputy director for Financial, Fiscal and Enterprise Affairs at OECD.