Chapter 11

TRADE IN SERVICES

1. OVERVIEW OF RULES

The phrase “trade in services” applies to international transactions in a diverse array of fields, including financial services, transportation, communications, construction, and distribution. When considering barriers to trade in services, domestic regulations governing their supply and consumption are more important than border measures (such as tariffs). This contrasts with trade in goods, where border measures play a significant role. These domestic regulations are put in place for a variety of reasons -- sometimes to protect domestic industries, but just as often to meet public objectives such as protecting culture and traditions, or protecting the interests of consumers.

Trade in services has steadily increased. According to WTO statistics, services now account for 19.2 percent of world trade (by shipping value), or about $2,415 trillion in 2005 (*see* Figure 11-1). This increase has led to a greater need to develop disciplines for trade in services. The General Agreement on Trade in Services (GATS), stipulating most-favoured-nation treatment, market access commitments and national treatment, was agreed to at the end of the Uruguay Round negotiations. All WTO Members, including developing countries, are signatories to the GATS. The GATS covers a wide range of service industries, including financial services, transportation, communications, construction, and distribution.

Figure 11-1

World Trade in Services (Export Value Basis)

	Export Value (billion U.S$)					
	1990	**1994**	**1998**	**2002**	**2004**	**2005**
Goods	3,439	4,241	5,422	6,272	8,907	10,159
Services	783	1,038	1,318	1,570	2,125	2,415
Total	4,222	5,279	6,740	7,842	11,032	12,574
Services Percentage	18.5%	19.7%	19.6%	20.0%	19.3%	19.2%

Source: INTERNATIONAL TRADE STATISTICS 2006, WTO Secretariat

2. LEGAL FRAMEWORK

Four Modes of Supply

The GATS covers governmental measures that affect trade in any and all services (excluding services supplied in the exercise of governmental authority). The GATS defines 155 service sub-sectors based on categories developed by the GATT Secretariat, and specifies four modes of trade in services:

1) Cross-border supply (supply of services from the territory of one Member into the territory of another Member);

2) Consumption abroad (supply of services in the territory of one Member to a service consumer of another Member);

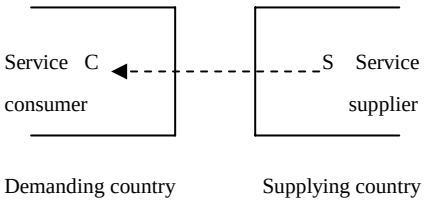
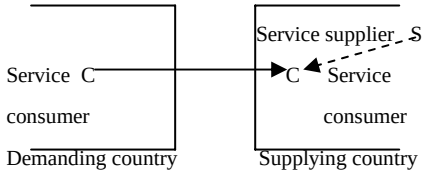
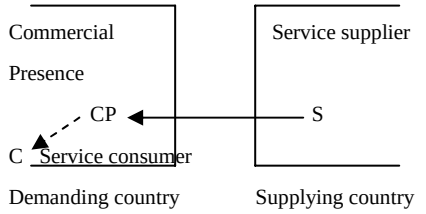
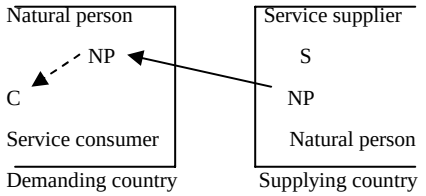
3) Commercial presence (supply of services by a service supplier of one Member through commercial presence in the territory of another Member); and

4) Presence of natural persons (supply of services by a service supplier of one Member through the presence of natural persons of that Member in the territory of another Member.)

(*See* Figure 11-2, below, for a more detailed overview of the four modes.)

Figure 11-2

Four Modes of Trade in Services

Mode	Description	Example	Schematic Diagram
1.Cross-border Supply	Supply of services from the territory of one Member into the territory of another Member (Border-crossing of services)	Receiving legal advice by telephone from a lawyer living abroad.	
2.Consumption abroad	Supply of services in the territory of one Member to a service consumer of another Member (Border-crossing of consumers)	Local consumption by a foreign tourist or businessperson (rental of electronic equipment etc.)	
3.Commercial presence	Supply of services by a service supplier of one Member through commercial presence in the territory of another Member (Border-crossing of commercial presence)	Financial services provided by a foreign branch	
4.Presence of natural persons	Supply of services by a service supplier of one Member through the presence of natural persons of that Member in the territory of another Member (Border-crossing of suppliers)	Invitation of a foreign artist	

Note:Symbols in the Schematic Diagrams

S:Service supplier (natural person or juridical person) ← :movement

C:Service consumer (natural person or juridical person) ⇠ :supply of service

CS:Commercial presence

NP:Natural person

Other Cross-Cutting Rules (GATS Rules, Domestic Regulation)

As shown below, obligations under the GATS include: 1) "obligations which apply to trade in services in all service sectors"; and 2) "obligations regarding trade in services in sectors where specific commitments have been undertaken."

GATS leaves negotiations for providing disciplines on Emergency Safeguard Measures (Article X), Government Procurement (Article XIII) and Subsidies (Article XV) to future, post-Uruguay Round multilateral negotiations. Discussions on these issues have been taking place in the Working Group on GATS Rules established by the Council for Trade in Services in March 1995.

Discipline of Domestic Regulation (Article VI) has also been discussed by the Working Group on Domestic Regulation, established in April 1999.

1) Obligations which apply to Trade in Services in All Service Sectors

(a) Most-Favoured-Nation Treatment (Article II)

Members must accord equal treatment (MFN treatment) to all other Members (*see* Chapter 1 of Part II for a discussion on MFN).

(MFN Exemption)

Trade in services, however, spans a wide range of fields that contain many measures that cannot be subject to MFN treatment for various historical or other reasons. Accordingly, the GATS stipulates that measures may be exempted from the MFN obligation subject to certain conditions, if such measures are registered at the time the GATS enters into force. The Council for Trade in Services shall review all exemptions granted for a period of more than five years. The first such review took place no more than five years after the entry into force of the WTO Agreement (*i.e.,* in 2000). In principle, such exemptions should not exceed a period of 10 years. These exemptions are subject to negotiation in subsequent trade liberalizing rounds.

(Cases in Which MFN Treatment Obligations Do Not Apply Under the GATS Provisions)

- Each Member is not prevented from taking part in an agreement liberalizing trade in services between or among the parties. (Article V)
- Each Member is not prevented from taking part in an agreement establishing full integration of the labour markets between or among the parties. (Article V *bis*)
- Each Member may recognize education, licenses, and certification granted in a particular country as domestically valid. (Article VII)

- Most-Favoured-Nation treatment shall not apply to the procurement by governmental agencies of services purchased for governmental purposes not with a view to use in the supply of services for commercial sale. (Article XIII)

(b) Transparency (Article III)

The lack of transparency in laws, regulations and other measures pertaining to or affecting trade in services may constitute a barrier to trade in services. The GATS, therefore, provides a general obligation to publish all such laws and regulations. This provision is designed to remove any barrier resulting from non-transparent procedures and to facilitate future negotiations on such procedures.

2) Obligations Regarding Trade in Services in Sectors Where Specific Commitments Have Been Undertaken

The GATS requires Members to list in the "Schedule of Specific Commitments" the sub-sector in which it is making a liberalization commitment and the nature of the commitment. The GATS seeks to achieve progressively higher levels of liberalization through successive rounds of negotiations focused on expanding areas and enhancing the content of liberalization.

Under the GATS, Members schedule liberalization commitments by listing the applicable sector or sub-sector (one of the 155 sub-sectors) and mode of supply (one of the 4 modes), and the nature of the commitment. This method -- where a Member identifies those sub-sectors in which it has made a commitment -- is known as a "positive-list" approach (or as a "bottom-up" approach). Members are allowed to add conditions and restrictions in terms of Market Access and National Treatment, where it is considered necessary, to their Schedules of Specific Commitments. They can also make "Additional Commitments" if they consider it appropriate to take on obligations additional to market access and national treatment. (Figure 11-3 contains an example of a Schedule of Specific Commitments; Figure 11-4 contains Specific Commitments of Major Trading Partners and Figure 11-5 contains Overview of MFN Exemption Lists of Major Trading Partners.)

Japan made commitments in approximately 100 sectors and undertaken MFN obligations in all areas without exemptions as a result of the Uruguay Round.

(a) Market Access (Article XVI)

Market access is an obligation whose terms and conditions are determined through specific commitments. Each Member may decide through negotiations to undertake a market access commitment (*i.e.*, a commitment not to maintain or adopt certain measures contained in an exhaustive list in Article XVI) in each sub-sector and mode.

There are six types of measures: (a) limitations on the number of service suppliers; (b) limitations on the total value of services transactions or assets; (c) limitations on total output; (d) limitations on the total number of natural persons that may be employed; (e) measures that restrict the types of legal entity through which a service is provided; and (f) limitations on the participation of foreign capital. Members may maintain some or all of these restrictions, which must then be specified in the Schedule of Commitments as reservations. Member countries may take measures that do not fall within the six types, or which have been reserved, unless they violate other articles in the GATS. The Market Access Article, however, does not ensure specific market access results (in terms of market share or otherwise)

(b) National Treatment (Article XVII)

National treatment is a principle that requires each Member to accord services and service suppliers of any other Member no less favourable treatment than that accorded to its own like services and service suppliers (*See* Chapter 2 of Part II for a discussion on National Treatment). National treatment is an obligation to be determined through specific commitments and each Member may decide through negotiations whether to undertake national treatment commitments in each sector and mode. In undertaking a national treatment commitment, a Member may still maintain some discriminatory measures by making reservations. For example, in undertaking a national treatment commitment in the banking sector, a Member may promise national treatment in all sectors of banking except for deposit operations. Any such reservation must be specified in the Schedule of Commitments.

(c) Additional Commitments

Pursuant to Article XVIII of GATS, Members may agree through individual negotiations to add conditions and restrictions that do not fit in the purview Market Access and National Treatment to their Schedules of Specific Commitments, in the form of "Additional Commitments". This is done where it is considered that active government measures are needed in the service sector in addition to the elimination of measures restricting market entry and measures discriminating against foreign services and service providers. The responsibility to implement these kinds of government measures is not covered by the obligations of market access or national treatment.

(d) Domestic Regulations (Article VI)

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.

(e) Payments and Transfers (Article XI)

A Member may not restrict international payments and transfers for current transactions covered by specific commitments undertaken in the GATS except to safeguard its balance-of-payments (*see* Article XII) or at the request of the IMF. Nothing in the GATS, however, affects the rights and obligations of the Members of the International Monetary Fund under the IMF.

Other Cross-Cutting Rules (GATS Rules, Domestic Regulation)

Article VI.4 aims to prevent procedural matters such as qualification requirements/procedures, licensing requirements/procedures or technical standards concerning the provision of services (e.g. procedures concerning the establishment of financial or construction service companies and acceptance of accountants) from being used as undue trade barriers by avoiding excessive regulations while securing regulatory transparency. To ensure that measures relating to qualification and licensing requirements and the like do not constitute unnecessary barriers to trade in services, the Council for Trade in Services shall, through such subsidiary bodies as it may establish, develop any necessary disciplines. In other words, this article

(a) Emergency Safeguard Measures (Article X)

Article X provided for multilateral negotiations on the question of emergency safeguard measures based on the principle of non-discrimination. The results of such negotiations were supposed to enter into effect on a date not later than three years from the date of entry into force of the WTO Agreement. However, to date the negotiations have not been successful.

(b) Government Procurement (Article XIII)

Article XIII provided for multilateral negotiations on government procurement in services under this Agreement within two years from the date of entry into force of the WTO Agreement. These negotiations have not yet been successful.

(c) Subsidies (Article XV)

Members recognize that, in certain circumstances, subsidies may have distortive effects on trade in services. Article XV provided that Members should enter into negotiations with a view to developing the necessary multilateral disciplines to avoid such trade-distortive effects. These negotiations have not yet been successful.

3) Other Provisions

(a) Negotiation of Specific Commitments (Article XIX)

To further the objectives of the GATS, Members shall enter into successive rounds of negotiations aimed at achieving progressive liberalization of trade in services, beginning not later than five years from the date of entry into force of the WTO Agreement (1 January 1995), and periodically thereafter. The process of liberalization shall take place with due respect for national policy objectives and the level of development of individual Members, both overall and in individual sectors.

(b)Annexes

Annex on Financial Services

Nothing in the GATS prevents a Member from taking measures for prudential reasons and to ensure the integrity and stability of its financial system.

Annex on Telecommunications

Members shall ensure that any service supplier of any other Member is accorded access to and use of public telecommunications networks and services on reasonable and non-discriminatory terms and conditions to supply a service included in its Schedule.

Annex on Air Transport Services

The Annex applies to measures affecting trade in air transport services and ancillary services. The GATS shall not apply to measures affecting a Member's traffic rights, or services directly related to the exercise of those rights, as recognized under existing bilateral agreements.

Annex on Movement of Natural Persons Supplying Services under the GATS

The Annex applies to measures affecting natural persons who are service suppliers of a Member and to natural persons of a Member who are employed by a service supplier of another Member. The GATS shall not prevent a Member from applying measures to regulate the entry of natural persons into, or their temporary stay in, its territory, provided that such measures are not applied in such a manner as to nullify or impair the benefits accruing to any Member under the terms of specific commitments regarding market access, national treatment, and similar issues.

Sector-Specific Rules

GATS provides special rules in separate annexes for specific sectors, such as financial services and telecommunications. For the financial services sector, there is also an Understanding on Commitments in Financial Services that provides more specific details regarding market access and national treatment provisions and that provides for a higher degree of liberalization. For basic telecommunications, there is a Reference Paper discussing interconnection, universal service, public availability of licensing criteria and other aspects of frameworks to promote competition. These additional commitments are attached to many Members' Schedule of Commitments as "Additional commitments" on a voluntary basis. (*See* Annotation 11-2 for the Reference Paper on regulatory frameworks on basic telecommunications.)

Figure 11-3
Example of Schedule of Specific Commitments

Horizontal Commitments

Sector or Subsector	Limitations on market access	Limitations on national treatment	Additional commitments
All sectors included in this schedule	4) Unbound except for measure concerning the entry and temporary stay of a natural person who falls in the following category: i) Activities to direct a branch office as its head.	3) Unbound for research and development subsidies.	

Sector-Specific Commitments

Sector or Subsector	Limitations on market access	Limitations on national treatment	Additional commitments
Services related to management consulting *	1) Unbound 2) None 3) The number of licences conferred to service suppliers may be limited 4) Unbound except as indicated in horizontal commitments	1) Unbound 2) None 3) None except as indicated in horizontal commitments	 **

Modes of supply: (1) cross-border supply; (2) consumption abroad; (3) commercial presence; and (4) presence of natural persons.

Notes

*Sector or subsector, when making liberalization available, shall be inscribed in this column. Articles XVI and XVII shall not apply to sectors or subsectors not indicated in this column.

**Commitments with respect to measures affecting trade in services but not subject to put in the schedule under Articles XVI or XVII shall be inscribed in this column.

Figure 11-4
Specific Commitments of Major Trading Partners

Sectors		US	CH	EU	CA	KR	HK	SG	MY	ID	TH	AU	PH	IN	JP
Business Services	Professional	*	*	*	*	*	*	*	*	*	*	*		*	*
	Computer and related	*	*	*	*	*	*	*	*	*	*	*		*	*
	R & D			*	*	*			*	*		*		*	*
	Real estate	*	*	*	*		*					*			*
	Rental/leasing	*		*	*	*	*		*		*	*	*		*
	Other	*	*	*	*	*	*	*	*	*	*	*		*	*
Communication Services	Postal														
	Courier	*	*		*		*						*		
	Telecommunications	*	*	*	*	*	*	*	*	*	*	*	*	*	*
	Audio-visual	*				*	*	*	*		*			*	*
	Other														
Construction Services	Buildings	*	*	*	*	*		*	*	*	*	*			*
	Civil engineering	*	*	*	*	*		*	*	*	*	*		*	*
	Installation and assembly	*	*	*	*	*		*	*	*	*	*			*
	Completion and finishing	*	*	*	*	*	*	*	*			*			*
	Other	*	*	*	*	*	*	*	*	*					*
Distribution Services	Commission agents	*	*	*	*	*					*	*			*
	Wholesale trade	*	*	*	*	*						*			*
	Retailing	*	*	*	*	*	*					*			*
	Franchising	*	*	*	*	*						*			*
	Other				*										
Education Services	Primary		*	*							*				*
	Secondary		*	*								*			*
	Higher		*	*								*			*
	Adult	*	*	*							*				*
	Other	*	*									*			
Environmental Services	Sewage	*	*	*	*	*					*	*			*
	Refuse disposal	*	*	*	*	*					*	*			*
	Sanitation	*		*	*						*	*			*
	Other	*	*	*	*	*					*				*
Financial Services	Insurance	*	*	*	*	*	*	*	*	*	*	*	*	*	*
	Banking	*	*	*	*	*	*	*	*	*	*	*	*	*	*
	Other														
Health Services	Hospital	*		*					*					*	*
	Other human health											*			
	Social			*											
	Other														
Tourism and travel services	Hotels and Restaurants														
	Travel agencies/Tour operators	*	*	*	*	*	*	*	*	*	*	*	*	*	*
	Tourist guides	*	*	*	*	*	*	*	*	*	*	*	*	*	*
	Other	*		*		*		*			*	*			*
		*													
Recreational, cultural, sporting	Entertainment	*		*					*						*
	News agency	*		*								*			*
	Libraries, archives, museums	*					*	*							*
	Sporting	*	*	*					*		*	*			*
	Other											*			
Transport Services	Maritime transport		*	*		*	*	*	*	*	*	*	*		*
	Internal waterways		*			*	*		*						*
	Air	*	*	*	*	*					*	*	*		*
	Space			*											
	Rail	*	*	*	*						*		*		*
	Road	*	*	*	*	*					*	*	*		*
	Pipeline											*			*
	Auxiliary		*	*	*	*	*				*	*	*		*
	Other			*		*									*
Other services									*						

Notes:

1) Sectors for which liberalization commitments have been made are shown with symbols (*). However, there are many cases in which liberalization commitments cover only a part of the sector or in which measures that are inconsistent with national treatment or that restrict market access are reserved. This table should not, therefore, be interpreted as a direct indication of the level of liberalization. The Secretariat Categories, defining 155 sub-sectors, are more detailed than those in this table.

2) CA:Canada; CH:China; KR:Korea; HK:Hong Kong; SG:Singapore; MY:Malaysia; ID:Indonesia; TH:Thailand; AU:Australia; PH:Philippines; IN:India; JP:Japan.

Figure 11-5

OVERVIEW OF ARTICLE II (MFN) EXEMPTIONS OF MAJOR TRADING PARTNERS

United States	1.Cross-sectoral (measures related to movement of natural persons, taxation measures, measures related to land use, measures of registration by small businesses) 2.Telecommunications services (One-way satellite transmission) 3.Banking services 4.Insurance services 5.Air transport services 6.Space transport services 7.Road transport services 8.Pipeline transport services
EU	1.Cross-sectoral (measures related to movement of natural persons, measures related to land use, measures related to investment) 2.Rental/Leasing services 3.Audiovisual services 4.Insurance services 5.Internal waterways transport services 6.Air transport services 7.Road transport services
Canada	1. Business services (Fishing-related services) 2. Film, video and television programming 3. Insurance services 4. Air transport services 5. Maritime services
Korea	1. Air transport services.
Hong Kong	None

Singapore	1. Cross-Sectoral (Measures related to movement of natural persons, Measures related to investment, taxation measures) 2. Professional services (Legal services) 3. Audiovisual services 4. Banking services 5. Insurance services 6. Air transport services 7. Maritime services
Malaysia	1.Cross-Sectoral (measures related to movement of natural persons, measures related to foreign investment)
Indonesia	1.Cross-Sectoral measures related to movement of natural persons 2.Construction services 3.Banking services
Thailand	1.Professional services (auditing services, publishing newspapers) 2.Maritime services 3.Air transport services 4.Road transport services
Australia	1.Audiovisual services
Philippines	1.Cross-Sectoral (measures related to movement of natural persons, measures related to investment) 2.Banking services 3.Maritime services
India	1.Telecommunications services 2.Audiovisual services 3.Entertainment services 4.Maritime services
Japan	None

Annotation 11-2

Reference Paper: the Regulatory Framework for Basic Telecommunications Services

Scope of Application

These disciplines apply to major suppliers who have the ability to materially affect the terms of participation in the relevant market for basic telecommunications services as a result of control over essential facilities or use of its position in the market.

Competitive Safeguards

Appropriate measures shall be maintained for the purpose of preventing major suppliers from engaging in or continuing anti-competitive practices.

Interconnection to be Ensured

Interconnection with a major supplier will be ensured at any technically feasible point in the network.

Universal Service

Any Member has the right to define the kind of universal service obligation it wishes to maintain. Such obligations will not be regarded as anti-competitive *per se* provided that they are administered in a transparent, non-discriminatory and competitively neutral manner, and are not more burdensome than necessary for the kind of universal service defined by the Member.

Public Availability of Licensing Criteria

Where a license is required, the following will be made publicly available:

(a) All the licensing criteria and the period of time normally required to reach a decision concerning an application for a license; and

(b) The terms and conditions of individual licenses.

Independent Regulators

The regulatory body shall be separate from, and not accountable to, any supplier of basic telecommunications services.

Allocation and Use of Scarce Resources

Any procedure for the allocation and use of scarce resources, including frequencies, numbers and rights of way, will be carried out in an objective, timely, transparent and non-discriminatory manner.

Annotation 11-3

Outline of Japanese Proposal for Energy Services[1]

Importance of Energy Services and Issues to be Considered

Securing an efficient and stable supply of energy is of great importance for achieving economic and social development. In addition, in order to pursue economic growth, it is of prime importance to increase the efficiency of providing energy services, as well as other services.

Regarding rule-making in the energy services sector under the GATS, in order to address the issues of public interest, such as the preservation of energy security, supply reliability, environmental preservation, and the maintenance of universal service and public safety, Member countries should reserve their own rights to adopt regulatory measures which are transparent, competition-neutral and not more burdensome than necessary. The difference in commitments scheduled under the GATS should be justified under such Member's rights.

Furthermore, the possible rules under the GATS for the domestic regulation of the energy services sector should recognize the diversity among Member countries, considering the fact that each country has a different history of energy services (*e.g.*, whether energy services are provided by a state-owned or private provider); rules also should consider the current industrial structure of a Member. However, to the greatest possible extent, rules should be non-discriminatory and should ensure the maximum transparency.

Expectations from the Negotiations

Classification

Japan proposes that, during the current negotiations, development of a new classification for the energy services sector be considered. Such classification should limit itself in scope to the energy services sector and should be developed so as to avoid conflict with existing commitments.

Discussions should comprehensively cover the entire range of energy services, from the wholesale of energy to final consumption by the consumer. An initial focus should be placed on the "core" energy services, namely, wholesale sales, transportation (transmission and distribution of electricity, pipeline transportation and transmission of heat) and retail sales of energy.

Energy services subject to consideration should be energy neutral and irrespective of the energy resources. However, careful consideration is necessary, for energy services

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[1] Japan's Proposal for Energy Services can be found at:
(http://www.meti.go.jp/policy/trade_policy/wto/wto_db/data/energy_pro0110e.pdf)

relating to nuclear power. In addition, Japan proposes to exclude discussions regarding public ownership of natural resources.

Market Access and National Treatment

All Member countries should consider negotiating on market access and national treatment to the greatest possible extent, taking into account the public interest.

The central government (including independent regulators) should ensure that local governments improve market access and national treatment within the market as a whole, in accordance with economic reality.

Japan expects that appropriate consideration will be given to removing barriers affecting the installation of specific materials/equipment for energy services and technical experts knowledgeable about the energy sector.

Review of Regulatory Frameworks

Japan believes that, in the negotiations on energy services, it would be useful to consider the effectiveness of frameworks for domestic regulation, because they contribute to the creation of a competitive environment taking into account the viewpoint of a non-discriminatory, fair and transparent use of the networks.

3. RECENT DEVELOPMENTS

Extended Negotiations

The Uruguay Round negotiations failed to reach agreement on three areas: maritime transport services, financial services and basic telecommunications services. Negotiations on these sectors, including the movement of natural persons (at the request of developing countries), continued after the conclusion of the Round (*see* Figure 11-6). An agreement regarding movement of natural persons was quickly reached in July 1995.

In the maritime services negotiations, the Uruguay Round negotiations included international shipping, auxiliary services such as freight handling, and port usage. Cabotage[2], however, was not included in the negotiation because many countries restricted foreign service providers from domestic shipping. Negotiations on maritime transportation continued, but ultimately were suspended in June 1996, because the United States did not submit an offer. Negotiations in maritime services resumed when the Doha round of service negotiations began in 2000. Countries are under a standstill agreement to maintain their present level of restriction.

Regarding financial services, a provisional agreement was reached in July 1995 and, in December 1997, a full agreement was reached among 70 countries on a Most-Favoured-Nation basis. The 5th Protocol entered into effect and, as of February 2004, had been ratified by 67 countries. As a result, permanent agreement was reached with the United States, EU and with major developing countries in Asia and Latin America.

The initial deadline for basic telecommunications was April 1996, but negotiations were subject to considerable delay. A successful agreement among 69 countries was finally reached on a Most-Favoured-Nation basis in February 1997. The agreement resulted in the signing and entering into effect of the 4th Protocol in February 1998 (which defines the deadline for ratification and the procedures for entering into effect; the additional liberalization commitments made by Members are annexed to this protocol).

The Uruguay Round and Before Seattle

GATS mandates the continued study of several issues without waiting for the start of the new negotiating round.

First, work on establishing disciplines for professional services was started. In professional services, work had begun in the accounting sector, where progress was being made toward standardization. The Working Party on Professional Services focused on establishing "Guidelines for Mutual Recognition Agreements in The

[2] Cabotage often refers to a right granted to foreign carriers and is defined as coastal navigation and trade, especially between parts within a country. *See* Webster's New World Dictionary, 3rd ed. at 194 (1988).

Accountancy Sector" (May 1997) and "Disciplines on Domestic Regulation in The Accountancy Sector," concerning of elimination trade barriers (December 1998). The disciplines included general, abstract and neutral provisions for transparency, licensing requirements, qualification requirements, qualification procedures and technical standards.

Later, in light of the three years that were required just for the accounting sector and the fact that Article VI:4 of the GATS is not limited to professional services only, some argued that a single organization should discuss disciplines for services as a whole, including professional services. This resulted in the reorganization of the Working Party on Professional Services in April 1999 into the new Working Party on Domestic Regulation, responsible for developing disciplines on domestic regulations for services as a whole, including professional services.

Working groups are also studying government procurement, safeguards and subsidies as they relate to services, but major progress has yet to occur. Opinions are especially divided on safeguards; some countries believe that some form of safeguard is needed, while others believe that approval of any safeguard should be subject to strict conditions. As a result, the deadline of the negotiations on safeguards has repeatedly been extended and discussions continue.

In addition, the Committee on Specific Commitments is discussing development of the procedures for the modification of schedules and revision of the current classification. With regard to classification, the committee is studying whether there is a need to revise the current classification, as well as the question of new services, and other issues.

Start of the Services Negotiations

The services liberalization negotiations (Negotiation of Specific Commitments) were mandated by the final agreement of the Uruguay Round and call for entering into successive rounds beginning in 2000(GATS Article XIX); this so-called "Built-in Agenda" also applies to agriculture. Discussions after the Seattle Ministerial Meeting did not progress smoothly. Following over one year of discussions, the "Guidelines and Procedures for the Negotiations on Trade in Services" was finalized in March 2001; it stipulates negotiating goals, principles, scope and modalities.

Later, at the Doha Ministerial Meeting of November 2001, Members decided to include services negotiations as part of a comprehensive round together with other areas. In December 2005 during the Hong Kong Ministerial, the Members agreed on the introduction of qualitative objectives and plurilateral negotiations. They also agreed that plurilateral requests should be submitted by March 2006; revised offers should be submitted by the end of July; and final lists of commitments should be submitted by the end of October. Accordingly, plurilateral requests were submitted in February and March and negotiations began; negotiations were then suspended at the end of July.

Figure 11-6

Framework of the Four Unfinished Areas

	Financial Services	**Basic Telecommunications**	**Maritime Transport Services**	**Movement of Natural Persons**
Present Situation	Concluded 13.12.97 (came into force on 1.3.99)	Concluded 15.2.97 (came into force on 5.2.98)	Suspended in June 1996 (negotiations resumed in 2000)	Concluded 28.7.95 (came into force on 31.1.96)
Present Treatment			Standstill	

4. ECONOMIC ASPECTS AND SIGNIFICANCE

In many developed countries, service industries account for about 60 to 70 percent of the gross domestic production and a similar percentage of the total labour force, making them a vital component of the national economy. Although to varying degrees, this tendency toward a so-called soft economy or service economy is something that can be observed around the world.

Movement of Production Factors

Unlike trade in goods, trade in services is usually accompanied by movement of production factors such as capital, labour, technology and managerial resources. Although trade in services can sometimes be accomplished without any movement of the service provider or consumer, as in the case of cross-border movement of visual and software products, this is rarely the case. Trade in services often requires relocation of the service provider to the place of consumption (*e.g.*, establishment of a business in the country of consumption, or relocation of natural persons to the country of consumption to provide services), or movement of the consumer to the place where the service is provided (*e.g.*, repair of machines abroad, or overseas trips for sight-seeing purposes). In addition, services have another characteristic distinct from that of goods: one cannot hold stock in services.

Since trade in services often requires movement of production factors, including capital, labour, technology and management expertise, liberalization of trade in services will create new relationships among production factors originating in different countries.

The effects on the domestic economy tend to be large, although the degree differs according to the form it takes, such as direct investment and movement of labour.

Direct investment will, in many cases, take the form of market entry of high-quality competitive service providers. Their participation may, in turn, change business practices in the importing country, have a positive effect on efficiency in the service industry there and provide consumers with a wider range of choices. In this case, existing domestic service suppliers would be faced with increased competition and, at times, be subject to merger or be driven out. However, the negative effects on the labour market are often small, and where new services are created, it will have a positive effect.

Movement of labour will have a more direct effect on the labour market. For example, if there is movement of unskilled labour from a low-wage country to a high-wage country, service suppliers will benefit from the use of cheap labour and be able to supply more cost-effective services. On the other hand, foreign unskilled labour will directly compete with domestic unskilled labour. Significant social costs may arise, depending on scale of the movement of labour.

Effects of Increased Efficiency in the Service Sector

We need to keep in mind that most services, such as financial services, transport and shipping, communications, distribution, construction, and energy, are inputs to other industries. Therefore, increased efficiency in a certain service sectors may benefit not only the specific service sector itself, but will often have a greater positive spill-over effect in other service and manufacturing sectors. Benefits of trade in a service sector are not limited to increased efficiency in that specific service sector.

To conclude, although the liberalization of trade in services may result in a short-term selection of some inefficient service providers, it will lead to improved economic welfare for consumers through increased competition over quality and prices. Over the long term, it will contribute to better productivity and competitiveness of service providers not only in the liberalized service sector, but also in industries that use that service as an input. The economic benefits gained from liberalizing trade in services are therefore immense. Thus, even in areas where regulation is required, steps must be taken to ensure transparency, procedural fairness and fair competitive conditions.

5. Major Cases

1) Canada –Measures Regarding Automobiles (DS139, 142)

Canada's preferential measures for wholesale automobile services under the "Auto Pact" violate the most-favoured-nation (Article II) and national treatment (Article XVII) obligations of the Services Agreement (GATS). Japan, together with the EC, contested Canada's auto program before the WTO; the Panel upheld virtually all of Japan's arguments. However, in May 2000, the Appellate Body overturned the Panel ruling, finding insufficient evidence that Canada's program impacted services. Canada, after completing its public comment procedures, issued an administrative order eliminating the preferential measures effective 18 February 2001. (For details, *see* the section on Canadian automobile measures in Part II, Chapter 1, Most-Favoured-Nation Principle.)

2) Mexico –Telecommunication Services (DS204)

Mexico permits several carriers to offer international telephone services, but the international long-distance telephone service regulations mandate "negotiations on interconnection rates with telecommunication businesses from certain countries by the long-distance service licensee that has achieved the largest share in the long-distance telephone market over the 6 months preceding the negotiations." In practice, accounting rate systems for settling interconnection rates with carriers from certain countries are conducted solely by TELMEX (Mexico's telecommunications company), which controls 60 percent of the market; other Mexican carriers merely apply the rates to which it agrees (the so-called uniform accounting rate system). The United States claimed that: (i) this accounting rate system is not based on actual costs; (ii) the system allows exclusive negotiation rights and the uniform accounting rate is unreasonable because it permits the major service provider to engage in anti-competitive activities; and (iii) the practice is contrary to the Reference Paper ("Prevention of Anti-Competitive Practices" and "Interconnection to be Ensured") included by Mexico in its commitment. The United States also claimed that Mexico's policy of prohibiting the use of cross-border exclusive lines violates the duty set forth in the GATS "Annex on Negotiations on Basic Telecommunications," which obligates Members to ensure access to exclusive lines under reasonable conditions. In August 2000, the United States requested WTO consultations with Mexico. In November of that year, the United States requested that a panel be established and again sought consultations with Mexico. The consultations took place in January 2001 and in February 2002. Japan participated as a third-party. A WTO panel was formally established on April 17, 2002. The panel issued its report in April 2004; the report was adopted on June 1, 2004. The panel found against Mexico with respect to the GATS. In accordance with the findings of the panel, Mexico issued revised international long-distance telephone service regulations in August 2004.

3) United States –Online Gambling Services (DS285)

The United States regulates internet gambling services. In March 2003, Antigua and Barbuda requested WTO consultations with the United States claiming that the US regulations violated US commitments to liberalize entertainment services (no restrictions to be imposed on Mode 1: cross-border supply of services), as well as GATS Articles XVI (Market Access), VI (Domestic Regulation), XI (Payments and Transfers) and XVII (National Treatment). Antigua requested the establishment of a WTO panel in June 2003. The panel issued its report on April 30, 2004, and circulated copies to Members in November 2004. The panel found that US federal regulations and state laws violated US market access commitments under GATS Article XVI However, the panel did not make any judgment on the consistency/inconsistency with other articles of GATS. Both parties appealed the ruling of the panel in January 2005, and the Appellate Body found violation of GATS Article XVI on the part of the United States.

The parties were unable to agree on a reasonable period of time for the implementation of the recommendations adopted by the DSB and as a result the period was determined through binding arbitration pursuant to Article 21.3(c) of the DSU. Currently a new panel is considering the existence and/or consistency of measures implemented by the United States to comply with GATS.

Column: GATS – Audiovisual Services

1) Discussion on Audiovisual Services

(a) Discussion during the Uruguay Round

During the Uruguay Round, negotiations were conducted to establish a GATS agreement on audio-visual and other culture-related services. Since these negotiations, opinions on this topic have been divided among countries. The EU, Australia, Canada and other Members argue that, since audio-visual services play an important role in maintaining and developing national languages, as well as in the historical and cultural heritages of peoples, measures for protecting the “cultural value” should be allowed as GATS exceptions. Japan, the United States and other Members oppose this argument, because audio-visual services represent a major area of trade in services and excluding them from the scope of GATS, based on the ambiguous concept of “cultural value”, would be inappropriate. Participating countries in the discussions ultimately agreed that the agreement will not include any provisions that exclude measures required for protecting the “cultural value” from the scope of service trade liberalization; but that the EU and other Members supporting the protection of culture will not make any commitments to liberalize audio-visual services (reservation of commitments to MFN exemption registration, market access and national treatment).

(b) Situation of the Present Round

The EU and other Members still strongly believe that protecting culture is important. On the other hand, the guidelines for negotiations, adopted in 2001, have established that no sector shall be excluded *a priori* from the scope of negotiations. Accordingly, audio-visual services have been included in the present services negotiations. Japan, the United States, Hong Kong, India and other Members interested in audio-visual services have formed the "audio-visual friends" group to discuss this topic with the goal of furthering related Member commitments in light of the aforementioned principle.

(c) UNESCO "Convention on the Protection of the Diversity Cultural Contents and Artistic Expressions"

UNESCO, which oversees issues including the "securing of cultural diversity," adopted the "Universal Declaration on Cultural Diversity" at its 31st General Session in 2001, for the purpose of protecting diverse cultures of the world from the risk of unification because of increasing globalization. At the Johannesburg Summit in 2002, French President Chirac announced his intent to develop the Convention on Cultural Diversity, an international commitment to the Declaration on Cultural Diversity. President Chirac's announcement was based on the belief that the cultures of nations need to be protected under the progress of globalization, because "cultural diversity is threatened by the unification of products, laws and standards, social structure, and lifestyles, as well as the rapid disappearance of languages." The International Network on Cultural Policy (INCP), an informal network among the culture ministries of 53 nations, including France and Canada, independently drafted the Convention on Cultural Diversity.

At its 32nd General Session in October 2003, UNESCO decided to address the preparation of the "Convention on Cultural Diversity" for the purpose of protecting the diversities in "cultural contents and artistic expression" The Convention was adopted at the 33rd General Session in October 2005. According to a statement issued by the UNESCO Secretariat in December 2006, 13 European nations including France, Austria, and Spain newly ratified the Convention. These nations joined the 22 nations including Canada, Mexico, and India that had previously ratified the Convention. The Convention entered into force on March 18, 2007, in accordance with the provision declaring that the Convention will enter into force three months after the deposit of the 30th instrument of ratification.

Japan had participated in the discussion of this Convention, urging the Convention not to be inconsistent with other international instruments such as the WTO Agreements and not to obstruct the free and international exchange and distribution of information and cultures. Attention should also be paid to the implementation of the Convention after it comes into force.

2) Regulations in Individual Countries

In addition to the EU measures discussed in Part 1, important regulations on audio-visual services maintained by other Members are described below.

(a) Australia

In Australia, licensed television broadcasting companies must meet requirements on the minimum number of airing hours for programs produced in the country, as well as on the corresponding numbers for programs of various kinds.

(a) Regulations on television broadcasts and commercials

· Regulations on television broadcasts

Under the "Broadcasting Services (Australian Content) Standard 2005," commercial television broadcasting licensees must broadcast Australian programs for 55 percent of broadcasts between 6:00 and 24:00 and must meet quotas on hours broadcast of different genres (dramas, documentaries, children's programs, *etc*.).

· Regulations on television commercials

Under the "Australian Content Standard in Advertising (TPS) 23," Australian-made commercials must account for at least 80 percent of all commercials aired.

(b) Broadcasting Services Act 1992

On October 18, 2006 the "Broadcasting Services Amendment (Media Ownership) Bill 2006," an amendment to the "Broadcasting Services Act 1992," was passed by the House of Representatives (it was passed by the Senate on October 12), thereby lifting restrictions on foreign investment and cross-media ownership. The limits on share holdings of media companies by foreign investment were also lifted and now require only prior approval by the Finance Minister (a determination of whether or not such action opposes the national interest).

< Existing foreign investment restrictions >

· Percentage of shares of a commercial television network not to exceed 15 percent for an individual (total foreign investment less than 20 percent).

· Percentage of ownership of a pay television network not to exceed 20 percent for an individual (total less than 35 percent).

· Percentage of ownership of national newspapers and metropolitan newspapers less than 25 percent for an individual (total less than 30%), and less than 50% for regional newspapers.

Furthermore, this removes the current ban on cross ownership of media markets (excluding pay television broadcasts) and makes it possible for one company to own multiple television, radio, and newspaper outlets in a single area (with the condition that more than five media outlets in metropolitan areas and more than four media outlets in regional areas remain).

(b) Canada

In order to protect its cultural industries, Canada has adopted measures for protecting its businesses related to books, periodicals, movies, videos, music and broadcast. Underlying these measures is Canada's concern that these businesses, exposed to fierce competition from its neighbor, the United States, may eventually be controlled by the latter due to Canada's cost disadvantages. The measures are aimed at preventing the country from losing its national identity as a result of such development.

In 1999, the Canadian government transferred the responsibility to screen foreign capital investment in cultural industries from the Canada Investment and Guarantee Agency to the Department of Canadian Heritage. The Canadian Heritage Minister has adopted systems to diversify Canada's cultural contents in movies, videos, audio contents, books and magazines, as well as policies to direct content distribution.

Column: GATS and the "Movement of Natural Persons"

1. Background to Negotiations at the Uruguay Round

During the Uruguay Round negotiations a request was made by developing countries which were trying to secure the freedom to allow the labor population of their countries to enter developed countries to add "transboundary movement of natural persons" as a fourth mode to the existing three modes of trade in services. (The existing Modes of Trade in Services were: 1, "cross-border service supply"; 2, "cross-border consumption"; and 3, "movement of production factors.") Developed countries responded that they would accept a discipline of "movement of natural persons" in the Agreement, (to be known as "Mode 4," or "movement of natural persons") as foreign capital and the advancement of workers go hand in hand with trade in services.

However, developed countries opposed Mode 4 because the liberalization of "labor movement" would require changes to immigration policy.

Simply establishing a discipline for the "movement of natural persons" does not guarantee liberalization due to the exception of some general rules, the level of liberalization is left to the commitments of individual countries, is the same as for other Modes. Developed countries attempted to make a commitment on intra-corporate transfers (the movement of an employee between the head office in a foreign country and a domestic subsidiary), but this proposal did not have any merit for developing countries, where the majority of businesses lack the capacity to have a foreign base of operations. Developing countries argued that natural persons, who lack a base of operations, should be accepted when hired on a contractual basis by a foreign business.

This gap between developed and developing countries was not able to be bridged by the end of the Uruguay Round. Negotiations on the "movement of natural persons" continued, linked with "financing." As a result of these negotiations, the "Annex on Movement of Natural Persons," an annex on the movement of individuals that recognizes the authority of Members' immigration controls and the applicable range of Mode 4, was adopted as an inseparable part of the GATS on July 21, 1995 and went into effect January 31, 1996. On July 28, 1995, a group of Member countries including Australia, Canada, and India revised their schedules of commitments to include such elements as additional categories of commitments and an extension of the permitted duration of stay under Mode 4.

2. GATS Rules

The scope of the "movement of natural persons" in GATS is defined by Article I: Scope and Definition, and by the "Annex on Movement of Natural Persons."

Article I defines the "movement of natural persons" as the supply of a service "by a service supplier of one Member, through presence of natural persons of a Member in the territory of any other Member."

The "Annex on Movement of Natural Persons," recognizes the right of Members' immigration control measures, allowing Members to apply "measures to regulate the entry of natural persons into, or their temporary stay in, its territory." However, it does not apply to "natural persons seeking access to the employment market of a Member," that is to say, measures affecting workers who move to seek employment, nor does it

apply to "measures regarding citizenship, residence or employment on a permanent basis."

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

1. This Annex applies to measures affecting natural persons who are service suppliers of a Member, and natural persons of a Member who are employed by a service supplier of a Member, in respect of the supply of a service.

2. The Agreement shall not apply to measures affecting natural persons seeking access to the employment market of a Member, nor shall it apply to measures regarding citizenship, residence or employment on a permanent basis.

3. In accordance with Parts III and IV of the Agreement, Members may negotiate specific commitments applying to the movement of all categories of natural persons supplying services under the Agreement. Natural persons covered by a specific commitment shall be allowed to supply the service in accordance with the terms of that commitment.

4. The Agreement shall not prevent a Member from applying measures to regulate the entry of natural persons into, or their temporary stay in, its territory, including those measures necessary to protect the integrity of, and to ensure the orderly movement of natural persons across its borders, provided that such measures are not applied in such a manner as to nullify or impair the benefits accruing to any Member under the terms of a specific commitment.

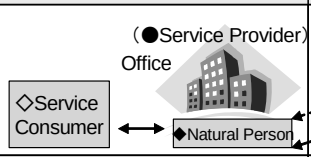
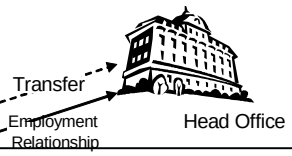
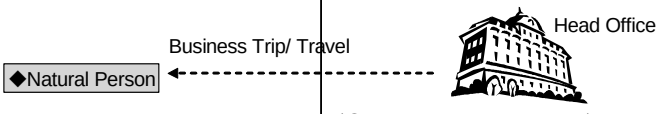
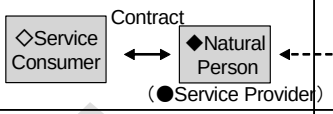
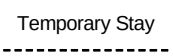
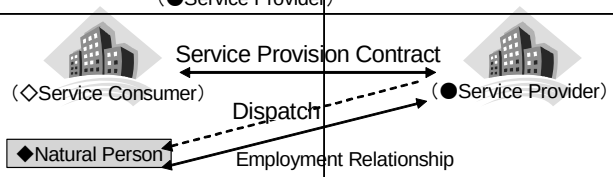
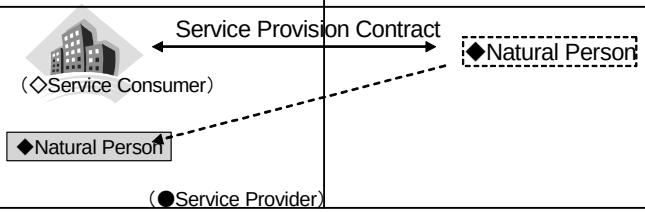
(2) Outline of Disciplines

Mode 4 places the same obligations on all categories as other modes: (a) "Most-Favoured-Nation Treatment" (GATS Article II); (b) "Transparency" (GATS Article III); and (c) securing of tribunals or procedures for administrative decisions (GATS Article VI, Paragraph 2). In addition, it places on Members the obligation for commitment details based on GATS Article XVI: Market Access and Article XVII: National Treatment.

(3) Commitment Methods of Individual Countries

The “movement of natural persons” was included in GATS during the Uruguay Round. However, as was detailed in “1. Background to Negotiations at the Uruguay Round” above, the actual level of recognition is determined by each Member individually in its Schedule of Commitments. The majority of countries have not determined Mode 4 commitments for individual service sectors, but have established comprehensive provisions in a table of “horizontal commitments,” the main types of which are described below.

Main Types of Horizontal Commitments

Main Types of Horizontal Commitments		Consumer Country	Source Country	Examples
Intra-Corporate Transferees: ICT				CEO, Manager, Professional Engineer
Business Visitors: BV				Business negotiations (no activity receiving compensation at that time)
Independent Professionals: IP				Independent lawyer who enters foreign country through contract with foreign consumer
Contractual Service Suppliers	Contract between corporations			Computer engineer employed by corporation dispatched to Japan via contract between corporations
	Contract between a corporation and an individual			Independent computer engineer who enters Japan via contract between corporation and individual

Following the Uruguay Round, Japan made horizontal commitments for three categories under Mode 4: (1) intra-corporate transferees; (2) self-employed service providers; and (3) business visitors.

1. Intra-corporate Transferees

A natural person who, for a period of more than one year immediately preceding the date of entry into Japan and application for temporary stay, has been employed by a corporation of a Member other than Japan and will be transferred to a Japan office of the same corporation for no more than five years, is permitted the following activities: (1) managing a branch office as the manager; (2) managing the corporation as a senior executive or auditor; (3) managing one or more corporate departments; (4) physics, engineering, and other natural science activities that require high levels of technical expertise and knowledge; and (5) law, economics, business administration, accounting, and other humanities activities that require a high level of knowledge.

2. Business Contact (Business Visitors)

Business contacts (including negotiations for the sale of services) and other related activities are allowed for a period of up to 90 days. However, this is based on the conditions that: (i) no compensation is received within Japan; and (ii) that neither direct sales nor direct provision of services are rendered to the general public.

3. Self-employed Service Providers (Independent Professionals)

A natural person who, for a period of more than one year immediately preceding the date of entry into Japan and application for temporary stay, has been employed by a corporation of a Member other than Japan and will work in Japan for no more than five years, is permitted to provide the following services: lawyer, foreign lawyer licensed in Japan, patent agent, marine procedure commission agent, certified pubic accountant, and licensed tax accountant. However, necessary qualifications be met. For instance, a “lawyer” is required to have received qualification to be a lawyer in Japan and also be licensed as a lawyer in Japan.

Japan’s Immigration Control and Refugee Recognition Act outlines the requirements to issue visa status; however, Japan has the right to implement relevant measures for immigration control, even in instances where such a right is not expressly reserved, provided that benefits rendered to Members from special commitments are not negated and there is no damage.

Column: E-Commerce-Main Points of Discussion

1) Main Points in WTO Discussion on E-Commerce

E-commerce has prompted WTO discussions over its relationship with existing WTO agreements because it symbolizes a new form of trade which frequently involves cross-border transactions. Specific areas being discussed are as follows:

(a) Handling of Digital Content Under Current Agreements

E-commerce is bringing substantial changes to the distribution structures for goods and services. The change does not remain in electronic processing of contracts and settlement of accounts; digital content lends itself to on-line distribution and, as a result, a market for international distribution is growing.

In the context of trade, the question is how to discipline on-line cross-border transactions of digital content within the context of the WTO.

The EU asserts that electronic commerce is a service activity and, from the standpoint of technical neutrality, should be disciplined only by the GATS. Digital content as well should be recognized as a form of service trade similar in nature to the programming content of broadcasting services.

Japan's position on this issue is that in cases where recording and cross-border transactions of digital contents through carrier media, for example paper or diskette form, fall within the coverage of GATT disciplines, it is appropriate that the same digital contents transmitted through the Internet should also be granted GATT-level treatment, *i.e.*, unconditional application of MFN, national treatment and the general prohibition of quantitative restrictions. The US similarly argues that, in discussing disciplines on digital content, it is essential to keep in mind the need to develop electronic commerce instead of restricting it via the narrow confines of the GATT or GATS. The US also argues that those disciplines should not reduce the level of market access currently enjoyed. Japan is wary of the EU's position that electronic commerce should be governed entirely by the GATS. The United States argued that, if governed exclusively by the GATS, the rapidly developing e-commerce field could be subject to the most-favoured-nation exemptions and reservations of market access and national treatment obligations that the EU has invoked for the 155 service sectors (particularly cinema, broadcasting), primarily for cultural reasons. It is essential to assure basic WTO principles such as most-favoured-nation and national treatment for the distribution of digital content.

(b) Taxation of Electronic Transmissions

Digital content that used to be delivered in physical form on floppy disks and CD-ROMs is increasingly being delivered on-line across national borders. The main problem in attempting to tax these cross-border transactions is that it is almost impossible for customs agencies to monitor them. If one attempts to tax the means of electronic transmission (for example, the transmission log) as a substitute, one runs the risk of imposing taxes far in excess of the value of the content because it is impossible to value the digital content itself separately from the means of transmission.

In addition to these difficulties in collecting customs duties on electronic transmissions, there is also the need to ensure a free trading environment to foster the growth of e-commerce. This has led many to support the establishment of an international agreement not to impose custom duties on electronic transmissions.

At the Second WTO Ministerial Conference of 1998, Members agreed to a "Ministerial Declaration on Global Electronic Commerce" that promised to maintain the current practice of not imposing customs duties on electronic transmissions until the next Ministerial Conference (1999). However, when physical goods are moved, ordinary tariffs apply. The impasse at the Third Ministerial Conference in 1999 delayed agreement on the handling of the taxation moratorium. The Fourth Ministerial Conference in Doha, Qatar in November 2001, however, officially announced that the moratorium would be extended until the Fifth Ministerial. Although the September, 2003 Fifth Ministerial Conference in Cancun collapsed and the taxation moratorium was not extended, parties agreed during the July 2004 General Council meeting that the moratorium would be extended until the Ministerial Conference in Hong Kong scheduled for the end of 2005. After that the Sixth WTO Ministerial Conference declared that Members would maintain their current practice of not imposing customs duties on electronic transmissions until the next Session of the Ministerial Conference.

(c) Fiscal implications of e-commerce.

It is difficult in electronic commerce to identify where goods are produced and consumed. This raises the question of how to harmonize electronic commerce with traditional concepts and practices in state taxation. Developing countries have expressed concern that the expansion of electronic commerce will lead to a reduction in state tax revenues. In order to convince developing countries otherwise, it is necessary to study the positive effects that the promotion of electronic commerce will have on national economies as a whole and on the negative impacts that may be seen in state tax revenues.

(d) Japan's Effort

The development of concrete rules will be crucial in facilitating the further evolution of e-commerce and the creation of an internationally harmonized e-commerce environment. Recognizing this, Japan has participated actively in WTO discussions on e-commerce. The Ministry of Economy, Trade and Industry (the former "Ministry of International Trade and Industry") issued its first proposal in June 2000, a second in October and a third in June 2001 to identify and stimulate discussion on key issues for consideration in relation to e-commerce and the WTO. The paper is available on the Ministry of Economy, Trade and Industry website at:

http://www.meti.go.jp/policy/trade_policy/wto/wto_db/html/ec_pro0010e.html.

Summary of Japan's proposal is as follows:

- Basic Concept

E-commerce is a powerful tool in the future world economy. It has the ability to alleviate the international gaps in information and to help achieve a global "eQuality". The term "eQuality" implies a strong faith in the absolute necessity of "equality" and "quality of life" for people living in the information society. The ideas expressed in the "eQuality" proposal are based on the principles and concepts founded in the "Okinawa Charter on Global Information Society" issued by the Kyushu-Okinawa Summit in July 2000, and on the Basic Law on the Formation of an Advanced Information and Telecommunications Network Society (IT Basic Law) that took effect in January 2001. The proposal attempts to balance three sets of competing interests.

The first is the balance between the interests of enterprises and the interests of consumers. We seek to ensure "eQuality" in the information society of all countries, and we must take care that corporate activities do not harm the interests of consumers. WTO members should take into consideration the viewpoints of both consumers and the industries when they formulate and implement policies.

The second is the balance between developed and developing countries. It is vital that we provide reliable, stable networks at a global level so that both developed and developing countries have the opportunity to expand their e-commerce opportunities. As we make the transition to an information-centered society, liberalization and facilitation alone will not be enough. We must create consistent environments that accommodate different social and cultural circumstances, and we must build capacity in developing countries so that both developed and developing countries enjoy "eQuality".

The third is the balance between liberalization and rules. Liberalization in the network economy invigorates economies by enabling corporate activities to expand internationally. On the other hand, there are justified fears that the information economy may give rise to an international oligopoly of global companies. Enjoying the benefits of liberalization is predicated upon fair competition in liberalized markets. Rule-

making is also vital to the building of a vigorous, active cyberspace, because people must be able to participate in market environments with full confidence that they will work. Thus, there must be a balance in the legal environment between promotion of the liberalization of e-commerce and the maintenance of necessary consumer protection and order.

- Main points raised in Japan's proposal

The establishment of the "E-commerce Committee"

To take these considerations a step further, Japan proposed the establishment of an "E-commerce Committee" (provisional title) under the auspices of the General Council. The new Committee should follow the progress of negotiations at the various Councils, providing guidance to them where appropriate, while also conducting its own considerations centered on cross-cutting issues beyond the mandates of individual Councils.

Trade Liberalization of E-Commerce-related Sectors

As borderless e-commerce entails the cross-border provision of telecommunications, settlements, distribution and other related services, market access also needs to be secured for these related services.

From the perspective of promoting the liberalization of trade in services closely related to borderless e-commerce, Japan supports the idea of selecting certain services as the "e-commerce cluster".

Consideration of domestic regulatory principles

The development of e-commerce makes it easier for companies to participate in markets in a number of countries, but also underscores issues related to domestic regulation. States continue to introduce a range of domestic regulations to achieve their respective policy goals, and these domestic regulations could potentially obstruct cross-border e-commerce and restrict trade.

It is desirable that domestic regulations in different countries be unified and minimized so as not to impair the development of e-commerce., Objectivity, transparency and necessity (*i.e.*, "no more burdensome than necessary") in domestic regulations related to e-commerce should be ensured as domestic regulatory principles. It is important to work toward the formation of additional principles and the criteria for determining them in light of the principles mentioned above.

Capacity Building of Developing Countries

The WTO and its Members should consider assistance to developing countries so that the benefits of e-commerce are spread equally to them. Specific forms of cooperation might include technology cooperation, infrastructure creation, sharing of information and experiences through close policy dialogues, and cooperation using regional frameworks like APEC.

The full paper on e-commerce is available on the Ministry of Economy, Trade and Industry website at: (Japanese only)

http://www.meti.go.jp/policy/trade_policy/wto/wto_db/html/ec_pro0106j.html

2) Background of WTO Discussion

The background of WTO discussions on electronic commerce is as follows:

(a) Adoption of Ministerial Declaration on Global Electronic Commerce

At the second WTO Ministerial Conference (the Geneva Ministerial Conference) in May 1998, ministers adopted a "Ministerial Declaration on Global Electronic Commerce." The Declaration paved the way for the formulation of a work programme for the consideration of all trade-related aspects of e-commerce and instituted a moratorium on the taxation of electronic transmissions.

(b) Creation of Electronic Commerce Working Programme

The work programme was created in October 1998 in response to the May 1998 declaration from the Second WTO Ministerial Conference. Subsidiary bodies (the Council for Trade in Goods, Council for Trade in Services, Council for TRIPS, and Committee on Trade and Development) discussed these issues through July 1999 and reported their findings to the General Council

(c) Suspension and Re-Opening of The E-Commerce Work Programme

The E-Commerce Work Programme had, for all intents and purposes, been suspended since the collapse of the Seattle Ministerial Conference in October of 1999. However, high demands for liberalization and rule formulation for rapidly developing e-commerce-related sectors, spurred the General Council to announce the resumption of the Work Programme in July 2000, nearly six months after its suspension at the Seattle Ministerial. While various WTO subsidiary organizations are addressing individual e-commerce issues, Japan and other WTO Members have come to recognize that many issues regarding the impact of e-commerce on WTO disciplines require crosscutting consideration beyond the capacity of these organizations. Subsequently, it was decided to hold a dedicated discussion on e-commerce in June 2001 as an arena for intensive discussion among experts on crosscutting issues. Presently, the WTO is considering the establishment of a taskforce on e-commerce to develop a broad understanding of the

impact that it will have on WTO disciplines (the impact on trade in goods, services and intellectual property, etc.).

(d) Fourth WTO Ministerial Conference

The Fourth WTO Ministerial Conference adopted a Ministerial Declaration. It was agreed to continue the moratorium on taxation of electronic transmissions until the Fifth Ministerial. Members also agreed to continue the Work Programme on Electronic Commerce and instructed the General Council to consider the most appropriate institutional arrangements for handling the Work Programme and to report on further progress to the Fifth Session of the Ministerial Conference.

(e) Discussions after the Doha Ministerial Conference

After the Doha Ministerial Conference, electronic commerce issues were examined principally in the dedicated discussion under the General Council. At the second meeting (May 2002) and thereafter, discussions on classification issues and fiscal implications have continued. Along with other countries, Japan actively contributes and has submitted a paper outlining its cooperation in IT areas from the perspective of development. Since a seminar under the auspices of the Committee on Trade and Development was held in April 2002, developing countries were interested in these issues. As a result of Members' efforts and intensive discussions, developing countries gradually understand the importance of promoting electronic commerce.

Also, the United States proposed that Members seek to reach an agreement on basic principles for the further development of electronic commerce (assurance of free trading environment, expansion of market access, permanent moratorium on custom duties, etc.). This idea was broadly supported by developed countries.

Moreover, parties agreed during the July 2004 General Council meeting that the moratorium would be extended until the Ministerial Conference in Hong Kong in December 2005.

(f) Sixth WTO Ministerial Conference in Hong Kong (December 2005)

The Sixth WTO Ministerial Conference declared that Members would maintain their current practice of not imposing customs duties on electronic transmissions until the next Session of the Ministerial Conference. Members took note that the examination of issues under the Work Program on Electronic Commerce was not yet complete, and they agreed to reinvigorate that work, including development-related issues and discussions on the trade treatment of electronically delivered software.

EU Value Added Tax (VAT) on Electronically Distributed Services

The EU adopted an amended Directive VAT (2002/38/EC) in May 2002, requiring non-EU companies selling digital contents to EU consumers to collect a VAT based on the country in which the consumer resides. EU members had to implement the directive by July 2003. Almost all Members have completed domestic legislation.

Under the directive, for transactions between non-EU businesses and EU consumers, companies will be required to register with a VAT authority in any one EU member state of their choice, and to levy a VAT at the rate applicable in the member state where the consumer of the service resides (place of consumption). On the other hand, for transactions between EU businesses and EU consumers, the companies charge a VAT at the location where the supplier of the service is established when making sales to the final consumer (country of origin approach). There are concerns that non-EU companies with no establishment in the EU will face more onerous administrative and compliance costs than EU companies, because they would have to verify the locations of all purchasers and charge the appropriate VAT rate.