

Brussels, 20 September 2002

## **ESF Position Paper on the desirability of Emergency Safeguard Measures in the GATS**

### **INTRODUCTION**

After the Doha conference the schedule of the GATS negotiations essentially focus on the request and offer procedure.

This does not mean that the discussion on main horizontal issues like for instance Emergency Safeguard Measures (hereafter ESM) does not continue in the WTO Working Party on GATS Rules.

In view of the importance of these horizontal issues, ESF welcomes the postponement of the deadline to 15 March 2004. This will provide more time for Members to find a balanced solution to the complicated issue of ESM and to initiate proper discussions on multilateral negotiations on public procurement in services in the Working Party. The ESF does nevertheless regret that the issue of ESM is not an integral part of the GATS and WTO single undertaking negotiations. Such inclusion would provide more pressure to achieve results.

The ESF has already submitted a substantial position paper on ESM in 1996. This position was further updated and enhanced in 1999. This paper does not change the positions presented in these earlier papers, they remain as valid as ever. The previous ESF papers did however, not deal with the question of desirability or feasibility of ESM. This paper does.

Given that the talks on this matter have been going on in Geneva since 1994 - and even earlier during the Uruguay Round - without producing any tangible results or progress, ESF decided that it was time now provide an impetus to the discussions by conveying the view of the European services industry on the desirability of such a mechanism.

ESF will remain vigilant on this issue and will revert to this matter, whenever required by the progress of the discussions.

### **SAFEGUARDS ARE AGAINST GATS BASIC PRINCIPLES**

The main goal of the ESF is the furthering of its members interests in the GATS negotiations and the strengthening of the Community's negotiating position in WTO to achieve those interests. The Services organised in the ESF basically wish to promote successful consecutive rounds of services negotiations in WTO.

The European service providers represented in the ESF find no reason why the GATS should be burdened with Emergency Safeguard Measures (ESM) at all. The whole concept of ESM goes against the basic framework of the WTO/GATS and the possible scenarios that ESM are supposed to protect against are already well catered for in the fabric of that framework.

### **SAFEGUARDS WILL BE COUNTER-PRODUCTIVE**

Moreover, analysis shows that at best ESM is a double-edged sword. While providing the proponents with the illusion of a comforting safety break in case of political necessity or expediency, it will very likely have the opposite effect and may actually ensure that a country claiming for such protection will in practice see that the benefits of the WTO/GATS process will not materialise because of the threat of such a mechanism.

At worst, ESM can be used as a legal cover to enable some WTO countries to re-introduce barriers through the back door and to renege on agreed commitments. Should this happen to any considerable extent the whole structure of the WTO/GATS framework would be in jeopardy. That would be unacceptable.

One of the key words for the service industries is legal certainty and thereby investment protection. ESM provide a potential danger for investments. Thus, services providers would as much as possible prefer to choose to invest in countries where such a risk does not exist. We encourage the European Union services negotiators to disseminate this important message from the service industry.

It should also be kept in mind by the proponents of setting up a Safeguard Mechanism for services, which are mainly from Developing Countries, that ESM increasingly represents a tempting instrument for Developed Countries also. Therefore an instrument originally seen by some Developing Countries as a protection against possible over-presence of foreign service suppliers from Developed Countries in their market might be implemented against their national service suppliers trying to get access to Developed Countries and equally to other Developing Countries services markets (obtained through GATS commitments!).

## **ARTICLE XII GATS: AN EXISTING SAFEGUARD FOR MACRO-ECONOMICAL DIFFICULTIES**

An additional consideration that needs to be taken into account is the fact that Article XII of the GATS provides the necessary general legal tool to allow trade restrictions to safeguard the Balance of Payments, in order to ensure at macro-economic level the possibility for such a requesting country to implement its programme of economic development or economic transition. Thus, an adequate instrument to deal with major economic imbalances is already provided for.

## **SAFEGUARDS NEED TO BE SPECIFIC**

ESM are traditionally seen as instruments that are used only for sector specific application. It seems that many WTO Countries, in particular the so called "Developing Countries" and the "Least Developed Countries" (LDC), which are favoring ESM consider its application in a sector specific setting that would potentially have macro-economic effects. But when analysing this possibility, ESF members fail to clearly identify concrete examples of situations that would possibly justify such a specific ESM. Sector specific ESM application with such macro-economic implications could be possibly envisaged in the energy supply services, but hardly anywhere else.

Also, it must be noted that – unlike in the area of goods - in the area of services, there is often an absence of reliable data (customs data or credible and disaggregated data for all the various service sectors). This would make it very difficult to establish a link between imports and damage to a specific domestic service sector and would both make it impossible to make a well-founded assessment of the effects (both beneficial as negative) of any ESM and the correct administration of such ESM once implemented.

## **NEED FOR A BUSINESS CASE**

There is first a clear need to identify already existing cases where such a mechanism might have been implemented, or at least to identify theoretical well-described potential credible cases. Such cases should be deeply analysed within the Working Party on GATS Rules, as to measure the potential benefits and potential negative effects. As far as the European service industries are concerned, and after thorough investigation, we have not be able to identify such a case.

It is to be noted that Article X of the GATS, which is the basis for the current multilateral talks on the question of ESM, specifies the procedure to be followed in case of necessity/emergency before the end of the negotiations (at that time, planned for three years). It allows, as stated in Paragraph 2, any WTO member to notify the CTS of its intention to modify or withdraw a specific commitment after a period of one year from the date on which the commitment enters into force. Paragraph 3 stipulates that this possibility shall cease to apply three years after the entry into force of the WTO agreement, i.e. July 1998. Given that the discussions on ESM are still ongoing, it is not clear whether this procedure is still valid. One should however underline that, to our knowledge, there is no country that has used this possibility for any of the hundreds of GATS commitments taken in 1994 and after. This is, in our view, already a strong case to show that ESM for services are not really necessary given that a much more radical measure – which is to withdraw the commitment without any compensation – has never been implemented.

The ESF is aware that, for political and psychological reasons, some Developing Countries need the adoption of an ESM Mechanism in the GATS in order to gain national support for/approval of the concessions they might make under the WTO/GATS to their constituents (Parliament, national industry, trade unions, etc.). We also hear the argument that the comforting thought that there is the possibility of an emergency brake might also help convince those countries to make more substantial commitments in their GATS schedules. ESF remains to be convinced by such arguments and by the fact that such an instrument, if any, would be applicable and would reach the objectives it had been set for. ESF urges the WTO members not to take the doubtful and dangerous path of adopting an International Trade Instrument that everybody would hope would never be implemented against itself but that they accept "just in case". A strong business case should be presented first.

## POTENTIAL EFFECTS THROUGH CROSS-MODAL APPLICATION

As an interested party in this reflection on ESM, the European Services Forum presents to you its own first attempt towards an analysis of the potential effects of implementation of an ESM in each of the four different modes of supplying a service.

As a **preliminary remark**, it is important to emphasise the fact that, contrary to safeguards applied to goods (which can be stopped at the border by the custom officials), it is not so easy to apply a safeguard measure to services. When a service company decides to do business abroad, it has four different modes to choose, depending on the domestic legislation on the hosting targeted country. The preferred (and often only allowed) mode is by setting up a presence in the host country (mode 3). This means that in the very large majority of the cases, the company management has decided to make a long-term investment and that its foreign presence will become part of the domestic economy of the host country and will reinvest its own profits in this country, and even often will be registered as local company (in case of joint-venture or subsidiary).

i) When one considers the application of ESM to the different modes of supply for services, it is difficult to envisage any successful application of ESM to **Mode 1 (cross border supply of services)**. Enforcement is the problem. It is physically very difficult to stop services like banking, insurance, marketing, IT and Computer services, management consulting, etc. in this age of modern information technology, without immediately resorting to the full instruments of a totalitarian state.

Obviously, for transportation services or any services with an actual physical need to cross borders (air transport, maritime transport, express delivery services, postal services, etc.), there are indeed possibilities to apply ESM on this mode. In case of problems for a national operator, certain Members might be persuaded to close the border to foreign transportation (mainly road, inland waterway, maritime and of course air transport) either totally or partly, or impose severe limitations.

Still, there are severe drawbacks to applying ESM on Mode 1 in transportation. Many countries are dependent on the availability of sufficient import/export capacity. Such measures may help the national/local service provider(s), but may scare away vital foreign service capacity. Moreover, it would severely hurt the users of the service in question and possibly even the general economic well-being of the country. The ability to implement ESM's in Mode 1 might also have a negative influence on the willingness of major trade blocks to even consider commitments on cross-border transport services to the detriment of small and medium companies from Europe and more importantly from Developing countries.

ii) The same enforcement problems would apply to **Mode 2 (consumption abroad)**. It would indeed be difficult to envisage, except once again for totalitarian countries, to prevent citizens from traveling abroad to consume tourism services, education services or health services. It is also difficult to find out what would be the specific purpose of such an ESM.

iii) The use of ESM in the case of **Mode 3 (commercial presence)** is more technically conceivable. However, practical implementation might reveal to be difficult.

**What would be the consequences of ESM to the targeted companies?** There is an easy answer for the new entrants. They will simply be denied access to the country, by not obtaining the required license or necessary authorisation. But if the measure applies only to the new

entrants, it will unfairly benefit the foreign companies already set-up. The Safeguard Measure should only apply to foreign companies, but to all foreign companies alike, according to the MFN clause...

**What is a foreign company in the services area?** Should the ESM target all joint ventures, subsidiaries and branches? Or only the branches of foreign companies? Or only the branches plus the joint ventures and subsidiaries where the foreign partners have the majority shareholdings? To apply such measures will be very difficult. It will also be totally unfair and discriminatory for these local partners who decided to merge their strengths with a foreign partner's so as to take advantage of their experience and know-how and to develop further.

However, since most of the countries that wish to obtain ESM at this stage wish also to attract investments, the application of such an instrument would be highly detrimental to achieving such a goal. Investors need to be sure that their investments are safe. The GATS rules and the GATS commitments were offering this legal certainty, but any application of ESM would mean that such favourable investment conditions are jeopardised.

iv) Finally, the use of ESM as regards **Mode 4 (movement of natural persons)**. Here, clearly, an application would be easy to implement and enforce. It is easy to stop delivering business visas, and to stop natural persons who want to do business legally at the border. Intra-corporate transferees, business visitors and other professionals who want to openly provide their services in a country that wants to apply ESM in a particular services sector are easily identifiable.

However, one has to wonder **why would it be necessary to implement such an ESM measure on mode 4 and would it be efficient?** Mode 4 is a mode of supply that is often used by the professional services sectors, given that "their product is their staff", i.e. the supply of the service is done by a person with a particular expertise and qualifications.

Let us imagine a case where a country – which has previously opened its market through its schedule of commitments - feels that its national accountancy services sector or legal services sector, or architectural services sector, is under threat of disappearing because of a overly strong foreign presence. To prevent the entry to the territory of new professionals (who most of the time come on a temporary basis) is not likely to rebalance the situation. Action on Mode 3 might be more appropriate, but see above. And this will not prevent the customers in the applying country to ask their (possibly long standing relation) regular (foreign) professional services provider to continue to provide services via mode 1 (see above).

However, if admitted that ESM on Mode 4 might provide an instrument for those countries that would desire to limit the number of professionals or workers entering, it is not unlikely that Developed countries would also be interested in using such a tool to the detriment of the Developing countries, which are strong "demandeur" in mode 4 commitments. Adopting an official Safeguard Mechanism in the GATS would be an invitation for politicians, industry and organised labour to call for its application, particularly in the main trading blocks.

The main **conclusion** of this short analysis must be that while it may appear politically expedient to call for ESM, when applying it to the different modes, it is indeed a double edged sword that, on the whole, does not provide any safeguard for countries, but rather brings more potential drawbacks and risks than the sought for "safe haven".

An overall application of ESM to all Modes would seem feasible but highly undesirable by the developing countries themselves in view of the negative consequences this would have in terms of scaring the foreign direct investors or scaring the foreign services suppliers, which without such a threat would have been interested in providing services that are actually needed by the population of these countries.

A more eclectic approach per Mode, would make application of ESM on Mode 1 totally undesirable and probably undoable for most services, on Mode 2 it would be ineffective, on Mode 3 it could be possible, but when applied would certainly have negative investment consequences for the Member that invokes it, and on Mode 4 will probably hurt Developing Countries more than it would benefit them.

## **RECOMMENDATION**

**In the view of the ESF, the application of so-called ESM's simply does not work in practice for services.** While providing a possible political comforting measure in case of extreme concern and need, it effectively does not really provide pragmatic surcease of economic sorrow. On the contrary, its application potentially worsens the position of the applying Member. This seems to be more and more the case for safeguard measures applied in the goods sectors.

Thus our main message is that, while recognising the overall desire of some WTO members to obtain ESM's, on careful analysis, this instrument contains major drawbacks for countries which are Foreign Direct Investment candidates instead of bringing the perceived protection and emergency intervention.

The European Services Forum would therefore recommend that all WTO Members look at this issue with a more pragmatic approach and to consider it from a less political point of view. All efforts should be made to bring this issue to a well-accepted conclusion.

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Position Paper on Emergency Safeguard Measures – 20 September 2002

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