

Desirability, Feasibility and Options for Establishing ESM within the AFAS

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Authors:

Mr Malcolm Bosworth and Mr Dionisius A. Narjoko

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EXECUTIVE SUMMARY

After almost endless discussions in the WTO since 1995 members have been unable to agree on whether to extend generic ESMs to services under GATS. These negotiations stalemated after missing several deadlines and, having been incorporated into the Doha Round, have been suspended since mid-2006 along with all negotiations. Essentially all members, except ASEAN economies, excluding Singapore, are either opposed or largely indifferent to their adoption.

In parallel with these multilateral negotiations, ASEAN Member Countries have agreed to consider whether to adopt a generic ESM under the ASEAN Framework Agreement on Services (AFAS). Both collectively and individually, they are also pressing for their adoption in various bilateral trade agreements. Such regional developments would seem premature since it would be virtually impossible for ASEAN Member Countries to adopt ESM for services unless such measures were first adopted multilaterally. Following the conclusion of Vietnam's membership, Lao PDR is the only ASEAN Member Country not belonging to the WTO, and it is undergoing accession. Thus to apply ESMs under AFAS without WTO acceptance would generally contravene their multilateral commitments, and would amount to them discriminating against each other. While Singapore has supported consideration of the possible adoption of ESMs in AFAS, it remains strongly opposed to this in the WTO.

The protracted and inconclusive debate in the WTO has highlighted many of the reasons why the feasibility and desirability of adopting ESMs in services is at least doubtful and probably even spurious. ASEAN Member Countries less Singapore have suggested a model that closely resembles ESMs applied to goods under the GATT. While this is understandable and a good starting point for any such discussions, it fails, however, to recognize that services are inherently different to goods, being intangible, non-storable and delivered not only cross-border as for goods but by three other modes of supply, namely by movement of consumers (consumption abroad), firms (commercial presence) and labour (temporary movement of people). The GATS is therefore fundamentally very different to the GATT, including in architecture. For example, the GATS does not make national treatment and MFN general commitments, and instead adopts a positive list whereby commitments to liberalize market access and national treatment apply only to scheduled services and modes of supply, and then only to the extent that limitations are not listed so as to preserve the right to apply inconsistent measures. Thus, the GATS provides widespread flexibility to members and also allows scheduling of safeguard-type measures, such as ENTs or progressive liberalisation timetables, and it does not follow that ESMs are justified for services.

The economic rationale for adopting an ESM for services is largely based on 'political economy' grounds, namely that it would promote more liberal commitments by providing

where necessary 'breathing space' for domestic industries to adjust to open trade and associated import surges. However, while the value of this role is difficult to prove or disprove, evidence for goods suggests it is by no means guaranteed or automatic, and cannot be assumed. Indeed, much of the evidence suggests the contrary, namely that domestic protectionist or vested interests can capture ESMs as a means of extending 'temporary' protection to delay rather than facilitate trade liberalisation and adjustment to import competition. If this happened, adopting an ESM for services as a liberalisation facilitator is likely to backfire, and end up adding another layer of flexibility in the GATS or AFAS (which adopts the GATS framework, including a positive list) that could simply weaken already weak commitments. Moreover, trade barriers are almost always an inefficient means of facilitating adjustment of domestic industries to import competition, and of the possible policy responses well-targeted subsidies are more likely to be effective. It would seem therefore more desirable for ASEAN Country Members to focus on the negotiation of appropriate disciplines on the use of subsidies for services under AFAS, as already is occurring within the GATS. On balance, the report largely rejects the 'political economy' value of a generic ESM in improving services trade liberalisation, especially if it is based on the GATT model with no improvements designed to strengthen this role. AFAS commitments are substantially no better than those offered in the WTO, which are generally non-liberalising.

The most difficult area against applying an ESM for services is how to treat commercial presence (mode 3), and there seems to be no satisfactory solution. Unless a nationality definition of domestic industry is used, resident foreign suppliers will be included as part of the domestic industry, and thus any ESM may only be applied against new foreign entrants. However, this may have adverse implications for MFN. Moreover, establishing causality between them and domestic injury would be impossible given that any such injury must surely have been caused by already established resident foreign suppliers. Thus, applying ESMs under a residency definition in practice almost amounts to excluding them from mode 3, thus making them redundant. However, under this scenario (or any attempt to sidestep the problems associated with mode 3 by specifically excluding it from any generic ESM) having an ESM is likely to have little or no 'political economy' value since the main mode of services delivery and the area of most concern to locally-owned suppliers would be excluded.

Using a nationality definition also raises problems. While it would exclude established foreign firms from the domestic industry and enable them to be targeted by ESMs, how would this be done and using what measures? Expelling or divesting them is hardly a sensible economic option, given that they employ people and for all intent and purposes provide the same economic benefits as locally-owned firms. Thus, excluding 'acquired' rights of established foreign firms from ESMs would seem necessary, as advocated by ASEAN less 1 Country Members. While this leaves 'expansionary rights' of such firms to be subject to ESM, this proposal also has major difficulties, and is likely to rebound badly on the economy and its attractiveness for FDI. Moreover, if the GATS definition is used and established foreign firms with minority domestic ownership (up to 49%) are to be subjected to ESM, then domestic interests are likely to be adversely affected almost as much as foreign interests. Protecting 'acquired' rights of established foreign suppliers while prohibiting new foreign entrants also raises MFN (discriminatory) concerns, and provide governments with greater flexibility to protect incumbent (including foreign) suppliers. Established foreign firms could be subjected to discriminatory taxes, but again the economic ramifications of doing so on employment and economic activity could be severe.

Many other problems abound in the possible application of ESM to services in both a regional and multilateral context, which have not been adequately addressed in the ASEAN less 1 proposal. However, if a generic ESM was to be adopted in AFAS, steps would be needed to minimize the potential for mis-use or abuse to meet protectionist pressures i.e. to 'safeguard' their use to maximise the likelihood of promoting rather than undermining trade liberalisation. Any 'political economy' instrument has a high probability of being captured by

protectionists and used to resist liberalisation unless itself sufficiently 'safeguarded.' A national 'public interest' test would be needed, and efforts made to ensure that ESMs were only available in cases where liberalizing commitments were made, subject to a 'limited time window' (five years). Commitments made 'below the status quo' should be ineligible for ESM. ESMs should also be subject to meeting pre-determined thresholds, such as sectoral coverage and/or modes of supply, or alternatively limited in application to a small set of 'sensitive' sectors. Tight sunset clauses (maximum of 2 to 3 years for all members) should be imposed, and consideration be given to limiting the operation of such a generic ESM for a definite period, such as 20 years. It would also enhance any liberalizing role of ESMs if their introduction could be used as a basis for other needed reforms, such as removing ENTs, especially non-specified or non-transparent ones, and the adoption under AFAS of a negative list approach.

A preferred option to a generic ESM in AFAS may be for ASEAN Country Members to negotiate well-controlled and targeted sectoral safeguard measures, including possibly in their schedules of commitments. However, these would not be problem-proof and would introduce their own complications.