



Increasing LDC Participation in Services through Special Priority Market Access in the WTO

I. Introduction

The WTO's General Agreement on Trade in Services, (GATS) operates on the Most Favoured Nation (MFN) principle. According to Article II of the GATS, each Member is mandated to accord immediately and unconditionally to services and service suppliers

of any Member, treatment no less favourable than it accords to like services and services suppliers of any other country. Derogation previously permissible such as MFN exemptions have been overtaken by time. According to Paragraph 2 of the Annex on Article II exemptions, any exemptions sought after the entry into force of the GATS Agreement,

Executive Summary

The participation of Least Developed Countries (LDCs) in international trade in services is minimal. Unlike the case of goods, in services, LDCs compete on a Most Favoured Nation (MFN) basis. It is therefore impossible for a country to give a market opening only to LDCs, on terms more favourable than is available to others. Bearing in mind that LDCs have the weakest capacities to compete, the present rules lock them out of the ever increasing opportunities in international trade in services. A key objective of the General Agreement on Trade in Services (GATS) is to reverse this trend, by providing a set of international rules that result in increased participation of LDCs.¹ Members have agreed that LDCs require special priority in services.² Simply put, special priority would entail more favourable treatment of LDC services suppliers under the GATS, including through priority market access. Various GATS negotiating mandates call for the development of an appropriate mechanism to operationalise the according of special priority to LDCs. Some of these include GATS Article IV: 3, the Guidelines and Procedures for negotiations, the Modalities for the Special Treatment of LDCs, and the Hong Kong Ministerial Declaration of December 2005. The LDC Group presented a proposal for a Mechanism to operationalize Article IV:3 of the GATS, which would create legal space for Members to accord special priority access to LDC services suppliers, without violating MFN. However, this proposal is being ignored, signalling Member's unwillingness to appreciate the issue's importance, and to deliver on the mandate. This Policy Brief argues for the need to find a WTO solution that implements an already existing mandate, as a means to increasing LDC participation in international trade in services.

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must follow the waiver process in Article IX (3) of the Marrakesh Agreement establishing the WTO. The status quo is that LDCs have got to be treated like all other Members.

This is in spite of the existence of Article IV: 3 of the GATS, which provides that special priority shall be given to LDCs in among others, negotiated specific commitments resulting in liberalisation of market access in sectors and modes of supply of export interest to LDCs.

While such legal provisions exist, they are not operational in the absence of an appropriate legal mechanism that can backstop Members according such priority, without contravening the MFN principle.

II. Why Special priority?

Most LDCs rely on agricultural products for their export earnings. This is a worrying trend because of the fragility of the agricultural sector, whose survival depends on such uncertainties as prices of primary commodities.

Worse still, at the international level, agricultural trade is heavily distorted, which negatively affects LDC exports.

International trade in services is continually growing, making bigger contributions to the gross domestic product (GDP) of countries. For the period 2000-2003, trade in services represented 16 per cent of the total trade of developing countries, expanding at the same pace as their trade in goods.³

The UNCTAD LDC Report of 2006 estimates that the decade 2000-2010 will be a first, in which growth of the economically active population outside agriculture will outpace agriculture.⁴ In this scenario, the services sector is singled out as a likely leader.

In recent years, LDCs have made cautious attempts at developing policies that can lead to robust services economies, as a complement to

agriculture. For LDCs, services continue to play a key role in the eradication of poverty because of their social, cultural, and welfare-enhancing functions.

The services sector plays a crucial role in human development in the form of essential services, as a hub of economic activity such as in tourism, and through inter-sectoral linkages, both forward and backward, created with other sectors such as manufacturing, investment, and agriculture.

Many LDCs have liberalized their services markets through policies of privatization, hoping to attract foreign direct investment, obtain technology, enhance efficiency and ensure growth in productivity. However, liberalization alone is not enough. Countries need sound regulatory frameworks to reap the benefits presented by international trade in services.

Regulatory requirements such as supporting laws and regulations that strike the right balance between government's role in the protection of public goods for public access (such as water/sanitation, health or education), and the need to attract foreign direct investment in a way that does not destroy local small and medium size enterprises, remains a challenge to LDCs.

The pre-requisites for a strong services sector such as basic infrastructure, telecommunications, banking and financial services, entrepreneurial, and technical skills, administrative and institutional capacities, are still under-developed in most of LDCs.

The development of domestic supply capacity in strategic sectors also remains a challenge for LDCs. Worse-still, the crucial assessments required to indicate which policy choices are key for liberalization of international trade in services from a sectoral, and modal perspective, have, for the most part, not been carried out in LDCs.

Therefore, expecting LDCs to compete in international trade in services on MFN basis (equal footing) with the rest of the WTO Membership, as is provided for in the GATS, excludes them from the benefits that this trade presents. It is no sur-

prise that while the rest of the world continues to record increments in services exports, LDCs remain net-importers of services.⁵

LDCs have comparative advantages in provision of services through the movement of their natural services suppliers (Mode 4) in all skill levels.⁶ Typically, these services suppliers send remittances to their countries of origin.

For LDCs, remittances have proved to be a major, and relatively stable, source of capital inflows. Bangladesh and Lesotho are examples of countries where remittances continue to make impressive contributions, going up to 27 per cent in the latter's case, when measured as a share of GDP.⁷ In Uganda, recent years have seen the contribution of remittances as one at par with traditional exports such as coffee and cotton.

Remittances not only improve a countries' ability to finance development objectives, but also trickle down to the livelihoods of recipients, allowing them to engage in economic activity.

This is becoming very critical for LDCs, since they have many middle- and lower-skill workers. While multilateral liberalization of temporary movement through commercially meaningful GATS commitments presents an important way to allow for continual benefit from remittances, such liberalization, on an MFN basis, may not necessarily result in improved actual utilization of such openings by LDCs.

This is so because other Members have better domestic capacity to take advantage of such openings. It is critical that such liberalization is complemented with special priority access for LDCs.

Special priority market access for LDCs is a critical first step in ensuring their beneficial participation in the international services economy. In the case of trade in goods, there is longstanding acknowledgement, through the Enabling clause⁸, that derogation from MFN is necessary for development.

Members can rely on this legal instrument to provide preferential market access to products from developing countries. Another example is the Preferential Tariff Treatment for Least Developed Countries, a waiver adopted by WTO Members in 1999.⁹

The markets created under such schemes have encouraged beneficiary countries to create domestic programs that build capacity to supply such markets. In many cases, this has generated a new momentum of economic activity, leading to the improvement of living standards. The same idea can be replicated in services, taking advantage of lessons learnt from experiences in the area of trade in goods.

For LDCs, services continue to play a key role in the eradication of poverty because of their social, cultural, and welfare-enhancing functions.

III. Treatment of LDCs in the GATS: *Insights on the architecture*

Article II of the GATS enshrines the MFN principle, which emphasizes equal treatment for all Members. However, this cornerstone of WTO law is not cast in stone. Article IV of the GATS provides detailed obligations that Members assume for the attainment of increased participation of developing countries in world trade.

In Article IV: 1, the need to increase the participation of developing countries through negotiated specific commitments including in sectors and modes of supply of export interest to LDCs is addressed.

Article IV:3 provides that special priority will be given to LDCs in the implementation of the obligations set forth in Article IV:1. Article IV: 3 is a cornerstone of LDC participation in the GATS, because it creates hope for preferential, and priority market access for them in the services sector. However, in the absence of clear means of operationalising, Article IV: 3 lies to waste.

V. Special priority for LDCs: *the broader mandate*

The Guidelines and Procedures for GATS negotiations¹⁰ adopted by the Council for Trade in Services (CTS) in March 2001, provide that special priority shall be accorded to LDCs according to Article IV: 3.

Paragraph 6 of the same Guidelines requires Members to give special priority to providing effective market access in sectors and modes of supply of export interest to LDCs¹¹, through negotiated specific commitments.

The Modalities for the Special Treatment of LDCs, (hereinafter referred to as the Modalities), adopted in September 2003, set out technical detail with which Members are to handle LDC issues in the services negotiations.

According to Paragraph 7 of the Modalities, Members are required to develop an appropriate mechanism with a view to achieving full

implementation of Article IV: 3 of the GATS, and facilitating effective access of LDCs' services suppliers to foreign markets (*emphasis added*).

From the political front, the General Council Decision of 31st July 2004, also known as the July Framework, called for special attention to LDCs in providing effective market access in their sectors and modes of supply of export interest.

At the December 2005 WTO Ministerial Conference in Hong Kong, Ministers agreed to develop methods for the full and effective implementation of the LDC Modalities, including the development of appropriate mechanisms for according special priority to sectors and modes of export interest to LDCs in accordance with Article IV: 3 of the GATS, and paragraph 7 of the LDC Modalities by 31st July 2006.¹²

This deadline has been missed owing to the overall suspension of the Doha negotiations.

In sum, it is clear that the mandate for developing a mechanism to accord special priority to LDCs is intact.

Table 1
Summary of mandates for according special priority

GATS Article IV:3 provides special priority for LDCs
Paragraph 6, LDC Modalities requires Members to provide effective market access
Paragraph 7, LDC Modalities requires Members to develop appropriate mechanisms with a view to achieving full implementation of GATS Article IV:3
Paragraph 47, Hong Kong Ministerial Declaration calls on Members to implement the LDC Modalities and give priority to sectors and modes of interest to LDCs
Paragraph 3, Annex C, Hong Kong Declaration calls for full and effective implementation of the LDC Modalities
Paragraph 9 (a), Annex C Hong Kong Declaration requires Members to develop appropriate mechanisms for according special priority in sectors and modes of interest in accordance with Article IV:3 and paragraph 7 of the LDC modalities
Paragraph 9 (b), Annex C, Hong Kong Declaration calls for undertaking commitments in sectors and modes of supply of interest to be identified by LDCs
Paragraph 11 (e), Annex C, Hong Kong Declaration provides a deadline for implementation of 9(a) of 31 July 2006

V. The LDC Proposal: *key elements*

In March 2006, the LDC Group submitted a proposal to the CTS in special session¹³, aimed at creating a Mechanism to accord special priority to market access in sectors and modes of LDC export interest.

This would allow developed countries, and developing countries declaring themselves in a position to do so, to grant LDC services suppliers, special priority, without contravening MFN.

The proposal's cornerstone lies in its Paragraph 1, wherein it is proposed that notwithstanding any provision of the GATS, non-reciprocal special priority shall be accorded only to LDCs in sectors and modes of supply of export interest to them.

The rationale behind proposing such a Mechanism is that it allows for a permanent and binding solution, within the WTO, to the problem of LDCs non-participation in international services trade.

Permanence is important in providing sustainable legal cover to Members providing LDCs special priority, from MFN violation claims.

The security, stability and predictability of market access created by this Mechanism would also create a necessary incentive for LDC governments to take direct policy choices to enhance utilization of the markets created by this process.

The need for a binding obligation is drawn from lessons learnt in the context of the Enabling Clause for trade in goods, wherein Members give preferential access only when they want to. As such, LDCs want certainty that Members will be

bound to deliver market access on the basis of this Mechanism.

The proposal differentiates assumption of obligations between developed and developing countries. For developed countries, LDCs propose that the obligation to provide non-reciprocal special priority be assumed on a mandatory basis, leaving it as best endeavour for developing countries declaring themselves in a position to do so.

This language is similar to that used in the Hong Kong Ministerial Declaration, for trade in goods, relating to the provision of duty free and quota free market access to products originating from LDCs.¹⁴

Table 2
Thematic features of the LDC proposal on special priority

- *Protection from MFN contravention*
- *Non reciprocity*
- *Binding/obligation nature*
- *Differentiated obligation between developed and developing countries*
- *Modification only allowed for market access enhancing purposes*
- *All LDCs are affected members for purposes of compensation*
- *DSU applicability*
- *Annual Review of special priority being provided by the CTS*

It is critical to recognize that developing countries cannot be expected to assume the same standard of obligation as developed ones.

The market access provided under this Mechanism should be facilitated to promote LDC services exports. Therefore, it is important that it responds positively to the development needs of LDCs.

One way to do this is pay attention to LDC development, financial and trade needs, as identified by them. Such a requirement on WTO Members also calls on LDCs to carry out individual national assessments so that they have these needs ready for articulation.

For purposes of clarity, it is important that the special priority granted to LDCs is placed in Members' schedules of commitments. This allows for transparency, and creates a clear obligation on the part of Members to respect such obligations.

In the event that a Member goes back on a commitment made to LDCs, the fact that such a commitment was scheduled would clearly create need for compensation to LDCs.

It is also important that the dispute settlement processes of the WTO are applicable to the special priority Mechanism. This would provide a forum through which LDCs can enforce their rights on the basis of the special priority Mechanism.

VI. State of play in negotiations: *Initial responses and counter proposals*

The LDC proposal has been met with mixed reactions. Initially, various concerns were raised, including in relation to: the legal form that such a mechanism would take, whether an amendment of the GATS was necessary, whether the proposal had to be binding, inconsistency with the MFN principle, what special priority means in practice, whether bilateral approaches cannot solve the problem, and whether reporting to the CTS on unilateral processes wouldn't suffice.

Some developing countries were supportive of the LDC proposal, notably the African group. However, some others were wary of the introduction of preferences in the context of the GATS, arguing that this would divert their markets.

On the basis of these questions, LDCs made responses at various sessions of the CTS. In time, it became clear that developed countries do not support the proposal. They do not support a permanent legal exception to the MFN principle of the GATS. They argue that MFN is sacrosanct and as such, cannot be contravened.

Developed countries also argue that implementation of the proposal would be burden-

some, as it would require a two-track regulatory regime for its administration. In general, developed countries feel that there are other non-binding, typically unilateral ways, in which special priority can be accorded. Consequently, the Quad, headed by the European Communities, presented a counter proposal by way of room document.¹⁵

In essence, the EC and friends propose a mechanism to report, and collectively assess, the extent to which Members are providing special priority to sectors and modes of supply of interest to LDCs in their services offers in the Doha Round. Here, it is proposed that each member submits a report indicating how their offers take LDC interests into account. These reports would then be circulated to LDCs for comment, and a dedicated session of the CTS-SS would collectively assess them.

The chair of the CTS would then prepare a report summarizing the results of such an assessment, and identifying best practices which Members can take into account in preparation of their final schedules of commitments. This would be Article IV: 3 implemented!

It is submitted that while the EC proposal contributes to the review function that the CTS

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has to take on services negotiations in general, it does not address the main concerns of LDCs. At best, it is a good contribution to the review requirement set out in Paragraph 9 (e) of the Hong Kong Declaration which calls for the development of a reporting mechanism to facilitate the review requirement in the LDC Modalities.

This still leaves the problem of LDC low participation pending. The objective of the LDCs is to *access markets on a priority basis*. No amount of reporting will achieve this in the absence of a legal carve out to the MFN principle. The EC proposal concerns itself with reporting how sectors and modes have been taken into account. LDCs want operationalisation of priority market

access. As such, the EC Proposal adds no real value to LDC concerns.

It is also worth noting that by creating obligations for non-LDCs, the co-sponsors disregard the well accepted practice in the WTO of differentiated responsibility between developed and developing countries.

When negotiations resume, the challenge will be to refocus these negotiations to proceed on the basis of the LDC proposal.

VII. Conclusion

It is established that LDCs are the weakest and most vulnerable Members of the WTO. They are defined as such because of their low GDP per capita, their low human assets, and their high degree of economic vulnerability. LDCs do not yet have capacity to compete on an MFN basis. The need for greater integration into the international trading system of this weak group will remain rhetoric if no bold steps are taken to achieve this in practical terms.

The proposal, as presented by the LDCs, offers an opportunity to increase LDC participation. It would create legal certainty and predictability, al-

lowing for a more coherent planning process at the domestic level, which, in time, would lead to improved capacities and efficiencies in strategic and niche sectors and modes of supply constituting export interest to LDCs.

The mandate to develop a legal mechanism already exists in the GATS, and the LDC Modalities. What is left is operationalisation and implementation. This implementation must be done within the WTO. At the highest level of decision making in the WTO, Ministers have agreed, going as far as setting a deadline for the development of a mechanism by 31st July 2006. When Members return to the negotiating table, they should come with changed positions. Proposals that *talk around* the issue such as focusing on reporting, while not dealing with real solutions do not help the process; they deter it.

Unilateral and bilateral approaches can only act as complements to, and not substitutes for, a WTO solution to the implementation of GATS Article IV: 3. WTO Members should seriously reconsider the LDC Proposal, bearing the practical realities of this group in mind. The development potentials of special priority would be concrete steps in the path to fulfilling the objectives of the GATS, contributing positively to the development component in the Doha Agenda of negotiations.

End Notes

1. GATS preamble, available at, <http://www.wto.org>
2. Article IV: 3 GATS, also see Modalities for the Special Treatment of LDCs in the Negotiations on Trade in Services TN/S/13, available at, <http://www.wto.org>
3. UNCTAD, *Handbook of Statistics, 2004*. Also see *Participation of the developing economies in the global trading system*, WT/COMTD/W/136.
4. UNCTAD, LDC Report, 2006, available at, <http://www.unctad.org>
5. Ibid.
6. The other modes through which services are supplied in the GATS are: from the territory of one Member into the territory of any other Member (Mode 1); in the territory of one Member to the service consumer of any other Member (Mode 2); by a service supplier of one Member, through commercial presence in the territory of any other Member (Mode 3). See 7. Article II GATS.
7. Note 3, *supra*.
8. Decision on Differential and More Favorable Treatment, Reciprocity, and Fuller Participation of Developing Countries- Decision of 28 November 1979 (L/4903)



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End Notes (continued)

9. WT/L/304
10. S/L/93, available at, <http://wto.org>
11. TN/S/13, available at, <http://wto.org>
12. Paragraph 47 Hong Kong Declaration. Paragraph 3, 9 (a), 9 (b), 11 (e) of Annex C, Hong Kong Declaration; WT/MIN (05)/DEC. available at, <http://www.wto.org>
13. Communication from the Republic of Zambia on behalf of the LDC Group; A mechanism to operationalise Article IV: 3 of the GATS. TN/S/W/59. available at, <http://www.wto.org>
14. Paragraph 47, and Annex F, Hong Kong Ministerial Declaration, WT/MIN(05)/DEC
15. Communication from the European Communities: A mechanism to assess the granting of special priority to sectors and modes of supply of interest to LDCs in the services negotiations in the offers of non-LDC Members. This proposal was co-sponsored by Canada, the US, Japan, and others.

Recent Publications

- Considering Gender and the WTO Services Negotiations – South Centre *T.R.A.D.E. Research Papers* 6. April 2006
- The Development Dimension of the GATS Domestic Regulation Negotiations – South Centre *Analytical Note* (SC/AN/TDP/SV/11). August 2006
- GATS Dispute Settlement Cases: Practical Implications for Developing Countries - *South Centre Analytical Note*. January 2005
- State of Play of the GATS Negotiations: Are Developing Countries Benefiting? – South Centre *T.R.A.D.E. Policy Brief* 4. November 2005