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Working Paper 2005-03

Pros and Cons of the  
General Agreement on Trade in Services  
(GATS)

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# 1 Introduction

For international trade in commercial services, January 1<sup>st</sup> 1995 marked a milestone in history. After nearly 8 years of negotiating, the *General Agreement on Trade in Services* (GATS) came into effect. It was aimed at setting globally accepted rules and standards for the cross-border trade in commercial services such as telecommunication, banking, insurance, tourism or management consulting. The rapid growth of the service sector since the 1970's required a legal framework for trade in services that appears even more important today as "... the services sector is the largest and fastest-growing sector of the world economy ..."<sup>1</sup>.

However, from the very first day of the idea about a ruling accord on services, critics have risen their massive doubts about its benefits on world economic welfare. While advocates of the GATS promote this agreement as most valuable in both legal and economic dimensions<sup>2</sup>, sceptical opponents condemn it as "globalisation's last frontier" towards a totally commercialized, profit-driven society<sup>3</sup>. But who is right in that issue? Does GATS really enforce and facilitate fair international trade in services and in turn increase prosperity in the majority of participating economies? Or does the agreement contribute to a further merciless commercialization, even in very sensitive areas of public services as many people tend to fear? Does GATS make the global marketplace a fairer and more efficient one or does society have to pay an even higher price than it gets in turn?

This special research paper is intended to examine the pros and cons of the *General Agreement on Trade in Services*. It attempts to give a description of its major features and an assessment of its most significant impacts - advantageous or threatening or even both - in order to figure out the strengths and weaknesses of the contract. At first, some glances at recent history about the journey from the goods-related predecessor of the GATS to the *World Trade Organization* are carried out (section 2). Afterwards, the agreement itself is outlined followed by an

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<sup>1</sup> WTO (2001), pp. 4

<sup>2</sup> Hasse (1997), pp. 20

<sup>3</sup> Barlow (2001)

examination of general advantages as well as potential weaknesses related to the provision (part 3). Section 4 deals with some special aspects and service areas that are among the most controversially discussed issues with regard to GATS. The report's closing part summarizes major findings and implications.

## 2 Historical Background

### 2.1 From GATT to WTO

The GATS is one of the three pillars of the *World Trade Organization* (WTO) that came into force on January 1<sup>st</sup>, 1995.<sup>4</sup> But the roots of this fairly young institution trace back to the 1940's. How they were developed, expanded and finally transformed into today's world trade order is outlined in this chapter.

In the mid 1940's, the Allies led by the United States drafted a world trade order consisting of three international institutions: the *World Bank*, the *International Monetary Fund* and an *International Trade Organization* (ITO). Economists and politicians recognized that foreign trade policy focusing on protectionism had been one of the triggers of the Great Depression and in broadest sense also of World War II. In order to prevent such disasters from reoccurring and to benefit from the advantages of free trade between nations, the ITO was expected to provide legal framework for fair and free global trade under the jurisdiction of the UN. The basic idea behind was the assumption of free trade serving as a catalyst for worldwide economic growth and increasing global welfare.<sup>5</sup> Since the end of the 18<sup>th</sup> century, theories had been promising huge welfare gains in case of free cross-border flow of goods.<sup>6</sup> With the newly drafted world trade system, this scenario was eventually intended to become reality. The ITO was meant to cover all international affairs dealing with employment, economic development, trade policy, competition policy

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<sup>4</sup> The *General Agreement on Tariffs and Trade* (GATT) and the *Agreement on Trade Related Aspects of Intellectual Property Rights* (TRIPs) constitute pillar 1 and 3, cf. Hauser/Schanz (1995), pp. 191

<sup>5</sup> Cf. Hauser/Schanz (1995), pp. 7; Rode (1998), pp. 5

<sup>6</sup> for an overview about free-trade-theories cf. Yüksel (2001), pp. 11 et seqq.

and production of raw materials.<sup>7</sup> In 1948 the *General Agreement on Tariffs and Trade* (GATT) was put into effect as a first step on the path towards the ITO covering its chapter on commercial policy. It contained obligations and commitments to reduce tariffs to ensure a free international trade of goods. When the foundation of the ITO failed due to various reasons<sup>8</sup>, the GATT remained the only multilateral framework governing cross-border trade in goods.

The Most Favoured Nation (MFN) and the National Treatment principles are the core elements of GATT. According to the former, all trading partners of a nation shall be treated equally when passing national borders as far as tariffs and quotas are concerned. The latter principle attempts to avoid different treatment of companies (goods) *in* the country once they have passed the border, i.e. any good irrespective of its origin is entitled to receive the same treatment as the most preferred one within a national market.<sup>9</sup> The whole provision referred only to the trade in goods, i.e. to movable, tangible assets. In the days of the establishment of the GATT, the significance of commercial services was not material.<sup>10</sup>

Since then, within 8 trade liberalization rounds in the next 40 years, the number of participating countries grew, tariffs were reduced even further<sup>11</sup> and rules for non-tariff barriers<sup>12</sup> were set. In 1993, the successful completion of the 8<sup>th</sup> trade liberalization round brought the most fundamental reform to the world trade system since GATT was set up: Two additional multilateral agreements, GATS and TRIPs, were passed and finally came into effect in 1995. At the same time (1995), the now 3 major accords were put under one institutional roof, the *World Trade Organization*. It marked the movement from a purely goods-related provisional accord (GATT) towards a complete set of rules for global trade within one international institution.<sup>13</sup>

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<sup>7</sup> Cf. Langhammer (2002), section 1

<sup>8</sup> for more details e.g. Yüksel (2001), pp. 26

<sup>9</sup> Cf. WTO (2004), section 7

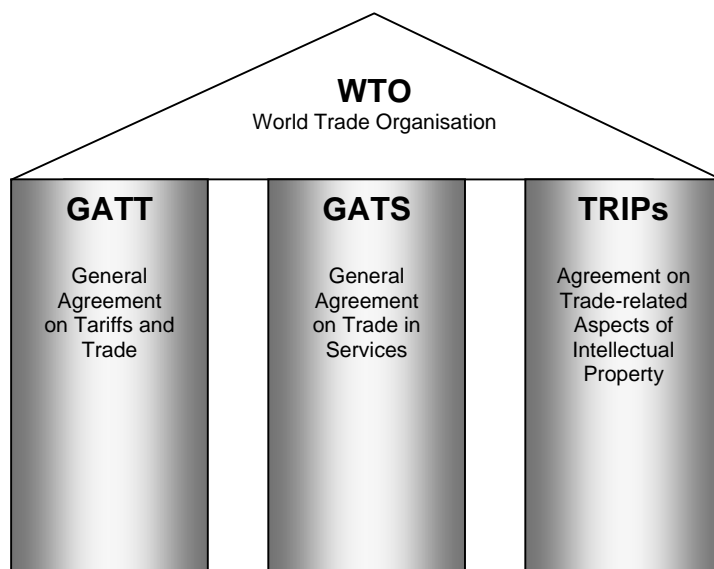
<sup>10</sup> Senti (2000), pp. 564

<sup>11</sup> Average import tariffs for industrial goods were reduced from 40 % (1947) to some 4 % (1999), cf. Senti (2000), pp. 220

<sup>12</sup> primarily, these are rules, policies, practices of governments that can affect trade, e.g. environmental standards or acknowledgement of personal qualifications

<sup>13</sup> Cf. Hauser/Schanz (1995), pp. 59

The layout of the current world trade system is illustrated in Exhibit 1. The WTO works as the institutional body under which the three major trade-related agreements GATT, GATS and TRIPs are administered. Its mission can be described as “Promoting the global free trade”<sup>14</sup>. Officially, the organization’s responsibilities and competences are centred towards administering the trade agreements, handling trade disputes, monitoring national trade policies, providing a forum for trade negotiations as well as providing technical assistance to developing countries.<sup>15</sup>



**Exhibit 1:** Layout of the World Trade System since 1995.<sup>16</sup>

<sup>14</sup> Altmann (2004), pp. 136: „Ihr Credo ist die Förderung des globalen Freihandels.“

<sup>15</sup> Cf. WTO (2001), pp. 17

<sup>16</sup> according to Hauser/Schanz (1995), pp. 6

## 2.2 The Path to a Service Agreement

The inclusion of a service-specific agreement within the world trade system has been a response to the fundamental changes in the global trade patterns that occurred over the last decades.<sup>17</sup> While goods-related trade was overwhelmingly predominant in the aftermath of World War II when GATT was put on track, international trade in services grew rapidly since the 1970's.<sup>18</sup> Changing customer preferences especially in the Western industrialized nations have triggered an increasing demand for services. At the same time, the beginning of liberalization of traditional state monopolies put these services into competition and promoted a broader offer to private and commercial users. And what was presumably most significant: Technological innovation in the fields of telecommunication have gradually enhanced the 'tradeability' of services.<sup>19</sup>

In 2001, services accounted for 60 % of global output, for 30 % of worldwide employment and for roughly 20 % of the world's international trade flows<sup>20</sup>; estimates even see the last figure to reach some 50 % by the year 2020<sup>21</sup>. All in all, the economic and social significance of services is continuously growing - the services sector has become the engine of global economic growth.<sup>22</sup>

Expanding the GATT rules to services was originally initiated by the United States in the 1980's in an attempt to improve access to the world market for the powerful American service companies in the capital-intense fields of financial services and telecommunications.<sup>23</sup> Other industrialized nations cautiously acknowledged the legal and economic necessity of a service agreement. Given the increasing significance of services for global trade, "the lack of a legal framework for international services was ... anomalous because the potential benefits of services

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<sup>17</sup> the same applies to TRIPs and TRIMs (Agreement on Trade Related Aspects of Investment Measures), cf. Beise (2001), pp. 114

<sup>18</sup> Cf. Senti (1997), pp. 69 et seq.

<sup>19</sup> Bundesministerium für wirtschaftliche Zusammenarbeit und Entwicklung (2003a), pp. 4

<sup>20</sup> Cf. Beise (2001), pp. 114; WTO (2004), section 1;

<sup>21</sup> Bundesministerium für wirtschaftliche Zusammenarbeit und Entwicklung (2003b), pp. 4

<sup>22</sup> Zänker (2002): "Der Dienstleistungssektor ist zum Motor der Expansion geworden."

<sup>23</sup> Cf. Hauser/Schanz (1995), pp. 193

liberalization are at least as great as in the goods sector, and dangerous because there was no legal basis on which to resolve conflicting national interest.”<sup>24</sup>

It became evident that a pure incorporation of services within the GATT was not feasible due to the different characteristics of services compared to goods.<sup>25</sup> As a consequence, the newly introduced GATS was tailored specifically at services while trying to apply the structure and basic rules of the GATT to the provision. According to the WTO, objectives of GATS are “... creating a credible and reliable system of international trade rules; ensuring fair and equitable treatment of all participants ...; stimulating economic activity through guaranteed policy bindings and promoting trade and development through progressive liberalization.”<sup>26</sup> With the establishment of GATS 10 years ago, (at least) a legal gap in the world trade system has been closed.

## **3 The General Agreement on Trade in Services (GATS)**

### **3.1 Basic Features of the Accord**

GATS covers all internationally traded services with exception of “... services provided to the public in the exercise of governmental authority ...” and “... all services related to the air transport sector ...”<sup>27</sup>. That means, apart from the area of air-transport, only public services that are neither provided on a commercial nor competitive basis, are *not* subject to the GATS.

In recognition of the distinctive nature of services opposed to goods, GATS does not only regulate traditional cross-border trade, but it defines four “modes of supply” how services can be delivered (see Exhibit 2).<sup>28</sup> Therefore GATS takes the rather subtle definition of services into account and rules all possible appearances

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<sup>24</sup> WTO (2001), pp. 4

<sup>25</sup> Cf. e.g. Langhammer (2002), section 2.3

<sup>26</sup> WTO (2004), section 1; Cf. Senti (2000), pp. 566 goes into the same direction

<sup>27</sup> WTO (2001), pp. 6

of international trade in services: Cross-border movement of the supplier, the consumer as well as of the service itself.<sup>29</sup>

<p><b>Mode 1: Cross Border Supply</b></p> <p>services flow from the territory of one member-country into the territory of another member-country</p> <p>e.g. international telephone calls, online shopping with non-domestic providers</p>	<p><b>Mode 2: Consumption Abroad</b></p> <p>consumers (e.g. tourists) from one member-state move into another member's territory to obtain a service</p> <p>e.g. tourism, medical treatment abroad</p>
<p><b>Mode 3: Commercial Presence</b></p> <p>service suppliers of one member-state establish a territorial presence in another member's territory to provide a service</p> <p>e.g. domestic subsidiaries of foreign bank</p>	<p><b>Mode 4: Presence of Natural Persons</b></p> <p>citizens of one member-country temporarily migrate to the territory of another member-state to supply a service</p> <p>e.g. accountants, doctors, teachers</p>

**Exhibit 2:** The four modes of service supply within the GATS.<sup>30</sup>

The accord has two major parts<sup>31</sup>: First, the framework agreement with the general rules and disciplines which apply automatically to all members and service sectors. These rules include the MFN-Principle, the obligation to transparency<sup>32</sup> and the general commitment to reach progressive liberalization via continuous negotiations.<sup>33</sup>

The second component of the contract contains country-specific schedules listing national liberalization commitments regarding market access and national treatment (*only*) for the designated fields of services. Each member state is assumed to be free in defining its own liberalization obligations in its schedule, so -

<sup>28</sup> Cf. Stoll/Schorkopf (2002), pp. 184, Senti (2000), pp. 567

<sup>29</sup> Cf. Stoll/Schorkopf (2002), pp. 185:

<sup>30</sup> according to WTO (2004), section 4 and Stoll/Schorkopf (2002), pp. 184

<sup>31</sup> Cf. Hassler (2003), pp. 8 et seq.

<sup>32</sup> all national rules, norms and regulations regarding execution of services have to be published

<sup>33</sup> Cf. Hauser/Schanz (1995), pp. 196 et seqq.

theoretically - only independently chosen service sectors will become subject to the specific liberalization commitments and obligations of the second part.<sup>34</sup>

Additionally, all countries are free to exclude service sectors entirely from all provisions of the agreement for a limited period of time. These exemptions are listed in annexes and will become subject to further negotiations within 10 years.

## 3.2 General Benefits

The growing economic significance of services and their cross-border trade had required a legal framework specifically adjusted to services in order to yield sustainable increases in prosperity. At least formally, this task has been fulfilled with the establishment of the GATS.<sup>35</sup> In that respect, setting up a multilateral framework in an area that has not been subject to internationally accepted rules before must be seen as a success by itself.<sup>36</sup>

Potential advantages related to the GATS-rules can be classified into three broad categories<sup>37</sup>:

### *Increased Competition*

Services liberalization can contribute to economic development (only) if it results in competition and a more efficient supply of services.<sup>38</sup> Competition in open service markets tends to create a more efficient service infrastructure that may serve as an engine for growth for the whole economy. Competition and growth normally result in lower consumer prices, better quality, wider choice, faster innovation and more efficient processes. It is generally acknowledged that an efficient service sector is a decisive prerequisite for a positive development of all industrial branches.<sup>39</sup>

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<sup>34</sup> Cf. WTO (2001), pp. 6 et seqq.

<sup>35</sup> Cf. Eiteljörge (1998), pp. 143

<sup>36</sup> Cf. Eiteljörge (1998), pp. 162

<sup>37</sup> Cf. WTO (2001), pp. 5

<sup>38</sup> Cf. Wiezorek-Zeul (2003), pp. 12

<sup>39</sup> Cf. Wiezorek-Zeul (2003), pp. 11

### *Improved Market Access*

For service companies, open markets provide an opportunity to capitalize on their competitive strengths, to generate economies of scale and thus to become more profitable. The WTO promotes this aspect as a key element for the development strategies of developing countries.<sup>40</sup>

### *Predictability and Transparency*

“GATS commitments have real value in providing secure and predictable conditions of access to markets, which benefits traders, investors, and, ultimately, all of us as consumers.”<sup>41</sup> Transparent, foreseeable and reliable conditions in foreign markets may encourage foreign direct investment. That in turn could enhance technology transfer and might have positive impacts for many other economic branches.

Apart from these 3 major issues, the “built-in agenda” of the agreement ensures that at least attempts for extending the scope of service liberalization are undertaken.<sup>42</sup> Given a certain willingness of the WTO members, that should be a clear opportunity for continuous, dynamic improvements and the amendment of the rules in case of unintended adverse impacts.

## **3.3 General Weaknesses**

Despite these numerous at least good-looking advantages, GATS has remained the most controversial contract of the WTO.<sup>43</sup> In the judgement of economists and experts in international law, it is seen as especially complicated and in certain areas yet uncompleted and provisional.<sup>44</sup>

From a formal point of view, GATS cannot be considered as a complete set of rules that automatically results in continuous liberalization effects. It rather

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<sup>40</sup> Cf. WTO (2001), pp. 5

<sup>41</sup> WTO (2001), pp. 13

<sup>42</sup> Bundesministerium für wirtschaftliche Zusammenarbeit und Entwicklung (2003b), pp. 4

<sup>43</sup> Altmann (2004), pp. 140: „... ist gegenwärtig mit das umstrittenste Teilabkommen der WTO.“

<sup>44</sup> Cf. Senti (2000), pp. 603

contains simply the *commitment* of the contracting parties to further liberalization talks.<sup>45</sup> Thus, it is only the very first step towards a free flow of services.

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<sup>45</sup> in accordance to that, section 3.1 places importance on the *willingness* of contracting states to reach further liberalization

The layout of the agreement as a combination of general rules, individual commitments and exemptions by country have led to greater individual flexibility with respect to liberalization efforts on the one hand, but on the other to an erosion of the relevance and credibility of the GATS: The principle of national treatment is no general obligation that applies to all services. Its validity in the service sector is rather dependent upon the commitments made by each particular country in its schedule.<sup>46</sup> From that perspective, the high flexibility of countries in determining independently which sectors to open (which very often serves as an argument in favour of the GATS) has become a setback of the agreement. On top of that, the national treatment principle only applies to services explicitly mentioned in the country schedules. Other, more recent and innovative types of services are not automatically included, but further and further negotiations are required. For this reason, several critics have stated, GATS is no real tool for continuous liberalization, it just locks in the current status quo.<sup>47</sup>

Similarly, the MFN rule is penetrated by several exemptions many countries have insisted on in an attempt to protect domestic service industries. How can an efficient, fair and free international trade in service be achieved with all these exceptions and limitations? This “flexibility” in connection with the broad definition of commercial services via the four modes of supply has left plenty of space for protectionist measures. In the GATS, labour intense services are nearly as highly protected as labour intense goods used to be in the GATT - the burden of that lies at the side of the developing countries whose major services export is labour.<sup>48</sup>

Until today, with some exception in the areas of telecommunications and financial services, the impact of GATS is not as material as it was promised.<sup>49</sup> Even the WTO implicitly admits “... while the negotiations succeeded in setting up the principle structure of the agreement, the liberalizing effects have been relatively modest. ... most schedules have remained confined to confirming status quo market conditions in a relatively limited number of sectors.”<sup>50</sup>

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<sup>46</sup> Cf. Eiteljörge (1998), pp. 167

<sup>47</sup> Cf. Senti (2000), pp.605

<sup>48</sup> Cf. Langhammer (2002), section 2.3

<sup>49</sup> Cf. Senti (2000), pp. 604

<sup>50</sup> WTO (2004), pp. 9

## 4 Special Areas of Controversy

### 4.1 Public Services

The area of public services includes some highly sensitive sectors such as education, health care, public transport or museums and libraries.<sup>51</sup> These fields of services as areas of “core governmental responsibility” used to be (and to certain extent still are) subject to close regulation, supervision and control by authorities.

GATS-related scepticism very often refers to that area. It is feared, that as a result of GATS, any service that used to be provided by governments as a public good might be opened up to private, exclusively profit-driven multinational corporations - which might mark the very end of social welfare.<sup>52</sup> However, it has not been defined clearly, whether these public services are covered by the GATS rules at all. If they satisfied the criterion for “being provided in the exercise of governmental authority” the whole accord would not apply.<sup>53</sup> On the other hand, if they fell under GATS, the “built-in commitment” of the provision would impose the obligation to reach progressive liberalization in these areas as well. That in turn could mean, competition and profit-drive in essential social-economic areas, presumably to the detriment of the customer. In the fields of health care and education for instance, GATS would probably strengthen and accelerate current tendencies towards a “two-class-treatment”. Many countries, especially the U.S., where these areas have massively been put under market laws, could serve as a negative example and a justification to reject GATS with regard to them.<sup>54</sup>

It is sometimes even doubted, that the exemption for “services in the exercise of governmental authority” plays a role at all<sup>55</sup>: In many states including Germany, education and health care system for example do not fulfill the requirements<sup>56</sup> as

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<sup>51</sup> in German the expression „öffentliche Daseinsvorsorge“ is used for these kinds of services

<sup>52</sup> Cf. Barlow (2001)

<sup>53</sup> Cf. Altmann (2004), pp. 142 et seq.

<sup>54</sup> u.A. (2004)

<sup>55</sup> Cf. Barlow (2001): „Since hardly any service sector in the world is entirely free, this exemption is increasingly meaningless.”

<sup>56</sup> i.e. provided neither on a commercial nor competitive basis, cf. section 3.1

they are provided not only by public, but also by private institutions.<sup>57</sup> Hence they are in principle subject to the GATS rules, at least to the general principles of MFN, transparency and progressive liberalization. The principles of national treatment, which would entitle commercial service providers to the same rights as far as public funding, subsidies and tax allowances are concerned, would only apply if the relevant sectors were explicitly named in the country schedule(s).<sup>58</sup> In theory, the decision to include sectors in that list of liberalization concession lies exclusively with the national governments themselves.<sup>59</sup> Any government is said to be free to decide which sectors to open, which markets to regulate or which ones to exclude completely from GATS.<sup>60</sup>

On the other hand, an entire exclusion of public services from domestic and international competition does not seem to be advantageous either. The objective of a high quality, efficient and reasonably priced system of public services accessible as well as affordable to anyone appears to be more feasible with a certain amount of competition as long as commercial objectives (such as profit maximization) are not more highly valued than satisfying social and societal needs.<sup>61</sup> But there are some doubts, whether the GATS framework at its current state adequately safeguards key social services from commercialization and drive for profits as long as governmental funding of core areas of public services is considered as a discriminating, unfair subsidy and serves as justification for claims from foreign service providers<sup>62</sup>.

A further aspect of criticism is the claim „... that the right to maintain public services and the power to enforce health and safety standards are under threat ...”<sup>63</sup> under the regime of GATS. If this was right, critics even perceive risks for the democratic constitutions of Western societies.<sup>64</sup> However, putting certain public service sectors under the rules of GATS does not automatically limit the right to legitimate the execution of the service itself by national rules and norms. The right

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<sup>57</sup> Cf. Hassler (2003), pp. 13

<sup>58</sup> Cf. Altmann (2004), pp. 142 et seq.

<sup>59</sup> however, within the European Union the competence for the WTO contracts and negotiations lies with the European Commission, not with national governments; cf. Altmann (2004), pp. 137

<sup>60</sup> Cf. Zänker (2002)

<sup>61</sup> Cf. Hassler (2003), pp. 13

<sup>62</sup> Cf. Wieczorek-Zeul (2003), pp. 15

<sup>63</sup> WTO (2001), pp. 2

to regulate according to national political objectives is even explicitly mentioned in the text of the agreement.<sup>65</sup> Therefore, the argument that national sovereignty with regard to rules and norms was under threat in case of a free international service market is simply wrong.

All in all it can be summarized that the fear of the agreement with regard to public services is slightly exaggerated. Cautiously opening even very sensitive sectors of public services for international competitors might stimulate competition if legal constraints for social objectives are set accordingly.

## 4.2 Developing Countries

From the beginning of the GATS negotiations, the developing countries considered a liberalization of service trade as a threat for their own economies and parts of their sovereignty.<sup>66</sup> Despite the fact that economic growth of the developing countries and their integration into the world trading system is heavily promoted in the written text of the GATS<sup>67</sup>, these countries do not appear of having benefited massively from the agreement. So far, their situation does not seem to have improved significantly as a result of the agreement. As German Secretary for Co-Operation and Development has pointed out, the international trade system still prefers countries that are economically more powerful; its impacts are still distributed asymmetrically to the detriment of the developing countries.<sup>68</sup>

In theory, GATS should help them to gain better access to potential markets as well as to improve and accelerate technology transfer to establish their own competitive service companies.<sup>69</sup> In addition, developing countries are not expected to liberalize as many sectors and types of transactions as the

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<sup>64</sup> Cf. Ladwig (2002)

<sup>65</sup> Cf. WTO (2001), pp. 11

<sup>66</sup> Stoll/Schorkopf (2002), pp. 178

<sup>67</sup> Cf. Senti (2000), pp. 572

<sup>68</sup> Wiczorek-Zeul (2003), pp. 9

<sup>69</sup> Cf. Senti (2000), pp. 605

industrialized countries; their special situation of economic development is acknowledged and supported by the GATS and by the WTO itself.<sup>70</sup>

In practice, most of the developing countries are hardly able to open much of their service sectors to international competition since they are not competitive and massively inferior to most Western multinational corporations.<sup>71</sup> Putting their “infant industries”<sup>72</sup> under the GATS regime would not increase their economic prosperity as claimed by the WTO, but rather cause a complete domestic collapse of these service branches. From this point of view, the value of their flexibility in terms of opening their market “step by step” as its granted by the agreement falls down to zero.<sup>73</sup>

In recognition of these aspects, developing countries are entitled to maintain more trade barriers and liberalize at a lower rate. Consequently, with exception of tourism, only few liberalization commitments have been made by them.<sup>74</sup> On the other hand, these trade barriers do also and especially limit trade flows between developing countries which does not work in favour of an accelerated economic development either.<sup>75</sup>

There are indeed some arguments for a cautious liberalization of service sectors in developing countries: The general services infrastructure may be improved, labour demand might go up due to foreign direct investment and the know-how transfer could be facilitated. Often, just an open market results in the availability of services, which in turn are essential input for other industry branches.<sup>76</sup> In the fields of water supply for instance, a partial liberalization incorporated in social regulations could highly improve the water supply in many countries of the Third World.<sup>77</sup> Similar aspects are conceivable in case of the telecommunications infrastructure for many of these countries.

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<sup>70</sup> Cf. WTO (2001), pp. 7

<sup>71</sup> Cf. Hassler (2003), pp. 17

<sup>72</sup> this term describes branches that are still under development and need to be safeguarded in order to grow and gain global competitiveness; this argument is often used to justify protectionistic measures, Cf. Hauser/Schanz (1995), pp. 194

<sup>73</sup> Cf. Bundesministerium für wirtschaftliche Zusammenarbeit und Entwicklung (2003b), pp. 6

<sup>74</sup> Cf. WTO (2001), pp. 8

<sup>75</sup> Langhammer (2002), section 4.2

<sup>76</sup> Wieczorek-Zeul (2003), pp. 11

<sup>77</sup> Cf. Hassler (2003), pp. 16

After all, the GATS creates a dilemma for the developing countries: On the one hand it offers promising opportunities to accelerate the extremely important know-how transfer whereas on the other hand, a liberalized service market could destroy domestic service industries in the worst case.

### 4.3 Audio-Visual Services

The field of cultural services such as movies, music and theatres is another issue where GATS-related disadvantages are feared.<sup>78</sup> Currently, audio-visual services are not covered by GATS at least as far as the EU is concerned. But in principle, any area can be subject to further negotiation rounds following the general commitment of “progressive liberalization”.<sup>79</sup>

Similar to public services, the principle of national treatment would make any promotion and preferential treatment of national productions of movies, music and television discriminating. Either these actions had to be abolished or they had to be granted to all national as well as international providers. Even the public funding of certain broadcasters via general fees would be illegal. As the powerful US-American entertainment industry has much more financial resources and experiences, they could become even more dominant than they are right now, not only in the U.S., but worldwide. The worst case then is described as the “American Media Imperialism” drives out the country-specific cultures.<sup>80</sup>

Certainly, the protection of the culture sector also pursues economic objectives. Almost any movie industry in the world is not as competitive in order to survive against the American audio-visual corporations.<sup>81</sup> But compared to the other major fields of controversy, the potential advantages in that specific area seem to be even lower. Based on that, demands for special treatment and indefinite exemption of cultural services from the GATS might be justified. It appears to be right that cultural goods and services should not be treated as mass consumption

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<sup>78</sup> Cf. Beise (2001), pp. 115

<sup>79</sup> Cf. Hassler (2003), pp. 7

<sup>80</sup> Cf. Hassler (2003), pp. 7; attac Marburg (2003), pp. 13; Beise (2001), pp. 115

<sup>81</sup> Cf. attac Marburg (2003), pp. 14

goods, special clauses should rather apply to them. Currently, the EU (whose GATS-relevant decisions are binding for Germany) has indefinitely excluded this area of services from the MFN principle.<sup>82</sup>

#### **4.4 Cross-Border Migration within Mode 4**

International migration of persons seeking permanent residence and employment is not covered by the GATS. Nevertheless, the definition of the service term within the GATS involves the cross-border movement (“temporary migration”) of natural persons for the purpose of supplying a specified service. The fourth mode of supply - presence of natural persons - would normally allow citizens of any WTO-member state to supply a service within the territory of another member. In theory, service provider offering cheaper labour moving to foreign countries would highly stimulate competition on the labour market abroad. Therefore, as far as labour-intense services are concerned, the developing countries as potential labour exporters would be able to capitalize on their comparative advantage; international labour division would be enforced.

Given that nowadays 64 % of all German employees are directly or indirectly related to the tertiary sector, studies estimate that liberalization in general reduces the number of domestic jobs in Germany (and presumably in most other Western “high-wages” countries). Especially demand for less qualified people is expected to decrease as a result of rising international competition in the labour market. This scenario can be assumed to occur much faster if Mode 4 was entirely opened.<sup>83</sup>

But especially because of this, Mode 4 has become subject to a huge number of national regulations aiming at discriminating foreign labour suppliers.<sup>84</sup> Examples are extremely severe procedures regarding immigration, stay or acknowledgement of qualifications.<sup>85</sup>

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<sup>82</sup> Cf. Bundesministerium für wirtschaftliche Zusammenarbeit und Entwicklung (2003a), pp. 16

<sup>83</sup> Cf. Ladwig (2002)

<sup>84</sup> Cf. Wiemann (2003), pp. 59

<sup>85</sup> Cf. Wiemann (2003), pp. 59

The developing countries are urging towards deregulating this mode of supply.<sup>86</sup> Nevertheless, fears of a broad liberalization of the international market for labour are currently not justified as the industrialized countries are very unlikely to agree to an extensive opening of their domestic labour markets. This topic will surely be one of the most crucial and dominant aspects in future liberalization talks as well as in protests of globalisation opponents. It can be doubted, that a widely accepted solution will be reached shortly. This is even worse as further commitments by the developing countries might depend on the willingness of the industrialized nations to deregulate this area of cross-border migration within Mode 4. If no party is willing to make concessions, the whole process could come to a standstill.

## **4.5 Negotiation Process and Irreversibility of Concessions**

The process of negotiation upon liberalization concessions within the GATS has become subject to fierce criticism. Negotiations are based on a request - offer system: Members are “offering” liberalization concessions for areas they are willing to and “requesting” other members to open sectors they wish to access.<sup>87</sup> This used to be done “behind closed doors” with only little tendency to inform the public about the current status. Based on that, the negotiations might be suspected to follow the principle of “you scratch my back and I scratch yours”. As a result the whole agreement tends to be perceived as undemocratic, non-transparent and secretive for non-experts.<sup>88</sup>

Critics in Germany state that agreements to liberalization concessions are made without involving those who tend to be most heavily affected, there was and still is hardly any public discussion specifically about GATS.<sup>89</sup> However, in order to receive support and objectivity from the broad public instead of fear and hostility, transparency and the involvement of the civil society appears to be absolutely necessary. In reaction to the massive criticism, the WTO has improved its

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<sup>86</sup> Cf. Senti (2001), pp. 620

<sup>87</sup> Cf. Hassler (2003), pp. 11 et seq., Altmann (2004), pp. 145

<sup>88</sup> Cf. Hassler (2003), pp. 11 et seq.

<sup>89</sup> Cf. u. A. (2004)

information policy since 2003; nevertheless, the existence of a democracy deficit is still acknowledged.<sup>90</sup>

In the area of negotiations the contrast between developing and developed countries becomes evident once again. Due to their weak financial and structural powers, the participation of the developing countries in the negotiations is often seen as insufficient in order to ensure equal and non-discriminating results. They and their interests appear to be de facto excluded, even betrayed as promises of the industrialized countries regarding the goods-related textile and agriculture sector have not been kept.<sup>91</sup>

Once concessions regarding specific fields of services are made, they are nearly irreversible. If a member state wishes to re-exclude a sector from its country schedule, it could be forced to compensate any affected member (which is all the 147 others). There is no opportunity of “testing” the impacts of opening certain sectors to international competition - once it has been opened, there is hardly any chance to close it again in case of adverse effects that have not or could not have been foreseen.<sup>92</sup> That might be one of reasons why progress in service liberalization has remained behind expectations so far.

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<sup>90</sup> Cf. Bundesministerium für wirtschaftliche Zusammenarbeit und Entwicklung (2003a), pp. 19

<sup>91</sup> Cf. Hassler (2003), pp. 17

<sup>92</sup> Cf. Altmann (2004), pp. 143

## 5 Conclusion

The WTO contract *General Agreement on Trade in Services* (GATS) has been subject of this special research paper. The main purpose was to figure out and assess pros and cons of the agreement.

Whether the GATS has been a success story with positive impacts exceeding adverse effects for global trade and welfare cannot be pointed out universally for all aspects, service areas and stakeholders. They rather have to be assessed precisely on a case-by-case basis. Nevertheless, some general tendencies have become evident:

The contract has its strengths in the broad definition of the services term, in its layout giving the member states plenty of flexibility with regard to their liberalization commitments and in creating a more predictable and transparent business environment for trade in services. Furthermore, it *might* improve market access, services infrastructure and competition; under some other crucial preconditions it might even accelerate technology transfer and economic growth especially in less developed countries.

On the other hand, the agreement has its deficiencies in recognizing and acknowledging the requirement for special treatment of some very sensitive social-economic service sectors that are likely to be harmed by unlimited competition in open markets. Moreover, welfare gains from services liberalization are not allocated equally among all members - so far the gap between developing and industrialized countries has not been reduced substantially as a result of GATS.

Today, 10 years after the provision came into force, the expectations with regard to global welfare and sustainable international growth triggered by the accord have not been met. By 2002, it has not been managed to create a standardized, uniform market for services. That was mainly due to national trade barriers which then still existed at a massive rate. Existing restrictions have slowed down worldwide growth to the detriment of consumers, corporations and countries of the Third

World.<sup>93</sup> Given the slow pace of liberalization measures and multilateral agreements, one can assume that the situation has not improved within the last 3 years since these judgements were made.

GATS is no complete set of rules that guarantees a constant level of liberalization. It is rather the starting point for further negotiations. The level of liberalization is more likely to decrease as soon as new types and innovations of services enter the market. A continuous negotiation process is necessary. The success is first and foremost dependent upon the member state's willingness to make concessions even if they do not benefit from them in the very first place.<sup>94</sup>

The near future might be decisive for the destiny of the GATS. If the WTO in cooperation with its member states manages to reduce the erosion of relevance of the accord and to extend the basis of the agreement, it will play a key role in a relatively open world trade order. However, if they fail, GATS will remain of minor importance as a static act of locking in the status quo.<sup>95</sup>

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<sup>93</sup> Zänker (2002)

<sup>94</sup> Cf. Senti (2000) , pp. 605 et seq.

<sup>95</sup> Cf. Senti (2000), pp. 603

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## **Declaration of Academic Integrity**

according to § 4 Abs. 1 APRO BA Wirtschaft as of 27-May-2003

This is to declare that I have independently composed the special research paper

*“Pros and Cons of the General Agreement on Trade in Services (GATS)”*

without any further devices except of the ones mentioned in the bibliography. The thoughts taken directly or indirectly from external sources are properly marked as such.

Stuttgart, 4-Feb-2005

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Oliver Hilger