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1 Introduction
Tackling EU Free Trade Agreements

This paper forms part of a series of eight briefings on the European Union's approach to Free Trade Agreements. It aims to explain EU policies, procedures and practices to those interested in supporting developing countries. It is not intended to endorse any particular policy or position, rather to inform decisions and provide the means to better defend them. The views expressed in the briefings do not necessarily reflect the views of the publishers.

Why Free Trade Agreements?

There are large and increasing numbers of Free Trade Agreements (FTAs) being negotiated, many of which feature far-reaching commitments on a broad range of issues.[1]

Trade agreements can be important. For neighbouring countries at similar levels of development, they can create larger, more effective and more attractive markets. Economic and political ties can be mutually reinforcing. However, when FTAs occur between countries at vastly different levels of economic development, they often serve to undermine rather than support the development process.

The incidence of North–South agreements is on the rise. Part of UNCTAD's 2007 Trade and Development Report was devoted to an analysis of North–South FTAs.[2] This is a summary of their findings:

- A broad range of issues that have serious development implications are being included in FTAs. These include issues that developing countries rejected at the World Trade Organization (WTO), including investment, government procurement and competition.
- Developing countries are required to implement broad and deep liberalisation in market access (for example, in goods, services and government procurement).
- Any market access gains for developing nations are likely to be severely limited because the reduction or elimination of (most) agricultural subsidies in rich nations are not included in FTAs. Gains are also limited by restrictive rules of origin, the prevalence of non-tariff measures and supply-side constraints.
- Many of the elements of FTAs reduce policy space, in some cases very significantly. If future FTAs are designed around current FTAs, this will "reduce or fully remove policy options and instruments available to a developing country to pursue its development objectives."[3]
- Reciprocity prelcudes special treatment that could be offered to developing countries in the context of multilateral agreements.
- North–South FTAs tend to weaken existing regional trade blocs.

UNCTAD (the UN Conference on Trade and Development) concludes that whilst FTAs have the potential to provide developing countries with new trading opportunities, these may be quickly eroded if the same developed nation negotiates FTAs with other countries. The size and durability of any gains in trade and

The term **'Free Trade Agreement'** (FTA) is often used to represent both bilateral and regional trade deals. FTAs can be negotiated between two or more countries, and can cover a range of trade issues (for example, tariffs on goods) and trade-related issues (for example, investment, services, intellectual property and competition). Where the FTA has a common external tariff across all members, this is termed a 'customs union'.

1 Quantifying FTAs is problematic. This is because the most commonly used source of information (the World Trade Organization) exaggerates the total number, not least because FTAs in goods and services are notified separately. In addition, many FTAs are in the process of notification, at different stages of implementation or are simply extensions of existing FTAs. Notwithstanding the above, at the end of 2006, 367 FTAs had been notified to the WTO of which 214 were in force. Of these, 158 FTAs cover trade in goods, 43 cover trade in services and 13 are extensions covering existing agreements. A large number of FTAs are in the process of being finalised, many of which contain provisions on trade in services.

2 UNCTAD, 2007. Trade and Development Report, 2007.

3 Ibid. Page 63.

investment are also highly uncertain. This is because short-term gains can be eroded if increased imports lead to balance-of-payments and external debt problems.

Critics of North–South FTAs have rightly pointed out that the different levels of political and economic power between, say, the EU and a third party leave the latter at a distinct disadvantage in bilateral negotiations compared to multilateral talks.

This imbalance has been evident in the 'Economic Partnership Agreement' (EPA) negotiations with African, Caribbean and Pacific (ACP) countries. Many of these countries have disagreed with both the content and process of the agreements. Invariably, many of their concerns have been dismissed by the European Commission (EC) but not without numerous delays to the negotiating timetable. To date, fewer than half of the developing countries involved have concluded any form of agreement with Europe, despite the power politics and tactics the EC has used to undermine many development components of EPAs and also the principle of partnership on which they should be based. The EC has:

- dismissed many of the proposals put forward by ACP countries;
- disregarded ACP institutions and processes;
- pushed issues that ACP countries had rejected within the WTO back onto the EPA agenda;
- threatened the loss of market access into the EU if ACP countries did not sign an agreement;
- dismissed consideration of alternatives despite a legal requirement to do so;
- sidelined dissenting voices, such as civil society organisations and trade unions;
- put deadlines before development.

However, in other talks, developing countries have been able to use the fact that the EU tends to negotiate with regional blocs to exert more leverage and resist EU pressure. One example is the EU–Mercosur negotiations. These started in 1999 but were suspended in 2004 because of divergent positions between the EU on one hand and Brazil, Uruguay, Argentina and Paraguay on the other. The Mercosur countries would not be brow-beaten into accepting an FTA with the EU when they clearly saw that the potential deal on the table was not acceptable.

EU FTA Strategy and 'Global Europe'

The EU has the largest number of FTAs of any major power, accounting for nearly half of those notified to the WTO and in force. Many of these are agreements with other countries in Europe, but in 2006, the EU announced its new 'vision' for future trade policy and negotiations in *Global Europe: Competing in the World*.[4] One of the main purposes of the Global Europe strategy is to promote Europe's commercial interests in world markets. It places a central emphasis on the rapid conclusion of a number of new far-reaching free trade agreements (FTAs) in nearly all global regions – and this would include about 120 developing nations (see Table 1 on page 3). If all these FTAs with developing countries (including China) were completed successfully, they would cover about 40 per cent of all EU trade with the rest of the world.

EU FTAs that are currently under negotiation (and some that have been completed recently) go considerably beyond WTO commitments. As well as deeper and quicker tariff liberalisation, EU objectives include negotiation on trade-related issues (known as the "Singapore Issues" in WTO circles and rejected by developing countries in that forum); and stronger rules and procedural requirements placed on intellectual property, food standards and other non-tariff measures.

4 European Commission, 2006a. Global Europe: Competing in the World. trade.ec.europa.eu/doclib/docs/2006/october/tradoc_130376.pdf

The communication reveals that the EU's overall strategic aims are:

- New and growing markets for EU goods and services. *Global Europe* identifies the need to forge strategic links with economically significant emerging markets with prospects for economic growth, such as India, Mercosur, Russia, Gulf Co-operation Council, South Korea and ASEAN. China is also mentioned for special consideration and a separate policy paper has been published.[5]
- The geopolitics of trade. The EC has identified partner countries according to the number and scope of FTAs they have underway with other countries, notably the US. As well as the 'priority' FTAs, new ones are underway with nations in Central America and the Andean Community. The EU has fewer strategic interests in these regions but clearly the fact that the US has, or is negotiating, FTAs with these countries, is an important consideration. It is no coincidence that the EU's existing FTAs, and those in advanced stages of negotiation, also mirror the ambitions of the US; for example EU–Mercosur is similar to the US–FTAA; EU–Mexico similar to the US–NAFTA and so on.
- Targeting higher levels of protection against EU export interests. The EU commits to reducing tariffs in third countries to open new markets for its exporters – despite some recognition that this can cause problems including revenue and employment losses and bankruptcies in developing countries. The EU is also targeting other barriers to trade (i.e. non-tariff measures) in what it calls "behind-the-border regulation". Important in respect of non-tariff measures is the proposal that would allow third-party stakeholders (i.e. EU companies) the right of prior consultation on any measure that the third party might want to introduce.
- The EU wants to ensure access to resources and raw materials for its producers. Those mentioned include agricultural materials, energy, metals, minerals, scrap metal, hides and skins.[6,7] In this regard the EU sets out to reduce or eliminate export taxes and other export restrictions. However, these are often in place in order to safeguard natural resources for environmental and developmental reasons.
- The prospect of introducing and enforcing "new trade-related areas" into FTAs, some of which have been rejected at the WTO. The EU lists intellectual property, services, investment, public procurement and competition as "areas of economic importance to us".[8] These are areas of regulation that have important development implications for the countries concerned.

5 European Commission, 2006b. *Global Europe: EU-China Trade and Investment, Competition and Partnership*. http://trade.ec.europa.eu/doclib/docs/2006/november/tradoc_131234.pdf

6 European Commission, 2006a. Op cit.

7 European Commission, 2007. *Global Europe: A Stronger Partnership to Deliver Market Access for European Exporters*. http://trade.ec.europa.eu/doclib/docs/2007/april/tradoc_134507.pdf

8 European Commission, 2006a. Op cit.

Table 1: EU and US FTAs with developing countries

	EU	US	
Existing FTAs	Euromed (9 countries) South Africa Mexico Chile	Bahrain Chile Morocco Singapore NAFTA (1)	Jordan Oman CAFTA/DR (6) Peru
Advanced stages of negotiation/ pending approval	Economic Partnership Agreements (76) Gulf Co-operation Council (6)	South Korea Colombia	Panama
Currently suspended	Mercosur (4 excluding Venezuela)	FTAA (33) SACU (5) Ecuador	UAE Thailand
First stages of negotiations (i.e. the EU's 'new FTAs')	India South Korea Andean Community (4) ASEAN countries (10) Central American Nations (6)	Malaysia	
Planned	China	Other ASEAN countries	

The EU is planning further FTA negotiations with a number of non-developing countries, particularly Russia and Ukraine, after these countries have joined the WTO.

Key lessons learnt from previous negotiations with the EU: How this manual can help

This manual is for those working towards trade agreements between Europe and developing countries that will really support development, whether they be trade officials, members of civil society organisations, private sector actors, or policy analysts. It is assumed that readers already have an interest and some knowledge of trade issues.

To date, little research has been conducted as to the lessons learnt from previous negotiations between the EU and third parties. This manual draws on academic research and NGO experience of the current and past EU negotiations to help draw out lessons learnt. Our experience shows that in order to influence the content of European trade agreements so that they serve development interests better, understanding in four main areas is important:

- Understanding the political context of Europe, within which the negotiations are conducted, is critical. There is a wide divergence of views within the 27 EU member states; it is important to understand these different views, and identify allies amongst member states as potential lobby targets. The EU negotiating teams are led by officials and civil servants who do not have a popular mandate and are largely unaccountable. Moreover, they often have a weak understanding of the links between trade policy and development. It is important to understand how to negotiate with technocrats in this regard.
- Understanding the bureaucratic processes and negotiating mindset will help to challenge some of the worst tactics (bullying, divide-and rule, etc) and help you to take the initiative and turn the tables on the EU rather than simply following procedures and processes set out by the EU.
- Understand the EU's offensive and defensive interests – both by issue and by sector – and potential trade-offs. Its defensive interests are usually to do with agriculture whilst its offensive agenda includes industrial goods, services, investment, competition, government procurement and intellectual property. In this respect, a detailed knowledge of tariff structures is critical to a successful negotiation.
- Understand your region's offensive and defensive interests, including development co-operation. Observing what concessions have been requested and even won in the past by other developing-country partners is important in this regard.

How to use the manual

The manual provides the following tools:

- Definitions of key terms and explanations of legal language to enable observers to understand the complex and often arcane texts of trade negotiations.
- An introduction to the trade policy-making and negotiating process within the EU.
- An overview of evidence and experience relating to the development implications of different trade policy choices and negotiating outcomes.
- An analysis of EU interests in the area under question.
- An analysis of developing-country interests in the area under question.
- An overview of past practice in negotiations between the EU and developing countries and regions – showing concessions won and tactics used by both sides.
- A guide to key references and resources to help you find information you will need to develop positions and analysis.

We hope that the manual will be useful to help interested groups to identify areas for further investigation and research, to analyse EU proposals and their development implications and ultimately to engage more actively with and influence the process of negotiations in their country and regions.

It is useful to note that this manual does not provide all the information that observers will need to understand the specific interests of every country or region – these will vary according to local development needs, strategies and economic structures, as well as the varying interests of the EU with respect to each partner.

While this manual is not neutral, neither does it aim to give a definitive answer on the development implications of any particular EU proposal or negotiating outcome. Liberalising services, for example, can be good or bad for development depending on the conditions in place and how this liberalisation fits with the development strategy of the country concerned. Instead, the manual identifies what these conditions might be, and what affects the contribution of services liberalisation to development.

The manual is not a final word on EU trade deals – as negotiations and understanding progress we will update each briefing as necessary. We welcome your feedback to assist us in this.

Please contact: tradeandcorporates@actionaid.org

Important information and where to find it

Global Europe (plus supporting annex)
http://ec.europa.eu/trade/issues/sectoral/competitiveness/global_europe_en.htm
http://trade.ec.europa.eu/doclib/docs/2006/october/tradoc_130370.pdf

Information and analysis on FTAs
www.bilaterals.org/

Information on EU FTAs
http://ec.europa.eu/trade/issues/bilateral/index_en.htm
http://trade.ec.europa.eu/doclib/docs/2006/december/tradoc_118238.pdf
http://trade.ec.europa.eu/doclib/docs/2006/december/tradoc_111588.pdf

Sustainability Impact Assessments of EU FTAs
http://ec.europa.eu/trade/issues/global/sia/studies.htm

Information on US FTAs
www.ustr.gov/Trade_Agreements/Bilateral/Section_Index.html
www.ustr.gov/Trade_Agreements/Regional/Section_Index.html

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1. Introduction: Tackling EU Free Trade Agreements
2. Inside European Union Trade Policy
3. The EU's approach to Free Trade Agreements: Market Access for Goods
4. The EU's approach to Free Trade Agreements: Services
5. The EU's approach to Free Trade Agreements: Investment
6. The EU's approach to Free Trade Agreements: Competition
7. The EU's approach to Free Trade Agreements: Government Procurement
8. The EU's approach to Free Trade Agreements: Intellectual Property

We will be updating these briefings as negotiations and understanding progress, and would welcome your feedback.

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2 Inside European Union Trade Policy

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What's at stake?

The European Union is the world's largest trading power and, taking into account combined contributions of the European Commission and individual member states, also its largest aid donor.

This paper provides insight into the players, processes and policies that guide the European Union's external activities on trade and their interaction with development assistance.

This understanding is important as:

- European Union negotiators often use arguments relating to their powers or processes to justify behaviour in negotiations;
- it is helpful in identifying allies, opportunities and targets to influence change.

Key players

This section outlines the roles and responsibilities of key players in European Union trade policy-making, and their interaction with civil society.

European Commission

The European Commission (EC) has the exclusive right to initiate trade policy proposals and is the EU's sole representative in trade negotiations. It has a "collegial" structure, made up of different "Directorates General" (DGs) with responsibility for different areas of community policy. Each DG has a Commissioner and a Director General. The Commissioner has a political mandate from member states with the endorsement of the European Parliament and is the equivalent of a Minister; a Director General does not have the same limited term of appointment and is a civil servant. The Directorates cannot operate in each other's respective spheres so must co-operate where these overlap or combine. This is achieved formally through inter-service consultation, where affected Directorates can comment on each other's proposals before sending recommendations for discussion and decision at the weekly meetings of the college of commissioners. It also happens informally through contacts between officials.

Key Directorates General with respect to trade negotiations

DG Trade: has responsibility for commercial policy and external trade and is generally the main player in trade negotiations.

DG Relex: Responsible for external relations with international organisations, EC delegations overseas and the EC's participation in common foreign and security policy. It also has responsibility for relations with particular regions: Korea, Southern Mediterranean, Latin America and Asia. DG Relex has some role in negotiations with those regions, although DG Trade will lead negotiations on trade.

DG Development: has responsibility for the EC's development policy and relations with the African, Caribbean and Pacific regions (ACP). European Development policy is laid out in the EU Consensus on Development that identifies a series of areas and cross-cutting issues for community intervention.

Other relevant DGs include: Taxud (responsible for tax and customs policy including Rules of Origin), Agri (agriculture policy), Fish (fisheries policy), Competition, Markt (intellectual property), SANCO (standards).

The EC, as a bureaucratic institution, takes instruction from its member states, via the Council (see below). However significant private lobby activity is also directed at the EC as the body that is instrumental in introducing new areas of activity and establishing the direction of policy. This direct interaction should not be neglected by civil society.

Besides these informal lobbying opportunities, there are two formal channels of interaction between the EC and civil society. The first is the European Economic and Social Committee (EESC) which has a consultative role and whose opinions are forwarded to the larger institutions: the Council, the Commission and the European Parliament. This group represents "organised civil society" including employer and employee organisations. It has access to negotiations, as well as the opportunity to take a speaking role in meetings. Informal civil society organisations (i.e. NGOs) can be represented in the EESC, but in practice have tended to seek to develop their own structures and channels of influence. For European development NGOs, the main umbrella organisation is CONCORD, the European NGO Confederation for relief and development.

The second channel is the Civil Society Dialogue process through which regular debriefings are given by EC officials to civil society – both businesses and NGOs. The meetings take place in a question–answer format, but offer very restrictive opportunities to cross-examine the EC or influence its positions properly. The process has been strongly criticised by NGOs as providing no engagement prior to decision-making and for the tendency for low-ranking officials to attend meetings, rather than those in charge of negotiations. The co-ordination group representing development NGOs, environmental NGOs, business and other interests meets with the civil society contact point to set the programme of CSD meetings.

The Council

The Council comprises ministers from the capitals of member states and is the formal body representing member states on European foreign and trade policy. It has the authority to mandate negotiations and approve deals. It delegates authority to the Commission to lead negotiations on its behalf. During negotiations, the Council considers trade at its regular GAERC (General Affairs and External Relations Committee) meetings and can take "decisions" to guide the conduct of the EC during talks. A significant number of decisions, particularly on issues falling within the exclusive competence of the European Commission (e.g. trade in goods) can be taken by Qualified Majority Voting (QMV). This means that a decision is passed if a two-thirds majority of member states that represent over 62% of the overall EU population vote in its favour. On other issues where the European

Commission has mixed competency with member states (e.g. services and investment), consensus is needed. Whilst the GAERC formally takes decisions, approves deals, etc, the details of trade talks and policies are considered in various council sub-groups mentioned below.

Article 133 Committee (C133)

This is the main committee where representatives of EU member states meet to discuss trade issues regularly. It has a formal consultative role to "assist" the EC in negotiations. It can assert considerable influence on the EC, and is the only body fully briefed on progress in talks and consulted on unpublished proposals. In reality, the EC shapes debate and sets the agenda within the C133. The committee meetings take place at deputy level fortnightly, and at full member level monthly. Officials from EU member state permanent representations in Brussels generally attend the former set of meetings, whilst experts or senior officials from capitals tend to travel to the latter. It has specialist subcommittees that meet to discuss services, textiles and mutual recognition. The C133 is largely secretive – minutes and lists of members are not published officially, although some civil society groups have worked to make at least lists of members available.[1] Whilst business lobby groups regularly meet with C133 committees, this is not yet happening systematically for NGOs.

1 See 'Important information and where to find it' on page 7

COREPER

COREPER prepares the decisions for the GAERC. It is made up of permanent representatives of EU member states and meets fortnightly. After discussion at the C133, COREPER prepares EC proposals for Council approval.

Regional working groups

The regional working groups comprise officials of EU member states who follow trade and foreign policy issues relevant to specific global regions. In principle, these are the discussion forum for regional trade negotiations. However, the C133 increasingly leads on these. Regional groups are still involved. Some relevant groups are the ACP (Africa, Caribbean, Pacific) working group, AMLAT (Latin America) and COASI (Asia, Oceania).

Civil society interaction with the Council mostly occurs at member state level. Informal lobbies with permanent representations are possible, but these officials tend to take instructions from their capital. Some member states meet with interest groups prior to C133 meetings, but this is not universal.

Presidency

Member states rotate presidency of the Council. This allows them in the year prior to their presidency to set the agenda for that period; however, during their six-month tenure they are required to behave more neutrally in Council discussions.

European Parliament

The European Parliament (EP) has a limited role in trade policy (although note that this may change under proposed reforms). It has no consultative status and was turned down for observer status on the C133. It has the power of "assent" if trade deals go beyond core issues into other areas such as intellectual property rights and investment. This means the parliament can approve or refuse ratification. It has exercised this right to refuse in the case of association agreements with Turkmenistan and Belarus.[2] However, the parliament has regular consultations with the European Commission on trade policy, via its International Trade (INTA) and Development (DEVE) committees. Parliamentary committees can also produce reports, petitions and resolutions and hold hearings and debates

2 Human Rights Watch, 4 December 2006

that carry some political weight. If these reports are carried out as part of the work programme of the Committee (decided annually), the Commission must respond. Or they can be at the own initiative of an individual Member of the European Parliament (MEP), in which case they are simply noted by the Commission. MEPs may also ask formal questions on any issue of constituency or other importance to Commission or to Council to obtain precise information on particular points or to force a policy statement to be made. These must be answered within three weeks (written priority question) or, for non-priority questions, within six weeks.

European civil society tends to have close relations with the parliament as it is the most directly representative body of the European Union institutions. As well as taking part in informal lobbying, civil society can provide input on reports and has taken part in hearings alongside Commission officials in the European Parliament.

Process

The external relations framework – linking trade and development

The European Union's common policy on trade and development assistance takes the form of trade and co-operation agreements with countries and regions, sometimes called "Association Agreements". Most agreements have a "three pillar" structure covering financial assistance, trade and other economic reforms, and political dialogue.

The process to achieve these agreements tends to be incremental, the final stage often being the negotiation of an FTA. It is worth remembering therefore that FTAs do not start from scratch – prior treaties and agreements, even if not labeled as trade deals, often include significant provisions relating to economic co-operation.[3]

The links between the three pillars are in fact quite weak. The political dialogue and co-operation chapters have been criticised as being strong on rhetoric but weak in implementation.[4] The European Commission does not impose sanctions in order to reinforce the political dialogue chapter, for example, except that usually there is a clause which allows the European Union to suspend trade if a partner country violates human rights.

The co-operation chapter lays the legal basis for development assistance and agrees priorities for spending. The European Union also adopts multi-annual regional strategies for the implementation of the Community co-operation and aid instruments. These documents guide the implementation of assistance in a given region and outline the different priority sectors of co-operation, the main actors of co-operation, and cross-cutting issues to be considered. On the basis of these regional strategies, the Commission and its delegations in third countries establish in consultation with recipient countries a support strategy and prepare a country strategy paper that includes a 'national indicative programme' for each country. Aid is delivered in accordance with these country strategy papers that are established for periods of three to six years depending on the region. The strategies are subject to annual and mid-term reviews.

One difficulty for developing countries in co-ordinating aid and trade deals with the European Union is that the two processes are not well linked or synchronised. Trade deals usually contain a sustainable development/co-operation chapter that contains promises of assistance and development co-operation, for example on labour standards. However, in practice these provisions are non-binding and lack teeth in implementation. Another difficulty lies in timing: although the trade deal enters into effect immediately, the framework for development co-operation is decided through a separate process that may not coincide with decisions in trade deals.

3 See 'Important information section and where to find it' on page 7

4 ICCO (2007), *The EU–Mexico Free Trade Agreement Seven Years on: A warning to the Global South*

These bilateral agreements are negotiated in the context of a broader framework of relationships between the European Union and the different regions of the world. European Union heads of states and foreign ministers take part in regular summits and ministerial meetings with the different regional groupings where political declarations in favour of strengthened co-operation and dialogue are adopted. Some of these joint declarations are key stepping-stones in co-operation, as was the case for the Barcelona declaration of 1995 that was the starting point of a closer co-operation framework between the European Union and the Mediterranean countries and was followed by the negotiation of association agreements.

Policies

Two principles are meant to guide the interaction between the EC's activities on trade and development:

Policy coherence for development: The EC Treaty (Article 178) states that Community policy in the sphere of development co-operation shall be complementary to the policies pursued by the member states and shall foster:

- the sustainable and economic development of developing countries, particularly the most disadvantaged;
- smooth and gradual integration of developing countries into the world economy;
- poverty eradication in developing countries.

Consistency principle: The Treaty of Amsterdam (1997) states that the EU's development policy should not be subordinated to other external policies, including trade.

Although these principles could be much improved, the two together make a strong case that EU commercial interests should not guide negotiating positions as far as trade policy and negotiations involving developing countries are concerned. Arguably, the effect of these principles has been primarily on the rhetoric of EC officials in trade talks; however, when used in combination with tools such as the sustainability impact assessments (SIAs), they can be a useful basis on which to argue for development interests.

Process of trade negotiations

As mentioned above, negotiations do not start in a vacuum – framework agreements and regional strategies agreed at the political level underpin them.

Negotiating Directive (the mandate)

Before the European Commission can begin negotiating it needs to take its proposals to member states in the form of a draft mandate. This sets out the issues for negotiation, the preferred outcome, and possibly a timetable for negotiations. The Commission drafts the mandate which is then discussed in C133 and COREPER before approval by qualified majority vote at the Council of Ministers. The Commission uses its mandate tactically in negotiations seeing it as an impetus to discuss particular issues, even when these prove unpopular, and as limiting its room for manoeuvre, for example in offering concessions or discussing extra-curricular topics. However, the status of the mandate is ambiguous – it is simultaneously used by the Commission negotiators as a bottom line and a target to achieve. The mandate can be modified (as was the case recently to allow South Africa to negotiate an Economic Partnership Agreement as part of the agreement with the Southern Africa Development Community) or ignored (although Singapore Issues are still in the European Commission's mandate to negotiate at the World Trade Organisation, these issues are no longer on the table). As the mandates are confidential documents, they are not open to public debate or influence, although civil society can raise key concerns with member states or even the European Commission.

Sustainability Impact Assessments (SIAs)

Once negotiations are launched, the Commission must carry out a Sustainability Impact Assessment to evaluate the impact of any proposed deal on sustainable development. These are not intended to influence the direction of negotiations, but to identify any necessary accompanying mitigation measures. This is reflected in the timing of the assessments, which are frequently finalised when talks are near completion or at an end. Civil society can influence the assessment process, suggesting sectors for examining or even proposing, consulting or commenting on drafts. Sustainability Impact Assessments have been criticised as too frequently accepting unproven optimistic assumptions of the benefits of preferred reforms, such as liberalisation.

During negotiations

Only officials of the European Commission, usually from the Directorate General of Trade, sit at the negotiating table on the European side. Member states monitor and influence negotiations via the C133 and occasionally via the General Affairs and Economic Relations Council. Civil society is updated via the Civil Society Dialogue process, and has some opportunity to raise concerns via informal lobbying.

After agreements

Once a deal is agreed, the text goes to the Council for final approval. Where the issue is exclusively European Commission competence, it is approved by qualified majority vote; where there is mixed competence a unanimous Council Decision is required. Assent from the European Parliament is required if the deal falls within its domain, for example if it has budgetary implications or sets up a specific institutional framework. Because of the expansion of the trade agenda, it is now rare that deals are solely within the Commission's competence, and therefore outside the Parliament's domain. Consensus approval by member states and the assent of parliament is generally required for new deals.

National parliaments

National parliaments can present issues for member states to raise within the C133 and improve transparency and scrutiny of the negotiating process. National parliaments can also have a ratification role.

After signing: Implementation and monitoring

The European Union tends to include two elements with respect to monitoring and review within its free trade agreements: dispute settlement procedures and provisions to be able to address possible future problems at the highest political level (ministers). To date no mechanism has been established to monitor the outcomes and impacts of free trade agreements, although agreements include provisions for periodic reviews at ministerial level to track progress in implementing the agreement. As there is no mandate for evidence-based analysis of the impact and no agreement between the parties on what would arise as a result of such assessments (nor the procedures for remedy if anything is going wrong),[5] some observers argue that the European Union is interested not in monitoring the results of its agreements but only in checking the compliance to the agreed commitments.

5 See the cases of EU–Mexico FTA (www.tni.org/reports/altreg/eumexicofta.pdf); and of EPAs (www.ecdpm.org/trade/epamonitoring).

Important information and where to find it

For links to key European institutions and lists of members and contacts, visit:
www.s2bnetwork.org/index.jsp?id=15&random=r0533412941731513

European Commission directory:
http://ec.europa.eu/staffdir/plsql/gsys_page.display_index?pLang=EN

For links to existing agreements and statements on DG Trade's approach to different regions:
http://ec.europa.eu/trade/issues/bilateral/regions/index_en.htm

DG Trade's civil society homepage:
http://trade.ec.europa.eu/civilsoc/index.cfm

DG Trade's Sustainability Impact Assessment homepage:
http://ec.europa.eu/trade/issues/global/sia/news.htm

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3 The EU's approach to Free Trade Agreements
Market Access for Goods

This paper forms part of a series of eight briefings on the European Union's approach to Free Trade Agreements. It aims to explain EU policies, procedures and practices to those interested in supporting developing countries. It is not intended to endorse any particular policy or position, rather to inform decisions and provide the means to better defend them. The views expressed in the briefings do not necessarily reflect the views of the publishers.

This briefing is divided into four sections:

- What's at stake?
- Tariffs and related issues: Analysing what's on offer from the EU
- Non-tariff barriers
- Rules of origin

What's at stake?

For developing countries

Trade can be a powerful force for development and poverty reduction. In the right circumstances, policies that reduce tariffs and other barriers to the movement of goods can increase trade and support development. However, to realise these gains, tariff liberalisation needs to be managed carefully and strategically.

Many agricultural, industrial and fisheries products are critical to human development, poverty reduction, food security, rural development and environmental protection. Properly managing these issues is important, and trade instruments such as tariffs can be significant, for example, in mitigating the potentially detrimental effects of unfair import competition resulting from European subsidies.

The EU is focusing not only on import duties but also export tariffs and non-tariff barriers. Tariffs and non-tariff barriers give a degree of protection to vulnerable and sensitive sectors, provide policy autonomy to the importing nation and raise revenues for the government.

On the offensive side, developing countries might wish to discuss damaging EU subsidies or any persisting barriers to European markets for their own goods. Protection of sensitive sectors through tariffs and non-tariff barriers such as standards are frequently cited as problems affecting potential developing-country exports to the EU. The value of these gains and the likelihood of winning them during a negotiation should be considered in assessing potential trade-offs. As many European tariffs are already at low levels, it is likely that the partner country or region will make greater concessions and face greater costs of adjustment.

Goods trade is the trade in tangibles – such as agricultural, industrial and fishery products as well as wines and spirits.

The 'free movement of goods' (also termed 'goods market access') remains the core element within EU Free Trade Agreements. The free movement of goods in EU FTAs covers issues that might hinder or facilitate trade, including both imports and exports, customs duties (tariffs) and other barriers to trade (also termed non-tariff barriers). FTAs also entail extensive and complicated rules of origin.

Box 1: What's at stake? Development and environmental implications

Policy space

Sustainable development and poverty reduction require policy space large enough for developing-country governments to craft and implement home-grown strategies. As long as all countries are not at equal levels of development, development in poorer nations requires temporary protection from foreign competition – different sectors of the economy will require changing levels of protection depending on the country's level of development.

Historical evidence shows that in order for countries to develop, they must change the composition of their exports, thereby reducing their vulnerability to shocks and generating employment. Developed countries not only export more – they export products with more added value. All advanced countries as well as the Asian tigers used manufacturing tariffs to protect their nascent industries. They only fully exposed firms to international competition when they were strong enough to compete on world markets. The existence of this 'pattern of optimal tariffs' is a key reason why developing countries need to maintain a high degree of policy autonomy.

However, successful development not only requires flexibility in the determination of tariff levels but other policies as well such as subsidies, export taxes and other non-tariff measures. Take export taxes: these are often in place to protect natural resources from over-exploitation (which could be justified under the General Agreement on Tariffs and Trade (GATT) Article XX) or to promote value-added within a particular country. Not only are all these policies under threat in EU FTAs, but many would be eliminated immediately or within a relatively short period of time. Because commitments would be irreversible, these tariffs could not be re-imposed and raised at some future date (the 'standstill principle').

Government revenues and public spending

Government revenues from tariffs are also under threat. In EU–Mercosur, loss of revenue to the Latin American countries could amount to over $4.3 billion which "could have negative impacts on social, educational and health expenditure".[1] Many African, Carribean and Pacific (ACP) governments earn a significant proportion of their revenue from imposing tariffs on imports. African governments rely on import taxes for an average of 25 per cent of their revenues.[2] Under any EU–ACP trade agreement, the hardest hit will be those who trade most with the EU (Nigeria for example will lose $427 million) and those who still have high tariffs (Cameroon will lose $149 million).[3] Specifically, Zambia stands to lose $15.8 million in government revenue, equivalent to its annual HIV and AIDS spending.

Government revenues are also predicted to fall heavily in certain countries in the EU–Mediterranean FTA, particularly Algeria, Lebanon and Palestine but also in Tunisia and Morocco; "if this [loss] is not mitigated by levying the same amount of income by other means, adverse impacts on health, education and social support programmes can be expected."[4]

Impacts on jobs, farmers, producers

If not carefully managed, eliminating tariffs on a wide range of products could result in significant dislocation of local producers as well as trade diversion, loss of output, exports and jobs, and increased imports with further implications for the trade balance and the debt position. In the EU–ACP negotiations, full liberalisation would lead members of the Eastern and Southern Africa (ESA) region to lose $212 million worth of trade with each other, while the EU would increase its exports to the region by $1.1 billion. Studies for Kenya's Ministry of Trade, the International Monetary Fund, and the European Commission indicate that under an EPA, up to 65 per cent of industry in Kenya is vulnerable to the opening up of markets, and millions of rural livelihoods are at stake. The European Commission's own impact assessment in advance of any EU–ACP agreement in West Africa confirms the potential impact of liberalisation: surges of imports could rise by 16 per cent for onions, 15 per cent for potatoes, 17 per cent for beef and 18 per cent for poultry.[5]

1 University of Manchester, 2007a. Trade SIA of the Association Agreement under Negotiation between the EU and Mercosur: The Automobile Sector Study. www.sia-trade.org/mercosur/phase1/MTR_AUTO_FINAL_EN.pdf. Page 39

2 Bilal, S. and V Roza, 2007. Addressing the fiscal impacts of an EPA, ECDPM, May.

3 Karingi, S. et al, 2007. Economic and Welfare Impacts of the EU-Africa Economic Partnership Agreements, ATPC briefing No 6, UNECA. www.uneca.org/atpc/Work%20in%20progress/10.pdf

4 University of Manchester, 2007b. The EU's SIA of the Euro-Mediterranean Free Trade Area. www.sia-trade.org/emfta/en/Reports/Phase2Finalreport Maro6.pdf Ibid, pages 18, 25, 31 and 32

5 PricewaterhouseCoopers, 2005. SIA of the EU-ACP Partnership Agreements – West Africa Agro-Industry.

Box 1: What's at stake? Development and environmental implications continued

The development of the domestic automobile sector in Mercosur, but particularly in Brazil and Argentina, has been a key strategic part of their industrial development. It is one of the sectors being targeted by the EU but could have serious economic and social impacts as a result of an EU–Mercosur deal; output and employment is expected to drop by between 13 and 16 per cent. This could equate to many tens of thousands of people losing their jobs.[6]

All these issues are highlighted in the EU's FTAs with the Mediterranean countries. In an assessment of the liberalisation of industrial products, the negative implications heavily outweigh positive ones. There were particular significant negative impacts for employment/ unemployment. In Algeria, Morocco, Egypt and Tunisia, employment in the total workforce is predicted to fall by 8 per cent. The sectors experiencing the biggest short-term employment losses include food and beverages, textiles and clothing, motor vehicle production, chemicals, iron and steel and wood products.[7]

The impact of the liberalisation of agricultural products in the Mediterranean countries is less severe but nonetheless, the negative implications again outweigh the positive ones. For example, employment falls should be expected in the livestock sector (Egypt) and in sugar, meat and dairy (Morocco); government revenues will fall (in Algeria, Lebanon and Palestine), and food insecurity will increase in food importing countries (i.e. Egypt).[8]

6 University of Manchester, 2007a. Op cit. page 57

7 University of Manchester, 2007b. Op cit. pages 24, 31 and 32

8 Ibid, pages 42 and 43

For the European Union

Agriculture and manufacturing sectors are significant export earners for European countries. Many European exports still face higher tariffs in target partner markets – and addressing this is a key offensive interest for the EU. The European Commission's assessment of growth in goods trade between FTA parties is heavily skewed in favour of the EU. EU trade would grow by 24.2 per cent with ASEAN (Association of South-East Asian Nations), 47.8 per cent with South Korea and 56.8 per cent with India. Yet in contrast, ASEAN trade to the EU would only grow by 18.5 per cent, 36 per cent from Korea and 18.7 per cent from India.[9]

Global Europe (see Briefing 1, Introduction to EU Free Trade Agreements) emphasises that in order to maintain the competitiveness of EU companies, increased market access for goods must be achieved.[10] Much of this market access is aimed at high-growth emerging markets. "[We] need to open markets and create new opportunities for trade and ensure European companies are able to compete fairly in those markets [by] going further and faster in promoting and openness and integration, by tackling issues which are not ready for multilateral discussion and by preparing the ground for the next level of multilateral liberalisation."[11]

As suggested in this quotation, non-tariff barriers and regulatory issues are equally a target of the EU. This covers elements such as quantitative restrictions (export and import bans), standards, technical requirements, conformity procedures, trade defence mechanisms, customs procedures and internal taxation and regulation. A particular priority for the EU appears to be sanitary and phytosanitary measures, standards and export bans. Many of these instruments can be important policy tools for public policy and economic development objectives and do not only have trade implications.

The EU is also targeting export restrictions, such as export tariffs, as it is keen to secure access to raw materials for European firms. These can be tools for developing countries to develop their own domestic processing and manufacturing industries, for example by providing affordable and predictable access to key inputs.

As part of the *Global Europe* strategy, the European Commission conducted a review of market access. The resulting publication shows that the Commission continues to pay lip-service to fighting poverty, development or protecting the

9 Agence Europe, 2007. Council green light to launch of negotiations for bilateral free trade agreements with ASEAN, South Korea and India. 23rd April.

10 European Commission, 2006a. Global Europe: Competing in the World. trade.ec.europa.eu/doclib/docs/2006/october/tradoc_130376.pdf

11 European Commission, 2006a. *Op cit.*

environment. In praising the benefits of market access for EU exporters, development, poverty and environmental issues are not even mentioned.[12]

On the defensive side, domestic agricultural subsidies are not included in EU FTAs and only sporadic reference in the past is made to export subsidies (ie in the EU–South Africa FTA). Agriculture remains the EU's most defensive sector.

12 European Commission, 2007. Global Europe: A Stronger Partnership to Deliver Market Access for European Exporters. http://trade.ec.europa.eu/doclib/docs/2007/april/tradoc_134507.pdf

Box 2: Understanding market access texts: Key terms and definitions

Article XXIV of the WTO's General Agreement on Tariffs and Trade (1994): Under WTO rules, Article XXIV governs the formation of a free trade area between two or more countries. Any free trade area must be concluded within a reasonable length of time and tariffs must be eliminated on 'substantially all trade' between both parties. WTO members have agreed that a reasonable length of time equates to ten years, except under exceptional circumstances. There is no accepted definition of 'substantially all trade' (although the EU interprets this as an average 90 per cent of trade having to be liberalised). No major sector is to be excluded and only products subject to total tariff elimination count towards the 'substantially all trade' target.

Most Favoured Nation (MFN): This is a commitment by a country that it will apply to another country the lowest tariff rate (for example) that it applies to any other trading partner. This is the guiding principle of the WTO. Thus, if a country cuts a tariff on a product to one country, this rate cut automatically applies to all other trading partners. This means that treatment of imports is non-discriminatory. Free Trade Agreements are one of the main areas where countries can deviate from this principle in that they are able to liberalise towards each other without having to offer this liberalisation to other WTO members.

Reciprocity: This is the principle that negotiating parties offer each other comparable concessions in trade deals. It is a generally accepted principle at the WTO, although it tends not to apply to developing countries who are allowed to offer "less than full reciprocity" (i.e. lesser concessions) or even non-reciprocity (no commitments in return – this tends to apply to Least Developed Countries).

Asymmetry: The principle of reciprocity is observed in WTO rules on FTAs, even North–South. However, as the coverage of trade concessions that must be offered by each party is left undefined, the EU sometimes offers to make use of de facto flexibility that this provides. For example, in order to hit the combined coverage target of 90 per cent of trade, the EU might liberalise 100 per cent and its developing country/region partner only needs to liberalise 85 per cent. It terms this approach "asymmetry".

Tariff lines: A tariff line corresponds to one item in the list of classification of goods used by customs authorities when applying border duties.These are usually according to the 'Harmonised System' of classification maintained by the World Customs Organisation. Goods can be differentiated to different degrees, indicated by the number of digits in the HS code. At the two-digit HS level, there are 97 chapters (or sectors). Agriculture is covered by HS chapters 1, 2 and 4 to 24; industrial products are covered by HS 25–97; fish and fish products are covered by HS chapter 3.

Dual pricing: Where the negotiating partner has two different prices, one for the domestic market (usually a lower price) and another for the export market (usually a higher price).

Standstill clause: No new tariffs can be introduced and once eliminated, tariffs cannot be re-imposed or raised. This principle in effect binds tariffs at current applied levels.

Rules of Origin (RoOs): In order to benefit from preferential tariffs or other treatment, producers need to prove that their good originates in one of the countries that benefits from this treatment. This is done by applying the relevant "rules of origin"

Non-tariff barriers (NTBs): These are rules, restrictions or other conditions than tariffs that make it difficult to import goods. These include Sanitary and phytosanitary measures (SPS) that are safety standards relating to food and human, animal and plant health and technical barriers to trade (TBT) that are other standards and regulations that distort trade.

The relationship between the WTO and FTAs

FTAs are covered by multilateral trade rules at the WTO. How trade in goods is dealt with in a North–South FTA falls under Article XXIV of the GATT 1994. South–South FTAs by contrast are covered by another WTO provision the 'Enabling Clause'. These are discussed in more detail in the 'Tariffs' section on page 6.

Market access text, language and proposals from existing and future EU FTAs

	Existing FTAs (Chile)	Draft negotiating mandates (Indian and ASEAN)	Latest developments on new FTAs	'WTO plus' for the negotiating partner?
Import tariffs	"Customs duties on imports shall be eliminated in accordance with the provisions of Articles 64 to 72" Art 60	"The aim of the Agreement will be to dismantle import duties and charges" Annex Para 7		**Yes.** Tariff liberalisation will be deeper and quicker
• **Exclusions**	These are built into the schedules.	"A comprehensive FTA covering substantially all trade" Section 2	To the EU, substantially all trade means 90 per cent. In the ASEAN and Indian FTAs, the EU is pushing for greater than 90 per cent	
• **Transitional periods**	"Customs duties on imports shall be eliminated in accordance with the following timetable" Arts 64 to 72. For Chile, tariffs on industrial products would be eliminated within 7 years, for agricultural products within 10 years, and for fishery products on the date the agreement came into force (i.e. year 0).	"... over a period of time not exceeding 10 years" Annex Para 7	EU will insist on a maximum seven years with India and ASEAN	
Export tariffs	"Customs duties on exports shall be eliminated as from the date of entry into force of this agreement" Art 60	"All customs duties, taxes or charges on exports ... to the other party which are not justified by exceptions under the Agreement shall be abolished upon the application of the Agreement." Annex Para 11	A priority for the EU. All export tariffs will go immediately unless justified under GATT articles XX and XXI	**Yes.** Export tariffs are not covered by the WTO
Trade defence Instruments	Articles 78, 92 and 93. Covers, anti-dumping and countervailing duties, safeguards and shortages clause.	"The Agreement will contain a bilateral agricultural safeguard clause ... the Agreement will include a clause on anti-dumping and countervailing measures [in accordance with WTO rules] ...The Agreement will also integrate commitments that go beyond WTO rules in this area in line with EC rules and previous agreements"	In the EU's new FTAs, the safeguard will only cover agricultural products. Some measures will be 'WTO plus'	**Yes.** The EU has already admitted that its TDIs will go beyond WTO rules.
Non-tariff barriers (esp SPS and TBT)	Articles 75 to 89. See also section below on export bans.	"The Agreement will forbid any ban, restriction or other non-tariff barrier (NTB) to trade which is not justified by the general exceptions" Annex Para 10	The exceptions will again fall under GATT Articles XX and XXI.	**Yes.** Particularly procedural aspects.
• **Import & export bans**	"All import and export prohibitions .... shall be eliminated upon the entry into force of this agreement" Art 76	"All ... quantitative restrictions on exports to the other party which are not justified by exceptions under the Agreement shall be abolished upon the application of the Agreement." Annex Para 11	A priority for the EU. All export restrictions will go immediately unless justified under GATT articles XX and XXI.	
Rules of Origin	Various mentions (Articles 26, 58, 79 and 81) but main provisions are in Annex III.	"A protocol setting out simple and development-friendly rules of origin to be applied"	Still under discussion. However, the EU is pushing for a development-unfriendly approach (value added) whilst developing countries would prefer a 'tariff jump' approach.	

Tariffs and related issues: Analysing what's on offer from the EU

How do the EU and others interpret WTO rules on FTAs?

The trade in goods in FTAs falls under WTO rules, specifically Article XXIV of the GATT (see Box 2 on page 4).

To the EU this means that in an FTA:[13]

- on average 90 per cent of total trade value between the two parties must be liberalised (also known as coverage);
- a small proportion of trade – about ten per cent – can be excluded from commitments by either party (measured either by trade volume (effectively value) and/or number of tariff lines);
- no major sector is excluded;
- the timeframe (the transition period) for this elimination should not exceed ten years unless under exceptional circumstances.
- "asymmetry" in coverage commitments is acceptable when negotiating with developing countries – provided that the 90 per cent target is reached (see below).

But many FTAs have much longer timeframes than this and coverage also varies. For example in the agreements between Australia and Thailand, and New Zealand and Thailand, Thailand got 20 years in both cases. And in the Canada–Chile agreement, Chile got 18 years.[14] Yet in contrast, every indication points to the EU pushing for FTAs with India, ASEAN, South Korea, the Andean Community and Central America with transition periods that are ten years or less, possibly as low as seven. And even then, the EU is pushing for tariffs to be eliminated in the front end of the transition period (what is called 'maximum front loading').

The EU has agreed to longer transition periods – i.e. in excess of ten years – in EPAs with ACP countries. These are some of the poorest countries in the world and as such many (for example countries in the ESA region) had initially requested a transition period of 25 years. Although transition periods of 15–20 years have been granted in the 'interim' EPAs initialled in December 2007, these apply for a very small number of products. The vast majority of liberalisation is set to occur within 10–15 years. As recently as September 2007, a demand from ESA was rejected by the European Commission who countered with the proposal that they would permit a period of only 12 years.[15] Should negotiating partners to the EU achieve longer periods, this may come at a price: in the past the EU has also proposed a trade-off that "sufficiently long transition periods should limit the scope for outright exclusions".[16] This appears to have been the outcome in the negotiations between the EU and the East Africa Community (see Box 3).

Box 3: Latest development in EPAs and market access between the EU and the East Africa Community (EAC)

In November and December 2007, a number of ACP countries initialled interim goods-only EPAs with the EU (as of end December 2007, some 35 ACP countries had 'initialled' deals). For example, the five countries of the EAC, which initially had been negotiating as part of the ESA region (16 countries), broke away to conclude the deal as a sub-region. EAC will get duty- and quota-free (DFQF) access to the EU market with the exception of rice and sugar which will be phased in. In return EAC has agreed to freeze tariffs at zero on 64 per cent of trade by 2010; eliminate tariffs on a further 16 per cent by 2023; and eliminate tariffs on a further 2 per cent by 2033. This translates into an 82 per cent opening of their markets within 25 years.

13 European Commission, undated. WTO compatibility of an EU-Mercosur free trade agreement http://ec.europa.eu/comm/external_relations/mercosur/bacground_doc/template_paper5.htm

14 Scollay, R., 2005. 'Substantially All Trade': Which Definitions are Fulfilled in Practice? An Empirical Investigation. A report for the Commonwealth Secretariat. 15th August 2005.

15 Report on the ESA-EC EPA negotiations 17th – 24th September Kigali, Rwanda

16 European Commission, 2006b. Comments from the EC on ESA Proposals on Trade Co-operation/Trade in Goods September 2006.

Box 3: Latest development in EPAs and market access between the EU and the East Africa Community continued

But what does this mean? Four of the five EAC countries are LDCs. They already have DFQF access to the EU market under the EBA arrangement. In return they have obtained a transition period of 25 years and can exclude 18 per cent of their trade. But given the timetable, they have also committed to open their markets by 64 per cent within three years and 80 per cent within 15 years. EAC countries have fronted-loaded their commitments and will only be allowed to protect a further 2 per cent of trade up to 25 years. In addition, these same countries, as part of ESA, had initially requested 57 per cent exclusions, but they finally agreed to just 18 per cent.

Whilst the principle of asymmetry is an improvement on straight application of the reciprocity principle in WTO rules, the EU approach has limitations. The extent to which the negotiating partner liberalises their trade should not be determined by arbitrary timeframes and product coverage. Because of massive differences in levels of development between the EU and the negotiating partner, the extent and timing of liberalisation should be based on their individual development and economic needs.

Also, something like 95 per cent of EU tariffs are already at zero (or close to zero). The greater adjustment costs will therefore be borne by the other country and not the EU, as was the case in the EU–South Africa FTA. The development limitations of the EU's approach to reciprocity and asymmetry are amply reflected in the impact assessment of a potential EPA in Kenya. To avoid any negative impact from an EPA, Kenya would need to exclude more than half its trade from liberalisation with the EU.[17] But as revealed in box 3, as part of EAC, Kenya got no more than 18 per cent exclusions.

17 TWN Africa and Oxfam International, 2007. *A Matter of Political Will*. www.oxfam.org/en/files/bn070425_EU_economic_partnership_agreements.pdf

The EU interpretation of Article XXIV is open to challenge, and practice and interpretation of WTO rules vary considerably. Key terms in the WTO rules remain undefined and negotiations to revisit these are ongoing as part of the WTO Doha Round of negotiations. The African, Caribbean and Pacific group of countries put forward a proposal that the principle of special and differential treatment – a fundamental WTO principle – should also apply to FTA rules where these involve developing countries. This would allow longer transition periods and lower liberalisation commitments for developing countries, for example. This principle has achieved widespread support among WTO members, including the EU, although negotiations are making little progress. An alternative approach is to use the WTO's "Enabling Clause" which allows non-reciprocal market access concessions to be made to developing countries. For North–South FTAs that involve only particular regions of developing countries to be covered by the Enabling Clause would also require amendments to WTO rules.

What are the implications for any developing countries that sign an FTA with the EU given that domestic agricultural subsidies are not included?

One of the anomalies of EU FTAs (when compared to the WTO) is that domestic agricultural subsidies are not included; and in only a few cases are export subsidies (refunds) mentioned as for example in the EU–South Africa FTA.

Moreover, the EU has excluded, and will continue to exclude, its own agricultural sectors from tariff elimination. However, these same sectors also carry large amounts of subsidies and are of export interest to developing countries because they include products such as sugar, rice, meat and dairy products, fruit and vegetables. As the following table shows, these same sectors produce surpluses which will continue to be exported and possibly dumped on world markets.

Main agricultural sectors excluded by EU from tariff elimination	Does this sector have high levels of EU domestic support?	Is subsidised production exported and possibly dumped in others' markets?
Meat products	Yes	Yes
Dairy	Yes	Yes
Cereals	Yes	Yes
Sugar	Yes	Yes but declining
Fruit and vegetables	Yes	Yes

How can developing countries protect themselves in FTAs?

There are several ways by which negotiating partners could protect themselves against damaging agricultural and industrial imports.

The first is through much longer transition periods for tariff elimination and backloading of implementation to the end of the transition period, as far as possible. This additional time during which tariffs can continue to be applied could be used to implement pro-active policies aimed at boosting the competitiveness of specific sectors, so that if and when the time comes for their liberalisation, they are in a better position to withstand foreign competition.

The second is through outright exclusions. Since WTO rules are clear in not requiring that all mutual trade among parties to a FTA should be liberalised, there is scope to constitute a list of sensitive products on which no liberalisation commitments are made (exclusion lists). Products included in such lists would be wholly excluded from any liberalisation commitment. But negotiating partners to EU FTAs need to be very diligent in choosing the specific tariff lines (and the correct number), not least to protect that sector against (dumped) EU subsidised products.

Negotiating partners could demand to exclude more than ten per cent of tariffs or trade. Whilst reciprocity is a key objective in all EU FTAs, in the past the EU has allowed for 'asymmetry' in the level of liberalisation. (By doing so, the EU argues that it provides a degree of special and differential treatment to the other country.) For example, in the EU–South Africa FTA, the EU agreed to eliminate tariffs on a higher percentage of products (95 per cent) than South Africa (86 per cent), by value.

However, asymmetry is not mentioned in the draft negotiating mandates for the new FTAs in Asia and possibly did not make it into the final negotiating mandates. The latest information from the negotiations between the EU and India confirm that the EU is pushing for a reciprocal and symmetrical trade agreement, despite the request from India for an asymmetrical approach (i.e. for the EU to liberalise 95 per cent of trade in goods and India 90 per cent). It is also interesting to note a change in the way that any exclusions are calculated; in their negotiations, both the EU and India have suggested exclusions will be based on the number of tariff lines and trade volume, not by value.

A third way in which negotiating partners could try to maximise flexibility is to use a combined trade volume/ tariff lines approach to hit 'substantially all trade' targets. Eliminating tariffs on 90 per cent of trade reduces the number of existing sectors that can receive protection, eliminating tariffs on 90 per cent of tariff lines allows countries to protect more sensitive sectors (as tariff lines that are not traded can be liberalised) but reduces the options to use tariffs to support industrial policy (it would not be possible to re-impose tariffs on a particular import such a local industry later emerge).

Another means of protection is through the use of Trade Defence Instruments (TDIs). Typically these include actions against unfair subsidies and the use of safeguards. Safeguard provisions work both ways and to date, much of the EU's emphasis has been on how the EU might best use these provisions to protect EU interests. This could limit any market access gains by the developing country partner.

Increasingly the EU may also try and limit the application of other forms of market protection that could be used by negotiating partners. It has made its intentions clear: to counter the "abusive and/or WTO-incompatible use of trade defence instruments by third parties".[18] The annex paper to *Global Europe* (and the EU Green Paper on Trade Defence Instruments) suggests that the EU may include procedures which will make TDIs more difficult for negotiating partners to use: "Current Trade Defence Instruments contain a degree of flexibility but might need to be reviewed in light of the new challenges posed by globalisation".[19,20] In any event the EU has confirmed that TDIs "will … integrate commitments that go beyond WTO rules in this area in line with EC rules and previous agreements".[21]

There has been much debate about safeguards for developing countries in the WTO as these can be difficult for developing countries to use effectively. Suggestions in agricultural negotiations at the WTO are that to be of benefit, a safeguard needs to be simple and effective to implement; be triggered automatically in terms of both volume and prices; and cover all products (particularly agricultural goods). Also, it should be able to have both increased duties (in potential violation of the standstill principle) and quantitative restrictions applied to it.[22] In addition, duty rates should be able to go beyond the bound rate where applicable and should be imposed for a sufficient duration to protect the particular sector or industry.

But both the ASEAN and Indian draft negotiating mandates stipulate that a safeguard would only cover agricultural products. In contrast, the recently signed EPAs have agreed more general safeguards as well as measures to protect infant industries from damaging imports – but these can only be imposed for a limited duration (i.e. twelve years for some of the Southern Africa Development Community countries). This wording is misleading however, as safeguards are inadequate to pursue industrial policies as they can only apply where injury can be proven to an *existing* industry.

For tariffs, what in particular are the EU's offensive/defensive interests?

In EU FTAs, tariffs would be eliminated on about 90 per cent of all trade. Clearly, this obligation goes considerably further than multilateral commitments at the WTO (WTO-plus). In multilateral talks, developing countries tend to benefit from lower concession requirements, or even none at all in the case of least developed countries.

Import tariffs

The EU's offensive interests on import tariffs in FTA negotiating partners are many and cannot all be listed here but in general, the priority sectors include cars, goods vehicles and parts; machinery and mechanical appliances; agricultural products; metals; textiles; and electrical equipment. For example, the EU's market access database is an excellent source of specific information regarding the EU's interests in this area (see 'Important information and where to find it' on page 13). In India, the following import tariffs are being targeted: agricultural products, ceramics and glass, copper and copper alloy scrap, textiles, steel, marble, food preparations, wines and spirits, fine papers and packaging board segment, and the automobile sector. (One study predicts that Europe's vehicle exports to India would be expected to increase by 700 per cent.[23]) For Mercosur, EU sectoral interests include ceramics and glass, cars, goods vehicles and parts, machinery and mechanical appliances and machinery and electrical equipment. In ASEAN, some of the targeted sectors include paper, spirits and ceramics.[24]

In previous FTAs, the EU has defended its agricultural sectors by maintaining (i.e. excluding) agricultural tariffs. This is likely to continue. But in the new FTAs the EU's defensive interests may change given that some countries in current FTA negotiations with the EU – for example Malaysia, Brazil, India and South Korea – are major industrial exporters and directly compete with EU producers. In the South Korean talks, the EU is reported to be baulking at commitments on automobile tariffs and steel.[25]

18 European Commission, 2007. Op cit.

19 Annex to the Global Europe communication (A Commission Staff Working Document) on page 23 at http://trade.ec.europa.eu/doclib/docs/2006/october/tradoc_130370.pdf

20 European Commission, 2006c. *Europe's TDIs in a Changing World Economy*. http://trade.ec.europa.eu/doclib/docs/2006/december/tradoc_131986.pdf

21 The draft negotiating mandates for the new FTAs with India, South Korea, ASEAN, the Andean Community and Central America have been posted at www.bilaterals.org

22 G33 proposal on common safeguard measures. www.tradeobservatory.org/library.cfm?refID=73080

23 Agence Europe, 2007. Ibid.

24 The source for these priority sectors is mainly the EU's market access data base. However, see also http://ec.europa.eu/enterprise/steel/conference_glass-ceramics/2007/speech_amilhat.pdf ; www.bilaterals.org/article.php3?id_article=6392 ; http://ec.europa.eu/external_relations/mercosur/bacground_doc/template_paper4.htm

25 Bridges, 2007. Still stuck on auto trade, EU–Korea FTA talks to continue into next year. Weekly Trade New Digest Vol. 11, Number 41 28th November.

Export tariffs

Secondly, there is the issue of tackling export restrictions (ensuring raw material supplies for companies in the EU). This is particularly important because the WTO does not cover export tariffs. Europe is clear that its FTAs need to go beyond import tariffs: "While tariffs remain an important issue, non-tariff barriers, and other regulatory restrictions "behind the border" have become increasingly important in determining the access of EU exporters to third country markets... the expansion of WTO rules has not fully kept pace with the expanding range of trade barriers … In areas such as export taxation … multilateral WTO rules do not fully reflect the complex problems faced by exporters."[26]

According to the EU, a number of export restrictions (mainly tariffs but also see next section) remain in the following sectors: agricultural materials, energy, metals, minerals, scrap metal, hides and skins. They are a priority for the EU because: "Measures taken by some of our biggest trading partners to restrict access to their supplies of these inputs are causing some EU industries major problems."[27, 28]

Eliminating these restrictions on exports is central to the EU's competitiveness agenda. On the EU's market access database, specific mention is made of export duties on raw hides and skins and raw and semi-finished leather products as barriers to trade from Argentina, Brazil (i.e. the Mercosur region) and India.[29]

Not surprisingly, the EU is demanding that the five new FTAs eliminate all customs duties, taxes or charges on exports upon the application of the Agreement. (This might even apply to some of EPAs although the interim deals suggest that countries may be able to continue to maintain some of them but not introduce new ones.) The EU has indicated that general exceptions might be applicable under GATT Articles XX (for example, protection of protected human, animal or plant life or health and the conservation of natural resources) and XXI (security reasons); how useful these exceptions prove in practice in FTAs, particularly for developmental reasons, remains to be seen.

Non-tariff barriers

What are the EU's priorities?

The term 'Non-tariff barriers' (NTBs) applies to export and import bans (quantitative restrictions), standards, technical regulations, conformity procedures, trade defence mechanisms, customs procedures (and trade facilitation) and internal taxation and regulation.

The EU is prioritising NTBs, and in short "will forbid any ban, restriction or other non-tariff barrier (NTB) to trade which is not justified by the general exceptions [GATT Articles XX and XXI]".[30]

According to Global Europe, the EU is also proposing policies that would allow interested stakeholders (i.e. EU companies) the right of prior consultation on any measure that the negotiating partner might want to introduce in the future and an enforcement procedure along the lines of the WTO's dispute settlement mechanism "*and make them accessible to industry*" (a development that departs from the WTO state-to-state procedures).[31]

In terms of issues, the EU appears to be placing particular emphasis on three areas.

Export bans and restrictions

The first is the elimination of all export restrictions (i.e. bans) to complement the fact all export tariffs will be abolished. This is all part of the EU's ambitions to gain access to raw materials.

26 European Commission, undated. Market Access Strategy. http://ec.europa.eu/trade/issues/sectoral/mk_access/cs101106c_en.htm

27 European Commission, 2006d. *Global Europe: A Stronger Partnership to Deliver Market Access for European Exporters*. http://trade.ec.europa.eu/doclib/docs/2007/april/tradoc_134507.pdf

28 European Commission, 2006a.

29 For a list of some of these export taxes, see http://mkaccdb.eu.int/cgi-bin/stb/mkstb.pl

30 See ASEAN and Indian EU draft negotiating mandates.

31 This is not explicit in the Global Europe document but is laid bare in the supporting Annex to the communication (A Commission Staff Working Document) on page 17 at http://trade.ec.europa.eu/doclib/docs/2006/october/tradoc_130370.pdf

As part of these FTA negotiations, the EU may well attempt to restrict or even prohibit the practice of dual pricing. This is where a negotiating partner has two prices, say in the energy market where there is one (lower) price for the domestic market and another (higher) price for the export market. The European Commission has made its intention in this area abundantly clear: "in order to remain competitive in the world, you firstly need affordable energy without unfair distortions deriving from dual pricing systems or non-competitive market structures … Securing and diversifying our sources of energy supply … is at the core of our external energy policy and will be a major priority in our negotiations with energy supplying countries (Russia in particular). Trade disciplines play a key role such as … addressing dual pricing systems."[32]

32 DG Trade speaking at a the conference 'From 2007 on: The principal challenges facing the European glass and ceramics industries' http://ec.europa.eu/enterprise/steel/conference_glass-ceramics/2007/speech_amilhat.pdf

Technical standards

The second issue is standards. According to the European Commission: "The gradual reduction of tariff barriers to trade has been accompanied by an increase in the number of measures creating technical obstacles to trade, such as regulations on packaging and labelling or conformity assessment procedures … they are sometimes wrongfully used in order to erect protectionist barriers around the domestic market."[33]

"The EU does not have significant provisions on TBTs [Technical Barriers to Trade] in its [existing] FTAs."[34] The inclusion of technical regulations in FTAs "is to facilitate and increase trade in goods by eliminating and preventing unnecessary barriers to trade while taking into account … the principle of non-discrimination, within the meaning of the WTO Agreement on Technical Barriers to Trade (TBT)".[35] This is likely to be the template for new FTAs. "The aim [of the new FTAs] will be to include provisions on the adoption of recognised international standards and on the streamlining of testing requirements."[36] This is in line with others' conclusions: because mutual recognition around EU standards and accreditation has caused so many problems, "in future, the EU is likely to emphasise the use of agreed international standards as much as mutual recognition in FTAs".[37]

33 European Commission, undated. Technical barriers to Trade. http://ec.europa.eu/trade/issues/sectoral/tbt/index_en.htm

34 Woolcock, S., 2007. *European Policy towards FTAs*. http://ecipe.org/european-union-policy-towards-free-trade-agreements/PDF

35 EU-Chile Agreement, page 45 at http://trade.ec.europa.eu/doclib/docs/2004/november/tradoc_111620.pdf

36 See ASEAN and Indian EU draft negotiating mandates.

37 Woolcock, 2007. *Op cit.*

Sanitary and phytosanitary (SPS) measures

The third issue is sanitary and phytosanitary measures. The EU is increasingly concerned about measures that restrict food exports from the EU: "In recent years, the use by third countries of food safety, animal and plant health issues as a trade barrier for imports has increased considerably. Governments frequently go beyond what is needed for health protection and use sanitary and phytosanitary restrictions to shield domestic producers of agricultural products from economic competition."[38]

In part this is due to a spate or food health scares in the EU over the last 20 years or so and the fact that importers have reacted by imposing various import restrictions on EU food products. Such is the growing concern in the EU over the growing use of SPS measures, the EU has established a separate SPS section in their market access database (see 'Important information and where to find it' on page 13).

38 European Commission, undated. Trade in agricultural goods and fishery products . http://ec.europa.eu/trade/issues/sectoral/agri_fish/sps/spsei_en.htm

What the EU appears to be doing is to shift the emphasis on SPS provisions more towards procedural aspects within Agreements. The WTO SPS agreement is largely silent on procedural obligations[39] yet in contrast, the EU–Chile agreement goes further than the WTO (i.e. WTO-plus) by laying out a whole series of procedural SPS measures. The EU–Chile agreement thus provides more robust legal security for EU exporters.[40]

The five new FTAs (and possibly EPAs) are likely to follow the EU–Chile example. The text in the draft FTA negotiating mandates reaffirms the general principles of the WTO SPS Agreement, including transparency and non-discrimination. Procedural aspects are likely to make the five new FTAs 'WTO-plus' as far as SPS measures are concerned, and possibly make it increasingly cumbersome and expensive for negotiating partners to use these provisions.

39 Isaac, G., 2006. The interaction between levels of rule-making in international trade and investment: The case fort SPS measures in Trade and Investment Rule-making: The Role of regional and bilateral agreements. Ed S Woolcock

40 Rudloff, B. and J. Simons, 2004. *Comparing EU free trade agreements : Sanitary and Phytosanitary Standards* . (ECDPM InBrief 6B). Maastricht : ECDPM with CTA -the Technical Centre for Agriculture and Rural Cooperation ACP-EU

But equally, negotiating partners should be giving even more attention to the proliferation of private standards on imports into the EU. More exacting private sector SPS standards are becoming the norm and creeping into public standards. The EU appears content to accept this trend. Private standards could be challenged under Article 13 of the SPS agreement. This was done when Caribbean and South American countries challenged private standards in relation to the EU banana sector. The EU responded by saying that it was powerless to intervene because the private sector argued that its standards reflect consumer demand which is justified under the SPS agreement.[41]

41 CUTS, 2006. *SPS standards and developing countries: The skeleton in the closet for the Doha Round*. http://www.cuts-citee.org/PDF/tdp-1-2006.pdf

Rules of origin

Is what is being proposed by the European Commission development-friendly?

Rules of origin are needed in preferential trade agreements to stop trade deflection through the country receiving preferences. However, rules of origin (RoOs) in current EU FTAs are viewed as highly restrictive and yet another barrier to trade imposed by rich nations.

Under the Cotonou Partnership Agreement, the EU committed itself to simple and development-friendly RoOs in the context of EPA negotiations. Despite this commitment and concrete proposals from several ACP regions, the Commission was unable to make a complete offer in time for the deadline (31 December 2007). Instead the Commission is proposing an interim arrangement for RoOs (lasting three years) and is pledging to offer more 'development-friendly' rules of origin in the future. The interim offer is largely based on the current rules, with some notable improvements to fisheries and textiles. As it stands, this offer is too limited in scope to make a substantial difference to the development prospects of ACP countries. One analysis of the EU-Cariforum agreement found that "The language is so complicated and technical that it seems impossible for anyone other than the drafters to understand what would be and what would not be eligible for export to Europe."[42]

42 Girvan, N., 2008. *Implications of the Cariforum–EC EPA*. www.normangirvan.info/wp-content/uploads/2008/01/girvanimplicationsepa10jan.pdf

At a global level, the European Commission has set out its proposals to make RoOs simple and development-friendly in its 2005 Communication entitled *The rules of origin in preferential trade arrangements*.[43] These provisions will form the basis of the Rules of Origins in the new EU FTAs with India, ASEAN, South Korea, Central America and the Andean Community. The EU's long-term solution is to go for a valued-added approach: goods would qualify for preferences if a certain percentage of valued added (VA) had accrued locally – and to extend cumulation of origin "between countries belonging to economically-integrated regional entities".[44] Yet typically, the level of value-added in developing countries is low, and below the thresholds currently established by the EU. Value-added varies considerably between products and between countries, which makes a uniform, simple and development-friendly system almost impossible. In addition, this approach can also be adversely affected by currency fluctuations and requires accounting systems that represent a significant administrative burden, particularly for smaller firms. It will be practically impossible to set a fair VA threshold unless it is very low, an approach that the Commission does not appear to be considering.

43 European Commission, 2005. *The rules of origin in preferential trade arrangements: Orientation for the future*. http://eur-lex.europa.eu/LexUriServ/ site/en/com/2005/com2005_0100en01.pdf

44 Ibid

A further issue for many developing country exporters – particularly amongst poorer nations such as the ACP – is that their production systems have been designed to satisfy existing rules, which are predominantly based on changes in tariff heading (CTH) (also known as a 'tariff jump'). In principle the concept is easy; imported products are allowed, into say the EU, so long as they have been transformed into another product with a different tariff heading to that of the input materials that were used. Many developing countries favour this approach but it has been rejected by the EU.

On cumulation, the new proposals appear to be *more* restrictive as the cumulation provisions are no longer ACP-wide, but are likely to apply only to each EPA region. Furthermore, in the interim EPA agreements, cumulation is only possible with countries that have signed the same EPA. Since many ACP countries have signed individual agreements, the rules of origin are now far more restrictive than under Cotonou.

Important information and where to find it

Global Europe
http://ec.europa.eu/trade/issues/sectoral/competitiveness/global_europe_en.htm
http://trade.ec.europa.eu/doclib/docs/2006/october/tradoc_130370.pdf
http://trade.ec.europa.eu/doclib/docs/2007/april/tradoc_134507.pdf
http://trade.ec.europa.eu/doclib/docs/2006/december/tradoc_131986.pdf

Key market access texts for EPAs, Mexico, South Africa and Chile
www.bilaterals.org/rubrique.php3?id_rubrique=52 (for latest EPA texts)
http://eur-lex.europa.eu/LexUriServ/site/en/oj/1999/l_311/l_31119991204en00030297.pdf (South Africa)
http://trade.ec.europa.eu/doclib/docs/2004/october/tradoc_111722.pdf (Mexico)
http://ec.europa.eu/trade/issues/bilateral/countries/chile/euchlagr_en.htm (Chile)

EU market access database (see 'trade barriers' and 'SPS' databases)
www.madb.europa.eu/mkaccdb2/indexPubli.htm

Draft negotiating mandates on the EU's new FTAs
www.bilaterals.org/rubrique.php3?id_rubrique=52

Sustainability impact assessments of EU FTAs
http://ec.europa.eu/trade/issues/global/sia/studies.htm

WTO and market access for goods
www.wto.org/english/tratop_e/markacc_e/markacc_e.htm

The EU FTA Manual is a series of eight briefings on the European Union's approach to Free Trade Agreements.

1. Introduction: Tackling EU Free Trade Agreements
2. Inside European Union Trade Policy
3. The EU's approach to Free Trade Agreements: Market Access for Goods
4. The EU's approach to Free Trade Agreements: Services
5. The EU's approach to Free Trade Agreements: Investment
6. The EU's approach to Free Trade Agreements: Competition
7. The EU's approach to Free Trade Agreements: Government Procurement
8. The EU's approach to Free Trade Agreements: Intellectual Property

We will be updating these briefings as negotiations and understanding progress, and would welcome your feedback.

Please contact: tradeandcorporates@actionaid.org

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4 The EU's approach to Free Trade Agreements
Services

This paper forms part of a series of eight briefings on the European Union's approach to Free Trade Agreements. It aims to explain EU policies, procedures and practices to those interested in supporting developing countries. It is not intended to endorse any particular policy or position, rather to inform decisions and provide the means to better defend them. The views expressed in the briefings do not necessarily reflect the views of the publishers.

What's at stake?

For developing countries

Services trade is the trade in non-tangibles – such as haircuts, healthcare, power supply, telecommunications and banking.

Many services are critical to human development and poverty reduction, like healthcare and education; others are important to a well-functioning economy, for example telecommunications, transport or banking. How a country manages its services sector to make sure these are available to its citizens and firms, affordable and of good quality depends in part on whether it allows foreign services firms to play a part in their supply and, if so, how it manages their involvement.

Services are important to economic development. Services are the fastest-growing area of trade (around six per cent per annum), but developing countries' share remains static despite the fact that they are often a key share of developing countries' exports. Even among LDCs, the average contribution of services exports to GDP was 2.5 per cent in 2003 with some island economies reaching levels of over 50 per cent.

The domestic service market is also important. A study of 30 developing countries shows that developing countries' service economies are more important and diversified than reported, often made up of small and micro enterprises, and important to employment.[1] Developing countries have great potential to expand their share of services trade, thereby contributing to growth and a more diversified economy.

Opening up the services sector to foreign investment can contribute to development. However, to take advantage of the opportunities and avoid costs, any liberalisation needs to occur in a carefully sequenced manner, and countries need to have the appropriate level of administrative and regulatory capacity to ensure this opening is beneficial (see box on page 2).

1 Riddle, D., 2002. *Services Export Capacity in Developing Countries. WTO Symposium on Assessment of Trade in Services.* www.wto.org/english/tratop_e/serv_e/symp_mar02_riddle_e.doc

When to liberalise?

Admitting foreign service suppliers can bring benefits to developing country economies. They can bridge gaps in providing essential public and business services, they can boost business opportunities and learning for local firms, create jobs, and bring competition on price and quality. However, these benefits are not automatic. Services liberalisation can equally have negative impacts on poor consumers, local firms and government's ability to regulate. Key factors such as the quality of local institutions and the competitiveness of local firms are important in determining impact. Services trade is difficult to analyse because it is hard to measure and barriers are more complex (regulations rather than tariffs). These factors combined would suggest a strong need for caution and wide consultation before making services commitments. Some considerations are:

Sensitive sectors: These are sectors essential to economic and social development, such as essential services, network infrastructure services, and financial services. They are often described as 'public goods' since their benefits extend beyond immediate returns to the direct consumer. These are services sectors where other priorities often take precedence over economic efficiency, for example universal access to basic healthcare. For cultural, political and economic reasons governments of many countries, including OECD countries, have maintained tight controls of these sectors and have been slow to liberalise. For example, in water services, the OECD estimates that 90 per cent of water provision is still in public hands. Where these sectors have been privatised, there has been a marked need for increased regulation and competition, although this is difficult to achieve due to natural monopoly characteristics or high levels of investment required for entry into these sectors.

Sequencing: Many studies (see 'important information and where to find it' on page 11) show that regulatory structures should be effective before liberalisation of key service sectors, or the potential benefits could be reduced or even reversed. The need for careful sequencing holds true particularly for many of the 'sensitive sectors' described above that tend to be natural monopolies.

A study of 30 African and Latin American countries found that competition in the telecommunications sector was significantly associated with increases in access to services and lower costs of calls. Privatisation alone was not beneficial in terms of efficiency or number of connections; it needed to be combined with regulatory capacity.

Building the domestic economy: A developing country government may wish to protect infant industries in order to promote a diversified, dynamic economy and to protect jobs and livelihoods. Although they are net importers of services, developing countries often have a wide variety of service suppliers. Faced with unequal competition too soon in their development, these dynamic but often small industries, risk being put out of business. Most developing country governments lack programmes for supporting these businesses and their views are rarely put forward in trade negotiations. These firms are important in terms of employment and GDP, but also for providing essential services to other parts of the economy. (OECD estimates that 10–20 per cent of input for production is services.) Maintaining a healthy domestic sector can be critical in promoting competition and to providing locally tailored solutions to local consumers, especially when these are not well served by larger corporations interested in wealthier clients.

For the EU

Services are the cornerstone of the external trade and competitiveness agenda of the EU. They represent 77 per cent of the EU's GDP and employment. The EU sees its future wealth as coming from the provision of premium goods and services. It lists the sectors of telecommunications, distribution, finance, insurance, transport and environmental services as those where European firms are world leaders.

Target regions of the competitiveness strategy are important economically for EU service industries: India imports 33 billion euros of commercial services from the EU, whilst ASEAN imports 89 billion euros and Latin America 27 billion euros.

The EC calls for "far-reaching liberalisation of trade in services, covering all modes of supply"[2] and at least parity with its competitors' FTAs in the target regions.

Liberalisation of services sectors generally involves tackling regulatory barriers affecting foreign service providers overseas. The EU recognises that this can be sensitive since it touches on the right to regulate domestically to achieve public policy objectives, but its stated aim in FTA policy is to move further and faster in promoting openness and integration and to reinforce regulatory ties. It further states that domestic regulation "must be done in a manner with the least restriction on trade, consistent with achieving other legitimate policy objectives."

2 See P17 Staff working paper to Global Europe available at: http//trade.ec.europa.eu/doclib/html/130370.htm

Understanding services texts: Key terms and definitions

Modes: These are the different ways in which services are traded across borders.

- The person providing the service can cross the border to do so (called Mode 4). An example is hiring a builder from overseas.
- The company can set up a branch in the country where its customers are (Mode 3). Foreign clothes shops and banks are examples.
- The customer can do the traveling (Mode 2), as for example when people eat in restaurants or get medical treatment abroad.
- Finally the service itself can cross the border (Mode 1). Previously this was confined to things like postal services, but the internet has enabled other services such as consultancy to "travel" in this way.

Countries make different liberalisation commitments according to each mode.

Sectors: These are the different types of service industries. The list of categories that is normally used is the one set up by the UN. The categories are broad, and it is useful to check to see exactly which activities are covered. The list can be found at: http://un.stats.un.org/unsd/cr/registry/regcst.asp?cl=16&Lg=1.

Schedules: As well as the texts of the trade agreements, there are lists of specific commitments per sector called "schedules". These list the sectors in which commitments are being made, as well as any limitations on free access to markets and any deviations from national treatment. Here is an example:

Sector or subsector	Limitations on market access	Limitations on national treatment
Packaging Services CPC 876	4) Unbound (The party is reserving the right to make changes to its market- access commitments in mode 4, so preserving maximum policy space.)	None (The party is committing to full national treatment, so cannot use measures which discriminate against foreign service suppliers.)

As with services negotiations at the World Trade Organisation, for those sectors committed, the European Commission asks its trading partners to eliminate quotas, Economic Needs Tests, requirements on the type of Legal Entity to be used, or limits on foreign shareholding and national treatment for firms entering the market, once they are established. Unless countries specify exceptions or "reservations" to these general conditions when they write up their schedules, they are considered to refrain from applying the above- mentioned policy measures.

The European Commission's latest texts take a new approach to how it organises its services commitments and schedules. Rather than having one annex dealing with each of the modes, it is including one annex on "cross-border trade" for modes 1 and 2 and another on "Establishment" which covers both mode 3 services commitments as well as investment in non-service sectors. Mode 4 commitments are outlined within the text of the agreement. It remains to be seen whether this will be detrimental to clear outcomes for mode 4 – which tends to be a sensitive topic for the European Commission, and an offensive interest for developing countries. It also raises new challenges for negotiators.

Understanding services texts: Key terms and definitions continued

Parity/ Most Favoured Nation (MFN): This means that investors and service suppliers from the European Union will automatically be treated as well as those from other countries/regions with which the negotiating party has a trade deal – both current and future ones.

Again the Commission has taken a new approach in some of its most recent texts and is seeking parity only with countries that are commercially significant. This means that smaller countries can conclude deeper deals without having to offer the same terms to the European Union.

National treatment: Once a European investor is established in the country it must be treated at least the same as local firms.

The legal backdrop: What WTO rules mean for services in Free Trade Agreements

The World Trade Organisation's General Agreement on Trade in Services (GATS) sets out the rules for services trade including how services must be dealt with in regional trade deals. Free Trade Agreements (FTAs) do not necessarily need to deal with services at all to be compatible with WTO rules. Countries can simply reaffirm in broad language their existing multilateral commitments under the GATS. The European Union has done this in the past, for example in their Euromed agreements.

Once services are included in regional trade deals, they must conform with the requirements of GATS Article V. This rule requires countries to make sure new deals "substantially" liberalise services trade, but allows developing countries flexibility.

The GATS contains important flexibilities, safeguards and other measures designed to help developing countries in particular to avoid the pitfalls of services liberalisation and enjoy the benefits of enhanced services trade.

In order for regional deals on services to be of interest to developing countries, one condition is that they should reinforce and not undermine these important measures and that the framework for their services liberalisation should be as least as favourable as that provided for in the GATS. The table below compares key GATS provisions with European Commission practice in Free Trade Agreements. It shows that in some important areas, European Free Trade Agreements are undermining flexibilities that are provided for under GATS.

GATS provision	EU FTA practice	Development implications
In FTAs, developing countries have greater flexibility both overall in the number of sectors liberalised and the extent of liberalisation in each sector committed. *GATS Article V:2* WTO members are also asked to "take account of the serious difficulties" of LDCs in making commitments. *GATS Article IV* The Hong Kong Ministerial Declaration reiterates that LDCs are exempt from commitments to liberalise services in the Doha Round.	Since these provisions are not well defined it is difficult to judge whether they are being implemented. In some EU FTAs (for example TDCA with South Africa) there is explicit reference to GATS V flexibilities for developing countries. In EPA negotiations, the EU appears to be seeking comprehensive coverage but allowing longer timeframes for liberalisation. There is nothing in draft EPA texts to indicate that the EU is exempting LDCs from services liberalisation commitments.	GATS rules generally require countries in FTAs to liberalise most sectors and to eliminate any discriminatory measures. Developing countries might wish to liberalise fewer sectors more slowly to promote local service industries, to keep control of key sensitive sectors or to develop regulatory capacity before liberalising. Developing countries might also wish to retain some policy tools, falling under the GATS, or to pursue development objectives such as quotas, joint venture requirements or measures that discriminate in favour of local firms.
Developed countries are to strive to help developing countries to increase their share of services trade, through liberalising sectors where they have potential to export. *GATS Article IV*	The EU always exempts key sensitive sectors from liberalisation in FTAs. Some of these are of export interest to developing countries, notably audio-visual services, and air transport services. The EU's offers in Mode 4, even in EPA drafts, fall short of developing country expectations as expressed in WTO talks.	Services are important to economic diversification and moves into value-added activity. Some commentators disagree on the potential benefits and pitfalls of Mode 4 liberalisation. The World Bank calculates that gains for developing countries could reach $150 billion per annum,[3] while others warn of the dangers of "brain drain". It is clear that by liberalising only the movement of the most qualified personnel, the EU risks preventing countries from adopting an optimal strategy.
The GATS allows countries to choose in which sectors they would like to liberalise. This contrasts with goods negotiations where countries commit to liberalise all sectors and can name upfront which few sectors to exclude. The GATS approach is called "positive list".	The ECU adopts a positive list approach to services. However, the EU also requests broad commitments such as a standstill on discriminatory measures (EU–Mexico) and on Most Favoured Nation treatment including market access (EPAs) which undermines this flexibility.	One of the perceived advantages of services negotiations is the flexibility they allow countries in deciding when and where to liberalise. MFN commitments mean countries will not be able to decide with which regions they would like to integrate most or first. This has been tempered in EPA negotiations by allowing countries to offer more favourable terms to trading partners that are not "major trading economies" defined as developed countries or those accounting for 1 per cent or more share of world exports. A standstill on discriminatory measures means that countries cannot introduce measures, even in sectors where they have not locked in GATS commitments.
Countries are allowed to exempt public services from GATS commitments even if the relevant sector is liberalised. These must be supplied "neither on a commercial basis, nor in competition with one or more service suppliers". *GATS Article I*	The EU repeats the language of the GATS exemption for public services, although in recent texts it is unclear to what extent the carve-out applies in the investment chapter, because of new organisation of texts.	Many governments, including in OECD countries, prefer to keep control of strategic sectors such as essential services (sanitation, health, education) or infrastructure services (telecommunications). The GATS language is felt to be ambiguous. It is unclear whether contracting out the provision of government services to the private sector or the co-existence of a private sector provider or the introduction of fee-based service provision could jeopardise use of the carve-out. Developing countries have been under significant pressure to liberalise these sensitive sectors and involve the private sector through donors and multilateral lenders.
The GATS contains other exemptions and safeguards impoFTAnt for countries to maintain financial stability and to achieve public policy objectives including: • security • public morals and order • human, animal & plant life and health • fraud prevention • data privacy protection • safety • direct taxation.	The EU allows many of the standard exemptions and safeguards allowed in GATS.	Some novelties have been introduced. The EU has introduced an exemption for protection of exhaustible natural resources. Access to natural resources and energy security are key objectives of Global Europe. These measures seem to aim at preserving equal European access to diminishing reserves. The EC has also introduced an exemption to protect "national treasures". Apparently missing from draft EPA texts are safeguards to prevent Balance of Payments difficulties.

3 Winters & Walmsley (2002), Relaxing the Restrictions on the Temporary Movement of Natural Persons: A Simulation Analysis

GATS provision	EC FTA practice	Development implications
Under GATS Article X, the WTO foresees the establishment of an Emergency Safeguard Mechanism (ESM). The details of this mechanism are not defined and are part of the Doha Round of negotiations.	The EU's position at the WTO has not been supportive of an ESM and there is no reflection of this possible tool and its application in its FTAs.	The ESM is potentially very important to developing countries in particular. This escape clause would help to cope with unforeseen import surges as a result of liberalisation commitments, and safeguard the interests of nascent domestic industries and defend against other negative impacts, for example financial imbalances such as those experienced in East Asia.
Developing countries are allowed to attach conditions to liberalisation commitments to enhance their services trade. *GATS Article XIX*	This provision is not recognised in EU FTAS.	Such conditions can be a useful instrument to safeguard and implement development policies. Examples of conditions WTO members have attached to GATS commitments and that might be useful to developing countries in this respect are: • Standards: such as service targets, performance requirements, specification standards (for example, to use local labour or to provide technology transfer), competition law (for example preventing price-fixing) • Price controls: Usually to ensure affordability of essential services • Entry controls: Professional and educational requirements, restrictions on marketing and use (e.g. zoning laws), prior authorisation requirements and licensing • Information regulation: Certification and labelling requirements for the benefit of consumers.
GATS Article VI has rules on how to balance the right of countries to introduce domestic regulations that affect foreign service providers with their commitment to liberalise in particular sectors. These rules are currently ill-defined and are under negotiation at the WTO.	The EU tends to take a strict approach to rules on how and when countries can introduce domestic regulations in sectors in which they have made commitments to liberalise their services. It requires these to be in pursuit of legitimate policy objectives and to be not more restrictive than necessary on trade.	In the Doha Round, developing countries are fighting to retain the right to regulate for development objectives and to avoid the "necessity test" which judges the validity of a measure based only on its impact on trade and not on other factors, for example, institutional capacity. Some EC texts also require commitments on the quality and type of regulatory and institutional arrangements. Countries should consider their capacity to fulfill these without jeopardising other spending commitments before accepting binding terms.
The GATS aims at progressive liberalisation and has an in-built agenda to make this operational. However, there is no requirement for FTA deals to include a timetable or process for further liberalisation between the parties.	Most EU agreements include a commitment to look at liberalising further later on. These have tended to become more far-reaching in subsequent agreements.	Developing countries should decide to what extent these commitments should be binding, and to what extent they want to set up new institutions and mechanisms to identify and implement further liberalisation.
GATS rules state that countries may reach agreement on mutual recognition of qualifications, standards, certification and should not do so in a way that acts as discrimination between countries. It does not call on countries to harmonise their regulations and requirements. It also calls on members to increase participation of developing countries, through strengthening domestic services capacity and competitiveness, and to improve their access to distribution channels and information networks. It foresees the establishment of "contact points" to assist services exporters	In its Global Europe paper the EC looks to co-operation on regulatory issues as a strong tool for harmonisation. The EC generally does provide contact points for services exporters and foresees more general co-operation provisions in EPAs. These are as yet undefined.	These features can be helpful for developing countries, if they help overcome the barriers to their services' exports. For example, mutual recognition of professional qualifications can help in facilitating the movement of service providers (mode 4). Co-operation can mean development assistance but can also mean help to address problems like access to technology or dealing with anti-competitive practices that stop developing country firms having access to essential reservation networks in the tourism sector. However, these can also place obligations on developing countries, limit their use of licences and be a "soft" means to achieve changes in their regulations to suit European firms.

Analysing offensive and defensive interests: Some questions to ask

Since there is no WTO compulsion to include services in an FTA, parties must be satisfied that the balance of their offensive and defensive interests is well served before signing up to any deal.

What the EU might want and what this might mean for development

In general, coverage and ambition have increased in subsequent agreements by the EU; for example in several of the Euromed agreements, countries simply confirmed their existing GATS commitments (and a future reassessment of commitments). The later EU–Mexico and EU–Chile have more substantive and detailed provisions, and frequently go beyond GATS requirements, for example in financial services and telecommunications liberalisation.

According to the EC's past practice and Global Europe statements, the EC is likely to seek liberalisation commitments from developing countries in at least the following sectors: telecommunications, distribution, environmental services and financial services.

Telecommunications

Access to telecommunications is important to economic activity, social cohesion and many other aspects of development.

Telecommunications markets tend to be natural monopolies because there is generally only one infrastructure and high set-up costs and the need for continual technology upgrades mean large firms tend to dominate. Liberalisation needs to be carefully planned and sequenced.

The GATS has a reference paper or template for telecommunications. The EC approach has differences which are useful to analyse.

Although the GATS paper requires information on requirements and conditions to be publicly available, the EC also sets out conditions for the regulatory authority and provisions for dispute settlement for providers. Implementations of these kinds of provisions can be expensive and burdensome.

According to GATS, developing countries are allowed to specify in their schedules conditions to strengthen their telecommunications infrastructure and participation in international trade in telecommunications services. The GATS paper also calls for technical co-operation to assist developing countries, including "encouraging" foreign suppliers to provide technology transfer and training to assist LDCs' development of the sector. None of these positive measures appear in EC texts on telecommunications.

The EC recognises that universal service obligations can be required, but places restrictions that these must be "transparent, objective, non-discriminatory", neutral with respect to competition and "not more burdensome than necessary for the kind of universal service defined by the Party". It also requires that directories of all users be published and updated on an annual basis! Recent texts also call for governments to compensate suppliers if universal service becomes an "unfair burden".

The EC also places restrictions on the right of firms to cross-subsidise and thus keep prices low for poorer consumers. It requires that these must not be "anti-competitive". This kind of provision has already created difficulties, for example for the Mexican government who lost a case brought by the US.

Financial Services

The financial sector is essential to economic development because it provides access to credit and savings facilities for entrepreneurs and farmers, for example. It is also key in promoting macro-economic stability and market development. Many OECD countries still maintain restrictions on foreign participation in their financial sectors, perceived as important to maintaining economic and political independence.

For these reasons, liberalisation of the sector must be carefully managed. Developing countries might hesitate to lock in liberalisation over a fixed period of time where they cannot be sure of the right conditions being in place or of the consequences of liberalisation.

Some possible impacts to consider are:

- Financial sector liberalisation without adequate regulations and supervision can lead to financial instability. For example, the EC text asks countries to allow full foreign ownership and board membership of their banks and not to impose any limits on foreign participation in the sector. Domestic providers may respond to foreign competition by lending imprudently or engaging in higher-risk activities, or unsound foreign institutions may enter the financial sector. Some countries might want to limit or restrict participation in risky sectors, for example debt markets or hedge funds.
- Increasing foreign participation through Mode 3, as the EC requests, can also increase capital flows, unless controls are introduced. This can lead to instability, as demonstrated by the East Asia Financial crisis of 1997, as well as exacerbating the problems of capital flight for developing countries.
- Financial sector liberalisation can reduce access to credit for customers who lack collateral or find formal information requirements difficult to fulfil. The IMF found that the presence of foreign banks results in less access to credit for the country's private sector.[4] An earlier study of financial markets in four African countries found that financial services liberalisation negatively affected access to credit in rural areas. This is exacerbated as domestic firms are often driven out of business. Concentration in banking activities in African countries has risen since the sector was liberalised.

4 E. Detragiache, T. Tressel, and P. Gupta (2006) 'Foreign Banks in Poor Countries: Theory and Evidence', IMF.

Many of these issues are not unique to EU deals. In fact much of the language on the scope, definitions, etc of the agreement comes directly from GATS text. However, there are some novelties in the EC's approach that deserve some further consideration:

- The EC includes far-reaching commitments on "effective and transparent regulations" and how these should be implemented. These can be burdensome if included as binding commitments for developing countries, but also they involve signing up to various international instruments and standards, some of which, for example the Basel Conventions, are controversial for developing countries who have not participated in the development of such standards.
- The EC's "prudential carve-out" clause is different from that in the GATS. This clause is intended to make sure that GATS commitments do not undermine financial stability or fiduciary responsibility. The GATS language requires that countries do not use this right to avoid their obligations. The EC adds language that the measures a country takes under this clause should be non-discriminatory and "not more burdensome than necessary". Developing countries might want to add additional criteria for prudential carve-out including their ability to supervise and regulate the sector.
- The EU in some agreements includes detailed provisions on dispute settlement and the kind of mechanisms that should be in place – down to the composition of the panel members. In combination with strict disciplines on domestic regulation this could create risk for developing country governments on implementing new policies or regulations to manage their services sectors.

- In some agreements the EC sets up a Supervisory Committee to supervise implementation and to allow the parties to discuss any "issues" as well as seeking to facilitate and expand bi-regional services trade. The current remit is imbalanced and might put developing country Parties under pressure to implement swiftly and further liberalise. A more balanced approach would consider also capacity to implement, monitoring development impacts as well as the usefulness of development co-operation with the EU.

Distribution services

Unlike the previous sectors there is no specific framework within the text of European Free Trade Agreements for distribution services. Liberalisation is determined via the usual request–offer process of negotiations. The sector is important for the EC, both because large EU firms dominate the sector, but also because distribution services are an important part of a well-functioning supply chain. For developing countries, the nature of the distribution sector is important for their own firms' efficiency and the viability of their markets and trade links.

However, efficiency is not the only consideration. There can be high short-term costs as many developing countries' distribution sectors, especially the retail part of them, are dominated by small traditional enterprises. Being able to supply the retail sector is also important especially for poor farmers. Introducing full liberalisation in this sector has tended to disadvantage these players who are too small to compete with large retailers or who – as in the case of farmers – lack the necessary access to credit, technology and flexibility to do business with them. Consumers are also not necessarily going to benefit from liberalisation, nor is competition or efficiency a guaranteed outcome, as the market is dominated by a few global players who dominate local markets as both sellers and buyers.

This is a sector that requires regulation to correct market failures and ensure best outcomes for local firms and consumers. Any services commitments should therefore be careful not to preclude important policy tools such as:

- Zoning regulations, limitations on opening hours or products for foreign or large traders that can ensure niche markets for local firms. Economic Needs Tests can ensure that local firms are not crowded by foreign firms.
- Price controls to protect consumers
- Joint venture, technology transfer requirements to ensure local firms benefit from the presence of large foreign firms
- Local employment, staff training requirements
- Requirements to sell certain local products.

Countries that cannot be sure to properly regulate the sector or feel that competition is likely to be lacking should also consider carefully before making commitments in this sector.

Making trade-offs: Analysing the EC's offer

As well as considering the impacts of their own liberalisation commitments, countries need to determine whether what the EC is offering is sufficient and appropriate to suit their own potential export interests and bring real economic benefits.

To do this, the EC's services liberalisation offer needs to be examined in conjunction with their current (revised) GATS offer, so that countries can be sure about what is additionally on offer to them beyond what they would obtain from a multilateral deal and therefore where they are given an edge over the remainder of WTO members. A link to this offer is provided in the section "Important information and where to find it" on page 11.

The EC has begun to organise its offers in separate annexes for different modes, and to include its mode 4 offer within the text of the agreement. Some key points to note on the EC's services offer are:[5]

- First, the EC generally treats some sensitive areas as off the table. These include audio-visual services and air transport services. Some developing countries clearly have domestic industries with export potential in these sectors. The EC also tends not to make offers in the health and education sectors where member states prefer to decide their own regimes.
- In modes 1 and 2, the latest EC offer seems to have small improvements over its existing GATS commitments and revised GATS offer. These involve the removal of some reservations and restrictions by individual EU member states, for example in the area of legal services. This is in line with the internal liberalisation process of the EU in its services market and a move toward more unified approach. Liberalisation of mode 2 is relatively uncontroversial since it involves allowing consumers to spend money overseas. Liberalisation of mode 1 is potentially of interest to developing countries that wish to export internet-enabled services.
- In mode 3, the EC's latest offer is to bind existing levels of liberalisation, with exceptions in sensitive sectors especially public services. It compares this to a quasi-negative list approach. Many developing countries do not have significant capacity to invest in Europe and should be wary of request for comparably sweeping commitments in return.
- In mode 4 the EC includes its commitments within the text of the agreement rather than as an annex. It uses the four categories generally used under the GATS:
  - **Key personnel:** Commitments in this category involve short-term transfers for skilled, senior personnel within the same company.
  - **Graduate trainees** are permitted to travel to and from their parent company and the EU for a limited period. In the GATS offer this is set at six months, in the latest offer examined, the limit is as yet undefined.
  - **Contractual Service Suppliers:** These are suppliers who do not have a branch established in the EU, but who have a short-term contract to supply services. There is a more extensive list of sectors where contractual service suppliers movements are liberalised. Numerical ceilings are removed, but economic means tests are to be applied in key sectors – notably health. This means that countries can deny access if it cannot be proven that the local economy cannot provide the service. Contractual service suppliers are also required to be educated to degree level apart from models and chefs!
  - **The independent professionals (IP)** category is liberalised for only a limited number of sectors. Contractual service suppliers and independent professionals categories, being delinked from the need to have a commercial presence in the EU, are generally of more interest to developing countries.

In general, the most highly skilled categories are those emphasised by the EC, although these are not those where developing countries might have most capacity or most interest to export.

The EU's working conditions and minimum wage requirements still apply to its Mode 4 commitments, this means that countries will not be able to exploit wage differential advantages.

It is worth noting that the definition of Mode 4 is limited to short-term service suppliers who do not enter the employment market. It does not cover non-service sectors or permanent economic migration. It also does not address visa or immigration formalities. These would need to be dealt with in separate deals, usually outside an FTA and between individual member states and the party in question.

5 This analysis is based on the EC's offer in EPA negotiations which is considered to be 'generous'. It is likely that in countries where there is a stronger economic interest and/or there are non-WTO members this offer will be reduced.

Developing countries should also consider what are the barriers affecting their services export performance and whether these are most appropriately addressed through the traditional method of swapping liberalisation offers and requests. For many of the relevant barriers to their exports, these would be most effectively addressed through increasing other areas of co-operation and not through trading services liberalisation commitments with the EC:

- **Capacity building:** As in other sectors, differences in infrastructure, human resources and technology access affect services export competitiveness of developing country firms, especially small and medium-sized enterprises (SMEs). Governments might also need to increase capacity both to regulate newly liberalised sectors, as well as to help with involvement in standard setting, etc. The EC does include co-operation chapters within its FTAs that seek to support diversification and competitiveness of developing country markets. These are generally "best endeavour" (i.e. not enforceable) and can be too overly general to be useful.
- **Standards:** As is the case in goods, standards, for example in the construction sector, can hinder developing country exports.
- **Mutual recognition:** Recognition of qualifications of service providers is particularly problematic in service sector.
- **Anti-competitive practices:** The dominance of multinationals and their anti-competitive business practices. This is particularly the case in construction, distribution services and tourism. For example in tourism, developing country firms are disadvantaged as they lack access to the Computer Reservations System and Global Distribution System, exacerbated by the technology gap.

Important information and where to find it

Existing GATS commitments and guidance on how to read them

Where to find out more about your country/region's services trade:
www.wto.org/english/res_e/statis_e/statis_e.htm
www.istia.org

Evidence and sectoral case studies

www.unctad.org: see especially "Trade in services and development implications" TD/B/Com.1/71, 16/01/2006

On regulation and sequencing, see working papers of Centre on Regulation and Competition, especially:
www.competition-regulation.org.uk/publications/working_papers/wp85.pdf

www.southcentre.org: see especially:
www.southcentre.org/publications/workingpapers/wp23.pdf

ECDPM/ILEAP on EC past practice in FTAs on services:
www.ecdpm.org/Web_ECDPM/Web/Content/Navigation.nsf/index2?readform&http://www.ecdpm.org/Web_ECDPM/Web/Content/Content.nsf/7732def81dddfa7ac1256c240034fe65/5eec2f71480080b82c1256eed002c6980?OpenDocument

Useful NGO sites:

www.somo.nl
www.wdm.org.uk/campaigns/past/gats/
www.citizen.org/trade/wto/gats/
www.servicesforall.org/

The EU FTA Manual is a series of eight briefings on the European Union's approach to Free Trade Agreements.

1. Introduction: Tackling EU Free Trade Agreements
2. Inside European Union Trade Policy
3. The EU's approach to Free Trade Agreements: Market Access for Goods
4. The EU's approach to Free Trade Agreements: Services
5. The EU's approach to Free Trade Agreements: Investment
6. The EU's approach to Free Trade Agreements: Competition
7. The EU's approach to Free Trade Agreements: Government Procurement
8. The EU's approach to Free Trade Agreements: Intellectual Property

We will be updating these briefings as negotiations and understanding progress, and would welcome your feedback.

Please contact: tradeandcorporates@actionaid.org

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5 The EU's approach to Free Trade Agreements
Investment

This paper forms part of a series of eight briefings on the European Union's approach to Free Trade Agreements. It aims to explain EU policies, procedures and practices to those interested in supporting developing countries. It is not intended to endorse any particular policy or position, rather to inform decisions and provide the means to better defend them. The views expressed in the briefings do not necessarily reflect the views of the publishers.

What's at stake?

For developing countries

Investment flows totalled $1036 billion in 2006, nearly half of which flowed from the EU. Currently developing countries account for around a one-third share in foreign direct investment (FDI). Investment has the potential to contribute to a country's development by providing:

- A source of capital for cash-strapped governments
- Services and infrastructure to fill gaps in the domestic economy
- New export opportunities
- Opportunities for technology transfer and skills upgrading
- Jobs and tax revenue
- Opportunities for local firms to sell goods and services, learn new techniques and encourage entrepreneurialism.

Evidence that investment deals help developing countries attract the right quality and quantity of investment is mixed at best[1]. Traditional international investment agreements are unbalanced, focusing exclusively on investor rights and protection. There is usually no express accompanying recognition of the right of the state to regulate to achieve public policy or development objectives, nor any acknowledgement of the need for obligations to be placed on the home state of the investor to help police corporate misconduct. This entails real risks for developing country governments, as is demonstrated by the explosion in the number of disputes brought by investors under investment agreements in recent years: over 250 known arbitrations have been brought by investors against host states, the vast majority of which have commenced in the last five years. These often result in financial penalties and the reversal of the government's policies.

The benefits of FDI are not automatic, and impacts can also be negative. Much depends on the behaviour of the investor, the state of the local economy and institutional factors. It is at least as important for developing countries to select and manage investment as to attract it.[2]

Investment in trade deals covers Foreign Direct Investment (FDI). This is when an investor from the 'home' state takes a significant share in ownership in a firm in a 'host' state and is involved in the day-to-day running of that enterprise over the longer term. Other types of investment can also be included and are usually covered in Bilateral Investment Treaties (BITS) for example stocks and shares, real estate or intellectual property.

1 Cosbey 2005: International Investment Agreements and Sustainable Development: Achieving the Millennium Development Goals

2 UNCTAD 2005

For the European Union

The EU's new approach to investment in Free Trade Agreements (FTAs) is a response to the perception that 'European investors are discriminated against vis-à-vis their foreign competitors and the EU is losing market shares'. The EU perceives that it is lagging behind the US in terms of the content and regional reach of its investment deals. It aims to target key regions according to their size and level of protection against EU export interests.[3]

3 See DG Trade issues note dated 31 May 2006: 'Upgrading the EU policy' and Global Europe competitiveness strategy

According to the Global Europe competitiveness strategy, Europe's future lies in moving up the value chain in premium goods and services, in particular with services such as telecoms, distribution, finance, transport and environmental services. Investment conditions are key to services industries which often rely on proximity to the customer. As global supply chain management becomes more important, the importance of non-tariff barriers and regulations overseas to the viability of EU industry increases. The EU also believes that FDI leads to increased trade.

Understanding investment texts: Key terms and definitions

International Investment Agreements (IIAs)/ Bilateral Investment Treaties (BITS): IIAs are agreements between two or several countries containing international law guarantees relating to the treatment of each other's investors and investments. These can take the form of BITS – which are agreements between two countries dealing only with investment, designed to promote and protect investment between them or increasingly through investment provisions contained in wider regional trade agreements (RTAs). There are also some multilateral agreements dealing with specific areas or aspects of investment such as the General Agreement on Trade in Services (GATS), Agreement on Trade-Related Investment Measures (TRIMS) and the Energy Investment Agreement (EIA).

Establishment: Establishment is when foreign nationals and companies set up a permanent business presence in a host country either as self-employed persons or by setting up or acquiring local businesses. Traditionally, the EU has allowed host states to retain control over the admission of investments into their territories. On the other hand, the US approach gives rights to investors during the making of the investment. Future investment provisions in EU trade agreements are likely to be influenced by the US approach. For example, a state must provide an investment national treatment and 'most favoured nation' treatment during the pre-establishment phase as well as the post-establishment phase.

Most Favoured Nation (MFN): The MFN rule requires host countries to accord to foreign investors and their investments treatment that is no less favourable than the treatment accorded to investors of any third state. Generally this applies to their treatment after they have been established. However, some IIAs might also extend this right to the establishment of investments, as has been the case of US IIAs and is likely to be reflected in the investment provisions found in future EU trade agreements.

Non-discrimination and national treatment: A national treatment obligation in an IIA requires host countries to treat foreign investors and their investments no less favourably than the investments of their own nationals. It can be applied only post-establishment, or in the case of US BITS and future EU trade agreements/RTAs[4], also for establishment rights.

4 According to the EU's internal issues 'Upgrading the EU policy' dated 31 May 2006

Fair and equitable treatment: The obligation on the host state to accord investments 'fair and equitable' treatment found commonly in IIAs has recently become controversial in view of the debate on its the precise scope. The classic interpretation of the breach of the fair and equitable standard is behaviour or conduct that would clearly shock the impartial observer. However, international law evolves over time, and today, the fair and equitable standard has been interpreted in recent cases to include transparency standards, for example. This makes the scope of commitments uncertain for developing countries, and they may be expected to reach high standards or risk losing disputes.

Understanding investment texts: Key terms and definitions continued

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Expropriation: Expropriation provisions are guarantees by the host state typically providing that it will not take the investor's investment unless it is for a public purpose and by paying compensation. It is well established under international law that expropriation provisions include both direct and indirect undertakings. Investors have frequently used the 'expropriation' provisions to challenge government regulatory measures under IIAs, including those regulations that were apparently made for the protection of the environment. For example, the banning of a polluting petrol additive (Methanex v. US) and refusing to permit a hazardous waste facility (Metalclad v. Mexico). The current debate in investment treaty law jurisprudence focuses on the distinction between legitimate state regulatory activity in the public interest and those state measures that are to be deemed expropriatory and therefore liable to the payment of compensation under BITs.

Investor–state dispute provisions: IIAs can contain investor–state or state–state dispute settlement provisions. The former are more controversial as they provide investors with the right to enforce directly legal guarantees contained in IIAs against the host state in an international arbitration governed by international law. The provision for direct recourse to arbitration against the host states does not require the involvement of the home state in a claim, nor does it need a prior contract between the investor and the state containing an arbitration agreement. A large number of BITs do not require investors first to use domestic courts to resolve the dispute, and tend to refer to international institutional arrangements such as the ICSID Convention. ICSID was established pursuant to the Convention on the Settlement of Investment Disputes between States and Nationals of Other States 1965 ('the ICSID Convention'), which came into force in 1966. Today, over 150 states have signed the ICSID Convention. ICSID, which is part of the World Bank Group, administers conciliation and arbitration proceedings of investment disputes between governments and foreign investors of states which are contracting parties to the ICSID Convention.

Market access: Market access for investment is equivalent to establishment. This language is used in GATS with regard to establishment (or 'commercial presence' in GATS-speak) of services investors/investments. In this context, market access means that where a country has undertaken commitments it will not impose certain restrictions – legal entity requirements, limitations on share ownership, or quotas.

Non-lowering of standards: These clauses are a recent innovation in IIAs. Their aim is to prevent a 'race to the bottom' in environmental, health, safety and labour standards and taxation incentives in order to attract investors.

Free flow of current payments and capital movements: Under these provisions, host governments usually commit not to restrict the investor's ability to transfer funds either into or out of the country, for example through limiting access to foreign exchange. Two types of payments are included in these categories: current payments (which include payments for trade and services, income from investments, interest on loans) and capital payments such as liquidation of original capital and capital appreciation.

Performance requirements: Some recent IIAs include express provisions barring or restricting 'performance requirements' beyond those required by the WTO TRIMS Agreement. Host states often impose obligations on foreign investments that oblige the investor to act in a way that is beneficial to the host economy. This includes requirements to employ or source locally, minimum levels of exports, maximum levels of imports, or to transfer technology. However, as such mandatory requirements can also interfere with the economics of an investment some IIAs bar or restrict them.

The legal backdrop: What WTO rules and BITS mean for investment in Free Trade Agreements

There is no WTO requirement for countries to include investment in Free Trade Agreements.

In fact, countries have found it difficult to set up a multilateral framework on investment, as is demonstrated by the failure of the OECD's Multilateral Agreement on Investment in 1998 and the rejection by developing countries of investment as part of WTO negotiations in 2003.

Some developing country WTO members already have some commitments on investment at the WTO notably through the agreement on Trade Related Investment Measures (TRIMS) and the General Agreement on Trade in Services (GATS) agreements. TRIMS commitments mean countries cannot use certain measures that are perceived as barriers to free trade, for example local content performance requirements. Least developed countries (LDCs) are currently exempt from TRIMS disciplines and they are attempting to extend this exemption in current WTO talks.

Developing countries that have made commitments under 'mode 3'[5] in different service sectors under GATS have essentially agreed to allow foreign investors in those sectors without using quotas, prohibitive licensing requirements or other measures deemed to restrict trade. These commitments are subject to any limitations they have put in place and certain other safeguards and exemptions allowed under GATS. Neither of these agreements constitutes a comprehensive set of rules on investment liberalisation and protection.

5 For further details see Briefing 4, The EU's approach to FTAs: Services

Although there is no multilateral agreement on investment, many developing countries have already made far-reaching commitments, often to EU member states, via bilateral investment treaties (BITS). These are reciprocal investment promotion and protection agreements between the two states. Common provisions are an assurance to provide compensation for expropriation and fair, equitable and non-discriminatory treatment. They usually provide for investor–state arbitration provisions. The EU is moving from fairly light investment provisions to more ambitious investment chapters as part of its FTAs, and the co-existence of these two sets of agreements will have implications for some countries.

Analysing offensive and defensive interests: Some questions to ask

What the European Commission might want and what this might mean for development

Judging only from past practice, the European Commission (EC) looks unlikely to seek far-reaching investment commitments in its negotiations on FTAs. Until recently, investment provisions were very shallow. For example, they did not provide market access or pre-establishment rights, and only weak investor protection provisions, if any. As the EC's internal issues paper shows, this is not likely to continue. A new, more ambitious approach is on the cards to compete with US NAFTA-style investment chapters, that will consolidate and build on what has gone before. These documents proposed a "minimum platform" for investment in new FTAs. The following table summarises the main likely aspects of new EC investment deals and their implications for development.

Issue	Examples of text language	Development implications
Non discrimination	'... each Party shall grant to establishments and investors of the other Party treatment no less favourable than that it accords to its own like establishments and investors'.	This provision requires governments to treat foreign and local firms equally. It prevents governments imposing conditions on foreign investors which would make them contribute to local development, for example requiring them to partner with local firms, use local suppliers, or export a given proportion of their production. It also means that governments might find it more difficult to provide more favourable treatment to particular local industries, for example to help disadvantaged groups or regions, or to encourage strategic local industries.
Market access	See Most favoured nation relating to establishment below:	
Free flow of payments and investment-related capital movements	'... undertake to impose no restrictions and to allow all payments for current transactions between Parties to be made in freely convertible currency.' '... undertake to impose no restrictions on the free movement of capital relating to direct investments made in accordance with the laws of the host country... and the liquidation and repatriation of capitals and any profit stemming therefrom.'	Especially without any safeguards or exemptions relating to balance-of-payments difficulties, liberalisation of the current account can lead to financial instability, as demonstrated by the East Asia Financial Crisis in 1997. Foreign investment increases the potential for capital flight from developing countries, especially if linked with a liberalisation of capital movements. Even legal methods relating to transfer pricing, can lead to developing countries losing valuable finances that could be harnessed for development. Co-operation and information exchange between partners for more transparent company reporting of profits and transactions would be more beneficial.[6]
Most favoured nation relating to establishment	'With respect to any matters affecting establishment...shall accord to the Community's establishments and investors a treatment no less favourable that that they may accord to any third country with whom they conclude an economic integration agreement after the signature of this Agreement.'	Depending on any reservations or exemptions that the country lists at the time of negotiating the agreement, this would limit the government's ability to screen and select investors. It would also limit the government's ability to choose with which countries it would like to integrate trade most or first. It would have to offer to the EU investors the same terms as to any preferred partner, for example within its own or neighbouring regions. In recent EPA deals, the EC has made a concession on this point, allowing countries to offer more favourable terms to any country that is not a 'major trading nation' (defined as an industrialised developed country or one that has one per cent or higher share of world merchandise exports).
Non-lowering of standards		These clauses can prevent countries competing with respect to labour and environmental standards or tax incentives, for example. They do not however address the problems relating to company behaviour forcing down these standards. They can also place limits on a country's policy choices and its right to change affected regulations. They also do not give countries the right to raise these standards, should they consider it beneficial to do so. This right may be effectively undermined by other provisions in IIAs, especially investor protection measures in BITS.
In-built agenda	'With a view to the progressive liberalisation of investments, the Parties shall review the investment legal framework, investment environment and the flow of investment between them consistent with their commitments in international agreement no later than .. years after the entry into force of this chapter.'	This is a binding commitment (indicated by the use of 'shall' rather than 'should') to review not only the implementation of the investment deal, but also the whole investment environment – which could be very broadly interpreted to include also general economic conditions, including infrastructure, credit provision and labour regulations, etc. The review is only to seek further liberalisation and does not allow for any rollback of commitments in the light of unintended adverse impacts on development, or for other measures to be upgraded, for example investment promotion measures by the EC or co-operation on policing the behaviour of EU firms in host markets.

The content of EU chapters in FTAs have implications beyond their own application, owing to their co-existence with EU member states' BITS. The EC has made it clear that it will not use the opportunity of negotiating more substantive EU-level FTA chapters on investment to revise EU member states' BITS or to address some of their more detrimental aspects with regard to development or their imbalanced character (that gives rights only to investors and responsibilities only to the host state).

6 Christian Aid 2006, 'Haemorraghing Money: A briefing on capital flight'

Instead, EU-wide deals will 'complement' these BITS provisions and in effect increase the scope of protection for EU member states by creating two parallel regimes of commitments of potential host states, one under BITS, the other under the EU FTA.

The new EU minimum platform proposes pre-establishment provisions for national treatment and MFN treatment, and therefore is a step up from EU member states' BITS, which usually do not contain investment liberalisation provisions (i.e. those providing for treatment at the pre-establishment phase). However, at the same time, the EU minimum platform has important features associated with BITS missing (including post establishment MFN, compensation for expropriation and, critically, an investor–state arbitration mechanism) which are found usually in BITS. Therefore, the benefit of the EC minimum platform proposals will be the greatest for those EU member states with BITS, as they would then get both pre-establishment and post-establishment protection. EU member states without BITS will also benefit from the pre-establishment national treatment and MFN provisions in the EU template, although they will not have the benefit of important BITS protections such as compensation for expropriation, post-establishment MFN treatment, fair and equitable treatment and an investor–state arbitration mechanism for enforcement of such rights, as the EU FTAs do not contain such provisions.

The implication is therefore that states considering signing up to an EU FTA that includes MFN provisions, must also consider the effect of extending the terms of their other international agreements to all EU member states.

Making trade offs – analysing what's on offer from the EU

As investment chapters of FTAs tend to be largely reciprocal, developing country signatories will benefit from the same terms and access to EU markets that they will also need to deliver. However, these rights are effectively imbalanced as the EU tends to be by far the most dominant source of investment and relatively few developing countries can set up shop in Europe.

In signing up to investment deals, developing countries can be giving up significant flexibility in selecting and managing investment, and therefore need to be sure that trade-offs are sufficiently weighted in their favour.

Developing country interests with respect to investment deals tend to be somewhat different from those of the OECD home-country markets:

- Developing countries might be interested in increasing investment in their markets. Investment agreements by themselves do not do this and investment promotion provisions tend to be limited and weak.
- Developing countries might be interested in closer co-operation to improve policing of the conduct of European firms in their markets, for example with regard to taxation and financial reporting, anti-corruption, or compliance with the OECD guidelines for multi-national enterprises.
- Developing countries might also be interested in development co-operation to help local firms to benefit from the presence of foreign firms or to ensure that institutional and regulatory capacity is sufficiently developed to properly manage foreign investment.

The International Institute for Sustainable Development (IISD) model investment treaty gives other ideas on useful alternative provisions that could be included in deals involving developing countries.

Important information and where to find it

For background on investment agreements, terminology and practice:

UNCTAD Series on issues in International Investment Agreements available at
www.unctad.org/Templates/Page.asp?intItemID=2322&lang=1

UNCTAD list of BITS by country
www.unctad.org/Templates/Page.asp?intItemID=2344&lang=1

Information on disputes
www.worldbank.org/icsid
www.lcil.cam.ac.uk/publications/icsid_reports.php
www.investmentclaims.com/oa1.html
www.ita.law.uvic.ca

Case Studies and analysis
www.iisd.org/investment (International Institute for Sustainable Development)
www.somo.nl

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6. The EU's approach to Free Trade Agreements: Competition
7. The EU's approach to Free Trade Agreements: Government Procurement
8. The EU's approach to Free Trade Agreements: Intellectual Property

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6 The EU's approach to Free Trade Agreements
Competition

This paper forms part of a series of eight briefings on the European Union's approach to Free Trade Agreements. It aims to explain EU policies, procedures and practices to those interested in supporting developing countries. It is not intended to endorse any particular policy or position, rather to inform decisions and provide the means to better defend them. The views expressed in the briefings do not necessarily reflect the views of the publishers.

What's at stake?

For developing countries

- Competition policy is a critical tool for governing the market. Used effectively it ensures that consumers and producers get a 'fair' price, and it can be an important tool for nurturing and supporting new industries, particularly small and medium-size enterprises.
- Developing countries increasingly need international co-operation to overcome the anti-competitive effects of international mergers and acquisitions on their own markets, and the anti-competitive practices of foreign firms in their markets. They often lack the leverage, capacity and even information to do this alone.
- Developing countries also appropriate domestic and regional competition frameworks as their markets develop, and as the privatisation and deregulation of recent decades mean that competition and regulation are needed to ensure welfare gains from foreign investments or private takeovers of former state monopolies. These upgrades can be expensive and technically challenging, so EU assistance might be helpful.
- Designing competition policies which are appropriate to developing-country conditions is critical for development gains. The current model of competition policy envisioned by the EU in its draft Free Trade Agreements (FTAs) may not be the appropriate model. Levelling the playing field in developing countries, for example with respect to state aid, might in fact lead to less competition as local firms cannot compete on equal terms with European ones. Competition models need to be appropriate to local conditions and policy objectives, and agreements must allow flexibility to achieve this.
- Developing countries are unlikely to achieve changes in competition rules in EU markets. Few developing countries invest in EU markets, so trade-offs for their own firms' benefit are limited. Moreover, it might be difficult for non-EU firms to bring cases directly against EU firms' anti-competitive practices, not least because of the procedural requirements involved which may be too costly for non-EU developing-country firms to pursue, or because their domestic competition authorities might not be equipped to deal with them fully.

Competition law is intended to improve the welfare and economic outcomes arising from structural issues in markets (such as monopolies) or from firms' behaviour (such as price-fixing or collusion).

For the European Union

- The EU has a strategic interest in developing international rules and co-operation on competition policies to ensure European firms do not suffer in third countries from anti-competitive practices or unreasonable subsidisation of local companies.
- The absence of competition and state aid rules in third countries limits market access as it raises new barriers to substitute for tariffs or traditional non-tariff barriers. The EU wishes to ensure that their trade partners refrain from having recourse to aids to protect their firms from international competition.
- The EU also sees a strategic interest in preparing for the next level of multilateral liberalisation by including competition in FTAs and obtaining convergence around the EU model.
- Competition rules would be backed up by trade defence instruments against unfair trade advantages caused by anti-competitive pricing, subsidies or other state-induced distortions.
- Unlike developed countries, whose fund transfers tend to go to private citizens, in developing countries the share of GDP spend on commercial state-owned enterprises is higher.[1] The EU may also be concerned over the use of state aid to support the competitiveness of developing-country firms in world markets – almost a quarter of the 100 largest developing-country multinational corporations are state-owned.[2]

1 World Bank, *Beyond Economic Growth* (2000), pp. 61–62, at www.worldbank.org/depweb/beyond/beyondco/beg_11.pdf.

2 UNCTAD, *World Investment Report 2006: FDI from Developing and Transition Economies: Implications for Development* (2006), pp. 122–124.

Understanding competition texts: Key terms and definitions

State aid: Financial or other help granted by a government (directly or otherwise) to support the establishment and/or operations of a firm or the production of certain goods.

Market dominance: Firms are considered to be dominant when they control a significant share of a market. They can abuse this position to fix prices or otherwise distort markets for their own benefits.

Concerted practices: This covers different forms of collusion like price-fixing, fixing output, and dividing up markets between a few firms that are able to dominate a market.

Hard-core cartels: A cartel is a formal agreement among firms (in markets where a few firms dominate) to fix prices or output, or otherwise collude for their mutual benefit.

Undertakings: These are individuals, enterprises, corporations or legal entities that may legally undertake or engage in business operations. This is a broad definition that covers any body engaged in commercial operations – public or private bodies, individuals or companies.

WTO and the legal backdrop to competition in FTAs

There is no WTO requirement for competition policy to be included in FTAs. In fact, there is no WTO agreement on trade-related aspects of competition, its consideration as a negotiating issue having been rejected by developing countries along with the other "Singapore Issues" at the Cancun WTO Ministerial in 2003, a situation formalised by the General Council in July 2004.

That said, competition policy may also be said to have been already embedded in the main agreements of the WTO. Both the General Agreement on Tariffs and Trade (GATT) 1994 (with respect to goods) and the General Agreement on Trade in Services (GATS) have provisions on monopolies, exclusive service suppliers,

subsidies to state enterprises, and restrictive business practices. And the Trade-Related aspects of Intellectual Property Rights (TRIPS) agreement recognises the right of governments to act against abuses of intellectual property rights having an anti-competitive effect in the relevant market.

What the EU might want

The EU was a strong proponent of competition rules at the WTO. It sought:

- agreement on core principles of transparency, non-discrimination and procedural fairness (protection of confidential information and right of petition to authorities, administrative decisions subject to judicial review)
- ban on hard-core cartels
- modalities for voluntary co-operation and information exchange
- capacity-building to help developing countries develop competition institutions
- flexibility for developing countries to take account of development needs.

In its FTAs, the EU goes further and also seeks substantive convergence around the EU model, as set out in the EU Treaty. The EU Treaty prohibits the following:

- Agreements, decisions or concerted practices between undertakings which affect trade and have as an objective or effect the prevention, restriction or distortion of competition
- Abuse by one or more undertaking of dominant market position
- Aid granted by the state through state resources or any form that distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods, in so far as it affects trade.

There can be exceptions to these general bans, if the practice improves production or distribution of goods or promotes technical or economic progress, provided the consumer gets a fair share of the resulting benefit and provided that there are not restrictions on competition that are not indispensable to the attainment of these aforementioned objectives, and provided that the measures do not allow the undertakings to eliminate competition in the products in question.

Very similar provisions can be found in the Euromed Agreements although the exceptions provisions are absent. The agreements also allow the EU to assess anticompetitive practices in the Euromed partner markets on the basis of its own rules criteria, which would give an advantage in invoking the Agreement's competition provisions against competitors of EU firms in Euromed markets.

In its agreement with South Africa, more flexibilities are included, for example:

- concerted practices must "substantially distort" competition before coming under the ban; and can be exempted if pro-competitive effects outweigh anti-competitive ones;
- the ban on state aid contains an exemption for aid which supports a "specific public policy objective"
- South Africa's domestic laws and regulations apply in implementing the agreement (in contrast to some of the Euromed agreements) so that South Africa can apply a locally appropriate definition of market dominance or measures to deal with it, for example.

The EU–Chile agreement is the "lightest" of all. Because of the established competition legislation and regulatory authority, it makes no reference to prohibited practices, only requiring each party to apply its respective competition laws, and agreement to co-operation and co-ordination among its authorities including "notification, consultation, exchange of non-confidential information and technical assistance".

EU agreements also tend to contain provisions on comity[3] and co-operation in investigation and remedies, information exchange (with respect for commercial secrecy) and, in some cases, for technical assistance in building institutional capacity.

According to draft negotiating mandates of the European Commission (EC) for these deals, they are likely to seek substantive agreements on rules and enforcement, binding agreements on co-operation and information exchange and a commitment to establish a competent regulatory authority.

3 Comity is the principle that countries will respect the the laws, judicial decisions, and institutions of each other.

Key questions in analysing development implications and trade-offs

Is the EU model the appropriate one?

Competition policy is intended to level the playing field to ensure efficiency and welfare gains. However, it assumes certain market conditions that might not exist in developing countries. Where access to domestically sourced capital is difficult, state support to private firms can increase competition, whereas overly strict rules could constrain this by allowing one or a few foreign firms to wipe out local competition.

Other public policy objectives might be more important in developing countries than favouring competitive outcomes. Japan and East Asian economies as well as some Latin American countries used state support to foster the development of big businesses that were internationally competitive and that led in the diffusion of new technologies and adaptation of imported technologies to domestic circumstances.[4] The UK formerly tolerated cartels in order to protect jobs.

4 Singh and Duhmale, South Centre Working Paper 7, November 1999.

These issues would imply that accepting strict substantive or even extra-territorial application of the EU model might not be the most appropriate option for developing countries. Leaving open the precise rules that might be applied (as in the EU–Chile deal) or making less stringent commitments that leave space for these considerations (as in the EU–South Africa deal) might be more appropriate. Most African, Caribbean and Pacific (ACP) regions have instead opted not to negotiate beyond co-operation on competition matters – however, this might be less palatable to the EC in markets where conditions for EU firms is more commercially significant.

How best can co-operation on cross-border cases and on the conduct of European firms be achieved?

Developing countries can benefit from co-operation with European authorities. For example, when European firms merge, the impacts on developing-country markets can be significant but are not necessarily taken into account in EC investigations or remedies. This was demonstrated in some African markets as a result of banking mergers in the 1990s which created anti-competitive situations in their financial services markets. Developing countries on their own can lack the leverage, capacity or information to address this.

The activities of European firms can have anti-competitive effects on developing-country markets. A well-known example is the impact of dominant supermarket buyers with highly integrated supply chains on suppliers in developing-country markets. Developing countries could benefit from co-operation with the EC on investigating and disciplining these kinds of firms. That is, support to restrain the anti-competitive conduct of European firms (especially multinationals) and limit the negative impacts of the mergers of multinationals on the domestic markets and competitiveness of developing-country firms should form part of the co-operation framework.

In addition, the EC can support, through skills transfers and other assistance, the development of competition policy in developing countries that would allow them to harness and link industrial policy to competition policy. This would imply accepting, as an integral part of the technical co-operation framework, that encouraging inappropriate competition may be ruinous and that the government may need to intervene in the entry and exit decisions of firms (whether private or state-owned) and promote an industrial policy that on the one hand encourages the development of stronger domestic firms (which may be oligopolies) and on the other hand promotes domestic competition among these firms.

Will partner country firms make gains from a leveling of the playing field in EU markets?

Developing-country firms operating in EU markets are less numerous than their counterparts. In general, developing-country firms willing and able to invest outside their home markets have tended to display a strong preference for investing in other developing-country markets as opposed to developed-country markets, although investments in the latter have also started rising. This has generated mixed reactions from developed-country governments involved in the process (for example, Dubai Port World and CNOOC in the US, Mittal Steel in the EU).[5]

5 UNCTAD, World Investment Report 2006: FDI from Developing and Transition Economies: Implications for Development (2006), pp. 120-121.

If there are insufficient trade-offs with regard to gains in EU markets or in gains from co-operation and capacity-building assistance – developing countries should consider in the light of their negotiating capacity whether inclusion of competition in FTA talks would actually add significant value.

What institutional and regulatory capacity upgrades are needed?

Accepting binding commitments on setting up regulatory authorities or even on transparency and information exchange can be a risky strategy for developing countries if they cannot be sure of having the capacity to fulfill these obligations. Best endeavour provisions might be a better option, or linking transition periods to capacity to implement or effective assistance being supplied by the EU.

Support for the development of domestic and regional competition legislation and structures is another interest of developing countries in deals with the EU, although maintaining independence as to what kind of regimes are set up is important.

Important information and where to find it

UNCTAD (2005): *Competition provisions in regional trade agreements: How to assure development gains*

Treaty Establishing the European Community, Official Journal of the European Union (C321 E/37, 29/12/2006, Consolidated version)

South Centre *TRADE Working Paper 7*, November 1999

Ajit Singh, *Competition and Competition Policy in Emerging Markets: International and Developmental Dimensions*, University of Cambridge, May 2002.

UNCTAD (2006), *World Investment Report 2006: FDI from Developing and Transition Economies: Implications for Development*

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7 The EU's approach to Free Trade Agreements
Government Procurement

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What's at stake?

For developing countries

- In developing countries, government procurement is a very important component of the economy, constituting between 10 and 20 per cent of GDP. The government's ability to purchase goods and services can be an important developmental tool; for example, in directing expenditure at locally produced goods and at local or domestic companies.
- Free Trade Agreements (FTAs) typically entail developing countries making commitments on the rules and processes governing government procurement, and opening up their government procurement markets to foreign firms.
- Locally appropriate and sound rules and processes for government procurement that ensure transparency and accountability can be important in helping to overcome corruption and ensuring value for money for government spending. However, experience is mixed of the effectiveness of importing EU-style models.
- Implementation of procurement reforms can be expensive – especially if rules relate to regional as well as national levels of government. This should be borne in mind when weighing up the choice between making binding rules commitments or agreements on co-operation and assistance.
- Developing countries tend to be excluded from the European procurement market by stringent standards and other non-tariff barriers. The European Commission (EC) states that this access may be restricted further for countries that do not open up government procurement markets through free trade agreements: According to *Global Europe*: "where important trading partners have made clear that they do not want to move towards reciprocity, we should consider introducing carefully targeted restrictions on access to parts of the EU procurement market to encourage our partners to offer reciprocal market opening".[2, 3]

Government procurement (GP) is the term used to describe the purchasing activities of all levels of government and government-controlled entities[1]. Rules governing treatment of foreign providers of goods and services to public entities, and requirements relating to procedural standards in public tendering and contracts, are an increasingly common feature of EU FTAs.

1 National defence and security are generally excluded from FTA coverage.

2 European Commission, 2006. *Global Europe: Competing in the World*. trade.ec.europa.eu/doclib/docs/2006/october/tradoc_130376.pdf

3 The Commission also states that 'for the sake of consistency with EU development policy, this approach would not be considered for poorer countries'.

For the European Union

- As set out in *Global Europe:* "Public procurement is an area of significant untapped potential for EU exporters. EU companies are world leaders in areas such as transport equipment, public works and utilities. But they face discriminatory practices in almost all our trading partners, which effectively close off exporting opportunities. This is probably the biggest trade sector remaining sheltered from multilateral disciplines." Consequently, the European Union is looking for "a sharper focus on market opening and stronger rules in new trade areas of economic importance to us notably … government procurement".[4]

4 European Commission, 2006. Op cit.

- Because of the failure of a multilateral agreement at the World Trade Organization (WTO), government procurement has been an integral part of the new breed of European FTAs. The goal for Europe is clear: "FTAs, if approached with care, can build on WTO and other international rules by going further and faster in promoting openness and integration, by tackling issues which are not ready for multilateral discussion and by preparing the ground for the next level of multilateral liberalisation. Many key issues, including …public procurement …, which remain outside the WTO at this time can be addressed through FTAs."[5]

5 European Commission, 2006. Op cit.

- Sectorally, European interests are in the areas of construction work, services surrounding architectural, legal, accounting and construction business, medical and pharmaceutical devices and services and office and computing equipment (accounting for about 50 per cent of government procurement in the EU). Europe is a world leader in the export of services, as well as in sectors such as construction, pharmaceuticals, public utilities and transport equipment. The draft mandates for EU FTAs with the Andean Community and Central American nations confirm the priority sectors for Europe: in the former, the EU is targeting water, energy, transport, and the information and communication sectors; for Central America, the priorities are water, energy and transport. In relation to India, the EU's market access database complains about discrimination in the country's procurement practices, and particularly targets the energy and port maintenance contracts for favouring local companies (see 'Important information and where to find it' on page 8).

Understanding government procurement texts: Key terms and definitions

Government versus public procurement: Often used interchangeably, but public procurement is technically the correct term as it covers not just purchases by government but also by public utilities and state-owned enterprises.

Reciprocity: In their FTAs, the EU expects the third party to reciprocate (i.e. give in return) any concessions granted by the EU. For example, if the EU agrees to open up its government procurement markets, it expects the other party to reciprocate.

National treatment (NT) and non-discrimination: Foreign (i.e. imported) and locally produced goods and services should be treated equally (i.e. trade should be conducted without discrimination).

Offsets: Measures used to encourage local development or improve the balance-of-payments accounts by means of domestic content, licensing of technology, investment requirements, counter-trade or similar requirements.

Price preferences: Foreign suppliers have their bids inflated by a certain percentage before being compared to bids from domestic suppliers as a means of favouring local and national companies.

Government procurement at the WTO

The multilateral agreements on trade in goods and services explicitly exclude government procurement. Currently, the General Agreement on Tariffs and Trade (GATT) 1994 excludes "procurement by government agencies of goods for their own use and not intended for commercial sale" (Article 111.8a).[6] The General Agreement on Trade in Services (GATS) Article XIII excludes procurement of services.[7]

However, a plurilateral Agreement on Government Procurement (GPA) at the WTO was first negotiated during the Tokyo Round. It entered into force on 1 January 1981 and was revised in 1994. Currently there are 13 members (counting the EU as one). The majority of developing countries are not party to the GPA.

The GPA "establishes a framework of rights and obligations regarding national procurement laws, regulations, and procedures of parties. Governments are required to apply the principle of national treatment to the products, services, and suppliers of other parties to the GPA and to abide by the Most Favoured Nation (MFN) principle (i.e. not to discriminate among goods, services, and suppliers of other parties)."[8] The GPA covers a number of important components:

- **transparency** in procurement (i.e. general rules and obligations on procurement policies, tendering procedures, etc., are made available to all interested parties) to which the principle of non-discrimination applies;
- the **award of contracts** (i.e. expanding **market access**) on a non-discriminatory basis;
- the **schedules** of national entities in each member country whose procurement is subject to the agreement;
- **compliance** through bid challenges.

With regard to **scope and coverage**, the Agreement does not apply to all government procurement of the Parties. The obligations under the Agreement only apply to:

- procurement by the procuring entities that each Party has listed in its schedules, relating respectively to central government entities, sub-central government entities and other entities such as utilities;
- all goods purchases, unless a nation secured exemptions during the negotiation of the agreement;
- services that are specified in positive lists;
- only those transactions that exceed certain threshold levels.

The GPA does recognise limited special and differential treatment for developing countries (see Article V). But by the same token, the agreement prohibits the use of various development measures which are used to encourage the development of domestic industries and links into local economies. For example, by limiting the use of offsets and, through the principle of non-discrimination, prohibiting price preferences to domestic suppliers."[9]

Notwithstanding this, developing countries may negotiate, at the time of their accession to the GPA, conditions for the use of offsets, provided these are used only for the qualification to participate in the procurement process and *not* as criteria for awarding contracts (Article XVI).

6 Juris International, 2006. Transparency in Government Procurement Practices. www.jurisint.org/pub/06/en/doc/C24.pdf

7 WTO, 2007a. GATS Negotiations of Services Procurement. www.wto.org/english/tratop_e/gproc_e/gpserv_e.htm

8 Evenett, S., 2003. *Can Developing Countries Benefit from Negotiations on Transparency in Government Procurement in the Doha Round?* www.evenett.com/reports/evenettgpanddoharound.pdf

9 Evenett, J. 2003. Is There a Case for new Multilateral Rules on Transparency in Government Procurement? In Evenett, J. (ed) *The Singapore Issues and the World trading System: The Road to Cancun and Beyond*. www.evenett.com/chapters/wtoguideprocurement.pdf

Using social and development 'objectives' in government procurement: An example of the kind of initiatives which could be under threat from the EU's current proposals

Perhaps the best example of using government procurement for achieving social objectives in developing countries comes from South Africa. Under current South African government policy, "previously disadvantaged individuals" are given preferences in the allocation of government contracts. This policy is known as "Black Economic Empowerment", and seeks to repair inequalities from the apartheid regime. BEE charters are now being applied across the country, and large companies now have quotas for procurement from black-owned, largely local companies. Eskom, the South African utility has established its own highly successful BEE scheme: "Eskom's policy is to maximise purchases from BEE firms of all sizes and a spread of industries. It also works to foster businesses owned by BEE women across all sectors of the economy. Beyond this, the company concentrates its developmental efforts on black suppliers in the manufacturing, construction and mining/extraction sectors and providers of professional consulting services. Eskom has set its own criteria reflecting different levels of black ownership in these companies to decide the procurement spend allocated to each category."[10]

10 Eskom, 2007. *BEE Case Study*. www.eskom.co.za/live/content.php?Item_ID=2784

A possible multilateral deal at the WTO ?

Since the WTO Ministerial in Singapore in 1996, some members have been trying to introduce a multilateral deal on government procurement at the WTO. Such was the level of disagreement at the WTO, members decided to look into the possibility of introducing an agreement covering only transparency. The EU confirmed that: "The transparency exercise is NOT about … obtaining national treatment in the award of contracts or allowing governments to challenge individual contracts through the WTO dispute settlement mechanism [EU Emphasis]."[11] Nevertheless, the work programme on transparency was extensive, examining:

- Procurement methods; i.e. should tenders be open, selective or limited?
- Publication of information on national legislation and procedures
- Information on procurement opportunities, tendering and qualification procedures
- Time-periods for tendering and awarding contracts
- Transparency of decisions on qualification
- Transparency of decisions on contract awards
- Domestic review procedures
- Information to be provided to other governments (notification)
- Dispute settlement procedures
- Technical co-operation and special and differential treatment for developing countries.

11 European Commission, 2007. *Government Procurement: Transparency in Government Procurement*. http://ec.europa.eu/trade/issues/sectoral/gov_proc/wto_nego/index_en.htm

Eventually, even the proposal for an agreement on transparency was thrown out at the WTO Ministerial in Cancun and formally removed from the negotiating agenda at a WTO meeting in August 2004.

An agreement on transparency in government procurement, whilst not ideal for the EU to say the least, would have established, albeit in a limited way, a multilateral agreement on 'government procurement' within the WTO. To the EU, this would have been a means of gently introducing policy changes to minimise resistance against the measure, and then to drive forward more and more offensive policy measures in the future. In 1996, the then Acting US Trade Representative, Charlene Barshefsky said: "The study on procurement is intended to be the first step toward an agreement on transparency practices in government procurement … this initiative will, as we continue to push it, help create an environment where businesses can expect a fair shake in competing for contracts with foreign governments."[12] Similar sentiments have been expressed by the European Commission.

12 USTR, 1996. Press release at end of WTO ministerial meeting in Singapore.

For many developed nations at the WTO, who put the issue onto the agenda at the Ministerial in Singapore in 1996, there is deep frustration that a fully fledged multilateral deal on government procurement has simply floundered. Partly as a result of this failure, the EU and other developed nations have introduced procurement chapters that incorporate and build on the GPA into their FTAs.

Government procurement: Key questions

What is the relationship between the WTO, GPA and current EU FTAs?

There is currently a great deal of similarity between existing provisions of EU FTAs and the GPA.[13]

13 Woolcock, S. 2006. Rule-Making in Public Procurement. In Woolcock, S. (ed) *Trade and Investment Rule-Making: The Role of Regional and Bilateral Agreements*. United Nations University Press.

	1994 GPA	EU–Chile	EU–Mexico[14]
Transparency	• Information on national procurement laws • Contract to be advertised	• Information to enable effective bid (Art 142) • Information on why bid was unsuccessful	• Information on tenders and decisions
Principle	• Non-discrimination (National Treatment and Most Favoured Nation)	• NT and non-discrimination	• NT and non-discrimination
Award of contracts	• Lowest price or most economically advantageous bid	• Lowest price or most economically advantageous bid based on certain criteria	• Lowest price or most economically advantageous bid based on certain criteria
Compliance	• Bid challenge	• Bid challenge • Independent review • Interim measures	• Bid challenge • Independent review • Interim measures
Scope and coverage	• Central government: > 130,000 SDRs for services > Five million SDRs for goods • Non-national government: > 200,000 SDRs for services, > Five million SDRs for goods • Utilities: > 400,000 SDRs for services, > Five million SDRs for goods	• Covers central and non-central government and utilities • Goods, services and works • Thresholds as per the GPA	• Covers central, non-central government and utilities • Goods, services and works • Thresholds as per the GPA for EU, slightly lower for Mexico as per NAFTA
Offsets and price preferences	• Offsets prohibited; preferences not explicitly mentioned but effectively banned through principle of non-discrimination	• Prohibited	• Offsets prohibited; preferences not explicitly mentioned but effectively banned through principle of non-discrimination

What is the relationship between Government Procurement and new EU Free Trade Agreements?

According to the EU, its new FTAs with Asian countries should be comprehensive and "should provide for enhanced provisions on trade in goods and services, and include binding provisions on regulatory transparency in areas relevant for mutual trade and investment, including… public procurement".[15]

Specifically for India and the Association of South-East Asian Nations (ASEAN), provisions on public procurement within the FTAs "shall provide for a set of binding rules including adequate transparency provisions that support the setting up of effective procurement systems. They will also provide for challenge procedures and co-operation in the field of electronic procurement. To the extent appropriate, the procurement chapter should be consistent with the revised Government Procurement Agreement. The Agreement will envisage the progressive liberalisation of procurement markets at national, regional and, where appropriate, local levels, as well as in the field of public utilities, in particular in

14 The negotiations in the EU–Mexico RTA have been concluded with the EU offering Mexico the higher thresholds of the GPA (and of the EC Directives) and Mexico offering the EU the lower thresholds of the NAFTA. This has been done to facilitate the tender procedure through a transparent and widely-known rule identical for all tenderers within each of the Members, and to avoid, for both procuring entities and suppliers, the need to handle different thresholds and verify which agreement applies for each call for tender.

15 See draft negotiating mandates for both India and ASEAN countries at www.bilaterals.org

priority sectors. The objective is to achieve gradual market access on the basis of the principles of non-discrimination and national treatment."[16] The wording in the South Korea draft mandate is slightly different, reflecting that fact that the country is party to the WTO GPA.

16 Ibid.

There is a thinly veiled attempt to provide some ASEAN countries with an element of special treatment: "Market access commitments will take into account the different levels of development of ASEAN countries". This reflects the fact that three ASEAN countries are least developed countries. However, a number of ASEAN countries have already indicated that they do not want to negotiate the issue at all.

Similar provisions to those contained in the draft negotiating mandates for India and ASEAN are also included in the Latin American FTAs that the EU is planning.

Of the potentially new FTAs (with African, Caribbean and Pacific countries, Mercosur, India, South Korea, ASEAN countries, the Andean Community and Central American nations), only Korea is party to the GPA. Clearly, for all the rest, any agreement on government procurement in FTAs will be "WTO-plus" in that they have decided not to join the WTO agreement. Agreeing to government procurement in FTAs will lock in parties to binding provisions with important development implications.

Is the EU making any developmental allowance for poorer developing countries on government procurement, for example in Economic Partnership Agreements?

The short answer is that the EU is making little if any allowance for African, Caribbean and Pacific (ACP) countries, some of the poorest nations in the world. Many ACP countries oppose the inclusion of government procurement; what they need above all is to establish national rules and build regional regulatory capacity. As of 2007, the EU has even refused to include binding obligations to provide technical and financial assistance to help ACP countries comply with any new government procurement rules.

Only relatively recently (i.e. late 2006 onwards) have the texts in the Economic Partnership Agreement negotiations started to cover government procurement. Some are less developed than others (for example, the procurement article of the EU–ESA (Eastern and Southern Africa) joint draft text of July 2007 is blank). In others, worryingly, with some of the world's poorest countries, the EU is pushing for strong provisions covering transparency, market access and the principle of national treatment.

In December 2007, the EU and the Caribbean (CARIFORUM) signed an Economic Partnership Agreement (EPA) which included government procurement. The authors have not seen the final text but the October 2007 draft proposal indicates possible language that might be included in future EPA deals on procurement. It includes (in square brackets) a proposal from the EU "for possible negotiations on market access".[17] In perhaps an attempt to persuade CARIFORUM to negotiate such issues, the EU proposal allowed for a price preference programme (provided that the preference is only for the part of the tender incorporating goods or services originating in a Signatory CARIFORUM State) and for offsets (provided that any requirement for, or consideration of, the imposition of the offset is clearly stated in the notice of intended procurement and the notice inviting suppliers to apply for participation in procurement covered). But these would be phased out over an undefined period.

17 EC_CARIFORUM, 2007. Economic partnership agreement between the Cariforum states, of the one part, and the European Community and its member states, of the other part. 1st October 2007.

Government procurement in the EU–SADC (Southern African Development Community) Economic Partnership Agreement was another where, in June 2007, Europe proposed a text in terms of the EU's offensive interests: "The Parties shall set as their objective the effective, *reciprocal and gradual opening of the government procurement markets*. Each Party shall ensure that the procurement of its entities

covered in Annex A takes place in a transparent, reasonable and *non-discriminatory manner, treating any supplier of either Party equally* and ensuring the principle of open and effective competition [Our emphasis]." Eventually, government procurement was not included in the EU–SADC interim deal of November 2007 but parties agreed to negotiate the issue when adequate capacity had been established.

What are the implications of government procurement on development?

Rich nations have gone to some lengths to highlight what they believe are the potential benefits to developing countries from being a party to a multilateral government procurement agreement. They argue that more open and efficient public procurement practices could contribute towards the sound management of public expenditures. There are indirect links from greater efficiency in the use of public resources and poverty reduction through the delivery of public services in health, education and infrastructure. Transparent procurement practices could also act as a control on corruption and contribute to an improvement in the quality of governance within the public sector.

Yet many developing countries have consistently opposed the inclusion of government procurement in the WTO negotiation agenda (and in other trade talks). This opposition is on the grounds that:

- There are fundamental concerns about the potential damaging effects on the development process. Procurement policies may be part of an industrial policy or an instrument to attain social objectives (for example, support for small and medium-sized enterprises, minority-owned businesses, disadvantaged ethnic groups, or certain geographic regions) through set-asides and preference policies.[18] In addition, a government's ability to procure from firms of its own choice can be an instrument for macroeconomic management.[19] There is the concern that premature or over-rapid opening of government procurement markets will allow large foreign firms to drive out local firms before increasing prices, as happens with predatory dumping. Procurement can account for some ten per cent of GNP (with commensurate implications on local employment), and there are immense implications for national development, local business and job creation/losses.

  This has been recognised by Joseph Stiglitz, former chief economist at the World Bank: "Government procurement policies have important economic and social roles in developing countries which would be curtailed if governments were mandated to observe national treatment principles. The level of expenditure and the attempt to direct the expenditure at locally-produced materials is a major macro-economic instrument, especially during recessionary periods, to counter economic downturn … Additionally, procurement policy might be used to boost domestic industries or encourage development in specific sectors of national interest. Social objectives could also be advanced by preferences for specific groups or communities, especially those that are under-represented in economic standing."[20]

- Most developing countries are unlikely to gain a significant share of the government procurement market in the developed-country partner's market. Developing countries' competitive advantage may lie in the provision of labour-intensive services, which would require liberalisation of labour flows from developing to developed countries. Where developing countries can compete in the supply of goods, the lack of information on tender invitations and of the expertise required in filing the tenders have so far prevented producers from developing countries from accessing this market.[21] To meet these conditions will often require a commercial presence in the developed country, which is a difficult obligation for firms from developing countries to meet.[22]

18 Stiglitz, J. and A. Charlton, 2005. *Fair Trade for All: How Trade can Promote Development*. Oxford University Press.

19 Stiglitz, J., 2004. *An Agenda for the Development Round of Trade Negotiations in the Aftermath of Cancun*, London: Commonwealth Secretariat, p18

20 In Stiglitz and Charlton, 2005. Op cit.

21 Rege, V., 2001. Transparency in Government Procurement: Issues of Concern and Interest to Developing Countries. Journal of World Trade 35(4): 489–515, 2001.

22 Hoekman B. and P. Mavroidis, 1997 (eds). *Policy in Public Purchasing: The WTO Agreement on Government Procurement*, Ann Arbor: University of Michigan Press.

- The scope of the issues is unclear (this is one of the issues 'under discussion' in the WTO's Working Group on Trade and Government Procurement).
- They lack the technical and institutional capacity to comply with international tendering procedures (many ACP countries have argued that, first and foremost, they need to establish national rules on GP and build regional regulatory capacity).
- Many poorer developing countries would simply not benefit. Many of the resources for procurement in these countries are given via international financial institutions, such as the World Bank, provisions for which are similar to the GPA. The GPA would also not apply to tied purchases from donor countries; tied aid is high in many of these countries.[23]
- Developing countries will have some scope to exclude sensitive sectors from coverage under a positive list approach. However, they will undoubtedly come under intense pressure from the EU to include many sectors that are of interest to European companies, as has happened in services negotiations at the WTO.
- There is simply a lack of evidence to support the imposition of government procurement policies within trade agreements. Very few studies have been conducted in this area. One that has been conducted is for the EU–India FTA by the United Nations Conference on Trade and Development (UNCTAD) in India. Their preliminary conclusions suggest that the inclusion of GP in the FTA would result in a "net welfare loss" to India.

23 Juris International, 2006. Op cit.

If the EU agrees to an FTA that only covers transparency in government procurement, might this be more development-friendly?

In their eagerness to get government procurement into FTAs and to placate any opposition from the third party, the EU might agree to an agreement that covers only transparency. However, this is likely to be viewed by the EU as a means of getting government procurement onto the agenda – and they would insist on negotiations on a fully fledged agreement at a later date. Agreeing to transparency commitments in a trade agreement can provide a strong and credible signal to the private sector and encourage more firms to bid for government contracts. However, countries have to be careful not to agree to commitments on international tendering procedures that they will struggle to implement and could be penalised for under the terms of the agreement.

Important information and where to find it

Global Europe
http://ec.europa.eu/trade/issues/sectoral/competitiveness/global_europe_en.htm
http://trade.ec.europa.eu/doclib/docs/2007/april/tradoc_134507.pdf

Key government procurement texts for EPAs, Mexico, South Africa and Chile
www.bilaterals.org/rubrique.php3?id_rubrique=52 (for latest EPA texts)
http://eur-lex.europa.eu/LexUriServ/site/en/oj/1999/l_311/l_31119991204en00030297.pdf (South Africa)
http://trade.ec.europa.eu/doclib/docs/2004/october/tradoc_111722.pdf (Mexico)
http://ec.europa.eu/trade/issues/bilateral/countries/chile/euchlagr_en.htm (Chile)

Draft negotiating mandates on the EU's new FTAs
www.bilaterals.org/rubrique.php3?id_rubrique=52

EU's market access database (which includes government procurement)
www.madb.europa.eu/madb_barriers/barriers_select.htm

The WTO's Agreement on Government Procurement
www.wto.org/english/tratop_e/gproc_e/gproc_e.htm

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4. The EU's approach to Free Trade Agreements: Services
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6. The EU's approach to Free Trade Agreements: Competition
7. The EU's approach to Free Trade Agreements: Government Procurement
8. The EU's approach to Free Trade Agreements: Intellectual Property

We will be updating these briefings as negotiations and understanding progress, and would welcome your feedback.

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8 The EU's approach to Free Trade Agreements
Intellectual Property

This paper forms part of a series of eight briefings on the European Union's approach to Free Trade Agreements. It aims to explain EU policies, procedures and practices to those interested in supporting developing countries. It is not intended to endorse any particular policy or position, rather to inform decisions and provide the means to better defend them. The views expressed in the briefings do not necessarily reflect the views of the publishers.

What's at stake?

For developing countries

- The management of intellectual property is essential not only to encourage innovation and technological advancement which are crucial to economic development; it also affects access to information and knowledge that has impacts on public health objectives, industrial development, food security and education. The challenge is to strike the right balance between rewarding innovators and promoting public access.
- Developing countries tend not to be owners of conventional intellectual property rights – they owned between 5.3 and 7.0 per cent of global patents in 2006. Developing country interests in intellectual property tend not to be well served by current protections and rules; for example they are rich in traditional knowledge and plant genetic resources.

For the European Union

- Developed countries tend to own the majority of recognised intellectual property rights. The EU, US and Japan together owned 75.7 per cent of the world's patents in 2006.
- IPRs account for a large proportion of the EU's GDP and are important to high-growth sectors. For example, the cultural and creative sector turned over €654 billion in 2003 (2.6 per cent of GDP), and employed 5.8 million people (3.1 per cent of the EU–25 workforce).
- *Global Europe* identifies knowledge sectors as those where EU firms are world leaders and addressing the high costs of poor intellectual property enforcement overseas as a main objective of the strategy.
- The EU has ambitions for multilateral rules on IPRs at the WTO that it is finding difficult to achieve, for example a strict register of Geographical Indications. Gaining acceptance of these rules in regional trade deals will strengthen its position at the WTO.

Intellectual property is any intangible asset that consists of knowledge and ideas, such as a scientific invention or a literary work. Intellectual property rights (IPRs) are legal protections that give the inventor or owner of an idea the exclusive right to certain benefits deriving from their original idea – some examples are patents, copyrights and trademarks. Rules on how these rights should be protected at a minimum are increasingly included in trade deals.

Understanding IPR texts: Key terms and definitions

You may want to look at the following glossary for some of the definitions: www.wipo.int/tk/en/glossary/

Patent: A government grant to an inventor assuring him the sole right to make, use and sell his invention for a limited period.

Copyright: Exclusive right to produce copies and to control an original literary, musical or artistic work granted by law for a specified number of years.

Trademark: Officially registered distinguishing mark to identify goods or services of a particular manufacturer or dealer.

Geographical indications: place names or words associated with a place used to identify products which have a particular quality, reputation or other characteristic because they come from that place; for example Champagne or Harar coffee.

Exhaustion of intellectual property rights: Once a product is sold on a market, the intellectual property owner no longer has rights over it – his/her rights are "exhausted". Whether or not the right continues to be exhausted when the good is imported from one market to another depends on the type of exhaustion regime the country has adopted, whether national or international.

Adapted from
W. Goode, *WTO Dictionary of Trade Policy Terms*, 4th edition, CUP 2003
Concise Oxford English Dictionary, 11th Edition, Oxford University Press 2006

WTO and the legal backdrop to Intellectual Property Rights

There is no WTO obligation to include intellectual property rights in Free Trade Agreements (FTA).

Most countries, including developing countries, are committed to minimum standards of intellectual property rights protection under the WTO Agreement on Trade-Related aspects of Intellectual Property Rights (TRIPS). Many countries have not yet been able to implement all its provisions, however, and Least Developed Countries recently won an extension of their exemption from TRIPS rules until 2013.

Other international treaties exist that cover intellectual property, and many developing countries are signatory to them. The main treaties are those administered by the UN's World Intellectual Property Organisation.

With respect to IPRs, the Convention on Biological Diversity (CBD) states that the Contracting Parties shall "ensure that such rights are supportive of and do not run counter to its objectives". IPRs may help to fulfill the objective of the CBD of providing access to genetic resources and fair and equitable sharing of the benefits arising out of the utilisation of such genetic resources.

The additional risk that EU deals might pose is not simply where they go broader and deeper than the partner countries' existing international commitments. Commitments within trade deals are backed up by dispute settlement provisions, and therefore countries could risk sanctions that would not be available under WIPO treaties, for example, for non-compliance.

What the European Commission might want and what this means for development

The European Commission's (EC's) past practice on IP chapters in free trade deals with developing countries has been to **require accession by the other party to various multilateral treaties**. The parties generally reaffirm their commitment to implement the TRIPS Agreement and also to accede to many or all of the following

international agreements within a specific time period:

- Berne Convention for Protection of Literary and Artistic Works (copyright)
- Paris Convention for the Protection of Industrial Property
- Patent Co-operation Treaty (PCT) and Patent Law Treaty (PLT)
- UPOV Convention 1991 (Act of the International Union for the Protection of New Varieties of Plants)
- Vienna Agreement Establishing an International Classification of the Figurative Elements of Marks
- Locarno Agreement establishing an international classification of Industrial Designs
- Madrid Protocol for the international registration of trademarks
- WIPO Copyright Treaty (WCT) and WIPO Performances and Phonograms Treaty (WPPT) (together referred to as the WIPO Internet Treaties).

Many of these agreements are procedural and do not set substantive standards of protection. For example, the Patent Co-operation Treaty allows inventors to file only one international application to facilitate obtaining patents in other member countries. Similarly the Patent Law Treaty seeks to harmonise patent procedures and to restrict the number of requirements in filing patents. This could be problematic for developing countries, who have to raise objections to any application within a limited period to avoid its default acceptance, but who may lack the capacity to deal with high volumes of applications. If countries are newly acceding to the Patent Co-operation Treaty, for example, this could result in a greater number of patents being filed in that country, meaning that protected inventions will not fall into the public domain in that country for the term of the patent's protection (20 years from date of filing, in accordance with TRIPS).

That is not to say that none of these agreements are controversial with respect to their application to developing countries. For example the **WIPO Internet treaties** do contain substantive provisions that go beyond TRIPS commitments and grant new exclusive rights and technological protection measures (TPMs) for rights-holders to protect their works on the internet and in digital media. The implementation of legislation on TPMs has been criticised for stopping not only copyright infringers, but also legitimate activities impacting on scientific research, for example, and impeding competition.

UPOV (1991) has also come under criticism for expanding plant breeders' rights, expanding application to all seed types, extending the term of protection and limiting exceptions for farmers' rights. In contrast to the earlier version of UPOV from 1978, farmers are not automatically allowed to re-sow seed (unless expressly forbidden); instead in the 1991 act the onus is on countries to expressly allow farmers the privilege of re-sowing seed harvested from protected varieties. Extending protection to all seeds and extending the terms of protection encourages cultivation of a narrow range of crops, with possible consequences for nutrition and food security.

Previous EU FTAs have tended to use a **definition of the scope of intellectual property** that is broader than that used in TRIPS – including issues such as traditional knowledge, genetic resources and non-original databases. The first two of these tend to be areas of offensive interest for developing countries and therefore their inclusion is welcome, while the protection of databases has been criticised for protecting investments rather than creativity or original works.

FTAs have also included opening **general statements on the desired level of protection** that parties set out to achieve. These have varied from simply "adequate and effective" to "highest international standards" or, at their most stringent, approximation to Community standards. However, these statements seem to be of a declaratory nature.

At the end of 2006, the EC's strategy shifted to:

- seeking full TRIPS implementation (respecting transition periods)
- promoting enforcement
- co-operating with developing countries in implementation and enforcement
- ensuring IPRs are supportive of public health, innovation and technology transfer
- expanding protection of geographical indications.

Some protection for **Geographical Indications** (GIs) already exists. TRIPS affords protection to GIs to prevent use that misleads the public as to the geographical origin of a good or that constitutes an act of unfair competition. For wines and spirits, TRIPS bars anyone from using the protected terms, even if the public is not misled. The EU would like to see this protection extended to all GIs. It also wants to see a register of protected terms with strong effects (established at the WTO and a clawback of exclusivity on European terms that are now used in new world products, such as Rioja and Roquefort). In previous EU deals, for example, that with South Africa, the EU has also concluded stand-alone agreements on wines and spirits trade which afford mutual recognition of GIs and phase out use of terms of European origin. The EU claims a disproportionate number of GI terms. Impacts could be important for developing-country firms that produce a product designated by one of these terms (either for internal consumption or for export) or import such a good from a third market.

With regard to **enforcement** the EU has adopted a multiple strategy to tackle internal infringements of IPRs through new legislation on border measures and enforcement, practical enforcement initiatives targeted at third countries[1] and through proposals in multilateral fora. The EU has stated that its new international Enforcement Directive will be used as a source of inspiration to "revisit" the IPR chapters in FTAs. The Directive goes beyond TRIPS in several respects including:

- extending the presumption of authorship detailed in the Berne Convention (i.e. for authors), to right-holders of related rights (for example, performer, producers of phonograms), thus shifting the burden of proof from claimants to defendants (eventual infringer would bear the burden of proving that the claimant is not the owner of the related right).
- extra rights of information-gathering in infringement cases, which may disproportionately facilitate the right-holders' work to the detriment of small and medium enterprises.

All in all, such detailed provisions may affect the freedom of countries stated in TRIPS "to determine the appropriate method of implementing the provisions of this Agreement within their own legal system and practice" (TRIPS, Article 1.1) and also impose standards originally designed for EU countries.

A Council Regulation on customs actions against goods infringing IPRs, requires authorities to take measures against goods not only when they are imported (the TRIPS requirement) but also on export and in transit. It also covers all types of IP, whereas TRIPS only mandates for trademarks and copyright. Other EU legislation precludes the TRIPS flexibility for small amounts of infringing goods to be imported for non-commercial purposes by travellers or in small consignments. In recent drafts the EU has not included binding provisions on enforcement, although its stated intentions are clear, and these provisions are more frequently appearing in US FTAs.

Recent EU draft IP chapters recognise the importance of the Declaration and Decision on TRIPs and **Public Health** and require the parties to accept the amending protocol. This is a positive measure. However, requirements to sign up to the Patent Co-operation Treaty may indirectly have adverse impacts on public health by increasing the number of patents applicable in developing countries; also it contains a condition that limits the right of countries to select their exhaustion regime. This means that countries are limited in their ability to import cheaper

1 Nov 2004 Strategy to Enforce Intellectual Property Rights in Third Countries, http://trade.ec.europa.eu/doclib/docs/2004/november/tradoc_120025.pdf

generic versions of patented drugs from third markets. In recent drafts the EC has avoided provisions on **data exclusivity**. Rules that would prevent producers of drugs or agricultural chemicals being able to use undisclosed data in their licence applications and would hinder the availability of cheaper generic products have not been included. These more lenient provisions in EU FTAs might not apply to the larger developing countries and regions, where the EC might push for more far-reaching deals.

Latest EC drafts also contain far-reaching provisions on **industrial designs**. There is a requirement to sign up to the Hague Agreement concerning the International Registration of Industrial Designs which allows the application for registration of a design to have effect in other parties' jurisdictions. It also extends the term of protection for designs from the ten years required under TRIPS to 25 years. It also seeks short-term protection of unregistered designs for a period of three years.

Finally, the **most favoured nation (MFN)** principle in the TRIPS Agreement means that whenever countries give a higher level of protection to any country, they must immediately accord it to all other members of the WTO. This means that all TRIPS-plus provisions will apply not only to EU nationals, but to nationals of all WTO members. This also means that for countries that have already signed FTAs with the USA, which tends to push for far-reaching TRIPS-plus provisions, these may already apply to EU nationals.

In terms of offensive interests, developing country interests look as though they will be better served in future Economic Partnership Agreements. Draft texts contain provisions relating to protection of genetic resources and traditional knowledge, assistance with implementation costs, and positive action on technology transfer and research and development.

Useful information and where to find it

Information on TRIPS
www.wto.org/english/tratop_e/trips_e/trips_e.htm

World Intellectual Property Organisation (contains links and explanations for most international IPR agreements)
www.wipo.int

Intellectual property watch (provides news and analysis on IPR developments)
www.ip-watch.org

South Centre:
www.southcentre.org/publications/publist_issue_area_GovernanceAndIP_index.htm

UNCTAD/ICTSD portal on IPRs
www.iprsonline.org/unctadictsd/description.htm

NGO websites

Médecins sans Frontières (MSF) on access to medicines
www.accessmed.msf.org

Centre for International Environmental Law on IPR and sustainable development
www.ciel.org/Tae/Trade_IntProperty.html

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