

NEGOTIATING A DEVELOPMENT-FRIENDLY SERVICES CHAPTER UNDER THE EPAS

By

*Aniekan Iboro Ukpe**

1. INTRODUCTION

Regional trade agreements as a traditional tool of international trade are designed to create larger and more integrated markets through the reduction of tariff and non-tariff barriers to trade between members. While in the past, the focus had been on liberalization of trade in goods, the onset of the Doha Round of multilateral trade negotiations gave new impetus for the progressive liberalization of trade in services. However, the lull in the Doha negotiations has seen many countries resort to both bilateral and regional free trade agreements covering services. Thus we have recently witnessed an increase in North-North, North-South and South-South RTAs seeking deeper liberalization commitments in services. Trade in services is indeed gaining increasing importance as a tool for the growth and development. Its acknowledged contribution to income/foreign exchange generation, job creation and competitiveness underscores its potential role in transforming developing countries' economies. This assumes much significance in the context of the several intra-regional RTAs being negotiated in ACP regions and also the on-going EPA negotiations between the EU and its ACP counterparts, which both seek to negotiate specific commitments in services trade. This is notwithstanding the weak negotiating capacities of many ACP countries on services issues.¹

While admitting that liberalization and greater cooperation in trade in services can strengthen RTAs and ultimately result in enhanced market access for member countries, it is necessary to define an approach for the peculiar context of North-South RTAs, which will secure the benefits of trade preferences for developing countries and guarantee their integration into global trade.² Such approach requires the design and implementation of appropriate policies and regulatory frameworks which will help strengthen services competitiveness and supply capacities in developing countries.

Effectively setting out from Section 2, the paper adopts a pseudo-legal approach in first laying out a brief on both the multilateral and bilateral frameworks for the negotiation of trade in services. This is with intent to explore any flexibility that may be useful in designing pro-development services rules of origin. The paper in Section 3 will attempt to define criteria that would not just ensure pro-development rules of origin but one that would also reflect special and differential treatment for developing countries. Section 4 will examine the use of services rules of origin in RTAs as a veritable tool for securing trade benefits for developing countries in RTAs. It will go on to discuss the economic and bargaining implications of a restrictive services rule of origin vis-à-vis a liberal one. Section 5 will sum up the entire analysis and emphasize the paper position.

* LL.B (Calabar); LLM (Dundee), Partner, Koko, Iboro Ukpe & Co. (Trade Consultants), Port Harcourt Nigeria; Programmes Officer (Legal), National Association of Nigerian Traders (NANTS). Email: (ani_abasi@yahoo.com).

The SADC region is currently negotiating a draft EPA Protocol on services covering areas such as energy, telecommunications, transport etc.
See Preamble of WTO Agreement.

2. LEGAL FRAMEWORK FOR SERVICES

In defining any bilateral or free trade agreements covering trade in services, regard must be had to the legal commitments of the parties already assumed in a prior framework. Of particular relevance to African countries are the WTO framework and the Cotonou Agreement. It is instructive to note that while African countries and indeed, all ACP countries are not under any obligation to enter into an agreement on services trade with the EU, they are already agreed to the broader objective of extending under the EPAs, their over three-decade long trade relationship to encompass the liberalization of trade in services in accordance with the provisions of the WTO General Agreement on Trade in Services (GATS).³

2.1 Framework set by the WTO Agreement.

Article V of GATS lays out preconditions for members who wish to conclude economic integration agreements under the multilateral trading system. Otherwise known as the economic integration exception, it forms the basis of exemption from the non-discriminatory (MFN) principle in the GATS. Article V of GATS requires that any RTA covering trade in services must have substantial sectoral coverage (including sectors, volume of trade affected and modes of service delivery) and must provide for the absence or elimination of substantially all discriminations concerning national treatment, while also prohibiting new ones. Unlike the case in GATT Article XXIV provision on trade in goods, the GATS, expressly provides for flexibilities in favour of developing countries.⁴ This means that where developing countries are parties to any economic integration agreement covering services such as the EU seeks under the EPAs, flexibility in their favour could very well be reflected in the enjoyment of a wider scope of national treatment restrictions, or the privilege to open fewer sectors, a lower volume of trade or fewer modes of supply or even the use of transitional periods and exclusion of basic services from liberalization.⁵ Very critical to the attainment of the objective of South-South cooperation is that developing countries, in exploiting GATS guaranteed flexibilities are able to extend more favourable treatment to juridical persons owned or controlled by natural persons from their territories without having to extend such treatment to any developed country, whether under a bilateral or the multilateral framework. This means that Africa countries should ordinarily be legally entitled to give more favourable treatment to local West African services providers in the context of intra-regional liberalization of services trade without being obliged to extend such treatment to the EU under the EPAs.

2.2 The Cotonou Agreement

Article 41 of the Cotonou Agreement contains what can be described as a commitment of the parties to the objective of extending their partnership to encompass the liberalization of services. It however provides that such extension will only be necessary after all the parties have acquired some experience in applying the MFN treatment under the GATS, special regard being given to the participation of the ACP parties. In recognition of the need for

³ See Cotonou Agreement, Article 41.4.

⁴ See GATS, Article V.3.

⁵ See CARIFORUM EPA, Annexure on commitments.

special and differential treatment to ACP service suppliers, the EU is specifically committed to efforts at strengthening the services supply capacities of ACP countries with a view to enhancing their competitiveness. Clearly, the Cotonou Agreement which is the underlying basis for the ongoing EPA negotiations does acknowledge the need for special and differential treatment in favour of ACP countries' services suppliers. It specifically obligates the EU to exercise such special and differential treatment in a way and manner that will not only be consistent with the priorities of ACP countries but will also meet the peculiar needs of these countries.⁶

2.3 The Parties Approach to Services Negotiation

Although all the parties to the EPA negotiations are agreed as to the noble development objectives of the EPAs, fundamental differences still exist between the parties on how to integrate the development dimension into the EPA. For the EU, the EPA will foster development mainly through trade liberalization and the creation of the right policy framework building on the Lomé Conventions on establishment and services, which contained non-binding national treatment of national and foreign companies from the contracting parties.⁷ In the Lomé Conventions, the objective of covering services was given as 'the support of ACP States' efforts to increase their domestic capacity to provide services with a view to improving the working of their economies'.⁸ The tourism, transport and communications sectors were listed as being of priority to these States.⁹ African countries, in accordance with the views of other ACP States and regions, view the development dimension of the EPA process as one to be ensured mainly by the implementation of programmes to enhance competitiveness and to develop the capacity to overcome the many supply-side constraints (including discriminatory regulatory regimes in international services trade) which has militated over its smooth integration into the global services market.¹⁰

As far as the services negotiations in the EPAs are going, it appears that the EU is very much pushing a trade liberalization objective with less emphasis on developing the capacities of ACP countries to prepare them for such liberalization. The EU is for instance seeking for full national treatment for its highly more efficient service suppliers.¹¹ Invariably, this may mean that such highly more efficient EU service suppliers would have unrestricted access to the West African market on similar terms with fledgling African service suppliers of 'like' services. Besides from the obvious fact that the immediate and direct competition that will result, will be overwhelming for the African services suppliers, this EU demand is very

⁶ Cotonou Agreement, Article 41.3.

⁷ Trade Negotiations Insights, *Farmers' Organizations Conduct EPA Mid-Term Review: The Case of West Africa*, Vol. 5, No. 1, Jan-Feb 2007 available at http://www.ictsd.org/tni/tni_english/6-/%20Eng%20Print%202403.pdf.

⁸ See Title IX of the Lomé Conventions.

⁹ Ibid.

¹⁰ Alaba, O., *EU-ECOWAS EPA: Regional Integration, Trade Facilitation and Development in West Africa*, p24, available at <http://www.gtap.ageon.purdue.edu/resources/download/2599.pdf>.

¹¹ See South Centre (2007), *Why Inclusion of Services in the EPAs is Problematic: Legal and Development Implications*, p.4.

restrictive of space for African governments who may need to fashion policies specifically aimed at increasing the participation of local services suppliers in the services trade.

The EU also seeks full MFN liberalization in the context of the EPAs.¹² This will imply that Africa countries will have to extend to the services supplier from the EU any treatment which they share among themselves or with other ACP countries, once such treatment is shown to be better than that given to the EU. Interestingly, the institution of MFN provisions in the EPAs has much wider implications having regard to the Global Europe Strategy being pursued by the EU. It would see services suppliers ('free-riders') from other EU FTA also getting unrestricted market access to Africa. Putting into perspective the EU position on MFN provisions in the EPA, the South Centre describes the EU approach as seeking the 'removal of quantitative restrictions like quotas, limitations on the total value of transactions, economic needs tests, limitations on number of operations or the participation of foreign capital, or even restrictions on the types of establishments'.¹³ Effectively, the MFN provisions will obligate African countries to totally open up particular sectors thereby denying them of the GATS and Cotonou-guaranteed rights to special and differential treatment including flexibilities in deciding what sectors to open; to what extent to open any sector; or even in the use of transitional periods and exclusion of sensitive services from liberalization.

3. DEFINING AN APPROACH FOR SERVICES NEGOTIATION IN AFRICA

As variously mentioned above, there is no obligation on Africa countries to undertake specific commitments in services negotiations with the EU. However, having regard to its huge potential in driving the economies of developing countries by providing services export opportunities and attracting greater foreign investment, this paper now proceeds to define an approach aimed at securing a development-friendly EPA chapter on trade in services. This effort sets out on two basics; firstly, that in accordance with the several sub-regional Road Maps on the EPA negotiations, any services liberalization commitment should promote the broader objectives of deepening regional integration and enhancing regional supply capacities within Africa.¹⁴ Secondly, it should follow a progressive approach with transitional periods reflecting asymmetries in favour of African countries. In consistency with the spirit and intent of the Cotonou Agreement and WTO framework, the later would mean the EU granting to African countries and regions, a deeper and broader market access and national treatment in services sectors and modes than the Africa parties would grant in return¹⁵.

3.1 Deepening Regional Integration

Regional economic integration is an important tool to foster the integration of African countries into the global trading system. The different regional economic communities have indeed adopted this as their primary objective.¹⁶ Article 35(2) of the Cotonou Agreement

¹² Ibid at 5.

¹³ Ibid at 6.

¹⁴ For instance, see Road Map for Economic Partnership Agreement Negotiations between West Africa and the European Community, 4th August 2004, available at http://trade.ec.europa.eu/doclib/docs/2004/october/tradoc_118923.pdf

¹⁵ See supra notes 6 and 8.

¹⁶ See ECOWAS Treaty, Preamble, Articles 2 and 3.

stipulates that 'economic and trade cooperation shall build on regional integration initiatives of the ACP states, bearing in mind that regional integration is a key instrument for the integration of ACP countries into the world economy'. Focusing on the case in West Africa, the joint EPA Road-map provides that since the cardinal objective of the EPA is to support the integration process in West Africa on the basis of priorities determined by the region, the rhythm of West African trade liberalization in relation to the EC shall then be related to such integration and shall be pursued flexibly and asymmetrically.¹⁷ While noting the bold initiative of West Africa in fast-tracking regional integration through the ECOWAS Trade Liberalization Scheme, much is left to be desired particularly, in respect to intra-regional trade in services. For instance, the Scheme has facilitated the free movement of persons across borders but has fallen short of shaping policies on recognition and harmonization of qualifications and standards. Practically, this will witness a situation where a doctor from Cote d'Ivoire freely moves his residency to Nigeria but is not able to carry on his practice there because he is not accredited by the Nigerian Medical Association and neither does the latter recognize the accreditation by its counterpart in Cote d'Ivoire. This is asides from the complete absence of regulatory frameworks to define and regulate standards and practice of such cross services. This typifies the daunting challenge African countries face in their bid to ensure universal access to basic services including health, education, water etc.

The several intra-regional integration process in Africa as far as services trade is concerned is still in its infancy. It will be consistent with common sense that the processes be allowed some maturity so that African countries and regions can exploit the benefits of a wider market while defining regulations to balance out commercial interest and obligations central to services provision such as universal access.

3.2 Enhancing Regional Supply Capacities

Without doubt, the EPA can help African countries build regional supply capacities, infrastructural development and international competitiveness necessary for its integration into the global services trade. However, having regard to the fact that many services sectors are still in their infancy and may require 'time-framed' conscious government policies aimed at increasing their participation in both regional and intra-regional trade, the need arises for some flexibilities in the treatment of local services suppliers. This could be achieved by the granting to the African parties, exemptions to the national treatment requirement. This would aim at securing a legally-supportable opportunity for African governments to offer special incentives and privileges to only local services supplier and services. Otherwise, would see such efficient services providers from the EU like Vodacom, Air France, Barclays Bank etc, have unlimited access to the African market on similar terms with fledging African services providers of 'like' services. The ominous effect of the resulting unfair competition on local services sectors is one which African countries cannot afford to risk.

3.3 Sectoral Coverage

Liberalization of services could have very varied effects on the economies of African countries depending on, among other things, the nature of the sector that is liberalized.

¹⁷ Joint West Africa-EC Roadmap, para 7.

While on the one hand, liberalization could result in availability of cheaper and more efficient services and increased employment rate, it could on the other hand also result in loss of jobs and income. In ensuring that liberalization of the services sector under the EPAs result in a positive development effects, one thing African countries must concern themselves with is striking an appropriate balance in deciding which sectors to liberalize. Countries will have to distinguish between sectors of basic/sensitive supply character which impact directly on poverty reduction on the one hand and on the other hand, sectors where it has real or potential competitiveness and is in need of investment. The former category which includes sectors like water and health services would usually require a minimum quality standard and at affordable pricing to impact positively on poverty reduction. Whether the liberalization or regulation of such basic services would meet the overall development goal of the region calls for intensive impact studies to be conducted before any decision is taken. Even in the event that the liberalization of services of basic supply character is desirable, bounding their commitments under the EPA may mean that African countries would lose the very vital policy space needed in deciding how to buffet and consequently stream the supply system in tandem with its development objectives. A unilateral approach to liberalization of basic services may be the first step in finding a right sequencing for the liberalization of basic and sensitive supply sectors.

It should be underscored that in deciding on which sectors to open up to the EU, African countries reserve the right to do so in a manner that meets their development priorities. This for instance should be held to mean that they are entitled make use of quantitative restrictions like quotas, economic needs test, caps on participation of foreign capitals etc, in defining the extent to which any particular sector is opened.

3.4 Modal Coverage

In respect to modal coverage, African countries have to concentrate on modes of export interest to them, which would mean, modes in which they can extract maximally favourable commitments from the EU. As can be seen in the CARIFORUM EPAs, the parties have made commitments across all the four modes of supply, with the CARIFORUM States concentrating efforts on Modes 1, 2 and 3. Less emphasis has been place on the even more important Mode 4, firstly, because of the burdensome market access requirements the EU attaches to its commitments¹⁸ and secondly, because of the CARIFORUM's desire to maintain coherency between its EPA and WTO obligations. In concentrating on its export interest, the CARIFORUM got the EU to open up sectors in which the CARIFORUM States are competitive or highly seeking for investment to develop capacities. Indeed, the EU market access granted to CARIFORUM in the highly development-valued entertainment sector has been described as 'the most significant it has offered in a trade agreement to date'.¹⁹

¹⁸ See UNCTAD, *Trade in Services and Development Implications*, p.13, TD/B/COM.1/85, 2 February 2007.

¹⁹ Francis, A and Ullrich, *Analysis of Economic Partnership Agreements: Trade in Services – Case Study of the CARIFORUM-EU Agreement* in *How to Ensure Development Friendly Economic Partnership Agreements – lessons Across Regions*, p.69, (Qualmann, R., Editor), (Eschborn, Germany: GTZ 2009).

Notwithstanding the current strict requirements of the EU on Mode 4 market access but rather having regard to the much acclaimed importance of Mode 4 supply for the trade and development of ACP countries, African countries can seize the opportunity of the current negotiations to secure less restrictive limitations on market access commitments.²⁰ Firstly, the region can demand for a relaxation of the high academic and professional requirements that the EU attaches to its commitments under Mode 4. Secondly, African countries can seek a 'quota system' from the EU, with longer stay periods as opposed to the 3 – 6 months time limitations that is usually attached to the EU's commitments in respect of the temporary movement of natural persons (Mode 4). This latter point would mean that a particular number of persons (at any one time) from each Africa country is allow entry into the EU for a considerable period upon meeting a much relaxed minimum requirement, whether academic, professional or otherwise. This however calls for a concerted effort by Africa countries to situate an appropriate balance in their quest to guarantee high mobility for its huge labour force and the need to stem brain-drain among its best human capitals.

3.5 Liberalization Modalities

This paper takes it for granted that African countries are committed to following the GATS-patterned approach in the liberalization of their services sector under the EPA. Particularly, this would mean the adoption of the GATS-styled four-mode liberalization, along with its liberalization factors market access. An analysis of the EU's approach to services liberalization at the bilateral level, depicts a new 'hybrid system' adopted by the EU in such negotiations.²¹ This hybrid system seeks to define new sets of modes of supplies and also seeks to integrate establishment rights in the sense of market access obligations not only in services sectors but also other production sectors. It also requires regulation obligations for specific services sectors immediately such sectors are committed.²² Having regard to the fact that most ACP States are still grappling with services negotiating under the WTO, any system such as the EU's hybrid system, in which African negotiators would have to start learning its legal structure and new definitions would be overwhelming on any little experience they have gained under the GATS system.

From a development perspective, the novel definitions and legal structure from the hybrid system may stealthily get African countries to decide on many issues which ordinarily could have been left for the commitment schedules. This scenario is best appreciated having regard to the difficulties in understanding the process and offers of the hybrid system as a whole. The best bet in terms of capacities, is for African countries to stick to a strict GATS-patterned approach in the entire negotiation process.

Following the GATS approach would also mean African countries insisting on a strict use of the cautious positive list approach in the listing of specific commitments in respective countries' schedule rather than the negative list approach. The former has the advantage of ensuring that only sectors which are deliberately listed are liberalized while the latter approach operates to liberalized sectors that were simply not contemplated at the time of

²⁰ See UNCTAD, Trade in Services and Development Implications, p.12, TD/B/COM.1/85, 2 February 2007.

²¹ See Trumm, S., in GTZ study supra n 21 at 36.

²² Ibid.

negotiations.²³ The negative list approach is very restrictive of policy space for African countries that currently have no sufficient study or data on any service sector or sub-sector.

3.6 Asymmetrical Liberalization

Both the GATS and Cotonou frameworks acknowledge the reflection of asymmetries in services liberalization between developed and developing countries (the EU and the ACP States) as necessary for the integration of the latter into the international services market.²⁴ Asymmetry is a legal expression of Special and Differential Treatment to which African countries are entitled to under both frameworks. While it is instructive to note that SDT could be stretched as wide as is legally possible to maintain flexibilities (policy space) in line with each developing country's development priorities, asymmetries here would be contextualized by drawing examples from the CARIFORUM EPA. A first mention is made of the 'progressive liberalization' built into the CARIFORUM EPA where further negotiations on services and investment are to take place within five years of entry into force.²⁵ The request by some African countries and regions for a moratorium before specific negotiations commence, could very well find support in this example. Having regard to the much weaker capacities of African countries in the services trade as against their Caribbean counterparts (for many of them, services rather than goods has for long being their stock-in-trade), it would very much be consistent with 'greater GATS-guaranteed' flexibility if the EU allows African countries an initial moratorium to build the almost non-existence internal regulatory capacities in their services sectors; conduct needed studies on sectors and sub-sectors; stimulate some level of competitiveness in the local services market and ultimately prepare for progressive liberalization under the EPAs.

Another very instructive reflection of asymmetries in the CARIFORUM EPA is seen in the varying depth of liberalization commitments among the parties. While the countries of the EU are committed to liberalize 94% of their services sectors, the CARIFORUM countries on the basis of some development indicators, are split between those committed to liberalized 75% of their services sectors and others committed to liberalize 65% of their services sectors. A GTZ study in surmising this level of asymmetry said that 'given the strength of the CARIFORUM services sectors in contribution to GDP and the percentage of total exports, the relatively narrow asymmetry in liberalization within the CARIFORUM-EU EPA will likely result in opportunities for development among the CARIFORUM States'. The lessons for African countries is firstly that even among themselves, GATS flexibilities certainly permit different levels of liberalization commitments across countries having regard to their development status and priorities. Secondly, having regard to their much lower experience in services trade as against their Caribbean counterparts, African countries indeed have a basis to request for greater asymmetries in their levels of liberalization as against the EU.

4 HOW THE RULES OF ORIGIN AFFECT SERVICES TRADE

²³ The negative list approach entails that once a sector is not listed, it is open to liberalization.

²⁴ Supra notes 6 and 8.

²⁵ Title II, CAP 1, Article 3 of the CARIFORUM-EU EPA.

Rules of origin, as typified in the case of trade in goods, are a set of rules which determine the 'nationality' of a product traded in international commerce.²⁶ It is used by preference giving countries to ensure that the activity which takes place in the beneficiary country is actually an indication of the real economic input from that country. In an FTA, this would effectively mean that 'substantial transformation' of a good must have taken place in a member country before such goods can be exported to a partner country at the preferential tariff²⁷. It seeks to ensure that concessionary market access granted to a particular country is not exploited by another country. Without them, imports would seek entry through the country with the lowest tariff.

In the peculiar case of trade in services protectionist measures take the forms of non-tariff barriers, including regulatory restrictions and quantitative limitations rather than tariffs. Instead of seeking to define the nationality or origin of a service, rules of origin in services more closely, concern themselves with defining the origin of a service supplier²⁸. Illustratively, in an FTA between the EU and ECOWAS, the questions of services rules of origin would be; in what circumstances would a South African company which has its subsidiary in Nigeria benefit from trade preference in the EU-ECOWAS FTA in supplying services to the EU? If an American moves over to reside in the UK, in what circumstances would he benefit from the trade preferences arising out of the EU-ECOWAS FTA?²⁹ To a great extent, the restrictiveness or otherwise of services rules of origin circumscribe potential benefits that could accrue to parties in an FTA. This is implicit in the fact that such rules of origin will determine the degree of trade preferences entailed in market opening commitments that parties to an RTA undertake. A restrictive rule of origin will ensure that as much as possible, only service providers from members in an FTA area benefit from enhanced market opening under the FTA while a liberal rule of origin will allow service providers from non-members to benefit from such enhanced market opening. The foregoing raises a fundamental issue on the use of services rules of origin; in granting preferential treatment to services or services suppliers on the basis of origin, does such rules of origin merely serve a definition role or it can be used to legitimately pursue broader policy objectives of FTA members? This is a question with serious economic and bargaining implications for developing countries and one which they must give utmost consideration in designing a development-friendly services rule of origin.

4.1 Economic Considerations

Services rules of origin play a much important role in determining the extent to which RTAs discriminate among third countries, and implicitly, the extent of potentially costly trade and investment diversion. In a situation where members of a preferential trade agreement like an RTA are committed to different levels of liberalization, the effective preference granted to any member will invariably depend on the degree of restrictiveness of the rules of origin. Illustratively, if in the context of the EU-EAC economic partnership agreement, the EU fully

²⁶ See Lazaro, D. and Medalla M., *Evolving Rules of Origin: Best Practices For RTAs/FTAs* (PIDS Discussion Paper 2006), p. 1. available at <http://dirp4.pids.gov.ph/ris/dps/pidsdps0601.pdf>.

²⁷ See Art 3, Protocol 1 of the Cotonou Agreement Rules of Origin See also Annex II Article 3 of Council Regulation (EC) NO. 1528/2007.

²⁸ Fink, C & Nikomborirak, D., *Rules of Origin in Services: A Case Study of Five ASEAN Countries*, p.3.

²⁹ While the first question is relevant for service exports supplied through Modes 1, 2, and 3, the second is relevant for Mode 4.

liberalizes its services market while the EAC countries maintain some regulations in the sector, the adoption of a liberal rule of origin by the parties will operate to make the liberalization tantamount to MFN liberalization. The implication of this would be that services and service suppliers from all over the world will only have to establish themselves in the EU to benefit from the preferential market access under the EPAs.

A possible implication could be seen in the face of the Global Europe Strategy which could see services or services providers from other EU FTAS benefit from EPA preferential market access even without having to establish any presence in the EU. Any decision to adopt either a restrictive or liberal rules of origin, is one that is ordinarily fraught with competing and conflicting policy considerations. On the one hand, adopting a liberal rule of origin would apparently be economically significant for developing countries as it would tend to reduce the costs of trade and investment diversion. On the other hand, it would also appear that a liberal rule of origin has downbeat implications for the bargaining positions of countries as is typified in the case of MFN liberalization: it can reduce the incentive for negotiating a preferential trade agreement and it can also reduce the negotiating leverage of members in any such negotiations with third countries.

Countries' choices between a restrictive rule of origin and a liberal one will obviously be shaped along the lines of each countries' existing level of market liberalization in services trade. In a scenario like that thrown up in the EPAs, where the EU, which is already very advanced in services trade seeks specific commitments from African countries, who hitherto have an almost non-existent experience in services trade, it would be expected that the African countries would indeed prefer a restrictive rule of origin that will ensure that it utilizes almost exclusively the benefits of the EPA liberalization vis-à-vis third countries. In principle, a liberal rule of origin will allow services suppliers from third countries to benefit from enhanced market access negotiated under an RTA while a restrictive rule will only allow services suppliers from member countries' to RTAs to enjoy the enhanced market access under the RTAs. The many economic and bargaining implications associated with the choices would now be examined in some details.

4.1.1 Accessibility to Efficient Services Suppliers

The policy choice on adopting a restrictive or liberal rule of origin for services trade is usually of much significance as it will ultimately determine the accessibility of an RTA partner to the most efficient services suppliers. Adopting a liberal rule of origin in an RTA ensures uninhibited competitiveness from services suppliers from all over the world. This provides an opportunity for the most efficient services suppliers or services to move into the integration area notwithstanding their nationality, provided however that they establish themselves in at least one member of the RTA. Increased competition will mean that consumers can get the most efficient services at much reduced prices. Another advantage arising here would be that the more efficient services suppliers from 'outside the RTA' would be in a position to share knowledge and skills with services suppliers from the RTA partners thereby increasing the efficiency and competitiveness of such local services suppliers. Such MFN liberalization that results from the adoption of a liberal rule of origin also has the advantage of indeed preparing infant domestic services suppliers for competition at the global level by first 'protectively' having them compete within the RTA.

Of much significance to the proper choice of rules of origin for an RTA, would be the development status of the parties to the RTA as this can certainly impede or enhance access to the most efficient services suppliers. In most services sectors, the most efficient services suppliers will usually be firms from developed countries. Where an integration scheme just involves developing country partners, it would simply follow that the most efficient services suppliers are outside the integration area. Thus a restrictive rule of origin in a North-South RTA would effectively lock developing country partners in an exclusive relationship with some of the most efficient services suppliers in the world. On the other hand, a restrictive services rule of origin in a South-South RTA may see African countries locked up in a suboptimal pattern of production and consumption. However, the former will be the case under the EPAs where the EU seeks to conclude an FTA with separate African regions. A restrictive origin rule will ensure that African countries benefit maximally from preferences under the EPAs to the near total exclusion of services suppliers from third countries and also enjoy all the advantages from most efficient services suppliers from the EU.

4.1.2 *Trade Diversion*

Preferential liberalization of services that directly results from the use of a restrictive rule of origin will usually in turn lead to a long-term trade diversionary effect. This is illustrated by the fact that the huge location-specific sunk costs associated with many services sectors and incurred by a first mover would usually mean that the first mover can exercise some monopolistic dominance of such sectors even in the face of a potentially more efficient second mover from outside the RTA. High location-specific sunk cost has very serious welfare implications to the extent that a first mover can indeed restrict entry of subsequent suppliers and effectively, resulting in market concentration and a fall in consumer welfare. This problem of high location-specific sunk cost may invariably see a country stuck to an inefficient service provider (first mover) notwithstanding a subsequent MFN liberalization. Clearly, a restrictive services rules of origin is capable of creating a monopolistic market within an integration area but at the same time, a restrictive origin rule may be necessary to help developing countries' Firms prepare for competition at the global level by first exposing them to graduated competition under the confines of a regional market. As Bhagwati points out, this may just be a typical example of how RTAs can be building blocks for multilateral liberalization.³⁰ Although a liberal rule of origin would to a great extent liberalize the services market and allow the most efficient services suppliers/services freely move into the scheme at competitive rates, developing countries, particularly African ones in making a choice on rules of origin, must have to balance this fact against the backdrop of the fact that their services industries are still at cradle stage and may require some preferential government policies to stimulate growth and competitiveness.

4.1.3 *Exports, Investments and Labour*

The restrictiveness of services rules of origin also has a great impact on the flow of foreign direct investments and the labour market of a country. A restrictive rule of origin will seek to restrict the enjoyment of export incentives to strictly speaking only services suppliers who are nationals of the members to the RTA. This is in exclusion of all suppliers from the rest of the world without distinguishing those who would have established presence within

³⁰ Bhagwati, J., (1990), *Multilateralism at Risk: The GATT is Dead, Long Live the GATT*, The World Economy 13 (2): 149 – 69.

the integration area. This could be useful where the government in any particular country within the area seeks to preferentially direct all such incentives to home-grown industries as a means to stimulate their growth and competitiveness. The fact however remains that increased revenue could have accrued to government by the use of a less restrictive origin rule that extends export incentives to third country firms with established presence. A less restrictive origin rule besides from carrying with it associated export gains, may also go a long way to bring new foreign direct investments into the integration area. The import of this is much appreciated in a situation where the majority of countries in an FTA have very strict entry conditions for services suppliers outside the FTA, such new services suppliers and services could then move into the few countries with liberal entry conditions and there from access the regional market. Extending the entry conditions issue further, a strict rule of origin that is typified by strict entry and residency conditions applicable to non-nationals of FTA members, may have a down effect on the labour market within the FTA such as driving up wage demands, limiting otherwise available basic services and soaring up costs, general shortage in supply of human capital etc.

4.2 Bargaining Implications

To the extent that the restrictiveness of rules of origin impinge on the incentives to negotiate bilateral or regional FTAs, they are of serious bargaining implications. Due to the expanded number of WTO members and the resultant time-consuming complexities in trade negotiations at the multilateral level, countries have resorted to negotiating bilateral or regional trade agreements with a smaller number of countries for quicker results in particularly services liberalization. Implicitly, reciprocal bargaining at the multilateral level has become less productive.

Another reason why countries increasingly prefer to negotiate bilateral and regional trade agreements rather than pursue liberalization at the multilateral level is to stem the 'free-rider' problem synonymous with trade negotiations at the WTO level. By virtue of the MFN provision, any preferential market access negotiated among a sub-set of members must be extended immediately and unconditionally to all other WTO members.³¹ This throws up a situation where a WTO member, A, although interested in some improved market access from another member, B, refuses to engage in reciprocal bargaining once it knows that there are other WTO members interested in the same market access. It simply waits for any of the third interested WTO members to engage B in reciprocal bargaining and enjoys the market access on an MFN basis, thus reducing the value of specific negotiations. In stemming this trend, FTAs may use restrictive rules of origin to ensure that a non-FTA member does not benefit from the improved market access negotiated by the smaller number of FTA members. In contrast, a liberal rule of origin will allow non-FTA members to benefit from improved market access negotiated under the FTA by merely establishing firms in any of the FTA members. This certainly reduces the value of reciprocal bargaining under FTAs vis-à-vis negotiations at the WTO level.

³¹ See Article II of the GATT.

5 CONCLUSION

Negotiating a pro-development services chapter under the economic partnership agreements between the EU and the African parties will to a large extent depend on firstly, how much the parties exploit GATS-guaranteed flexibilities in favour of African countries and secondly, the restrictiveness of the rules of origin adopted between the parties. Flexibility can be reflected in the form of a progressive approach to liberalization with transitional periods reflecting asymmetries in favour of African countries. Besides from the fact that this would mean the EU granting to African countries and regions, a deeper and broader market access and national treatment in services sectors and modes than the Africa parties would grant in return, the use of transitional periods would allow African countries time to sequence their intra-regional services commitments, build regulatory capacities and then be in a position to exploit the benefits of a wider services market.

The choice of rules of origin will eventually determine how much African countries will benefit from improved market access in the context of the EPAs. The parties need to decide at the earliest stage to what extent non-FTA members should benefit from the preferences under the FTA as this will impact on the extent of benefits of FTA members and will overall, determine the extent of restrictiveness of the rules of origin to be adopted by the parties. While it may appear that a restrictive rule of origin may well restrict RTA benefits to members almost exclusively, this has to be balanced against the utility of a liberal rule of origin in preparing infant domestic services suppliers for competition at the global level by first 'protectively' having them compete within an RTA. The choice for EPA services rules of origin should be guided by the fact that the EU firms are already some of the most efficient firms in the world and as such the main concern for African countries would be how to ensure that non-EPA parties do not benefit from the preferences negotiated under the EPAs.