

## Legal Problems in Expanding the Scope of GATT to Include Trade in Services

Philip H. Gold

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## NOTES AND COMMENTS

### LEGAL PROBLEMS IN EXPANDING THE SCOPE OF GATT TO INCLUDE TRADE IN SERVICES

The General Agreement on Tariffs and Trade (GATT), a multilateral agreement for the limitation of trade barriers, does not apply to transnational trade in services.<sup>1</sup> Contracting states, therefore, are not prohibited from imposing barriers to trade in services. United States companies dealing in services have been encountering an increasing array of obstacles and restrictions in foreign countries<sup>2</sup> which have limited the ability of those companies to compete effectively abroad.<sup>3</sup>

Based on complaints of American companies operating abroad, the Office of the U.S. Trade Representative (USTR) has compiled a list of more than 2000 specific barriers<sup>4</sup> to international trade in services. These impediments to trade range from those that restrict access to foreign markets to those that discriminate against doing business in the foreign country once

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1. General Agreement on Tariffs and Trade, *opened for signature* Oct. 30, 1947, 61 Stat. A3, A7, T.I.A.S. No. 1700, 55 U.N.T.S. 187.

The GATT has been modified in several respects since 1947. The current version is contained in GENERAL AGREEMENT ON TARIFFS AND TRADE, IV BASIC INSTRUMENTS AND SELECTED DOCUMENTS (1969). The term GATT is also used to refer to the organization made up of the contracting parties to the General Agreement which provides a forum for coordination of international trade issues. The term General Agreement is used to refer specifically to the agreement itself.

2. Washington Post, Oct. 17, 1983, at G1, col. 3.

3. *Service Industries Commerce Development Act of 1982: Hearing on H.R. 5519 Before the Subcomm. on Commerce Transportation, and Tourism of the House Comm. on Energy and Commerce, 97th Cong., 2nd Sess., 97-156 (1982)* (statement of Giza Feketekuty, Assistant U.S. Trade Representative for Policy Development and Services) [hereinafter cited as G. Feketekuty].

4. The following sources of information may be obtained from the Office of the United States Trade Representative [hereinafter cited as the USTR]

a. U.S. Government Inventory of Selected Impediments to Trade in Services (a 228 page computer printout covering barriers to thirteen U.S. service industries). The printout provides information by country regarding the type of barrier and industry affected.

b. U.S. Draft Inventory of Selected Impediments to Trade in Telecommunications, Data Processing and Information Services (a 13 page computer printout which includes current and potential barriers to these service exports). The inventory lists barriers by country and contains information on the trade implementations as well as the possible motivations for these restrictive actions.

c. A Preliminary Survey of Entry Restrictions and Operational Constraints Imposed on Foreign Banks in a Particular Country (a 22 page computer printout containing information on type of restriction, practicing country, and implications of these restrictive actions).

market access has been obtained.<sup>5</sup>

Not all the barriers complained of are the result of unfair discriminatory practices. While many are deliberate protectionist practices designed to shield domestic services industries from foreign competition, others result from measures designed to achieve legitimate national social or economic policy objectives, but which may differ from United States regulatory practices.<sup>6</sup>

Because of the growing economic importance of the services sector, this trend toward proliferating barriers to international free trade in services has become a matter of deep concern to the U.S. government as well.<sup>7</sup>

The importance of the services sector to the U.S. domestic economy has increased dramatically as the economy has matured from being primarily agricultural and industrial to one that is based on high technology and is service-oriented.<sup>8</sup> It has become our nation's primary source of economic growth and employment. It is estimated that the services sector now accounts for the employment of 7 out of 10 working Americans and for about 65% of the U.S. gross national product (GNP).<sup>9</sup> Of the 20.5 million new jobs created in the U.S. during the last decade, 18 million are estimated to have been in services.<sup>10</sup>

The importance of international trade in services to the U.S. economy is indicated by the growing surpluses in the services account (invisibles) in

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5. *A Review of U.S. International Aviation Policy*, 97th Cong., 2nd Sess., 97-88 (1983) (statement of William E. Brock III, United States Trade Representative) [hereinafter cited as *W. E. Brock, International Aviation Policy*].

6. See G. Feketekuty, *supra* note 3.

7. See W. E. Brock, *International Aviation Policy*, *supra* note 5.

8. See INT'L TRADE ADMIN., U.S. DEPT. OF COMMERCE, CURRENT DEVELOPMENTS IN U.S. INTERNATIONAL SERVICE INDUSTRIES (1980) [hereinafter cited as CURRENT DEVELOPMENTS]. See generally Ginzberg and Vojta, *The Service Sector of the U.S. Economy*, 244(3) SCI. AM. 48 (March 1982); Reich, *The Next American Frontier*, ATLANTIC MONTHLY 43 (March 1983).

9. USTR, U.S. DOMESTIC STRATEGY FOR SERVICES TRADE (July 9, 1982) [hereinafter cited as DOMESTIC STRATEGY].

Generally included in the service industries which are significant in international trade are accounting, advertising, banking, communications, computer services, construction and engineering, consulting and management services, educational services, franchising, health services, motion pictures, shipping and air transport, and tourism (including the overseas development of hotels and motels). CURRENT DEVELOPMENTS, *supra* note 8, at 2.

The list is open-ended. Newer professional services that are becoming significant internationally include executive search services, public relations, and temporary help services. Trade Issues in Professional Services (1982) (unpublished work available from the USTR).

10. DOMESTIC STRATEGY, *supra* note 9, at 1. See also G. FEKETEKUTY, NEXT STEPS IN U.S. TRADE POLICY (1981) (available from USTR) [hereinafter cited as NEXT STEPS].

the U.S. balance of payments.<sup>11</sup> On occasion, the figures are cited to show that services surpluses not only have compensated for merchandise trade deficits in recent years, but also are responsible for producing the overall net surpluses in 1979 and 1980.<sup>12</sup> Since the bulk of the services account earnings comes from returns on direct investments, these surpluses may not be appropriately solely attributed to sales of service industries abroad.<sup>13</sup> On the other hand, actual exports of services may well be about 50% higher than balance of payments data may suggest because a number of services exports are not currently measured.<sup>14</sup> Ambiguities arising from differences in concepts of what is meant by services in the context of international trade may result in differing interpretations of the balance of payments accounting figures.<sup>15</sup>

Trade data show that over the past decade, the U.S. has become more dependent economically on the rest of the world and that the U.S. economy has become less dominant in the world economy.<sup>16</sup> The growing economic power and competitiveness of Japan and the EEC countries, the declining competitiveness of basic industries and the low rates of investment in capital goods and in research and development in the U.S., and the energy crisis which resulted in increased payments to the oil exporting countries are important factors responsible for these shifts.<sup>17</sup> The exchange rates problem — the increases in the value of the dollar relative to the currencies of our trading partners — is undoubtedly also partly responsible<sup>18</sup> because it increases the relative costs of U.S. exports.

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11. CURRENT DEVELOPMENTS, *supra* note 8, at 4.

12. See, e.g., Note, *Liberalization of International Trade in the Service Sector: Threshold Problems and a Proposed Framework Under the GATT*, 5 FORDHAM INT'L L.J. 371, 376 (1982).

13. See CURRENT DEVELOPMENTS, *supra* note 8, at 1.

14. NEXT STEPS, *supra* note 10, at 5.

The USTR recognizes that the statistics on trade in services are inadequate. The problem is now under review and study to find ways to improve data collection. See USTR, 1(5) INT'L SERVICES UPDATE 14 (Sept. 1982).

15. See G. J. CLONEY II, THE COMPOSITION AND ROLE OF TRADE IN SERVICES 7 (1981) (available from the Chamber of Commerce of the United States, Wash., D.C.).

16. USTR, TWENTY-FIFTH ANNUAL REPORT OF THE PRESIDENT OF THE UNITED STATES ON THE TRADE AGREEMENTS PROGRAM 1980-1981, 16 (1982) [hereinafter cited as TRADE AGREEMENTS REPORT]. See Reich, *supra* note 8.

17. See NEXT STEPS, *supra* note 10. See generally Ginzberg and Vojta, *supra* note 8; and Reich, *supra* note 8.

The recent price breaks in oil due to glutted markets may break the OPEC cartel and provide a beneficial stimulus to the world economy. It is doubtful, however, that it will significantly improve the relative competitive position of the United States with respect to other developed countries. See *Oil: The War Begins*, TIME 62 (March 7, 1983).

18. See TRADE AGREEMENTS REPORT, *supra* note 16.

The general phenomenon of the emergence of the services sector and its increasing importance to both the domestic and international trade economies is not limited to the U.S., but is seen in the economies of many other countries as well. In the twenty-four OECD countries, trade in services grew from \$67 billion in 1970 to \$140 billion in 1976.<sup>19</sup> Services now account for a fourth of total world trade and have been growing at about 17% over the past decade compared to about 6% for world trade as a whole.<sup>20</sup> Despite its growth in services exports, the U.S. share of world trade in services fell from about 25% to about 15% between 1969 and 1980.<sup>21</sup> For the world as a whole, the gross value of services trade rose from about \$80 billion in 1967 to nearly \$650 billion in 1980.<sup>22</sup> This phenomenon is not limited to developed countries; some developing countries are emerging as substantial exporters of services as well.<sup>23</sup>

The growing importance of international trade in services to the U.S. economy is further enhanced by close interrelationships to trade in goods.<sup>24</sup> For example, exports of computer software are frequently linked to exports of computer hardware. Telecommunication services and equipment and construction and engineering services and capital equipment are similarly interrelated.

When the services industries, in their campaign for relief from the burdens of the anticompetitive and restrictive barriers to free trade, brought their problems to the attention of the U.S. government, they found a receptive audience.<sup>25</sup>

In the view of the U.S. government, as expressed by Ambassador William E. Brock, the U.S. Trade Representative, "U.S. service industries represent the great hope for expansion of our foreign commerce."<sup>26</sup> The U.S.

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19. Krommenacker, *Trade-Related Services and GATT*, 13 J. WORLD TRADE 510 (1979).

20. G. Feketekuty, *supra* note 3, at 2.

21. DOMESTIC STRATEGY, *supra* note 9, at 2; G. Feketekuty, *supra* note 3, at 3.

22. G. Feketekuty, *supra* note 3, at 2.

23. See G. J. CLONEY II, *supra* note 15, at 3.

24. See G. Feketekuty, *supra* note 3, at 2.

25. Private sector executives have been actively working at lobbying and writing since the late 1960s. The major currently active private sector groups are the Services Policy Advisory Committee (SPAC), the International Services Industry Committee of the U.S. Chamber of Commerce, the Industrial Sector Advisory Committee on Services (ISAC 13), and the International Chamber of Commerce. The SPAC was established by the USTR in accordance with the Trade Agreements Act of 1979, 19 U.S.C. §§ 2501-2582 (Supp. V 1981), to provide overall policy guidelines on international trade in services. See USTR, 1 INT'L SERVICES NEWSLETTER, Issue 4 (Jan.-June 1981), and Issue 5 (Sept. 1982).

26. *Foreign Barriers to U.S. Trade: Part I, Service Exports, Before the Subcomm. on International Finance and Monetary Policy of the Senate Committee on Banking, Housing*

government is confident that the high degree of competitiveness of the U.S. services sector, particularly the high technology industries, will enable it to compete effectively for the vast potential for future expansion of the world market for services in a free trade environment.<sup>27</sup>

In their efforts to secure the elimination of the barriers to free trade, the services sector and the U.S. government are seeking the expansion of the scope of the GATT to include trade in services. The ultimate goal is a round of multilateral negotiations resulting in an international trade in services code.<sup>28</sup>

The services issue was one of the highest priorities of the U.S. at the GATT ministerial meeting held in Geneva in November 1982.<sup>29</sup> The outcome of the Geneva GATT ministerial conference was a setback for the services sector.<sup>30</sup> The expectations were modest: official recognition of the importance of trade in services and a commitment to consider the issues in order to lay the groundwork for possible future multilateral negotiations. The reality was harsh. The ministers, in their communique, merely recommended that interested nations continue their studies of the issues and exchange of information at the national level and tabled the issue.<sup>31</sup>

*and Urban Affairs*, 97th Cong., 1st Sess. 97-39 (1981) (statement of Honorable William E. Brock, United States Trade Representative) [hereinafter cited as W. E. Brock, *Foreign Barriers to U.S. Trade*].

27. See G. Feketekuty, *supra* note 3.

28. W. E. Brock, *International Aviation Policy*, *supra* note 5; see also TRADE AGREEMENTS REPORT, *supra* note 16, at 5.

29. See NEXT STEPS, *supra* note 10.

30. The GATT ministerial meeting was by most accounts a near disaster. Held during a period of worldwide deepening recession and increasing unemployment, and amidst calls to increasing economic nationalism and protectionism, the ministers were in sharp disagreement on most issues. See N.Y. Times, Nov. 28, 1982, at A1, col. 8; and N.Y. Times, Dec. 5, 1982, at F8, col. 3.

31. The communique dealt with services in three short paragraphs as follows:  
Services

The Contracting Parties Decide:

1. To recommend to each contracting party with an interest in services of different types to undertake, as far as it is able, national examination of the issues in this section.

2. To invite contracting parties to exchange information on such matters among themselves, *inter alia*, through international organizations such as GATT. The compilation and distribution of such information should be based on as uniform a format as possible.

3. To review the results of these examinations, along with the information and comments provided by relevant international organizations, at their 1984 session and to consider whether any multilateral action in these matters is appropriate and desirable.

USTR, COMMUNIQUE, GATT MINISTERIAL (Nov. 29, 1982) (obtained from USTR).

The outcome was also another rebuff for the U.S. The U.S. was the primary proponent of the plan for a GATT commitment on trade in services issues and had worked assiduously over the prior eighteen months to prepare its proposals and to enlist international support.<sup>32</sup> The U.S. proposals called for a "commitment to conduct future negotiations on trade in services and to undertake a work program expressly for the purpose of laying the groundwork for negotiations." Nevertheless, the "commitment to undertake a detailed work program on trade in services (without an expressed commitment to negotiations), supported by a political statement on the importance of trade in services and the need for trade ministers to facilitate the development of a systematic approach to services trade problems" would have been considered an acceptable minimum.<sup>33</sup> No commitment of any sort was obtained, nor was there any statement of importance or need.<sup>34</sup>

It is widely recognized that international trade in services is extraordinarily complex and problematic in that it presents many conflicts among the competing national policies and interests of various countries. It also poses conflicts between the international economic policy goal of trade liberalization and national domestic policy goals. These conflicts have given rise to many difficult political, economic, and legal issues. No quick and easy solutions are likely.

The primary focus of the remainder of this Comment is on certain fundamental legal issues which arise from consideration of broadening the scope of the GATT to include trade in services, and which need to be resolved before meaningful multilateral negotiations toward a services code can take place. The legal relationship between the GATT and the prospective services code, including the applicability of the GATT to trade in services and the legal status and effect of the envisioned services code within the GATT legal system, are examined in Part I. Next, in Part II, the identification and classification of discriminatory NTB's to make them amenable to code treatment are discussed. Finally, in Part III, the issues arising out of defining the scope of commercial activities to be encompassed by the

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32. At present there remains a lack of broad international consensus, but there seems to be growing agreement that liberalization is needed. Great Britain, Germany, and Sweden have been the most supportive. Switzerland, Netherlands, Norway, Finland, Canada, Japan, and Australia were also supportive to varying degrees. France and Italy and most of the less developed countries (LDCs), particularly India and Brazil, are generally opposed. See USTR, PREPARATIONS FOR GATT MINISTERIAL SERVICES 6 (1982) [hereinafter cited as PREPARATIONS]. See also Wall Street J., Oct. 5, 1981, at 1, col. 1 (setting forth the views of various nations).

33. USTR, PREPARATIONS, *supra* note 32, at 1.

34. See *supra* note 31.

services code, particularly establishment trade, are considered.

#### I. LEGAL RELATIONSHIP BETWEEN THE GATT AND PROSPECTIVE SERVICES CODE.

One of the major trade policy objectives of the U.S. government is a future round of multilateral negotiations resulting in a services code within the GATT.<sup>35</sup> The contemplated code would establish general principles of law and standards of conduct to govern international trade for all services industries. It would also establish mechanisms and procedures for consultations and resolution of disputes and for future discussions of service issues. Such a code would reduce barriers impeding access to markets abroad and set effective rules and procedures for dealing with trade in services issues. It would move international trade in services issues from the political arena toward a legal arena.<sup>36</sup>

The GATT provides the most appropriate international forum for several reasons. These are its existing mandate to reduce barriers to trade and to eliminate discriminatory treatment in international commerce, its broad membership, its capacity for negotiating binding agreements, and its framework for consultation, investigation, and dispute settlement.<sup>37</sup>

Before serious consideration of the specific application of GATT principles and legal obligations to specific trade in services issues can take place, however, certain complex and difficult preliminary legal issues must be resolved and the specific trade in services issues must be clearly defined.

##### A. *Applicability of the General Agreement to a Trade in Services Code*

In the existing GATT legal structure,<sup>38</sup> the General Agreement comprises the basic trade policy commitments of the contracting parties. The central obligation of the parties is to limit tariffs on particular goods to a specified maximum. The detailed commitments by each country to limit tariffs on particular items are contained in its own individual tariff schedule. The obligations relating to the tariff schedules are contained in Article

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35. See *supra* note 28.

36. See Jackson, *The Birth of the GATT-MTN System: A Constitutional Appraisal*, 12 LAW & POL'Y IN INT'L BUS. 21 (1980) for rationale and discussion of power-oriented versus rule-oriented trade dispute settlement techniques.

37. See TRADE AGREEMENTS REPORT, *supra* note 16, at 33. See also Krommenacker, *supra* note 19; and Note, *supra* note 12, at 392.

38. See J. JACKSON, LEGAL PROBLEMS OF INTERNATIONAL ECONOMIC RELATIONS 474 (1969) [hereinafter cited as LEGAL PROBLEMS]. See generally Jackson, *supra* note 36; and J. JACKSON, WORLD TRADE AND THE LAW OF GATT (1969) [hereinafter cited as WORLD TRADE].



II of the General Agreement. This makes the tariff schedules an integral part of the GATT and its treaty commitments. Further details of obligations on certain subjects are contained in special "side agreements" which apply only to the parties to these side agreements.

By reference to the existing GATT structure relating to the arrangement of the obligations with respect to goods, a legal structure encompassing trade in services within the context of GATT can be derived. The fundamental principles and legal concepts ought to be severable from the specific treaty commitments of the General Agreement in which they are embodied. The fundamental principles upon which the GATT is based — reciprocity,<sup>39</sup> mutual advantage,<sup>40</sup> and nondiscrimination<sup>41</sup> — should be as applicable to trade in services as they are to trade in goods. The basic legal concepts of GATT in which they are embodied are: most-favored-nation obligations (MFN),<sup>42</sup> national treatment,<sup>43</sup> and transparency.<sup>44</sup> These basic

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39. Reciprocity is used here in the broad sense to mean the exchange of concessions perceived to be of equivalent value or of the existence of equivalent competitive opportunities rather than in the literal sense of strict equal treatment. *See* G. FEKETEKUTY, *INTERNATIONAL TRADE IN BANKING SERVICES: THE NEGOTIATING AGENDA* at Chapter Six (available from the USTR). *See generally* LEGAL PROBLEMS, *supra* note 38.

40. These principles are found in the preamble to the General Agreement which declares the means to achieve the economic objectives of the GATT to be "by entering into reciprocal and mutually advantageous arrangements." GATT, *supra* note 1.

The principles of reciprocity and mutual advantage also imply the rejection of the mercantilist philosophy that there had to be winners and losers in commercial transactions. The expectation is that, under the GATT, there should only be winners. *See* Jackson, *supra* note 36.

41. MFN and national treatment are the two primary rules of nondiscrimination. *See infra* notes 42 and 43.

Because of the many exceptions and loopholes, true nondiscrimination is an elusive and often illusory goal. *See generally* Jackson, *supra* note 36.

42. The MFN obligations prohibit discrimination as between goods from different importing countries. Article I contains the major MFN clause of the GATT. This unconditional MFN obligation is the cornerstone of the GATT. Under this clause, each member of GATT is obligated to treat other GATT members at least as well as it treats that country which receives its most favorable treatment with regard to imports or exports. Similar nondiscrimination language pertaining to specific subjects is also contained in other articles. *See, e.g.,* WORLD TRADE, *supra* note 38, at 255. *See generally* LEGAL PROBLEMS, *supra* note 38, Chap. 9.

43. The national treatment obligation prohibits discrimination between goods which are domestically produced and goods which are imported. As contained in Article III of the GATT, it specifies that imports shall be treated no worse than domestically produced goods under internal taxation or regulation measures. *See generally* LEGAL PROBLEMS, *supra* note 38, Chap. 10.

44. Transparency is akin to the notion of procedural due process. It refers to identifiable, visible, and regularly administrated procedures in government administrative regulations and practices. *See generally* Note, *United States-Japan Trade Developments Under the MTN*

legal concepts similarly should be applicable to both types of trade. Additionally, the flexibility and protection of national interests provided by exceptions<sup>45</sup> and by the escape clause<sup>46</sup> would serve the same functions and perhaps be even more important to trade in services than trade in goods.

The "existing legislation" clause of paragraph 1(b) of the Protocol of Provisional Application (PPA)<sup>47</sup> has proved troublesome in the past<sup>48</sup> and might become even more so when applied in the context of services. However, without "grandfather rights," it is unlikely that a multilateral trade in services agreement could ever be concluded.

Many of the deficiencies which exist in the present GATT system would be imported into any trade in services agreement negotiated under GATT.<sup>49</sup> The goal of bringing trade in services within a legal system ought

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*Agreement on Government Procurement*, 5 FORDHAM INT'L L.J. 139 (1981-82); LEGAL PROBLEMS, *supra* note 38.

45. The most important exception in the GATT is the Article XXV waiver authority. Others include the use of quotas in a balance of payments crisis (Art. XII-XIV), deviation from the MFN obligation for customs unions and free trade areas (Art. XXIV), and general exceptions for national health and safety measures (Art. XX) and national security (Art. XXI). See WORLD TRADE, *supra* note 38.

An important use of the Article XXV waiver can be seen in the Generalized System of Preferences (GSP) programs. Such GSP programs which allow developed countries to extend duty-free treatment to certain imports from less developed countries (LDCs) and which would otherwise have been in conflict with the unconditional MFN obligation, were authorized by a waiver adopted by the contracting parties on June 25, 1971. See Berger, *Preferential Trade Treatment for Less Developed Countries: Implications of the Tokyo Round*, 20 HARV. INT'L L.J. 540 (1979).

46. The escape clause, contained in Article XIX of the GATT, was included at the insistence of the United States. It provides for the use of temporary restraints on imports in cases where imports are causing serious injury to domestic industry. Extensive use of exceptions and the escape clause have eroded the unconditional Article I MFN obligation. See LEGAL PROBLEMS, *supra* note 38, Chap. 11. See generally WORLD TRADE, *supra* note 38.

47. Protocol of Provisional Application to the General Agreement on Tariffs and Trade, Oct. 30, 1947, 61 Stat. 5, 6, T.I.A.S. No. 1700, 55 U.N.T.S. 308.

The GATT has never itself been applied. It is only through the PPA, signed in late 1946 by the 22 original members, that the GATT is applied. Originally it was thought that, after the ITO Charter came into force, the GATT would be applied definitively. See LEGAL PROBLEMS, *supra* note 38, § 7.1.

48. The PPA applies Part II of the GATT "to the fullest extent not inconsistent with existing legislation." Problems were generated by disputed interpretations of the terms "inconsistent" and "existing." See LEGAL PROBLEMS, *supra* note 38, § 7.2; WORLD TRADE, *supra* note 38. See also Jackson, *The GATT in United States Domestic Law*, 66 MICH. L. REV. 249 (1967).

49. Although the GATT system has been enormously successful overall in reducing tariff barriers and promoting a large increase in international trade, many weaknesses have appeared in the GATT system. Some of these weaknesses are substantive in that they involve rules that have proven substantively inadequate or the lack of rules to deal with important problems. The

to be clearly distinguished from the goal of reforming the GATT. If the goal is to bring international trade in services within the scope of a legal system, then the GATT umbrella, with all its defects, offers the only realistic possibility. The alternative of negotiating an independent multilateral trade agreement, with its own organizational supporting structure for administration and dispute resolution wholly outside the GATT, is unrealistic. Aside from being unnecessarily cumbersome and duplicative, essentially the same countries who are parties to the GATT would be the prospective parties to any contemplated independent arrangement and their own individual national problems, and concerns, policies, and predispositions would follow them. Furthermore, an independent arrangement could only serve to further undermine the existing GATT.

The alternative to agreements achieved by bilateral negotiations is an interim solution that the U.S. government is actively pursuing.<sup>50</sup> The necessity of negotiating each agreement separately, however, is arguably inefficient. It also has the associated risk that third parties might still claim the benefits of any negotiated concessions through the unconditional GATT Article I MFN obligation<sup>51</sup> or through the MFN obligation under a bilateral Friendship, Commerce, and Navigation (FCN) treaty,<sup>52</sup> even though the concessions might relate to services rather than goods. In defending against this risk, the U.S. might be placed in the uncomfortable position of differentiating between two types of trade it ultimately wishes to treat uniformly.

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major substantive problems include erosion of the MFN principle, inability to deal adequately with NTBs, trade in agricultural goods, problems of developing countries, safeguards, and constitutional weaknesses that make amendment or development of new rules difficult, if not impossible. In addition, the dispute settlement procedures have not been working well. The effect of these inadequacies has been to make noncompliance with legal obligations a more viable policy option for governments. See Jackson, *supra* note 36. See also LEGAL PROBLEMS, *supra* note 38, Chap. 7.

50. When services are covered by bilateral FCN treaties or bilateral agreements covering certain service sectors, e.g., aviation, the U.S. seeks full enforcement of the provisions. Where no provisions exist, consultations are held in the context of the overall bilateral commercial relationship with the country concerned. See TRADE AGREEMENTS REPORT, *supra* note 6; NEXT STEPS, *supra* note 10.

51. The unconditional MFN clause provides that any treatment by a GATT member to any other country, including countries which are not GATT members, must be granted to all GATT members. LEGAL PROBLEMS, *supra* note 38, at 532. See *infra* notes 66-70 and accompanying text.

52. The U.S. has in force 52 bilateral FCN treaties, treaties of Amity and Commerce, and similar executive agreements. Of these, 43 contain an unconditional MFN clause. Hufbauer, Erb & Starr, *The GATT Codes and the Unconditional Most-Favored-Nation Principle*, 12 LAW & POL'Y IN INT'L BUS. 59 (1980). See E. ARAKAKI, TREATIES OF FRIENDSHIP, COMMERCE AND NAVIGATION AND THEIR TREATMENT OF SERVICE INDUSTRIES (Feb. 2, 1981) (available from the Int'l Trade Admin., U.S. Dept. of Commerce).

The extension of existing Multilateral Trade Negotiations (MTN) codes to include services is another alternative under consideration by the USTR.<sup>53</sup> Although this alternative may appear to be attractive, because it should be easier simply to extend a code to include services than to negotiate an entire new code, it raises many problems. Since the MTN codes are not part of the GATT treaty obligation and are binding only on the limited number of parties that have accepted them,<sup>54</sup> questions as to the binding effects of the amended treaties are raised. The result might be a substantial number of slightly different treaties, each binding different parties, and general confusion as to the multiple obligations and which countries were bound by them.

The most significant obstacle to extending GATT to services is that the language of GATT refers throughout to "goods" and to specific concepts which relate to goods. A strict construction would therefore imply both the intent to exclude and the actual exclusion of services from the scope of application of these provisions.<sup>55</sup> For example, the extensive use of the word "product" and the conceptions of tariffs, antidumping, countervailing duties, and valuation of customs restrictions, which are expressed in the terms of trade in goods, are not only not directly applicable to trade in services, but, in fact, inconsistent with such an application. On the other hand, however, nothing in the language of the General Agreement expressly excludes services. The concern for trade in services in GATT is not new. There was a recognition from the outset that trade in goods and trade in services are often interrelated. For example, it was recognized that a trade in goods could not take place without services, such as transport insurance, and that, therefore, discriminatory practices affecting these services could affect trade in goods.<sup>56</sup>

The Government Procurement Code negotiated at the MTN includes services to a limited extent. It applies to "any law, regulation, procedure and practice regarding the procurement of products by the entities subject

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53. The extension of the codes regulating government procurement, standards, subsidies, customs valuation, and customs practices are considered likely candidates. *NEXT STEPS*, *supra* note 10, at 15.

54. See *infra* notes 60-70 and accompanying text. Amendments to the codes will similarly be binding only on parties that accept them. See Jackson, *supra* note 36.

55. The preparatory work for the ITO and the GATT also suggest the intent to exclude services from the scope of coverage. See *WORLD TRADE*, *supra* note 38, at 528.

56. See Krommenacker, *supra* note 19; and Note, *supra* note 12.

Recently, interest in exploring services issues and the possibility of extending existing GATT commitments to trade in services issues has been shown by the GATT Secretariat and Consultative Group of 18 (CG-18). See USTR, 1 *INT'L SERVICES NEWSLETTER*, Issue 4 (Jan.-June 1981), at 3.

to this Agreement." This includes services incidental to the supply of products if the value of these incidental services does not exceed that of the products themselves, but not service contracts *per se*.<sup>57</sup> The exclusion of service contracts *per se* ought not to be interpreted as expressing hostility to including trade in services within the scope of GATT, but rather, as an indication of uncertainty as to the application of the express provisions of the General Agreement. The Government Procurement Code further provided that "the Committee *shall*, at an early stage explore the possibilities of expanding the coverage of this Agreement to include service contracts."<sup>58</sup>

It is fair to conclude from this that, while the General Agreement may not have been intended to apply to trade in services and may be construed to exclude, by its terms, trade in services, nevertheless, it does not necessarily prohibit the inclusion of trade in services within its scope.

In fact, it may be advantageous that the specific provisions of the General Agreement do not apply to trade in services. The key is to expressly adopt this construction of the terms of the General Agreement. The specific detailed provisions and the obligations they entail may then be severed from the general principles of the basic GATT obligation. These general principles could be embodied in a new trade in services code with its detailed provisions drafted to meet the specific problems common to services industries. Additional supplementary codes could be negotiated to deal with specific problems of particular industries that are not commonly shared by others.

However, the danger in adopting this position is that the argument can be turned against its proponent. A GATT member that was opposed to promulgation of a trade in services code could argue that this construction of the language — "to any product" — implied that the entire GATT system, and not merely the General Agreement, was not intended to apply to services. The opposed member could further argue that, because the GATT was not intended to apply to services, it would be improper or illegal to pursue multilateral negotiations on a trade in services code under GATT auspices and that, before such negotiations could properly be conducted under the auspices of GATT, the General Agreement would have to be amended. This would require acceptance<sup>59</sup> by two-thirds of the GATT members and would therefore be unlikely to be achieved.

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57. GENERAL AGREEMENT ON TARIFFS AND TRADE, BASIC INSTRUMENTS AND SELECTED DOCUMENTS, 26th Supp., Sales No. 1980-3 (1980) Art. I, para. I(a) [hereinafter cited as BISD]. See Note, *supra* note 44. See also Recent Development, *International Trade: GATT Tokyo Round*, 20 HARV. INT'L L.J. 695 (1979).

58. BISD, 26th Supp., *supra* note 57, Art. IX, para. 6(b) [emphasis added].

59. GATT, *supra* note 1, Art. XXX. See *infra* notes 61-66 and accompanying text.

### B. *Legal Effect of a Services Code Under the GATT*

The envisioned code or set of codes for trade in services would be similar in character and legal effect to the codes negotiated at the Tokyo Round of Multilateral Trade Negotiations (MTN).<sup>60</sup> The services code is contemplated as being a statement of general standards of conduct for international trade in services, to be distinguished from the detailed undertakings of a trade agreement. This code would be legally binding only on parties who consent to be legally bound and sign the agreement.<sup>61</sup> As such, the services codes, like the MTN codes, would have the legal character and effect of an independent treaty.<sup>62</sup> With respect to the General Agreement itself, the services code would have the legal character of draft provisions.<sup>63</sup> These provisions would be without binding effect on nations other than parties until incorporated in the GATT, and then only "in respect of those contracting parties which accept them."<sup>64</sup> Under the GATT system, members have reserved the right to accept or reject new legal obligations individually. Amendment requires acceptance by two-thirds of the GATT members.<sup>65</sup>

The actual legal effect of a code, then, depends on whether it acquires the acceptances of two-thirds of the GATT members required to become an amendment, because the MFN clause extends negotiated benefits to all GATT members on a multilateral basis.<sup>66</sup> This enables all GATT members to receive the benefits of concessions granted by any member in bilateral negotiations. The effect of this would be, for example, that GATT members who refused to sign the treaty might receive the benefits of the new codes negotiated at the MTN without becoming obligated under them.<sup>67</sup> To avoid sharing the benefits, the final signatories of the MTN treaty adopted the position that the benefits and obligations of each code will apply only to code signatories and will not be extended to other GATT members through

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60. See generally Comment, *GATT and The Tokyo Round: Legal Implications of the New Trade Agreement*, 11 CAL. WEST. INT'L L.J. 302 (1981); Jackson, *supra* note 36; and Recent Development, *supra* note 57.

61. See Jackson, *supra* note 36.

62. See *id.*, at 39.

63. Comment, *supra* note 60, at 317. See generally WORLD TRADE, *supra* note 38, on amending the GATT.

64. GATT, *supra* note 1, Art. XXX.

65. *Id.* Amendments to Part I or Articles XXIV and XXX require acceptance by all the contracting parties.

66. See *supra* note 51.

67. See Comment, *GATT and The Tokyo Round*, *supra* note 60, at 302; Graham, *Reforming the International Trading System: The Tokyo Round Trade Negotiations in the Final Stage*, 12 CORNELL INT'L L.J. 1 (1979).

the MFN clause.<sup>68</sup> In other words, they intend the MTN most-favored-nation obligation to be conditional, to be distinguished from the unconditional MFN obligation of Article I of the General Agreement.<sup>69</sup> This position appears to be in clear conflict with a strict construction of the Article I unconditional MFN clause.

This conflict between conditional and unconditional GATT MFN obligations might be avoided in the case of a trade in services code by the express adoption of the construction that the Article I MFN clause applies only to goods, and not to services, because of the language "to any product."<sup>70</sup>

This proposal, then, envisions a services code with substantive provisions stating general standards of conduct and embodying the legal concepts underlying the General Agreement but severed from its specific obligations. The code would have the legal status both of an independent treaty and, with respect to the General Agreement, of a draft provision. Like the MTN codes, the trade in services code could adopt the conditional MFN obligation. The parties to the code would then be bound by its obligations and would receive its benefits. This would, of course, not resolve the existing conflict and impending confrontation between the conditional and unconditional MFN obligations, but neither should it unnecessarily exacerbate the situation.

## II. IDENTIFICATION AND CLASSIFICATION OF NONTARIFF BARRIERS TO TRADE IN SERVICES

Discriminatory regulatory and administrative practices of foreign governments constitute a major source of the many serious problems that U.S. service industries are encountering abroad in international business activities. These governmental practices act as barriers — obstacles to con-

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68. See Hufbauer, Erb & Starr, *supra* note 52.

The benefits of the six codes relating to nontariff barriers are extended fully only to code signatories. While every GATT member is eligible to sign each Code, it is only upon acceptance that the member is assured of the full range of benefits. *Id.* at 61.

69. See *id.* for a rationale for reconciling prior U.S. unconditional MFN commitments with the conditional MFN application of the MTN codes. See generally LEGAL PROBLEMS, *supra* note 38, Chap. 9, for a discussion of conditional and unconditional MFN obligations.

70. See *supra* notes 55-59 and accompanying text.

Since the FCN treaties are generally applicable to services, the potential conflicts between the conditional MFN obligations and the unconditional MFN obligations of these FCN treaties remain unresolved. See E. ARAKAKI, *supra* note 52. Under the Trade Agreements Act of 1979, only a few of the 43 nations whose bilateral agreements with the U.S. contain unconditional MFN clauses are likely to receive the benefits of a services code without the reciprocal assumption of substantially equivalent benefits. See Hufbauer, Erb & Starr, *supra* note 52.

ducting business — and, as such, are analogous to nontariff barriers (NTBs) affecting trade in goods.<sup>71</sup>

These discriminatory regulations and practices are often difficult to identify. They are widespread, numerous, and diverse in character. They often stem from obscure or arbitrary administrative practices. In other words, many of these discriminatory regulations and practices lack transparency.<sup>72</sup> The primary source of information regarding these NTBs is the private services sector. Based on reports by private sector groups, the USTR compiles, periodically updates, and publishes inventories of selected barriers to trade in services.<sup>73</sup> The information is undoubtedly incomplete. Many barriers have yet to be identified and new ones are continually being erected.

From the entrepreneur's point of view, the specific barrier is the problem. It is the obstacle to be overcome. From the point of view of being suitable for drafting a code, however, a large collection of specific barriers of diverse character is unmanageable; they must be classified somehow.

If problems common to services industries in general can be identified, classification of barriers according to these functional characteristics would allow drafting a code applicable to trade in services generally, as distinguished from an industry by industry approach.<sup>74</sup> Although supplementary codes dealing with specific problems unique to certain industries may still be necessary, the general approach is preferable by far. It will provide unity and coherence by treating international trade in services as an entity and will avoid the fragmentation, duplication of effort, and inevitable conflicts inherent in an industry by industry approach.

The barriers may be grouped in several ways corresponding to a variety of categories of common characteristics. One suggested list of barriers, categorized according to types of government restriction or practices encountered by service industries generally, is the following:<sup>75</sup>

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71. See *supra* notes 2-6 and accompanying text. See generally Marks and Malmgren, *Negotiating Nontariff Distortions to Trade*, 7 *LAW AND POL'Y IN INT'L BUS.* 327 (1975); R. BALDWIN, *NONTARIFF DISTORTIONS OF INTERNATIONAL TRADE* (1970).

72. See *supra* note 44.

73. See *supra* note 4.

74. See G. J. CLONEY II *supra* note 15, at 16; Note, *supra* note 12, at 402.

The general European argument has been that the focus should be on a narrow examination of individual service sectors since the problems in each area are unique. The United States favors a comprehensive examination of the types of trade issues encountered by services industries. PREPARATIONS, *supra* note 32, at 7.

75. CONGRESSIONAL RESEARCH SERVICE U.S. INT'L SERVICE TRADE 9 (Aug. 1980); quoted in Note, *supra* note 12, at 384.



1. Restrictions on remittance and repatriation of profits, fees, and royalties;
2. Restrictions that mandate full or partial local ownership or service firms or that exclude foreign firms from access to the local market;
3. Restrictions on personnel, including visas, work permits, professional licensing, and the employment of local labor;
4. Discriminatory taxes placed exclusively or inequitably on foreign business income, profits, or royalties;
5. Inadequate protection of intellectual property, trademarks, copyrights, and technology;
6. Government subsidies that favor the competitive position of locally owned firms in the home market or in third-country markets;
7. Government-owned or government-controlled enterprises in the service industries;
8. Discriminatory licensing regulations, fees, and taxes;
9. Excessive duties on or outright prohibition of unnecessary imports;
10. Absence of international standards and procedures for services; and
11. Discriminatory restrictions on government procurement.

Although the list is somewhat redundant and the industry bias is obvious from the manner of expression, the nature of the barriers and problems, as perceived by the services industries, is made clear. In their view, a trade in services code should address the problems and dismantle the barriers. While it may not be possible to dismantle the barriers, this list does articulate issues that could be addressed by a code prescribing general standards of conduct.

Another classification of barriers that may be more useful is that articulated by Cloney.<sup>76</sup> While it is similarly based on major functional activities essential to the operations of the services industries, it is stated in neutral and more general terms. Cloney has identified the following categories of discriminatory practices:

1. Practices which have the effect of denying access to markets;
2. Practices relating to transactional and financial considerations which have or can be administered to have restrictive effect upon trade in services;
3. Practices which restrict or impede access to inputs needed by a foreign service firm or its establishment to provide a service;
4. Practices which limit or restrict the foreign enterprise's ability to market and sell its service; and

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76. See G. J. CLONEY II, *supra* note 15, at 39-42.

5. Governmental regulatory practices which can have a discriminatory or trade-chilling effect upon foreign service companies.

The classification of barriers focuses on the discriminatory effect of the barrier on the industry and could provide a basis for the organization of a general trade in services code. Appropriate standards of conduct would govern each category and would apply to any specific barrier in it. If the barrier constitutes a regulation or practice which violates the standard, the offending country would be obligated under the code to take corrective action unless the regulation or practice is otherwise permitted under an exception.

These classifications ignore whether the motive, intent, or purpose served by the barrier is permissible or proper. A given barrier complained of could represent reasonable government regulation or unfair trade-distorting discriminatory treatment. Some discriminatory practices may be expected or excused if a recognized legitimate national purpose is served.<sup>77</sup> Standards of conduct governing these situations would also be contained in the code. Exceptions analogous to those recognized for trade in goods, such as development of an infant industry, prevention of serious injury to a domestic industry, providing for national security, and dealing with a balance of payments crisis would clearly be necessary. Reasonable regulations for the protection of citizens through technical and professional standards would also be necessary and proper. Such regulations and administrative practices should, however, be covered by code standards prescribing transparency and procedural regularity.

### III. FUNCTIONAL CLASSIFICATION OF SERVICES

Having considered the classification of NTBs to provide the basis for the organization of a general services code, it is now appropriate to consider the structure of the international services sector to determine the scope of commercial activities to which the code might apply. The great diversity and heterogeneity of the types of services and the ways in which they may be provided makes the classification of services trade according to these characteristics a complex problem. The national accounting definition of services is open-ended; services are defined as all output not derived from the four goods-producing sectors — agriculture, mining, manufacturing, and construction.<sup>78</sup> Although service companies are generally thought of as dealing in intangibles, their output is often information reduced to tangible

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77. See G. Feketekuty, *supra* note 3. See generally Marks and Malmgren, *supra* note 71.

78. Ginzberg and Vojta, *supra* note 9, at 48.

forms, such as films, tapes, plans, and reports.<sup>79</sup> Some services, such as data processing, may be provided entirely by electronic means of communication.

One approach to the problem is to identify and define specific service activities on an industry by industry basis. This approach ought to be rejected for the same reasons as in the case of the classification of barriers. A more fruitful approach is to search for common denominators.

#### *A. Meaning of International Trade in Services*

The fundamental issue to be resolved is the determination of what is meant by international trade in services. In the case of international trade in goods, the focus is on what crosses the border. The common denominator is that tangible products — goods or merchandise — cross a border. The basic notion is the exportation of goods by the producing country and their importation by the consuming country. When this basic notion is applied by analogy to trade in services, the fundamental problem becomes evident. Much of what has traditionally been considered by the services sector and the U.S. government to be within the scope of international trade in services does not appear to conform to the basic export/import model.

Two fundamental trading techniques — ways in which services are provided to foreign markets — which have been identified are “across-the-border” trade and “establishment” trade.<sup>80</sup> These two trading techniques obviously do not distinguish trade in services from trade in goods and are applicable to both. Although both the concept of establishment trade and the fact that establishment trade plays a dominant role in the traditional conception of what is meant by international trade in services are well known, their significance appears to be inadequately appreciated in the context of the problems involved in laying the groundwork for multilateral negotiations leading to an international trade in services code.<sup>81</sup>

#### *B. Across-the-Border Trade*

The concept of across-the-border trade as applied to services is analogous to the traditional export/import model of trade in goods. Services are provided by a seller/producer in the exporting country to a buyer/consumer

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79. See CURRENT DEVELOPMENTS, *supra* note 8; G. J. CLONEY II, *supra* note 15.

80. See G. J. CLONEY II, *supra* note 15, at 12-16.

81. See *id.*; Note, *supra* note 12; NEXT STEPS, *supra* note 10; TRADE AGREEMENTS REPORT, *supra* note 16; INT'L CHAMBER OF COMMERCE, LIBERALIZATION OF TRADE IN SERVICES: FURTHER POINTS FOR DISCUSSION, Doc. No. 13-22/INT. 12 (1981-08-31) [hereinafter cited as INT'L CHAMBER OF COMMERCE, FURTHER POINTS].

in the importing country. Across-the-border trade includes:<sup>82</sup>

1. Logistic services necessary for international transport and supply of goods, people, information, and other services;
2. Producer services, such as management or technical services, necessary to foreign production of goods and services; and
3. Other directly traded services such as engineering and information services, commercial insurance, and merchant banking.

Although across-the-border services might present administrative problems relating to valuation and record-keeping, no conceptual problem arises as to whether they are within the scope of international trade in services and amenable to treatment under the contemplated code. Being analogous to trade in goods, they could similarly be classified and taxed at the border.<sup>83</sup>

### C. *Establishment Trade*

The concept of establishment trade is that the transaction requires physical proximity between the seller/producer and the buyer/consumer because the service (or merchandise) is not or cannot be transported or otherwise provided across the border.<sup>84</sup>

From the viewpoint of the parties to the transaction, its purported international character is largely illusory. It is attributable to the fact that one of them is "foreign" and the other is "domestic."

The key to understanding why establishment trade has traditionally been considered to have international character is to focus on the flow of currency resulting from the transaction between the seller/producer and the buyer/consumer. If an international currency exchange is involved, then the transaction affects the balance of payments between the two countries.<sup>85</sup> It is the currency exchange transaction affecting the balance of payments between the countries which provides the basis for characterizing the transaction between the buyer and the seller as international trade.<sup>86</sup>

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82. G. J. CLONEY II, *supra* note 15, at 13-15.

83. The International Chamber of Commerce has proposed a discriminatory sales tax on services transactions to serve the function of providing a domestic preference analogous to the role of a tariff for trade in goods. See INT'L CHAMBER OF COMMERCE, *FURTHER POINTS*, *supra* note 81.

84. See G. J. CLONEY, II, *supra* note 15, at 15-16.

85. See LEGAL PROBLEMS, *supra* note 38, Chap. 13.

86. *Id.*

Tourist trade provides a good example.<sup>87</sup> When an American tourist travels abroad, he purchases goods and services locally with the currency of the host country which he obtained by exchanging American dollars. His purchases may be viewed as exports by the host country and imports by the U.S. because of their balance of payments effects, even though neither the tourist nor the merchants may have considered themselves as engaging in international trade when they carried out the transactions.

The case of an American company providing consultant services to clients in a foreign country from a branch office established in that country provides an example of the converse.<sup>88</sup> The consultant and client are unlikely to perceive their transaction as being international trade. The consultant provides the services locally and is paid in local currency. However, if the company wishes to repatriate the money, it must first exchange the local currency into American dollars. Again, it is this currency exchange transaction affecting the balance of payments between the countries which gives the trade its international character. It may be viewed as the exportation of consultant services by the U.S. and the importation by the host country in which the services were actually rendered.

Regardless of why foreign establishment occurs, whether by choice or business necessity, a serious question is raised as to whether such trade should be considered within the scope of the meaning of international trade in services for the purpose of inclusion in the scope of the services code.

#### *D. Issues Raised by the View that Establishment Trade is Included Within International Trade In Services*

The view that establishment trade is properly includable within the meaning of international trade in services and therefore should be included within the scope of a trade in services code, raises a plethora of complex and serious issues: the right to establishment,<sup>89</sup> investment and repatriation

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87. International tourism has traditionally been viewed as a part of international trade. Its importance to the host country is due to the dual impact of the expenditures of tourists in stimulating the local economy and in favorably affecting the balance of payments. See *CURRENT DEVELOPMENTS*, *supra* note 8, at 114-21.

88. A Subsidiary or branch is the classic model of an establishment enterprise. See *CURRENT DEVELOPMENTS*, *supra* note 8; and G. J. CLONEY II, *supra* note 14.

89. Rights to establish and operate business firms are generally covered in Treaties of Friendship, Commerce, and Navigation (FCN). A survey of all the FCN treaties in force, to which the United States is party, showed that the treatment of the right to establishment differs from treaty to treaty, depending largely on the date of the treaty. The post World War II treaties generally provide for national treatment, but exclude the most important service industries from the national treatment standard, and also contain other exceptions. All the FCN treaties provide for MFN treatment as a floor. See E. ARAKAKI, *supra* note 52.

of profits,<sup>90</sup> and foreign currency exchange and balance of payments.<sup>91</sup> These threaten to make it more difficult to attain the consensus necessary for multilateral negotiations to take place.

These issues are not unique to the services sector. Nothing inherent in the nature of services industries, as distinguished from goods-producing industries, gives rise to these issues. Yet, the analogous situations with respect to trade in goods do not seem to raise the issues in the same way. Many American corporations operate transnationally. When an American corporation establishes a production facility in a foreign country, the plant is considered as part of the domestic economy of that country.<sup>92</sup> It provides employment for the citizens of the country and contributes to its GNP. It is only when the company sells the merchandise to the U.S. (or another "foreign" country) that the transaction becomes characterized as international trade. Then it is considered to be exportation from the country in which the plant is located and importation into the U.S. and the appropriate tariffs are assessed by the U.S. on the imported goods.<sup>93</sup>

The GATT-MTN system applies only to the tariffs and to nontariff barriers that distort across-the-border trade.<sup>94</sup> These companies may be in establishment trade situations similar to services companies, with similar problems relating to the right to establishment, investment and repatriation of profits, and foreign currency exchange and balance of payments. In any event, however, these issues do not currently fall within the scope of the GATT legal system.

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90. The United States has expressed continuing concern with investment and repatriation of profits issues independent of the context of international trade in services issues generally. See TRADE AGREEMENTS REPORT, *supra* note 16.

Although the U.S. government now recognizes the importance that the services sector places on these issues, it seems not to adequately appreciate their significance in the context of achieving the goal of multilateral negotiations leading to a services code. See USTR, TRADE ISSUES IN ADVERTISING (1981); USTR, TRADE ISSUES IN PROFESSIONAL SERVICES (1982); USTR, TRADE ISSUES IN THE ENGINEERING AND CONSTRUCTION AND RELATED CONSULTANCY SERVICES INDUSTRY (1981).

91. See LEGAL PROBLEMS, *supra* note 38, Chap. 13. Although many economists believe that trade measures should not be used for balance of payments reasons, nations frequently do employ trade measures for this purpose.

One major problem is that the jurisdictions of two major international organizations, GATT and IMF, are involved and the boundary line is unclear. See *id.*, at 899.

92. See *id.*, Chap. 15. The product may still be considered "foreign," however. The Volkswagen plant located in western Pennsylvania employs local residents, pays taxes locally, and contributes to the local economy generally. Yet the VW cars produced for sale in the U.S. market are still considered as "foreign" or "imported" by their U.S. purchasers despite that they are domestically manufactured.

93. *Id.*

94. See Jackson, *supra* note 36.

This comparison of the establishment situations of the services sector and the production sector may not be entirely fair to the services companies because their competitive situations may not be equivalent. The services companies tend to establish in highly competitive markets in the developed countries whereas the production companies tend to establish in less developed countries where the cost of labor is cheap.<sup>95</sup> Therefore, the burdens on the services companies created by these establishment problems are likely to be heavier and more acute.

The American service industries apparently hold very strong views that establishment trade is properly includable within the meaning of international trade in services and that these establishment issues should be addressed by a trade in services code.<sup>96</sup> These views have also become firmly embedded in U.S. government policies and initiatives.<sup>97</sup> These are all very complex issues that are difficult enough to deal with individually. Questions about whether a country should allow foreign individuals or companies to enter the country, to own or operate enterprises in the country in direct competition with domestic businesses, and to participate internally in the domestic economy touch and concern national sovereignty far more than free trade. To attempt to bring them all together into a single negotiation would appear to be an invitation to failure.

#### *E. Application of Non-Discrimination Principles to Establishment Trade*

There remains an additional set of potential problems arising from including establishment trade within the meaning of international trade in services and, therefore, within the scope of the services code. These issues arise out of the application of the GATT non-discrimination principles — MFN and national treatment — to establishment trade in services.

Although a generalized right to free establishment would undoubtedly be unacceptable to most countries,<sup>98</sup> the code could provide for the bilateral negotiation of conditions for establishment between parties to the code. Perhaps a licensing system might be implemented. To ensure that foreign-own-

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95. There are obviously exceptions. The cost of labor at the VW plant in Pennsylvania is higher than it would be in Germany.

However, in general, a foreign establishment enterprise will be welcomed by the host country, even actively solicited, when it offers needed employment and other local economic benefits. On the other hand, when the establishment enterprise is perceived as primarily competing against local business or attempting to penetrate the local market, rather than offering economic opportunity, it is more likely to encounter official hostility.

96. See G. J. CLONEY II, *supra* note 15; CURRENT DEVELOPMENTS, *supra* note 8.

97. See G. Feketekuty, *supra* note 3; W. E. Brock, *International Aviation Policy*, *supra* note 5; NEXT STEPS, *supra* note 10.

98. See INT'L CHAMBER OF COMMERCE, FURTHER POINTS, *supra* NOTE 81.

ed firms, once established, would be able to compete fairly with domestic firms, without the impediments of discriminatory barriers, would require equal treatment by the host government, i.e., national treatment.<sup>99</sup> In other words, the national treatment obligation for establishment would be necessary regardless of whether the firms are preexisting or newly established under the terms of the services code.

The effect of an MFN obligation gives rise to complications. Even a conditional MFN obligation would extend the benefits of any bilaterally negotiated establishment rights or national treatment obligation to other parties to the services code who reciprocated.<sup>100</sup> Formally there would be no "free rider" problem because the conditional MFN obligation would not allow any party to receive the benefits without incurring the obligations.<sup>101</sup> Still, some nations might be reluctant to agree to such an arrangement because the benefits might have a grossly disproportionate economic value to third parties when compared with the obligations reciprocally undertaken.

#### IV. CONCLUSION

The increasing economic importance of the services sector to both the U.S. and world economies, the proliferation of discriminatory nontariff barriers, the absence of rules governing international trade in services, and the resulting declining American share of the world market for services provide the impetus for the U.S. to seek to move international trade in services from the political arena into a legal framework. This comment has attempted to deal with some of the fundamental legal issues arising from consideration of widening the scope of GATT to include international trade in services. Such issues need to be resolved before meaningful multilateral negotiations of a trade in services code can take place.

A general international trade in services code, analogous to the MTN codes in character and legal effect, was found to be feasible. The contemplated code would have the legal status not only of an independent treaty, but also of a side agreement to the GATT which would be legally binding only on the signatory parties to the services code until accepted by the requisite two-thirds of the GATT members. Since the General Agreement, by its terms, does not apply to services, the services code would need an independent legal structure parallel to the General Agreement, with its provisions drafted to meet the special circumstances of trade in services. The fundamental principles of the GATT could be incorporated therein.

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99. *Id.* See *supra* note 43.

100. See *supra* notes 66-70 and accompanying text.

101. *Id.*



The classification of nontariff barriers to trade in services to make the barriers amenable to code treatment was found to be feasible. The classification of the services sector into across-the-border and establishment trade revealed complex and difficult issues arising out of the problem of including establishment trade within the meaning of international trade in services. The emergence of these issues leads to the conclusion that it will be very difficult to attain the consensus sought for the multilateral negotiations.

The European Economic Community (EEC) agreement has created an interesting situation. Within the EEC, the members have achieved, by the terms of the agreement, all the objectives the U.S. is seeking to attain and more — free movement of persons, services, and capital, and no restrictions on the freedom of establishment.<sup>102</sup> By the Lomé Convention, the EEC has also achieved a special economic relationship to 46 African, Caribbean, and Pacific states which includes provisions relating to establishment, services, payments and capital movements.<sup>103</sup> At the same time, the EEC has erected a barrier to the U.S. and the rest of the world. The EEC countries are faced with the dilemma of whether the disadvantages of opening their protected market are outweighed by the opportunities which would become available to them to penetrate new markets throughout the rest of the world. Since the American market is at present more open to the EEC countries than is the European market to Americans,<sup>104</sup> the EEC countries may very well decide they have more to lose than to gain by agreeing to multilateral negotiations of an international trade in services code.

If the U.S. government succeeds in achieving an international trade in services code which includes establishment trade and which provides for a right to establishment, an interesting situation might arise. As a matter of policy, the U.S. allows "political" refugees to enter and take up residence. On the other hand, "economic" refugees are denied entry and, if apprehended, are deported.<sup>105</sup> If such economic refugees from a nation party to the services code demanded the right to enter under a claim of the right to establishment, the U.S. might find itself in an embarrassing dilemma. Is there a principled basis for distinguishing highly educated professionals

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102. Treaty of Rome, 298 U.N.T.S. 3, as amended through 1976.

103. Lomé Convention of 1975, O.J.L. 25 of Jan. 30, 1976; 74 INT'L LEGAL MATERIALS 595 (1975).

104. See PREPARATIONS, *supra* note 32; CURRENT DEVELOPMENTS, *supra* note 8; TRADE AGREEMENTS REPORT, *supra* note 16.

105. See N.Y. Times, Aug. 24, 1982, at 19, col. 3; and N.Y. Times, Aug. 26, 1982, at 28, col. 1.

from poorly educated, but ambitious and industrious individuals, all acting as entrepreneurs and offering their services for fees?

*Philip H. Gold*