Negative-list schedules of the TPP

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Abstract

Negative list schedules of commitments are a prominent characteristic of the Services and Investment Chapters of the proposed TPP agreement. In this short paper I consider the evident benefits, and the less evident shortcomings of negative-list schedules of commitments. I suggest that even superficially ambitious negative-list agreements are difficult to parse and prone to manipulation by interested producers and agencies.

Accentuating the positive

One of the early attempts to liberalise services markets by reciprocal agreement was the little-noticed Services Trade Protocol to the Australia-New Zealand Closer Economic Relations Trade Agreement (ANZCERTA), adopted in 1989. That agreement — apparently the world’s first stand-alone services trade agreement — had a negative-list format. The innovation attracted little interest from business groups or even government agencies.¹ But it led to almost-free Trans-Tasman exchanges.²

The special circumstances of Australia-New Zealand trade that permitted the negative-list approach did not translate into the multilateral effort to create a global agreement on services. In the Uruguay Round, the familiar GATT model of positive list schedules of commitments seemed a more practical starting point. My memory, now, of the

¹The ANZCERTA Services Trade protocol was devised by one of my reports at the time, Dr Walter Goode. Contradicting the claims I make below, we adopted a negative list approach in part because we lacked resources to craft a sector-by-sector solution. The branch I headed in the Department of Foreign Affairs and Trade was responsible for all of the negotiating groups in the Uruguay Round other than agriculture, but never comprised more than a dozen people.

discussions in the Uruguay Round negotiation group was that we chose a positive list schedule because it was:

1. **Easier to create.** Few governments had the capacity or motivation even to survey the full range of laws and regulations affecting traded services in the time available. Indeed, most administrations and business groups had some trouble with the concept of a traded service. Tariff schedules that employed a shared nomenclature for individual goods traded across borders were a familiar template that negotiators could extend to services. The existing UN Central Product Classification codes were able to classify traded services as defined activities, guiding the creation of a national schedule at a sufficient level of detail to cover most services-trading activities (although the taxonomy of services is never complete).

2. **Less exacting.** Given the reluctance of low and middle-income countries to join in the services negotiations (even after the ‘mid-term” deals at Montreal in ) the goals for liberalisation in the initial GATS were modest. In order to ensure schedules were complete — and to pave the way for future negotiation — we needed some means not only to record a ‘binding’ of any reductions in barriers but also to schedule barriers that Members offered neither to cut nor bind. Bindings used in the positive-list goods schedules of GATT already had this character. They allowed governments to make commitments in the absence of any immediate commercial benefit to trading partners. This meant that a GATT schedule could be more or less ‘complete’ in scope without necessarily requiring any change in commercial policies. We had the same objectives in the drafting of GATS.

3. **Potentially ‘progressive’**. A positive listing, that identified cross-border and investment barriers seemed likely to promote progressive refinement and deepening of the national schedules on a more ‘granular’ basis than would be possible in a negative-list approach. Future agreements could open markets on a ‘targeted’ basis by reference to a positive list.

In 1995, we hoped the opportunity to make, no or unbound commitments on sectors in the initial GATS schedules would allow governments to accept the same degree of ‘universal’ coverage of traded services as we see in the GATT schedules for goods. The proposed return to the negotiating table after five years would launch a series of progressive refinements of the schedules and deepening commitments.

But it did not. The conservative definition of market access barriers in Article XVI made it possible to have schedule on cross-border market access (not National Treatment) that was “complete” but omitted mention of whole sectors where no defined access barriers existed. On entry into force, all schedules were “defective” in the sense that they omitted mention of many traded services as defined by the GATT Secretariat (some

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3Between the end of the negotiations in early 1994 (or late 1993 for GATS) and the final date for submission of national schedules for WTO Members: in principle, January 1995

4At the time the Brussels Tariff Nomenclature: the Harmonized System came into effect in 1988 but was not yet in wide use.

5The specifications of Art XVI compelled the scheduling of a sector only where certain numerical or quantitative barriers to entry existed.
160 UN CPC codes). Then, the “continuing negotiations” scheduled for a Millennium Round were abandoned in the smoke of Seattle. Still today, twenty years later, the broadest GATS schedules cover about 120 sectors; the narrowest only 2. Later-acceding Members have more complete schedules.

Still, it would be misleading to blame the positive lists for this meagre result. GATS schedules accentuated the positive without eliminating the negative: perhaps the worst of both choices. The GATS allows for negative specification of commitments on market access and on operations within sectors. The national schedules specify market access “terms, limitations and conditions” and national treatment “conditions and qualifications.” Where an entry in a GATS schedule reads “Unbound, except …” it offers a positive list of commitments. But where it takes the form “None, except …” it signifies a negative list of unspecified, possibly trade-restrictive, regulations.

Negative-list benefits

NAFTA (1992) was the first major services FTA based on a negative list that reserved certain laws and policies. It also introduced the dual Annexes for ‘ratchet’ reservation of non-compliant laws and for laws whose non-compliance would extend into the future. The United States then transferred this model to FTA negotiations outside of North America; e.g., US-Singapore. It became a template for many later negative-list agreements, especially where one of the partners was a high-income country. The Australia-United States Free Trade Agreement (2004) uses the same template, as does the proposed TPP.

There are strong arguments in favour of negative-list schedules. They are:

- **Broad:** Analysis of regional FTAs involving East Asian economies shows that negative-list services agreements tend to cover a broader range of service sectors. Still, this says nothing about the depth of (liberalizing) commitments. Nor does the association of negative-list and breadth show the direction of causality. Do negative lists entail breadth, or are trading partners with higher ambitions more likely to choose negative lists?

- **Parsimonious:** A negative-list schedule does not bear the burden of complete coverage of the ever-more-diverse services sector. Whatever is not excluded is open to competitive supply.

- **Dry:** There is no watery gap between the commitments made and the restrictions actually maintained by members of the agreement. GATS is notorious for the amount of “slop” built into commitments that bind access barriers much higher than actual commercial policies require. Negative lists conserve actual policies, so there should be no room to raise protection by stealth.

- **Ratchet-ready:** In principle any trade binding – including GATS bindings – is subject to ratchet provisions; you cannot readily increase a bound rate (and you have to compensate any increase). But a bound positive commitment changes only

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6Carsten Fink and Martin Molinuevo, “East Asian Free Trade Agreements in Services: Roaring Tigers or Timid Pandas?”, World Bank,
on the occasion of a formal negotiation. Negative list agreements automatically capture any improvements in access and operations, as they happen, without negotiation.

- **Recyclable**: once an economy has adopted a negative list schedule (has completed the legislative and regulatory survey necessary to create the negative list) it tends to apply the same list in later agreements and probably, by default, on an MFN basis. Australia’s TTP schedule first appeared in part in the 2004 AUSFTA. It turned up wholly formed only months before the final text of the TPP in Australia’s schedule of concessions in its FTA with China.

An aside here; I suspect that two factors in the first few years of this century made the use of negative-list schedules much more compelling than they were in the mid-1990s. The first, was experience of — and bluntly, disappointment with — the GATS. Its lack of ambition and animation prompted some WTO Members (especially high-income countries) to find alternative frameworks and forms for services agreements. The second, was the growing evidence that a dynamic services sector and competitive services supply explained much of the difference in TFP performance between high income countries as they struggled out of the post-’Dot-com’) recession. Open services market proved essential, too, to the growth and management of production networks. Guarantees on regulations in business services, transport, express delivery, financial and design services markets, on establishment and the movement of key personnel became indispensable for the dispersion of high-tech production around the globe.

Still, negative-list agreements also have less desirable characteristics, to which I now turn. These characteristic faults call for close attention when governments negotiate a trade agreement surrounded by (choose your sporting metaphor) a scrum/full-court-press of industry ‘advisors’ — as was the case in the TPP negotiations after 2011.

**Conservative negotiating function**

When devising a negative-list schedule, a trade negotiator faces the risk of two kinds of error. We might call them

- **Type 1**: failing to list a restriction on access or operations that the government wishes to retain or extend, and;
- **Type 2**: listing a restriction that is later found inconvenient or irrelevant

If we consider all trade policy as experiment (as we should), this classification aligns with its use in physical science: Type 2 errors are at worst an embarrassment but Type 1 errors can be fatal.

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7 Services such as education, health, communications, IT and other business services, are key adjuncts in the ‘residual’ that represents the dynamism of Total Factor Productivity growth in the Solow growth model. There are many analyses looking at differences in TFP growth in the ‘naughties’ between high-income anglophone and non-anglophone countries. In their classic paper “Mind the Gap! International Comparisons of Productivity in Services and Goods Production”, (German Economic Review 8, no. 2 (2007): 281-307.) Robert Inklaar, Marcel Timmer and Bart van Ark show that the growth gap was due mainly to differences in competitive supply of market services rather than to differences in goods production.
A government with a positive-list schedule of commitments such as the GATS, can remedy any omission later without necessarily changing the agreement by unilateral extension of market access or removal of limits on operations. But no omission in a negative list – a Type 1 error – can be unilaterally remedied.

We may suppose that in every services negotiation, a government has both liberalizing goals and defensive goals that it needs to weigh in making commitments. A negotiator devising a negative-list schedule will prefer, conservatively, to err in striking this balance on the side of Type 2 rather than Type 1. The result of this conservative negotiating function is, very likely, negative lists that are longer, or broader — or both — than policy goals require.

Then, even the simplest negatives can be bewildering. Take the first item on Australia’s TPP Annex I Schedule:

For all services, [reserves with respect to] National Treatment, Most-Favoured-Nation Treatment, [Investment] Performance Requirements, Senior Management and Boards of Directors, Local Presence [requirements], all existing non-conforming measures at the regional level of government.

Now, both Chapter 9 (Investment) and Chapter (Cross border trade in services) carefully specify that their obligations are to apply at both the central and regional levels of government. But Australia’s first reservation in Annex I effectively nullifies this obligation for any current law or regulation of any State or Territory government ('regional' is so defined for Australia). Under Australia’s federal division of powers, however, these ‘regional’ governments wield almost all powers affecting health, education and infrastructure services such as water and energy supply; many powers affecting the registration of companies; many powers affecting insurance; most powers affecting land and mining; a large range of powers regulating professional services or delegated to regional professional services bodies… and so on.

Even an observer familiar with the State/Federal division of powers in Australia — presumably not many foreign services suppliers are well-informed — would be hard pressed to say what is left of Australia’s obligations on market operations (especially) by foreign services suppliers in these sectors given the scale of the reservation contained in these words.

I should add that the identical broad reservation appears in the Australian schedule for the 2004 FTA with the United States. The TPP text offers no new horizons here. Perhaps, in the intervening 12 years, State and Territory legislation of services markets has become more open to competitive international supply. But who can tell? The sole national framework to address these issues at State level (the 1995 National Competition Policy) ran out of puff a decade ago. The Turnbull government has praised the most recent attempt to revive and complete aspects of that reform (the Harper Competition Policy Review, 2015). But, so far, has taken no action while giving every sign it will wimp out on egregious barriers such as coastal shipping.
A positive-list schedule such as a GATS contains highly visible commitments whose impact is about as clear from the description as these things can be. But the commitments on a negative list obscure both the reservation they contain and the scope of trade they do not reserve. For all its potential ‘ambition’, a negative-list schedule in this way disguises both the benefits and the limits of the agreement.

The TPP negative list schedules do not refer, as a positive list does, to actually-traded services. Instead they list non-compliant legislative frameworks. Any improvement in market access or operations by foreign services suppliers that may flow from the agreement occurs only in the “gaps” between the items on the negative list. That is, newly contestible markets, from an exporters’ viewpoint, are the negative spaces between the “territories” marked out by the reservations. How can an exporter who is not an expert in the laws of the target market assess the breadth of these new opportunities? She can not.

The disjoint nature of the items of a negative list also makes it difficult to form an assessment of the overall impact of the agreement. It is difficult to get a sense of what the different reservations add-up to when there is no structure to the list.

In a GATS schedule, the use of modes-of-delivery provide a sub-structure for the positive-lists. Across sectors, Mode 1 is rarely restricted by GATS schedules; a variety of quantitative limits afflict Modes 2 and 4; Mode 3 restrictions on establishment are quantitative but on operations usually focus on control of the entity and, less often, on the quantity or quality of production. The four modes, present in every scheduled sector, expose the nature of protection at the sector level and assist comparison between sectors.

But negative lists have no sub-structure. They are merely a more-or-less disordered collection of diverse legal (or, as we saw in the Australian annex, constitutional) frameworks without evident characteristics in common.

Perhaps it is also a consequence of this heterogeneity that agreements taking the negative list approach, including TPP, have no ‘horizontal commitments’ such as we find in GATS. There, horizontal measures may either enhance or restrict market access (establishment) or national treatment (operations) in a very powerful way, cutting a swathe across all sector-commitments.

Why are horizontal commitments absent? The heterogeneity of the reserved legislation may be part of an explanation but cannot entirely account for it. It is possible to imagine some horizontal commitments that would simultaneously modify all of the diverse items in a negative list of reserved laws. For example, there could be a horizontal commitment adopting a definite time limit on the preservation of Annex I domains from the disciplines of the agreement.

I suggest that there is a more fundamental reason that horizontal commitments are missing from agreements like TPP. Each of the legislative frameworks that Members have listed in their Annexes I & II have, most likely, been “tuned” in the political
economy to the particular characteristics of the sectors or producers or regulators that they serve and protect. Probably, each of these laws defines an agency-client relationship between relevant arms of the TPP governments and the services sectors that they regulate. Each of these relationships is likely to be implicit, specific, confidential and fully-invested. Cross-cutting horizontal commitments would, simply, not fit the diverse interests embodied in these relationships.

In short, a conservatively drafted negative list probably gives too much comfort to established competitors and to their government-agency cooperators, and too little information or assurance to everyone else. It is a rich field for the sort of public choice analysis that Simon Lester talked about yesterday.

Standstill and signalling

Is my assessment so far too skeptical? To conclude, I would like briefly to push skepticism still further in two directions.

First, a conservatively drafted negative list is very likely a 'standstill' agreement on services protection. That’s not a bad thing; but it’s not an ambitious thing either. Other pressures need to be brought to bear, over the top of such a negative list, to secure progress. Either trading partners must insist on narrowing the list before they accept it, or – more commonly, I suspect – other specific elements of the agreement such as defined disciplines on the movement of business people, the prohibition of data protection at the border or the introduction of rights of establishment, must pressure the domains protected by the negative list. This is the case in the proposed TPP.

Second, the murky protection offered by negative lists weakens the signals that a trade agreement sends to the political economy.

As we head into the second quarter of the century, regional trade agreements have become overrated as instruments of trade liberalisation, structural reform and foreign policy. Most offer modest and diminishing returns in these domains. Still, they have one characteristic that is as powerful today as it ever was: they are credence goods. When their provisions are certain, firm, and attract good compliance by members they constrain sovereigns abroad and parliaments at home to do what they promised. For reasons I won’t detail here, such credible signals make trade adjustment less costly and structural reform more effective.

But the items on a negative list are no such promise. Only half an undertaking impacts those domains protected by Annex I carve-outs: that they will see no stronger protection from foreign competition. But the fuzzy character of the reservations and the agency-client relationships that likely underlie them signal that the maintenance of current protection remains a biddable good in the political economy of services markets.

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8If the TPP’s claims are stronger than most, it is because it provides a single platform that may lead to incremental micro-economic reform in two of East Asia’s most important trading economies: Japan and Vietnam