

Public Services and the GATS

1. Introduction

The strength of a society depends unequivocally upon a foundation that ensures the provision of a range of quality public services to all who need them, regardless of their ability to pay for them. It is perhaps perplexing then that the provision of public services, even those thought of as essential or basic services, is increasingly in the hands of private companies, leading inexorably to their commercialisation, threatening their reach to those that need them most, and potentially eroding the sustainability of their provision from both a social and environmental perspective.

This subchapter aims to achieve the following: to provide an overview of the role and relevance of public services, and to examine the link between the provision of public services and the General Agreement on Trade in Services (GATS); the primary vehicle of the liberalisation of services within a multilateral, rules-based system of international trade and therefore an area of specific concern. Consequently, with respect to the first aim, this subchapter will examine the evolution of “public services” and why it remains important to retain an element of government intervention in their provision. With respect to the second, the chapter will focus on the scope of the GATS and the tensions inherent in the interpretation of Article 1:3 of the GATS, which deals with the “public services” carve-out from the agreement.

This subchapter is divided into 5 sections. After this Introduction, Section 2 will examine what is meant by “public services”, including the usefulness of the more restrictive conception of “essential” or “basic” services. Section 3 focuses on the role of public services in addressing sustainable development concerns, particularly the relationship between public services and their privatisation. Section 4 is devoted to the relationship between public services and the GATS. Much has been written on public services and the liberalisation of trade and this section aims at synthesis of arguments on both sides of the divide, which have become increasingly more vocal and passionate as the services negotiations in the WTO proceed as part of the Doha Development Round. Section 5 concludes.

2. What are “public services”?

It is easy to think of examples of public services: law enforcement, defence, and primary education are some of the most obvious. However, what constitutes a “public service” differs in different contexts, among groups in society, and across time and space. What is and what is not a public service depends on a range of factors, from social norms and historical developments to conceptions of the role of the state and the nature of the

market. The extent of publicly provided services also depends on the resources available to governments, which are different in developed and developing countries¹.

An understanding of public services depends on the lens through which the concept is viewed². It could focus on *what* is supplied, *to whom and under what conditions* the service is supplied, or on *who* is supplying the service. For these reasons, a precise and substantive definition of “public services” is difficult to provide. (The problem is compounded by the fact that neither the GATS nor any other services trade agreement on a regional or bilateral level explicitly use the term “public services”.) A common conception of a public service is one that is supplied by any level of government, governmental agency or public enterprise. Under this conception, therefore, public services could include any service one would care to name, from law enforcement and defence to health, education, transport, telecommunications, financial, and sporting and cultural services. A public service may be more precisely defined as any service provided for large numbers of citizens, in which there is a potential and significant market failure, justifying government involvement, whether in production, finance, or regulation³. While under this definition the range of potential public services is similarly broad, it does not discount the possibility that the public sector may not be directly involved in the actual supply of the public service. Nevertheless, there are problems with this conception too and we shall return to it later in the section.

At various points in history, public services were either provided directly by public authorities or by a mixture of what today would be termed “public-private initiatives”. In the 18th century, for example, public services were provided by farming out concessions to private companies who were then given a protected monopoly to raise charges and taxes to finance the business⁴. The commercialisation of public services today is thus not a new feature of the modern economic system but represents a return to the “ancien regime” of public services, which itself was replaced by a system of extensive public ownership and provision during the late 19th century that continued well into the first part of the 20th century⁵.

Today the “ancien regime” of public services is in the ascendancy once again. Partly a result of their own initiatives and partly a result of orthodox economic consensus following the global economic slowdown in the 1980s, the privatisation of public services by governments has recently gathered pace in various guises and forms. Nevertheless, despite this trend, the extent of the provision of public services in most countries remains a peculiar characteristic of its market orientation. Coordinated market economies such as Japan, France, Germany and the Scandinavian countries still have a much larger public sector (i.e., spend proportionally more on public social services) than the more liberal market economies of the United States and the United Kingdom⁶. The United States’ health care system, for example, is dominated by private operators while in the United Kingdom public-private partnerships are increasingly the order of the day.

Table 1 (below) shows government consumption as a proportion of GDP in 1985 and 1999 as well as the percentage change in the data over the period of analysis. While government consumption as a proportion of GDP has fallen in each of the countries listed

in the table it is interesting to note that it has fallen more significantly in the more liberal market oriented economies, such as the US and the UK.

Table 1. Change in government consumption as a proportion of GDP, 1985-1999

	Government consumption as a proportion of GDP		Percentage change
	1985	1999	
Canada	21.8	18.9	13.30
France	23.7	23.3	1.69
Germany	20.1	19.1	4.98
Netherlands	25.0	22.9	8.4
UK	21.5	18.5	13.95
USA	20.8	17.7	14.90

Source: Grout, P. and Stevens, M. (2003).

Despite historical trends in the provision of public services, an economic rationale for the public provision of certain services can be found in Adam Smith’s *Wealth of Nations*, published in 1776 and generally held to have set out the principles of a free-market economy. Modern economic justifications for publicly provided services are rooted in an analysis of market failure. As such, *public services* have often been treated synonymously with *public goods*. A pure public good will be underprovided by the market since, once provided, it is difficult to prevent its consumption or use by other people. (Typical examples of a pure public good include national defence and lighthouses.) Obviously, services such as health and education are not pure public goods; there are costs involved in their supply to additional individuals and it is possible to prevent such services from being consumed by certain individuals or groups of individuals.

Treating public services and public goods synonymously is most unfortunate as it assumes publicly provided services are deviant cases of market failure, defining them negatively in terms of what they are not, not what they are⁷. The definition of public services provided earlier in the section – i.e., any service provided for large numbers of citizens, *in which there is a potential and significant market failure*, justifying government involvement, whether in production, finance, or regulation – is guilty of this making precisely this mistake. What definitions like this tend to do (albeit unintentionally) is narrow the set of services that can justifiably be provided by public systems within the prevailing economic discourse.

Finally, it is important to consider what is meant by “essential” or “basic” public services and to ask whether the ostensibly more restrictive conception is perhaps more useful than the term “public services” *per se*. By essential services, one typically has in mind basic utilities such as electricity and water as well as health and education. These services already constitute a significant part of the WTO’s services sectoral classification list (W/120) and when one includes transport services, the conception of essential or basic services threatens to become so broad as to be practically meaningless.

Again, what constitutes an essential public service differs in different contexts. The notion runs up against the same difficulties encountered in attempting to define “public services” and, of course, one has the added difficulty of attempting to clarify what is meant by the word “essential”. It would be difficult to argue that tourism, for example, is not an “essential” service in Tanzania. Tourism in Tanzania accounts for an increasingly substantial share of Gross Domestic Product and is a lead sector in GDP growth. Unlike basic utilities, the supply of tourism services is obviously not essential when viewed through the lens of universal access. In terms of its contribution to GDP growth and employment, however, it most certainly is and arguably might require some form of public involvement.

3. Public services and sustainable development

Public services represent a fundamental aspect of the social, economic and cultural fabric of any society. Education and health services (including water and sanitation services) are critical in being able to achieve a number of the United Nation’s Millennium Development Goals (MDGs), including the provision of universal primary education, reductions in infant mortality, and improvements in maternal health. The privatisation of public services – rooted in neo-liberal conceptions of the role of the state – is arguably threatening governments’ ability to achieve these goals and, hence, threatening the very notion of “sustainable development” itself.

The impact of public services on growth and development has become a growing area of research by economists, sociologists and others. The emerging consensus is twofold: First, that public services have a positive effect on the productivity of the whole economy; and second, that the privatisation of public services is not necessarily the first-best option given the need for their reform. The belief that public sector reform cannot take place without privatisation is not borne out by experience. Many developing countries have extended their coverage of water and electricity systems through the public sector, providing an affordable service and improving efficiency in the process. Notable examples include rural electrification in South Africa, the extension of water and sanitation services in mega-cities such as Sao Paulo, and the maintenance of an efficient, financially viable water system in Ramallah, in the West Bank⁸.

There are a number of risks attached to the project of privatising public services⁹. From an economic perspective, an obvious danger is the transfer of ownership coupled with the preservation of market structure; in other words, the change from a public monopoly to a private one, particularly in developing economies without institutional arrangements to deal with competition policy concerns. New, private owners simply capture existing monopolistic rents and, without the spur of competition, persist in inefficient behaviour. Second, privatisation arguably draws resources away from the state. When services for more affluent citizens are privatised, local governments may lose the revenue needed to cross-subsidise poor and marginalised groups. Thus, governments may be saddled with the responsibility of serving low-income groups without the benefit of progressive revenue streams¹⁰. The result is the development of a two-tier structure of service

provision in which the wealthy pay for their own services, privately, while the poor are left to pay more for their services through an increasingly impoverished public sector. Third, private companies cannot commit their shareholders to remain in any venture which ceases to make an adequate risk-adjusted return on their capital and, thus, cannot make the sort of long-term commitment to public services that is often required. For example, a critical issue in making basic education work in very poor communities is addressing the question of teacher training, which requires a substantial upfront investment with little immediate return, and culturally appropriate means to keep teachers in rural and remote areas. This implies a long term investment without very high and immediate financial returns. One cannot envisage private sector providers easily doing this¹¹. Fourth, a one-size-fits-all approach to privatisation may destroy the structural strengths of the system and fail to solve the (context-specific) weaknesses. Fifth, the process of privatisation is often spearheaded by the Ministries of Finance, which tend to focus on maximizing revenues from the sale of public assets without necessarily considering their downstream economic and social impacts.

The list above is not exhaustive but rather illustrative of the dangers inherent in the privatisation of public services. The higher the probability of any of these risks in any particular case the more tenuous the link between the provision of public services and sustainable social and economic development. Perhaps for these reasons the tide appears to be turning once more. Many governments are increasingly sceptical of the benefits of privatisation. South Africa has deliberately decelerated the sale of state-owned enterprises (SOEs) while Egypt has similarly ruled out the sale of state-owned electricity and water companies. There is growing awareness among policy makers sensitive to the need for sustainable development that public service reforms can (and indeed must) take place within the public sector based on principles of transparency, accountability and participation¹².

It is important not to review the case either for or against privatization in purely ideological terms but look individual contexts and countries. The case of South Africa is an interesting one and future research should look at a range of case studies in comparative perspectives.

3.1 Public Services, Privatization and South Africa: A Case Study

The birth of a new democracy in South Africa resulted in a gradual change in South Africa's economic policy landscape with introduction of various micro-economic and macro-economic reforms. It is, however, important to bear in mind that a large part of South Africa's reforms were driven internally and not by global institutions such as the World Bank or the International Monetary Fund. Similarly the need to privatize some state owned assets were driven by domestic considerations rather than pressure from an external agency. It is important to bear in mind that South Africa, unlike many other countries on the African continent did not undergo a World Bank type structural adjustment program. Some critics would, however, argue that although economic policy was driven by domestic interests, it resembled elements of structural adjustment.

Two central tenets of policy change in services and utilities in South Africa in the last ten years have been privatization and the reduction of barriers to entry to reduce market power in various sectors. Four key parastatals in the electricity, transport, telecommunications and defence sectors, which accounted for 86% of aggregate State Owned Enterprises (SOE) turnover, 94% of total SOE income, 77% of total SOE employment, and 91% of the total assets of these enterprises, really matter for the privatisation process in South Africa. A few isolated incidents of privatisation in the 1980's aside, a programme of privatisation and restructuring of South African SOEs was undertaken in the mid-1990's.

There were several facets to the privatisation programme. These consisted of a combination of privatisation, strategic equity partners often with a significant minority stake by foreign investor or strategic management partners, with the precise mix tailored to the industry in question. The privatisation process in South Africa has been largely focused on divestiture of 'non-core businesses', such as resorts, broadcasting stations and related services in the transport sector, as well as the restructuring of utilities by selling minority stakes to so-called strategic equity partners and Black Economic Empowerment (BEE) groupings. The impact of this on actual empowerment is difficult to measure at the stage. What is clear is that this provided one vehicle for creating opportunities for black firms to enter the mainstream of the economy. This has however, been limited to a few firms and has not had a significant impact on broad based empowerment of the poor. The privatisation process, at best, creates some opportunities for black entrepreneurship, but does not, for example, boost the opportunities for small and medium enterprises in any significant way where the scope for broad based empowerment is wider.

An ex-post analysis of the impact of privatisation is not possible as the South African government did not develop a full-blown fast paced privatisation strategy. It was part of a broader process inducing more efficiency in the economy, as well as restructuring firms that were essentially inefficient and a burden to the state. In fact, at this stage none of South Africa's state owned utilities have been fully privatized. Two factors, explain the slow pace of privatization in South Africa. Firstly, the nature of inequality and high levels of unemployment has made it difficult for the current government to simply introduce massive deregulation in the economy. Secondly, and more importantly, there is a growing realization amongst senior policy makers that the country has to enhance its capacity to effectively regulate privatized firms that are no more under government ownership. This is a formidable challenge and privatization in the presence of weak regulatory capacity is likely to undermine and set back the process of creating more efficiency in the economy and better access to services for the poor.

A key problem in utilities has been the ways the sequencing has evolved in South Africa. For example, there has been some level partial privatisation without any changes in market structure. Partial sale to private investors has simply transformed the public monopoly into a private one, without creating the incentives for efficiency or innovation that competition could spark. In sum, what is most striking about the restructuring process in South Africa is the fact that little emphasis was placed on the introduction of competition in the sectors concerned. It is common knowledge that privatisation *per se*

does not make companies more competitive or industries efficient. Partial privatisation has been given priority in the utility sectors. In some cases, it could be argued, this has been at the expense of competition and regulation as 'strategic equity partners' demanded extended monopoly rights or were guaranteed limited price regulation.

It is extremely difficult to generalize about what are often vastly different sectors in the economy with very different dynamics. However, the case of energy and telecoms is quite interesting. The energy industry in South Africa is currently undergoing a restructuring process, including the introduction of competition in certain parts of the electricity supply chain. There are essentially four facets to the energy industry: generation, transmission, distribution, and retail. Ironically, the cost of electricity in South Africa is very low by global standards. This might lead one to conclude that if energy prices are low, the market structure of the sector, whether dominated by a monopoly or highly competitive, is irrelevant. However, this is not true and the reason for the co-existence of a monopoly that typically prices above its marginal costs is more complex.

There are two fundamental sets of factors that explain why energy prices are low in South Africa. First, the financial viability of the state monopoly, Eskom, is attributed to various distortions, such as prices that are below international averages. This is due to the use of low-grade coal-based energy, in the production of which environmental costs are not internalised. Second, Eskom has until recently enjoyed implicit subsidies, such as exemptions from taxation and dividends. Effectively this meant that there was no accountability in the way capital was invested. Hence, it is important to distinguish the economic from financial profitability of the sector. Although these firms may be financially viable in that they are not a burden on the country's fiscus, they may not be economically viable because they receive either explicit or implicit subsidies from the government. (see Steyn, 2004)

It's clear that in the case of energy we have a situation where the economy as whole bore the brunt of bad investment decisions. Although it may seem that consumers benefited from low energy prices, this may have come at an enormous tax burden of which could have otherwise been used elsewhere in more effective ways (see Eberhard, 2003). This rather unusual state of energy pricing in South Africa explains why future reform may lead to an increase, rather than a decrease, in prices for the poor.

Another interesting case is fixed line telephony, which is still a monopoly. Access to communications services has been limited partly because telecoms prices in South Africa are well above international prices. Needless to say, telecoms are a critical sector in the economy and have serious implications for consumers and small businesses.

South Africa's sole fixed line telecommunications carrier, Telkom has a monopoly and is protected by the Telecommunications Act that gave it monopoly status until 2002/3 in various segments such as, amongst others, national and international long distance calls, and local access. South Africa is already in violation of its WTO commitments – but even if it was not – in order to ensure that competition was allowed what are the important

issues we have to take on board. The first is what the cost to the economy is of maintaining the current structure and form of the communications sector has been very high. The partial privatization has been a real cost to the economy and the major challenge has been to change the market structure by creating more competition before privatizing.

In view of the uniqueness of different sectors that underwent some level of privatization, it is hard to provide any clear assessment of privatization on prices and access to the poor. What is, evident, however is that access to many services such as energy, roads, education and water have improved for the poor in South Africa over the last ten years – this, however, has less to do with actual reforms or privatisation than it has to do with changing budgeting priorities of the new democratic government. It is also important to bear in mind that lack of access to these services is the result of widespread poverty and not necessarily because of any reform or privatisation. This poses specific difficulties for the South African government. For example, an important challenge that the South African government faces is whether it should simply redistribute income or subsidise the provision of services to the poor. It is important to bear in mind that privatization per se does not necessarily bring prices down and improve access to the poor. There is an important role for government on this front. More important than privatization is the need to introduce more competition in sectors that previously took on monopoly characteristics. In cases where, this a monopolies will exists – like in parts of energy for a long time, a major challenge that has been facing government has been to develop an effective regulatory capacity, which to date leaves a lot to be desired.

Although domestic political economy considerations will drive pace of privatization in the South African economy in the future, the GATS negotiations, more than the World Bank or IMF inspired policies is likely to be one external stimulus to reform in the economy. GATS could potentially have important implications for South Africa's domestic reform initiatives. It is important to stress that market access issues are, to some extent, different from domestic competition and regulatory issues. Clearly, there are strong interconnections and the major challenge facing the government is to ensure coherence and consistency in policy. On the domestic efficiency side, market access may be less effective than competition policy. Although South Africa's GATS commitments have played some role in putting the government under pressure to bring an end to, telecoms for example, they have been largely ineffective in accelerating reform.

4. Public services and the GATS

There has been much debate regarding the provision of public services and the scope of the GATS. The debate has increased in intensity and fervour recently and the many positions put forward by both supporters of the GATS and its critics range from the justified to the patently misguided. Supporters argue that the progressive liberalisation of services will result in the reallocation of resources to their most efficient use, acting as a spur to growth and development. Critics warn that untrammelled liberalisation carries with it substantial risks, particularly for developing countries. In addition, liberalisation and privatisation are not uncommon bedfellows and the pressure to both liberalise and

privatise, critics argue, will seriously compromise governments' ability to pursue legitimate policy objectives. It is not the purpose of this chapter to resolve the debate – for it cannot possibly do so – but it will endeavour to present the arguments as objectively as possible within the context of an examination of Article 1:3 of the GATS, which deals with the public services carve-out from the agreement.

Before we examine Article 1:3 of the GATS, it would perhaps be worthwhile to briefly consider its purpose by way of some admittedly sweeping generalisations. The GATS was negotiated during the Uruguay Round (1986-1994) and came into force in January 1995. Successful negotiations on basic telecommunications and financial services were concluded in 1997 – widely regarded as the WTO's "golden year" – and a new round of services negotiations began in January 2000. The GATS is a multilateral agreement designed to promote the progressive liberalisation of services within a rules-based system governing international trade. As such, therefore, its primary objective is to facilitate the opening up of a range of services in Members' economies to what Professor Sally of the LSE terms "the fresh winds of international competition"¹³. While the gains from liberalisation are meant to accrue to the liberalising economy, the GATS negotiations – as with all other trade negotiations – allow participants to receive politically palatable concessions that culminate in an overall package of deals designed to cushion the blow of those interest groups worst affected by the liberalisation process.

Much has been made of the flexibility of the GATS. Importantly, in the first place, Members are at liberty to decide which sectors to liberalise. Only then are Members required to list any limitations to the provision of services in these sectors by foreign providers in a schedule of commitments. It is to these services (notwithstanding certain exceptions and carve-outs) that the articles of the GATS apply as well as the overriding objective of progressive liberalisation through successive rounds of negotiations. The above procedure is commonly referred to as the "positive-list" approach. It differs from the NAFTA-style "negative-list" approach, which assumes that all sectors are open to international competition unless stated otherwise. While both the "positive-list" and "negative list" approaches are theoretically able to achieve the same level of liberalisation, the former is thought to be less onerous and, hence, more palatable to developing country Members. The ultimate flexibility, of course, is a Member's right to withdraw from the WTO completely. In the United States, for example, Congress has the opportunity of voting to quit the organisation every five years. While the opportunity exists, it is extremely unlikely that Members who have taken the trouble to accede to the organisation will choose to leave it.

The GATS is not, therefore (as some critics of the agreement suggest), a vehicle for privatisation but instead a vehicle for private service suppliers, through their governments, to seek access to, and fair treatment in, the markets of other Members. The GATS is, quite simply, as the European Union famously declared "first and foremost an instrument for the benefit of business"; however the agreement itself neither requires the privatisation of services in Members' markets nor does it *force* Members to liberalise services. In and of itself, the GATS merely provides a framework within which to *promote* services liberalisation. Since the WTO is a member-driven organisation, what

pressure there is to liberalise comes from the Members themselves, particularly those Members who have specific and focused interests in the various negotiations and the capacity to pursue their negotiating agendas effectively.

When representatives of civil society argue that, under the GATS, governments will fatally compromise their right to pursue social policy objectives and to protect public interests they are, in the vast majority of cases, confusing what the agreement is able to enforce with the ability of Members to push their own interests within the negotiations. More pragmatic critics of the GATS therefore acknowledge the need for rules governing international services trade rather than call for their elimination altogether. In a perfect world the GATS may be described as a “helpful auxiliary” or “external constitutional prop” that governments can use as one of many levers to facilitate the process of services liberalisation¹⁴. In the cut and thrust world of trade negotiations, potential weaknesses in the agreement itself could turn a helpful auxiliary into a Cassandraian curse.

4.1. Article I:3: what is it and what does it mean?

Article I of the GATS determines the scope of the agreement. The GATS applies to “measures by Members affecting trade in services” (Article I:1). The term “trade in services” is defined as supplying services in any of the four modes (Article I:2); in other words, cross-border supply (Mode 1), consumption abroad (Mode 2), commercial presence (Mode 3), and the temporary movement of natural persons (Mode 4). Article I:3 (a) defines “measures of Members” as measures of governmental and non-governmental entities. Articles I:3 (b) and (c) then state that “services” includes “any service in any sector *except services supplied in the exercise of governmental authority*”. Such services are defined negatively to mean any service which is supplied “neither on a commercial basis nor in competition with one or more service suppliers”.

The scope of the GATS thus depends on how the notion of “services supplied in the exercise of governmental authority” is understood¹⁵. A service that is supplied in the exercise in governmental authority must meet two cumulative conditions: It must neither be supplied on a commercial basis nor must it be supplied in competition with one or more service suppliers. In other words, in order for a service to be excluded from the GATS both criteria must apply. Any service that is not supplied on a commercial basis but in competition with one or more service suppliers *or* is supplied on a commercial basis but not in competition with other service providers would *not* be considered a service supplied in the exercise of governmental authority and, therefore, would be considered to fall within the scope of the GATS.

Effectively, then, the scope of the GATS with respect to public services depends on an understanding of the notions “supplied on a commercial basis” and “supplied in competition with one or more service suppliers”¹⁶. There is a great deal of ambiguity regarding these notions in WTO documents and discussions and between Members themselves¹⁷. For example, in the background note on *health and social services*, the Secretariat observes that “the institutional arrangements governing the provision of

health, medical and social services may vary widely, from complete government ownership and control to full market orientation.

“On the one hand, there is the possibility of services being provided “in the exercise of governmental authority”, meaning, according to Article I:3 (c) GATS, that they are supplied neither on a commercial basis nor in competition. A case in point of such activities – not covered by the GATS – is the provision of medical and hospital treatment directly through the government, free of charge. In contrast, other systems may allow for full private participation without access controls, apart from quality- and qualification-related regulation, at freely negotiated prices.”

The background note goes on to observe that the co-existence of government-owned and private hospitals “may raise questions... concerning their competitive relationship and the applicability of the GATS: in particular, *can public hospitals nevertheless be deemed to fall under Article I:3?*” The note concludes by stating “that the hospital sector in many countries, however, is made up of government- and privately-owned entities which both operate on a commercial basis, charging the patient or his insurance for the treatment provided. Supplementary subsidies may be granted for social, regional and similar policy purposes. *It seems unrealistic in such cases to argue for continued application of Article I:3 and/or maintain that no competitive relationship exists between the two groups of suppliers or services.*”¹⁸

Perhaps due to the increase in public awareness and growing civil society concerns regarding the link between public services and the GATS, the Secretariat appears to contradict its earlier understanding of the scope of the GATS in the background note by making the following observation in a Post-Uruguay Round Inventory and Issues Special Study: “It is perfectly possible for governmental services to co-exist in the same jurisdiction with private services. In the health and education sectors this is so common as to be virtually the norm... *It seems clear that the existence of private health services, for example, in parallel with public services could not be held to invalidate the status of the latter as ‘governmental services’.*”¹⁹

Given the uncertainty surrounding the understanding and interpretation of Article I:3 of the GATS, any objection raised by one Member regarding the applicability of Article I:3 to a “public service” supplied by the government of another Member is likely to be dealt with by the WTO’s Dispute Settlement Body (DSB) on a case by case basis. Indeed, short of an amendment to the GATS clarifying the meaning of the phrases “supplied on a commercial basis” and “supplied in competition with one or more service suppliers”, this would appear to be the only basis on which to proceed should a dispute arise. Here, critics of the GATS have repeatedly argued that in such cases, a narrow interpretation of “services supplied in the exercise of governmental authority” is likely to be made by the DSB²⁰. The narrower the interpretation, the wider the scope of the GATS and the larger the set of services to which the GATS would apply.

The remainder of the section will therefore examine the phrases “supplied on a commercial basis” and “supplied in competition with one or more services suppliers”

more closely. With respect to the former, the word “commerce” is defined as the activity of buying and selling. Therefore, any service that is not supplied free of charge could be considered to be “supplied on a commercial basis”. In the arena of public services, however, even when services are supplied at subsidised rates to those who cannot afford them, some price is charged. So it is not obvious that simply because a price is charged for a service, it should be considered to be supplied on a commercial basis.

What, then, is the determining characteristic of a service supplied on a commercial basis? One typically engages in commercial activity with the intention of making a profit. A service that is not supplied on a commercial basis would then be one for which the price charged is insufficient, given the costs of supplying the service, to realise a profit. This would be a service supplied on a not-for-profit (*sans but lucratif*) basis and, provided its supply is not in competition with one or more service providers, would fall outside the scope of the GATS. Depending on the particular circumstances of the case, additional criteria would have to be applied to determine whether the supply of service at a price just covering the costs of the provider could be considered “commercial”²¹.

Considering the second phrase, “supplied in competition with one or more service suppliers”, Hartridge (2000) notes – again in apparent contradiction to earlier statements issued in various background notes by the WTO Secretariat – that “it is perfectly possible for public services to co-exist with private services in the same sector without calling into question the status of the former as governmental services”²². Despite the fact that most modern public service systems consist of a complex, continually shifting mix of governmental and private funding and governmental, private not-for-profit and private for-profit delivery, the confidence of the remark is not necessarily borne out by a closer examination of the phrase from an economic and legal perspective.

In order to establish when a service is supplied on a competitive basis, the following two-step approach is suggested: First it should be asked if there is a situation in which two or more service suppliers supply the same or a comparable service. Second, it is necessary to establish if the services supplied substitute or complement each other²³. Assuming the provision of comparable services, two service suppliers are only in competition if one supplier’s services can substitute the services of another. (There are, of course, degrees of competition, which may complicate matters further. The above understanding of competition tends towards a strict interpretation of the term.) In these cases, the size of the market in which the two suppliers operate is of crucial significance. A government hospital in Johannesburg is not necessarily in competition with a private hospital if the number of patients requiring treatment exceeds the ability of one hospital to provide it. Furthermore, a private hospital is more likely to target a particular segment of the population (i.e., those with the ability to pay for private healthcare) while a government hospital is more likely to serve the poorer segments of the population.

Krajewski (2001) applies his two-step approach to primary education: “(I)t could be argued that public schools and private schools provide the same or a comparable service, since they are both providing children of a certain age range with a certain amount of general education. It could also be said that public and private schools are targeting the

same market: Since every child can only go to one school, the loss of a service consumer (i.e., a school child) by the public school can be supplemented by the private school. Consequently, it can be argued that public and primary schools are providing a service “in competition” with each other. However, it could also be argued that the services are not comparable, because public schools usually fulfill a universal supply obligation, while private schools often don’t. Similarly, it could also be argued that public schools with a universal service obligation target the entire market while private schools target only a certain segment of that market, i.e., those who are able and willing to pay school fees.”

It is simply not good enough to glibly assume that there is no need for further interpretation or clarification of Article I:3 because “no question has been raised by any Member” regarding the exclusion²⁴. Until uncertainty is eliminated from Article I:3 (i.e., until the article itself is amended in a such a way as to resolve the uncertainty), it is perhaps right that certain countries such as South Africa have consistently refused to make commitments in sectors like health and education in which they have an overriding obligation to reduce poverty and inequality²⁵. The GATS may well be a “helpful auxiliary” for Member countries unilaterally embarking upon the project of trade liberalisation but Professor Sally’s description arguably ignores situations in which the unequal balance of negotiating power between Members results in the weaker party finding it difficult to resist a request to liberalise aspects of its public service regime by a stronger, more dominant party with specific and focused interests.

On the other hand, one should be careful not to ignore the limitations of the GATS in an international trading system marked by the proliferation of regional trade arrangements (RTAs). Again, the South African example is fruitful. South Africa has embarked on an ambitious bilateral negotiating agenda. Not only will the majority of services agreements within the various RTAs adopt the arguably more onerous NAFTA-style architecture, but if the agreements themselves are not to fall foul of GATS Article V on regional integration then they are required to cover “substantially all trade”; including health and education, which the South African government has strenuously resisted putting on the multilateral negotiating table²⁶. Once sensitive sectors such as health and education are included in regional agreements, the argument to exclude them from the ambit of the GATS is seriously compromised. To commit these sectors in one arena while attempting to bar them from another reveals an underlying weakness in strategy formulation that key WTO Members are likely to exploit. Not only does this underscore the importance of a close coordination of the regional and multilateral tracks of services liberalisation (rather than the substitution of one for the other) but it may also result in a reversal of a situation in which multilateral events condition what goes on bilaterally outside the WTO. For those who believe in the primacy of multilateralism, the cart could well be pulled before the horse before too long.

5. Conclusion

Sustainable social and economic development critically depends on an efficient and affordable provision of public services. It is clear that public service in many countries is

in dire need of reform. However, privatisation is not necessarily the panacea many economists of a neo-liberal bent presumed it would be, and the process of privatisation often threatens to fray rather than strengthen the link between public services and sustainable development. From an economic point of view, pro-competitive reforms of services are good in theory yet the process of services liberalisation has attracted its fair share of detractors concerned that the primary vehicle for services liberalisation – the General Agreement of Trade in Services (GATS) – may open the door to further waves of privatisation in the public service sphere. There is a great deal of uncertainty regarding Article I:3 of the GATS, which deals with the public services carve-out from the agreement. While this uncertainty in the understanding of key phrases in Article I:3 persists governments will remain cautious in opening up essential services to international competition, whether they choose to embark upon a process of privatisation or not. Until such ambiguities are resolved, the GATS will not be viewed by its critics as anything remotely resembling a “helpful auxiliary” in the reform of public services.

¹ Krajewski, M. (2001), “Public Services and the Scope of the General Agreement on Trade in Services (GATS)”, Center for International Environmental Law (CIEL), Geneva.

² Krajewski, op. cit.

³ Grout, P. and Stevens, M. (2003), “Financing and Managing Public Services: An Assessment”, CMPO Working Paper Series No. 03/076.

⁴ Hall, D. (2003), “Public Services Work!”, Public Services International (PSI), www.world-psi.org

⁵ Ibid.

⁶ “Liberal” and “coordinated” market economies refer to the nature of politico-economic institutional arrangements governing the activities of economic agents. In liberal market economies, agents coordinate their activities primarily by way of competitive market arrangements. In coordinated market economies agents depend more heavily on forms of non-market relationships. See Hall, P., and Soskice, D. (2001), *Varieties of Capitalism: The Institutional Foundations of Comparative Advantage*, Oxford University Press.

⁷ Hall, op. cit.

⁸ Ibid.

⁹ Ibid.

¹⁰ Alexander, N. (2003), “Local-Global Links: International Financial Institutions (IFIs) and Local Governments”, a presentation to the Ford Foundation’s Local Governance Learning Group (LOGO) in Santiago, Chile.

¹¹ Speaking Notes for World Social Forum Event “GATS and the Future of Public Services” 25th January, Oxfam International, 2003.

¹² Hall, op. cit.

¹³ Sally, R. (2002), “Developing Countries and the Liberalisation of Services: Strategies for Market Access and Growth”, a report for the Commonwealth Business Council (CBC).

¹⁴ Ibid.

¹⁵ Krajewski, op. cit.

¹⁶ Ibid.

¹⁷ Ibid.

¹⁸ Health and Social Services, Background Note by the Secretariat, 18 September 1998, S/C/W/50, p. 10-11, No. 37-39 (emphasis added).

¹⁹ WTO, Market Access: Unfinished Business, Post-Uruguay Round Inventory and Issues Special Study No. 6, Geneva April 2001, pp. 123-124 (emphasis added).

²⁰ “GATS and Public Service Systems: the GATS ‘governmental authority’ exclusion”, International Branch, Ministry of Employment and Investment, Government of British Columbia, discussion paper, 2001.

²¹ Krajewski, op. cit.

²² Hartridge, D. (2000), “Service Trade and Globalisation: Governmental Services and Public Policy Concerns”, speech given to the European Services Forum.

²³ Krajewski, *op. cit.*

²⁴ GATS: Facts and Fiction, World Trade Organisation, 2001.

²⁵ The reader is referred to Krajewski (2001) for suggested amendments to GATS Article I:3.

²⁶ Article V states that the GATS “shall not prevent any of its Members from being a party to or entering into an agreement liberalizing trade in services between or among the parties to such an agreement, provided that such an agreement: (a) has substantial sectoral coverage; (b) provides for the absence or elimination of substantially all discrimination, in the sense of Article XVII, between or among the parties, in the sectors covered under subparagraph (a), through (i) elimination of existing discriminatory measures, and/or (ii) prohibition of new or more discriminatory measures, either at the entry into force of that agreement or on the basis of a reasonable time-frame, except for measures permitted under Articles XI, XII, XIV, and XIV bis.”