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# RESEARCH Paper

## Trade in Services and EPAs: The Way Forward for EAC

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## ***Executive summary***

An underlying phenomenon of international trade in goods is that none of it does occur without an aspect of services rendered to the process. In regional trade agreements, significant market opening commitments are made between parties than done under the multilateral context. Under the economic partnership agreement (EPA) between the European Union and East African countries (EAC), the EU, the world's most competitive services exporter, will be eagerly looking to gain substantial new opportunities in EAC services sectors than the EAC countries have committed at the WTO. And, to guarantee that new barriers will not be introduced in sectors that have not been committed or opened in the EAC EPA, the EU will most likely insist on including a standstill clause in the agreement. This paper explores some of the options which EAC countries and the EU should consider in moving forward the discussion on services liberalisation as part of their EPA.

Although there is more scope to expand the contribution of trade in services to development of EAC countries, this can only happen under a competitive and well regulated environment. However, the limited level of regulatory development and lack of functional competition law in the EAC countries; the limited competitiveness of local service providers; and, the limited knowledge on the readiness of services sectors for liberalisation, all suggest that the EAC should move forward cautiously on liberalising their services sector to the EU. It is not possible, therefore, to determine with certainty whether liberalisation of services sector under the EPA with the EU would kill the budding industries in the EAC region or will support and enhance their growth. All options, including agreement simply on development cooperation would therefore need to be explored and a more informed and strategic approach taken to ensure that services liberalisation promotes development in EAC.

Even where effective domestic regulation would be the most appropriate tool for EAC to overcome any anti-competitive practices from the EU, the tool should only be used to promote the realisation of national policy objectives without promoting trade protectionism.

However, as they juggle which services sectors or sub-sectors to offer to EU, before making any such commitment, the EAC countries would need first to define:

- a) their offensive interests: the services where they have high export potential (and where there exists effective regulatory framework) where they require export market in EU;
- b) their defensive interests: the sensitive services that are better not liberalised and best reserved for domestic suppliers (criteria for excluding such services must be clear);
- c) their FDI needs: the services with high potential but where they would require foreign investment or competition to increase efficiency and lower the cost of inputs; and, lastly,
- d) the non-sensitive sectors with relatively low export potential which they would not mind offering to any country at the WTO; but which they should offer in exchange for premium concessions, for instance, giving (d) in exchange for (a).

Due to their inadequate preparations, the EAC should request for sufficient time to carryout all the necessary studies to explore the implications of a services liberalisation for their economies, develop suitable strategies and negotiate terms that will promote their development. Most importantly, both parties should ensure that development and poverty reduction objectives stay central to the negotiations, and the EU to extend maximum flexibilities to the EAC in relation to services, in recognition of the terms of GATS article V and the limited levels of development of these countries. If at all, the EU should allow EAC countries, if they do not wish to negotiate a full services agreement, to conclude an EPA without such terms and but allow EAC the access development assistance to support the development of their services sector.

## I. Introduction

With an interim Economic Partnership Agreement (EPA) on trade in goods having been agreed between the European Union (EU) and the countries of East African Community (EAC), attention in the current phase of negotiations has turned to the remaining issues in the negotiations to conclude a comprehensive agreement that include services liberalisation.

The EU is the most competitive services exporter in the global economy; it understands its strength and competitiveness in the area of services trade, thus agreeing terms on services is high up on their agenda. On the other hand, EAC services sectors are still weak (the EAC's share of global services exports is even less than its share of global goods exports); the region is ill prepared in terms in-depth studies needed to explore the implications of a services liberalisation for their economies; hence, negotiating terms on services with the EU poses major challenges.

Furthermore, a regional free trade agreement suggests that parties make significant commitments that they have under the multilateral framework under the authority of world trade organisation (WTO). In this regard, the EU, the world's most competitive services exporter, will be eagerly looking to gain substantial new opportunities in EAC services sectors than the EAC countries have committed at the WTO.

This paper explores what is at stake for the EAC in negotiating services with the EU, options for moving forward in these negotiations and the current state of play in EU-EAC services negotiations.

## 2. Importance of the services sector in the EAC

According to the World Bank's estimate, the services contribution in the Eastern and Southern African (ESA) region averages 50percent to the GDP of many countries<sup>1</sup>. As can be seen in the table 1 below, services are also very important to the economies of all the EAC countries, especially in Burundi, Kenya and Uganda where they contribute over 45percent of GDP and have been growing in recent years.

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<sup>1</sup> World Bank WDI 2005, online available <http://www.worldbank.org>.

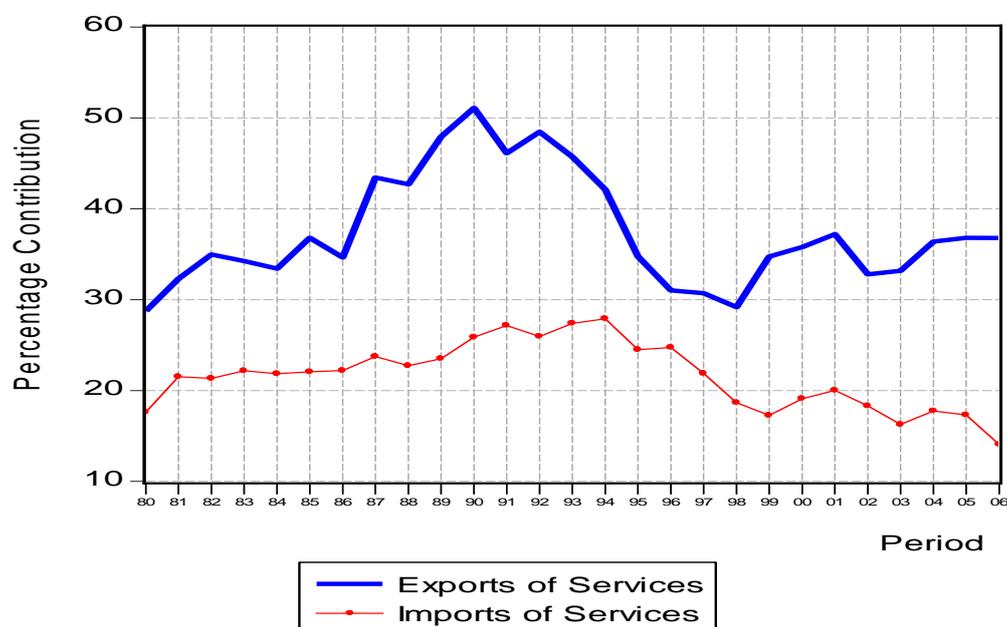
Table 1 – Importance of services to EAC economies

Country	Services as % of GDP		
	2000	2005	2006
Burundi	40.8	45.1	-
Kenya	50.7	54.4	54.1
Rwanda	38.1	37.3	37.8
Tanzania	39.2	37.0	37.3
Uganda	42.4	48.4	49.2

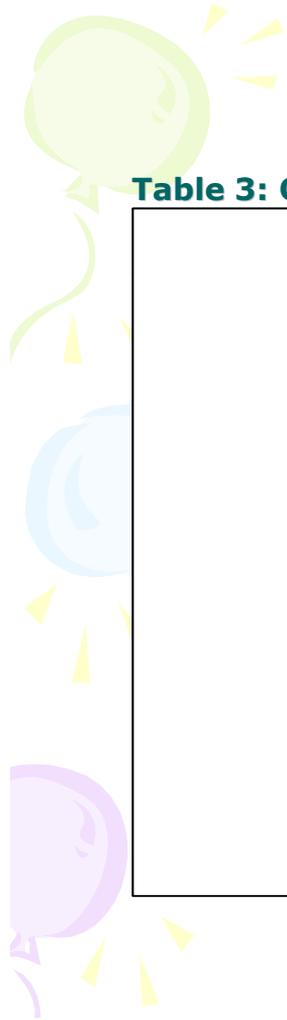
Source: World Bank, World Development Indicators

In Kenya, services sector has been the most important sector since independence as seen in the contribution to trade in goods and services (table 2), employment (table), GDP, backward and forward linkages with other sectors of the economy, foreign exchange earnings from exports and remittances, and attracting FDI.

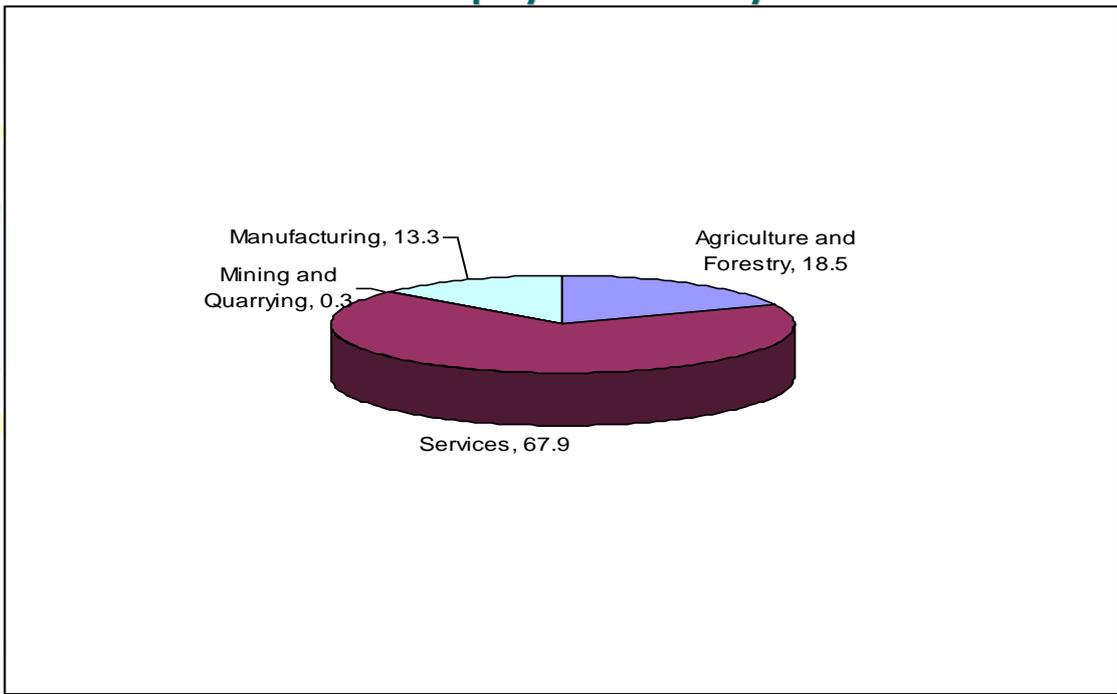
Table 2: Contribution of Services to Trade in Goods and Services in Kenya



Data from UNCTAD



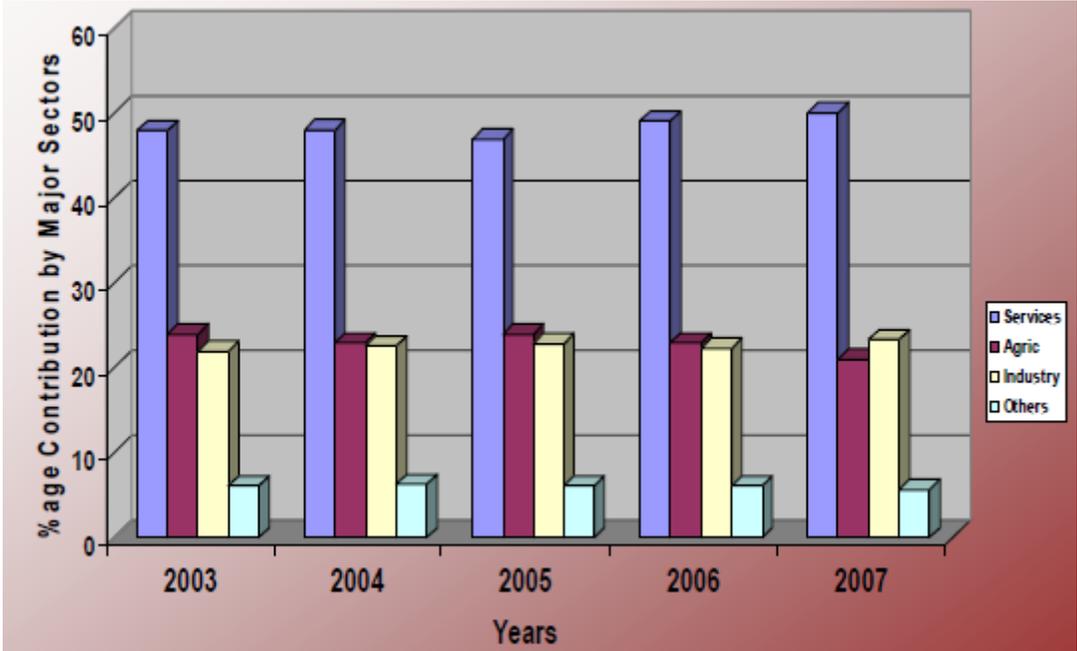
**Table 3: Contribution to employment in Kenya**



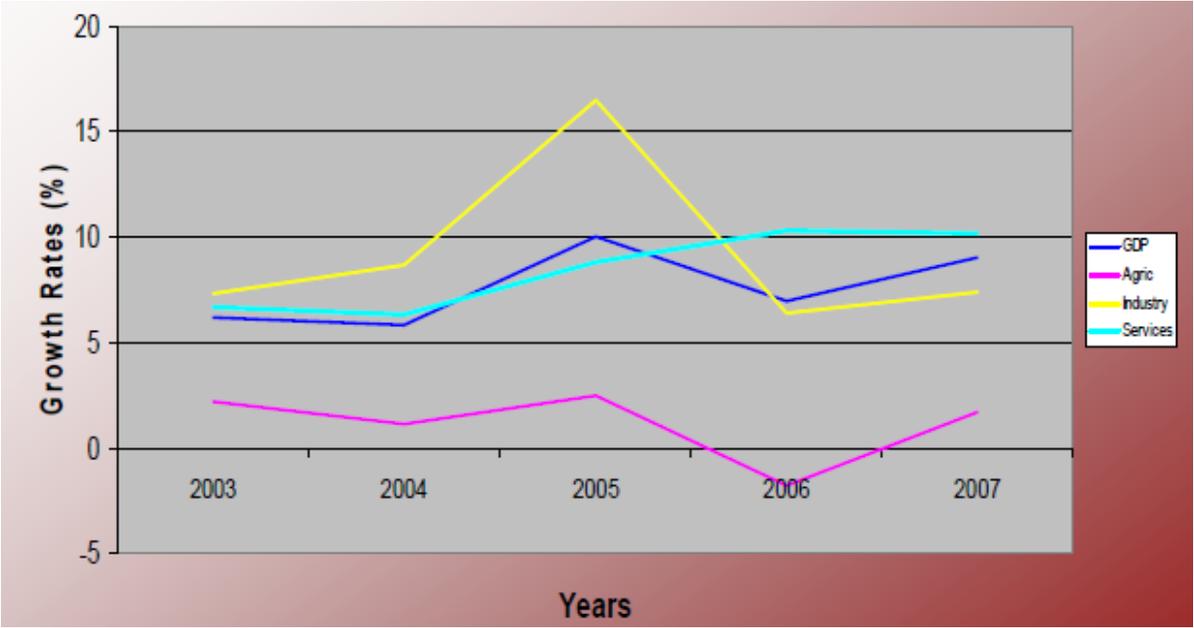
Source: CUTS 2007

In Uganda, the sector is the main contributor to the country's GDP (table 4) and whenever the country's GDP has been on a negative growth, attributed mainly to falling growth in the agricultural sector, the growth of services has been offsetting some of the negative growth experienced in the country's economy (table 5)

**Table 4: GDP by Major Economic Activities in Uganda (Current Prices): 2003-2007**



**Table 5: Growth Rates of GDP and Main Sectors (2003-2007)**



When it comes to thinking about the importance of the services sector to exports, only 3 of the EAC countries had services exports above \$200m in 2005, Kenya, Tanzania and Uganda (table 6). For these countries the primary sectors responsible for these exports were business and communications; although Uganda also had exports in computer and information services.

**Table 6 – Main services exports of EAC countries**

Country	Total services exports	Main (worth more than \$30m) commercial services exports besides travel and transport (by core sector)
Kenya	2000: \$993m	-
	2005: \$1,886m	Communications (\$178m)
Tanzania	2000: \$6128m	Other business (\$97m)
	2006: \$1,483m	Other business (\$110m), Communications (\$32m)
Uganda	2000: \$213m	-
	2006: \$464m	Other business (\$33m), Computer / info (\$32m)

Source: UNCTAD statistical handbook

### 3. Preparedness of EAC services sectors for liberalisation<sup>2</sup>

More than ever, EAC countries need accessible and affordable infrastructural services like water, transportation, energy, and ITC services as well as education and health to improve their productivity, generate new jobs and increase earnings. Services are thus essential in improvements of human welfare through improvements in provisioning of both social and economic services, which is central in achieving the MDGs. However, most social and economic services remain inaccessible, prohibitively expensive, or when accessible, are of low quality and unsuited to the needs of consumers (World Bank, 2003).

In the following paragraphs, we have elaborated on the state of preparedness and the main challenges facing services sector in EAC which should be taken into account while the region considers liberalising the sector under the EPAs. The main challenges discussed are the region's weak supply capacity owing *inter alia* to a wide array of infrastructural, technological, financial and regulatory constraints as well as human resource constraints. Some of these constraints could also be attributed to the fact that for a long time, services were viewed as non-tradable, and were therefore monopolised by State, especially in the provisioning of services under the sub-sectors like health, education, banking, telecommunication, and transport. Although the three EAC countries have developed some significant services exports it is likely these services exports are accounted for by a small number of (probably foreign owned) operations and / have limited competitiveness at the global (or even regional) level. It is

<sup>2</sup> This section is mostly drawn from RTFP (2009)

therefore vital that development efforts are made under the EPAs and focus given on how to better supply such services in the poorest countries by addressing the developmental constraints identified in this study.

### *Regulatory and Institutional Constraints*

The aim of liberalisation of services sector is to contribute to economic gains by promoting competition, which in turn promotes efficiency and lower prices from which consumers gain and markets expand. However, for EAC countries the gains from past liberalisation over the last two to three decades have been stifled due to lack of suitable regulatory and institutional arrangements and so markets have not been disciplined and the private sector has not delivered on its potential. For these reasons competitiveness has not been developed in most EAC services sectors and most public monopolies which were privatised have simply turned into private monopolies. Secondly, there hasn't been adequate legal protection to give the private investors the confidence to invest even after the last waves of liberalisation. As Mattoo and Zanini (2007) also state, even if liberalisation were to promote private investments, but without provisions for consumer protection, such investments may simply end up harming consumers through production of unsafe goods; and, without access widening policies liberalisation may end up creating a dual services sector where private markets only serves an elite/affluent sections of the society and not the more marginalised.

The necessity of such complimentary reforms and the delicate challenge of creating effectively functioning and equitable markets mean that services market opening in EAC should be undertaken gradually, sequenced with other necessary reforms and informed by knowledge of legal gaps that need to be addressed. This final point highlights the importance of undertaking comprehensive assessments of the services sectors to identify what their capacities are and what regulatory and institutional measures will best support their development.

Recent analysis of the regulatory framework in EAC Partner States illustrates that the EAC countries have some relevant regulatory frameworks in place, however many of these are inadequate even in sectors that have already been liberalised (RTFP 2009). However, it is also clear that there are still significant regulatory gaps in the EAC countries, which pose challenges for moving ahead on liberalisation.

Research by the Regional Trade Facilitation Program (RPTF 2009)) and CUTS (CUTS 2006) also show how competition regimes in the EAC countries are non-existent (see table 7) or where they exist have limited capacity to deliver on their mission of protecting competition. CUTS' work on consumer regimes in the EAC region also highlights how consumer protection laws and systems are still weak, suggesting these need to be strengthened further if the private sector is to be disciplined appropriately.

**Table 7 – Summary of regulatory environment in EAC countries**

Cross-cutting laws	EAC Partner States									
	All EAC states									
East African Competition Act	All EAC states									
	Burundi		Kenya		Rwanda		Tanzania		Uganda	
	Yes	No	Yes	No	Yes	No	Yes	No	Yes	No
Immigration law and regulations	X		X		X		X		X	
Competition law and regulations				X			X			X
Investment law and regulations	X		X		X		X		X	
Company law and regulations										
Public procurement law and regulations			X		X		X		X	
Intellectual property rights law and regulations			X				X			

*Source: ComSec (2008)*

*Infrastructural, Technological and Human Resource Constraints*

The analysis in this section has thus far focussed on legal and regulatory issues, but then there are also clearly issues relating to the competitiveness of local services providers that need to be taken into account if liberalisation is not to simply wipe out local providers in favour of foreign ones. Even a cursory look at the level of infrastructure, human resource and technological development of many services sectors in EAC countries suggests that local producers face huge challenges. This highlights the importance of governments and donors in providing support to improve the competitiveness of local producers as they open up to Foreign Service providers.

The analysis presented in this section suggests that the EAC are not as well prepared for services liberalisation at present, and that significant investments in regulatory and competitiveness development would need to be elaborated comprehensively and undertaken upfront if liberalisation is to deliver its promised benefits. It also suggests that any liberalisation undertaken should be done so gradually and sequenced effectively with other complementary measures and reforms.

*Lack of knowledge on existing capacities, levels of competitiveness and challenges*

One factor which makes assessing the competitiveness of EAC services sectors difficult is the fact that little is actually known about their levels of competitiveness and the measures that are required to support them to prosper. This technical work still needs to be done and should be pre-requisite of any serious consideration of negotiation with the EU. In addition, the legal parameters and implications of the services negotiations need to be fully understood by the EAC as they suggest that if formal rules on services are agreed they will involve significant commitments and therefore serious implications for the future of their services sectors. The legal parameters and implications of the services negotiations are the topic of section 4.

What is also clear is that there is still insufficient knowledge about the challenges facing services sectors in the EAC and the measures therefore required to support them to prosper. The main challenge facing EPA negotiations is lack of information on their services sectors and lack of capacity to access and utilise market information. The EAC data base on services sector is poor and unreliable and therefore need to be addressed as a matter of priority. Besides, these countries lack the necessary capacity that can help them in making revised offers. Other challenges include: high regulation restricting market access of interest to EAC in European markets; unfair competition from EU-based multinational services providers given their history, size and connection to multilateral and bilateral agencies that provide development aid to EAC; inadequate skills in information communication technology (ICT) industry and less developed basic ICT infrastructure; limited skills in international business consulting; low penetration of EAC-owned companies in its own regional market and EU markets; lack of venture capital finance service investment targeting export market; high logistics costs; cumbersome documentation; variations in regulations and laws across EAC countries affecting trade in services. It is therefore important that further work is done to explore all the challenges facing EAC services sectors and that any decisions on market opening are taken on the basis of such analysis suggesting it is suitable (RTFP 2009). It will also be important for the East African markets to harmonise regulations and have capacities built at that level first before venturing into serious negotiations with the EU on opening the services sector. A development-oriented EPA would be that which lays emphasis on improving EAC's infrastructure development, regulatory framework, access to finance and credit access to market and training (Janet Abila).

#### **4. The GATS Framework and What EPAs commitments will involve<sup>3</sup>**

Before we move to the main analysis in this section, let us state at the outset that EAC countries do not need to negotiate and agree any terms on services in an EPA in order for their trade with the EU to be WTO-compatible. Therefore, unlike the EPAs negotiations on goods, the EAC could walk away from any services negotiations with the EU without contravening WTO law.

However, because the parties have committed to include services in their EPA, provisions of the WTO's general agreement on trade in services (GATS) have to be invoked to govern such agreement. Accordingly, liberalisation of services between EAC and EU must include "substantial sectoral coverage" regarding the number of sectors included; the modes of supply and the volume of trade affected (Article V of the GATS)<sup>4</sup>. EAC would also be obliged to extend national treatment to Foreign Service suppliers from EU by eliminating "substantially all discrimination".

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<sup>3</sup> This section is drawn mostly from ComSec (2008)

<sup>4</sup> The "substantial coverage" is qualified by a footnote to GATS article V:1(a) which states that "agreements should not provide for the a priori exclusion of any mode of supply".

If agreed, the agreement must be implemented “either at the entry into force of that agreement or on the basis of a reasonable time-frame”.

Generally, the GATS covers all services delivered through the four modes of supply (see Box 1) and all measures affecting trade in services. Its most important principles include non-discrimination, (i.e. most favored nation (Article II), national treatment (Article XVII) and transparency in market access (Article III)) and provides rules on domestic regulation (Article VI), mutual recognition (Article VII), general exceptions (Article XIV), guiding principles on progressive liberalisation (Article XIX), specific commitments in schedules (Article XX), compensatory adjustment in cases of withdrawal of concessions (Article XXI), dispute settlement provisions (Article XXIII), denial of benefits (Article XXVII). For developing countries, the objective of GATS (as stated in Article IV) is to ensure that the countries (especially the least developed) secure a better share of the growth in international trade. This is to be achieved by:

- Strengthening the domestic services capacity of developing economies and their efficiency and competitiveness through access to technology on a commercial basis;
- Improving their access to distribution channels and information networks; and
- Providing them with the flexibility to select the sectors of export interest to them in which they wish to undertake commitments fully or partially and the conditions they wish to attach (GATS Article XX)<sup>5</sup>.

The implications of the GATS provisions are therefore substantial and challenging for the EAC countries. If they agree to negotiate services they will have to engage in substantial market opening with the EU across all modes and sectors, which will require them to decide whether they are able to open up such a swathe of their service sectors. However, EAC could make use of the flexibility provided by Article XX by deciding the sectors to offer and the levels of such offers; they should be allowed to progressively extend market access to EU in line with their development situation; attach conditions aimed at achieving their increased participation in international trade<sup>6</sup>; and policy space to regulate in the public interest, and in line with national policy objectives<sup>7</sup>.

Such flexibilities were taken advantage of by CARIFORUM in their services agreement with the EU. The CARIFORUM signatories notified a range of sectoral limitations especially in relation to modes 3 and 4, with a much lower level of limitations notified for modes 1 and 2. Interestingly, limitations ranged from notifying modes that were unbound, to notifying phase-in schedules (including delaying implementation until 2022, in some sectors). The extent to which such flexibilities will suffice for their interests will depend on the degree to which they can afford to open up and the willingness of the EC to extend such flexibilities to them.

The GATS, however, does not cover services which are supplied in the exercise of governmental authority, that is, neither on a commercial basis nor in competition with one or more service suppliers, are excluded from the scope

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<sup>5</sup> Such conditions could include limitations and conditions on market access, national treatment, undertakings relating to additional commitments, timeframe for implementation, or the date of entry into force of any commitment in a schedule of commitments. This is seen to be sufficient to offer developing countries additional options to protect their sensitive service sectors from liberalisation.

<sup>6</sup> See Article XIX (2) and Article IV of the GATS

<sup>7</sup> See Preamble to the GATS

of the Agreement (Article I (3) (b) and (c) of the GATS). Typical examples of services that are provided in the exercise of governmental authority are *police services, and the monetary operations of central banks*. It may be argued that this exclusion precludes, in many instances, the GATS' application to the health sector, since most health services are provided by governments. However increasingly, health services are provided by private entities as well, arguably in competition with government in some cases. In such cases, the exemption would not apply. It is also true that many public services (including health), have since been unilaterally liberalised through privatisation processes, owing to developing country responses to the International Monetary Fund' structural adjustment programs.

### Box 1: Four modes of supplying services

#### ***Mode 1: Cross-border***

In mode 1, it is the service, not its supplier or its consumer, that moves from the territory of one WTO Member into the territory of another. For example, an EU stock-broking firm buying or selling shares for a Kenyan resident over the Internet. The EU is, therefore, exporting financial services across the border to Kenya and Kenya is importing the same from the EU.

#### ***Mode 2: Consumption abroad***

In this case, the consumer moves from his country to the territory of another WTO Member and gets service in that territory. For instance, a Kenyan fee-paying student may travel to EU to study at a European university. Thus, the EU is exporting its education services to Kenya and Kenya is importing education services from the EU.

#### ***Mode 3: Commercial presence***

Under this mode, the service is traded by a service supplier moves his capital and sets up a commercial presence typically through foreign direct investment in the

## 5. What will the EU's approach to services negotiations likely be?<sup>8</sup>

### 5.1 EU defensive interests

The services sectors of the EAC countries are still quite weak and would struggle to be able to compete with competitive EU service providers for the EU market. The most significant area of services for the EAC is therefore movement of workers, mode 4. Despite the best efforts of developing countries to negotiate Mode 4 opportunities for lower skilled workers, at the WTO the EC's current Mode 4 commitments and its GATS offer apply only to higher skilled workers, i.e. those with a university degree or a professional qualification or even professional experience.

The Caribbean countries were able to negotiate some substantive Mode 4 concessions from the EU in their EPA. However, these were achieved mainly through making substantial commitments of their own in terms of the number of sectors and modes they liberalised, and these opportunities are only available to skilled workers.

There is therefore a serious question about what concessions in sectors / modes of interest to them the EAC will be able to extract from the EU during these negotiations; and whether the price in terms of reciprocal concessions that would be required to extract them would be worth paying.

### 5.2 EU Offensive interests

A hypothesis on the likely direction and extent of EU offensive interests in relation to services negotiations with the EAC can be developed by analysing the approach that the EU has taken to WTO, CARIFORUM EPA and other RTA services negotiations.

WTO negotiations - The EU has been one of the most active participants in the WTO services negotiations. Its main requests in these negotiations were in business, financial, distribution (including retail), tourism and construction services and telecommunications. Looking specifically at its requests to LICs, its main interests were in telecommunication, business, financial, transport and professional services (WDM 2003). It therefore seems likely that the EC will be looking to open up opportunities in these sectors of the EAC countries.

CARIFORUM EPA negotiations: The EC-CARIFORUM EPA contains an extensive services chapter and includes terms requiring both parties to liberalise substantial areas of their services sectors. On signing the agreement both

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<sup>8</sup> Ibid

parties agreed to a standstill in applying additional protectionist measures to their services sectors. They also agreed to apply any more favourable services terms agreed with third countries to each other (most favoured nation clause).

In terms of sectoral coverage, the EU agreed to commitments in over 90% of its services sectors, with most CARIFORUM countries agreeing to commitments in 65% (for LDCs) to 75% (for non-LDCs). However, the Dominican Republic agreed to commitments in 90% of sectors and the Bahamas and Haiti deferred making services commitments until mid 2008 (CRNM 2008a).

**Table 8 - Summary of CARIFORUM-EU EPA services terms**

	EUROPEAN UNION	CARIFORUM
<b>Market Access</b>	Over 90%	65%-75%; 90% by Dominican Republic; Belize and Haiti still to submit (mid-2008)
<b>Main sectors opened</b>	Business, Construction, Distribution, Environmental, Financial, Transport, Tourism and Recreation services	Business, computer and related, research and development, environmental, management consultancy, maritime transport, entertainment, tourism
<b>Main limitations</b>	Mode 1, Mode 4	Mode 3, Mode 4
<b>Mode 4 commitments</b>	New commitments made for professionals in 29 sectors, independent professionals in 11 sectors and entertainment	Limited
<b>Most Favoured Nation</b>	Applies to agreements with third countries responsible for more than 1% of world trade (CARIFORUM had demanded this be 3%) or regions responsible for more than 1.5% of world trade (CARIFORUM had demanded this be 4.5%)	
<b>Future liberalisation</b>	To be discussed in 5 years	
<b>Development Cooperation</b>	Specified on cultural industries, the tourism sector (including on tackling anti-competitive practices), meeting environmental challenges meeting the technical and health production standards required by global markets	

*Source: ComSec (2008)*

Other RTA negotiations - The terms of other EU FTAs illustrate some quite varied and in many ways quite defensive models that the EAC could follow in negotiating services with the EC. The EAC could - like South Africa - choose to make no immediate commitments on services, agree to weak terms on discussing future commitments and still

demand significant economic and financial support from the EC. Alternatively, they could - like Mexico - make a commitment to only agree full services terms following the completion of the GATS negotiations, an approach that would allow such an agreement to be consistent with the overall multilateral environment.

**Table 9 – Summary of terms of other EU FTAs**

	<b>MED agreements</b>	<b>TDCA, South Africa</b>	<b>Global Agreement, Mexico</b>	<b>Association Agreement, Chile</b>
<b>YEAR SIGNED</b>	1995-2002	1999	1997	2002
<b>Most Favoured Nation</b>	Yes, general provision	Only for commitments under GATS	Yes, general provision	Not included as general provision
<b>Market access</b>	No	No	General provision	General provision, bans several reservations
<b>National treatment</b>	For right of establishment only in Jordan (with reservations); and maritime transport	Only for commitments under GATS	General provision	General provision
<b>Government procurement</b>	No	No	Yes	Yes
<b>Mode 4</b>	Provisions vary, but no more than GATS; article on further dialogue	No	Limited	Rules of movement to be reviewed 2 years after entry into force of agreement

*Source: ComSec (2008)*

However, in referencing the cases of South Africa and Mexico, it is important to note that these agreements were negotiated in 1999 and 1997 respectively and it is widely accepted that the EU's approach to RTAs has become more mercantilist since then.

The EU's 2006 Global Europe strategy (EC 2006), which outlines the EU's strategy for promoting its economic competitiveness globally, provides a clear illustration of this current approach. Amongst other elements this strategy identifies the importance of opening markets in key economies for EC exports, particularly for the services sector, through negotiating ambitious bilateral agreements. It specifically notes how previous FTAs negotiated by the EC have been motivated by development objectives and geopolitical concerns, and that a new market-opening approach to bilateral agreements is required.

### 5.3 EU approach to development cooperation

One important element of services negotiations which has attracted the attention of ACP policy-makers is the potential for such an agreement to include a commitment by the EU to provide development assistance and other forms of cooperation to help the ACP develop the competitiveness of their services sectors. Although this element of the negotiations does provide opportunities, the case of the EU-CARIFORUM EPA shows that such terms are unlikely to include any concrete and specific commitments, but mainly best endeavour general commitments. In addition, the case of the EU-South Africa FTA shows that such support could be provided without any market opening commitments being made by the EAC.

## 6. State of play of services negotiations in EAC

### 6.1 State of Play at the WTO

Greater policy reforms in EAC started with the SAPs in mid 1980s with rapid change in the 1990s which brought in initiatives such as liberalization, privatization, and deregulation reforms in most EAC countries. Effects of these initiatives vary across EAC but they have left Uganda a more opened economy to trade and investment than any other EAC country. But out of the Uruguay Round (UR) concluded in Casablanca, most EAC countries were forced to go very substantially in their commitments and their commitments during the SAP does seem not to have been recognised as satisfactory enough, considering their development situations. Kenya's initial offers after the UR include tourism and communications, and later on with supplementary offers on financial services and telecommunication.

However, it is Uganda that has substantially liberalised its services sector under the WTO. The country permits foreign investors to hold up to 100% equity subject to limits on individual share ownership which is currently set at a maximum of 30% in sectors such as: *Banking, Insurance, Telecommunications, Tourism, stock brokerage, construction of residential buildings and roads, water supply, mass transportation, production and distribution of energy, professional services, and, establishment of liaison offices or local branches of foreign companies*

Under the request and offer process, which is the main method of the negotiations at the WTO, EAC countries have submitted requests and have also made offers to many WTO members. Kenya, for instance, submitted requests to 17 WTO members which include fellow African countries like Burundi, Rwanda, Mauritius, South Africa, Zambia, Swaziland, Egypt, Lesotho, Namibia, Malawi, Zimbabwe, Mozambique, Botswana, and other countries such as Canada, Norway, United States of America, and the European Union. Most of these requests were related to movement of natural persons commonly referred to as Mode 4 where Kenya is deemed to have export potential. Likewise Kenya received requests from some WTO members. The requests received, particularly, from

the USA and the European Communities were very comprehensive in terms of sectoral coverage and modes of supply. See appendix 1 for list of EU requests to Kenya under the WTO and table 10 in the appendix 2 for a list of Kenya's GATS Commitments.

## **6.2 State of Play in the EAC-EC EPA Negotiations**

Negotiations on services between the EAC and EC are continuing, with all options still on the table. The EC has already submitted a text which outlined its interests in services negotiations with the EAC partner states. The EC in its text has identified areas for negotiations in trade in services. These areas include: *Movement of natural persons; Computer services; Postal and Courier services; Telecommunication services; Financial services; Maritime transport services; Electronic commerce; and Technical cooperation*

In the services sectors mentioned above, the EC wants EAC states to eliminate measures affecting trade in services and also offer national treatment to European companies supplying services locally.

The EAC have made a counter text in response to the EC text. At the last meeting of the EAC preparatory meeting for the 7<sup>th</sup> EAC-EC EPA, technical officials' negotiations held in the first week of March 2009 in Kigali, Rwanda, it was agreed that the EAC states should submit a joint request to the EC highlighting their interests in services negotiations. However, in the case of offers, it was agreed that each EAC states would have their own schedules of services commitments to the EC consistent with their individual levels of development and national development goals (a flexibility granted by GATS Article XX).

It was also noted that the EAC states have limited export interests in market access in services due to capacity constraints. It was, therefore, recommended that EAC-EC negotiations in services should ensure effective support from the EC to address supply-side constraints and the establishment and strengthening of regulatory legal frameworks and institutions. The sectors that have been analysed to inform Kenyan positions in services include: *Distribution, Transport, Tourism, Environmental, Banking and Insurance, Energy, Education, and ICT.*

## **6.3 State of Play within the EAC Common Market Negotiations**

The EAC partner states have agreed to negotiate under the common market the liberalisation of trade in services in four sectors: *Transport services except Marine and Railways services; Business services; Financial services; and Telecommunication services*

The negotiations in these sectors have started at the technical level.

During the joint meeting of the EPA experts and the EAC common markets High Level Task Force on trade in services, it was observed that:

- The EPA and the EAC common market negotiations processes are taking place concurrently and therefore the need to share information on a continuous basis to ensure coherence and effective coordination. This was important in order to ensure that the EPA process does not jeopardise the opportunities that existed at the regional level for the EAC states.
- The EAC partner states should offer a fewer number of sectors and less favourable treatment to EC than what EAC states should offer to each other. In this respect, under the EAC common market negotiations, a substantial number of sectors should be covered more than the four sectors that have been agreed upon. There was convergence to add Tourism, Distribution, and Education services on the list of those sectors to be negotiated. This was important in terms of deepening regional integration among the EAC partner states. This makes in total seven sectors set for liberalisation among EAC partner states:
  - a) Transport services except Marine and Railways services;
  - b) Business services;**
  - c) Financial services;
  - d) Telecommunication services;
  - e) Tourism;
  - f) Distribution; and,**
  - g) Education.**

EAC partner states have agreed that their commitments on these sub-sectors are to be ready by 31<sup>st</sup> August 2009.

## 7. Conclusions and Way Forward

Given the state of development of the services sectors in the EAC countries, the developmental and competitiveness challenges of EAC services sector, the **competitiveness** of the EU in services, the extensive commitments a services agreement will involve and the limited value of concessions they can hope to extract in services, the EAC need to approach the EPA negotiations very carefully. For these reasons the EU also need to show maximum flexibility to the EAC in any services negotiations that occur in line with the flexibility given in the GATS Article XX to all developing countries.

What follows are recommendations for the EAC and EU in the ongoing EPAs services negotiations.

For the EAC:

- to explore all options available to them in negotiating services with the EU, including the option of an agreement simply on development cooperation and not rules.
- to scale-up their efforts to assess the capacity and competitiveness of their services sectors; the potential legal implications and opportunities in signing a services agreement with the EC; and identify their negotiating priorities

- to present a united front in demanding maximum flexibility in all aspects of the negotiations from the EC
- to demand that the EC makes clear and accountable commitments in relation to development assistance and cooperation in any agreement
- to focus on what it wants from EC first then define its market access requests
- to relate its negotiations to all national and regional development plans or policy statements and sectoral plans. This is supposed to drive EAC's approach in trade and other negotiations.
- As a strategy, no EAC country should schedule an entire sub-sector unless it is entirely sure that it is prepared to open to competition any new services that may evolve in that sub-sector. This is the lesson from the Antigua Gambling case since betting and gambling was included in the "Other" section of Sporting services. EAC must, therefore, diligently use the detailed CPC when scheduling commitments. They have to check that they have scheduled anything at the two-digit level as they need to be as specific as possible.
- There would be need for all EAC countries to do exhaustive review of their laws to ensure that they find ALL or any restrictions on market access or national treatment that exist. But should any country chose to open a sector in which there is no domestic legislation or regulations or inadequate regulations, it would need to set the date for liberalisation of that service in the future with the aim of getting the regulatory regime effectively in place by then. Such offers would need to be complemented by getting firm commitment from EC they will provide funding to support the development of regulatory regimes as may be required.
- The GATS Article V would be critical for any consideration in deciding the level of liberalization to settle for. But one would have to note that Art V requires that new barriers should not be introduced in bilateral trade between the two parties to an RTA or FTA later on; it also recognises that countries in an RTA/FTA may need to commit to liberalise beyond what they have at the multilateral level. This means that the EC will most likely want a standstill clause or guarantee that new barriers will not be introduced in sectors that have not been committed or opened in the EAC EPA and would push EAC to go beyond their WTO commitments. A good example is in the CARIFORUM EPA where although small states made very light commitments in the EPA (between 50--60 percent sectoral coverage in terms of CPC listing) they had to include a standstill clause. EAC countries will have to figure out what they can get away with, and what meets EC bottom line. It is likely, therefore, that although smaller EAC economies may get off easy in terms of what EC would request from them, the little they offer will have to be safeguarded by a standstill close as EC pushes to get more offers from the bigger EAC economies that provide attractive market and big returns for EU businesses/companies.
- EC is interested in large infrastructural services; its requests to Kenya include a wide range of business services, telecoms, transport, maritime, financial, construction, distribution, etc. So, although Kenya may escape in most other areas, it will be required under the EPA to offer what can be defended to definition or concept of "substantial sectoral coverage," notwithstanding the developing country flexibilities in GATS Art V. But scheduling should not be done only on a defensive basis. You must target sectors where there is high export potential to open which require foreign investment (mode 3) or competition to increase efficiency and lower the cost of inputs to services and manufacturing, etc; you must also identify those that are non-sensitive and with relatively low export potential and dangle them for liberalisation in exchange for better concessions from EC.
- GATS Art V says that in principle you should not exclude any modes, but EAC countries should be witty enough in deciding how they calibrate their offer terms of the different modes to fine tune their market access commitment.
- Finally, EAC should not make offers in a vacuum as offers should be linked to requests. EAC would have to be entirely sure what they want from the EC and hold out on offers in areas of interest to EC until they get clear concessions of interest to them. Individual EAC countries may not consider that they have great bargaining power but this increases as they make requests as a group, even though they may provide different offers in the groups offer. But EAC should not forget that the EC wants all ESA and SADC states to come on board with full EPAs. So, the strategy of holding out on what EC is interested in may be of some value for them in the negotiations because EC is likely to concede.

- On a more technical front, EAC negotiators must read carefully and know in detail all the documents on scheduling (Guidelines and revisions to that and notes) prepared by WTO secretariat.

For the EU:

- to ensure that development and poverty reduction objectives stay central to the negotiations, as demanded by the Cotonou Partnership Agreement
- to extend maximum flexibilities to the EAC in relation to services, in recognition of the terms of GATS article V and the limited levels of development of these countries
- to allow the EAC sufficient time frames to explore the implications of a services agreement for their economies, develop suitable strategies and negotiate terms that will promote their development.
- to offer clear and accountable commitments in relation to development assistance and cooperation in any services agreement
- to allow any ACP country that does not want to negotiate a full services agreement to conclude an EPA without such terms and access development assistance to support the development of their services sector.

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## 9. Appendices

### Appendix 1: List of services sub-sectors where EU has made requests to Kenya

- 1. Business Services:
  - 1.A.a Legal services (861),
  - 1.A.b. Accounting and bookkeeping services (862),
  - 1.A.e. Engineering services (8672),
  - 1.A.f. Integrated engineering services (8673),
  - 1. B.a-to-e. Computer and related services (841-845+849),
  - 1. F. Other Business Services
    - 1.F.a. Advertising (871),
    - 1.F.b. Marketing research (864010),
    - 1.F.c. Management consulting services (865),
    - 1.F.d.Services related to management consulting (866),
    - 1.F.e. Technical testing analysis services (8676),
    - 1.F.m. Related scientific and technical consulting services (8675),
    - 1.F.n. Maintenance and repair of equipment (not including transport equipment (633+8861+8868),
- 3. Construction and related engineering services
  - 3.A. General construction work for buildings (512)
  - 3.B. General construction work for civil engineering (513)
  - 3.C. Installation and assembly work (514+516)
  - 3.D. Building completion and finishing work (517)
  - 3.E. Other (511+515+518)
- 4. Distribution Services
  - 4.B. Wholesale trade services (622, 6111+6113+6121)
  - 4.C. Retailing services (631+632, 6111+6113+6121+613)
- 6. Environmental Services
  - 6.A. Water for human use and waste water management
    - This includes water collection, purification and distribution services through mains, except steam and hot water, and,
    - 6.A.Waste water services (9401)
  - 6.B. Solid/hazardous waste management (9402) where they are interested in:
    - Refuse disposal services (94020), and
    - Sanitation and similar services (94030)
  - Protection of ambient air and climate where they are interested in:
    - Services to reduce exhaust gases and other emissions and improve air quality (94040)
  - Remediation and cleanup of soil and water where their main interest is:
    - Treatment, remediation of contaminated/polluted soil and water (part of 94060)
  - Protection of biodiversity and landscape where their main interest is:
    - Nature and landscape protection services (part pf 94060)
  - Other environmental and ancillary services where they are interested in:
    - Other environmental protection services not classified elsewhere (94090), only with respect to environmental impact assessment impact and environmental risk analysis
- 7. Financial services
  - 7.A.a-to-d. All insurance and insurance-related services (8121, 8129, 81299, 8140) to be opened variously in different modes



SECTOR-SPECIFIC COMMITMENTS	SPECIFIC ACTIVITIES AND (CORRESPONDING CPC)
	<ul style="list-style-type: none"> <li>i. voice mail (7523<sup>**</sup>),</li> <li>j. online information and database retrieval (7523<sup>**</sup>),</li> <li>k. electronic data interchange (EDI) (7523<sup>**</sup>),</li> <li>l. enhanced/value-added facsimile services incl. store and forward, store and retrieve (7523<sup>**</sup>),</li> <li>m. code and protocol conversion (n.a.),</li> <li>n. online information and/or data processing incl. transaction processing</li> <li>o. other <ul style="list-style-type: none"> <li>▪ internet and internet access services,</li> <li>▪ satellite based communication (mobile services, cellular/mobile telephone, mobile data services, personal communications services, paging),</li> <li>▪ terrestrial based communication (mobile services, cellular/mobile telephone, mobile data services, personal communications services, paging)</li> <li>▪ fixed satellite services (for public use),</li> <li>▪ vending of telecommunications terminal equipment<sup>1</sup>,</li> <li>▪ installation and maintenance of telecommunications terminal equipment<sup>1</sup>.</li> </ul> </li> </ul>
D. Audiovisual	<ul style="list-style-type: none"> <li>a. Motion picture and video tape production services excluding distribution services (9611)</li> <li>b. Motion picture projection services (9612)</li> </ul>
7. FINANCIAL SERVICES	
A. All insurance and insurance-related services (812 <sup>**</sup> )	<ul style="list-style-type: none"> <li>a. Life, accident and health insurance services (8121),</li> <li>b. Non-life insurance services (8129),</li> <li>c. Reinsurance and retrocession (all classes) (81299<sup>*</sup>)</li> <li>d. Services auxiliary to insurance including broking and agency services (8140)</li> </ul>
B. Banking and other financial services excluding insurance	<ul style="list-style-type: none"> <li>a. Acceptance of deposits and other repayable funds from the public (81115-81119),</li> <li>b. lending of all types, including consumer credit, mortgage credit, factoring and financing of commercial transaction (8113)</li> <li>d. All payments and money transmission services (81339<sup>**</sup>)</li> <li>e. Guarantees and commitments (81199<sup>**</sup>),</li> <li>g. Participation in issues of all kinds of securities and provision of services related to such issues except underwriting (8132),</li> <li>i. Asset management except pension fund management (8119<sup>**</sup>+81323<sup>*</sup>)</li> <li>k. Advisory and other auxiliary financial services (8131 or 8133)</li> </ul>
9. TOURISM AND TRAVEL-RELATED	
A. Hotels and Restaurants including catering (641-643)	

SECTOR-SPECIFIC COMMITMENTS	SPECIFIC ACTIVITIES AND (CORRESPONDING CPC)
B. Travel Agencies and Tour Operators Services (7471)	
C. Tourist Guide Services (7472)	
11. TRANSPORT SERVICES	
C. Air Transport Services	d. Aircraft repair and maintenance services <sup>2</sup> (8868 <sup>**</sup> ) e. Supporting services for air transport such as selling and marketing of air transport services and computer reservation system (CRS) services (746)
F. Road Transport Services	a. Passenger transportation (7121+7122) b. Freight transportation (7123) c. rental of commercial vehicles with operator (7124) d. maintenance and repair of road transport equipment (8868) e. supporting services for road transport (744)
12. OTHER SERVICES NOT INCLUDED ELSEWHERE (95+97+99)	
Metrological data information	

The (\*\*) indicates that the service specified constitutes only a part of the total range of activities covered by the CPC concordance (e.g. voice mail is only a component of CPC item 7523).

<sup>1</sup>Information provided for the purposes of transparency: subject to type approval and licensing procedures

<sup>2</sup>As defined in paragraph 6 of the Annex on Air Transport Services

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