

COMMUNICATION FROM JAPAN

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**THE RELATIONSHIP BETWEEN THE FUTURE
MULTILATERAL INVESTMENT RULES AND THE GATS**

I. INTRODUCTION

1. As trade and investment are very closely related, many of the WTO Agreements cover cross-border investment activities, either directly or indirectly. These Agreements include GATS (*General Agreement on Trade in Services*), TRIPS (*Agreement on Trade Related Aspects of Intellectual Property Rights*), TRIMS (*Agreement on Trade Related Aspects of Investment Measures*), and ASCM (*Agreement on Subsidies and Countervailing Measures*). Among them, relevance of the GATS to the ongoing work was made clear throughout the discussion at the Working Group last year.

2. Therefore, the intention of this paper is to analyse the possible relationship between the future multilateral investment rules and the GATS. It explores how the GATS relates to investment and how the future multilateral investment rules could deal with the areas already covered by the GATS, with a special focus on development dimensions. This paper attempts to lay out some issues for discussion, and does not intend to propose any particular approach.¹

II. HOW THE GATS RELATES TO FDI

3. GATS mode 3 directly deals with FDI through the concept of "commercial presence," as a means for supplying services in foreign countries. Mode 3 is defined as; "the supply of a service by a service supplier of one Member, through commercial presence in the territory of any other Member."² The GATS covers establishment of commercial presence, which basically equates to the concept of FDI, and in this sense, FDI in the services sector is already clearly covered by the GATS.

4. It is sometimes argued that the GATS does not deal with FDI *per se* but rather deals with the supply of services, and covers FDI (or establishment of commercial presence) only to the extent that FDI is necessary for trade in services. This argument points out that FDI is covered by the GATS

¹ Throughout this written contribution, consideration is limited to foreign direct investment (FDI). It is only for the sake of convenience and this does not indicate Japan's position as to what the scope of investment should be.

² GATS Article 1:2(c).

only as a result of the GATS covering certain modes of services supply, and providing rules on FDI is by no means the purpose of the GATS. However, it needs to be noted that FDI in the services sector enjoy a more predictable and secure status which is not the case for FDI in the goods sector.

5. Importantly, from the standpoint of an investor, GATS guarantees certain treatment to foreign investors, which is absent in GATT. An investor seeking to establish a production base for automobiles would be able to enjoy certain treatments under the future investment rules, just as an investor seeking to establish a commercial presence for rent-a-car services enjoys certain treatment under the GATS mode 3. Both service suppliers and investors in manufacturing industry seek to establish commercial presence in foreign countries from exactly the same economic motive – to be able to supply their goods/services in the market. Especially for investors trying to operate an integrated business model, for example, manufacture automobiles in the host country and then use those automobiles for rent-a-car services, absence of rules for investment in the non-services sector is not desirable.

6. More importantly, there are no reasons to differentiate benefits generated by these FDI's from the host countries' perspective. Liberalisation of trade and investment contribute to more competitive markets in the host countries through increase in supply of services and production of goods, which could bring the local consumers more benefits through goods and services at more attractive costs and of wider range of variety. They both lead to increase in local employment, tax revenue, export capacity, technology transfer etc., and contribute to the growth of the local economy. It needs to be noted, however, that a flexible structure like GATS will allow the host country to maintain policy space for necessary regulation and development policies in areas of their choice. This point is discussed later.

7. These indicate that commercial presence in services industry and production base of manufacturing industry hold the same meaning in economic terms, which reduces the significance of discussing whether GATS mode 3 and FDI are different, and upholds the legitimacy of considering the future investment rules in parallel to the GATS mode 3.

III. THE FUTURE INVESTMENT RULES AND FDI IN THE SERVICES SECTOR

8. Since the GATS already covers FDI in effect, there is a potential tension between the GATS and the future investment rules. On the question of how the future investment rules should deal with FDI in the services sector, there are two approaches; one being to exclude the services sector covered by the GATS and the other to include it.

9. If the services sector covered by the GATS is to be excluded from the future investment rules, there will be minimum tension between the future investment rules and the GATS, as they will apply to different sectors. In this case, the level and the content of the disciplines need to be harmonised to avoid unjustifiable differences in the treatment of services and non-services sector. This could be done by taking into account the structure and provisions of the GATS as much as possible when designing the future investment rules. Issues to be considered in this regard include whether to include pre-establishment phase, require *de facto* (as opposed to *de jure*) national treatment, and cover temporary entry of investors and their employees, following the GATS approach.

10. If the services sector is to be included in the future investment rules, one set of rules will apply across the board, to both services and non-services sectors, enabling exactly the same treatment in both sectors. However, this approach may necessitate revision of the GATS to avoid conflict or inconsistencies between the two disciplines which could complicate the legal structure of the existing rules.

IV. DEVELOPMENT DIMENSION

11. One of the most important features of GATS from a development perspective is its structure. It adopts a hybrid approach, under which there is no general obligation regarding market access(MA) and national treatment(NT). Each Member chooses the sectors and the conditions it will commit MA and NT, and each Member will be obliged to provide certain treatments only to the extent that they are indicated in the Schedule of Specific Commitments. Each Member may take full consideration of its own national priorities and development policies, when making its commitment. This approach has proved to enable each Member to make commitments in sectors of its choice in line with its national policies.³

12. It should be remembered that GATS Article 19 explicitly provides in the context of Negotiation of Specific Commitments that: "The process of liberalization shall take place with due respect for national policy objectives and the level of development of individual Members, ...There shall be appropriate flexibility for individual developing country Members for opening fewer sectors, ... progressively extending market access in line with their development situation... ." The GATS approach should serve as a certain reference when designing the future investment rules, as ensuring compatibility between a multilateral framework and each country's development policies and right to regulate is an essential task.

V. CONCLUSION

13. This paper attempts to make clear that the GATS is extremely relevant when exploring the future investment rules. The GATS already covers FDI through mode 3, and the GATS and the future investment rules could play a similar role for the investors as well as the consumers in the host country. Thus, GATS has certain implications on the design of the future investment rules.

14. When considering the numerous issues such as whether the future investment rules should cover the services sector, include the pre-establishment phase, provide for *de facto* national treatment, address temporary entry of investors, adopt a positive list approach or a negative list approach, the provisions of the GATS need to be taken into account. More importantly, the development-related aspect of GATS, notably the flexible structure of the GATS, needs to be recognized and be fully taken into consideration in the discussion at the Working Group.

³ It also needs to be reminded that if this approach is to be adopted, considerations on industrial classifications are necessary. This issue is very important for both legal stability and transparency for investors. (see Japanese Government submission; WT/WGTI/W/125).