



European Commission services' position paper on the Sustainability Impact Assessment in support of negotiations of the Trade in Services Agreement (TiSA)

July 2017

1. Introduction

This paper sets out the European Commission services' response to the findings and recommendations of the Sustainability Impact Assessment (SIA) on the Trade in Services Agreement (TiSA) involving the European Union (EU) and 22 other participant countries. The SIA was commissioned by the European Commission's Directorate-General for Trade and was carried out by the independent consultancy company Ecorys with the contribution of CEPR (Centre for Economic Policy Research). It was completed in June 2017. The TiSA negotiations were officially launched in April 2013 and by December 2016, when TiSA negotiations were paused, 21 negotiating rounds had taken place.

SIAs are trade-specific assessments carried out by external consultants to support major trade negotiations. SIAs are designed to provide negotiators and policymakers with an evidence-based *ex ante* assessment of the potential sustainability impacts that may arise from a proposed trade agreement. This SIA of TiSA drew on the methodological framework set out in the Commission's [Handbook for Sustainability Impact Assessment](#)¹.

The SIA provides an assessment of the potential impacts of TiSA on the economy, on social and labour aspects, human rights and the environment, but also on EU competitiveness (with a special focus on SMEs), consumers and potentially significant impacts on developing countries and least developed countries. The SIA also examines more in depth the potential impacts on a number of key economic sectors, such as water transport, financial and insurance services, computer and electronic communication services, and e-commerce.

The SIA process comprised a consultation of stakeholders, including by way of three meetings with civil society in Brussels and an online stakeholder survey.

The final report is publicly available on DG Trade's website:

<http://ec.europa.eu/trade/policy/policy-making/analysis/sustainability-impact-assessments/assessments/>

¹ This revised version of the SIA Handbook was published in April 2016 when this SIA TiSA was underway. Although the SIA consultants broadly follow the approach outlined therein, it should be noted that the terms of reference specifying the analytical requirements under which this SIA was produced were based on the previous Handbook.

2. Overview of the consultant's findings

Reflecting the negotiations, the TiSA SIA is based on the assumption that binding the existing level of liberalisation in services is the main outcome of the TiSA. This is considered a key outcome because there are substantial differences between commitments made in the GATS compared to actual policy, a gap referred to as "binding overhang". Reducing the binding overhang implies decreasing uncertainty related to the existing level of market access. The main challenge of the TiSA SIA is therefore to measure the effects related to the reduction in policy uncertainty.

2.1. Economic impacts

Methodology

The Consultant quantified the economic impact of TiSA with a version of Computational General Equilibrium model (CGE) developed by Bekkers, Francois and Rojas-Romagosa (2015)². The CGE model makes it possible to assess the impact of a change of policy in services on both the services sectors and the rest of the economy (manufacturing and also agriculture for which services are inputs) while keeping other policies unchanged relative to the baseline. The exercise simulated the impact of trade cost reductions associated with the reduction of the trade policy uncertainty related to the binding overhang.

The quantitative trade cost reduction was obtained by estimating a gravity equation. On average (for sectors and countries), the results of the econometric analysis show that exporters are expected to respond to more secure market access as if trade costs fell by 3.4 percent on average for OECD participant destination markets, and by 5.8 percent for low and middle income destination markets.

Importantly, as the Consultant highlighted, data on services trade are more limited than on goods trade. The assumptions on trade cost reductions draw on estimates of the overall coefficients which are then applied to sectorial data. The quantitative part of the SIA does not include direct modelling and estimation of services trade through Mode 3 (commercial presence) which is a very important mode of supply. In addition Mode 4 (movement of natural persons) is not separated from Modes 1 and 2. The Consultant underlines that, given these limitations, their analysis is not able to fully capture the impacts of TiSA, but only provides an indication of the direction of the impacts.

The Commission services observe that, as it was stated in the terms of reference for this SIA, the Consultant was expected to elaborate an innovative methodology for assessing the economic value of trade in services negotiations. The long duration of the study testifies that efforts have been made to elaborate such innovative methodology. However, this was not achieved. Consequently, the final product is subject to the major limitations explained by the

² Eddy Bekkers, Joseph F. Francois, and Hugo Rojas-Romagosa 2015. "Melting Ice Caps and the Economic Impact of Opening the Northern Sea Route," CPB Discussion Paper 307, CPB Netherlands Bureau for Economic Policy Analysis.

Consultant. The choice of the CGE model has been criticised by a number of stakeholders that consider it inappropriate for this SIA on services. The Commission services do consider that this is the only available alternative to assess the macroeconomic impact of trade policy accounting for all the direct and indirect impacts; however they have doubts about the way the model has been applied (see also the remarks on sectorial effects below) and would have preferred the Consultant to define, within the CGE framework, a more innovative and theoretically sound approach to the reduction of trade costs rather than the standard one that was used, so as to better account for the specificities of services trade.

A number of remarks can be made in this respect. First, the GTAP database (i.e. the database used by the model) does not account for tariffs for the services sectors, which means that differentiating price wedges (i.e. difference between the prices charged in a country and the world prices) for services sectors is not possible. Second, while technological change is very important for the services sectors, this is exogenous in the standard framework used by the Consultant. Third, the methodology used does not explicitly take into account the fact that a reduction of trade policy uncertainty impacts both fixed and variable costs, but instead imputes all the cost reductions at the border. Finally, the assumptions used for trade cost reductions draw on estimates of the overall coefficients for the services sectors; sectorial specificities like those of the water transport sector are thus not reflected. Therefore, the Commission services consider that the quantitative analysis produced by the model should be considered only as a very general indication.

Macroeconomic effects on the EU and other countries

The Consultant concludes that TiSA will have a positive impact on the EU economy, albeit macroeconomic effects are modest under both experiments³. Household income and wages show similar increases for all skills groups (lower skilled, medium skilled, and higher skilled) and in both experiments. The largest effects are expected on trade flows, although these changes are relatively small as well. The other TiSA participants are also expected to experience an increase in real national income, although the gains are relatively small and there is some variation across countries. For countries not participating in the TiSA negotiations, including developing countries and least developed countries (LDCs), the Consultant did not find any significant impact of the Agreement.

Sectoral effects in the EU

At sectoral level, TiSA is expected to have a small but positive impact in most sectors. Most services sectors are projected to expand their output, although the changes are very small. However, according to the CGE model results the water transport sector would slightly contract (by 0.3-0.5%). The deeper qualitative analysis of the water transport sector, carried out by the Consultant in the specific sectorial part of the final report, shows that the negative impacts on this sector are in reality most probably due to the limitations of the CGE model

³ The first (experiment A) involves binding current market access across all current TiSA participants. The second (experiment B) involves an expansion of TiSA to cover more Asian countries: China, Malaysia, Philippines, Thailand, and Vietnam.

used for this study, which cannot fully take into account the specificities of the water transport business, and in particular of maritime transport.

In this light, the Commission services have examined with particular attention the findings relating to the sectorial effects in respect of water transport. Generally, in standard trade models, reductions in trade costs due to liberalisation of a sector with a comparative advantage – as is the case of maritime transport, where the EU is a major actor and very competitive international player – would bring an expansion and not a contraction of the sector. The Consultant was able to demonstrate that the negative result in this case derives from the impact of trade cost reductions on imports and exports but was not in a position to explain further. It remains unclear, for example, whether the findings are explained via price effects, supply effects, the lack of capital mobility assumed in the model (which limits the gains coming from being market leader in specific sectors) or whether it was driven by other constraints. A significant possibility is that the result can be explained by the fact that the model did not take into account the specificities of the sector. Water transport services are different from other services in the context of a CGE model as they contribute both as a product and as a transport margin (difference between c.i.f. and f.o.b) which is a component of supply. The Consultant however chose to apply the trade costs reduction on the "product" side only. In addition, as already explained above, assuming similar costs reductions for the water transport services as those applied in other services sectors represents another important limitation.

The Commission services have not found an explanation or academic reference that would justify this choice. Neither have they seen any convincing explanation about where exactly the benefits corresponding to the EU potential losses in the water transport sector would go (i.e. which countries could in absolute terms take over the market shares lost by the EU).

The qualitative analysis further carried out by the consultant in the sectorial study on water transport (section 5 of the final report) points to opposite conclusions, reversing the negative picture and attributing some of the gains of other countries to the EU, given the fact that EU vessels also trade under non-EU flags. This, however, cannot be considered a proper explanation of the counterintuitive results provided by the CGE model, and the two very different indications provided by the qualitative and quantitative assessments are finally not fully reconciled. This reinforces the Commission services' view that the Consultant's model was not adequate to address the TiSA framework as explained above. For all these reasons, the Commission services continue to have serious doubts about the results relating to this sector.

Effects on SMEs

The Consultant found that SMEs in general have difficulties in accessing the right information on (and complying with) relevant regulations and procedures when exporting and are therefore likely to benefit from TiSA.

The Commission services agree with this assessment, in consideration of the increased legal certainty and enhanced transparency of rules/information that the Agreement is likely to bring about.

2.2. Social impacts and Human rights' impacts

The social effects of TiSA for the EU are estimated to be mainly indirect and limited, stemming from changes in economic indicators (changes in wages, sectoral employment, prices, etc.). The Consultant concludes that TiSA is likely to have a small positive impact on real household consumption and real wages whilst the reallocation of labour in the EU is expected to be very close to zero for all skill categories. Also no significant changes (close to 0 for most countries including the EU) in consumer prices are expected. The Consultant also refers to the concerns raised about TiSA's effect on public services, and highlights in this respect that TiSA is not expected to produce any change in the obligations of the EU relating to public services as compared to GATS and other EU FTAs. The effect of TiSA on the right to regulate has also raised concerns among stakeholders, but the Consultant notes that this right will be embedded in the Agreement, making it legally binding.

The Consultant found that the positive changes in real national income and real wages will contribute to the right to an adequate standard of living and that the expected increase in wages also points to an increase in the demand for labour and could in reality lead to higher employment levels and therefore contribute to the right to work. According to the Consultant, the overall effect on labour rights is unclear, as there are both positive forces (increased economic development which allows for better working conditions) and negative forces (increased competition that may put pressure on standards) at play. The Consultant concludes that from a quantitative point of view, the modelling results show that TiSA is expected to lead to economic growth, which will enhance tax revenues and thus could increase public expenditures on health, education and other public services. Whether this would actually happen is of course a matter of national or local policy and impossible to predict at this stage.

The Commission services note that TiSA is likely to lead to limited but positive social impacts and similarly small but positive effects on human rights. It confirms that it is committed to protecting public services at all levels of government, including the local level, and this includes issues regarding regulation and (de)privatisation.

2.3. Environmental impacts

According to the Consultant, the impact of TiSA on the environment is expected to be small and indirect, mainly stemming from changes in economic indicators, including a smaller than 0.1 percent increase in emissions of air pollutants. At the same time, TiSA could help accelerate the diffusion and uptake of environmental services (and indirectly of environmental goods), depending on the extent to which commitments are made, as also shown in the case studies. The Consultant also refers to some concerns among a number of civil society groups over how TiSA may affect semi-public sectors since for example the possible increase in private sector participation in these sectors (e.g. waste management) might result in an increase in bargaining power of private economic interest and a possible loss of government control. However, the Consultant also notes that in its offer for TiSA, the EU reserves the right to run monopolies and grant exclusive rights, and that in any case EU governments will always keep the ability to regulate public services in a non-discriminatory way.

The Commission services take note of this assessment and confirm that in all its free trade agreements the EU always reserves the right to run monopolies and grant exclusive rights in almost all sectors, including environmental services/waste management. Moreover, as the Consultant correctly points out, EU governments will always keep the ability to regulate in general (i.e. also for non-public services), as long as they do not discriminate between domestic and foreign operators.

3. Commission services' views on the recommendations

3.1. Economic impact

The Consultant recommends the Commission to negotiate an ambitious Agreement in terms of binding applied practice by commitments.

The Commission's objectives in the TiSA negotiations are fully in line with this recommendation.

The Consultant suggests opening up TiSA to other interested parties during the negotiations, and after the negotiations are finished.

The Commission has always supported opening TiSA to other interested Parties, noting however that additional participation before the conclusion of the Agreement would be difficult to achieve. The future multilateralisation of TiSA was one of the EU's key requests for joining the TiSA negotiations and the EU has been instrumental in designing the architecture of TiSA in a way that it can be folded into the GATS in the future.

Although additional analysis showed that the results for the EU water transport sector are indeed expected to be positive when taking into account the global nature of this sector, the Consultant suggests that developments in this sector are monitored over time after the implementation of TiSA and that, should changes in this subsector turn out to be negative, additional measures could be taken if needed.

For the reasons already mentioned before (see point 2.1 above), the Commission services do not share the overall assessment relating to the water transport sector. However the Commission services will certainly give due consideration to any positive or negative element that stakeholders may bring to their attention during the period of implementation of the Agreement.

The consultant recommends to consider the establishment of an information point dedicated to SMEs, or of an SME Committee in TiSA (as it was also discussed in the TTIP negotiations) that deals with issues and problems faced by SMEs.

TiSA participants aim at establishing a simple and cost-effective administrative structure, with a limited number of bodies empowered to discuss the implementation of the Agreement in all relevant areas, including those of relevance to SMEs. While it is not planned to establish dedicated contact points or Committees for SMEs in particular, TiSA is indeed expected to

establish general contact points in each Party, thereby allowing service suppliers, including SMEs, to obtain relevant information via their home country/jurisdiction.

3.2. Social and human rights impacts

The Consultant suggests that the TiSA final text includes provisions aiming at increased consumer protection and promoting coordination between all TiSA partners in this field.

The Commission services agree on the importance of consumer protection and will seek to incorporate, to the extent possible, consumer protection principles in TiSA. For example, a provision - proposed by the EU - is under discussion that will require Parties to establish an adequate consumer protection framework for electronic commerce. With the objective of facilitating the use of mobile electronic communications when travelling, relevant provisions have been designed to ensure transparency and competition on roaming rates. Such provisions are still subject to agreement of all TiSA participants before finalisation of the negotiations.

The Consultant recommends that the effect of TiSA on gender equality in the EU should be monitored through further studies and ex-post impact assessments. Monitoring should in particular include issues such as female employment, the gender pay gap, female representation in upper management, and the extent of female employment in unpaid care and domestic work.

The Commission is committed to ensure gender equality across all of its policies. The Commission services note that the analysis of gender impacts from trade remains challenging methodologically and that the growing literature does not yet give straightforward answers to the question of how trade liberalisation affects men and women differently. Nevertheless, this issue will certainly feature in the future ex-post evaluation which will be undertaken a few years after the Agreement has been in place. At the same time the Commission services regret that the Consultant itself did not try to go further in this regard in the SIA, notably in relation to some of the indicators contained in the recommendation itself.

Although no significant labour market changes are expected, the Consultant considers it good to monitor changes in the labour market as a result of TiSA, especially in sectors that might contract or where imports are expected to increase relatively more, and to promote the ability of labourers to move from one sector to another.

The Commission services will monitor labour market changes as part of their regular monitoring activities related to trade agreements. However, they also note the difficulties encountered by the Consultant in attempting to establish the methodological and analytical guidelines for assessing labour market impacts resulting from trade in services in the future.

The Consultant notes that no changes in obligations by the EU are expected with respect to public services from TiSA and underlines the importance that the EU defends its position in the negotiations with respect to its offer for public services. The Consultant highlights that several ideas have been put forward by stakeholders over the course of negotiations to improve the protection of public services under TiSA as compared to GATS, and recommends that the Commission engage in continuous and open dialogue with interested stakeholders so as to

ensure that any possible concern in this sensitive area is known and can be timely addressed, or that potential interesting new ideas can be taken on board (see also recommendation HR5).

The Commission services fully agree with this recommendation. The EU has consistently maintained its safeguards for public services in the TiSA negotiations, like in any other negotiation. The Commission services have been engaging with the relevant stakeholders to discuss the proposals related to public services and have participated in open dialogues with interested parties to address concerns, both in public as well as on a bilateral basis.

The Consultant recommends that, in line with the resolution of the European Parliament of 25 January 2016, a comprehensive, unambiguous, horizontal, self-standing, and legally binding provision based on GATS Article XIV be incorporated in TiSA, which fully exempts the existing and future EU legal framework for the protection of personal data from the scope of the Agreement, without any conditions that this must be consistent with other parts to the TiSA. As announced in the Trade for All Communication, the Communication on Building a European Data Economy⁴, and the DSM mid-term review Communication⁵, the Commission will seek to use EU trade agreements to set rules for e-commerce including cross-border data flows and tackle new forms of digital protectionism, in full compliance with and without prejudice to the EU's data protection rules. The Commission is currently working with the European Parliament and the Member States to develop a solid approach that strikes the right balance between these objectives.

The Consultant considers that, although some improvements in terms of transparency of the TISA negotiations have been made in the EU in comparison with previous trade negotiations, room for further improvement still exists.

The Commission services agree on the importance of an open and transparent process in trade negotiations with substantial involvement of relevant stakeholders and of the civil society. In this respect, it is important to stress that all the EU's negotiating proposals and offers in TiSA have been made public, as well as a number of factsheets concerning the various areas under negotiation and a number of other explanatory documents. Furthermore, regular meetings with stakeholders, both in public and on a bilateral basis, have taken place in Brussels and in Geneva. Even if not all negotiating documents can be shared with the public, the Commission services will continue to work closely with the Council and the Parliament which already receive all negotiating documents and are regularly updated on the results of the rounds, and will continue to engage with stakeholders notably in the context of DG Trade's Civil Society Dialogue.

The Consultant recommends that TiSA includes provisions to promote the ratification and implementation of the main ILO Conventions. This could also be done through initiatives outside the Agreement (e.g. co-operation and capacity building). This will at a general level improve human rights' resilience to effects from this Plurilateral Agreement.

⁴ COM(2017) 9 – 10 January 2017

⁵ COM (2017) 228 – 10 May 2017

The Commission services share the consultant's view on the importance of promoting international labour standards. The Commission services underline however that labour standards are an important but a complex theme, in particular as the objective is the full integration of TiSA within the multilateral trading system. The Commission will remind TiSA partners of the importance of promoting decent work, of respecting and realising the fundamental rights and principles at work, and of complying with ILO conventions. The Commission services will in any case continue to engage with partner countries through relevant channels, including in cooperative processes aimed at strengthening compliance with international labour standards, independently from the existence of binding provisions in FTAs.

Finally, the Consultant recommends to follow up the ex-ante impact assessment by an ex post impact assessment, in line with the Commission's practice, and to include provisions in TiSA which would allow such ex-post evaluation to impact positively on the development of the Treaty over time.

The Commission services are committed to monitoring the impacts of any future Agreement as part of their regular monitoring activities and to carry out an ex-post evaluation of the Agreement after its implementation. TiSA Parties are also considering to include in the Agreement a review clause that would allow further adjusting the Agreement's objectives over time.

3.3. Environmental impacts

The Consultant recommends that, since TiSA may help to accelerate the diffusion and uptake of environmental services with positive environmental effects, the EU be ambitious, and promote the binding of policies in this area.

The Commission services confirm their strong interest in the diffusion and uptake of environmental services with positive environmental effects in this and other trade agreements, coupled with the necessary reservations to protect e.g. public services, water etc..

4. In-depth sector studies: conclusions and recommendations

On **water transport services**, since the modelling results predicted a small negative impact of TiSA on the EU water transport services sector (despite the fact that qualitative analysis suggests that the EU sector is likely to gain from TiSA), the Consultant suggests to monitor the changes in the sector stemming from TiSA. The consultant also suggests including provisions in the Agreement that encourage TiSA participants to work towards ratification and implementation of ILO core conventions and MARPOL Annexes. When such a mechanism would not be feasible within TiSA, the Consultant recommends promoting future ratification and implementation outside TiSA.

The Commission services' position on the water transport findings of this SIA has already been mentioned above (see point 2.1 above – pages 3-4). As far as the recommendation on MARPOL Annexes is concerned, the Commission services' position is the same as indicated above for the ILO core conventions (see point 3.2 above – page 8).

On **finance and insurance services**, the Consultant underlines the various efforts by legislators to improve supervision and consumer protection in the finance and insurance sectors and recommends to include the clause on adoption and implementation of internationally agreed standards, clear definitions, and to push for guidelines and agreements at international level (in the various existing international fora) specifically in new areas where regulation and standards are not yet or still are being developed.

The Commission services take note of the recommendations. The EU has put in place over the last years a sound regulatory framework for the supervision and regulation of financial services and remains committed to work in international fora on international standards. The Commission services are convinced that TiSA, as also shown in the SIA, will have a positive impact on trade in financial services which is an important economic sector in the EU.

On **ICT and telecommunications services**, the Consultant predicts a small impact on output and trade, and consequently on employment and the environment. This is due to the fact that TiSA will mainly bind policies that are already currently applied and the model used in the study does not take into account the movement of natural persons and foreign direct investment, arguably the two most important modes of supply for computer services and electronic communications. The Commission services share this analysis and these conclusions.

On **E-commerce**, the Consultant concludes that transparency about regulations, rules and processes will benefit e-commerce operators, by reducing cross-border information and search costs. For consumers, transparency will reduce the information costs and the uncertainty associated with purchasing goods or services from abroad. Therefore, TiSA can be an important first step towards a better global governance of e-commerce. By covering and including all important areas of e-commerce, TiSA could provide the framework to be used in future bilateral or multilateral negotiations of e-commerce. Promoting e-commerce is not only about e-commerce specific policies but also about policies related to auxiliary sectors such as logistics and distribution or financial services. The Commission services share this analysis and these conclusions.

5. Conclusions

The Commission services welcome this SIA on TiSA and share the vast majority of the conclusions and recommendations made by the Consultant, with the few exceptions mentioned in this paper. Although the overall benefits from TiSA are estimated to be limited, this SIA encourages in general the Commission services to continue in their objective of working as a leading force towards an ambitious TiSA agreement which can be further multilateralised.