OPINION

PIECE

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Why regulatory cooperation matters for business

Facilitating international business requires more than trade negotiation alone. Liberalization of market access restrictions at the border is necessary. But for trade in services, it is not sufficient.

This is because the extent of public ownership and the degree of domestic regulatory intervention has traditionally been higher in the services sector than in the goods sector.

Many of the barriers to trade in services consequently lie in regulatory regimes, not only at borders, but deep behind borders, in a myriad of domestic regulations that constrain the manner in which commercial services business is conducted.

The efficiency of domestic regulation, i.e. the extent to which it avoids imposing undue compliance costs on services providers, is vital to domestic services industries' productivity and international competitiveness (Sáez et al., 2014). Improved efficiency in domestic regulation of services helps grow the local services industry even when it also facilitates foreign entry. This is the distinctive "win-win" of services trade and the underlying rationale for international efforts to agree on principles to guide regulatory best practice in services.

It makes sense, given how important domestic regulatory regimes are, both for international competitiveness and for international market access, that cross-jurisdictional regulatory connectivity should become a matter of significant services business interest.

This is especially the case as the globalization of services intensifies with the shift to the digital economy. Business perception surveys (e.g. PECC, 2016; OECD, 2018b) now consistently show that business respondents consider regulatory disconnects to be the paramount obstacle to increased services trade.

To make matters worse, regulatory fragmentation in the global services economy appears to be on the rise. In 2018, the OECD Services Trade Restrictiveness Index (STRI) showed increased regulatory tightening in telecommunications and computer services. In 2019, the OECD's new digital STRI shows significant regional heterogeneity impacting on services traded over the internet, with the effect that regulatory barriers risk derailing the benefits of digitalization. Looking at the whole digital ecosystem, heterogeneity is especially evident in regulations affecting infrastructure and connectivity, the areas also

experiencing most recent tightening of policy changes.

These regulatory barriers translate into hefty tax equivalents that significantly exceed average tariffs on traded goods (as high as 80 per cent in some sectors) and raise the price of services (as much as 20 per cent in some sectors). Larger firms are more able to find ways around the regulatory disconnects, so this impacts most severely on MSMEs, raising their average trade costs by an average additional 7 per cent (OECD, 2018b).

The need for international regulatory cooperation in services is not new. It has long been recognized as a contributing element of regulatory best practice. This is partly because international benchmarking and sharing of information are helpful in the domestic regulatory design process. It is also because regulatory interoperability across different jurisdictions has proved essential to improving the effectiveness of domestic regulations in achieving their public policy purposes: think international air transportation (ensuring safety and connectivity) or shared expertise in the development of technical standards (Mumford, 2018). But the need for regulatory cooperation has grown exponentially since the GATS came into effect.

As services become increasingly tradeable across borders as a result of new technologies, the need for dedicated regulatory cooperation efforts will become increasingly evident to governments. After two decades of post-GATS business reality on the ground, the business community is beginning to agree that unlocking further trade liberalization on services is going to require a big push in terms of regulatory cooperation.

Some commentators (e.g. Mattoo, 2015) suggest that regulatory cooperation has become a critical pre-condition for further services trade liberalization, at least in the WTO. Mattoo argues for a sequenced approach, with much greater immediate effort on regulatory cooperation, because without the greater mutual understanding, enhanced confidence and familiarity that come from regulatory interaction, efforts at services trade liberalization will remain stymied.

From a services business perspective, neither trade liberalization nor regulatory cooperation are independently sufficient to facilitate international flows of services. Both are necessary; for services trade to grow, the two must go hand-in-hand.

Some services sectors and some modes of supply experience higher degrees of regulatory heterogeneity than others. Mode 4 of the GATS has always been and remains highly constrained by regulatory disconnect. Mode 3 has been the least impacted and traditionally has shown the highest growth rate. Thanks to digitalization, mode 1 should be top of the charts – but is much more constrained than it should be, if regulators could only find appropriate ways to engage.

That is the crux of the problem. Where and how should regulators engage? Regional groupings are already grappling with this. The WTO needs to do the same.

Over the last decade, 77 per cent of RTAs have included provisions on trade in services, up from 16 per cent in the 1990s (Braga et al., 2019). As businesses increasingly call for greater regulatory seamlessness, the services aspects of RTAs are edging towards deeper levels of integration, including greater alignment on regulatory principles. Agreeing on the elements that constitute regulatory best practice is a vital first step.

Efforts are also needed on mutual recognition and equivalence – the outcomes of regulatory cooperation in action.

As a non-negotiating forum, APEC has been well positioned to set some influential precedents in regulatory cooperation relevant to facilitating trade in services. To name a few: the APEC Business Travel Card, Asia Region Funds Passport, Cross-Border Data Privacy Rules and Non-binding Principles for Domestic Regulation in Services. Most regional integration fora recognize the importance of complementing services trade negotiation with efforts to reduce regulatory irritants and disconnects across regional markets. The EU Services Directive is all about improving the regulatory environment for cross-border services trade, including in professional services; the EU Digital Single Market similarly establishes a strategy to build regulatory interoperability. Regulatory excellence is a core pillar of the Master Plan on ASEAN Connectivity. The Caribbean Community (CARICOM) has developed a regional Certificate of **Recognition of CARICOM Skills** Qualification: the Common Market for Eastern and Southern Africa (COMESA) has a Yellow Card for cross-border motor vehicle insurance. The list goes on, but most regional fora remain seriously underutilized in terms of their potential for regulatory cooperation.

Business is looking for a big push – at all levels but specifically in the WTO – and especially with respect to the many regulatory building blocks required for digital trade. The e-commerce negotiations have the potential to show the way.

To build a foundation for this effort to succeed, WTO members need to create new fora to help share perspectives and build regulators' confidence in each others' approaches and perspectives.