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Council for Trade in Services

THE WORK PROGRAMME ON ELECTRONIC COMMERCE

Note by the Secretariat

1. This paper has been prepared to assist the Council for Trade in Services in its examination of the treatment of electronic commerce in the GATS legal framework. Because there is considerable overlap between the list of points remitted to the Council in the Work Programme and the subject-matter of the earlier Secretariat Note WT/GC/W/90, some of the content of the present paper will be familiar from the earlier note. The paper addresses the points in the Council work programme in terms of the relevance to them of GATS provisions. It does not provide authoritative interpretations of these provisions, which can only be made by the Ministerial Conference.

Scope (including modes of supply) (Article I)

2. The GATS applies to "measures by Members affecting trade in services" (Article I:1). In order to examine the applicability of the Agreement to electronic commerce, we need to consider in turn the definition of trade in services, the measures falling within the scope of the Agreement and its sectoral coverage.

3. The Agreement defines trade in services as the supply of a service through any of four modes: cross border supply, consumption abroad, commercial presence and presence of natural persons (Article I:2).[1] These modes distinguish between services transactions on the basis of the territorial presence of the supplier and the consumer of the service. The Agreement makes no distinction between the different technological means by which a service may be delivered - whether in person, by mail, by telephone or across the Internet. The supply of services through electronic means is therefore covered by the Agreement in the same way as all other means of delivery. Because of the way in which it can render the distance between supplier and consumer virtually irrelevant, it is perhaps natural to think of electronic commerce essentially in terms of cross-border supply. But it is important to bear in mind that Modes 2, 3 and 4 also cover the electronic delivery of the service. For instance, a foreign bank established locally may supply its services to consumers electronically, or a foreign natural person present locally may use electronic means to deliver consultancy services. It is also important to note that the "supply" of a service is defined to include the production, distribution, marketing, sale and delivery of a service (Article XVIII(b)).

4. Legal obligations in the GATS apply to all measures affecting trade in services. Measures affecting the electronic delivery of services, such as a charge on the import of a service by electronic means, are "measures affecting trade in services", just as they would be if imposed on delivery by any

[1] The four modes of supply are defined as follows: (1) cross-border, where the service is supplied from the territory of one Member into another; (2) consumption abroad, where the consumer purchases a service which is delivered in the territory of another Member; (3) commercial presence, where the service supplier of one Member establishes a subsidiary or a branch in another Member to supply a service; (4) presence of natural persons, where the service is supplied by a person working in the territory of another Member.

other means. It is important to note that the term "affecting" has been interpreted to cover not only measures which directly govern the supply of a service but also measures which indirectly affect it. [2]

5. Furthermore, measures by Members are defined broadly to include measures taken by central, regional or local governments, as well as non-governmental bodies in the exercise of powers delegated by the government. Therefore, governments can be held accountable in the WTO for decisions or actions affecting trade in services by non governmental bodies, such as those regulating particular service sectors, which exercise delegated powers. This may be particularly relevant, for example, if such bodies were to have responsibility for the administration and assignment of domain names, a function that is analogous to the numbering assignments in telecommunications, and may be governmental or delegated by governments.

6. The GATS covers any service in any sector (Article I:3(b)) with only two exceptions: services supplied in the exercise of governmental authority, neither on a commercial basis nor in competition with one or more service suppliers; and most air transport services.

Distinguishing between modes 1 and 2

7. Even though it is clear that the delivery of services by electronic means may take place by any of the modes of delivery mentioned above, it is not always easy to specify whether a transaction takes place under mode 1 or mode 2. The difficulty of making a clear distinction between cross-border supply and consumption abroad was noted in the financial services context (see S/FIN/W/9) where so many transactions are done electronically, but it is clear that the same difficulty arises for other forms of electronic commerce. According to the Scheduling Guide (MTN.GNS/W/164), the distinction between cross-border supply and consumption abroad hinges upon whether the service is delivered in the territory of the Member or outside. It is difficult to make this rule operational when electronic delivery makes a transaction possible without the movement of either the supplier or the consumer.

8. A large part of the problem here may be that the Scheduling Guide focuses on the wrong question. There is no operational need, in the administration of the GATS, to classify transactions according to the modes of supply, though it might be interesting to do so for statistical purposes. The real function of the modes is to categorize commitments in national schedules. The question of the mode under which a transaction takes place only becomes important if there is disagreement about the legitimacy of a measure taken by a Member affecting the transaction, in which case the measure would be judged against the Member's commitments. Seen from this viewpoint, the distinction between modes 1 and 2 becomes clearer, and is operationally effective. If a Member has entered "None" under mode 1 for a particular service, any measure restricting the ability of a foreign provider to supply the service from across the border would be illegitimate; if it has entered "None" under mode 2, any measure restricting the domestic consumer's ability to buy the service abroad would be illegitimate. The four modes should therefore be seen essentially as the framework within which commitments are made, and which defines the freedom of Members to take particular kinds of measures. This is not a complete answer to the problems arising from the application of the modes, which certainly merit discussion, but it may be a helpful approach to the matter. In the context of electronic commerce, it means that in considering the consistency with national commitments of a measure affecting electronic supply, one would ask first on whom the measure impinged – the

[2] See paragraphs 7.277-7.286 of the report of the Panel on "European Communities – Regime for the Importation, Sale and Distribution of Bananas – Complaint by the United States" (WT/DS27/R/USA) and paragraphs 217-222 of the report of the Appellate Body on "European Communities – Regime for the Importation, Sale and Distribution of Bananas – Complaint by the United States" (WT/DS27/AB/R).

provider or the consumer – and judge its consistency in the light of commitments under mode 1 and mode 2 [3].

MFN (Article II)

9. Article II (MFN) is a general obligation which applies to all services sectors and all measures by Members affecting trade in services – unless, of course, a Member has listed a specific MFN exemption. The obligation requires each Member to accord immediately and unconditionally to services and service suppliers of any other Member treatment no less favourable than that it accords to like services and service suppliers of any other country. The standard of no less favourable treatment has already been interpreted to prohibit *de jure* as well as *de facto* discrimination between like services and service supplies of Members of the WTO.[4]

10. In principle, likeness depends on attributes of the product or supplier *per se* rather than on the means by which the product is delivered. If two like services were treated differently because they were delivered in different ways, then such treatment could be challenged as being inconsistent with the MFN obligation. By way of illustration, consider a goods example. If country X imposed a higher duty on a shirt sent by air than on a shirt sent by sea, then any exporter using air transport could legitimately claim that X was extending less favourable treatment to its product than to the like product of some other Member (who happened to use maritime transport). The situation would be no different if country X imposed a higher tax on legal advice delivered electronically than on the same advice delivered by post.[5] However, Members may wish to consider further the issue of likeness.

Transparency (Article III)

11. Like the MFN obligation, Article III (transparency) is a general obligation that applies to all services sectors. Members are required to publish all relevant measures of general application which pertain to or affect the operation of the GATS. These measures would include those which affect the electronic supply of services, and would also include measures taken by non-governmental bodies in the exercise of designated authority. The other obligations contained in Article III (the notification requirement in paragraph 3 and the requirement to establish enquiry points in paragraph 4) would also extend to measures of general application affecting the supply of services through electronic means. The field of electronic commerce is in general lightly regulated at present, but any existing regulations, or any which might be adopted in future would need to be notified under Article III.

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[3] Establishing the locus of a transaction for legal purposes may be important, however, for reasons which go beyond GATS disciplines. Issues concerning the country of legal jurisdiction of a transaction have already begun to arise in e-commerce, especially in relation to consumer protection, policing of illegal activities such as on-line gambling and obscenity, and, perhaps most importantly, determining the jurisdiction of validity and enforceability of commercial contracts and obligations. In business-to-business electronic commerce transactions, the parties (at least the larger firms) usually draft contracts indicating the agreed locale of jurisdiction for the matters concerned. But for other transactions, the locus of legal jurisdiction is an open question. However, this is not a matter relating to the scope of the GATS.

[4] See paragraphs 7.299-7.304 of the report of the Panel on "European Communities – Regime for the Importation, Sale and Distribution of Bananas – Complaint by the United States" (WT/DS27/R/USA) and paragraphs 231-234 of the report of the Appellate Body on "European Communities – Regime for the Importation, Sale and Distribution of Bananas – Complaint by the United States" (WT/DS27/AB/R).

[5] It is, of course, true that a Member may make *inter-modal* distinctions if its commitments with respect to the four modes differ. Thus it may allow cross-border delivery but not the establishment of commercial presence. But *intra-modal* distinctions based on the technique of delivery would in principle be open to challenge.

12. Electronic means can be used to disseminate information on measures affecting trade in services, including through enquiry points.

Increasing participation of developing countries (Article IV)

13. Effective participation in electronic commerce requires access to computers and related equipment at world prices, to efficient telecommunication services and to training. Article IV is concerned with enhancing the participation of developing countries in world trade. This is to be facilitated through negotiated specific commitments relating to strengthening their domestic service capacity *inter alia* through access to technology on a commercial basis, the improvement of their access to distribution channels and information networks, and the liberalization of market access in sectors and modes of supply of export interest to them. In principle, all these elements are relevant to electronic commerce. For instance, liberalization by the developing countries themselves in areas like telecommunications can lead to the development of the domestic infrastructure needed for electronic transactions. At the same time, liberalization by their trading partners of the cross-border delivery mode should facilitate sales of certain labour-intensive services in which developing countries have a comparative advantage which they have so far been unable to exploit because of restrictions on the movement of natural persons.

14. Under Article IV:2 developing countries service suppliers have access to contact points which are required to provide information related to the commercial and technical aspects of the supply of services, including by electronic means. Information on registration, recognition and obtaining of professional qualifications is likely to be particularly important, since fulfilling these requirements is likely to be a pre-condition for supplying many services irrespective of the mode of delivery. Developing country suppliers can also obtain information on the availability of relevant services technology, which may be particularly useful in the context of electronic commerce. Again, electronic means can be used to enhance the functioning of these contact points.

15. Issues relating to the transfer of technology would also be highly relevant in an area where technology is developing rapidly, as here.

Domestic regulation (Article VI)

16. Article VI requires that in sectors where specific commitments are undertaken, each Member should ensure that all measures of general application affecting trade in services are administered in a reasonable, objective and impartial manner. It also requires that each Member create judicial, arbitral or administrative tribunals or procedures which provide, at the request of an affected service supplier, for the prompt review of, and where justified, appropriate remedies for, administrative decisions affecting trade in services. All of these provisions apply to regulations or standards affecting the electronic supply of services. The question of standards is likely to be particularly important, since one of the basic characteristics of the Internet itself is the use of common frameworks and standards for interconnectivity and interoperability in order to maintain "universal" communication. To a degree perhaps not found it any other area, there is a need to ensure that technical standards do not constitute unnecessary barriers to trade in services.

Recognition (Article VII)

17. Article VII of the GATS, dealing with recognition, attempts to strike a difficult balance between its trade creating and trade diverting effects. On the one hand, Article VII:1, notwithstanding the general MFN obligation, allows Members to extend recognition unilaterally or through agreements to the education or experience obtained, requirements met, or licenses or certifications granted in another country. The remaining paragraphs of Article VII seek to ensure that the rights of third countries are protected - and that recognition does not have an unduly trade-diverting effect.

Article VII:2 requires a Member who enters into a mutual recognition agreement (MRA) to afford adequate opportunity to other interested Members to negotiate similar agreements. If a Member grants recognition autonomously, then it is obliged to give any other Member adequate opportunity to demonstrate that education, experience, licenses, or certifications obtained in that other Member's territory should be recognized. Article VII:3 stipulates that a Member must not grant recognition in a manner which would constitute a means of discrimination between countries in the application of its standards or criteria for the authorization, licensing or certification of services suppliers, or a disguised restriction on trade in services.[6]

18. The role of recognition may change with the development of electronic commerce. On the one hand, the possibility for distant transactions makes it more difficult for the regulatory authority to make recognition of qualifications a pre-condition for entry into the market. Thus it is possible for doctors and financial institutions from countries whose qualifications/regulations are not recognized by country X to offer their services over the Internet to consumers from X. On the other hand, distance may imply greater consumer ignorance of the true attributes of the supplier, so that the consumer becomes more reliant on quality signals such as recognition of the foreign qualifications/regulations by the home government. Thus we would expect recognition to continue to influence the pattern of trade, but more by playing an information role vis-à-vis the consumer than by acting as an entry condition for the supplier.

Competition-related Provisions

(a) Monopolies and Exclusive Services Suppliers (Article VIII)

19. Article VIII requires each Member to ensure that any monopoly supplier of a service does not "in the supply of the monopoly service in the relevant market" act in a manner inconsistent with the MFN obligation and the Member's specific commitments.[7] There are at least two respects in which Article VIII is relevant to electronic commerce. First, where the basic telecommunications service is still monopolised but market access has been granted to competitive Internet access providers, Article VIII would require governments to ensure that the monopolist does not discriminate against rival Internet access providers. They would, for example be entitled to reasonable terms and conditions for their access to and use of leased-circuits obtained from a public telecom operator when operating in a country that has taken commitments on their services. Secondly, Article VIII requires that exclusive suppliers of Internet services do not frustrate commitments made on other services which are being supplied by Internet.

20. The telecommunications sector is the focus of two additional sets of rules: the generally applicable Annex on Telecommunications, and the Reference Paper on regulatory principles in basic telecommunications which has been incorporated into their schedules of commitments by around 60 WTO Members. At the risk of some oversimplification, we can see the first as primarily a response to the central role of telecommunications as a medium of transporting services, and the second as a response to the particular difficulties in achieving liberalization in a sector characterized by dominant suppliers of network infrastructure in the foreseeable future.

[6] It is worth noting that Article VII:5 states that "wherever appropriate, recognition should be based on multilaterally agreed criteria" and requires Members to work towards the establishment and adoption of such criteria. The issue, of course, is how much discretion the phrase "wherever appropriate" gives Members in deciding whether to follow their own rather than internationally agreed criteria.

[7] A monopoly supplier of a service is defined in the GATS as any person, public or private, which in the relevant market of the territory of a Member is authorized or established formally or in effect by that Member as the sole supplier of that service (Article XXVIII(h)).

(b) The Annex on Telecommunications: Reinforcing Access Guarantees for Users

21. The Annex on Telecommunications is of particular significance for electronic commerce. It was drafted during the Uruguay Round by negotiators realizing that, despite Article VIII, telecom operators were in a unique position in having the potential to undermine commitments undertaken in schedules in any service sector in which telecommunications were essential to doing business. Three aspects of the Annex make it a more powerful defender of the rights of users of telecommunications services than Article VIII. First, it is silent about market structure and therefore applies to publicly available basic networks and services regardless of whether these are supplied by a monopoly or through competition.

22. Secondly, the Annex carries its own non-discriminatory disciplines on telecom service suppliers and, unlike Article VIII, does not depend on whether a Member has undertaken a national treatment commitment in the sector. The Annex requires governments to ensure that other Members' suppliers are afforded reasonable and nondiscriminatory access to and use of public telecommunications transport networks and services (PTTNS) for the supply of a service included in its schedule.[8] The term "non-discriminatory" refers to most-favoured-nation and national treatment as defined in the Agreement, as well as to sector-specific usage of the term to mean "terms and conditions no less favourable than those accorded to any other user of like public telecommunications transport networks or services under like circumstances". The suppliers of any service listed in a government's schedule, say financial services, are thus assured of non-discrimination with respect to access and use to telecom services even if a member has not committed to national treatment with respect to that particular service.

23. Finally, the Annex offers greater specificity in certain areas than Article VIII. For instance, it elaborates further on transparency obligations for the sector. It requires Members to ensure that relevant information on conditions affecting access to and use of public telecom transport networks and services is publicly available. It also lists examples of such measures. These include tariffs and other terms and conditions of service, specifications of technical interfaces with such networks and services, and conditions applying to attachment of terminals or other equipment.

(c) The Reference Paper: Ensuring Competition in the Supply of Telecom Services

24. In the basic telecommunications negotiations, there was concern that despite the commitments to liberalize both trade and investment, telecommunications markets would still frequently be characterized by dominant suppliers that controlled bottleneck or essential facilities.[9] Dominant players in the telecom market, left free to make decisions about how to treat other suppliers, would be capable of frustrating the market access and national treatment commitments made by governments in the negotiations.[10] Therefore, additional commitments on the behaviour of

[8] In Annex definitions: "Public telecommunications transport service" means any telecommunications transport service required, explicitly or in effect, to be offered to the public generally and typically involving the real-time transmission of customer-supplied information without any end-to-end change in its form or content. 'Public telecommunications transport network' means the public telecommunications infrastructure permitting telecommunications between and among network termination points.

[9] Participants felt that neither Article VIII nor the Telecom Annex would be adequately equipped to deal with potential anti-competitive practices. First, Article VIII did not cover dominant suppliers who may face limited competition. While the Annex was wider in scope, there were some doubts over whether the interconnection guarantees it contained applied to rival telecom suppliers and not just to the users of telecom services. Secondly, there was concern that the disciplines contained in Article VIII and the Annex were too general to guard sufficiently against possible anti-competitive practices. For example, the Annex contained no clear disciplines, beyond "reasonableness", over the pricing or promptness of access or on bundling practices.

[10] For instance, a major supplier, with control over essential facilities, could allow rivals to enter the local telephone call market but deny them dialling parity. That is, while its own customers had seven digit

major suppliers of telecoms services were assumed by the great majority of participants in the basic telecommunications negotiations. The regulatory principles embodied in the "Reference Paper" govern anti-competitive cross-subsidization, the terms of interconnection, the misuse of information, licensing criteria, transparency and other matters relevant to the prevention of abuse of dominant market positions. The Reference Paper, in so far as it fosters competitive conditions in the supply of telecommunication services, should help in the creation of efficient infrastructure for electronic commerce.

(d) Business Practices (Article IX)

25. In general, the development of electronic commerce should serve to enhance competition. First, the fixed costs of entering new markets are likely to be reduced: for instance, a bank can reach its clients without needing to create costly branches. Secondly, search and travel costs are likely to decrease: consumers can search more easily for cheaper services and are not obliged to consume them from proximate sources. Hence, electronic commerce should reduce the scope for trade-restrictive business practices by increasing both the contestability of markets and the mobility of consumers. However, it is not inconceivable that some suppliers may still acquire a degree of market power. If such suppliers resort to anti-competitive practices then Members can take advantage of Article IX which provides for consultation and information exchange between the concerned Members.

Protection of privacy and public morals and the prevention of fraud (Article XIV)

26. Article XIV of the GATS contains general exceptions which are obviously relevant to electronic commerce. The Article permits Members to take any measure necessary to achieve certain public policy objectives, including the protection of public morals and the maintenance of public order. Measures to curb obscenity or to prohibit internet gambling might well be justified on these grounds. Since both forms of electronic commerce – the supply of services online and the electronic retailing and wholesaling of goods and services – depend to some extent on the security and privacy of communications, it is worth noting that Article XIV(c) permits Members to take any necessary measures to protect the privacy of the personal data of individuals and the confidentiality of individual records and accounts, and to prevent deceptive and fraudulent practices. Like other such exceptions provisions, Article XIV is subject to a safeguard against abuse in that measures taken under it may be challenged by other Members on the ground that they are not necessary, or are more restrictive than necessary, to achieve the stated objective. Nor should they be applied in a manner which constitutes unjustifiable discrimination between Members or a disguised restriction on trade in services. Article XIV*bis* provides similar legal cover for actions taken by a Member to protect its essential security interests, but it does not include the necessity test embodied in Article XIV.

Specific commitments: market access and national treatment

27. Before we examine the GATS provisions on market access and national treatment, it may be useful to recall the types of services trade which are relevant to electronic commerce, and on which specific commitments may be made. Three types of transaction are involved:

(a) the provision of Internet access services themselves – meaning the provision of access to the net for businesses and consumers;

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telephone numbers, those of the rival could be allotted sixteen digit numbers. We can imagine the impact a seemingly innocuous "technical restriction" would have on the relative attractiveness for customers of the two suppliers.

(b) the electronic delivery of services, meaning transactions in which services products[11] are delivered to the customer in the form of digitised information flows;

(c) the use of the Internet as a channel for distribution services, by which goods and services are purchased over the net but delivered to the consumer subsequently in non-electronic form.

28. Electronic commerce requires access to the Internet network. The commercial provision of Internet access must be distinguished from the supply of other services through the medium of the Internet. Companies provide access in return for a fee. For this purpose they need access to telecommunications networks, usually by way of leased circuits. The treatment of Internet access services in GATS Schedules may need to be clarified. In many countries where the provision of telecommunications services is still a public monopoly, the monopoly provider is likely to be the only supplier of Internet access. In countries which have liberalised their telecommunications regime, competing Internet access providers (IAPs) may offer access to the Web, with a different array of supporting services. Ten Members have made explicit commitments on the supply of these services in the negotiations on basic telecommunications. Such explicit commitments are clearly necessary where monopoly or other access limitations apply to most telecoms services, but it is desired to liberalize Internet access. Members which have committed to full liberalization of basic telecoms have not in general felt it necessary to specify Internet access services. Members may wish to consider whether, possibly in the context of the next Round, it would be desirable to make more explicit commitments on Internet access in liberalized telecom markets, particularly since the obligations in the Annex on Telecommunications apply only to services on which a specific commitment is made. In general, the status of IAPs in relation to GATS rights and obligations would appear to merit further examination. As with all services, the absence of commitments does not of course mean that market access for IAPs is impossible: it may indeed be the case that provision of the service is not permitted, but it may equally mean only that there is no guarantee of continued access.

29. The electronic supply of services is understood to mean a transaction in which the service is supplied to the customer in the form of digitalized information; the entire transaction takes place electronically.

30. It is important to distinguish from the delivery of services in the form of digitalized information a second form of electronic commerce in which goods, and services which cannot be delivered electronically, are ordered and paid for on-line but are delivered to the customer in tangible form. This is essentially distribution services: the well known Amazon.com internet bookshop is an obvious example. Many businesses also sell their own goods and services directly to the public rather than through independent retailers or wholesalers, very often by electronic means: airline companies are an example of this. Commitments on distribution services under the GATS include electronic distribution, meaning the right to offer and sell goods on the Internet. In terms of GATS commitments the purchase of goods in this way is no different from ordering and paying for them by telephone or mail. If the goods ordered have to be imported, the importation will be subject to whatever tariff bindings and other GATT obligations are applicable. Tariffs applied to imported goods or services in this context are not covered by the standstill on customs duties on electronic transmissions which was agreed at the second Ministerial Conference in May 1998. Members may wish to give thought to the classification of certain marketing activities in the area of services, since here the existing classification systems are less clear than in the case of goods.

[11] The word "products" is sometimes mistakenly thought to be a synonym for "goods". Throughout this paper it is used to denote either a service or a good. Its usage in this sense in the services context is well established – as in "new financial services products".

31. It should be borne in mind that a commitment on distribution services is not a commitment to allow the supply of any service or good which may be offered for sale over the Internet. In the same way, a fully liberal commitment on basic telecommunications confers rights to supply telecommunications services; it is not a commitment to allow the supply of any service – banking services for example – which can be provided by telephone.

Market-access commitments on electronic supply of services (including commitments on basic and value added telecommunications services and on distribution services) (Article XVI)

32. Article XVI lists 6 types of restrictive measures which are prohibited unless they are scheduled. This is not of course an exhaustive list of all the measures governments may take to restrict or deny market access, but it is an exhaustive list of the types of market access limitations which can be scheduled and thus maintained. It does not include restrictions on the technical means by which a service may be delivered – for example, on supply by electronic means. This means two things: first, that no such restrictions could be scheduled and second, that such a measure, if taken, would not be in direct violation of specific commitments under Article XVI. However, it seems clear that if a Member were to prohibit or restrict the electronic supply of a scheduled service, the measure would be challenged under Article XXIII:3 as nullifying or impairing the benefits which other Members could reasonably have expected to accrue from the market access commitment. In other words it would probably become the subject of a "non-violation" complaint.

National treatment (Article XVII)

33. A full national treatment commitment requires a Member to extend to services and service suppliers of any other Member, in respect of all measures affecting the supply of services, treatment no less favourable than that it accords to its own like services and service suppliers. The standard for judging whether treatment is "no less favourable" for the purposes of Article XVII is whether the measure affects conditions of competition between foreign and national services and service suppliers in favour of the latter. Paragraphs 2 and 3 of Article XVII make it clear that the standard of no less favourable treatment prohibits *de facto* as well *de jure* discrimination between national and foreign service providers. It would also be possible to schedule a national treatment limitation discriminating against electronic supply by foreign service providers, though it may be questioned whether negotiating partners would find such a restriction acceptable. There are no such restrictions in national schedules at present. As discussed in the context of Article II on MFN, likeness in the national treatment context also depends in principle on attributes of the product or supplier *per se* rather than on the means by which the product is delivered.

Customs duties

34. Customs duties are border measures and would therefore be relevant to cross-border supply, whether under mode 1 or mode 2. It is very uncommon for them to be applied to services: the Secretariat is aware of only one case – the application of customs duties on ship repair services purchased abroad by the US. There may however be other cases and there is no reason in principle why customs duties should not be applied to services, whether supplied electronically or in any other way. Any duties so imposed would be "measures affecting trade in services" as explained above.

35. In May 1998 Members undertook a temporary commitment, which is not legally binding, not to impose customs duties on electronic transmissions. There are already in existence legally binding commitments on customs duties, as on other discriminatory taxes. In general it can be said that any tax which would increase the bound level of protection of a committed service would be inconsistent with a Member's commitments. In the context of the GATS what really matters is whether or not a Member has made a national treatment commitment ruling out recourse to discriminatory taxes. If a Member has made such a commitment in a particular sector, then all discriminatory taxes (including

customs duties by definition) are in any case prohibited. The GATS national treatment obligation applies to all measures affecting the supply of services, unlike the GATT national treatment obligation which does not apply to border measures like tariffs and quotas. The commitments on customs duties does not cover internal taxation. If a Member has not made a national treatment commitment, then it remains free to impose discriminatory internal taxes, so the commitment not to impose customs duties would not preclude recourse to discriminatory measures with an identical effect. Hence, in the GATS context it is the national treatment commitment which is crucial to ensuring equality of competitive conditions. A national treatment commitment would not of course affect a Member's freedom to impose taxation on a non-discriminatory basis.

Classification issues

36. All services are covered by the GATS, whether delivered electronically or otherwise, and the classification of virtually all services products is not in doubt – even though, as has been made clear in the exchange of information exercise, the existing classification systems are often imperfect or incomplete. However questions have arisen relating to the classification of certain products which can be delivered both in electronic and physical form. The most clear example is standardized computer software, which can be supplied electronically over the internet or sold on a physical carrier. These different forms are very close substitutes for each other, and from the customer's view point their content is the same. This phenomenon of close substitutability gives rise to the question whether the trade regime applying to the electronic and physical forms should also be the same.

37. It is important to maintain the principle that all services delivered electronically are covered by the GATS: the question here is whether some products delivered electronically should be defined and treated as not being services. It is not a matter which can be decided by simple reference to a definition, since we have no comprehensive definition either of services or of goods. The great bulk of products delivered electronically, like telecommunications and financial services, are clearly identified in the services classification lists and in GATS Schedules, so their classification is not an issue. And the only products delivered electronically which are subject to internationally recognized and enforced obligations (through the GATS) are services. But there is no classification which would permit us to say that all intangible products, or even all electronically delivered products, are services by definition. One of the important characteristics conventionally distinguishing services from goods has been that goods are tangible, and of course it would be impossible to deliver a tangible product electronically. But it would be possible for Members, if they saw any practical advantage in doing so, to agree that some intangible products should be regarded and treated as goods even when electronically transmitted, in which case the rules of GATT would apply to them. The most important consideration, however, would be the criteria on the basis of which such products would be distinguished from other products delivered electronically and whose status as services is not in question. Any suggestion that "electronic transmissions" as such should be regarded as outside the scope of the GATS would of course fundamentally damage the entire Agreement and undermine a wide range of existing commitments, since the vast majority of cross-border trade in many sectors is done electronically. It should be remembered that the legal regime applying to transactions throughout the WTO system – whether they are governed by the GATS, the GATT or a sectoral agreement such as those on Agriculture or Textiles – is determined by the nature of the products being traded, not by the means of their delivery.

38. In a related argument it is pointed out that electronically transmitted books and other digitalized information can be "downloaded" and copied, thus creating a tangible good – and that digital technology permits large-scale copying of high quality. It should be clear that the issue before the Services Council is the classification of the electronic transaction – the transmission and receipt of the text or other digitalized information over the Internet. What is done with the information after downloading is another matter. If hard copies are produced, whether legally or not, this is a manufacturing process resulting in the production of goods, into which the electronic transmission

could be seen as a services input: as we know, virtually all manufactured goods involve services inputs of various kinds. If such copying is done without authority, and particularly if it is done on a commercial scale, there would be a problem of copyright piracy which should be dealt with under the law of the country concerned. This is not a new problem – copyright piracy of printed and broadcast material has been going on for generations – but the high quality of digitalized copying may give it a new dimension. However, this is a matter for the TRIPS Council.

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