NATIONAL TREATMENT AND MARKET ACCESS: ISSUES IN TRADE IN SERVICES

by

Debra P. Steger

August, 1988

Series on Trade in Services

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PREFACE

The objective of this paper is to examine the implications for the Contracting Parties of the General Agreement on Tariffs and Trade of adopting new legal obligations, particularly the principle of national treatment, for international trade in services.

In this study, we review the trade in services provisions of the Canada-U.S. Free Trade Agreement and outline the experience of the European Economic Community in liberalizing services trade.

Our examination of the European Economic Community's experience leads us to ask the question:

> *Is a commitment to national treatment, in itself, sufficient to achieve liberalization of trade in services?*

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TABLE OF CONTENTS

I. INTRODUCTION

Trade in services has become an increasingly significant element of world trade. Consequently, liberalization of trade in services and resolution of international disputes involving services have become matters of major concern to the world trading economy. On the initiative of the United States, the General Agreement on Tariffs and Trade ("GATT"), which has dealt traditionally with trade in goods, is tackling the problem of liberalizing trade in services in the Uruguay Round of multilateral trade negotiations. The Canada-U.S. Free Trade Agreement ("FTA") represents a significant breakthrough in liberalization of trade in certain services sectors between the two countries. While the FTA represents the first comprehensive attempt by Canada and the United States to develop new rules governing international services trade, the European Economic Community has had considerable experience in attempting to liberalize services trade. This paper reviews the trade in services provisions of the FTA and examines the experience of the European Economic Community in liberalizing services trade.

II. SERVICES IN THE CANADA-U.S. FREE TRADE AGREEMENT

1. TRADE IN SERVICES

Trade in services has become an increasingly significant feature of the world economy. In 1985, world trade in services was estimated to be in the range of $400-$500 billion annually, about one-quarter of the amount of world trade in goods. In Canada and the United States, services account

for an overwhelming percentage of gross domestic product and a major source of employment growth. In 1984, Canada-U.S. trade in services represented approximately $20 billion.

Despite its significance in the world economy, international services trade, by and large, is not regulated by international agreements. The General Agreement on Tariffs and Trade ("GATT") is focused primarily on trade in goods. As a result of U.S. initiatives, some of the 1979 Tokyo Round agreements include provisions covering some goods-related services trade. The United States has emphasized trade in services as a priority in the Uruguay Round of multilateral trade negotiations currently underway.

The FTA represents an important first step in the adoption of general principles governing trade in services albeit on a more limited basis than the European Economic Community commitment to a common market. The FTA, although groundbreaking, is also cautious in its approach to the regulation of bilateral services trade. It is cautious because it applies only to "covered services" and does not, for the most part, require changes to existing measures.

(a) General Services

"Covered services" under the FTA include agriculture and forestry, mining, construction, distributive trades, insurance and real estate, and commercial services. The latter includes cleaning services; advertising and promotional services; collection agency services; telephone answering services; services to buildings; equipment rental and leasing services; personnel supply services; hotel services; professional services; commercial, economic, marketing, and statistical services; public relations services; repair and maintenance services; business consulting services; management services; computer services; telecommunications services and tourism services. In the area of professional services, the FTA covers engineering, architectural and surveying services, accounting and auditing services, scientific and technical services, librarian services, and agricultural consulting services.

Financial services are dealt with in a separate chapter of the FTA. The general services chapter does not apply to financial services, with the exception of insurance. Transportation services and cultural industries are also excluded from the services chapter, as are basic telecommunications services (such as telephone services), doctors, dentists, lawyers, childcare and government services (such as health, education and social services).

The obligations contained in the FTA are not as extensive as some of the U.S. proposals for regulation of international services trade being advanced in the Uruguay Round of multilateral trade negotiations. Only in the areas of financial services, tourism, architecture, and enhanced telecommunications services (dealt with in specific chapters or sectoral annexes) will the FTA require any changes to existing laws, regulations or policies.

With respect to the future, the FTA establishes the GATT principle of national treatment as the primary obligation in the services area. Subject to certain qualifications, Canada and the United States have agreed to treat persons or firms of the other country no less favourably than their own nationals with respect to the provision of covered services. Under the FTA, provision of covered services includes:

- the production, the distribution, sale, marketing and delivery of a covered service and the purchase or use thereof;
- access to, and use of, domestic distribution systems;
- the establishment of a commercial presence (other than an investment) for the purpose of distributing, marketing, delivering or facilitating the covered service; and
- any investment for the provision of a covered service and any activity associated with the provision of a covered service.

The obligation to provide national treatment applies to provincial and state governments as well as to the federal governments of both countries. Governments, however, will not be restricted from treating nationals of the other country differently from their own nationals where the difference in

treatment is no greater than is justified for prudential, fiduciary, health and safety or consumer protection reasons. Where a government proposes a new policy that discriminates against foreign nationals, it must notify the other country prior to implementing the new policy, and must be able to justify it as being no greater than necessary for one of the above public policy objectives.

Beyond the basic national treatment obligation, there is a requirement that neither country may introduce any measure that constitutes a means of arbitrary or unjustifiable discrimination against persons of the other country or a disguised restriction on bilateral trade in covered services. The FTA provides explicitly that the services chapter imposes no obligations or rights concerning government procurement practices or the use of subsidies. In other words, in a covered services area such as advertising, a government that chose to specify that government contracts for advertising services would be granted only to locally-based companies would not be affected by the terms of the FTA. Also, if a government decided to provide a new subsidy program or tax benefit to encourage the provision of accounting services in a particular region, it would not have to allow nationals of the other country equal opportunity to qualify for benefits under that program. The services obligations also do not apply to any new taxation measure as long as it does not constitute a means of arbitrary or unjustifiable discrimination or a disguised restriction on trade between the two countries.

The benefits of freer trade in services are exclusively reserved for persons that are nationals or controlled by nationals of either Canada or the United States. Both countries have reserved the right to deny the benefits of the services chapter to firms that are owned or controlled, directly or indirectly, by persons from a third country.

A special obligation has been included in the FTA governing licensing and certification procedures. Both countries have agreed in principle that licensing and certification requirements for professional or other services should relate to matters of competency or the ability to provide a service and should not have the effect of impairing the access of

nationals of either country to provide their services in the other country. To that end, Canada and the United States have agreed to work together to develop methods for mutual recognition of licensing and certification requirements for the provision of covered services by persons of either country.

Understanding the national treatment obligation is critical to understanding the services chapter of the FTA. The obligation to extend national treatment to nationals of the other country means that Canada and the United States have agreed to treat providers of services from the other country no less favourably than domestic providers of the same services in like circumstances. However, if there are important health, safety, prudential, fiduciary or consumer protection reasons for treating firms of the other country differently, governments may do so as long as the treatment is equivalent in effect. Existing laws and regulations that are discriminatory may be maintained but, if amended, there is an obligation not to make them more restrictive.

The national treatment obligation will not in itself lead to the harmonization of regulation of services on both sides of the border. In fact, in the annex on enhanced telecommunications services, it is explicitly recognized that the two countries will have different regulatory systems with different procedures for setting rates, licensing providers of services and otherwise regulating the provision of services. The primary obligation for regulators in future will be to ensure that Canadian and U.S. providers of covered services operating in the same country are treated equivalently.

Canada and the United States both recognize that the rules on services trade, although a significant first step, are not an end in themselves. The two countries have agreed to cooperate further to develop new rules and to extend the obligations of the services chapter by negotiating further sectoral annexes and modifying or eliminating existing measures that are contrary to the FTA principles.

(b) Financial Services

Federally-regulated financial services are covered in a separate chapter of the FTA. The services chapter applies only to insurance services, and not to other financial services. Provincial or state regulation of securities dealers, loan and trust companies, near banks and other financial institutions is not covered by the FTA.

Canada has already started the process of deregulation in the financial services sector. As a result, the strict separation that traditionally existed between the functions of banks, insurance companies, trust and loan companies and securities dealers is being largely relaxed. Although some U.S. states are beginning to permit some cross-ownership of financial institutions, there has been no major regulatory overhaul of U.S. federal banking legislation as yet.

The FTA has had to accommodate this regulatory disparity by imposing rather different obligations on the United States and Canada in the area of financial services. With respect to future regulatory changes to the *Glass-Steagall Act* and other federal legislation, the United States has agreed to accord Canadian-controlled financial institutions the same treatment as their U.S.-controlled counterparts. Canada has agreed to provide U.S.-controlled financial institutions with the opportunity to expand through the acquisition of other financial service businesses as a result of the deregulation process. The former commitment involves future consideration; the latter commitment involves modifications to existing laws and policies.

Despite the strict separation of powers among the different types of financial institutions in the U.S., banks are currently authorized to underwrite and deal in debt obligations of, or guaranteed by, the United States of America or its political subdivisions. The FTA would permit domestic and foreign banks to trade in a similar way in the debt instruments of Canadian federal and provincial governments. Future U.S.

issues of provincial hydro-electric utility bonds, for example, could be floated through U.S. banks rather than exclusively through underwriting houses.

Foreign banks operating in the United States have enjoyed favoured treatment in that they have been allowed to expand beyond the limits of a state in circumstances where their U.S.-owned competitors are often confined to a single jurisdiction. This privilege is currently scheduled to be reviewed in 1988. The FTA provides Canadian-controlled banks with a standstill guarantee that they will not, in any event, lose their existing right under the *International Banking Act of 1978* to operate in more than one jurisdiction.

For its part, Canada will be required by the FTA to amend a series of federal statutes that impose foreign ownership restrictions which inhibit the sale of a substantial interest in a bank, a life insurance company, a sales finance company, a loan company or a trust company to non-Canadians. Generally speaking, these statutes prohibit the entry in the books of the financial institution of any transfer of shares that would result in ten per cent or more of the shares being held by an individual who is not ordinarily resident in Canada, or by a legal entity controlled by any such individuals. The entry of a transfer of shares of such an institution is also generally prohibited if the result would be that a number of non-Canadians would hold, in the aggregate, twenty-five per cent or more of the outstanding shares. Existing Canadian federal legislation will have to be amended to make these prohibitions inapplicable to U.S. or U.S.-controlled investors.

The Canadian government has recently proposed new legislation that would require approval for any transfer of shares in an insurance company, a loan company or a trust company that would result in any one person, together with associates, holding ten per cent or more of the outstanding shares of any class of shares of the financial institution. This requirement is not specifically related to foreign-ownership concerns. Rather, it relates to concerns about corporate concentration. The FTA would prohibit the use of this review power in a discriminatory manner so

as to prevent U.S.-controlled entities from acquiring shares in a Canadian financial institution, while allowing Canadian-controlled entities to make such an investment.

There is a large gap in the FTA rules with respect to U.S. investment in Canadian financial institutions as they will not apply to any measure of a provincial government. Provincial governments play a very significant role in Canada in the incorporation and regulation of financial institutions other than banks. Many such institutions are incorporated provincially. Some provinces impose their own foreign ownership restrictions upon entities constituted under provincial law; for example, Ontario loan and trust companies are subject to the same ten per cent (and twenty-five per cent in the aggregate) restriction on transfers of shares to foreigners, as currently applies to federally-incorporated loan and trust companies. That provincial limitation will not have to be changed as a consequence of the FTA.

The provinces also exercise regulatory jurisdiction over non-bank financial institutions that carry on business within their territories irrespective of the jurisdiction of incorporation of such an institution. Even a federally-incorporated and licensed insurance, loan or trust company must hold a provincial licence in most Canadian provinces in which it carries on business; it cannot operate as of right under the authority of its federal licence. Although the provinces do not now require any degree of Canadian ownership as a condition for initial or continued licensing, the FTA would not preclude them from creating such a condition in future, except in relation to insurance services. The services chapter of the FTA would prohibit new provincial measures relating to the provision of insurance services that discriminate against U.S. or U.S.-controlled entities.

Finally, the financial services chapter of the FTA will eliminate some of the restrictions under the Canadian *Bank Act* on the operation and expansion of foreign bank subsidiaries (Schedule B banks) as they apply to U.S.-owned entities. In particular, in the case of Schedule B banks that are subsidiaries of U.S. banks:

- the amount of capital is not to be constrained by the umbrella limit on the domestic assets of foreign bank subsidiaries;

- the opening of branches is not to require Ministerial approval; and

- the transfer of loans from a bank subsidiary to its parent is to be permitted subject to prudential requirements of general application.

In summary, the financial services chapter represents an incomplete, piecemeal approach to some isolated issues in the financial services area that are not the same on both sides of the border. The two countries explicitly recognize that this chapter does not signify their "mutual satisfaction ... concerning the treatment of their respective financial institutions" and that laws and policies should evolve to the mutual benefit of both countries as the rules governing financial markets are liberalized. Further bilateral negotiations relating to financial services will be the responsibility of officials of the Canadian Department of Finance and the U.S. Department of Treasury. The general dispute settlement mechanisms of the FTA will not apply to the financial services sector.

(c) Telecommunications and Computer Services

A sectoral annex to the general services chapter of the FTA provides specific commitments with respect to "enhanced" telecommunications and computer services. For regulatory purposes, "enhanced" telecommunications services have been distinguished from "basic" services. The Canadian Radio-television and Telecommunications EEC Commission (the "CRTC") and the U.S. Federal Communications EEC Commission (the "FCC") have adopted essentially the same definition of "basic" services as the provision of direct transmission capacity. Both

regulatory agencies include in their definition of basic service: speed, code, and protocol conversion which occurs within the carrier's network as long as the transmission parameters do not alter the nature of the transmission. "Enhanced services" are defined, by the CRTC and the FCC, as everything else, and include the storage, manipulation, and transmission of data on a commercial basis. The FTA incorporates the same definitions of basic and enhanced services as those employed by the CRTC and the FCC.

Computer services are defined with some precision in the annex to mean services, whether or not conveyed over the basic telecommunications network, that involve generating, acquiring, storing, transforming, processing, retrieving, utilizing or making available information in a computerized form. A number of such services are listed, including computer programming, prepackaged software, computer-integrated systems design, computer processing and data preparation. This list makes it clear that the annex, while primarily directed at ensuring a free, non-discriminatory flow in computing services that ride the telecommunications networks of each country, also comprehends the direct provision of computer services.

Insofar as the direct provision of computing services is concerned, this annex is an important complement to the general rules on commercial presence in the services chapter and the chapter on temporary entry for business persons which will ease transborder movements of computer services, sales management, installation and maintenance personnel.

The provisions of the services chapter will apply to the following regulatory measures relating to enhanced communications and computer services:

- access to, and use of, basic telecommunications services including local and message toll or long distance service, private-line or leased-line services, dedicated voice and data networks;
- resale and shared use of basic telecommunications services;

- the purchase and lease, or attachment, of customer premises equipment (e.g. telephone sets, private branch exchanges, data terminals);
- regulatory definitions of basic and enhanced services;
- technical standards for certification, testing or approval procedures (subject to the product standards chapter); and
- the movement of information across borders and access to data bases or related information stored in the other country.

The annex itself provides that Canada and the United States will maintain existing access to basic services for the provision of enhanced and computer services, and maintain or introduce effective measures to prevent anti-competitive conduct by a monopoly telecommunication carrier in the enhanced services market, either directly or through dealings with its affiliates that adversely affect a firm in the other country. Anti-competitive conduct is defined as including cross-subsidization, predatory conduct, and the discriminatory provision of access to basic telecommunication facilities or services.

This annex confirms existing regulatory policies on enhanced telecommunications services in both Canada and the United States and does not require any specific changes to existing policies or practices. It does not require the introduction of any more telecommunications service competition than already exists in federally-regulated telecommunications markets in Canada and the United States. The annex may, however, create an incentive to bring Canadian and U.S. regulatory measures aimed at preventing anti-competitive behaviour by monopoly telecommunications carriers more into line.

Provincial telecommunications regulators have, on the other hand, lagged behind the CRTC in allowing enhanced services competition. The FTA may create pressures on them to catch up to the CRTC, thereby establishing a national enhanced telecommunications services market in Canada. Generally, U.S. state regulators have adopted a competitive stance to enhanced services similar to the FCC's policy.

An important provision of this annex is that Canada and the United States have agreed not to impose new limits on transborder data flows for industrial development purposes. Current restrictions on data processing contained in the Canadian *Bank Act*, however, will be maintained. The possibility of adapting measures to prevent the storage and processing of Canadian-originating information in the United States in order to stimulate a domestic data processing industry has been a recurrent theme in Canadian government circles over the last twenty years.

The provisions of this annex are intended to work together with the accelerated reductions in tariffs on computing equipment. The greater certainty of non-discriminatory network access for enhanced services in both countries may encourage greater marketing efforts by computing equipment firms in each country.

(d) Architecture

A separate annex to the services chapter will apply to measures relating to the mutual recognition of professional standards and criteria for the licensing and conduct of architects and the provision of architectural services.

Canada and the United States have agreed to endorse and promote the adoption of mutually acceptable professional standards and criteria relating to education, examination, experience, professional development and conduct and ethics for architects. The Royal Architectural Institute of Canada and the American Institute of Architects have undertaken to develop, in consultation with the appropriate regulatory bodies, mutually acceptable professional standards and criteria prior to the end of 1989.

Upon receiving the recommendations of these professional associations, Canada and the United States have agreed to encourage provincial and state regulatory authorities to accept and adopt their recommendations on mutual recognition of architects.

(e) Tourism

Tourism services are covered in another sectoral annex to the services chapter. The services covered by this annex include travel agencies, travel insurance, international passenger transportation, hotel reservation services, transportation terminal services, tour operations, and related retail and rental services.

In this annex, Canada and the United States have agreed to maintain in future the free and open practices both countries employ now with respect to tourists from the other country. The real purpose of this annex is not to eliminate any bilateral restrictions on tourism trade but to set an example for other countries in the Uruguay Round of multilateral trade negotiations.

In particular, Canada and the United States have agreed that neither country will impose restrictions in its territory on the promotion of tourism opportunities by the other country or by its provincial, state or local governments. Any departure or arrival fees charged by either country to tourists from the other must be applied equally to nationals of the country imposing the fees and be limited to the approximate cost of services rendered. Any restrictions imposed by one country on the value of tourism services that its residents or visitors to its territory may purchase from persons of the other country must conform to provisions of the Agreement of the International Monetary Fund ("IMF") which prohibit the imposition of restrictions on international currency payments and transfers without the approval of the IMF and which prohibit currency practices that discriminate against other parties to the IMF Agreement.

Adoption of the principles contained in this annex will not represent any change in the *status quo*. Currently, neither country imposes departure or arrival fees or currency restrictions on tourists from the other country. There is now a virtually unrestricted market in tourism between Canada and the United States. The two countries have also agreed to consult at least once a year to identify and eliminate impediments to tourist trade and to find ways of facilitating increased tourism between them.

2. TEMPORARY ENTRY OF BUSINESS PERSONS

A general easing of restrictions on the cross-border movement of business personnel between Canada and the United States will be an important factor in facilitating the free flow of goods and services between the two countries. In the last few years restrictions on the entry of consultants and professionals as well as sales representatives and maintenance personnel have been a significant non-tariff barrier to trade. The FTA establishes a special regime for temporary entry of Canadian and U.S. citizens into each other's territory for business purposes. No changes are contemplated in the immigration rules that determine who will be granted permanent resident status by either country.

On the Canadian side, there are a number of regulations and policies that will have to be changed as they apply to U.S. business persons engaging in temporary business activities in Canada. Under the Canadian *Immigration Regulations*, an individual who is neither a citizen nor a permanent resident (landed immigrant) of Canada may not work in Canada without first obtaining an employment authorization, commonly called a "work permit." There are a few exceptions to this requirement but none that favour a person who is employed or self-employed outside Canada or who will not be paid from Canadian sources for his or her services performed in Canada.

Under existing law, a U.S. employee of a U.S. business enterprise, a U.S. entrepreneur or a U.S. professional would normally have to obtain a work permit to carry out any business function in Canada. The harshness of this is only alleviated by Canadian immigration officials stretching the exceptions or turning a blind eye. The difficulty that a visitor faces in satisfying the work permit requirement is not just the cost ($50) and the paper burden but, more importantly, meeting the usual condition of having to persuade an officer of Employment Canada to certify that job opportunities for Canadian citizens or permanent residents will not be adversely affected by the issue of the permit.

The FTA would require Canada to grant temporary entry, without the necessity of a work permit, to any citizen of the United States who is engaged in trade in goods or services or in investment activities and who comes to Canada in the course of performing certain occupational functions and for certain business purposes, all as specifically prescribed by the FTA. The listed occupations involve some degree of skill and, in most cases, the type of activity carried out in Canada must be limited either in its nature or in that the principal beneficiary must be U.S.-based. In particular, the categories include:

- technical or market researchers carrying out research for an enterprise located in the United States;
- purchasing, production management, financial services and supervisory personnel involved in transactions for an enterprise located in the United States;
- sales representatives taking orders for goods or services;
- buyers purchasing for an enterprise located in the United States;
- installers and maintenance personnel performing certain after-sales services in respect of equipment purchased from an enterprise located outside Canada; and
- public relations and advertising personnel consulting with business associates.

Some of these categories already have the benefit, in part at least, of existing exceptions to the work permit requirement under the *Immigration Regulations*; others are brand new exceptions and will clearly reflect special treatment for U.S. business visitors to Canada.

As there are also FTA provisions relating to intra-company transferees, referred to below, we assume that the business visitor rules will not apply to U.S. citizens who have been seconded for a period of time to a Canadian affiliate or branch of their U.S.-based employer. Such an individual would probably be treated as having ceased to work for an enterprise located in the United States, for the purposes of the business visitor categories, and therefore as eligible to enter Canada, without an immigrant visa, only if qualified under the intra-company transferee rules.

In fact, the FTA does not make it clear what length of stay or what number of periodic visits may be enjoyed by a business visitor or, indeed, when the privilege of temporary entry may be taken to have been abused in that a temporary stay has become, in fact, a long term settlement.

U.S. business visitors to Canada may be subject to exclusion, as other visitors, on security or health grounds. But, otherwise all that may be required is proof of U.S. citizenship and demonstration of the purpose of the visit in terms that fall within one of the designated categories.

In certain other situations not coming within the business visitor rules, Canada will be obliged to issue work permits to U.S. citizens engaged in trading in goods or services or in investment activities, enabling them to enter and work in Canada under the authority of such a permit. A work permit may be issued at a port of entry (a border crossing, an airport or a port) to a U.S. citizen and need not be secured in advance from a Canadian immigration post outside the country.

When a work permit is required to be issued to a U.S. citizen by the terms of the FTA there will be no underlying requirement that an officer of Employment Canada first certify that in his or her opinion there will be no adverse effects on employment opportunities for Canadian citizens or permanent residents. The groups that will get the benefit of certification - free (validation exempt) entry are intra-company transferees, traders and investors and professionals.

Intra-company transferees are U.S. citizens seeking temporary entry to Canada to work, within their corporate or business group, in a capacity that is managerial, executive or involves specialized knowledge. They must be destined to work or render services in Canada for an employer for whom they have worked continuously for at least a year immediately prior to entry, or an affiliate or subsidiary of such an employer.

Canadian immigration policies currently permit the entry of senior executive or managerial staff on an intra-company transfer basis without any employment certification. However, the FTA would appear to

contemplate the broadening of this policy insofar as it affects U.S. transferees, so as to cover managerial and executive personnel who are not top management, and personnel utilizing "specialized knowledge" who are not managers of any kind. The latter description may prove to be particularly elastic, capable of describing a broad spectrum of experienced and skilled workers. Under the present policy transferees must be assigned to work at permanent and continuing establishments of their employer in Canada. As a result, employees intending to work on construction or other engineering sites or projects are not eligible for consideration as intra-corporate transferees. The FTA would preclude any such blanket exclusion for U.S. citizens in the future.

The trader and investor classification under the FTA covers, first, U.S. citizens carrying on a substantial trade in goods or services who are seeking temporary entry to Canada in a capacity that is supervisory or executive or involves essential skills. The trade in question must be primarily between Canada and the United States. Since sales representatives, purchasers of goods and services, and certain service personnel may enter with even fewer impediments as business visitors, the number of U.S. citizens seeking temporary entry to Canada as traders may not be significant.

This classification, in its second element, covers a U.S. citizen who would enter Canada on a temporary basis solely to develop and direct the operations of an enterprise in which he or she has invested, or is in the process of investing, a substantial amount of capital. The investment need not involve control of the Canadian enterprise and, indeed, could be a debt rather than an equity investment. It is probably sufficient if the capital invested is a substantial sum in the abstract although some might argue that it must be substantial in relation to the overall capitalization of the enterprise.

Finally, U.S. citizens who are engaged in professions of a kind described in the FTA may enter Canada on a temporary basis. As is evident from other chapters of the FTA, this does not mean that they would then be entitled, as of right and without holding any relevant federal or

provincial certification, to carry out professional activities of such a nature and duration as to constitute professional practice in a Canadian jurisdiction.

The professions included for the purposes of this classification are not just those occupational categories that have been traditionally recognized as professions or that involve a substantial measure of self-governance, but extend to such occupations as that of hotel manager and technical publication writer. In some instances, a certain minimum academic or work experience is essential and, in a few cases, the type of professional activity that may be carried out is limited, for example, U.S. physicians may only be engaged in teaching or research in Canada. Professionals may be asked, at the port of entry into Canada, for proof of citizenship and documentation demonstrating that they are engaged in one of the listed professions and describing the purpose of entry.

As in the case of U.S. business visitors or any other visitors, those U.S. citizens who will be entitled to enter and work in Canada on the basis of a work permit issued on a certification-free basis will be subject to general security and health restrictions. A work permit is usually issued, in accordance with current Canadian practice, for a period of up to one year, subject to further extensions. After a permit holder has been in Canada for three years or so, there is likely to be some reluctance on the part of an immigration officer to grant a further renewal, particularly without certification by an officer of Employment Canada. As in the case of business visitors, the FTA is silent as to when a temporary sojourn may be properly characterized as having become permanent. Since the FTA contemplates the issue of work permits to intra-corporate transferees, traders and investors, and professionals, it may be assumed that the present timetable for that instrument of approval will, at least, be acceptable.

An individual who has a complaint about being denied entry contrary to the provisions of the FTA must use the administrative appeal mechanisms available under Canadian or U.S. immigration law. If

immigration authorities of one country engage in a pattern of practice contrary to the FTA, the other country may invoke the FTA institutional provisions to resolve the problem.

We have described the FTA provisions permitting temporary entry of U.S. citizens into Canada for business purposes. The obligations upon the United States in relation to Canadian business persons are essentially reciprocal. There are some technical variations because of differences in regulations under the Canadian *Immigration Act* and the U.S. *Immigration and Nationality Act*. It should be noted that preferential admission into either country is open only to citizens of the other country and not to permanent residents or landed immigrants.

The FTA represents a first step toward the freer movement of business personnel between Canada and the United States. The objective of the FTA is to reduce the unnecessary harassment that many business travellers experience at the border. Over the longer term, a consultative mechanism will be established, at the level of immigration officials, to develop measures for further facilitating temporary entry of business persons between Canada and the United States on a reciprocal basis.

3. INVESTMENT

(a) Foreign Investment Policies

Government policies and programs regulating foreign direct investment have often been a source of friction in Canada-U.S. relations. In the 1950's and 1960's, a period of tremendous growth, U.S. investment flowed relatively freely into Canada. As a result, by the early 1970's, about three-fifths of the Canadian manufacturing and mining industries, and approximately three-quarters of the Canadian petroleum industry, were foreign-owned, principally by U.S. investors.

In response to growing concerns in Canada about increasing levels of foreign ownership, the government of Canada introduced the *Foreign Investment Review Act* ("*FIRA*") in 1973. Under *FIRA*, establishment of

new businesses in Canada, direct acquisitions of Canadian businesses by foreign firms and indirect acquisitions of Canadian businesses (involving transfers of ownership of foreign-based parent corporations) were subject to review to determine whether such investments were of "significant benefit" to Canada. During the review process, foreign firms were often encouraged to give undertakings about export performance, import substitution, employment, local sourcing of products, research and development efforts and capital investment plans.

Although *FIRA* was always controversial, U.S. complaints reached a boiling point in the early 1980's when the Canadian government initiated the National Energy Program and proposed more aggressive regulation of foreign investment under *FIRA*. The U.S. government protested and subsequently brought a complaint under the GATT regarding certain of the commitments commonly included in undertakings given to the Canadian government pursuant to *FIRA*. A GATT panel found that Canada had contravened the GATT by urging private firms to commit to source supplies in Canada but ruled that the GATT did not apply to export performance requirements. Canada accepted the GATT ruling and altered its practices under *FIRA*.

In 1984, the new Conservative government introduced the *Investment Canada Act* which altered *FIRA* considerably. The *Investment Canada Act* eliminated the requirement of review for the establishment of new businesses except for cultural businesses, and established thresholds of $5 million (Cdn.) and $50 (Cdn.) million for review of direct and indirect acquisitions, respectively. Although the *Act's* objective is to promote direct investment in Canada, the Investment Canada agency continues to seek undertakings from foreign investors in a limited number of sectors, such as the oil and gas industry.

The FTA will reinforce the recent trend toward liberalization of Canadian foreign investment policies and provide greater transparency in the investment restrictions that remain on both sides of the border. Except

for the cultural, financial services and transportation industries, future bilateral disputes over investment policies and programs will be subject to the general dispute settlement procedures provided in the FTA.

The investment chapter of the FTA parallels many of the obligations and commitments contained in the services chapter. With the exception of certain changes to the *Investment Canada Act* agreed to in the FTA, all other existing investment restrictions and review requirements are grandfathered and may be amended. Any entirely new investment policies or regulations must be consistent with the principle of national treatment. In other words, any new policies or programs designed to regulate foreign investment in future must not discriminate against U.S. investors. This applies to provincial governments as well as to the federal government. The investment provisions apply to all goods-producing activities and services activities covered in the services chapter, with certain specific exclusions. The transportation industry, the cultural industries, and financial services, except for insurance services, are excluded from the provisions of the investment chapter.

The national treatment obligation concerning future investment policies applies to the establishment of a new business or the acquisition of control of an existing business by a U.S. investor, subject to the provisions of the FTA. Canada has agreed to make certain changes to the *Investment Canada Act* as it applies to investments by U.S. investors. Specifically, Canada has agreed to phase out the screening of indirect acquisitions within three years after the FTA comes into effect and to raise the threshold for screening of direct acquisitions to $150 million (Cdn.) by 1992 from $5 million (Cdn.) at present. Currently under the *Investment Canada Act*, an acquisition by a non-Canadian is not reviewable if the gross assets of the Canadian business to be acquired are less than $5 million (Cdn.) in the case of a direct acquisition, or less than $50 million (Cdn.) in the case of an indirect acquisition.

In response to U.S. grievances concerning FIRA's former propensity to request undertakings, the FTA explicitly precludes the imposition of trade-related performance requirements on U.S. investors. Thus,

Investment Canada or any other investment review agency in future may not require U.S. investors to provide undertakings with respect to export performance, import substitution, local sourcing or levels of domestic content. However, an investment review agency, as a condition of approving an investment in future, may continue to require a U.S. investor to give undertakings relating to factors such as research and development efforts or job creation. Minimum domestic equity requirements, except for designated industries, are prohibited in the future.

The FTA will not affect the right of the Canadian government, under the *Investment Canada Act*, to review investments by U.S. investors in designated culturally-sensitive Canadian businesses, whether through the establishment of a new business or the acquisition of an existing Canadian business of whatever size. Canadian "cultural industries" are defined as those involved in the production, distribution or sale of books, newspapers, periodicals or music; the production, distribution, sale or exhibition of films, video recordings, audio recordings, or records; and radio and television broadcasting (including cable TV, satellite programming and broadcast networks). As a matter of policy, the Canadian government currently requires new foreign investment in Canadian book publishing and distribution enterprises to be in the form of joint ventures with Canadian control, or in the case of an acquisition of control, to be accompanied by an undertaking to divest control to Canadians within two years at fair market value. Under the terms of the FTA, where the Canadian government requires the forced divestiture of a cultural business, acquired indirectly by a U.S. investor, the government will be obliged to make an offer to purchase the business at fair market value in the absence of Canadian purchasers ready and willing to acquire the business at a reasonable price.

The new thresholds for review of acquisitions by U.S. investors under the *Investment Canada Act* will not apply to investments in the uranium and oil and gas industries. Review of investments in those areas will remain subject to existing *Investment Canada Act* thresholds and established policies which are to be clarified by an exchange of letters between the two governments. The Canadian policy with respect to the

uranium industry has been to limit foreign ownership to 33 1/3%, but that level was increased effective December, 1987 to 49%. The policy in the oil and gas industry is to require undertakings on the part of a foreign firm acquiring a Canadian firm to secure significant Canadian equity participation in the Canadian firm or in selected Canadian resource properties and to spend substantial sums on exploration and development in Canada. Recently, the Canadian government has indicated that it would not approve the sale of control of an oil and gas company that was in a healthy financial state to non-Canadian investors.

As well as providing a right of establishment in future to U.S. investors, the FTA also provides U.S. investors with a "right to exit." Under the FTA, a U.S. investor who owns a Canadian business and wishes to dispose of that business, will be able to sell to a foreign investor outside of the U.S. or Canada more readily than could a Canadian owner. Where a U.S. investor sells a Canadian business to an investor from a third country, the new *Investment Canada Act* thresholds that apply to U.S. investors will apply to that third country investor. The peculiarity of this provision is that a U.S. investor attempting to dispose of a Canadian business may be treated more favourably than a Canadian investor in the same position. A U.S. investor may be able to sell a Canadian business without a requirement of *Investment Canada Act* review to a foreigner from a third country while a Canadian selling a business of comparable size may not. There may be strong pressure to reduce review requirements for sales of businesses by Canadians to investors from third countries as a result of the U.S. "right to exit" provided for in the FTA.

The FTA also provides for procedures governing expropriation, ensuring due process and fair compensation, as well as ensuring repatriation of earnings subject to laws of general application, such as those relating to insolvency or the imposition of withholding taxes. Where either Canada or the United States decides to expropriate a business owned by an investor of the other country, such expropriation must be for a public purpose, be made on a non-discriminatory basis, be made in accordance with due process of law and be accompanied by prompt payment of adequate and effective compensation at fair market value.

It should be noted that the FTA provides certain exclusions from, or qualifications of, the national treatment obligation with respect to foreign investment. Government procurement practices are explicitly excluded from the investment chapter. As noted above, financial services (with the exception of insurance), transportation services and the cultural industries are also excluded from the investment chapter. Government taxation measures and subsidy programs are also not subject to the national treatment or other investment provisions provided that they do not constitute a means of arbitrary or unjustifiable discrimination against investors from the other country or a disguised restriction on trade.

Where a government decides to privatize a government-owned enterprise in future, it will be permitted to impose national ownership restrictions in determining who may purchase that entity. This applies to enterprises owned, directly or indirectly, by the federal government, a provincial government or a Crown corporation. It also applies to the subsequent privatization of any business enterprise acquired or established by a government in future.

(b) Monopolies

The FTA contains special provisions concerning the maintenance or designation by a federal government of monopolies. It provides that either country may maintain existing, or designate new, monopolies in any relevant market. Prior to designating a new monopoly that might affect the interests of firms in the other country, a government must notify the other country and consult, if requested. Also, where there may be an adverse impact on firms in the other country, the government establishing the monopoly is required to endeavour to regulate the monopoly's operations in such a manner as to minimize the possible adverse impact.

Where either country designates a monopoly, it will be obliged to ensure in its regulation or supervision of the monopoly that it does not discriminate in sales against persons or goods of the other country in its monopoly market or use its monopoly position, in another market, to

engage in anticompetitive practices that adversely affect a firm of the other country through the discriminatory provision of a good or covered service, cross-subsidization, or predatory behaviour.

The monopolies provisions of the FTA parallel Article XVII of the GATT which deals with state trading enterprises. The GATT and FTA provisions are designed to prevent the use of state-mandated monopolies to circumvent the trade-enhancing measures of those agreements through discriminatory sourcing, pricing and/or distribution practices.

4. INSTITUTIONAL PROVISIONS AND DISPUTE SETTLEMENT

The FTA establishes institutional mechanisms designed to promote the avoidance or settlement of trade-related disputes between Canada and the United States. Currently, the two countries do not have a formal bilateral process for notification, consultation, or resolution of disputes affecting trade. Apart from the GATT, there are no formal mechanisms for resolving such disputes. Although the GATT procedures are being improved, there is considerable opinion in the world trading community that the GATT dispute resolution mechanisms are not working because of lengthy delays, hesitation on the part of governments to use them, imbalances of power between disputing countries and the GATT record of lack of adequate resolution in many cases.

The FTA requires Canada and the United States to notify and consult with each other with respect to any existing or proposed new government measure or action that might materially affect the operation of the FTA. Under the FTA, a Canada-United States Trade Commission will be established to supervise the proper implementation of the FTA, to resolve any disputes that may arise over its interpretation or application, to oversee its further elaboration, and to consider any other matter that may affect its operation. The Commission will be composed of representatives of both member countries and will be headed by Cabinet ministers responsible for international trade or their designees. It will have the authority to create subsidiary ad hoc committees or working groups to investigate and resolve disputes or to negotiate and develop new rules as provided for in the FTA.

The institutional mechanisms will not be available to resolve countervailing or antidumping disputes. Those will be dealt with by the new binational panel procedures for antidumping and countervailing duty cases. Nor will the Canada-U.S. Trade Commission deal with disputes involving financial services, except for insurance. They will be dealt with by consultations between officials of the U.S. Treasury Department and the Canadian Department of Finance.

Essential to the proper functioning of the FTA are its provisions for notification and consultation. Each country is required to provide written notice to the other country of any existing or proposed legislation, regulations, governmental procedures or practices that might materially affect the operation of the FTA. It is important to recognize that any governmental measure or action that may affect the object and purpose of the FTA would be required to be notified. At the request of the country affected, the country proposing the measure is required to provide information in response to any questions asked.

In addition, each country may request formal government-to-government consultations with respect to any existing or proposed measure, whether or not it has been notified, that it considers would affect the operation of the FTA. The establishment in the FTA of formal channels for government-to-government communications concerning any government measures that may affect trade is an important new development in Canada-U.S. trade relations.

Where a problem arises, Canada and the United States are directed to make every attempt to arrive at a mutually satisfactory resolution of the dispute by government-to-government consultations. If they fail to resolve the matter, either country may apply in writing to the Commission. The Commission is required to convene within 10 days to endeavour to resolve the dispute. The Commission may use a range of different mechanisms to reach a mutually satisfactory resolution of the dispute. It may appoint a special committee or a working group or call on technical advisors or on the assistance of a mediator to achieve a consensus solution. Where a dispute

has been referred to the Commission and there has been no resolution within 30 days, the Commission is required upon the request of either country to establish a panel of experts to consider the matter. All disputes involving "emergency actions" taken under that chapter of the FTA must, and any other dispute the Commission selects may, be referred to a binding arbitration panel.

There are explicit time limits at every stage of the dispute resolution process. In any case involving an "emergency action", or any other case where the Commission has referred the matter to binding arbitration, the decision of the panel will be final. In other cases, the Commission will make a final decision, which in the normal case will be based on the panel's report. The Commission must reach its decision by consensus. If the Commission does not reach its decision expeditiously, and the complainant country feels that it is being injured by the continuing action of the other, it may retaliate with measures of equivalent effect until the matter is resolved.

Dispute resolution under the GATT mechanisms has not proven to be an entirely satisfactory way to resolve international trade disputes. GATT procedures are often lengthy and GATT panel decisions are not binding in their own right. The dispute resolution mechanisms of the FTA are an improvement over the GATT procedures because they provide a faster process for dispute avoidance and resolution. Under the FTA, panel rulings in antidumping, countervailing duty, emergency action and certain other cases so designated by the Commission will be binding on the two countries and their agencies.

The establishment of an independent, binational Commission to supervise the operation of the FTA, assist in its further elaboration and resolve disputes is an important achievement in Canada-U.S. trade relations. New formalized channels for communication between the two governments, prior to taking any new measures or actions which may affect trade, will be established where there were none before. Also, the express, short time limits set out for every stage of consultation,

conciliation, arbitration and dispute adjudication should help to ensure that matters are dealt with in an expeditious and efficient manner, at least cost in terms of time and money to private firms.

III. THE EXPERIENCE OF THE EUROPEAN ECONOMIC COMMUNITY

1. TREATY OF ROME PROVISIONS

Title III of Part Two the European Economic Community ("EEC") Treaty outlines the principles and procedures for implementation of the free movement of persons, services and capital between EEC Member States. Subject to certain exemptions for reasons of public security, public health and public policy as well as public service in each national government, the EEC Treaty directs the removal of barriers to the free movement of services, workers and capital by the end of the transitional period. [1]

In the case of services, the goal was to progressively abolish all restrictions on the provision of services between nationals of Member States. (The provisions of the Services Chapter may, on the unanimous approval of the EEC Council, be extended to nationals of a third country who provide services and are "established within the Community.") The general principles were that no new restrictions on the freedom of movement of services were to be introduced as of the date of the coming into effect of the EEC Treaty and that existing restrictions would be abolished according to a program established by the Economic and Social Committee of the European Assembly. In particular, priority was to be given to services which directly affected production of goods or service sectors which assisted in the promotion of trade in goods. As long as restrictions on freedom to provide services remained, each Member State was obliged to apply national treatment to nationals of other Member States providing services within its territory. That is, any restrictions were to be applied equally without distinction as to nationality.

Services are characterized as follows in the EEC Treaty:

1. Services normally provided for remuneration, to the extent that they are not governed by the provisions of the EEC Treaty relating to the free movement of goods, persons or capital. This includes commercial, industrial, handicraft and professional activities;[2]

2. Services performed by a self-employed person who is a national of a Member State, or by a company or firm incorporated in or organized under the laws of a Member State and having its registered office or principal place of business within the EEC;

3. There must be a "cross-frontier link" in the provision of services.[3] The provider of a service must be established in a Member State other than the Member State of the person for whom the service is intended. Specifically, transborder services may be provided in one of the following ways:

    - where the supplier of services moves to the country of the recipient; [4]

    - where the recipient moves to the country of the supplier of services; [5] or

    - where the service itself is transferred across borders, and the supplier and the recipient remain in their own countries.[6]

Freedom of establishment and freedom to provide services are distinct obligations under the EEC Treaty and are dealt with separately, in Chapters 2 and 3 of Part Two, Title III respectively. The right of establishment is the right to establish oneself, either as an individual or as

a corporate entity in a Member State other than one's state of nationality while enjoying the same treatment as nationals of that State. The Treaty provides that freedom of establishment includes the right to "pursue activities as self-employed persons and to set up and manage undertakings" of companies and firms. The Services Chapter, on the other hand, encompasses the movement of a service, usually temporarily, across a boundary. That Chapter permits a national of another Member State to temporarily pursue his or her activity within the Member State where the service is provided, without invoking the right of establishment provisions. In these circumstances, the foreign provider of the service is to receive the same treatment as a domestic service provider. However, as many of the same economic activities, persons and companies are covered by both the establishment and services obligations, several common provisions apply to both principles.[7]

Articles 55 and 56 of the Treaty, which apply equally to the freedom to provide services and the right of establishment, set out general exceptions to these principles. Under Article 55, the provisions of the Treaty relating to the right of establishment or the freedom to provide services do not apply to activities which are connected, even incidentally, with the exercise of official authority by any Member State. Article 56 permits a Member State to discriminate against foreign nationals on the grounds of public policy, public security or public health.

2. IMPLEMENTATION

Treaty Articles 59-66 inclusive provide principles, and procedures for their implementation, to allow free movement of trade in services. First, there is a standstill obligation imposed by Article 62. Effective January 1, 1958, the date the Treaty came into force, Member States were obliged to not introduce any new restrictions or to increase existing restrictions.

Second, the Treaty established a twelve-year transitional period, from January 1, 1958 to January 1, 1970, during which all restrictions on the freedom to provide services were to be phased out. By December 31, 1961, the EEC Council was supposed to draw up a general program for the

abolition of existing restrictions by Member States. The general program was to set out, for each services sector, specific directions and a timetable for the liberalization of trade. The general program was to be implemented by the promulgation of directives by the EEC Council, on the proposal of the EEC Commission and after consultation with the Economic and Social Committee and the European Parliament. These directives were to be adopted unanimously by the EEC Council until December 31, 1961, but after that date, a qualified majority of the EEC Council would suffice.

Third, transportation services were not included in the services chapter. Transportation is dealt with separately in Title IV of Part Two of the Treaty. The liberalization of banking and insurance services related to the movement of capital was to be effected along with the progressive liberalization of movement of capital under Chapter 4 of Title III, Part Two.

According to the Treaty, the coordination of laws in the services area was to be effected by directives issued by the EEC Council on the proposal of the EEC Commission. Coordination of laws was necessary because different rules existed in the Member States concerning the pursuit of economic activities by self-employed persons. These different rules had to be coordinated or harmonized so that common standards would apply throughout the EEC. The mutual recognition of diplomas, certificates and other evidence of formal qualifications is critical to the implementation of the freedom to provide services and the right of establishment, especially for the professions. The Council was therefore required to issue directives to give effect to the mutual recognition of formal qualifications by all Member States within the EEC.

It was originally intended that the legislative work necessary to achieve freedom to provide services in three aspects: abolition of restrictions, coordination of laws and mutual recognition of qualifications, would proceed simultaneously. In the case of the medical and pharmaceutical professions, however, the Treaty specifically required that the coordination of laws relating to the exercise of these professions proceed before the progressive abolition of restrictions by the Member States.[9]

3. THE LEGISLATIVE HISTORY

By the end of the first stage of the transitional period, the EEC Commission had proposed, and the EEC Council had adopted, general programs setting out the conditions and timetables for the abolition of restrictions on the freedom to provide services and the right of establishment within the Community.[10] The general program on services defined existing restrictions and provided a timetable for their progressive abolition.

The general program on services divided restrictions on the freedom to provide services into two main groups: those which affect the person or company providing service (directly or indirectly) by regulating the provider of the service, and those which affect the services provider by regulating the service itself.

The first group of restrictions are those resulting from legal and administrative rules or administrative practices in a Member State which prohibit or hinder a person in his or her pursuit of an activity as a self-employed person by treating him or her differently from nationals of the Member State. Examples given in the general program include government measures which prohibit the provision of services by foreign nationals or require foreign nationals to have special authorization or qualifications, including prior residence or training in the Member State. Other examples include differential taxation of national and foreign services providers, requiring deposits or security from foreign nationals, limiting or hindering access by foreign nationals to sources of supply or outlets of distribution, denying or restricting the right of foreign nationals to participate in certain social security and welfare programs, and granting less favourable treatment to foreign nationals in the event of nationalization, expropriation or requisitioning of assets. Indirect restrictions on the competence of foreign nationals to exercise rights, normally attaching to domestic providers of services, can also be significantly discriminatory measures. These types of measures include the exclusion or limitation of foreign nationals concerning any of the following: entering into contracts for work, hire or employment and full

enjoyment of all rights under such contracts; tendering for public works contracts; obtaining licences and authorizations; acquiring, using or disposing of all types of property, including intellectual property; borrowing or having access to credit; receiving governmental assistance; and acting as parties to legal or administrative proceedings.

The second group of restrictions are on the service itself and apply irrespective of nationality but have the effect of hindering or impeding the provision of services by foreign nationals. Examples may include restrictions on the transfer of funds needed to perform services or as payment for services.

By January 1, 1970, the EEC was far short of achieving its goal of abolishing all restrictions on the freedom to provide services. The EEC Commission had proposed 101 directives to the Council for the abolition of restrictions, coordination of laws and mutual recognition of professional qualifications to give effect to the right of establishment and the freedom to provide services. Only 40 directives were adopted by the Council. Thirty of these directives dealt with the abolition of restrictions in the following sectors: payment for services; cinematography; wholesale and retail trade; intermediaries in commerce, industry and crafts; reinsurance and retrogression; agriculture; forestry; horticulture; mining and quarrying; processing; electricity, gas, water and sanitation; real estate; food manufacturing and hotels and restaurants. Seven directives dealt with transitional measures for some of the above sectors. Only three directives dealt with the coordination of laws, and no directives were adopted concerning the mutual recognition of professional qualifications prior to 1970.

Between 1970 and 1985, another 33 directives were adopted by the EEC Council for the abolition of national restrictions, coordination of laws and mutual recognition of professional qualifications in the following sectors: public works and supply contracts; itinerant activities; motor vehicle insurance; non-life direct insurance, co-insurance, and direct life insurance; securities, banking and other financial services; trade in toxic products; movement and residence of services suppliers; and various

professional services including insurance agents and brokers, dentists, doctors, veterinary surgeons, lawyers, general care nurses, midwives and hairdressers. Nearly half of these directives dealt with the coordination of laws and mutual recognition of professional qualifications.[11]

In 1985, the EEC Commission published a White Paper entitled, "Completing the Internal Market."[12] The status of the freedom to provide services within the EEC at that time was summarized as follows:

> The provision in the EEC Treaty that restrictions on the freedom to provide services should be progressively abolished during the transitional period not only failed to be implemented during the transitional period, but several important areas failed to be implemented at all. Disgracefully, that remains the case.[13]

The White Paper set out a new timetable for the completion of the single, integrated, internal market in goods, services and capital by 1992. As far as the internal market in services is concerned, a great deal of work remains to be done concerning the abolition of restrictions and coordination of laws, primarily in the sectors of banking, insurance, transportation, securities, broadcasting and television.[14]

4. A SECTORAL EXAMPLE: INSURANCE SERVICES

In the following pages, we will examine the EEC's efforts to liberalize trade in services within the Community.[15] The insurance sector is highly regulated in all Member States. National control and supervision of this sector in most countries is based largely on the grounds of protecting the public interest. However, because the form of national regulatory control varies from one Member State to another, there has been fragmentation in what should be a common market in insurance.[16] The problems encountered by the EEC authorities are very complex. The solutions which

have been found or suggested for some of these problems may also be useful as precedents for other financial services sectors, such as banking,[17] and also for the Canada-U.S. Free Trade Agreement.

The general programs on the right of establishment and the freedom to provide services provide for the progressive abolition of restrictions on insurance services in the following aspects: reinsurance and retrocession, direct insurance other than life insurance, direct life insurance, and insurance agents and brokers. During the transitional period, the only concrete endeavour was with respect to reinsurance and retrocession. On February 25, 1964, the EEC Council adopted a directive abolishing restrictions on the right of establishment and the freedom to provide reinsurance and retrocession services.[18] Reinsurance operations had already become internationalized by that time, however, and there were few remaining restrictions imposed by the Member States. This directive did little more than confirm the *status quo*.[19]

When the EEC authorities broached the subject of direct insurance, they immediately faced intractable problems. The difficulties encountered are reflected in the meager results of the EEC's legislative work in this field. So far only four directives have been adopted by the EEC Council. They are the First Coordinating Directive on Non-Life Direct Insurance (the "First Coordinating Directive"),[20] the Directive on the Freedom of Establishment in Direct Non-Life Insurance,[21] the First Coordinating Directive on Direct Life Insurance (the "Life Insurance Directive"),[22] and the Coordinating Directive on Community Co-Insurance (the "Co-Insurance Directive").[23] The EEC Commission has submitted a number of draft directives to the EEC Council.[24] The most important one is the Proposal for the Second Coordinating Directive on Direct Non-Life Insurance (the "Draft Second Coordinating Directive").[25]

The problems encountered by the EEC authorities in liberalizing trade in insurance services stem from national regulatory control and supervision by the Member States. We will first analyze the main forms of national regulation and then examine the means adopted or suggested by the EEC authorities to liberalize trade.

(a) Authorization

Many Member States require a foreign insurer to obtain prior authorization before carrying on business in their territory. The specific requirements vary among Member States. Some Member States make the granting of authorization conditional upon establishment of the insurer in their territories. In other Member States, authorization will not be granted unless there is a need for an extra establishment in the local insurance market or a security deposit is made. Nationals of these Member States are also subject to the same requirements when they want to establish an insurance business in the domestic market. Although a blanket requirement of prior authorization does not seem to constitute a covert form of discrimination against foreign insurers, it clearly does form an obstacle to the freedom to provide services as well as the freedom of establishment. Member States that maintain the authorization requirement argue that it is an effective means of supervising insurance operations in their territories, and is justifiable on the grounds of protecting the public interest.

The First Coordinating Directive confirms the authorization requirement and also obliges all Member States to require prior authorization of insurance providers.[26] The Directive fails to specify or harmonize the criteria for granting prior authorization. It provides, however, that a Member State may not use the "economic requirements of the market" and prohibits the requirement of a security deposit. Discretion whether to grant authorization to foreign insurers is left largely to the governments of the Member States.

The Life Insurance Directive contains the same provisions as the First Coordinating Directive concerning authorization requirements.[27] The Co-Insurance Directive also subjects the leading insurer to the authorization requirement provided for in the First Coordinating Directive. However, it is not clear in the Co-Insurance Directive whether the leading insurer must obtain authorization from the Member State where it is established or the Member State where the service is provided.[28] Although

the authorization requirement clearly forms a restriction on the freedom to provide services, its compatibility with the EEC Treaty depends upon whether it is justifiable on the grounds provided by Article 56. The question must be considered together with the problems created by the divergent national regulation of financial guarantees of insurance enterprises. We will first examine that form of national regulation and then address the issue of the compatibility of the authorization requirement with the EEC Treaty.

(b) Financial Guarantees

All Member States require insurance undertakings operating in their territories to maintain certain solvency margins and guarantee funds, and to possess certain amounts of technical reserves consisting of equivalent and matching assets located in their territories. The criteria for determining solvency margins and calculating technical reserves vary among Member States. The requirement of localization of equivalent and matching assets to make up the technical reserves increases the costs incurred by an insurance enterprise in operating multinationally and places a multinational operation at a competitive disadvantage as compared with a purely domestic enterprise.

However, these requirements are justified on the grounds of protecting the public interest to ensure that insurance enterprises operate within their means and are able to meet their liabilities. Since these requirements apply to all insurance enterprises within a Member State irrespective of nationality, they do not violate the national treatment principle. Nevertheless, these divergent requirements often form serious obstacles to the right of establishment in the insurance services sector. To facilitate the exercise of the right of establishment by Community insurance enterprises, the EEC has, in some cases, instituted a "home control" system and directed the harmonization of criteria for determining solvency margins and technical reserves.

In the First Coordinating Directive, the supervisory authority of the Member State in whose territory an insurance enterprise has its head office is given the primary responsibility for ensuring that such enterprise maintains an adequate solvency margin in respect of its entire business operations. The supervisory authority is responsible, as well, for verifying the state of solvency of the insurer and ensuring that the company's assets are equivalent to its underwriting liabilities in all the Member States where it carries on business. The supervisory authority of the Member State where the insurer has a branch or an agency is given supplementary responsibilities of supervision, including periodic checks on the local operations of the insurer and furnishing information concerning the insurer's business operations to the Member State where the insurer's head office is located.

The First Coordinating Directive provides uniform criteria for determining solvency margins and guarantee funds. However, the Directive fails to harmonize the criteria for determining technical reserves and defining what constitutes equivalent and matching assets. Each Member State has the right to require an insurer carrying on business in its territory to establish what it deems as sufficient technical reserves calculated according to its own rules or practices and covered by equivalent and matching assets localized within its territory. The Draft Second Coordinating Directive proposes a set of uniform criteria for determining technical reserves as well as equivalent and matching assets, and also proposes the elimination of requirements for localization of equivalent and matching assets within the territory of a secondary host country.

If adopted by the EEC Council, the Draft Second Coordinating Directive, together with the First Coordinating Directive, will provide a basic "home control" system which may provide a feasible solution to the obstacles created by the divergent national regulation of insurance services within the EEC. Under these Directives, the authorities of a Member State where an insurance enterprise has its head office will assume the main responsibility for supervising its operation. The authorities of the host Member States in which an enterprise provides its services will have

supplementary responsibilities for supervising its business operations in their territories in close and constant cooperation with the authorities of the home state.

With the "home control" system in place, the argument of the Member States that the authorization requirement is a necessary means of supervision is no longer tenable. The authorization requirement is an unnecessary restriction on the freedom to provide services and the freedom of establishment because it is inconsistent with the system of "home control" which entrusts the primary responsibility for supervision to the home Member State. Thus, the First Coordinating Directive represents a first step towards the adoption of a "home control" system. Adoption of the Draft Second Coordinating Directive would complete that process. The Draft Second Coordinating Directive also proposes that an insurance enterprise which has its branch or agency in one Member State and intends to carry on business in another Member State is required to seek prior authorization from its home State. The home State would be required to grant the requisite authorization after consultation with the host State.

(c) Specialization

Some Member States require that non-life and life insurance services be provided by separate enterprises in their territory. Other Member States have no such requirement, or even encourage the same enterprises to engage in the provision of both life and non-life insurance services on the condition that they keep separate accounts for the two classes of insurance. German law imposes additional specialization requirements which apply irrespective of nationality. It prohibits the simultaneous undertaking in German territory of health insurance, credit and suretyship insurance, and legal expenses insurance.

With the divergent national systems, the question arises whether a diversified insurance company, established and authorized in one Member State to sell both life and non-life insurance, can establish a branch and provide both types of services in another Member State, such as Italy where simultaneous undertakings are prohibited. If not, is the Italian restriction

justified on the grounds of protecting the public interest? In the *Debauve* case, [29] the European Court held that the Belgian prohibition of commercial advertising on television was justifiable on the ground of protecting the public interest as long as the prohibition was applied equally to all advertisers regardless of nationality. The Italian prohibition also does not violate the national treatment principle. Presumably, it could be justified on public interest grounds because it is based on the fear that life insurance funds, representing the savings of the ordinary public, might be used to support the risks of the insurance companies.

The system of "home control" would most likely provide a solution to the problem. The home State of a diversified insurance enterprise would have to ensure that separate accounts are kept for each class of insurance and that funds from life insurance would not be misappropriated to support the risks arising under other insurance business. The host State, where the enterprise provides services or establishes a permanent presence, would be required to eliminate any prohibition of simultaneous undertaking of non-life and life insurance activities within its territory.

The same may not be said of the German specialization requirement. That restriction cannot be justified on grounds of protecting the public interest. The reason for the specialization in legal expenses insurance is historical; health insurance is closely connected with public compulsory insurance and credit insurance is usually backed by the government. The EEC Commission has proposed two directives to deal with problems of specialization of legal expenses and credit insurance.

(d) Material Control

Some Member States exercise control over the terms and conditions of insurance policies. They prescribe standard terms for insurance contracts, approve tariffs, and prohibit insurers from using "one-off" contracts beyond a certain period. Insurers are prohibited in some States from introducing new wording or new standard clauses without prior authorization. The reasons advanced for material control are to ensure uniform policy conditions and protect the general public against

unscrupulous insurers. Other Member States exercise less onerous control. Still others adopt a *laissez-faire* attitude. The problem of divergence of national policies concerning material control relates to the matter of competition policy and must, therefore, be considered in the light of EEC competition policy.

(e) Conclusions

At present, the authorization requirement is one of the most difficult problems faced by the EEC in liberalizing trade in insurance services. The complexity of the problem is reflected in several recent cases decided by the European Court of Justice.[30] In the early 1980's, Germany, France, Ireland and Denmark amended their domestic laws, purportedly to conform to the directives adopted by the EEC Council, especially the Co-Insurance Directive. However, the EEC Commission found that the amendments made by those four Member States were contrary to the EEC Treaty's provision relating to the freedom to provide services and the Co-Insurance Directive. After many unsuccessful attempts to encourage the four Member States to comply, the EEC Commission launched four separate actions in the European Court against Germany, France, Ireland and Denmark.[31] The Netherlands and the United Kingdom, where the insurance industry is traditionally strong and internationalized, intervened in these proceedings in support of the EEC Commission while the four defendant States, supported by Belgium and Italy, appeared on behalf of each other in their respective proceedings.

Among the contested laws of the defendant Member States the German legislation was the most restrictive. Therefore, it was representative of the problems posed in these proceedings. With respect to the direct insurance business, German law provided that where a company wished to provide services in Germany through salesmen, representatives, agents or other intermediaries, the latter must be established there. It also prohibited insurance brokers established in Germany from arranging insurance for German residents with insurers established in another Member State. With respect to co-insurance, German law required the

leading insurer to be established in Germany and to obtain authorization from the German government. It also set very high threshold values for risks, below which co-insurance was prohibited.

The EEC Commission sought from the European Court a declaration that the German laws were contrary to Articles 59 and 60 of the EEC Treaty and/or the Co-Insurance Directive. The European Court held, with respect to the direct insurance restrictions, that the German laws constituted an unjustifiable restriction, and were therefore contrary to Treaty Articles 59 and 60. However, the Court held that the restrictions were justified for "compulsory insurance or for insurance for which the insurer either maintains a permanent presence equivalent to an agency or branch or directs his business entirely or principally toward the territory of the Federal Republic of Germany."[32] With respect to co-insurance, the Court held that Germany also had failed to fulfill its obligations under Articles 59 and 60 and under the Co-Insurance Directive by requiring the leading insurer to be established and authorized in its territory in order to insure risks situated there.

As far as the direct insurance business is concerned, the effect of the European Court's judgment is difficult to assess. It will probably have little impact on German law as the judgment is self-contradictory. On the one hand, the Court held that the German requirement that salesmen, representatives, agents and other intermediaries of EEC insurers be established in Germany was contrary to Articles 59 and 60 of the EEC Treaty. On the other hand, the Court stated that the requirement was not contrary to Articles 59 and 60 where an insurer maintained a permanent local presence equivalent to an agency or branch.

This confusion stems from the Court's effort to maintain a distinction between the freedom of establishment and freedom to provide services in the EEC Treaty. In its judgment, the Court stated clearly that where an insurer established in one Member State intended to have a permanent presence in another Member State, the latter's authorization requirement, although constituting a restriction, was justifiable on the grounds of protecting the public interest. It reasoned further that the

insurer could not avail itself of Articles 59 and 60 or the provisions of the First Coordinating Directive and the Life Insurance Directive since the latter related solely to the freedom of establishment. In any case, the Court stated that "in the present state of Community law, it is for the State in which the service is provided to grant and withdraw that authorization."[33]

The current state of trade in insurance services within the Community may be summarized as follows. An insurer established in one Member State will enjoy freedom to provide certain insurance services in another Member State as defined by the First Coordinating Directive and the Co-Insurance Directive. However, this freedom is strictly confined within the meaning of provision of services as defined by Articles 59 and 60. If the insurer intends to establish a permanent presence in a Member State it will be at the mercy of the supervisory authorities of that State. This is so even though it wishes to establish there in order to have a closer relationship with clients or to provide services more efficiently. Even though an insurer may be granted authorization to take up and pursue insurance business in all nine Member States, it may be too costly to operate on a Community-wide basis since the insurer may be required to maintain assets in all nine Member States to match the technical reserves required by those States. Furthermore, if an insurer wishes to participate in co-insurance by providing services within the meaning of Articles 59 and 60, it will be restricted by the legislation of some Member States fixing high threshold values for risks below which co-insurance is prohibited. There is still far from a common market in insurance services within the EEC.

5. GENERAL ISSUES

There are a few critical issues which must be addressed in any analysis of the provisions of the EEC Treaty relating to services. They include the definition of services, the distinction between the freedom of establishment and the freedom to provide services, and the means used to implement these principles. We will examine these issues as they have arisen in cases decided by the European Court of Justice as well as national courts.[34]

(a) Supply of Goods or Services

Because of the complexity of the services industry, it is very difficult to find a precise and all-embracing definition of services. The definition of services used by the EEC Treaty is a residual one. Anything not covered by the provisions of the EEC Treaty relating to the free movement of goods, capital, persons or transportation is considered a service. No attempt is made to define a service according to the intrinsic nature of the activity. Considering the purposes of the EEC Treaty, this approach is understandable. The objective of the EEC Treaty is to create a common market in goods, persons, services and capital within the Community. Since a totally free market for all economic activities is envisaged, ideally it should not matter whether an activity is regarded as involving the supply of goods, services, persons or capital.

In the thirty year history of implementation of the EEC Treaty, the European Court has dealt with the goods-or-services question in a remarkably few cases. In the *Cinétheque* case, [35] the European Court held that the marketing of movie videos was not the supply of services but the movement of goods. This determination is surprising because there is quite a difference between blank video cassettes and movie videos. However, the issue in this case was whether the French legislation prohibiting the marketing of video cassettes of a movie until one year after the first public showing of the movie in cinemas was contrary to Article 59 of the EEC Treaty. The Court held that the French restriction was a justifiable one and did not infringe Article 30 of the EEC Treaty as it related to the movement of goods.

In the *French Newspapers* case, [36] the European Court held that the printing of newspapers was not the supply of services but the manufacture of goods. The issue here was whether the French tax credit granted to publishers who had their newspapers and periodicals printed in France was compatible with the EEC Treaty. The Court held that the French tax law infringed Article 30 of the Treaty, since it was discriminatory against

other EEC publishers. However, even if the printing of newspapers and periodicals was classified as the provision of services, the result of this case would have been the same.

The distinction between goods and services has not presented an impediment to the EEC's efforts to liberalize trade in services within the Community. The distinction is relatively unimportant where the same principles of national treatment and right of establishment apply equally to the provision of goods and services. However, where only a partial liberalization of services trade is envisaged, such as under the FTA, a clear and precise definition of which services are covered is crucial to the success of the agreement.

(b) Freedom of Establishment and Freedom to Provide Services

As noted above, the authors of the EEC Treaty created a distinction between the freedom of establishment and the freedom to provide services. However, the demarcation line between the two is difficult to draw as Article 60 permits a cross-frontier supplier of services to pursue its activity temporarily in a Member State where the service is provided. This provision fails to specify how much time is "temporary". A French regulation permits doctors established in other Member States to provide services in France only for two days without having to comply with the "single centre" rule. That is, no doctor or dentist established in France is permitted to have more than one practise centre.[37]

At present, a supplier of services established in one Member State enjoys a certain degree of freedom only within the meaning of the provision of services as defined in Articles 59 and 60.[38] If a supplier wishes to establish a permanent presence in another Member State to carry on its activities, it will still face many restrictions. Adherence to the principle of national treatment will not of itself lead to a common market in services. This fact raises a challenge to the arbitrary distinction between the freedom of establishment and the freedom to provide services. The usefulness of such a distinction is questionable.

The beneficiaries of the two freedoms under the EEC Treaty are similar categories of persons. As far as the provision of services is concerned, the provisions of the EEC Treaty relating to establishment cover the same economic activities performed in one Member State by nationals of another Member State. The difference is that these activities are carried out in the case of establishment, by persons or firms located in the Member State where the activities are performed, and in the case of provision of services, by nationals located in another Member State. Such a difference does not seem to justify separate legal treatment.

In the normal case, a national of one Member State will not want to establish in another Member State as an end in itself. Usually, the purpose will be to provide services more efficiently in the host State. Therefore, the freedom to provide services should imply a right of establishment for that purpose. Viewed in this light, the freedom of establishment is only a necessary corollary of the freedom to provide services and not the other way around. The right of establishment should not be equated as a general principle of the same significance as the freedom to provide services or the free movement of goods. A better approach would be to deal with the issue of establishment as foreign investment in goods or services.

(c) National Treatment

Adoption of the principle of national treatment requires the abolition of all discriminatory restrictions based on foreign nationality. National treatment is a fundamental principle of the GATT as it relates to the liberalization of trade in goods. With respect to trade in services, the question has arisen whether the application of the principle of national treatment will ensure free trade in services. In other words, are there other restrictions which are not discriminatory on the basis of nationality but which hinder the free flow of services trade? It may be useful here to take a closer look at the relevant provisions of the EEC Treaty.

Paragraph 1 of Article 59 provides as follows:

> Within the framework of the provisions set out below, restrictions on freedom to provide services within the Community shall be progressively abolished during the transitional period in respect of nationals of Member States who are established in a State of the Community other than that of the person for whom the services are intended.

Paragraph 3 of Article 60 provides as follows:

> Without prejudice to the provisions of the Chapter relating to the right of establishment, the person providing a service may, in order to do so, temporarily pursue his activity in the State where the service is provided, under the same conditions as are imposed by that State on its own nationals.

Article 65 provides as follows:

> As long as restrictions on freedom to provide services have not been abolished, each Member State shall apply such restrictions without distinction on grounds of nationality or residence to all persons providing services within the meaning of the first paragraph of Article 59.

It is clear that the authors of the EEC Treaty envisaged the abolition of two categories of restrictions on the freedom to provide services.[39] In the *Webb* case, [40] the European Court stated that "the abolition of the restrictions on the freedom to supply services within the Community entails more than the abolition of discrimination on the grounds of nationality or place of establishment and extends to the removal of all obstacles to the freedom to supply services across the Community's internal borders, save to the extent that they are preserved by Articles 55 to 66."[41] Article 65 directs that, from the date of the entry into force of the EEC Treaty, all Member States must abolish all discriminatory restrictions based on nationality or residence.[42] This Article has been declared to have direct effect in the domestic law of all Member States. The EEC Council was entrusted with the responsibility to enact directives for the abolition of other categories of restrictions.

There is no provision in the Establishment Chapter comparable to Article 65 of the Services Chapter, which obliges Member States to apply all restrictions, pending their abolition, without distinction on the basis of nationality or residence. In the Establishment Chapter, the meaning of "restrictions" is less clear. In the *Auer* case, [43] the European Court stated that "it may be seen from the provisions of Articles 54 and 57 of the Treaty that freedom of establishment is not completely ensured by the mere application of the rule of national treatment, as such application retains all obstacles other than those resulting from the non-possession of the nationality of the host State and, in particular, those resulting from the disparity of the conditions laid down by the different national laws for the acquisition of an appropriate professional qualification."[44]

The clarification of this point is of more than mere academic significance since it is often argued that a national measure does not constitute a restriction if it applies irrespective of nationality. For example, in the *Canninga* case, [45] a sub-contractor was charged with infringing the Dutch labour legislation which required all labour contractors to obtain a permit. The accused invoked his freedom to provide services under the EEC Treaty. A Dutch appellate court dismissed the appeal, however, holding that the relevant provisions of the EEC Treaty purported to prohibit only discrimination on the basis of nationality and the Dutch permit requirement applied equally to all labour contractors.

Article 65 of the EEC Treaty goes beyond the scope of the national treatment principle by prohibiting, in addition, any discrimination on the basis of residence. This is of practical importance since the laws of many Member States require nationals to reside in their territories in order to carry on certain economic activities there. In the *Van Binsbergen* case,[46] Mr. Van Binsbergen, a Dutch national, engaged another fellow national, Mr. Kortmann, to represent him in an unemployment insurance dispute before the Dutch social security court. Mr. Kortmann was not a lawyer but an independent legal advisor specializing in social security matters in the Netherlands. Such activities were not subject to any rules or regulations and did not depend upon the possession of any diploma or membership of

any professional body in the Netherlands. However, the procedural rules of the social security court provided that only a person established in the Netherlands could act as a legal representative in proceedings before it. In the course of representing his client, Mr. Kortmann left to reside in Belgium and was consequently barred from representing his client before the Dutch social security court. The European Court held that the Dutch rule was an unjustifiable restriction on the freedom to provide services.

An even more difficult problem concerning the national treatment principle is whether it applies to relations between a Member State and its own nationals. In other words, is a Member State entitled to treat its own nationals differently from the nationals of other Member States? In the *Knoors* case,[47] Mr. Knoors, a Dutch national, resided in Belgium and carried on the business of central heating and plumbing there for many years. When he applied to establish his business in the Netherlands, the Dutch authorities rejected his application on the grounds that he could not be considered to be a "beneficiary" as defined in the relevant Directive because the Directive was not intended to give rights to Dutch nationals vis-à-vis their own government. The European Court applied the principle of equal treatment of nationals of all Member States based on the concept of "Community citizen" and held that the government of the Netherlands was wrong in denying Mr. Koors' application.

In the *Broekmeulen* case,[48] Mr. Broekmeulen, also a Dutch national, was educated and licensed to practise general medicine in Belgium. When he applied to practise general medicine back home, the Dutch authorities rejected his application unless he satisfied the Dutch requirement of one-year of practical training. At that time, the Directive already adopted by the EEC Council on mutual recognition of doctors' diplomas listed the diploma of the University of Louvain as a recognized qualification for the practice of general medicine throughout the Community. The Dutch government argued that in view of the modern development of medicine, it was necessary to require some practical training of general practitioners after graduating from universities; that the Dutch rule applied to Dutch nationals only; and that many Belgian nationals were admitted as general medicine practitioners in the Netherlands without having to undergo the

required practical training. The European Court held that the refusal by the Dutch authorities to admit Mr. Broekmeulen was unlawful even if other Dutch nationals who qualified locally were required to undergo the supplementary training.

It is clear that the national treatment principle has only limited scope in the liberalization of trade in services. Discriminatory restrictions based on nationality or residence are easily identifiable and liable to attack, particularly after the European Court's rulings in the *Reyners* and *Van Binsbergen* cases that Articles 52, 59 and 60 are directly applicable and could be relied on by complainants in the national courts. It is far more complex to remove restrictions resulting from diverse national regulation of services sectors and disparate national requirements concerning professional qualifications.

By 1985, when the EEC Commission released its White Paper the objective of removing discriminatory restrictions based on nationality had largely been accomplished. Also, the European Court in several decisions had proclaimed the EEC Treaty principles of freedom to provide services and right of establishment to be directly applicable as domestic law in the Member States. However, many obstacles to the free flow of services trade within the EEC remain.

IV. CONCLUSION

One of the lessons to be drawn from the EEC's experience in attempting to create a common market in services is that the application of the principle of national treatment is not in itself sufficient to achieve complete trade liberalization. In a highly-regulated service sector such as insurance, or in a sector such as banking, divergences in national supervisory controls often constitute obstacles to free trade in services. The *de jure* application of the principle of national treatment is often not an effective solution in such circumstances and may even lead to more restrictive or unequal treatment of foreign services. In order to

accommodate the particular needs of banking, for example, it has been treated separately from other services in both the EEC Treaty and in the Canada-U.S. FTA.

The choice by the drafters of the EEC Treaty of the term "freedom to provide services" indicates that they recognized the limitations of national treatment. The word "freedom" has a broad connotation. It suggests that Member States must go beyond equality of treatment between nationals and non-nationals within their borders to achieve true liberalization of trade in services. The EEC Treaty provides for an attack on restrictions on free movement of services on three fronts: the removal of existing restrictions to services transactions, the coordination of laws and standards within the Community, and the mutual recognition of professional qualifications.

By January 1, 1970, many of the discriminatory restrictions based on nationality had been eliminated by Community law. Also, European Court decisions proclaiming the EEC Treaty principles of freedom to provide services and right of establishment to be directly applicable in the domestic law of Member States, helped to reduce restrictions based on nationality. However, many obstacles remain. The EEC Commission has grouped all of the remaining restrictions into three categories: physical barriers, technical barriers and fiscal barriers. The removal of these remaining barriers is a prerequisite to the completion of a common market in goods, services, persons and capital.

The term "technical barriers" describes certain non-discriminatory restrictions which, nevertheless, constitute burdens for cross-frontier suppliers. The *Seco* case provides an illustration of such restrictions. In that case, a cross-frontier supplier of services objected to paying certain social security contributions in the host Member State where he provided services because he was already paying similar contributions in the Member State where his enterprise was established. The European Court of Justice held that the national measure requiring payment of contributions, although apparently non-discriminatory, constituted a form of covert discrimination against the cross-frontier supplier because it increased his cost of supplying services in that Member State.

This decision on the part of the European Court is indicative of the extent to which the Community is prepared to go in removing even non-discriminatory practices which constitute restraints to the free movement of services among Member States. The principle of national treatment has, to a certain extent, become a secondary goal within the Community. The abolition of discriminatory practices and the introduction of policies and domestic laws encouraging equivalent competitive opportunities for all EEC services providers are of greater priority. As noted above, the European Court in the *Webb* case reiterated that the abolition of restrictions on the freedom to supply services entailed more than the abolition of discrimination on the grounds of nationality or place of establishment, and extended to the removal of all obstacles to the free movement of services across internal Community boundaries. Indeed, it is only in the case where restrictions remain that national treatment is required as a minimum standard. Article 65 of the EEC Treaty makes it clear that as long as restrictions have not been abolished, those restrictions are to be applied in accordance with the principle of national treatment.

Despite the exceptions for public policy, public security or public health, it is clear from the cases noted above that any restrictions justified for those reasons must be reasonable and that the European Court will enforce the removal of barriers to the full extent possible. The only other exception, that of restrictions on nationality for positions in government services, is not an unreasonable one.

The existence of supranational authorities to enforce the Treaty, and to ensure that its principles and objectives are achieved, helps to ensure that principles such as national treatment do not become limitations on the free movement of services. In circumstances where national treatment actually imposes a burden on the cross-border provider of services, the EEC Commission or the European Court can be called upon to ensure that the practice does not continue.

The EEC Treaty goes beyond the right to freely provide services across intra-Community boundaries, it also includes the right of establishment. That is, the provider of a service need not remain established only in his or her host country while providing services to a purchaser in another country. The services provider has the right to establish his or her services activity in the host country subject to certain exceptions. Under the Treaty, providers of services who choose to establish themselves in the host country must be governed by the same conditions which apply to nationals of that country. No new restrictions on the right of establishment may be introduced in any Member State, and the progressive abolition of restrictions on the freedom of establishment has begun within the Community. In addition, a services provider may temporarily pursue his or her activity in the host State.

Clearly, the EEC is moving toward unfettered trade in services. Many of the provisions of the EEC Treaty have the effect of domestic law in Member States. Also, its provisions go beyond the principle of national treatment to include the removal of discriminatory residence requirements and even certain non-discriminatory practices. The removal of restrictions which result from diverse national regulatory schemes for specific sectors and different national requirements for professional qualifications will take much longer. Given the progress made to date it can be said that the free movement of services in the European Community will be accomplished in the near future.

National treatment is, nevertheless, an important first principle since the most serious restrictions are often directed at foreign nationals in order to protect local service industries. The application of the national treatment principle is particularly important at the beginning of a trade liberalization process under an international agreement. It is also an important first principle where only a partial liberalization of trade in services is envisaged, or where greater liberalization is expected to evolve over time, such as in the Canada-U.S. FTA.

The FTA does not go nearly as far as the EEC Treaty. Only certain services are covered by the services chapter, some sectors require further negotiation, and others are covered in other chapters with specific limitations. The FTA represents a far more limited attempt at liberalization of trade in services than the EEC Treaty. The FTA's achievements also appear to be less ambitious than the proposals made by the United States for the Uruguay Round of multilateral trade negotiations. Only financial services, tourism, architecture and enhanced telecommunications services will require any changes to existing laws, regulations or policies. Nonetheless, within the context of the FTA, the principle of national treatment is an important first step. Providers of covered services from either country must be treated no less favourably than domestic providers of the same service in like circumstances. Similar to the EEC Treaty, there is an exception to this principle in that health, safety, prudential, fiduciary or consumer protection reasons may be used to justify legitimate restrictions so long as they are reasonable and the ultimate treatment of nationals of each country is equivalent in effect.

At the same time, the national treatment obligation of itself will not lead to the harmonization of regulation of services on both sides of the border. Indeed, the FTA goes beyond the basic obligation of national treatment in the general services chapter, imposing a requirement that neither country may introduce any measure that constitutes a means of arbitrary or unjustifiable discrimination against persons of the other country or a disguised restriction on bilateral trade in covered services. In the case of telecommunications, for example, it is recognized in an annex to the FTA that each country will have different regulatory systems with different procedures for such aspects as setting rates and licensing services providers. The main obligation of regulators on either side of the border will be to ensure that the providers of covered services operating in the same country are treated equivalently regardless of their country of nationality.

In the case of financial services, the separate chapter of the FTA which covers federally-regulated financial services uses a special concept of national treatment. The concept of equality of competitive opportunity is of

particular importance in the financial services sector where national treatment *per se* could actually create restrictions for a foreign provider of financial services. Equality of competitive opportunity is intended to permit the two parties to come to agreements on the specific rules which should apply to permit the providers of services from each country to compete on the same footing with the other's domestic financial institutions.

Transboundary investments in service sectors covered by the general chapter on services will be subject to the national treatment principle by virtue of Chapter 16, which raises the thresholds for reviewing foreign investment into Canada. The new review thresholds for investments will apply to all services covered by the general services chapter, but will not affect financial services, transportation services or cultural businesses. Given the limited number of covered services and the prospective application of the obligation to provide national treatment in the FTA, the EEC commitment to remove all remaining restrictions on the right of establishment and the free movement of services would appear to provide a better basis for comprehensive liberalization of services trade. Further, the fact that there are formal EEC institutions which can both enact and direct national governments to observe common regulations and policies reduces the significance of the principle of national treatment as a means of liberalizing trade. Where national treatment is not enough to remove barriers to entry, the European Court or EEC Commission can define, and enforce, whatever measures are required.

In the FTA, both Canada and the United States recognize that the rules on services trade, although a significant improvement, are not an end in themselves. They have agreed to develop new rules and to extend the obligations of the services chapter by negotiating further sectoral annexes. The financial services chapter requires also further negotiation and development. The results of this work may be the extension of the national treatment principle to include the abolition of existing restrictions along the lines of the EEC model, and eventually the elimination of non-discriminatory restrictions relating to the right of establishment. Further bilateral negotiations are required to push the FTA in the direction of the EEC Treaty provisions with respect to the free movement of services.

While the FTA represents only an initial step in the process of liberalization of trade in services, both the FTA and the EEC experience indicate the deficiencies which can be associated with the use of the national treatment principle alone. In order to achieve true liberalization of trade in services, without the attendant restrictions so desirable to national governments, national treatment must continue to be the initial goal. However, a comprehensive plan of action must also include progressive removal of all discriminatory restrictions and, ultimately, removal of non-discriminatory restrictions which affect free trade in services. Equally important for many service sectors is the corollary right of establishment, commercial presence, or the opportunity to invest in other member countries.

The EEC experience demonstrates that effective joint institutions are required to direct and enforce the abolition of restrictions as well as to develop common standards for the future. Unlike the EEC, the FTA will not establish permanent, joint institutions with the ability to enact and enforce common regulations and policies. Ultimately, the success of the FTA in liberalizing services trade will depend largely on the willingness and cooperation of the Canadian and U.S. governments to reduce restrictions and negotiate common rules. Any progress made in the Uruguay Round to develop a general framework agreement, establishing general principles such as national treatment and right of commercial presence or establishment, and in negotiating specific sectoral agreements, should encourage the continued bilateral reduction of restrictions in the FTA. As shown by the EEC experience, however, achieving substantive progress in liberalizing trade in services can be difficult and protracted. Whether the lessons of the EEC and the FTA will be applicable in the Uruguay Round, where there are major economic, political and social differences underlying the sensitive negotiations, remains to be seen.

FOOTNOTES

1. For general references, see Burrows, Free Movement in European Community Law (1987), pp. 209-242; EEC Commission, European Perspectives: Thirty Years of Community Law (1981), pp. 304-317; Sundberg-Weitman, Discrimination on Grounds of Nationality: Free Movement of Workers and Freedom of Establishment under the EEC Treaty (1977); Maestripieri, "Freedom of Establishment and Freedom to Supply Services" (1973), 10 Comm. Mkt. L. Rev. 150; Van Gerven, "The Right of Establishment and Free Supply of Services within the Common Market" (1965-66), 3 Comm. Mkt. L. Rev. 344; Watson, "Freedom of Establishment and Freedom to Provide Services: Some Recent Developments" (1983), 20 Comm. Mkt. L. Rev. 767; Greer, "The EEC and the Trend Toward Internationalization of Legal Services: Some Observations" (1987), 15 Int'l Bus. Law. 383; Lando, "The Liberal Profession in the European Communities" (1971), 8 Comm. Mkt. L. Rev. 343; Morse, "Provision of Services: the Professional Supervision Exception" (1979), 4 European L. Rev. 375; O'Caiomh, "The Implementation of the Directive on Lawyers' Freedom to Provide Services in Ireland" (1980), 5 European L. Rev. 235; Richardson, "International Trade Aspects of Telecommunications Services" (1986), 23 Comm. Mkt. L. Rev. 385; Scheider, "Towards A European Lawyer" (1971), 8 Comm. Mkt. L. Rev. 44; Walters, "Uncertain Steps Towards A European Legal Profession" (1978), 3 European L. Rev. 265; and Wilson, "EEC: Freedom to Provide Services for EEC Lawyers" (1978), 19 Harv. Int'l L. J. 379.

2. See Article 60, EEC Treaty, paras. 1 and 2..

3. See Article 59, EEC Treaty, para. 1.

4. This includes services supplied by the liberal professions in the wide sense of the word, including consultants, entertainers, industrial technicians involved in the assembly, repair or maintenance of machinery; and those in certain ancillary activities such as sales representatives, market researchers, maintenance personnel as well as certain craftsmen and agricultural workers. This type of personal service differs from that supplied by those in connection with the exercising of the right of establishment in that the supplier stays only temporarily in the country of the recipient. See, Article 60, EEC Treaty, para. 3.

5. Such services may be supplied on the arrival of the recipient in the country of the supplier for personal reasons such as tourism, family visits, or study; for business reasons; or for medical or para-medical care.

6. Such services may include processing, finishing, testing, banking, insurance, advertising and information flows.

7. Article 66, EEC Treaty provides that Articles 55 to 58, which apply to right of establishment, apply equally to the chapter on services.

8. See Article 61(1), EEC Treaty.

9. See Article 57(3), EEC Treaty.

10. The General Program for the Abolition of Restrictions on Freedom of Establishment, [1962] Official Journal of the European Communities, Special English Edition, Second Series, IX, at p.7; and the General Program for the Abolition of Restrictions on Freedom to Provide Services, [1962] Official Journal of the European Communities, Special English Edition, Second Series, IX, at p. 3.

11. See EEC Commission, Annual General Reports on the Activities of the European Economic Community, (1958-1967) and Annual General Reports on the Activities of the European Communities, (1967-1986).

12. EEC Commission, "White Paper on the Completing the Internal Market",(1985).

13. Ibid., at p. 5.

14. See EEC Commission, "White Paper on the Completing the Internal Market", (1985); EEC Commission, "First Report on the Implementation of the EEC Commission's White Paper on Completing the Internal Market" (1986), COM (86) 300 Final, and "Second Report on the Implementation of the EEC Commission 's White Paper on Completing the Internal Market" (1986), COM (87) 203 Final.

15. For general references, see Ellis, European Integration and Insurance (1980); Steindorff, "Insurance and Freedom to Provide Services" (1977), 14 Comm. Mkt. L. Rev. 133; and Chappatte, "Freedom to Provide Insurance Services in the European Community" (1984), 9 European L. Rev. 3.

16. Salomonson, "Problems and Experiences in the Application of the Treaty of Rome to the Insurance Industry" (1966-67), 4 Comm. Mkt. L. Rev. 289, at p. 290.

17. See Welch, "A Common Market for Mortgage Credit" (1986), 23 Comm. Mkt. L. Rev. 177; Clarotti, "Progress and Future Development of Establishment and Services in the EEC in Relation to Banking" (1984), 22 J. Comm. Mkt. Studies 199.

18. EEC Council, Directive on the Abolition of Restrictions on Freedom of Establishment and Freedom to Provide Services in Respect of Reinsurance and Retrocession (64/225/EEC), Official Journal of the European Communities (1964) 878/64/131. (hereinafter cited as O.J.)

19. Pool, "Moves Towards A Common Market in Insurance" (1984), 21 Comm. Mkt. L.Rev. 123, at p. 124.

20. EEC Council, First Directive on the Coordination of Laws, Regulations and Administrative Provisions Relating to the Taking Up and Pursuit of the Business of Direct Insurance Other Than Life Assurance (73/239/EEC), O.J. (1973) L228/3.

21. EEC Council, Directive on the Freedom of Establishment with Respect to Non-Life Direct Insurance (73/240/EEC), O.J. (1973) L228/20.

22. EEC Council, Directive on the Coordination of Laws, Regulations and Administrative Provisions Relating to the Taking Up and Pursuit of the Business of Direct Life Insurance (79/267/EEC0), O.J. (1979) L63/1.

23. EEC Council, Directive on the Coordination of Laws, Regulations and Administrative Provisions Relating to Community Co-Insurance (78/473/EEC), O.J. (1978) L151/25.

24. See, for example: EEC Commission, Proposal for A EEC Council Directive on the Coordination of Laws, Regulations and Administrative Provisions Relating to Legal Expenses Insurance O.J. 1979 C198/2, as amended O.J. (1982) C78/9; EEC Commission, Proposal for A EEC Council Directive on the Coordination of Laws, Regulations and

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25. EEC Commission, Proposal for the Second Directive on the Coordination of Laws, Regulations and Administrative Provisions Relating to the Taking Up and Pursuit of the Business of Direct Insurance Other Than Life Assurance and Laying Down Provisions to Facilitate the Effective Exercise of Freedom to Provide Services, O.J. (1976) C32/2.

26. Article 6 of the First Coordinating Directive provides that:

> "1) Each Member State shall make the taking up of the business of direct insurance in its territory subject to an official authorization.
> 2) Such authorization shall be sought from the competent authority of the Member State in question by:
> a. Any undertaking which establishes its head office in the territory of such State;
> b. Any undertaking whose head office is situated in another Member State and which opens a branch or agency in the territory of the Member State in question;
> c. Any undertaking which, having obtained in accordance with Article 7(1) an authorization for a part of the national territory, extends its business beyond such part ..."

27. See Article 6 of the Life Insurance Directive.

28. Article 2 of the Co-Insurance Directive provides that:

> "1) This Directive shall apply only to those Community co-insurance operations which satisfy the following conditions:
> (c) for the purpose of covering this risk, the leading insurer is authorized in accordance with the conditions laid down in the First Coordinating Directive, i.e. he is treated as if he were the insurer covering the whole risk."

29. Procureur du Roi v. Debauve, Case 52/79, [1981] 2 C.M.L.R. 362.

30. Edward, "Establishment and Services: An Analysis of the Insurance Cases" (1987), 12 European L. Rev. 231 and "Establishment and Services in the EEC: the Insurance Cases" (1987), 32 J. Law & Society of Scotland 187.

31. Re Insurance Services: E.E.C. Commission v. Germany, Case 205/84, [1987] 2 C.M.L.R. 69; Re Co-Insurance Services: E.E.C. Commission v. France, Case 220/83, [1987] 2 C.M.L.R. 113; Re Co-Insurance Services: E.E.C. Commission v. Ireland, Case 206/84, [1987] 2 C.M.L.R. 150; and Re Insurance Services: E.E.C. Commission v. Denmark, Case 252/83, [1987] 2 C.M.L.R. 169.

32. Re Insurance Services: E.E.C. Commission v. Germany, Case 205/84, [1987] 2 C.M.L.R. 69, at p. 112.

33. Ibid., at p. 106.

34. For case comments, see Lasok, "Leading Cases on the Movement of Goods, Persons, Services and Capital in the European Economic Community" (1980), 5 European L. Rev. 313; Leenen, "Recent Case Law of the Court of Justice of the European Communities on the Freedom of Establishment and the Freedom to Provide Services" (1980), 17 Comm. Mkt. L. Rev. 259; Devine, "Establishment and Services in the European Community in the Light of Recent Case Law" (1974), 9 The Irish Jurist 294; Bronkhorst, "Freedom of Establishment and Freedom to Provide Services Under the EEC Treaty: Three Judgments of the Court of Justice" (1975), 12 Comm. Mkt. L. Rev. 245.

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38. In practice, it is difficult to define the provision of services within the meaning of the EEC Treaty. The European Court states repeatedly in several judgments that the provision of services must be within the meaning of the EEC Treaty to be considered under the Services Chapter. Otherwise, the matter will be dealt with under the Establishment Chapter. However, in a number of cases where there was no cross-frontier link in the supply of services and no question of establishment arose, the Court still classified the activities in question as the provision of services. See e.g., Dona v. Mantero, Case 13/76, [1976] 2 C.M.L.R. 578 and Van Dijk's Boekhuis BV v. Staatssecretaris van Financien, Case 139/84, [1986] 2 C.M.L.R. 575.

39. The EEC Treaty itself does not define the other category of restrictions. However, the definition of restrictions given in both of the general programs seems to suggest that there is actually only one category of restrictions which is based entirely on nationality and which can be divided into two subgroups - one overtly discriminatory and the other covertly discriminatory.

40. Webb, Case 279/80, [1982] 1 C.M.L.R. 719. See also Ministère Public v. Van Wesemael and Poupaert and Ministère Public v. Follachio and Leduc, Case 110/78 and 111/78, [1979] 3 C.M.L.R. 87.

41. Webb, *ibid* at p. 728. In the same case, Advocate General Slynn states in his opinion that "an examination of Articles 59 to 66 of the EEC Treaty discloses that while discrimination on grounds of nationality or place of establishment constitutes, in the absence of justification on such grounds as public policy, conclusive evidence of 'restriction' such as is envisaged by Article 59, it is not an essential or exclusive element of such a restriction. This much is implied in Article 65, which provides that 'as long as restrictions on freedom to provide services have not been abolished, each Member State shall apply such restrictions without distinction on grounds of nationality or residence ..."

42. In Debauve, *Supra*, at p. 382. Advocate General Warner observed that "it is difficult to hold, *note 29*, that Article 59 is concerned only with discrimination, for there would then be little, if anything, left to be abolished under its provisions that was not specifically abolished by Article 65.", at p. 382.

43. Ministere Public v. Auer, Case 136/78, [1979] 2 C.M.L.R. 373.

44. Ibid., at 386. See also Reyners v. The Belgian State, Case 2/74, [1974] 2 C.M.L.R. 298.

45. Canninga v. Officier Van Justitie, [1977] 1 C.M.L.R. 262.

46. Van Binsbergen v. Trade Association of Engineering Industry of the Netherlands, Case 33/74, [1975] 1 C.M.L.R. 298.

47. Knoors v. Secretary of State for Economic Affairs, Case 115/78, [1979] 2 C.M.L.R. 357.

48. Broekmeulen v. General Medical Practitioners Registration Committee, Case 246/80, [1982] 1 C.M.L.R. 91.

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