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Regulatory Framework and Trade Liberalization in Bilateral Swiss-EC Transport Agreements

by

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The topic of this Expert Meeting is the regulatory and institutional dimension of trade in services. There is no doubt that from the perspective of market players the relevance of the regulatory framework is as high as that of trade measures. Trade measures are encapsulated in the notions of market access, non discrimination and the most-favored-nation treatment. The regulatory framework is about such measures as technical standards, authorizations and licensing requirements.

I was asked by UNCTAD to present concrete cases of interrelation between regulatory and trade measures in the context of the experience gained in the bilateral contractual relations between Switzerland and the European Community. As this session is devoted to infrastructure sectors and since UNCTAD has a reputation for its expertise in the field of transport, that sector will be the focus of this presentation.

The topic of the meeting is the regulation of services in the General Agreement on Trade in Services (GATS) and in regional trade agreements. To place the topic in its proper context, it shall be said first that Switzerland and the European Community do not have a comprehensive "trade agreement" on services. However, they are bound by an array of sectoral agreements, many of which covering parts of the services sector.[2] Among those sectoral agreements the ones that matter here are *the Agreement on Land Transport*[3] and *the Agreement on Air Transport*[4]. Both of them were negotiated between 1994 and 1999, signed on 21 June 1999, and entered into force on 1 June 2002.

THE BILATERAL AGREEMENT ON LAND TRANSPORT (ROAD)

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[2] See : Daniel Thürer, Rolf H. Weber, Wolfgang Portmann, Andreas Kellerhals (eds), *Bilaterale Verträge I & II, Schweiz – EU : Handbuch*, Europa Institut Zürich, Schulthess Juristische Medien AG, Zürich, 2007. See in particular Chapters III and IV.

[3] Agreement between the European Community and the Swiss Confederation on the Carriage of Goods and Passengers by Rail and Road, Official Journal of the European Communities L 114 Vol. 45, 30 April 2002, pp. 91-131, http://eur-lex.europa.eu/JOHtml.do?uri=OJ:L:2002:114:SOM:EN:HTML ; RS 0.740.72, http://www.admin.ch/ch/d/sr/0.7.html.

[4] Agreement between the European Community and the Swiss Confederation on Air Transport, Official Journal of the European Communities L 114 Vol. 45, 30 April 2002, pp. 73-90 ; RS 0.748.127.192.68, http://www.admin.ch/ch/d/sr/0.7.html.

Given the topic of this meeting, it is interesting to recall how Switzerland and the Community decided to negotiate the Agreement on Land Transport. It all started because of the request of the European Community that Switzerland should replace its weight limit for heavy vehicles of 28 tons with the EC weight limit of 40 tons.

The main element that motivated the negotiation was thus a typical regulatory norm. However, very quickly it turned out that other elements had to be taken on board and finally the agreement covers almost all aspects of road transport regulation and policy, namely:

- technical harmonization;
- trade liberalization (market access, national treatment, recognition);
- coordination of transport policy;
- the "taxation system" (tax on heavy traffic).

In this respect, Article 1 of the Agreement is telling. That Article describes the three general principles and objectives of the Agreement as follows :

> "1. This Agreement between the Community and Switzerland is aimed, on the one hand, at liberalising access by the Contracting Parties to each other's transport market for the carriage of passengers and goods by road and rail in such a way as to ensure the more efficient management of traffic using routes which, from a technical, geographical and economic viewpoint, are most suitable for all the modes of transport covered by the Agreement and, on the other, at laying the basis for a coordinated transport policy.
>
> 2. The provisions of the Agreement and their application are based on the principles of reciprocity and free choice of mode of transport.
>
> 3. The Contracting Parties undertake not to take discriminatory measures when applying this Agreement."

As said, one major provision of the Agreement is the harmonization of the weight limits provided for by paragraph 3 of Article 7. Under that provision, Switzerland accepted to "make its legislation on the maximum weights limits … equivalent to that in force in the Community on the date of signature of the Agreement". The fact was that in the context of North-South trans-European transport the Swiss weight limit caused some diversion of heavy traffic around Switzerland.[5]

That a technical services standard was the main motive for negotiating the Agreement needs to be underscored given the very topic of this meeting. The weight limit is typically akin to "domestic regulation" as defined under Article VI of the GATS. The domestic measure at hand had some trade impact to the extent that 40 ton vehicles had – in those days – to unload part of their cargo in order to enter the Swiss territory.

More generally, under the Agreement, all Swiss technical standards on road transport were harmonized with those of the Community. Paragraph 1 of Article 7 states that "Switzerland shall adopt … arrangements that are equivalent to Community legislation on the technical conditions governing road transport".

The GATS concept of "domestic regulation" under Article VI goes beyond technical standards though. One example of Swiss domestic regulation is the ban on night driving for road carriage. In

[5] According to the Swiss Federal Office of Transport (FOT), diverted traffic is defined as flows of traffic that do not take the shortest route but instead avoid a country for a certain reason (road taxes, weight restrictions, strict running schedule, etc.).

this respect the bilateral Agreement sets out a non-discrimination obligation, namely in its Article 15(3), which reads : “Exemptions from the ban on night driving shall be granted on a non-discriminatory manner”. The same provision establishes a one-stop-shop for granting the exemptions from the ban on night driving upon application by carriers. Furthermore, Article 15(1) sets the exact times of night driving ban as follows : “The ban on night driving on Swiss territory shall apply only between 22.00 and 05.00”.

The Agreement provides for the deregulation of some types of international transports. Firstly, in respect of goods transit, Article 10 provides that “[t]he international carriage of goods … in transit across the territory of the Contracting Parties shall be deregulated.”. Second, in respect of goods transport between Community Member States, transport by Swiss carriers is deregulated since 2005 under Article 12. This type of operation is referred to as “*grand cabotage*” in EC jargon. However, national cabotage inside individual EC Member States, as well as national cabotage inside Switzerland, remain “not authorised” for Swiss and EC carriers respectively, as stated in Article 14.

In terms of licensing and recognition the Agreement represents a milestone. Article 9 enshrines the use of the “Community authorisation for Community carriers” and of “a similar Swiss authorisation for Swiss carriers” in the carriage of goods between the Parties. In the same vein, transport of goods in transit is carried out under each Party’s license (Article 10), and transport of goods between EC Member States (“*grand cabotage*”) is “carried out under the Swiss licence” (Article 12). This amounts to a mutual recognition as defined in Article VII of the GATS. On top of that, Annex 4 to the Agreement sets out a few transport operations (*e.g.* mail transport as a public service) to be “exempt from any carriage authorisation and any system of licences”. The provisions of the Agreement on licensing requirements for goods transport are thus very liberal and trade supportive.

The mutual recognition of authorizations and licenses makes it possible for natural and juridical persons that have been admitted to exercise a transport activity in a Party to exercise that activity in the other Party, in the context of international transport operations. This is commonly referred to as “access to the profession”.

International transport of <u>passengers</u> (both regular and occasional) was liberalized too. Paragraph 1 of Article 17 provides that such transport shall be “permitted ... without discrimination as to nationality or place of establishment”, while paragraph 3 of that Article provides for the recognition of the Community license and the Swiss license by the respective Parties. Occasional as well as “special regular” transport services do not require authorization by virtue of Article 18(1) and (2). Cabotage is not authorized for transport of passengers, but Article 20(2) contains a grand-fathering clause in that regard.

In GATS terms, Mode 1 is thus to a large extent liberalized under the bilateral Agreement on Land Transport. (The four modes of delivery are defined in Article I:2 of the GATS).

An important part of the Agreement is its Title VI on “<u>coordinated transport policy</u>”, in particular its chapter C on “road transport charging systems”. Title IV is based on such principles as : “no discrimination, whether direct or indirect, on the ground of the nationality of the carrier, the place of registration of the vehicle, or the origin and/or destination of the transport operation”, “free choice of the mode of transport”, “no unilateral quantitative restrictions”, “proportionality”, “transparency” and “reciprocity” (see Article 32).

The main measure provided for under this Title is the introduction by Switzerland of new regulation for a “non-discriminatory tax on vehicles” in accordance with Article 40. The Agreement sets out in great details the parameters of the Swiss tax. That provision was, for Switzerland, the counterpart for eliminating its maximum weight limit. It was felt necessary to accompany the profound liberalization steps in respect of technical and trade norms by a rebalancing measure in the fiscal

area, in order to continue the effective implementation of its national transport policy objectives such as the shift of the largest possible share of freight traffic from road to rail. The Agreement provided for the gradual introduction of the new tax by incremental steps over a few years from entry into force.

The second pillar of policy coordination is the establishment of a rail and combined transport capability in accordance with Article 33. This too was seen by Switzerland as an indispensable measure to shift the transit carriage across its territory towards public transportation services, in particular in view of the sensitive case of transit through the Alps.

Of course, after almost seven years of implementation, you will be interested to know the effects of the above provisions. In short, the Agreement brought substantial benefits for both Parties.

The trade and economic impacts of the Agreement on Land Transport are significant.[6] Thanks to the combined effect to the aforementioned measures, the number of heavy vehicles could be reduced by 10 % between 2000 and 2007 while the transport volume increased by 60 %. Between 2000 and 2006 the number of kilometers driven diminished by 3 % while the tkm (tons-kilometers) increased by 20.5 %. This is due to the fact that the average load of trucks increased from 6.7 tons to 8.9 tons in the import/export sector as a result of the elimination of the 28 ton weight limit (productivity gains). The fact is that a 40 ton vehicle can contain twice as much freight as a 28 ton vehicle.

The main economic sectors that benefited from the increase of the weight limit are those relying on bulk transport, such as the chemical industry, the oil sector, the concrete industry or the production of foodstuff. Retail trade however could not take benefits from the higher weight limit while it was hurt by the newly introduced tax.

The combined effect of a higher weight limit and higher taxation led to a higher rate of load of trucks, including a lower number of "unladen" journeys.

Due to its comprehensive nature and far-reaching provisions, the Agreement between Switzerland and the Community considerably achieved both to facilitate trade in road transport services and to implement other policy objectives in a regional context. This example shows how domestic regulation goes hand in hand with trade liberalization. Surely, the benefits of the trade measures alone (market access) would not have fully developed their effects without an appropriate reshaping of domestic regulation – in particular the lifting of the weight limit as demanded by the EC – and without appropriate steps being taken for mutual recognition of authorizations and licences.

THE BILATERAL AGREEMENT ON LAND TRANSPORT (RAIL)

Though the provisions of the Agreement on Land Transport relating to rail transport are also very comprehensive in their kind, they do not contain as many rules as for road transport. The main provision regarding rail transport is straight as it provides for access rights and transit rights for rail operators of the Parties (Article 24). This so-called "free access" is granted between the Parties on the basis of relevant Community legislation (the "relevant" Community acts are listed in Section 4 of Annex 1 to the Agreement).

Article 25(4) provides for the mutual recognition of rail transport licenses, thus reinforcing the liberalization introduced under Article 24.

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[6] See : Rolf Zimmermann, "Effets économiques et sociaux de l'Accord sur les transports terrestres", in *La Vie économique* 11-2008, pp. 28-30.

Incidentally, the liberalization of trade under Article 24 made it necessary for the Parties to enhance regulation. Specific rules as well as an institutional setting had to be put in place to regulate the market of, and to allocate, so-called “train paths” by one company on the infrastructure of another company on a “fair and non-discriminatory basis” (Articles 27 to 29). Such rules are necessary given that rail capacity is a scarce infrastructure. Obviously, in the old world of state monopolies that sort of regulation had no *raison d’être*.

Concretely, Articles 27 to 29 contain provisions regarding : the designation of bodies for capacity allocation, their management, collection of user fees, procedures for application including deadlines, priorities in capacity allocation and special rights, transparency of allocation rules including publication, right of appeal. In the GATS, rights of appeal are covered by paragraph 2 of the Article on Domestic Regulation while procedures for application are dealt with in paragraph 3 of that Article.

The provisions on liberalization and organization of the free access to railway infrastructures has been implemented smoothly. In Switzerland the body in charge of the allocation of rail capacity initially rested with the incumbent rail operators and subsequently was turned into a separate and by-and-large independent independent body. All the institutions, rules and procedures for permitting a market-based trade in rail capacity are in place.

Another “reregulation” accompanying the liberalization undertaken under the Agreement pertains to the requirement to submit safety certificates – yet another type of domestic regulation – provided for under Article 26 of the Agreement. For obvious safety reasons companies of one Party using the infrastructure of the other Party are required to undergo such certification procedure under the applicable requirements of that other Party.

THE BILATERAL AGREEMENT ON AIR TRANSPORT

The two main pillars of the Swiss-EC Agreement on Air Transport are competition rules (Chapter 2 of the Agreement) and granting of traffic rights (Chapter 3). Competition rules pertain to issues such as abuse of dominant position, undertakings, state aid and anti-competitive practices. Such provisions are of the same nature as the competitive provisions contained in the “Reference paper” on telecommunication negotiated under the GATS. By virtue of Article 11 of the Agreement the competition provisions “shall be applied and concentrations shall be controlled by the Community institutions in accordance with Community legislation”. The relevant *acquis* is listed in the Annex to the Agreement. That major transfer of powers is the counterpart to the equally major opening of the Community air space established under Chapter 3.

Chapter 3 of the Agreement starts by providing that “any discrimination on ground of nationality shall be prohibited” in the context of civil aviation between the Parties (Article 3). This general obligation is complemented by Article 4, which provides that “there shall be no restrictions on the freedom of establishment” of nationals of the Parties, including the “setting up of agencies, branches and subsidiaries” by nationals of the Parties. In GATS terms, this amounts to a full liberalization of Mode 3 (commercial presence).

The granting of traffic rights is governed, in particular, by Article 15 of Chapter 3. Paragraph 1 of Article 15 provides for the granting of “traffic rights between any point in Switzerland and any point in the Community”, *i.e.* the third and fourth freedoms. The same provision grants to Switzerland “traffic rights between points in different EC Member States”, *i.e.* the so-called fifth, sixth and seventh freedoms (in EC jargon).

Paragraph 3 of Article 15 provides that Parties shall negotiate the liberalization of cabotage (eighth freedom). Such negotiation has started formally.

The Agreement provides that any previously concluded bilateral air transport agreement between Switzerland and an individual EC Member State is superseded. Grand-fathering is maintained though, provided that there is no discrimination and that competition is not distorted.

In addition to and separate from the issue of traffic rights, ground-handling is liberalized between the Parties on the same terms as provided for in the relevant EC legislation, which is taken over by Switzerland.

On the institutional side, after entry into force of the Agreement Switzerland was admitted to participate to the European Air Safety Agency (EASA) and to the Single European Space (SES). The participation to EASA is not only highly relevant for carriers but also in respect of the authorization on EC territory of aircraft maintenance companies or production companies.

In sum, the bilateral Agreement on Air Transport is very comprehensive in scope and is based on equal rights for Swiss and Community operators. It liberalizes most traffic rights and fully allows commercial presence for civil aviation (Mode 3). Furthermore, liberalization extends to auxiliary air transport services such as ground-handling services.

The trade and economic impacts of the Agreement on Air Transport were positive.[7] Not surprisingly the Agreement led to a more open and competitive air transport sector, to the establishment of more business by Community carriers in Switzerland, and to diminishing air transport fares. By liberalizing fully cross-border investments in the air transport sector the Agreement led to much easier and more efficient possibilities for refinancing. In the context of broader regional air transport networks, the transport routes available to Swiss travelers was improved, as well as the attractiveness of Swiss airports.

CONCLUSIONS

The agreements on land and air transport are exemplary in showing the relationship between trade liberalization and domestic regulation. Both agreements contain far-reaching market-access and non-discrimination provisions. At the same time, both contain a host of other provisions.

In terms of paragraph 4 of the Domestic Regulation Article of the GATS, the bilateral transport agreements address all measures covered by that paragraph, *i.e.* technical standards (e.g. the 28 ton weigh limit), licensing requirements (e.g. for road transport), and qualification requirements (e.g. licenses for natural persons for access to profession in international road transport). The universe of domestic regulation, respectively Article VI of the GATS, is of course broader than that, and such other domestic measures are dealt with in the agreements too (e.g. procedures and requirements related to the Swiss ban on night driving; procedures and requirements for the allocation of rail paths in relation to access to railway capacity).

Going beyond domestic regulation as understood in Article VI GATS, the agreements address such issues as recognition (corresponding to Article VII of the GATS) and transparency (covered by Article III of the GATS).

[7] See : Urs Haldimann, Manuel Keller, “L’impact de l’Accord bilatéral sur le transport aérien”, in *La Vie économique* 11-2008, pp. 31-34.

The bilateral transport agreements provide for the mutual recognition of an array of authorizations and licenses for natural and juridical persons (international goods transport; international passengers transport; rails licenses).

Institutional arrangements are another important component of the agreements, and in this respect the structures of the arrangements are varied.

In certain cases, liberalization was accompanied by the introduction of new regulation (*e.g.* the Swiss tax on heavy traffic; allocation rules for trade in rail paths; competition disciplines in air transport). In relation to the question of "sequencing", it is worth nothing that those new regulations were introduced in parallel to the liberalization process – and to some extent progressively – and not in anticipation of it.