



## Policy Statement

# The liberalization of trade in financial services

*Prepared by the Commission on Financial Services and Insurance*

### Liberalization of trade in financial services

This ICC policy statement was prepared by the ICC Commission on Financial Services and Insurance, a specialized ICC working body that examines major policy issues and builds consensus among users, providers and intermediaries of financial and insurance services. This statement complements the general policy recommendations submitted to the WTO by the ICC Commission on Trade and Investment Policy.

The importance ICC attaches to the services sector reflects the economic interests of its members in more than 130 developing and industrialized countries around the globe and the importance they attach to improving market access worldwide. Services are coming to dominate the economic activities of countries at virtually every stage of development, making services trade liberalization a necessity for the integration of the world economy.

ICC has continued its activist role since the Uruguay Round by providing business advice during the subsequent negotiations on basic telecommunications, financial services, and professional services, each of which advanced the cause of trade liberalization. ICC recognizes the achievements that have been made in liberalizing trade in financial services through the 1997 WTO agreement in the aftermath of the Uruguay Round and, since then, by individual country initiatives. However, ICC is concerned about most countries' reluctance so far to commit to further financial services liberalization in the current WTO/GATS negotiations. As a significant number of barriers remain and many unilateral liberalization measures are not included in countries' commitments under the 1997 WTO Financial Services Agreement, the ongoing WTO services negotiations should seek to incorporate substantive measure to liberalize trade in financial services into the results of the Doha Development Round. The legal binding of existing as well as ongoing unilateral liberalization measures in the WTO would greatly enhance legal certainty and predictability for trade in financial services.

ICC urges all WTO member countries to recognize that services trade liberalization, complemented by transparency, competition, and regulatory reform are critical to economic growth and stability. In terms of economic importance, services in general and financial services in particular are key sectors for growth and employment in both industrialized and developing countries.

Thus, further liberalization of trade in financial services (i.e., banking, insurance, securities and related services) could make a significant contribution to economic development worldwide. Moreover, providers, users, and consumers stand to benefit from greater competition, choice, and convenience.

The success of the current negotiations will depend on the active participation of all WTO member countries. Every country must recognize that the elimination of obstacles to trade in financial services will play a critical role in their financial services infrastructures and economies. ICC encourages industrialized countries to provide technical support to developing countries to help them further develop the legislative, regulatory and human resource requirements, which are key components of efficient markets.

### **Avoid discriminatory regulation**

ICC urges all WTO member countries to reject misuse of financial regulation, by embodying barriers to trade and investment in the financial service sector. ICC warns that discriminatory limitations on market access that would restrict foreign equity ownership, the number of foreign service providers, the type of legal entity required (for example branches or subsidiaries) and the scope of operations would jeopardize the development of financial markets by inhibiting the advantages brought by foreign competition such as strengthening market efficiency but also by undermining the strength of local service providers.

### **Movement of capital**

While significant liberalization of market access for international financial firms' local presence should, ideally, precede capital-account liberalization, ICC calls all WTO member countries to strive for capital account convertibility as soon as a reasonably sound and competitive financial sector is in place. Public authorities and the business community in less developed countries should work together with their counterparts in industrialized countries to achieve effective reform by creating a stable and appropriate national financial infrastructure that would allow the free movement of capital, crucial to national markets' development. Free movement of capital should be included in developing countries' policy objectives and also motivate them to commit in the Doha Round to corresponding liberalization in cross-border trade in financial services, envisaging transitional periods and prudential regulation where appropriate.

### **Emerging Safeguards Mechanisms (ESMs)**

WTO member countries are urged to avoid the inclusion of ESMs, and ICC stresses that no measures should be taken to inhibit the activities of companies in connection with local commercial presence. ICC is concerned that there are already many safeguard measures in WTO member countries. While these measures may still be in line with existing WTO provisions such as the balance-of-payment safeguard and the prudential carve-out for financial services in the GATS, world business believes that an increased number of safeguards would damage the legal certainty of liberalization commitments in the WTO, which is a prerequisite for market access by foreign financial firms. This, in turn, could seriously affect the efficiency of the financial sector in domestic economies both by raising the cost of capital and by reducing the flow of international

capital and hence limiting the potential benefits from international financial market integration. ICC is also concerned that discussions on ESMs would delay results of the negotiations on liberalization of financial services and thereby jeopardize the benefits of the Doha Round for national economies.

## **Implementation of the 1997 Financial Services Agreement and new WTO members' accession commitments**

In the context of the 1997 Financial Services Agreement (Fifth Protocol to the GATS – hereafter referred to as “the 1997 Agreement”), WTO member countries made binding commitments to provide non-discriminatory national treatment and market access in financial services, as specified in their country schedules, to financial services firms from any WTO member country. Through the WTO, there is now a strong body of trade rules as well as a formal process for enforcing rules and resolving trade disputes. ICC urges all WTO member countries that signed the 1997 Agreement to endorse and implement it in full. In addition, WTO accession candidates should commit to a degree of openness for their financial sector that would mirror the increased average level of liberalization in the world of today.

## **Specific recommendations for further liberalization of trade in financial services**

### **■ Right of establishment**

The 1997 Agreement produced some significant improvements in providing non-resident financial services providers – such as banks, securities firms, insurance companies and non-bank financial companies – with the opportunity to establish and expand their commercial presence in a number of foreign markets. Nevertheless, there is much to be done still to ensure that countries improve their commitments to open their markets on a non-discriminatory basis to foreign firms to enable them to operate in the legal form of their choice, as allowed by the host country for domestic firms, including wholly owned subsidiaries, joint ventures, branches and representative offices.

Improved commitments should include the removal of:

- restrictions on corporate form;
- obstacles to majority ownership;
- limits on majority ownership and control of joint ventures by foreign firms;
- obstacles to expansion;
- economic needs tests for investments;
- prohibitions and limitations on establishing and licensing of commercial presence;
- and allow the grandfathering of existing investments, activities and rights.

### **■ Market access and national treatment**

ICC recommends that foreign firms should have the same access to markets as domestic firms, and that anticompetitive regulation and discriminatory application of prudential measures such as capital or reporting requirements should be avoided. Where necessary, existing investments and activities should be safeguarded and those WTO members which have not made commitments to protect existing investments and activities should do so. Companies should be free to repatriate their earnings and to transfer or liquidate their business.

As regards regulation and supervision of legally dependent branches of foreign firms, as far as possible host country authorities should rely on the home country authorities' supervision, provided it meets internationally accepted standards, such as the Basel Capital Accord for Banks (Basel II). This should enable host regulators to allow regulatory and supervisory relief for the local branches of foreign firms without affecting their responsibilities to regulate the conduct of business in their local market.

National governments should ensure that market commitments access at a national level are not compromised by restrictions imposed at sub-national level.

#### ■ **Cross-border provision of services**

Countries have taken steps, although at an uneven pace, to reduce barriers to foreign financial services firms. As economies increasingly turn to global financial markets to meet a portion of their capital needs, foreign financial firms are helping to channel both foreign and domestic savings to these markets.

Non-resident financial services firms face many barriers, including:

- limitations on cross-border access, including the right to buy and sell financial products across borders and to participate in and structure transactions;
- lengthy and difficult approval for new products;
- restrictions on foreign exchange;
- limitations to trading in domestic stocks.

Considering the significant contribution of foreign financial services firms to development, nations should reduce and eventually eliminate these barriers by establishing clear and non-discriminatory approval procedures for the activities of non-resident firms.

#### ■ **Impartial and transparent regulation**

In order to encourage and support growth, markets for financial services must meet several goals, including:

- protecting investors;
- assuring disclosure of information by issuers;
- creating secondary markets with efficient pricing mechanisms.

However, companies often face hurdles in their foreign operations as a result of:

- legal systems which lack transparency and are subject to arbitrary actions and sudden changes;
- unclear and impractical licensing requirements and procedures.

Market access by itself does not necessarily guarantee liberalization. Discriminatory local regulatory requirements often prevent foreign financial services firms from competing on a level playing field with domestic firms. Transparency and impartial enforcement of regulations are conducive to equal competition amongst foreign and local firms. Implementation and harmonization of regulatory principles should help WTO members achieve an adequate and predictable regulatory environment for financial markets which is impartial, efficient and transparent.

To achieve such an environment globally, there is a need to improve transparency through GATS commitments, taking into account the following guiding principles:

- Rules, regulations and licensing requirements should be imposed, and regulatory actions should be taken, only for the purpose of achieving legitimate public policy objectives that are expressly identified.
- Regulations should be clear and understandable.
- Regulation should be enforced in a non-discriminatory manner, in particular excluding political, national or other extraneous considerations.
- The introduction of new products and services by firms should be governed by the standards set

- forth in relevant rules and regulations.
- All regulations, including requirements to obtain, renew or retain authorization to supply a service, should be publicly available at all times.
- To prevent unnecessary distortions to the market, regulators should issue and make available to the public final regulatory actions and the basis for those actions, to enhance public understanding thereof.

In addition, the process of rulemaking should allow advance public notice of rule changes and provide adequate opportunity for comment by market participants, whether domestic or foreign. A corporate and commercial legal system (including bankruptcy law) which establishes the rights of creditors and shareholders, and thus offers predictability and stability, should be given high priority. The enforcement of commercial contracts is also essential to the integrity of the financial services market.

#### ■ **Electronic commerce and financial services**

In considering GATS and e-commerce, the following areas are of most importance when addressing financial services:

- Services provided through e-commerce should be treated in the GATS on a technology-neutral basis. For example, commitments made under the cross-border mode of supply should be without reference to the technological method used.
- GATS commitments should facilitate e-commerce. As such, commitments should especially be sought in cross-border trade and consumption abroad, building on commitments concerning commercial presence as they develop and are negotiated through the GATS. In order for liberalization of financial services to yield optimum results, it should be recognized that the liberalization of related services, such as financial information, telecommunications and IT services, is also of great importance.
- Regulations should be transparent and adaptable and acknowledge developments in the market, so that regulators can respond quickly to technological change. Recent history has shown that e-commerce has grown most rapidly in those countries which have refrained from new e-commerce specific regulation. In this new environment, enabled by the internet and related technologies, increased competition can also serve to protect consumers' interests.
- Governments should work through international organisations to ensure international consistency of legislation. Questions of jurisdiction and applicable law should be addressed at the international level, taking into account the possibilities opened up by e-commerce.
- While this dialogue continues, and certainly during the Doha Round, it is important that no new barriers are imposed.

#### ■ **Movement of natural persons**

The need to move professional, technical and managerial personnel across national boundaries for purposes linked to international trade and investment is crucial to business, and especially to service providers. We therefore recommend that the movement of natural persons be treated as a priority issue in the GATS negotiations. Rules and practices to achieve greater certainty, transparency and speed in the movement of natural persons are:

- agreement on common definitions of key business personnel;
- agreement on transparent processes (i.e. a simple explanation of visa and work permit requirements and annual statistics on numbers of temporary working visas);
- common terms for intra-company transfers;
- provision for short-term movement of key business personnel;
- co-ordinated treatment of modes 1,3 and 4 (i.e. a link with cross-border supply of services and foreign establishment).

ICC encourages WTO member countries to make particular efforts to schedule additional commitments under GATS “mode 4”, due to the increasing need to move professional, technical and managerial personnel across national borders for purposes linked to international trade and investment; an area of particular interest to developing countries. Further progress should also be made towards the mutual recognition of professional qualifications.

ICC strongly believes that the financial sectors of both industrial and developing countries would profit from improved temporary access for highly-skilled personnel, such as managers and experts, from other WTO member states. This would facilitate the transfer of knowledge and the net effect on domestic employment would be positive rather than negative. In addition, mode 4 liberalization is, to a large extent, a prerequisite for mode 3 liberalization, e.g. sending managers and experts to establish a commercial presence.

Thus, to fully realize the benefits of opening up financial sectors for foreign firms, a sufficient degree of openness for temporary movement of personnel is required.

■ **Implementation and phasing-in approaches**

Members of the WTO should continue to explore ways to develop capacity-building programmes to help developing countries establish the regulatory and financial services infrastructure needed to support the market opening commitments to be made in the ongoing GATS negotiations.

WTO work on regulatory issues will be useful to support domestic regulatory reform efforts, including the adoption of international standards. In this respect, the WTO can benefit from co-operation with international supervisors and draw on the work on standards which has been undertaken by bodies such as the Basel Committee on Banking Supervision, the International Association of Insurance Supervisors (IAIS) and the International Organization of Securities Commissions (IOSCO).

As developing countries move forward with liberalization, attention may need to be given to the different stages of development of financial markets among WTO members and the possibility of a temporary negative impact of such liberalization on an individual domestic industry.

Accordingly, ICC acknowledges that the liberalization objectives it has outlined may need to be phased in over an appropriate period in certain countries, especially developing economies. These phase-in periods will vary by country depending on its local market, legal, regulatory and administrative frameworks. It may be appropriate for certain liberalization steps to be phased in before others. Developed countries should support capacity building programmes within the WTO and other organizations which will assist countries to create the conditions necessary for full implementation of liberalization commitments.

However, in the services negotiations, governments should still include timelines for meeting liberalization commitments and these should be as short as is reasonable in light of the specific circumstances of each member country.

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**About ICC**

ICC is the world business organization. Grouping together thousands of member companies and associations from over 130 countries, it is the only representative body that speaks with authority on behalf of enterprises of all sizes and sectors in every part of the world.