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FINANCIAL SERVICES TRADE

New WTO Accord Necessary To Ensure Open and Fair Markets Into The Next Century

ISSUE

Liberalizing trade in financial services enhances and strengthens capital market efficiency, and bolsters financial sector stability. Increased competition stimulates innovation and provides consumers with the broadest range of products and services at the lowest cost. There are additional special benefits from financial services sector liberalization, which has a knock-on effect for economic growth, both in individual countries and globally. This results in enhanced opportunities abroad for all U.S. firms.

U.S. trade negotiators have pursued trade policies which promote global economic growth through open and fair financial services markets. Many U.S. trading partners, however, either discriminate against foreign firms operating in their markets or they exclude them altogether. Foreign firms have virtually unlimited access to the U.S. markets.

POSITION

SIA strongly supports the inclusion of financial services in the World Trade Organization's (WTO) "GATS 2000 Negotiations." Current trends in trade and financial market conditions underscore the critical importance of further liberalization of financial services trade.

Globalization is fueled by liberalized trade and investment, and technological change, and has enhanced efficiency and competition. The direct connection between liberalization, globalization and growth has produced enhanced market conditions and increased opportunities for securities firms around the world, as well as for those who use them. The success of the GATS 2000 negotiations is vitally important to sustaining these trends.

SIA's objective is to build upon the progress made in the 1997 financial services sector negotiations to achieve an accord that reduces and eliminates the remaining barriers U.S. securities firms face in foreign markets. To continue meeting the credit and investment needs of issuers and investors in global markets, U.S. financial services firms must be allowed open and fair access to foreign markets. SIA recommends that negotiators reject deficient offers, such as those that codify the status quo without any progress; enshrine existing discriminatory practices; or, do not fully grandfather existing investments and operations.

BENEFITS OF THE 1997 ACCORD

The financial services sector, including the U.S. securities industry, secured some meaningful benefits from this agreement, including:

- creation of international rules for financial services firms;
- reduction and removal of discriminatory restrictions;
- institution of dispute settlement for agreement violations;
- specific liberalizing measures in emerging markets; and
- establishment of a “floor” from which to build future liberalization.

However, countries generally failed to commit to further liberalization beyond existing practice.

WHAT NEEDS TO BE DONE

The GATS 2000 negotiations will provide an excellent opportunity to eliminate obstacles from foreign markets that hamper the competitiveness of U.S. firms and reduce U.S. economic growth and job creation. Remaining barriers to entry and discriminatory treatment stifle the innovation and creativity of the securities industry, thus making the GATS 2000 negotiations of tremendous importance. Moreover, GATS 2000 provides an opportunity for countries to “bind” the additional liberalization measures (i.e., those which exceed commitments made under the GATS) implemented since the conclusion of the last Round.

POLICY DISCUSSION

To accomplish SIA’s objectives, the following core principles must be incorporated in a financial services agreement:

Commitments to Open Markets

In the last Round, many of the commitments made were to only “lock-in” current practice. Any agreement reached during the Year 2000 Round must also grandfather existing investments and not create new restrictions. This is particularly important given that during the past two years, many countries have opened their markets beyond the commitments they made at the conclusion of the last Round. Current access levels must be made part of any final agreement. While some progress was made in 1997 on efforts to reduce and eliminate existing barriers, much work remains to be done. To meet the GATS goal of “Progressive Liberalization,” the GATS 2000 negotiations must result in substantial binding commitments by countries to remove specific financial services barriers still in place. Unless countries go beyond existing market practice and commit to lifting specific barriers, the agreement will provide little tangible benefit to the U.S.

Establishment of Commercial Presence and National Treatment

Establishing and developing relationships are critical elements in providing financial services. While the U.S. is the global leader in the export of financial services, a business presence in the host country may be the only way for firms to provide their products and services competitively. Despite the progress made during the last Round, many developing nations still deny foreign investors the right to structure their businesses efficiently, or they prevent them from establishing a local commercial entity at all. In many cases, establishment is limited to minority ownership, or hindered by an “economic-needs test.”*

The ability to operate competitively through a wholly-owned commercial presence or other form of business ownership must be a fundamental element of an agreement. Once established, companies in foreign markets should receive the same (i.e., national) treatment as

domestic companies. Without such treatment, foreign firms may establish, but be subject to rules and regulations which limit their ability to operate and compete.

Key Emerging Markets Still Make Establishment Difficult For Securities

Foreign Majority Ownership Permitted?

	<i>Yes</i>	<i>Needs Test</i>	<i>No</i>
Argentina	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Brazil	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>
Chile	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>
India	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Indonesia	<input checked="" type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Malaysia	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Philippines	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>
Singapore	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Thailand	<input type="checkbox"/>	<input type="checkbox"/>	<input checked="" type="checkbox"/>
Venezuela	<input checked="" type="checkbox"/>	<input checked="" type="checkbox"/>	<input type="checkbox"/>

Transparent Laws and Regulations

Transparent and fair regulatory systems play an integral role in the development of deep and liquid capital markets which attract market participants, increase efficiency and spur economic growth and job creation. Lack of transparency in the implementation of laws and regulations can seriously impede the ability of securities firms to compete fairly. In negotiating greater access for goods, reductions in tariffs provide a readily available way to reduce barriers to trade; i.e., tariffs on widgets can be reduced from 50 percent to ten percent over a five-year period. Financial services firms, however, are

confronted with non-tariff barriers in the form of regulatory restrictions, and lack of transparency in the implementation and application of regulations. These barriers can prevent access in much the same way as tariffs, but unlike tariffs, no quantitative mechanism exists to reduce them.

SIA urges negotiators to work on provisions that would, *inter alia* provide for equal access to regulatory proposals; require public availability of proposed regulations; provide an adequate public comment period on new regulations; and mandate the enforcement of regulations in a non-discriminatory manner.

While prudential concerns should be taken into account so as not to reduce legitimate concerns of regulators, unwarranted regulatory prohibitions also limit the ability of U.S. firms to compete in foreign markets. In some cases, the sale of specific products requires regulatory approval. In other instances, the ability to establish is impaired in light of restrictions on new licenses. Elimination of these barriers is complicated, especially when countries claim their restrictions are prudential in nature. However, many of these restrictions well exceed any legitimate prudential objective.

Reasonable Transition Periods

Creation of an open and sound environment for healthy competition is the core of the WTO process. U.S. financial services firms, in part because of their deep experience of working in partnership with official supervisors and self-regulatory bodies at home and abroad, are in a position to make significant contributions to global financial stability through active participation in the development of local capital market capabilities. Full market access and national treatment are critical prerequisites for the spread of best practices in risk management, legal and compliance, and technological applications for financial services.

However, the securities industry understands that some developing market firms and regulators may need time to adapt and reform their supervisory and business practices to additional competition. Consequently, while initial opening market measures should be made, reasonable transition periods toward liberalization are consistent with internal commitments made by member countries to take immediate steps toward sound supervisory and market practices. Remaining market access and national treatment restrictions should be progressively eliminated throughout the transition process, and permanent restrictions in terms of products, geography or market share should be eliminated.

Increased Cross-Border Access

The cross-border provision of financial services should be an important element of a WTO financial services agreement. Cross-border provisions should, for example, include the right to buy and sell financial products across borders and the right to participate in and structure transactions. This can be accomplished while addressing appropriate prudential concerns.

Elimination of Investment and Equity Limitations

U.S. institutional and retail investors hold nearly \$1.9 trillion of foreign stocks. Increasingly, U.S. investors are looking to securities from developing markets to diversify their holdings. However, they are often constrained by ceilings and limitations on the purchase of these securities, which artificially raise their costs. Additionally, these limitations also have costs to

the local markets, reducing liquidity and increasing volatility. These restrictions should be reduced and, eventually, eliminated.

U.S. FINANCIAL SERVICES SECTOR: An Engine for Economic Growth

GROSS DOMESTIC PRODUCT \$626 BILLION

The U.S. financial services sector accounts for 7.7% of U.S. GDP

FOREIGN EXPORTS \$15.8 BILLION

U.S. financial services firm exports exceed those of telecom, education, and legal services, and reached record heights in 1998, three times such exports at the beginning of the decade.

TRADE SURPLUS \$5.9 BILLION

Financial services firms provide cutting edge services and products that are sought by foreign individuals, institutions, and governments, nearly three times the surplus at the start of the decade.

EMPLOYMENT 6 MILLION

U.S. financial services firms employ almost 6% of total U.S. private non-farm jobs. Many of these jobs support foreign operations.

WAGES PAID \$335.7 BILLION

Wages in the financial services sector are nearly 9% of all earnings in the U.S. economy.

FOREIGN REVENUES 25% OR MORE

Many internationally competitive U.S. financial services firms garner one-quarter or more of their revenue from foreign sources.

* In some markets, national regulators of financial or other sectors have employed the so-called "economic needs test" to screen and often discourage new foreign direct investment. Economic needs tests are utilized by national regulators to screen new investment, and take into account *inter alia*, the number of existing firms, level of competition, and the size of the market, as criteria in the process of granting a license to establish a commercial presence. Overall, the economic needs test is subject to abuse as a subjective determination, which may ignore how a local market will benefit from the introduction of a new competitive entrant or supplier.