01.08.2014

THE 22ND TNF-SERVICES MEETING

NEGOTIATIONS ON FINANCIAL SERVICES

BACKGROUND NOTE

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Introduction

Financial services is one of the first four sectors identified in the Roadmap for SADC trade in services negotiations. It was originally intended that requests for commitments would be tabled by SADC Member States by March 2013, with the circulation of initial offers by June 2013.

Classification

The classification used in the WTO Services Sectoral Classification List W/120 provides the following classification of financial services:

A. Insurance;
   (a) Direct life insurance
   (b) Direct non-life insurance
   (c) Reinsurance and retrocession
   (d) Insurance intermediation and auxiliary services

B. Banking and other financial services (e.g. securities; money broking, financial reporting):
   (a) Acceptance of deposits and other repayable funds from the public
   (b) Lending of all types
   (c) Financial leasing
   (d) All payments and money transmission services
   (e) Guarantees and commitments
   (f) Trading on own account or for customers: money market instruments, foreign exchange, derivative products, exchange rate and interest rate instruments, transferable securities, and other negotiable instruments

(g) Securities
(h) Money broking
(i) Asset management
(j) Settlement and clearing services
(k) Provision and transfer of financial information and financial data processing
(l) Advisory and other auxiliary financial services

This classification is used in all offers so far tabled, and is reflected in the table of offers analysed in the Annex to this paper.

Some developed country WTO Members (the EU, Japan and the US) have used an alternative classification contained in an Understanding on Financial Services. This, however, has not been used by the majority of WTO Members and has not been proposed for the SADC negotiations.

Study of financial services in the SADC region

A study of financial services within the SADC region commissioned by the Secretariat and presented at a sector forum in Johannesburg in July 2013 found that:

- Many of the market access and national treatment limitations listed in SADC Member States' WTO schedules are too general, referring to underlying legislation but not the specific conditions which may or may not limit market access;
- Many limitations are prudential and may not need to be listed (see prudential carve-out below);
- Some limitations may not or may no longer reflect the current regulatory situation.

Banking

- In general the banking sector in the SADC region is relatively open to trade and competition, with few barriers to market access (other than prudential measures);
- Most barriers in banking apply in mode 4 and restrict the ability of banks and other financial institutions to employ foreign staff;
- Many SADC countries still impose foreign exchange controls or restrict the ability of local consumers to access financial services (cross border) from abroad;
- In most SADC Member States there are prudential limits on the shareholdings in financial institutions.

Insurance

- In general the insurance sector also seems open to trade and competition;
- While market access appears relatively open to foreign operators, restrictions on the legal form of commercial presence exist, particularly in relation to branches;

- The majority of SADC Member States do not impose ownership restrictions on foreign insurers;
- Many Member States do not restrict foreign capital participation in the domestic market;
- Legislation seems to be restrictive as regards foreign acquisition of domestic government owned insurance companies;
- Many SADC countries restrict the ability of local consumers to access financial services (cross border) from outside the country, particularly short-term and life insurance products;
- Reinsurance is generally more open;
- Foreign insurance companies wanting to repatriate their earnings face barriers in some Member States, mostly under foreign exchange regulations;
- Certain Member States prescribe that insurers are to cede a certain amount of their business with a predetermined reinsurer;
- Many mode 4 restrictions similar to those found in banking.

The study recommended that the following issues be considered during the negotiations:

i) <u>The importance of keeping banking markets open and competitive</u>: The study commented on the apparent paradox between the openness of markets, the lack of access to finance and the high cost banking, and asked:

   a. *Whether the regional banking environment was as open as it seemed on paper;*
   b. *What was the future for regulatory reform of the banking sector in the SADC region;*

ii) <u>The role and treatment of microfinance</u>: The study noted the importance of access to micro-finance for low-income consumers and the emergence of regional micro-finance institutions, and asked:

   i. *Whether the micro-finance sector needed to be scheduled and negotiated separately from banking;*
   ii. *Whether an understanding under the TiS Protocol on cross-border trade and investment in the micro-finance sector might be useful, underpinning the decision of SADC Ministers of Finance and Investment in July 2009 to include the regulation and supervision of micro-finance institutions in the work programme of the Committee of Insurance, Securities and Non-bank financial Authorities (CISNA);*

iii) Access to the national payments system: The study noted the increasing feasibility for non-bank institutions to participate in banking activities, but the existence of restrictions in most Member States limiting such access to banks. This limited initiatives such as mobile banking and raised market entry costs. The study argued for an appropriate balance between prudential requirements and restrictions on market access, and asked:

   i. *Whether there was evidence that access to the payment system in some SADC countries was used to keep out new entrants;*
   ii. *Whether there were examples from other countries, within and outside the region, that could offer guidance on how regional payment systems could be developed and optimised;*

iv) The need for an understanding on financial services, including a prudential carve-out: The study noted that many potential barriers to trade and investment in banking and insurance were couched in prudential regulations, and asked:

   i. *How far SADC prudential regulations were out of step with international best practice;*
   ii. *Whether it was possible to achieve harmonisation of certain aspects of prudential regulation across the SADC region, e.g. through an understanding under the Finance and Investment Protocol (FIP) – see below;*
   iii. *Whether it was possible to reach some kind of mutual recognition agreement between SADC financial regulators on standards of prudential supervision.*

Relationship with other SADC initiatives

In parallel with the trade in services negotiations, initiatives relating to regional integration of financial services is being undertaken under the SADC Protocol on Finance and Investment (FIP), which was signed by SADC Heads of State and Government in August 2006 and came into force in April 2010.

The detailed areas of focus of the FIP are contained in 11 Annexes which deal with: Investment, including the creation of a regional common investment zone; Macroeconomic Convergence; Cooperation in Taxation and Related Matters; Development Finance Institutions; Regulation and Supervision of the Non-bank Financial Services Institutions; Cooperation and Coordination of Exchange Control Policies; Cooperation in the area of Information and Communication Technology for Central Banks; Harmonisation of the Legal and Operational Frameworks for Central Banks; Payment, Clearing and Settlement Systems in SADC Countries; Harmonisation of Insurances, Securities and Non-Banking Authorities; Cooperation Among SADC Stock Exchanges; and Anti-Money Laundering. An Annex on Accounting and Auditing Standards is currently being developed.

Whereas the FIP does not include specific commitments to reform or reduce barriers to trade and investment, it complements existing and proposed regional trade agreements by encouraging cooperation, information-sharing, skills development and harmonisation across a wide range of regulatory issues that are key to financial sector strengthening and integration. Progress across these areas has, however, been slow and largely in response to international developments, where these coincide with the regional objectives of the FIP.

Negotiations under the Trade in Services Protocol have a complementary role to play. For example, there is a clear relationship between liberalisation of market access for foreign financial service providers and regulatory reform under the FIP. Specifically, there is a need in relation to commitments under the TIS Protocol to ensure that regulatory measures maintained for prudential reasons are not undermined. Hence, it will be important in this negotiation to consider the need for and terms of a so-called “prudential carve out”, which has applied in relation to commitments in financial services undertaken under the WTO General Agreement on Trade in Services (GATS).

Discussion point:

a. How could additional commitments under the Protocol on Trade in Services support the objectives of regional integration under the FIP?

Assessment of offers

Of the requests that have been submitted, six (6) Member States have focused on insurance services, and seven (7) have made requests in banking and other financial services. Taken together, all Member States have received requests for commitments in one or more financial sectors. Nine (9) Member States have responded with initial offers.

In **insurance**, generally speaking Mode 1 has remained unbound, with the exception in four (4) cases where offers have been made in reinsurance and retrocession. Mode 2 has also been left unbound in two (2) offers, limited in one case to insurance of risks not covered in the country concerned, or unbound only in relation to direct life insurance in a fourth case. Otherwise, Mode 2 offers are relatively open. In Mode 3, most offers have been relatively open. Some limitations have been proposed such as local incorporation requirements (with a limitation to incorporate as subsidiaries in one case), limitations on the provision of compulsory insurance, and in one case a residency requirement for intermediary services, which is the sub-sector most cautiously committed in Mode 3.

In relation to **banking and other financial services**, the position has been reversed, in that Mode 1 and 2 commitments seem to be more liberal than Mode 3. The position is analysed in Table 1:

Table 1: Summary of commitments offered in banking and other financial services

Sub-sector	Mode 1	Mode 2	Mode 3
(a) Acceptance of deposits and other repayable funds from the public	Unbound : 3 Limitation : 2 None : 4	Unbound : 2 Limitation : 1 None : 6	Unbound : 0 Limitation : 5 None : 3
(b) Lending of all types	Unbound : 3 Limitation : 2 None : 4	Unbound : 2 Limitation : 1 None : 6	Unbound : 0 Limitation : 5 None : 2
(c) Financial leasing	Unbound : 2 Limitation : 2 None : 5	Unbound : 1 Limitation : 1 None : 7	Unbound : 0 Limitation : 5 None : 3
(d) All payments and money transmission services	Unbound : 2 Limitation : 2 None : 4	Unbound : 1 Limitation : 1 None : 6	Unbound : 0 Limitation : 5 None : 2
(e) Guarantees and commitments	Unbound : 2 Limitation : 2 None : 5	Unbound : 1 Limitation : 1 None : 7	Unbound : 0 Limitation : 5 None : 3
(f) Trading on own account or for customers: money market instruments, foreign exchange, derivative products, exchange rate and interest rate instruments, transferable securities, and other negotiable instruments	Unbound : 3 Limitation : 2 None : 4	Unbound : 2 Limitation : 1 None : 6	Unbound : 0 Limitation : 5 None : 3
(g) Securities	Unbound : 3 Limitation : 2 None : 3	Unbound : 2 Limitation : 1 None : 5	Unbound : 0 Limitation : 5 None : 2
(h) Money broking	Unbound : 4 Limitation : 2 None : 1	Unbound : 2 Limitation : 1 None : 4	Unbound : 0 Limitation : 5 None : 2
(i) Asset management	Unbound : 3 Limitation : 3 None : 2	Unbound : 2 Limitation : 1 None : 5	Unbound : 0 Limitation : 5 None : 2
(j) Settlement and clearing services	Unbound : 4 Limitation : 2 None : 2	Unbound : 2 Limitation : 1 None : 5	Unbound : 0 Limitation : 4 None : 1
(k) Provision and transfer of financial information and financial data processing	Unbound : 4 Limitation : 2 None : 2	Unbound : 1 Limitation : 1 None : 6	Unbound : 0 Limitation : 5 None : 2
(l) Advisory and other auxiliary financial services	Unbound : 2 Limitation : 3 None : 2	Unbound : 1 Limitation : 1 None : 5	Unbound : 0 Limitation : 4 None : 2

Annex on Financial Services

The GATS Annex on Financial Services is an integral part of that agreement and hence applies to all SADC Member States that are also Members of the WTO. It recognises that instability in the banking system can affect the whole economy and that financial services regulators need a very wide latitude to take prudential measures, such as those for the protection of investors, depositors and insurance policy holders, and to ensure the integrity and stability of the financial system.

The Annex on Financial Services contains one key provision, known as the "prudential carve-out", and is expressed as follows:

> "Notwithstanding any other provisions of the Agreement, a Member shall not be prevented from taking measures for prudential reasons, including for the protection of investors, depositors, policy holders or persons to whom a fiduciary duty is owed by a financial service supplier, or to ensure the integrity and stability of the financial system. Where such measures do not conform with the provisions of the Agreement, they shall not be used as a means of avoiding the Member's commitments or obligations under the Agreement."

In other words, if a regulatory measure is applied for prudential reasons (as set out in the carve-out), they may in principle be taken without question. The main condition is found in the second sentence, which says that they must not be applied as an excuse for avoiding commitments such as market access of national treatment. So although the scope of the carve-out is wide, it is not unlimited.

Other provisions support the carve-out, notably:

- Members may recognise prudential measures of any other country in determining how their own measures relating to financial services may be applied;
- Members may become parties to a recognition agreement or arrangement, but they must also allow other Members to negotiate or join such agreements or arrangements, or comparable ones;
- Specific requirements for the expertise of any dispute settlement panels.

Discussion point:

b. Member States have already agreed that there is some justification for designing a prudential carve out for the Protocol on Trade in Services. How far does the GATS Annex on Financial Services provide a model text for a similar provision in the Protocol on Trade in Services? What drafting changes, if any, might be needed for the SADC region?

SADC Secretariat, July 2014

ANNEX: ANALYSIS OF REQUESTS AND OFFERS

Requests

As at July 2014, requests for liberalisation commitments in financial services have been made as follows (excluding Mode 4):

	DRC	MOZ	MUS	SWZ	SYC	ZAF	ZMB
A. Insurance		All MS: All sub-sectors	BWA, MOZ, MWI, NAM, TZA, ZMB, ZWE: All sub-sectors LSO: eliminate restrictions on foreign ownership and number of licences; repatriation of profits	AGO, BWA, DRC, MOZ, MWI, NAM, SYC, TZA, ZMB: All sub-sectors	All MS: All sub-sectors	AGO, BWA, DRC, MOZ, MWI, NAM, SYC, SWZ, TZA, ZMB, ZWE: All sub-sectors MUS: Reduction of remaining limitations	AGO, DRC, LSO, MOZ, MWI, NAM, SWZ, TZA, ZWE: All sub-sectors MUS: Sub-sector (c)
B. Banking and other financial services	ANG, ZMB: Modes 1-3 in all sub-sectors	All MS: All sub-sectors	BWA, DRC, NAM, TZA, ZMB, ZWE: Sub-sectors (a)-(f) MOZ, MWI: improvements in Mode 4, repatriation of profits	BWA, DRC, LSO, NAM, SYC, TZA, ZMB, ZWE: All sub-sectors MUS: Sub-sectors (i) and (k). ZAF: Sub-sector (k)	All MS: All sub-sectors	AGO, BWA, DRC, MOZ, MWI, NAM, SYC, SWZ, TZA, ZMB, ZWE: All sub-sectors LSO: Improvements including (c) and (f(vi)). MUS: Reduction of remaining limitations	AGO, DRC, NAM, SWZ, TZA, ZWE: All sub-sectors LSO: Sub-sectors (a)-(h) MUS: Sub-sector (a) and (j)

Offers

The following Member States have made offers in financial services:

Insurance

	DRC	MOZ[1]	MWI	MUS	SYC	SWZ	TZA	ZAF	ZMB
Mode 1	(a)-(d) : Unbound	(a)-(d) except (c) : Unbound, except for distribution of insurance covering risks without insurance cover in Mozambique (c) : None	(a)-(d) : Unbound	(a)-(d) except (c) : Unbound (c) : Limitations on compulsory reinsurance	(a)-(b) : Unbound (c) : None (d) : Not offered	(a)-(d) : Unbound	(a)-(d) : None	(a)-(d) except (c) : Unbound (c) : Unbound except for approvals needed for reinsurers of life and short-term insurance; local incorporation and registration requirements	Not offered
Mode 2	(a)-(d) : Unbound	(a)-(d) except (c) : Unbound, except as in Mode 1 (c) : None	(a)-(d) : Unbound	(a) : Unbound (b)-(d) : Limitations on compulsory insurance and reinsurance	(a)-(c) : None (d) : Not offered	(a)-(d) : None	(a)-(d) : None	(a)-(d) : None	Not offered

[1] The MOZ offer contains horizontal conditions for the financial services sector as a whole

Insurance

	DRC	MOZ[2]	MWI	MUS	SYC	SWZ	TZA	ZAF	ZMB
Mode 3	(a)-(d) : Unbound	(a)-(d) : None	(a)-(d) : Foreign companies required to incorporate as subsidiaries	(a)-(b) : None (c) : None except for limitations on compulsory reinsurance (d) : None (brokers); None, except for limitations on compulsory insurance and intermediary services	(a)-(c) : None (d) : Not offered	(a)-(c) : Nationality limitations on shareholding (d) : Residency requirement for intermediary services	(a)-(d) : None, except that services must be provided through a limited liability company registered in Tanzania	(a)-(d) : Local incorporation and registration requirements	Not offered

2 The MOZ offer contains horizontal conditions for the financial services sector as a whole.

Banking and other financial services

	DRC	MOZ[3]	MWI	MUS	SYC	SWZ	TZA	ZAF	ZMB
Mode 1	(a)-(l) : Exchange controls apply	(a)-(l) : None	(a), (f)-(k) : Unbound (b)-(e): None	(a)-(g) : None (h)-(l) : Unbound	(a)-(l) : Unbound	(a)-l) except (g) and (h) : None (g)-(h) : Not scheduled	(a)-(l) : None	(a)-(l) : Unbound, except for (i) and (l) – registration requirement	(a)-(g) except (b) and (d) : None (b) : Unbound (d) : Not offered
Mode 2	(a)-(l) : None	(a)-(l) : None	(a), (f)-(k) : Unbound (b)-(e) : None	(a)-(l) : None	(a)-(l) : None	(a)-l) except (g) and (h) : None (g)-(h) : Not offered	(a)-(l) : None	(a)-(l) except (k) : Unbound (k) : None	(a)-(g) except (b) and (d) : None (b) : Unbound (d) and (h)-(l) : Not offered

[3] The MOZ offer contains horizontal conditions for the financial services sector as a whole.

	DRC	MOZ[4]	MWI	MUS	SYC	SWZ	TZA	ZAF	ZMB
Mode 3	(a)-(l) : Credit institutions must be legal entities, requiring prior approval, a minimum paid up capital and local/general ENTs	(a)-(l) : None, except	(a)-(k) : Only through subsidiaries of foreign banks	(a)-(l) except (j) : None (j) : None, except inter-bank transactions to be cleared through Central Bank	(a)-(l) : None, except credit reference and analysis only two years after WTO accession	(a)-l) except (g) and (h) : None, except: (a): Unbound for wholesale deposit services, residency requirement on Board of Directors (f) : Nationality requirement for foreign exchange bureau services (g)-(h) : Not offered	(a)-(l) : None, except that services must be provided through a limited liability company registered in Tanzania	(a)-(l) : Limitations on dealings in foreign exchange, incorporation requirement for custodial services for securities and financial instruments including derivatives; registration requirement for asset management , collective investment schemes, derivatives and advisory services; separate capitalization requirement for trading on account of customers	(a)-(f) except (b) and (d) : None (b) : Limitation to establish as subsidiary (g) : Limitation to incorporate or register locally; residency requirement on Board of Directors (d) and (h)-(l) : Not offered

SADC Secretariat
July 2014

[4] The MOZ offer contains horizontal conditions for the financial services sector as a whole.

GENERAL AGREEMENT ON TRADE IN SERVICES

ANNEX ON FINANCIAL SERVICES

1. *Scope and Definition*

(a) This Annex applies to measures affecting the supply of financial services. Reference to the supply of a financial service in this Annex shall mean the supply of a service as defined in paragraph 2 of Article I of the Agreement.

(b) For the purposes of subparagraph 3(b) of Article I of the Agreement, "services supplied in the exercise of governmental authority" means the following:

(i) activities conducted by a central bank or monetary authority or by any other public entity in pursuit of monetary or exchange rate policies;

(ii) activities forming part of a statutory system of social security or public retirement plans; and

(iii) other activities conducted by a public entity for the account or with the guarantee or using the financial resources of the Government.

(c) For the purposes of subparagraph 3(b) of Article I of the Agreement, if a Member allows any of the activities referred to in subparagraphs (b)(ii) or (b)(iii) of this paragraph to be conducted by its financial service suppliers in competition with a public entity or a financial service supplier, "services" shall include such activities.

(d) Subparagraph 3(c) of Article I of the Agreement shall not apply to services covered by this Annex.

2. *Domestic Regulation*

(a) Notwithstanding any other provisions of the Agreement, a Member shall not be prevented from taking measures for prudential reasons, including for the protection of investors, depositors, policy holders or persons to whom a fiduciary duty is owed by a financial service supplier, or to ensure the integrity and stability of the financial system. Where such measures do not conform with the provisions of the Agreement, they shall not be used as a means of avoiding the Member's commitments or obligations under the Agreement.

(b) Nothing in the Agreement shall be construed to require a Member to disclose information relating to the affairs and accounts of individual customers or any confidential or proprietary information in the possession of public entities.

3. *Recognition*

(a) A Member may recognize prudential measures of any other country in determining how the Member's measures relating to financial services shall be applied. Such recognition, which may be achieved through harmonization or otherwise, may be based upon an agreement or arrangement with the country concerned or may be accorded autonomously.

(b) A Member that is a party to such an agreement or arrangement referred to in subparagraph (a), whether future or existing, shall afford adequate opportunity for other interested Members to negotiate their accession to such agreements or arrangements, or to negotiate comparable ones with it, under circumstances in which there would be equivalent regulation, oversight, implementation of such regulation, and, if appropriate, procedures concerning the sharing of information between the parties to the agreement or arrangement. Where a Member accords recognition autonomously, it shall afford adequate opportunity for any other Member to demonstrate that such circumstances exist.

(c) Where a Member is contemplating according recognition to prudential measures of any other country, paragraph 4(b) of Article VII shall not apply.

4. *Dispute Settlement*

Panels for disputes on prudential issues and other financial matters shall have the necessary expertise relevant to the specific financial service under dispute.

5. *Definitions*

For the purposes of this Annex:

(a) A financial service is any service of a financial nature offered by a financial service supplier of a Member. Financial services include all insurance and insurance-related services, and all banking and other financial services (excluding insurance). Financial services include the following activities:

Insurance and insurance-related services

(i) Direct insurance (including co-insurance):

(A) life
(B) non-life

(ii) Reinsurance and retrocession;

(iii) Insurance intermediation, such as brokerage and agency;

(iv) Services auxiliary to insurance, such as consultancy, actuarial, risk assessment and claim settlement services.

Banking and other financial services (excluding insurance)

(v) Acceptance of deposits and other repayable funds from the public;

(vi) Lending of all types, including consumer credit, mortgage credit, factoring and financing of commercial transaction;

(vii) Financial leasing;

(viii) All payment and money transmission services, including credit, charge and debit cards, travellers cheques and bankers drafts;

(ix) Guarantees and commitments;

(x) Trading for own account or for account of customers, whether on an exchange, in an over-the-counter market or otherwise, the following:

(A) money market instruments (including cheques, bills, certificates of deposits);
(B) foreign exchange;
(C) derivative products including, but not limited to, futures and options;
(D) exchange rate and interest rate instruments, including products such as swaps, forward rate agreements;
(E) transferable securities;
(F) other negotiable instruments and financial assets, including bullion.

(xi) Participation in issues of all kinds of securities, including underwriting and placement as agent (whether publicly or privately) and provision of services related to such issues;

(xii) Money broking;

(xiii) Asset management, such as cash or portfolio management, all forms of collective investment management, pension fund management, custodial, depository and trust services;

(xiv) Settlement and clearing services for financial assets, including securities, derivative products, and other negotiable instruments;

(xv) Provision and transfer of financial information, and financial data processing and related software by suppliers of other financial services;

(xvi) Advisory, intermediation and other auxiliary financial services on all the activities listed in subparagraphs (v) through (xv), including credit reference and analysis, investment and portfolio research and advice, advice on acquisitions and on corporate restructuring and strategy.

(b) A financial service supplier means any natural or juridical person of a Member wishing to supply or supplying financial services but the term "financial service supplier" does not include a public entity.

(c) "Public entity" means:

(i) a government, a central bank or a monetary authority, of a Member, or an entity owned or controlled by a Member, that is principally engaged in carrying out governmental functions or activities for governmental purposes, not including an entity principally engaged in supplying financial services on commercial terms; or

(ii) a private entity, performing functions normally performed by a central bank or monetary authority, when exercising those functions.