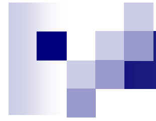


# Dangers of Further Liberalization of Financial Services in TISA

**Melinda St. Louis**

**Public Citizen's Global Trade Watch**

**"Trade in Services Agreement: The Dangers of Liberalizing Services"**

**Geneva, Switzerland, 17 October 2014**

- Lessons for promoting a robust, well-regulated financial sector
- Contradictions with trade and investment rules replicated and deepened in TISA
- Implications

## The reasons countries may liberalize:

- **improving countries' access to international capital**
- **lowering prices for consumers**
- **helping to recapitalize failing domestic firms**
- **encouraging the transfer of technology and skills**

**But if left unregulated, can lead to dangerous instability**

# Financial markets are not essentially stable

**According to data from Bank of International Settlements, during the 25 years preceding the most recent global financial crisis…**

- **93 countries suffered a total of 117 systemic disturbances in their financial systems**
- **51 less severe disturbances**
- **An average of six a year**

**We all know how financial crises lead to unemployment, wash away development gains…**

# Financial deregulation was a cause of the global financial crisis

- **Excessive risk-taking before the crisis created a shadow banking system**
- **Companies took advantage of countries' commitments to liberalize trade in financial services to engage in "regulatory arbitrage"**
- **Unregulated capital flows leave developing countries particularly vulnerable, as capital flows tend to be procyclical**

**Consensus: Financial markets need rules, limits and surveillance in order to make market failures less frequent and costly**

# Conflicts with General Agreement on Trade in Services (GATS)

***During the financial deregulatory period of the 1990s…***

- **Uruguay Round of the World Trade Organization’s General Agreement on Trade in Services (GATS) rules were negotiated**
- **More than 100 WTO members took financial services commitments in the GATS**
- **Doha Round requests on services pushed for further liberalization under current rules without recognizing lessons from crisis**
- **TISA furthers this agenda, and indications are that main proponents are not reconsidering the deregulatory rules in GATS**

# UN Stiglitz Commission

**“The framework for financial market liberalization under the Financial Services Agreement of the General Agreement on Trade in Services (GATS) under the WTO and, even more, similar provisions in bilateral trade agreements may restrict the ability of governments to change the regulatory structure in ways which support financial stability, economic growth, and the welfare of vulnerable consumers and investors.”**

***-Report of Commission of Experts, 2009***

# UNCTAD Trade and Development Report

**“The General Agreement on Trade in Services (GATS) of the World Trade Organization (WTO), many bilateral trade agreements and bilateral investment treaties (BITs) include provisions relating to payments, transfers and financial services that may severely limit not only the application of capital controls, but also other measures aimed at re-regulating or restructuring financial systems.”**

***-Chapter 4, p. 100-103, UNTDR, 2011***

# Conflicts: Market access rules

**Conflate liberalization and certain types of deregulation. In committed sectors…**

- **Prohibit bans of financial services or products (e.g., bans on toxic derivatives)**
- **Prohibit size limits on entities (e.g. too-big-to-fail regulations)**
- **Prohibit requirements on legal form (e.g., firewalls between deposit and investment banking)**

# Conflicts: Transfers rules

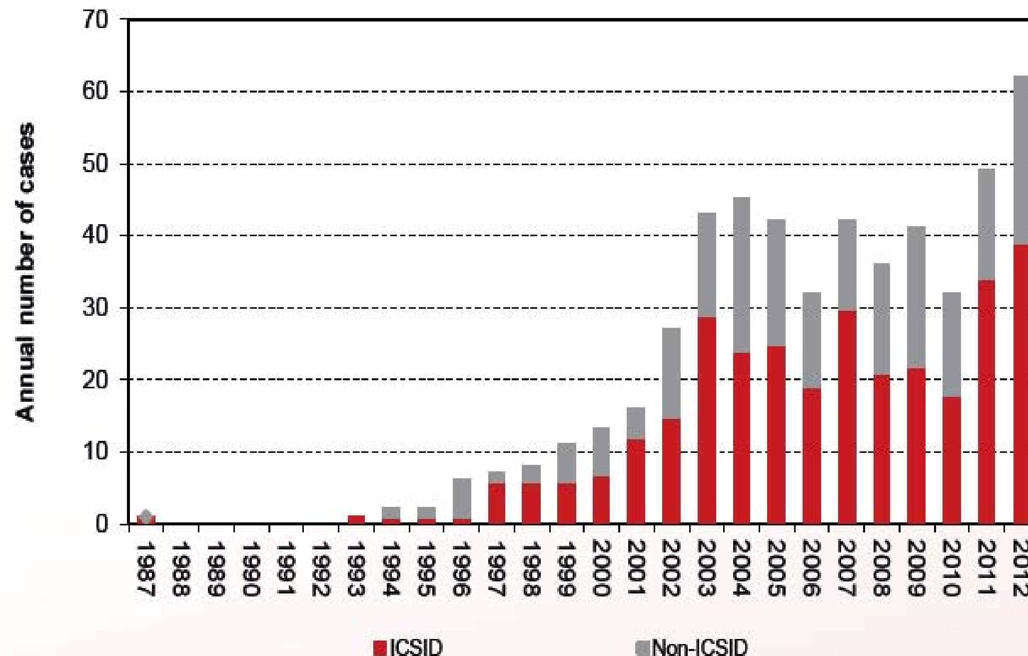
- Prohibit any restrictions on capital flows related to a service in a committed sector
- Implicates capital controls intended to protect stability from destabilizing “hot money” flows, asset bubbles, etc.
- IMF institutional view now recognizes capital controls as a legitimate policy tool in certain circumstances
- European Commission staff paper in 2010 noted potential conflicts with Financial Transactions Tax

# Exceptions may be insufficient to protect policy space

- **Prudential measures exception is not a "carve out", and is ambiguous if not self-cancelling**
  - **(Article 2(a) of GATS Financial Services Annex):** **Ambiguous second sentence:** ***"Where such measures do not confirm with the provisions of this agreement referred to in this paragraph, they shall not be used as a means of avoiding the Party's commitments of obligations under such provisions."***

- **Balance of Payments exception may be insufficient for capital controls and financial transactions taxes**
  - **GATS Art. XII:** **Only allows short term use in balance of payments crisis with IMF approval. But lists 10 limitations on countries' ability to respond to a balance of payments crisis, nine of which go beyond IMF requirements on capital restrictions or current restrictions or both.**
  - **So, cannot have in place to stop in flows of hot money. Also widely agreed that prudential exception does not apply to transfers**

# Conflicts: Investor to state dispute settlement (ISDS)




**Examples of ISDS implicating financial reg**

- **CME v Czech Republic:** **challenge too-big-to-fail regulations –** ***Investor awarded $265 Million***
- **CMS Gas v Argentina :** **challenge emergency stability measures –** ***Investor awarded $133 Million***
- **Postova v Greece:** **challenge sovereign debt restructuring measures – case pending**

**So far, it appears that there is not ambition to include ISDS in TISA – if included would be even more problematic**

# WTO Members Raise Concern/Call for Review in Light of the Crisis

- **February 2011– Barbados tabled paper raising concerns at Committee on Trade in Financial Services (CTFS)**
- **October 2011 – Ecuador proposed Ministerial Declaration calling for a review of rules to ensure policy space for macroprudential regulation; received support from developing countries; blocked by U.S. and EU**
- **March 2013 – Dedicated discussion held at CTFS – countries discussed macroprudential measures undertaken to safeguard financial stability**

# Further Concerns with TISA

- **Negative list for National Treatment**
- **Standstill on current level of regulation**
- **“Ratchet” – lock in unilateral deregulatory measures taken in the future**
- **Potential for further disciplines on domestic regulation, such as a dangerous multiple “necessity test”**
- **At best, insufficient balance of payments exception from GATS; at worst, no exception at all**

**All these could tie governments’ hands for future regulatory needs to avoid crises..**

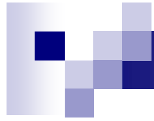
# Leaked TISA Annex on Financial Services

- **U.S. and EU – which pushed financial services liberalization and where global financial crisis originated - are most active in negotiations**
- **The currently voluntary "Understanding on Commitments in Financial Services" serves as a basis for TISA text – much more extensive rules than GATS**
- **Replicates the same problematic GATS "prudential exception" – instead of learning from crisis**

# Leaked TISA Annex on Financial Services

- **Standstill – Governments would be expected to lock in current level of deregulation**
- **Cross-border data flows – Governments would lose the right to require data to be held onshore, regardless of privacy concerns in other jurisdictions (such as U.S.)**
- **“Transparency” in developing new regulations – could provide new avenues for financial services industry to influence/challenge/delay new regulations**

- Why would countries deepen liberalization commitments in financial services sectors if the deregulatory rules are not fixed to ensure needed policy space for financial regulation?
- Such a project in TISA would contradict efforts elsewhere (G20, Basel, etc.) to encourage more robust financial regulation to avoid future crises.



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