



Negotiating Group on the Multilateral Agreement on Investment (MAI)

Expert Group No.5 on “Financial Services Matters”

THE TREATMENT OF PRUDENTIAL MEASURES IN THE MAI

(Note by the Chair)

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1. The Expert Group on "Financial Services Matters" has been mandated by the Negotiating Group to examine in particular the development of text on the treatment of prudential measures in the MAI. The present note is intended to serve as a basis for discussions.
2. There is consensus on the need to recognise the special nature of financial services and the critical role of financial institutions in the functioning of the economy, and to ensure that MAI obligations do not interfere with the legitimate exercise of prudential oversight aiming at protecting users of financial services and maintaining the integrity and stability of the financial system [DAFFE/MAI(96)25].
3. Recent international agreements dealing with financial services include a prudential clause (see Annex 1). One approach for the MAI would be to adopt a text similar to that contained in the Annex on Financial Services of the GATS. **The text might then read as follows:**

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Article A. Prudential measures

1. Notwithstanding any other provisions of the Agreement, a Contracting Party shall not be prevented from taking [reasonable] prudential measures with respect to financial services [, including measures] for the protection of investors, depositors, policy holders or persons to whom a fiduciary duty is owed by a financial [institution] [enterprise], or to ensure the integrity and stability of its financial system.
 2. Where such measures do not conform with the provisions of the Agreement, they shall not be used as a means of avoiding the Contracting Party's commitments or obligations under the Agreement."
4. **The Group may wish to consider how to define certain terms used in this draft text.** The Group may consider a definition of financial services based, for instance, on the definition used in the GATS (see Annex 2). To define "financial institutions" if this term were to be retained, one option would be to use the definition provided in NAFTA¹. The definition of investors and investments is under consideration by the Drafting Group No. 3.
5. The draft text leaves as an option whether it should use a closed list of measures which could qualify as "prudential". If the expression in brackets ",including measures" is deleted, the text would define "prudential measures" as only those necessary for the protection of users of financial services and the stability and integrity of the financial system. **The Group may wish to consider whether such a closed list is appropriate, whether it should cover other specific objectives as well, or be open-ended as in the GATS.**

¹ Article 1416 of NAFTA: "financial institution means any financial intermediary or other enterprise that is authorised to do business and regulated or supervised as a financial institution under the law of the party in whose territory it is located".

6. The proposed text recognises the right of a Party to take prudential measures which do not conform with National Treatment, MFN and the other provisions of the Agreement, provided that the measures are not used as a means of avoiding the Member's commitments². The inclusion of the term “reasonable” to refer to prudential measures in paragraph 1 of the draft article may help avoid possible abuse. The exercise of a Party's right to take prudential measures which may not conform with the provisions of the Agreement would be subject to the dispute settlement mechanism of the MAI. **The Group may wish to consider the need to specify how financial services experts would participate in the panel for disputes on issues relevant to financial services, and make proposals to the Negotiating Group in this regard.**

²It may be noted that, as far as the establishment of branches is concerned, the OECD Current Invisibles Code accepts only those requirements which are not more burdensome than those applying to domestic institutions (see Annex).

ANNEX 1

Selected texts of prudential provisions in international agreements

OECD Code of Liberalisation of Current Invisible Operations

Annex A

LIST OF CURRENT INVISIBLE OPERATIONS

E. Banking and Financial Services

General Remarks:

1. *Regarding operations in the country concerned, Members may take measures for the maintenance of fair and orderly markets and sound institutions and for the protection of investors or other users of banking or financial services, provided those measures do not discriminate against non-resident providers of such services.*

Annex II to Annex A

CONDITIONS FOR THE ESTABLISHMENT AND OPERATION OF BRANCHES, AGENCIES, ETC. OF NON-RESIDENT INVESTORS IN THE BANKING AND FINANCIAL SERVICES SECTOR

General

1. Laws, regulations and administrative practices shall ensure equivalent treatment of domestic enterprises and of branches or agencies of non-resident enterprises operating in the field of banking or financial services (including securities dealing) so that the establishment of branches and agencies of non-resident enterprises shall not be subject to more burdensome requirements than those applying to domestic enterprises.

Prudential Considerations

7. Domestic laws, regulations and administrative practices needed to assure the soundness of the financial system or to protect depositors, savers and other claimants shall not prevent the establishment of branches or agencies of non-resident enterprises on terms and conditions equivalent to those applying to domestic enterprises operating in the field of banking or financial services.

Energy Charter Treaty

Article 9(4):

Nothing in this Article shall prevent:

(a) financial institutions from applying their own lending or underwriting practices based on market principles and prudential considerations; or

(b) a Contracting Party from taking measures:

(i) for prudential reasons, including the protection of Investors, consumers, depositors, policy-holders or persons to whom a fiduciary duty is owed by a financial service supplier; or

(ii) to ensure the integrity and stability of its financial system and capital markets.

GATS

ANNEX ON FINANCIAL SERVICES

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.

NAFTA

Chapter 14:

Financial Services

Article 1401: Scope and Coverage

1. This Chapter applies to measures adopted or maintained by a Party relating to:

(a) financial institutions of another Party;

(b) investors of another Party, and investments of such investors, in financial institutions in the Party's territory; and

(c) cross-border trade in financial services.

Article 1410: Exceptions

1. Nothing in this Part shall be construed to prevent a Party from adopting or maintaining reasonable measures for prudential reasons, such as:

(a) the protection of investors, depositors, financial market participants, policy-holders, policy-claimants, or persons to whom a fiduciary duty is owed by a financial institution or cross-border financial service provider;

(b) the maintenance of the safety, soundness, integrity or financial responsibility of financial institutions or cross-border financial service providers; and

(c) ensuring the integrity and stability of a Party's financial system.

4. Notwithstanding Article 1109(1), (2) and (3), as incorporated into this Chapter, and without limiting the applicability of Article 1109(4), as incorporated into this Chapter, a Party may prevent or limit transfers by a financial institution or cross-border financial services provider to, or for the benefit of, an affiliate of or person related to such institution or provider, through the equitable, non-discriminatory and good faith application of measures relating to maintenance of the safety, soundness, integrity or financial responsibility of financial institutions or cross-border financial service providers. This paragraph does not prejudice any other provision of this Agreement that permits a Party to restrict transfers.

ANNEX 2

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ANNEX ON FINANCIAL SERVICES

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.