



Expert Meeting on
**THE IMPACT OF ACCESS TO FINANCIAL SERVICES,
INCLUDING BY HIGHLIGHTING THE IMPACT ON REMITTANCES ON
DEVELOPMENT: ECONOMIC EMPOWERMENT OF WOMEN AND YOUTH**
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SESSION 6:
FINANCIAL INCLUSION, TRADE AGREEMENTS AND REGULATORY REFORM

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Trade in Financial Services: Preserving Policy Space for Stability and Financial Inclusion

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**SINGLE-YEAR EXPERT MEETING ON THE IMPACT OF ACCESS TO
FINANCIAL SERVICES
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Outline

- **Lessons for promoting a robust, well-regulated financial sector to protect stability and promote financial inclusion**
- **Potential contradictions with governments' trade “market access” and “transfers” obligations**
- **Limitations of exceptions**
- **Alternative approaches**

Liberalization of the financial services sector

Potential Benefits...

- 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**

Development gains can be swiftly washed away in the wake of a severe financial crisis.

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 international trade/investment obligations

During the financial deregulatory period of the 1990s...

- **Uruguay Round of the World Trade Organization's General Agreement on Trade in Services (GATS) negotiated**
- **Bilateral and regional free trade agreements and investment treaties replicated and sometimes deepened GATS model**

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)

Limitations of Prudential Exception

- **GATS Financial Services Annex Article 2(a) – Called a “carveout” but actually only a defense once a measure has been challenged**
- **Prudential measures exception is ambiguous if not self-cancelling**
- **GATS negotiating history shows that stronger “carveout” language was proposed but weaker actual language adopted**
- **Policies taken for social goals (financial inclusion) would not be covered by this exception**

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**
- **Exceptions in GATS are not sufficient to protect policy space**

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 2011

“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

“Transparency” in Development of Future Regulations

- Leaked draft text of TISA provisions related to **“effective and transparent regulation”** could lead to undue industry influence over rulemaking at an early stage
- Such **“transparency”** and **“notice and comment”** procedures in the U.S. regulatory context in the last 30 years have evolved to require **pernicious cost-benefit analyses**, creating **lengthy delays** and **extensive litigation** through judicial review in the rulemaking process

Example from U.S.: Silica Rule

- Rulemaking process for standard to protect workers from silica exposure begins in 1998
- Endless reviews, including cost-benefit analyses, delays draft rule until 2011
- OIRA reviews draft for ~2 years. White House clearly fearful of electoral impact
- Rule finally now proposed
- Rule will prevent 60 workers/year dying, countless injuries

Current negotiations

- **Trade in Services Agreement (TISA)**
 - **Leaked draft of Financial Services Annex suggests that lessons from the crisis have not been taken into account**
- **Trans-Pacific Partnership (TPP)**
 - **Same rules for financial services have been agreed**
 - **Most recent deadline for conclusion missed due to continued controversy**

Alternative approaches to ensure policy space

- **Ecuador-led discussion at World Trade Organization about macroprudential financial regulation**
- **Stronger exceptions to preserve policy space for capital controls / exempt financial services from investor to state dispute settlement in TPP**

Ultimately, may need to clarify/update trade rules to ensure broad policy space so that countries can capture the benefit of trade in financial services for their growth and development goals while creating a robust regulatory framework to safeguard financial stability and promote financial inclusion.



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