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COMMUNICATION FROM CANADA

Transitional Review Mechanism in connection with Paragraph 18 of the Protocol on the Accession of the People's Republic of China

The following communication, dated 4 November 2004, from the delegation of Canada is being circulated to the Members of the Committee on Trade in Financial Services.

1. Canada recognizes the earnest efforts on the part of China to implement its WTO commitments for financial services. Related to liberalization commitments under the GATS, China's operational requirements (including registered capital requirements) for banking have for the most part been made less onerous, and more in line with international best practices. As well, Canada is encouraged that the requirement that foreign banks must wait one year between receiving approval for a given branch and submission to the China Banking Regulatory Commission (CBRC) of an application to open another branch has been removed. Canada expects that branch licenses will be available on a national treatment basis from now on.

2. Continued liberalization of the securities and fund management sectors, such as increases in the permitted investments of financial institutions and in the number of Qualified Foreign Institutional Investors (QFIIs), signals that China is committed to the development of its domestic capital markets. Finally, improved market access for foreign insurance firms has produced concrete benefits to Chinese consumers and workers, as well as financial institutions. Canada also looks forward to the extension of provincial licenses to foreign insurance firms later this year.

3. Following on Canada's submissions for the TRM process in 2002 (S/FIN/W/20) and 2003 (S/FIN/W/33), the main focus of this inquiry is to clarify certain aspects of the Chinese financial sector regulatory regime, including how certain specific measures are regarded to be consistent with China's commitments in its Schedule of Specific Commitments and/or the Working Party Report on China's Accession. Two comments also address the promotion of a transparent financial sector regulatory regime in China.

4. In accordance with paragraph 18 of China's accession protocol, and in order to contribute to an informed discussion, Canada requests that China provide responses and relevant information concerning these questions and comments before or during the next meeting of the Committee on Trade in Financial Services.

Questions and Comments

A. INSURANCE

1. Canada would be interested to receive any specific information regarding China's plans to implement its licensing regime for province-wide access by foreign life insurance firms. We understand that in China, some large metropolitan areas are classified as provincial jurisdictions. Regarding provinces that contain more than one city, will firms need to be established in the capital city before being able to expand into other cities in that province? As well, does a provincial licence allow the establishment of multiple branches or sales offices without prior approval by CIRC?

2. Can China please provide an explanation of the licensing procedures for Chinese life insurance firms seeking province-wide access? If it differs from the upcoming regime for foreign companies, can China please indicate how it will ensure that national treatment is provided?

B. BANKING

3. Canada understands that the *Procedures on the Administration of Foreign Debts of Foreign Capital Banks in the Territory* issued on 27 May 2004 by the National Development and Reform Commission (NDRC), the People's Bank of China (PBOC) and the CBRC – as well as further implementing rules released on June 21st by the State Administration of Foreign Exchange (SAFE) – outline limitations on the amount of foreign exchange funding foreign banks may acquire from abroad through the imposition of a quota system. These regulations artificially cap the extent to which foreign banks' foreign currency lending can be financed offshore. Can China please explain how these regulations and implementing rules respect its GATS market access and national treatment commitments? We wonder whether this limitation provides a level playing field for foreign banks, especially for new branches that have no prior business to help assess their quota, but who would be severely restricted in their first year growth if the quota were too low. Alternatively, how will China accommodate established foreign banks that are expanding at a rapid pace and who would be very restricted by a quota that is primarily based on the level of its past business (as is the case for 2004 quotas)? Can China please indicate how the quotas will be established for 2005 and beyond, and explain how it will ensure transparency when setting quotas for each bank?

4. The above-mentioned regulations and implementing rules, when taken with Article 30 of the *Administrative Regulations on Foreign-Invested Financial Institutions*, further limit the foreign currency lending activities of foreign banks. This is because Article 30 requires that the value of a foreign bank's foreign currency deposits received within China shall not exceed 70 percent of the value of its foreign currency assets within China. Essentially, a foreign bank can only fund up to 70 percent of its foreign currency loans with funds deposited in China, and at least 30 percent of its loan funding must be from abroad. This requirement limits the ability of foreign banks to lend foreign currency without bringing in foreign currency from abroad. Therefore, this policy actively supports foreign borrowing as a means of financing lending, while the above-mentioned 2004 regulations and implementing rules restrict foreign borrowing (and the resulting foreign currency lending activities of the bank). Can China please indicate how both these regulations respect the equal competitive opportunities it is bound to provide in its GATS national treatment commitments when they act to doubly restrict the funding sources for foreign banks?

C. GENERAL

5. To ensure that foreign firms can form clear expectations regarding their rights and obligations when operating in China, Canada would like to encourage the China Insurance Regulatory Commission (CIRC), CBRC, China Securities Regulatory Commission (CSRC), and SAFE to communicate with firms in writing as much as possible, especially regarding interpretation of relevant

rules and regulations, and when responding in detail regarding such things as regulatory approvals or quotas on the use of foreign capital.

6. In a transitional period such as this, where a number of regulations are being promulgated in China, the importance of regulatory transparency is paramount. In this context, Canada encourages China to take necessary steps to ensure regular and effective application of public comment procedures on draft laws and regulations, as well as publication of those measures well in advance of their effective date. Does China plan to introduce any procedures or laws to promote a standardized public consultation process among the CBRC, CIRC, CSRC, SAFE and NDRC?
