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International Trade in Financial Services: The NAFTA Provisions

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Inauguraldissertation zur Erlangung der Würde eines Doctor iuris der Rechts- und Writschaftswissenschaftlichen Fakultät der Universitär Bern. Die Fakultät hat diese Arbeit am 11. Juni 1988 auf Antrag der beiden gutachter, Prof. Dr. Thomas Cottier und Prof. Dr. Regula Dettling-Ott, als Dissertation angenommen, ohne damit zu den darin ausgesprochenen Auffassungen Stellung nehmen zu wollen.

Preface

GOAL OF THIS WORK

Since its beginnings, the debates about the North American Free Trade Agreement (NAFTA) within the Parties' communities have greatly overshadowed the discussion of it outside North America. While inside Canada, Mexico, and the United States the Agreement is often seen in terms suggesting either doomsday for all involved or economic prosperity such as the world has never seen. In the non-American nations, NAFTA is rarely discussed, and when it is, then it is generally in a comparison with European integration. The Agreement, however, not only affects billions of dollars worth of traded goods and services, but it goes further than any other free trade zone[1] in sectoral coverage and depth of changes. The incorporation of a developing country's market within its scope just adds significance to NAFTA's attributes. In short, NAFTA cannot be ignored as it has too much potential to affect the way international trade and international trade law develops.

Chapter Fourteen has been selected as the object of study because of the importance of the financial service provisions to the NAFTA. Without the liberalization of financial services, trade in goods and services would be severely hindered, and the goals of the Agreement could never be fully achieved. I limit my study to the effects of the Chapter Fourteen provisions on the banking system in order not to compromise the depth of the analysis for breadth. Much of the analysis, however, can be adapted to the insurance and securities sectors.

I attempt to explain, in language understandable to non-specialists, the provisions' legal impact on non-Party banks, particularly in light of the new World Trade Organization's (WTO) regulation of trade in financial services. This is important as the findings reveal that there can be more effects on non-Party enterprises than arise directly from the text of the treaty. This opens the question of how an enterprise can minimize the competitive

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[1] The term 'free trade zone' is used to indicate a particular type of economic integration area, namely one in which internal trade barriers are removed, but each member retains control over its own external trade frontiers. This is as opposed to a customs union, in which the members establish a common external trade regime as well as eliminating internal trade barriers.

disadvantages it faces on a regional market (a question perhaps for international business managers as much as for lawyers).

Finally, I aim to illustrate how two legal systems—the financial service law system and the international trade law system—are responding to the increasing invasion of each other's spheres of existence by means of the example set in NAFTA's trade in banking services regime. The NAFTA's use of trade law principles to regulate the intra-regional financial services trade was the first to do so within the context of purely economic integration. Whether the needs of the banking system have been taken into consideration to a sufficient degree remains to be seen. I begin to discuss how trade law principles will need to meld with the principles of banking law in order to spur further dialogue on how to ensure that trade in banking services (or trade in financial services) will be sustainable in the long term.

SUMMARY

The study of preferential integration areas has long been a topic of concern for international economic lawyers, and the effects of such areas on the multilateral trade system have been examined with economic analyses and philosophical legal arguments since the formal multilateralization of trading relations following the Second World War. Counterpoised to the long history of integration areas is the study of trade in services. Here, international economic law only began to address the legal framework in the late 1970s. Even newer is international economic law's attention on trade in financial services. The present study combines the old and the new in examining how a particular preferential trade arrangement addresses trade in financial services.

NAFTA establishes a free trade zone among the territories of Canada, Mexico, and the United States. Trade in goods, services, and investment, as well as the regulation of trade-related areas such as intellectual property protection and competition policy are to be progressively liberalized under the supervision of an intergovernmental committee. Among NAFTA's wide sectoral coverage is trade in financial services, regulated in Chapter Fourteen of the Agreement. Although the NAFTA itself has been the topic of much scholarly investigation, the effects of the Agreement on those not party to it has been given much less attention. Moreover, the financial services provisions—although integral to NAFTA—have not garnered the attention of legal analysts interested in the third country effects of the regionalization of North America. I chose these provisions to study in part out of a curiosity to discover if the near absence of other studies in the area was based on a finding that there was simply nothing to say or whether the effects or the areas of law relevant to such analysis were too complex to parcel or whether there was a reason based on a mixture of these two possibilities.

The work contained here presents the results of a close examination of NAFTA Chapter Fourteen. The substantive legal provisions are presented and analyzed mainly from the perspective of international trade law, with the incorporation of general international law principles and financial

service law principles where I think appropriate. Chapter Fourteen's legal effects on NAFTA Parties' trade systems are then projected. More importantly, this book sets out to determine the legal effects of Chapter Fourteen on non-Party banks. In doing so, the current state of international law on trade in financial service must be considered, and I therefore set forth the present rules contained in the WTO's regulatory framework for trade in financial services to the extent necessary for my purposes. The provisions of the two agreements are then synthesized to determine where the NAFTA is compatible with the WTO laws and where the non-NAFTA WTO Members may encounter violations of their legally-protected rights under the law of the WTO.

The first two chapters, which make up Part I, give an overview of the context in which the Chapter Fourteen provisions are considered. Chapter 1 presents an account of the development of the Agreement, including the main forces for and against it within the Parties. It begins with an account of the Parties' historical bilateral relations, with an emphasis on early attempts to establish preferential trade agreements. This is followed by a short description of the Parties' multilateral trade relations. For readers not familiar with international economic law, there is an overview of the World Trade Organization legal system. This is intended to give the reader an introduction to the structure of the various agreements of the WTO and the ideology of the system. More detailed discussions of relevant WTO obligations are contained in subsequent chapters. Within the discussions of the multilateral relations, I set out each of the Parties' participation in the international trade law system of the General Agreement on Tariffs and Trade (GATT) and the current WTO. This is important for the later analysis of how the NAFTA obligations of the Parties interact with the WTO rules on financial services trade, and thus how the NAFTA affects third countries. Following these sections is an examination of the NAFTA negotiating process, with an emphasis on examining the domestic forces within each Party that helped or hindered passage of the NAFTA agreements within each national legislature. In Chapter 2 I cursorily explain each Party's banking system, in order that the reader realize how the treaty does (or does not) change the legal banking environment in the NAFTA territory.

Part II contains the core of the book. Chapter 3 focuses on the Chapter Fourteen provisions specifically. In this chapter, the individual provisions are explained and interpreted according to the general principles of international law on interpretation of treaties. Thus, the interpretation focuses on the plain language of the text and secondarily, as according to the context of the Parties and their goals in formulating the obligations contained in the chapter. In Chapter 4, I explain how Chapter Fourteen has changed the legal environment for Party banks, looking to the results of the Agreement's existence for banks in each Party's territory.

The chapters comprising Part III are detailed examinations of the NAFTA's role in the international economic law system and are thus of greatest interest to those studying the interaction of regional trade arrangements with the multilateral trade system. In Chapter 5, I present a discussion of how to determine whether a third party bank will be eligible for the NAFTA advantages, as the NAFTA's bank-nationality rules permit even non-Party-based institutions to benefit in many cases. Then the WTO rules

on preferential trading arrangements are set forth to answer the question of whether NAFTA is a 'WTO-legal' agreement, and the effects of such a decision are explained to the extent possible given the lack of legal precedent. Chapter 6 compares the individual provisions of Chapter Fourteen with the provisions of the WTO. This includes a detailed account of the development and content of the financial services provisions of the WTO under the General Agreement on Trade in Services (GATS). I then review the NAFTA Parties' individual WTO commitments taken in the December 1997 round of negotiations on financial services. The provisions of the NAFTA and GATS/WTO are then categorized according to their compatibility with each other, in order to indicate where a non-Party WTO Member bank might have protectable rights under international law. Chapter 7 sets out the legal effects of NAFTA on non-Party banks. Here I place particular emphasis on the indirect effects of Chapter Fourteen—those effects that arise not from the Parties' obligations under the Agreement, but rather from the fact that the NAFTA exists and is developing its own system of laws, influenced by the non-governmental groups and individuals that involve themselves in promoting regional law as opposed to national or multinational law.

Part IV concludes the main investigation into Chapter Fourteen and its legal effects on banks. Chapter 8 contains a projection of how an expansion of NAFTA could affect banks. This short discussion considers the problem from two angles: that of a purely accession-driven expansion of NAFTA; and that of an incorporation of NAFTA into a hemispheric free trade area. Chapter 9 concludes the book. It first contains a summary of the results of my work, but then goes on to set out some final thoughts on the idea of regulating global financial services under an agreement based on trade law principles. I assert that the NAFTA Chapter Fourteen, as an example of such an agreement, must take into account the legitimate interests of both the international trade system and the financial services legal system if it is to accomplish its aim of promoting a liberal and secure framework for trade in financial services.

K.N. Schefer
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