

**COMMUNICATION FROM THE REPUBLIC OF KOREA**

Negotiating Proposal for Financial Services

The following communication has been received from the delegation of the Republic of Korea with the request that it be circulated to the Members of the Council for Trade in Services.

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**I. BACKGROUND: PERSPECTIVE ON FINANCIAL SERVICES LIBERALIZATION**

1. Financial services are one of the most important infra-services and liberalization of trade in financial services has considerable impact on an economy as a whole. A well-functioning financial system provides an important vehicle for efficient allocation of financial assets and promotion of economic competitiveness.
2. Liberalization of trade in financial services has many positive aspects, including (i) increased economic growth through the introduction of foreign capital, (ii) adoption of advanced financial practices and know-how, and (iii) greater financial market efficiency through increased competition.
3. However, in the current international financial environment characterized by rapid and massive movement of private capital, an imprudent financial services liberalization could have negative effects on the development of financial systems as well as on the stability of emerging market economies. The 1997 Asian financial crisis is a case in point. Ill-prepared liberalization of financial services lacking sound financial infrastructure and strong supervisory system actually weakened financial system and eventually resulted in financial crises.
4. Following the Asian financial crisis, the international community discussed on the strengthening the financial systems of emerging market economies as a part of reforming the international financial architecture. The discussions were deemed to contribute to widespread adoption of international standards on financial supervision. Nevertheless, financial systems of emerging market economies are still fragile.
5. Therefore, Korea believes that international community should encourage developing countries to take more efforts to strengthen their financial systems in preparation for the further liberalization of their financial markets. In this respect, negotiations on financial services should aim at achieving more orderly and sequenced liberalization in accordance with the levels of developments of financial market and supervisory system of member countries.

## **II. SCOPE AND MODALITY OF THE NEGOTIATIONS**

### **A. HORIZONTAL COMMITMENTS**

6. While the main method of negotiation shall be Request and Offer approach, Korea recognizes that a formula approach aiming at undertaking horizontal commitments may enhance the level of liberalization of financial services. However, it would be desirable that horizontal commitments should be applied in such a way as to guarantee stability of trade in financial services, taking into account the financial circumstances of member countries.

7. In the same vein, the adoption of an "Understanding of Commitments on Financial Services" by all Members as a part of their specific commitments of the financial services may force some Members to adopt financial liberalization beyond what their financial circumstances allow for. The level of horizontal commitments, therefore, should be established through thorough discussion among member countries.

### **B. CREDITS FOR AUTONOMOUS LIBERALIZATION**

8. Autonomous liberalization of financial services is a valuable voluntary contribution to expanding trade in financial services. Providing credits for such autonomous liberalization is an effective tool for encouraging member countries to take self-generating financial liberalization measures. Consequently, credit must be given to autonomous liberalization measures in the financial services negotiations in accordance with the criteria to be developed at the Council for Trade in Services Special Session.

## **III. EXPECTATIONS FROM THE NEGOTIATIONS**

9. Korea believes that financial services negotiations should aim at gradual removal of various obstacles and barriers that distort the flows of financial services. Korea is of the view that the initiatives of advanced countries in this respect are particularly important.

### **A. CONSTRAINTS ON COMMERCIAL PRESENCE**

10. Trade barriers that constrain commercial presence, including limitations on equities sharing, types of operation, number of operations and nationality of management or employees, need to be gradually abolished by all member countries.

### **B. MFN EXEMPTIONS**

11. MFN exemptions are of the most fundamental principles of the multilateral trade system, and thus should be eliminated except for those which can be justified for historical or geographical reasons. In particular, the reciprocity test applied by certain countries to protect and assist the expansion of foreign operation of their financial institutions should be abolished without exception.

### **C. DIFFERENT LIMITATIONS APPLIED BY SUB-CENTRAL GOVERNMENTS**

12. Different regulations applied by sub-central and local governments on types of operation, ceiling on equities sharing, or other limitations on trade in financial services act as critical barriers to establishing or expanding operations of services suppliers. Therefore, the financial services negotiations should aim at harmonizing different regulations maintained by sub-central and local governments.

D. LIBERALIZATION OF CROSS-BORDER TRADE IN FINANCIAL SERVICES

13. Cross-border financial transactions, especially those related to capital transactions, could increase volatility of financial systems. The recent development in e-finance based on the expansion of internet transactions has created a new international financial environment with greater possibility for large-scale and rapid cross-border capital movements. In addition, financial transactions without commercial presence tend to increase the possibility of capital reversal which can cause financial crisis through contagion effect and self-fulfilling behaviours. In-depth discussion, on the framework of prudential regulations on cross-border trade in financial services, are required in the financial services negotiations.

14. Korea is of the view that liberalization of cross-border transactions should be limited to those which (i) assist other economic activities and (ii) are not related to large-scale capital movement, such as financial consulting services and credit rating business.

E. TRANSPARENCY OF PRUDENTIAL REGULATIONS

15. Prudential regulations and measures are essential to ensuring the stability of financial markets. The financial services negotiations should not erode the principles that protect the right of financial authorities to implement prudential regulations as described in paragraph 2(a) of Annex on Financial Services.

16. However, prudential regulations should not be abused to restrain market access of foreign suppliers. They should not aim at reducing the range of operation of foreign financial services suppliers or imposing excessive burdens on them. Korea looks forward to discussion on how to develop more transparent and objective prudential regulations in the future negotiations.

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