



## CONSULTATION ON TRADE NEGOTIATIONS WITH THE UNITED STATES

The Securities Industry and Financial Markets Association (SIFMA) believes strongly in free, rules-based international trade and cross-border investment. With the United Kingdom (UK) preparing to negotiate trade deals independently of the European Union (EU), we look forward to the opportunity to create a comprehensive and forward-looking UK-United States (U.S.) free trade and investment agreement (FTA). We appreciate this opportunity to feed in our initial thoughts through your consultation.

The eventual terms that the UK and EU reach on their future relationship are yet to be determined. But that future relationship with the EU will form part of the context in which the UK makes its own trade policy, including with the U.S. Moreover, despite Brexit, SIFMA hopes to see continued and increasing trade, investment and regulatory cooperation between all three jurisdictions – the UK, U.S. and EU - in the future. Therefore, this contribution represents an *initial* outline of what UK and U.S. negotiators should be focused on as they approach potential negotiations rather than a definitive or exhaustive account of industry priorities.

The long-standing UK-U.S. relationship has important economic dimensions, underpinned by significant similarities in the structure and performance of financial services. London and New York remain the world's leading financial centers. Financial services account for around seven per cent of GDP in both economies. The UK is both the largest consumer of U.S. financial services exports, and the largest supplier of U.S. financial services imports. Both are capital market-based financial systems, with similar regulatory philosophies.

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<sup>1</sup> SIFMA is the leading trade association for broker-dealers, investment banks and asset managers operating in the U.S. and global capital markets. On behalf of our industry's nearly 1 million employees, we advocate on legislation, regulation and business policy, affecting retail and institutional investors, equity and fixed income markets and related products and services. We serve as an industry coordinating body to promote fair and orderly markets, informed regulatory compliance, and efficient market operations and resiliency. We also provide a forum for industry policy and professional development. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit <http://www.sifma.org>.

These common foundations mean a future UK-U.S. trade agreement offers an unprecedented opportunity for putting financial services at the heart of a new, 21<sup>st</sup> century economic relationship and enhancing the economic benefits to both countries.

The future relationship between the UK and U.S. in financial services, through a trade and investment agreement and related mechanisms of cooperation, should aim to have four key characteristics:

- Ensure that both economies maximize opportunities for exports and cross-border investment in financial services, integrating the U.S.-UK market in financial services and strengthening the competitive advantage of the industry in both the UK and U.S.
- Be forward looking and transparent and designed to tackle regulatory frictions early in the rule-making process.
- Strengthen the UK and U.S. as leading influencers of the future international financial regulatory agenda as *rule-setters*.
- Help re-define how trade and investment agreements are conceived, by fully integrating services and addressing truly 21<sup>st</sup> century challenges arising from modern technology and cross-border operations.

SIFMA welcomes the UK Government's pledge to develop trade and investment policy in transparent and inclusive ways. Its consultation regarding trade negotiations with the U.S. as well as similar exercises regarding Australia, New Zealand and the Comprehensive and Progressive Trans-Pacific Partnership are most welcome. We hope these efforts allow industries, such as financial services, to help the UK Government develop a solid foundation for active negotiations from 2019 onwards.

The recent conclusion of the U.S., Mexico and Canada Agreement (USMCA) offers pointers to the U.S. and UK as well as some lessons for improving trade policy. For example, for the first time in any U.S. trade agreement USMCA included a prohibition on local data storage requirements in circumstances where a financial regulator has the access to data that it needs to fulfill its regulatory and supervisory mandate. At the same time, there is significant scope compared with USMCA to enhance investor protections to ensure a level playing field between financial services and other sectors. USMCA is therefore a starting point for the U.S. and UK but the latter should be more ambitious. We elaborate on some of these issues below.

In terms of the substance of the future relationship between the two economies, including but not limited to a formal FTA, SIFMA urges negotiators to include the following elements, which we have divided into those based on technology and those related to more long-standing trade issues (such as, for example, investor protection).

### **Technology Elements**

- **Ensure the Free Flow of Data:** In the USMCA Financial Services Chapter, Article 17.19: Transfer of Information, is a good example of a strong free flow of data

provision that a UK-U.S. agreement can draw upon. It updates the approach from the GATS Understanding reached in 1997.

- **Prohibit Data Localization Measures:** In the USMCA Financial Services Chapter, Article 17.20: Location of Computing Facilities prohibits data localization as long as financial institutions provide the access to data to regulators for their regulatory and supervisory purposes. Again, this should be a foundation for UK-U.S. negotiators.
- **Coordination and collaboration on Cybersecurity:** In the USMCA Digital Chapter, Article 19.15, the Parties agreed to endeavor to build capacities of the national entities responsible for cyber incident response and to strengthen collaboration and cooperation to identify cybersecurity incidents and engage in information sharing. With the UK-U.S., such provisions may be expanded recognizing the long-standing relationship.
- **Prohibit measures that would require a financial institution to transfer or allow access to its source codes and algorithms:** This provision is included in USMCA Digital Chapter, Article 19.16 and applies to the financial sector. A U.S.-UK agreement should aim to replicate this provision.
- **Prohibit measures that would require a financial institution to purchase or use a particular technology:** In USMCA this protection was not extended to financial institutions. However, we support doing so in a U.S./UK agreement. See the Investment Chapter Article 14.10.1(c).
- **Prohibit measures that would require technology transfer:** In USMCA this protection was not extended to financial institutions. However, we support doing so in a U.S./UK agreement. See the Investment Chapter Article 14.10.1(f).
- **Explore how to deepen regulatory cooperation in the fintech space,** complimenting multilateral and other bilateral efforts aimed at promoting cross-border financial technology development and growth.
- **Seek to ensure that financial institutions can use cloud technologies.**

#### Other key elements

- **Investor Protections:** Financial institutions must invest abroad to serve customers and clients and, in doing so, make significant investments under the prudential regime of the trading partner. These investments, for example, should be protected in a UK-U.S. agreement from non-discriminatory treatment, direct and

indirect expropriation, under the minimum standard of treatment, including fair and equitable treatment, performance requirements and ensure free transfers.

- **Effective Dispute Resolution System:** The most effective dispute settlement mechanism for investors is Investor-State arbitration. A UK-U.S. agreement should include such a mechanism and ensure it extends to financial services to enable investors to bring their claims on a depoliticized basis and seek damages for breaches of the obligations.
- **Maximize cross-border market access in trade and investment:** The U.S. and the UK enjoy very open and diverse markets in financial services. For example, U.S. firms provide over \$50bn of financial services to the UK through their UK-based operations – more than the annual value of U.S. cross-border financial services exports to the UK. A UK-U.S. FTA could build on this further, by enshrining a gold standard in terms of mutual market access, enhancing volumes of cross-border financial services transactions and foreign direct investment. A UK-U.S. agreement should utilize a negative-list approach when scheduling commitments supported by a “ratchet mechanism” that will capture future liberalization in the sector of the trading partner. Traditional free trade agreements have covered very few commitments in the area of cross-border trade in services. At a minimum cross-border supply of financial services must include traditional insurance commitments, investment advice, portfolio management and electronic payment systems. We are also keen to engage in a broader conversation with the respective governments to explore other services that could be committed to for the cross-border supply of those services.
- **Transparency:** A UK-U.S. agreement should include robust transparency obligations that ensure stakeholders have the opportunity to review and comment on proposed measures. Such obligations would ensure industry and other stakeholders can engage with regulators to craft meaningful outcomes to meet regulatory objectives while not hindering the industry’s ability to serve its clients. The agreement should also set clear rules regarding how regulators will engage with applicants for a license, including timelines and fees.
- **Government Procurement:** A UK-U.S. agreement should seek to ensure that financial institutions will not be discriminated against in the procurement of services by the government and its related entities. Too often in trade agreements government procurement is excluded through government procurement chapters or in financial services chapters themselves. A new and fresh approach is warranted to ensure this type of business continues to be open to financial institutions.

- **Subsidies:** A UK-U.S. agreement should set a high standard to discipline subsidies to financial services related entities. Provisions in the financial services chapter should discipline the granting of subsidies to state-owned financial institutions with limited exception for certain programs.
- **Priority Sector Lending:** Today governments seek to require foreign financial institutions to participate in programs that require lending in particular sectors or to domestic firms. Often these sectors are not the sectors of typical business expertise for the foreign financial institution and require it to take on risk it otherwise would not. These programs undermine stability and opportunities to engage in other types of business when capital must be reserved for such programs. Although not an issue between the UK and U.S., the governments should set a high standard to prohibit these types of requirements in trade policy more generally.
- **Establish deeper regulatory co-operation.** There is a strong record of UK-U.S. regulatory co-operation in financial services (for example, the resolution strategies jointly developed in 2012 for their largest financial institutions). Even deeper regulatory co-operation, managed under clear requirements agreed between the respective regulators, would go still further in mitigating conflict and complexity before they manifest themselves. Improving cross-border regulatory processes would in turn improve the efficiency of cross-border regulation, benefit market participants and - as importantly - their end-user clients, with scope for added rigor without any threat to existing domestic rules and standards. A list of examples of issues that could benefit from enhanced regulatory cooperation is included as an annex to this submission.

There are a range of options for *how* improved regulatory cooperation is codified. One possibility would be to enshrine, *within* the text of a UK-U.S. trade agreement, a joint regulatory coordinating mechanism. Another is to house regulatory cooperation *outside* of a trade agreement, comparable in nature to the existing U.S-EU Regulatory Forum but with more ambitious outcomes and stronger transparency and industry engagement. We believe these options should be evaluated and discussed between industry and the respective Governments in coming months: effective regulatory cooperation between the UK and U.S. will be vital not just in terms of the standards developed in those markets but also in terms of setting the tone at the global level and enabling the two countries to demonstrate leadership in multilateral for a such as the Financial Stability Board and International Organization of Securities Commissions. Taking time to examine how best to achieve all that, and to discuss it with stakeholders, will be worthwhile.

## **Conclusion**

SIFMA believes that now is the moment for the UK and US authorities and their respective financial services industries, to begin laying the groundwork for how the new UK-U.S. relationship can develop over the next decade and beyond. Further trade, investment and regulatory co-operation between the UK and the U.S. will lead to greater job creation, enhance economic growth and support increased competitiveness on both sides of the Atlantic. It is a prize worth delivering.

## **ANNEX: Examples of how enhanced regulatory cooperation between the U.S. and UK could strengthen cross-border capital markets**

In designing and re-defining a new trade and investment relationship, the UK and U.S. have a unique opportunity to deepen regulatory cooperation between them, promoting real and dynamic transatlantic markets based on a level playing field. Examples of existing issues that such cooperation could help address include:

- **Cross-border resolution and prudential framework**. The UK and U.S. could strengthen their cooperation in relation to resolution of cross-border groups. For example:
  - secured support agreements could be recognized by each jurisdiction in substitution of internal TLAC;
  - each jurisdiction could grant recognition to the other's rules and supervisory practices relating to living wills, valuation capabilities in resolution, funding in resolution and similar resolution matters;
  - each jurisdiction's law would recognize the write-down/conversion powers of the other jurisdiction's regulators if the relevant instruments are governed by the first jurisdiction's law. This would avoid the need to have contractual recognition of bail-in clauses;
  - on prudential matters, rules on large exposures could be harmonized to facilitate exemptions from large exposures limits for sub-groups in the other jurisdiction;
  - any preferential treatments in the capital and liquidity regimes (such as for the purposes of the Net Stable Funding Ratio, Liquidity Coverage Ratio, or Standardized Approach to Credit Risk) could be extended to exposures/assets in the other jurisdiction.
- **UK Solo regime**: The PRA elects to apply 'solo' capital requirements at the level of individual regulated entities and deduct investments made in subsidiaries from the capital of those entities. The UK could align its approach to other EU members states and the U.S. where solo requirements do not apply or investments in affiliates are risk weighted.
- **Basel III/IV finalization**: The UK is frequently an early adopter of international standards. UK could harmonize implementation of the remaining Basel III standards in terms of calibration and timing with the U.S. Likewise, U.S. could harmonize rules (i.e., tailor gold-plating; e.g., revisit internal TLAC to be more flexible).
- **Ring-fencing**: In contrast to the U.S. IHC, the UK has not opted to ring-fence wholesale financial services. Ring-fencing is more appropriate for retail financial services and is inconsistent with the nature of wholesale banking. Harmonizing/tailoring ring-fencing would also encourage other jurisdictions to refrain from imposing similar requirements.

- **Equivalence / substituted compliance regimes for markets regulation.** Existing equivalence regimes (derived in the UK from EU legislation) could be enhanced and improved. The existing patchwork of regimes could be replaced with a single comprehensive regime for the entire financial sector, with appropriate governance, cooperation arrangements and transparency. The regimes would be based on equivalence of outcomes rather than line by line correspondence of rules.
- **Capital rules for cleared transactions:** Clarification and harmonization of capital requirements for cleared transactions across jurisdictions, including to address concerns about capital treatment of initial margin.
- **Security exchange rules:** Some form of exchange recognition or some ability for exchanges to conduct business directly with U.S. institutional investors and U.S. market dealers.
- **Licensing, Remuneration, and Senior Managers Regime:** UK/U.S. mutual recognition of individual licensing for professionals who move between the U.S. and UK to promote mobility. UK's Senior Managers regime makes it more difficult to attract senior executive talent. UK could align its restrictions on bonuses and other variable compensation with U.S. for competitive parity, since U.S. doesn't appear to be moving forward with executive compensation rule.