



Re: Request for Comments on Negotiating Objectives for a U.S.-Japan Trade Agreement

The Securities Industry and Financial Markets Association (SIFMA)¹ welcomes the opportunity to submit comments regarding the negotiating objectives for a U.S.-Japan trade agreement.

The relationship between the U.S. and Japan in financial services trade and investment is an important one. Both are amongst the world's largest economies and, as a result, important members of the G20 and other multilateral fora that help frame rules for cross-border trade and investment in financial services. Strengthening the foundation of this relationship creates significant potential for enhancing cross-border trade and investment in financial services and throughout every other sector of these economies that are supported by financial services.

The links between U.S. and Japan's capital markets are already deep. Two-way portfolio transactions in securities between the U.S. and Japan totaled \$1.95 trillion in 2017, a 4.3 percent decline from 2016. In 2017, U.S. portfolio holdings of Japanese securities totaled over \$1.0 trillion and Japanese portfolio holdings of US securities reached \$1.98 trillion, 74% and 65% increases respectively since 2007. Focusing on government bonds, U.S. holdings of Japanese government bonds has nearly tripled since 2007 to \$149.2 billion. Japan is the second-largest holder of U.S. Treasuries, holding \$1.0 trillion, roughly 83% above its 2007 level. Clearly, we are important investors in one another's countries.

SIFMA recognizes that this important process is taking place shortly after the United States Mexico Canada Agreement (USMCA). That agreement includes some valuable benchmarks that provide an excellent starting point for the future relationship with Japan. However, in some areas we believe that the U.S. and Japan should go further, aspiring to a modern, 21st century gold standard agreement that recognizes the increasing

¹ 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>.

importance of services (including financial services) to the global economy and the cross-border relationships within.

We divide our comments into two overarching sets:

- The first are related to the treatment of technology, reflecting its increasing importance to business and the issues it presents for trade negotiators;
- The second relate broadly to SIFMA views related to long-standing concepts and challenges in the trade (and investment) space.

Technology Elements

- **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 negotiators as they work towards a U.S.-Japan agreement and it is critical that the opportunity is taken to affirm U.S. policy on this issue which is vital to the future evolution of the global economy.
- **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 U.S.-Japan agreement can draw upon. It updates the approach from the General Agreement of Trade in Services (GATS) understanding reached in 1997 – an approach that has been outdated by the passage of over twenty years.
- **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 U.S.-Japan agreement, such provisions should be consolidated and if possible expanded.
- **Prohibit Measures That Would Require a Financial Institution to Transfer or Allow Access to its Source Codes and Algorithms:** The provision prohibiting such measures is included in USMCA Digital Chapter, Article 19.16 and applies to the financial sector. A U.S.-Japan agreement should aim to replicate this provision which provides vital protections to financial institutions.
- **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. We believe this should be rectified in future trade and

investment agreements that the U.S. enters into including a U.S.-Japan 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. Again, that should not be regarded as precedent as it leaves financial institutions open to unnecessary risk and uncertainty which hampers cross-border investment. We therefore support a robust prohibition against technology transfer in a U.S./Japan agreement. See the Investment Chapter Article 14.10.1(f).
- **Explore How to Deepen Regulatory Cooperation in the Fintech Space:** such an initiative would compliment 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 U.S.-Japan agreement from non-discriminatory treatment, direct and indirect expropriation, under the minimum standard of treatment, including fair and equitable treatment, performance requirements and also ensure free transfers.
- **Effective Dispute Resolution System:** The most effective dispute settlement mechanism for investors is investor-state arbitration. A U.S.-Japan 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. We also support inclusion of an enforceable state-to-state dispute settlement mechanism that provides for the strongest standards of protection for financial services.
- **Maximize Cross-Border Market Access in Trade and Investment:** The U.S. and Japan enjoy very open markets in financial services. For example, in 2016 U.S. firms provided \$22.4 billion of financial services to Japan through Japan-based operations;² U.S. financial institutions supply of services in Japan is second only to what they provide through affiliates in the UK. Conversely, Japan-based firms provided \$25.6 billion of financial services in the U.S.³ A U.S.-Japan Free Trade Agreement could build on this further, by enshrining a gold standard in terms

² [Bureau of Economic Analysis, Services Supplied to Foreign Persons by U.S. MNEs Through Their MOFAs \(2016\)](#)

³ [Bureau of Economic Analysis, Services Supplied to U.S. Persons by Foreign MNEs Through Their MOUSAs \(2016\)](#)

of mutual market access, enhancing the volume of cross-border financial services transactions and foreign direct investment. A U.S.-Japan 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 FTAs have covered very few commitments in cross-border trade in services. At a minimum cross-border supply of financial services must include traditional insurance commitments, investment advice, investment banking, asset 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 cross-border supply.

- **Government Procurement:** A U.S.-Japan 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 either 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 and a U.S.-Japan agreement is an opportunity to help establish one.
- **Subsidies:** A U.S.-Japan 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. The U.S.-Japan agreement should set a high standard to prohibit these types of requirements in trade policy more generally.
- **Establish Deeper Regulatory Co-operation:** The U.S.-Japan trade agreement is a unique opportunity to use the negotiation of a trade and investment agreement between Japan and the U.S. to establish a formal and comprehensive mechanism for cross-border financial regulatory cooperation. Such a mechanism can be principles based, with clear requirements agreed between the respective regulators to mitigate conflict and complexity before they manifest themselves. Improving cross-border regulatory development, implementation and enforcement would improve the efficiency of cross-border regulation, benefit market participants and - importantly - their end-user clients, with scope for added rigor without any threat to existing domestic rules and standards. There are a number of specific

features it will be important to get right with such a mechanism but we highlight two specifically:

- **Stakeholder Engagement:** Robust transparency obligations that ensure stakeholders have the opportunity to review and comment on proposed measures will be vital to the success of such a mechanism. 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.
- **Basis for Future Regulatory Cooperation:** There are a range of options for *how* improved regulatory cooperation is codified. One possibility would be to enshrine, *within* the text of a 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 far more ambition regarding outcomes as well as stronger transparency and industry engagement. We believe these options should be evaluated and discussed between industry and the respective Governments in coming months. This should also be considered within the context of the entire suite of trade and investment agreements the United States is currently pursuing.

Conclusion

The issues set out above are those that SIFMA and the U.S. based financial services industry believes are most urgent in the context of a prospective U.S.-Japan trade negotiation and, ultimately, agreement. It is not an exhaustive list of potential issues and there is important work ahead in terms of subsequent analysis and dialogue between the respective Governments and stakeholders. However, we believe that maximizing resources devoted to approaching these issues in the spirit that we propose would ensure a foundation for a trade agreement between the United States and Japan that will help strengthen prosperity and job creation for both economies.