

CHINA'S FINANCIAL REGULATIONS: ARE OTHER WTO MEMBERS' CONCERNS REALISTIC OR OVERCRITICAL?

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Since China's WTO accession it has been involved in four WTO disputes relating to financial services as the respondent, while other WTO Members remain concerned that China continues to limit access to foreign financial services and service suppliers. As other WTO Members' concerns could be either realistic or overcritical, this paper aims to explore whether there are any further inconsistencies in China's GATS obligations and financial regulations. After reviewing all WTO Members' concerns on China's financial services, this paper examines the consistency of four frequently and constantly raised issues with the GATS agreement and China's WTO obligations. As a result, this paper finds that two regulations are inconsistent with Article XVI and Article XVII of the GATS: the 20 per cent cap on shareholding in a Chinese-funded bank by a single foreign financial institution, and the 1 million RMB minimum for foreign banks' local currency business. Further, China still has not complied with its transparency obligations under the Accession Protocol and Working Party Report. These findings are significant for the Chinese government as well as other WTO Members who already have or want to have close trade relations with China in financial services.

I INTRODUCTION

Since China's World Trade Organization (WTO) accession, other Members have been paying serious attention to China's compliance with the General Agreement on Trade of Services (GATS) because of China's great participation in services trade. While China is well-known for products made

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in China, it is also one of the top traders in world commercial services. In 2011, 10 years after China's WTO accession, China's gross imports and exports of services rose from USD 66 billion to 362.4 billion at an annual growth rate of 20.4%.¹ Among the top economies,² in 2015 China's services trade shared 6% of world total export and 10.11% of the import market, which was only slightly lower than the United States but higher than all other countries.³ However, despite these positive aspects of China's WTO accession, concerns have been raised about China's compliance on trade in financial services immediately after its WTO accession, and to this day.⁴

A series of GATS-related disputes against China and issues continuously presented by other Members illustrate tensions regarding China's GATS obligations and its compliance. So far in 2017, China has been involved in six GATS disputes as the respondent, four of which are related to financial services. Other Members alleged that China's measures at issue⁵ or its actions⁶ were inconsistent with its obligations under Articles XVI and XVII of the GATS. In addition to these disputes, other WTO Members remain concerned that China continues to limit access to foreign services and service suppliers in some Chinese service sectors, frustrated the efforts of foreign service suppliers to achieve anywhere near their full market potential.

Many questions have been raised concerning trade in services under the Transitional Review Mechanism (TRM) and the Trade Policy Review (TPR). Among all service sectors, China's financial services have been most frequently questioned by other Members under both the TRM and TPR. Under the TRM, Members have brought forward comments and questions about financial services in a separate document to the specific Committee on Trade in Financial Services, instead of a document to the Council for Trade in Services.⁷

¹ During the period 2000–2010, 'China's Statistics of Trade in Services 2011' Data group, source: The WTO's International Trade Statistics Database, data released by the Ministry of Commerce, PR China.

² Top 12 economies including the United States, China, Japan, Germany, United Kingdom, France, Brazil, Italy, India, Russian Federation, Canada, and Australia, according to the World Bank Gross Domestic Product 2014.

³ Data from World Trade Organization, Statistic Database.

The United States: 14.52% (export) and 10.17% (import); Japan: 3.32% (export) and 3.77% (import); Brazil: 0.69% (export) and 1.49% (import); India: 3.27% (export) and 2.65% (import); Russia: 1.07% (export) and 1.88% (import); Canada: 1.60% (export) and 2.07% (import); Australia: 1.02% (export) and 1.16% (import); the European Union (EU): 25.19% (export) and 19.74% (import). Even though the share of EU is much higher than China, the data of the EU is not comparable with China as a community of states.

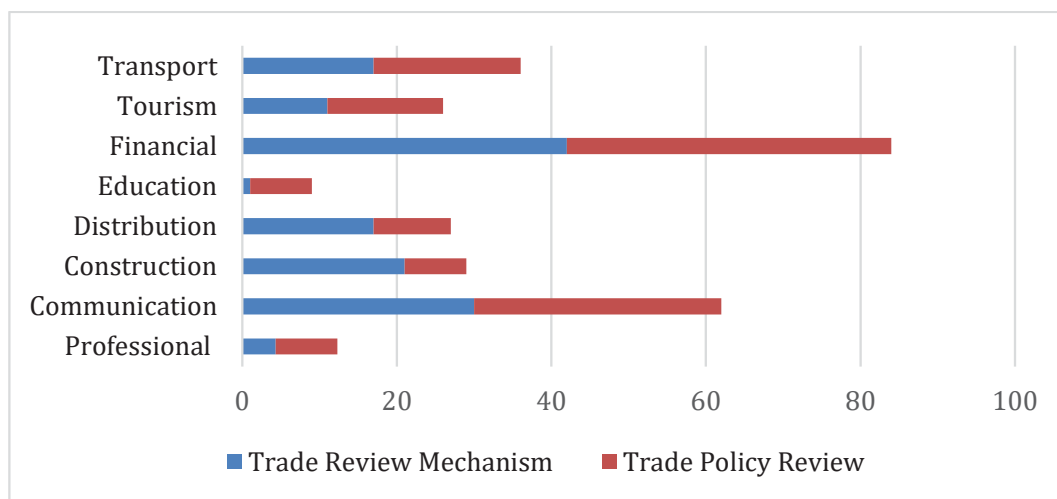
⁴ See below, after the first ten years of China's WTO accession, other Members raised concerns about China's trade in services under the Transitional Review Mechanism, and continue to query trade in services under the Trade Policy Review.

⁵ China—Measures Affecting Financial Information Services and Foreign Financial Information Suppliers, Dispute DS378, DS373 and DS372.

⁶ China—Certain Measures Affecting Electronic Payment Services, Dispute DS413.

⁷ For example, in 2002, the European Union put forward comments and questioned on TRM China trade in services in the WTO document (Restricted S/C/W/211), in which the European Union clearly stated: 'Please refer to the comments and questions sent on insurance, banking and securities services to the Committee on Trade in Financial Services' (S/FIN/W/18).

**Figure A: Number of Members Raising Concerns
(by Service Sector)**



Although China has replied to other Members' concerns under the TRM and TPR, this does not mean that these responses eliminate the possibility of GATS-inconsistency and are acceptable to the other Members. However, not all issues posed are considered GATS-inconsistencies because other Members may have unrealistic expectations of achieving full market potential in China. These issues could be valid or overcritical, but they trigger consideration of one question—apart from the issues deriving from the former GATS disputes against China, are there any further inconsistencies in China's GATS obligations and relevant domestic measures in financial services?

An examination of the TRM and TPR with respect to China's financial services reveals four issues that have been frequently and constantly raised by other Members. These issues could be summarised as: limitations on foreign investment in China-funded financial services; conditions on branches of foreign banks with respect to engaging in local currency business; and China's transparency obligations. As these oft-cited issues have not resulted in WTO disputes or been addressed by the Chinese government, this research will examine whether or not these issues are consistent with China's WTO obligations.

II LIMITATIONS ON FOREIGN INVESTMENT

Under the TRM and TPR, the European Community, the United States, Australia, Japan and Mexico consider that Articles 8 and 9 of the *Measures for the Administration of Investment and Shareholding in Chinese-funded Financial Institutions by Foreign Financial Institutions* (hereinafter the Measures)⁸ establishes foreign ownership restrictions in the banking sector. This issue has been questioned 15 times under the TRM and 14 times under

⁸ 境外金融机构投资入股中资金融机构管理办法, Order of the China Banking Regulatory Commission No. 6 [2003], promulgated on 8 December 2003.

the TPR but at the time of writing had neither been claimed for a WTO dispute nor revised by the Chinese government.

Article 8 of the Measures regulates the percentage of shares that an individual foreign financial institution can own in a Chinese-funded financial institution, which cannot exceed 20%. Article 9 does not directly regulate the maximum percentage of shares that can be owned, but states that a non-listed Chinese-funded financial institution must be supervised and administrated as a foreign financial institution if multiple foreign financial institutions own more than 25% of its shares. In other words, over 25% of collectively foreign equity investment classifies a non-listed Chinese financial institution in the Chinese stock exchange as a foreign financial institution. Other Members consider that the percentage caps of foreign shares in Chinese-funded financial institutions are inconsistent with China's WTO obligations, because China committed to ensuring that qualified foreign financial institutions would be permitted to establish Chinese–foreign joint banks and did not schedule any limitations on the percentage of foreign ownership in these banks.

The Chinese government's response to these regulations and practices was that there were no violation of the commitments in the Schedule because: (1) the issue of foreign equity participation in China's domestic banks was, by nature, an issue of cross-border merger and acquisitions, which was beyond the scope of China's WTO accession commitments;⁹ (2) the 25% threshold was not a cap on foreign shares, but only a criterion to determine the nature of a financial institution (whether a Chinese bank or a joint venture bank);¹⁰ and (3) the qualification of an enterprise as a joint venture was that foreign equity participation should be no less than 25% (the proportion of foreign investment in an equity joint venture shall be no less than 25% of the registered capital of the joint venture, the horizontal commitments in the Schedule).¹¹ China's responses reveal that the controversy derives from the identification of the nature of foreign equity participation in Chinese-funded banks. China considers the 20% and 25% foreign share values as percentage caps on foreign investment, while concerned Members regard them as market access limitations on Chinese–foreign joint venture banks in terms of the maximum percentage of foreign shareholding.

To verify the GATS-consistency of this issue, it is necessary to first clarify foreign investment in Chinese-funded banks and Chinese–foreign joint venture banks, by refining the terms used for Chinese-funded banks, joint venture banks and the relationship between foreign investment and trade in services.

⁹ Committee on Trade in Financial Services, 'Report of the Meeting Held on 27 November 2006, Note by the Secretariat' Restricted S/FIN/M/53 30 November 2006, hereinafter China's Responses 2006, at [28].

¹⁰ Committee on Trade in Financial Services, 'Report of the Meeting Held on 12 November 2007 Note by the Secretariat' Restricted S/FIN/M/55, 16 November 2007, hereinafter China's Responses 2007, at [44].

¹¹ Committee on Trade in Financial Services, 'Report of the Meeting Held on 1 December 2008 Note by the Secretariat' Restricted S/FIN/M/57, 4 December 2008, hereinafter China's Responses 2008, at [32].

This paper then discusses whether the 20% and 25% caps on foreign shares on Chinese-funded banks are consistent with China's GATS commitments.

A Context

Under the 2014 TPR, the United States asked China what in practice it meant to regulate a bank as a foreign-funded institution and how did this differ from being regulated as a Chinese financial institution. China answered that 'separate regulation on foreign-funded banks in practice is for the consideration of classified regulation ... and banking regulators implement differentiated regulation on various institutions according their characteristics', and 'China formulated some special provisions on the regulation of foreign-funded banks by referring to best international practices and mature experience of other countries according to the characteristics of foreign-funded banks for the consideration of prudential regulation'.¹²

Regarding Chinese-funded commercial banks, Article 2 of the Measures emphasises that Chinese-funded financial institutions/commercial banks are established *within China* according to law. Laws relating to the establishment of Chinese-funded commercial banks include the *Commercial Bank Law of People's Republic of China* (hereinafter the Commercial Bank Law)¹³ and the *Measures of China Banking Regulatory Commission for the Implementation of Administrative Licensing Matters Concerning Chinese-funded Commercial Banks* (hereinafter the Measures Concerning Chinese-funded Commercial Banks).¹⁴

The Commercial Bank Law is the fundamental law regulating all commercial banks that are established to absorb public deposits, make loans, arrange settlement of accounts and engage in other business in accordance with this law and the *Company Law of People's Republic of China*. The Measures Concerning Chinese-funded Commercial Banks state that Chinese-funded commercial banks include large state-controlled commercial banks (referred to as state-owned commercial banks),¹⁵ the Postal Saving Bank of China,¹⁶ joint-

¹² Trade Policy Review Body 1 and 3 July 2014, Trade Policy Review China Minutes of Meeting Addendum, WT/TPR/M/300/Add.1, 9 September 2014, 192.

¹³ 中华人民共和国商业银行法, adopted at the 13th Session of the Standing Committee of the Eighth National People's Congress on 10 May 1995, and revised on 27 December 2003 for the first time, and revised on 25 August 2015 for the second time by the Standing Committee of the National People's Congress.

¹⁴ 中国银监会中资商业银行行政许可事项实施办法, Order of China Bank Regulatory Commission No. 2 [2006], was revised by Order of CBRC No. 1 [2013] on 15 October 2013 for the first time and revised by Order of CBRC No. 2 [2015] on 5 June 2015.

¹⁵ See general, state-owned commercial banks include Industrial and Commercial Bank of China Limited (ICBC 中国工商银行), Agricultural Bank of China Limited (ABC 中国农业银行), Bank of China Limited (中国银行), China Construction Bank (CCB 中国建设银行), Bank of Communication (交通银行). All are listed banks on the Shanghai Stock Market.

¹⁶ See general, China Post Group owned by the State is the only shareholder of the Postal Saving Bank, but the situation will change because the Postal Saving Bank started a USD 8 billion IPO process in Hong Kong on August 2016.

stock commercial banks¹⁷ and urban commercial banks.¹⁸ Moreover, Article 11 of the Measures Concerning Chinese-funded Commercial Banks has regulations echoing the 20% and 25% caps: the proportion of the shares of a single foreign financial institution as the promoter or strategic investor of a Chinese-funded commercial bank cannot be more than 20%, and the total shares of several foreign financial institutions as the promoters or strategic investors cannot be more than 25%.

Foreign banks have shares in China's state-owned commercial banks, such as GIC Private Limited owns 0.07% of the Industrial and Commercial Bank of China; the Standard Chartered Bank owns 0.37% of the Agricultural Bank of China; the Bank of Tokyo–Mitsubishi UFJ Limited owns 0.18% of the Bank of China; and the Hongkong and Shanghai Banking Corporation Limited (100% owned by HSBC Holdings plc) owns 18.7% of the Bank of Communication. Among 12 joint-stock commercial banks, three have foreign financial institutions as the majority shareholders: Hua Xia Bank (Deutsche Bank Luxembourg SA, 9.28%; Deutsche Bank Aktiengesellschaft, 8.21%), China Bo Hai Bank (Standard Chartered Bank [Hong Kong] Limited, 19.99%) and Evergrowing Bank (United Overseas Bank, 12.4%).

Moreover, Banco Bilbao Vizcaya Argentaria had a 5% shareholding in China CITIC Bank valued at 5.01 billion Hong Kong dollars (HKD) until 2013 when it sold all its stocks for 13.136 billion HKD; and Citigroup Inc. had a 20% shareholding in China Guangfa Bank, but sold all its stocks to China Life Insurance Company in 2016.¹⁹ With respect to urban commercial banks, the shareholders of most are Chinese financial institutions, companies, enterprises and local governments.

A small number have foreign financial institutions as shareholders, such as the Beijing Bank (ING Bank NV, 13.64%), Tianjin Bank (Australia and New Zealand Banking Group, 12.03%), Shengjing Bank (VMS Investment Group, 4.63%), Shanghai Bank (BancoSantader SA, 7.20%), Ningbo Bank (Overseas–Chinese Banking Corporation, 20%), Nanjing Bank (BNP Paribas, 3.69%), Xi'an Bank (Scotiabank Globe, 19.99%) and Qi Lu Bank (Commonwealth Bank of Australia, 20%). Even though foreign financial institutions can be shareholders of state-owned commercial banks, joint-stock

¹⁷ See general, 12 joint-stock commercial banks until 2016, including China Merchant Bank Co. Limited (CMB 招商银行股份有限公司), Shanghai Pudong Develop Bank Co. Limited (SPDB 上海浦东发展银行), China CITIC Bank Co. Limited (CITIC 中信银行股份有限公司), Hua Xia Bank Co. Limited (HXB 华夏银行股份有限公司), China Everbright Bank Co. Limited (CEB 中国光大银行股份有限公司), China Minsheng Banking Corporation (CMBC 中国民生银行股份有限公司), Industrial Bank Co. Limited (IB 兴业银行股份有限公司), China Guangfa Bank Co. Limited (CGB 中国广发银行股份有限公司), Ping An Bank Co. Limited (PAB 平安银行股份有限公司), China Zheshang Bank Co. Limited (CZB 浙商银行股份有限公司), China Bo Hai Bank Co. Limited (CBB 渤海银行股份有限公司), Evergrowing Bank Co. Limited (EB 恒丰银行股份有限公司).

¹⁸ See general, there were 132 urban commercial banks until 2016, <<http://www.cbrc.gov.cn/chinese/jrjg/index.html>>.

¹⁹ See general, all data in this paragraph is updated to 30 June 2016.

commercial banks and urban commercial banks, in practice they do not have more than a 20% shareholding.

In relation to foreign-funded banks, the State Council of China promulgated the *Regulation on the Administration of Foreign-funded Banks* (hereinafter the Regulation)²⁰ and the *Detailed Rules for the Implementation of the Regulation on the Administration of Foreign-funded Banks* (hereinafter the Rules for Implementation)²¹ regulating wholly foreign-owned banks, joint venture banks, branches and representatives of foreign banks. Article 2 of the Regulation defines a Chinese–foreign joint venture bank as established by a foreign financial institution and a Chinese company or enterprise. The Regulation establishes conditions, procedures and capital requirements for the establishment of joint venture banks, but does not mention the ratio of investment from foreign financial institutions.

Until 2016, there were 46 foreign-funded banks.²² In practice, most foreign-funded banks prefer to establish branches and wholly foreign-owned banks in China. For example, some former joint venture banks have reclassified to the Chinese-funded commercial bank (Xiamen International Bank) or wholly foreign-owned bank (International Bank of Paris & Shanghai). Only a small number of Chinese–foreign joint venture banks are still running, with examples being the SPD Silicon Valley Bank established by Shanghai Pudong Development Bank and Silicon Valley Bank with 50% shareholdings each; Hua Yi Bank established by Fubon Financial Holding Co. Limited (80%) and Shanghai Pudong Development Bank (20%); and Sino–German Bausparkasse established by China Construction Bank (75%) and Bausparkasse Schwaebisch Hall AG (25%). The minimum shareholding for foreign financial institutions in joint venture banks is 25%, as indicated in the horizontal commitments in the Schedule. Further, the minimum 25% requirement for foreign investment is also regulated in Article 4 of the *Law on Chinese–Foreign Equity Joint Ventures*.²³

A comparison of Chinese-funded commercial banks with Chinese–foreign joint venture banks with respect to the relevant laws and regulations mentioned above is presented in Table 1 over the page.

²⁰ 外资银行管理条例, Order No. 478 of the State Council, promulgated and came into force on 11 November 2006, and was revised by the Decision of the State Council on Amending Some Administrative Regulations on 29 July 2014, Order No. 653 of the State Council.

²¹ 外资银行管理条例实施细则, Order of the China Bank Regulatory Commission No. 6 [2006] issued on 24 November 2006, amended by Order of the China Bank Regulatory Commission No. 7 [2015] on 1 July 2015.

²² China Bank Regulatory Commission, <<http://www.cbrc.gov.cn/chinese/jrjg/index.html>>.

²³ 中外合资经营企业法, Order No. 48 of the President of the People's Republic of China, adopted by the 5th National People's Congress on 1 July 1979, amended by the National People's Congress on 4 April 1990, and amended for the second time by the National People's Congress on 15 March 2001.

Table 1: Chinese-funded Banks and Chinese–Foreign Joint Venture Banks

Bank type	Similarity	Difference
Chinese-funded bank	<ul style="list-style-type: none"> * Established within China * According to the same law (Commercial Bank Law and Corporate Law) * Chinese judicial person * Requirements for foreign shareholders or investors: <ul style="list-style-type: none"> (a) their total assets must be no less than 10 billion USD at the end of the year prior to the filing of the establishment application (b) their capital adequacy ratio must reach the average level at the place of its registration and the regulation of CBR. 	<ul style="list-style-type: none"> * Administrative licensing procedure * Maximum shareholdings for foreign financial institutions: 25% by law and 20% in practice * Certain types of bank: state-controlled bank, the Postal Saving Bank, joint-stock bank, urban bank * Foreign promoter or investor must have been rated as ‘good’ for its long-term credit in the previous 2 years by an international rating institution acknowledged by the CBRC, and have retained a favourable balance in the previous 2 accounting years.
Chinese–foreign joint venture bank		<ul style="list-style-type: none"> * Applying the Regulation * Shareholdings of foreign financial institutions: at least 25% (in practice), but less than 100% (by law) * Subject to approval by the Chinese government * The unique or major foreign shareholder must be a commercial bank

B 25% Shareholdings

Article 9 of the Measures states that a non-listed Chinese-funded financial institution must be supervised and administrated as a foreign financial institution if multiple foreign financial institutions own more than 25% of its shares, but this limitation does not apply to listed Chinese-funded financial institutions. As indicated above, four state-owned commercial banks with foreign financial institutions as shareholders are Chinese-funded banks listed on the Shanghai Stock Exchange; and three joint-stock commercial banks have foreign financial institutions as shareholders, one of which (Hua Xia Bank) is a listed bank. The 25% cap does not apply to these listed banks, and they are still Chinese-funded banks if a foreign financial institution owns more than 25% of the shares.

Non-listed Chinese-funded banks are still Chinese-funded banks if the aggregate foreign participation is less than 25%, but they must be supervised and administrated as a foreign financial institution if foreign participation is more than 25%. Other WTO Members are concerned that the regulation is inconsistent with China’s GATS commitment that within five years after accession, any existing non-prudential measures restricting ownership and juridical forms of foreign financial institutions will be eliminated. However, the Chinese government stated under the 2008 TPR that if foreign investors wish to raise their shares in a non-listed Chinese bank to above 25%, this will

be regarded as the establishment of a new joint venture and the transaction will be subject to the approval of the CBRC, according to the Regulation and its Rules for Implementation.²⁴ This is consistent with China's horizontal commitment that 25% is a threshold for the participation of foreign equity in Chinese–foreign joint ventures. The criterion for determining whether an enterprise qualifies as a joint venture is that foreign equity participation is no less than 25%.

In practice and according to domestic regulations, multiple foreign financial institutions have the right to any level of participation. When the proportion of foreign ownership is lower than 25%, it is still a Chinese-funded bank; when this proportion is 25–100%, it is a Chinese–foreign joint venture bank; and, when it is 100%, it is a wholly foreign-owned bank. Besides, rather than forbidding more than 25% foreign investment, Article 9 clearly states that such an organisation must be supervised and administrated as a foreign financial institution (Chinese–foreign joint venture bank). Therefore, the 25% cap on investment by multiple foreign financial institutions does not violate China's commitment to eliminating restrictions on ownership.

Other WTO Members have also expressed concern about what it means to be regulated as a foreign-funded institution in practice, and whether this differs from being regulated as a Chinese financial institution. If the difference leads to less favourable treatment for foreign investors, the 25% cap may be inconsistent with China's national treatment obligations. Table 1 shows that China's regulatory measures for domestic and foreign-invested banks do differ somewhat. The most significant difference is that the key or major foreign shareholder²⁵ of a joint venture bank must be a commercial bank,²⁶ but any foreign financial institution can be the promoter and investor of a Chinese-funded bank. However, the Chinese government underscores that it is necessary 'to implement different prudential measures to foreign-invested banks, according to the types of risks they face, to safeguard the interests of

²⁴ Trade Policy Review Body, 21 and 23 May 2008, Trade Policy Review China, Minutes of Meeting Addendum, WT/TPR/M/199/Add.1 28 August 2008, 250.

²⁵ See general, Article 4 of the Detail Rules for the Implementation of the Regulation on the Administration of Foreign-funded Banks, which interprets the term of key shareholder as a commercial bank, which holds 50% or more of the total capital or total shares of the Chinese-foreign equity joint bank to be established, or which does not hold 50% or more of the total capital or total shares of the Chinese-foreign equity joint bank to be established but is to have:

1. half or more of the voting rights of the Chinese–foreign equity joint bank to be established;
2. the power to control the financial and operating policies of the Chinese–foreign equity joint bank to be established;
3. the power to appoint and dismiss most of the members of the board of directors or any similar power institution of the Chinese–foreign equity joint bank; and
4. half or more of the voting rights in the board of directors or similar power institution of the Chinese–foreign equity joint bank to be established.

In this sense, even though the foreign investor cannot hold 50% or more of the total capital, it can still be the key shareholder and must be a commercial bank. For example, as listed above, Standard Chartered Bank (Hong Kong) Limited has 19.99% of China Bo Hai Bank, Scotiabank Globe has 19.99% of Xi'an Bank, Commonwealth Bank of Australia has 20% of Qi Lu Bank, and these foreign banks are the biggest shareholder.

²⁶ Article 11 of the Regulation on the Administration of Foreign-funded Banks.

Chinese depositors and maintain the stability of the domestic financial system'.²⁷ The Schedule clearly states that 'within five years after accession, any existing *non-prudential* measures ... shall be eliminated'. The Chinese government may persist with the requirement that being a commercial bank is a prudential measure to foreign-funded banks by providing reasonable elucidation. In this case, the requirement for being a commercial bank may not be inconsistent with China's commitments as it is not a non-prudential measure. The partition of prudential and non-prudential measures on financial services is discussed later.

C 20% Shareholdings

Article 8 of the Measures demonstrably regulates that the proportion of the investment or shareholding in a Chinese-funded financial institution by a *single* foreign financial institution can be no more than 20%. Unlike Article 9, having over 20% of shares being held by a single foreign financial institution is not sufficient to change a Chinese-funded bank to a foreign-funded bank, but it is strictly forbidden by domestic regulations.

Article XVI:2(f) of the GATS states that limitations on the participation of foreign capital, in terms of maximum percentage limit on foreign shareholding or the total value of individual or aggregate foreign investment, shall not maintain or adopt based on either a regional subdivision or its entire territory, unless otherwise specified in a Member's schedule. Limitations within the meaning of Article XVI:2(f) should take one of two forms: (1) a maximum percentage of capital that can be held by foreign investors; or (2) a total value of foreign investment, either by an individual investor or foreign investors as a whole.²⁸

Four elements of Article XVI:2(f) must be interpreted to determine whether the challenged measure is inconsistent with Article XVI: first, whether the challenged measure contains limitations on 'foreign shareholding or the total value of individual or aggregate foreign investment'; second, whether the limitation is in terms of 'a maximum percentage'; third, whether there are limitations on the services covered by a committed sector or subsector; and finally, whether the limitation is listed as an exception to market access in the Schedule.

1 Foreign Shareholding or Individual or Aggregate Foreign Investment

Article 8 of the Measures literally states that it is about investment or shareholding in a Chinese-funded financial institution by a single foreign financial institution; thus, this measure is addressed to impose limitations on foreign shareholding and individual foreign investment.

²⁷ Trade Policy Review Body, 31 May and 2 June 2008, Trade Policy Review China Minutes of Meeting Addendum, WT/TPR/M/230/Add.1 22 February 2011, at 132.

²⁸ China—Measures Affecting Trading Rights and Distribution Services for Certain Publications and Audio-visual Entertainment Products Report of the Panel, WT/DS/363/R 12 August 2009, at [7.1360].

2 *A Maximum Percentage*

The 2001 Scheduling Guidelines²⁹ provides examples of limitations to market access drawn from schedules of specific commitments. For Article XVI:2(f), it enumerates as ‘foreign equity ceiling of x per cent for a particular form of commercial presence’,³⁰ and clarifies that ‘numerical ceilings should be expressed in defined quantities in either absolute numbers or percentages’.³¹ The words used in Article 8 are that ‘no more than 20 per cent’, which establishes a ceiling for foreign investment in Chinese-funded banks. The enforcement of the regulations prohibits foreign shareholding or investment over 20%. In doing so, it enacts a maximum limitation in terms of the percentage of participation of foreign capital.

3 *Covered by a Committed Subsector*

Even though the Measures regulate financial institutions, the terms of Chinese-funded financial institution include Chinese-funded banks; other WTO Members’ concerns focus on banking services but not the other financial institutions. In the Schedule, China has committed to subsector ‘banking and other financial services’. The measure seems to be covered by the committed subsector of banking services. However, China claims that it did not make commitments with respect to the acquisition of domestic banks by foreign financial institutions.³²

As a preliminary issue, China needs to clarify whether the Schedule includes specific commitments with respect to acquisition notwithstanding the fact that the word ‘acquisition’ does not appear in the Schedule. Article XX:3 of the GATS provides that WTO Members’ schedules shall be annexed to the GATS and shall form an integral part thereof, which means ‘the task of identifying the meaning of a concession in a GATS schedule is like the task of interpreting any other treaty text’.³³ Further, Article 3.2 of the DSU rules that Members’ schedules must be interpreted according to the ‘customary rules of interpretation of public international law’, which is well-stated in Articles 31 and 32 of the Vienna Convention.^{34, 35} Therefore, commitments in the Schedule must be interpreted like any other treaty text according to the rules codified in Article 31 and, to the extent appropriate, Article 32 of the Vienna

²⁹ Guidelines for the Scheduling of Specific Commitments under the General Agreement on Trade in Services (GATS), S/L/92 28 March 2001.

³⁰ Ibid [12].

³¹ Ibid [9].

³² China’s Responses 2006, above n 9, at [28]. ‘However, the issue of foreign equity participation in China’s domestic banks was, by nature, an issue of cross-border merger and acquisitions (M&A), which was beyond the scope of China’s WTO accession commitments, and therefore irrelevant for the TRM’.

³³ United States—Measures Affecting the Cross-Border Supply of Gambling and Betting Services Report of the Appellate Body, WT/DS285/AB/R, 7 April 2005, at [160].

³⁴ Vienna Convention on the Law of Treaties, done at Vienna on 23 May 1969, and entered into force on 27 January 1980. United Nations, *Treaty Series*, vol. 1155, 331. China’s accession of Vienna Convention was on 3 September 1997.

³⁵ China—Certain Measures Affecting Electronic Payment Services Report of the Panel WT/DS413/R, 16 July 2012, at [7.8].

Convention. Pursuant to Article 31, the Schedule must be interpreted in good faith in accordance with the ordinary meaning to be given to the terms when read in their context and in light of the object and purpose of the GATS and the WTO agreements.³⁶

This paper will start by examining the ordinary meaning of key terms. As dictionary definitions are generally not conclusive, it will have to examine the context of the Schedule, which includes the W/120,³⁷ the remainder of the Schedule, the provisions of covered agreements other than the GATS, the substantive provisions of the GATS and schedules of other Members.³⁸ Pursuant to Article 32 of the Vienna Convention, it will also refer to supplementary means of interpretation, including the history of negotiations, to confirm the meaning resulting from the application of Article 31.³⁹

Regarding the ordinary meaning of acquisition, the definition in the *Shorter Oxford English Dictionary* reads as follows: ‘an asset or object bought or obtained, a purchase of one company by another’. The ordinary meaning of acquisition does not appear to connect with trade in services. Reading acquisition in the context of the Schedule, W/120 and its cross-references, the CPC⁴⁰ has been used as a tool for interpretation because W/120 is part of the negotiating history of the GATS and is normally used by Members in the preparation of their GATS schedules. Examining the immediate context of the Schedule shows that China followed the W/120 structure in the Schedule, and made reference to CPC codes. Looking beyond the GATS to other covered agreements, Article 22.3(f) of the DSU provides a reference that confirms the relevance of W/120 to the task of identifying service sectors in Members’ schedules.⁴¹ Unfortunately, the context provided by the Schedule indicates that the acquisition is not a service subsector under W/120 and CPC. Thus, the main argument around this issue should not relate to deciding whether China has made commitments on the acquisition, but to deciding whether the measure is a pure activity of investment or overlaps with providing banking services in the mode of commercial presence (Mode 3).

As a supplementary means of interpretation, commercial presence clearly covers foreign investment of services, as discussed above. Moreover, Article XXVIII of the GATS clearly connects acquisition and trade in services by defining commercial presence as any type of business or professional establishment including through (i) the constitution, acquisition or maintenance of a juridical person; or (ii) the creation or maintenance of a branch or a representative office within the territory of a Member for the purpose of supplying a service. Thus, the measure limiting foreign investment

³⁶ United States—Measures Affecting the Cross-Border Supply of Gambling and Betting Services, Report of the Panel, WT/DS285/R, 10 November 2004, at [6.46].

³⁷ Services Sectoral Classification List, note by Secretariat, 10 July 1991, MTN. GNS/W/120, hereinafter W/120.

³⁸ Report of the Appellate Body, US—Gambling, above n 33, at [178].

³⁹ Report of the Panel, US—Gambling, above n 36, at [6.48].

⁴⁰ Central Product Classification, submitted to the United Nations Statistical Commission, DRAFT ESA/STAT/SER.M/77/Ver.1.1, 5–8 March 2002, hereinafter CPC.

⁴¹ Report of the Appellate Body, US—Gambling, above n 33, at [181].

on Chinese-funded banks is covered by China's commitments to banking services provided by the mode of commercial presence.

4 *Specified in a Member's Schedule*

In 7.B, Banking Services and Other Financial Services of the Schedule, China lists three types of exception—geographic coverage, clients and licensing—for Mode 3 in the limitations on market access column. However, none of these exceptions refer to the maximum percentage limitation on foreign shareholding or the total value of individual or aggregate foreign investment.

Based on the above analysis, Article 8 of the Measures setting up the 20% cap on investing in a Chinese-funded bank by a single foreign financial institution falls within the scope of individual foreign investment; enacts a maximum limitation in terms of the percentage participation of foreign capital; is covered by banking services providing in Mode 3; and was not carved out in the Schedule as a limitation on market access. Therefore, Article 8 of the Measures contains a limitation on the foreign equity participation in terms of a maximum percentage limit on foreign shareholding under Article XVI:2(f) of the GATS, and is contrary to China's commitments in its schedule.

In terms of this potential inconsistency, China argued that 'the stipulations are related to the need of prudential supervision provided for in the Annex under the GATS, the implementation of which is for the purpose of protection of investors, depositors and ensuring the integrity and stability of the financial system'.⁴² As China's banking sector is still under-developed and the effects of the international financial crisis are still being felt, China has every reason to be cautious regarding further liberalisation of the subsector.⁴³ The Annex clearly states that a Member shall not be prevented from taking measures for prudential reasons, including for the protection of investors, depositors, policy holders or persons to whom a fiduciary duty is owed by a financial service supplier, or to ensure the integrity and stability of the financial system. However, the Annex also emphasises that where such measures do not conform to the provisions of the GATS, they shall not be used as a means of avoiding the Member's commitments or obligations.

III **CONDITIONS ON LOCAL CURRENCY BUSINESS**

Regarding local currency business, China has listed geographic restrictions, client limitations and licensing qualifications in the market access column, and national treatment as the exception in its GATS obligations. Although the restrictions and limitations were indeed removed after 11 December 2006, WTO Members in 2005 began querying the situation around engaging in local currency business by branches of foreign banks. Four Members expressed concern about the issue of local currency business under the TRM, including

⁴² Trade Policy Review, above n 27, 238.

⁴³ Ibid.

Japan (2005, 2007, 2008),⁴⁴ the United States (2006, 2007, 2008),⁴⁵ Canada (2007)⁴⁶ and the European Communities (2007, 2008, 2009, 2011),⁴⁷ and four Members made inquiries under the TPR, including the European Communities (2006),⁴⁸ Japan (2008),⁴⁹ Mexico (2008)⁵⁰ and Australia (2012).⁵¹

Table 2: Commitments to Local Currency Business in China's Schedule

Sector and subsector	Limitations on market access	Limitations on national treatment
<p>7. B. Banking and Other Financial Services (excluding insurance and securities)</p> <p>Banking services as listed below:</p> <p>(a) acceptance of deposits and other repayable funds from the public</p> <p>(b) lending of all types, including consumer credit, mortgage credit, factoring and financing of commercial transaction</p> <p>(c) financial leasing</p> <p>(d) all payment and money transmission services, including credit, charge and debit cards, travellers' cheques and bankers' drafts (including import and export settlement)</p> <p>(e) guarantees and commitments</p> <p>(f) trading for own account or for account of customers: foreign exchange.</p>	<p>(3)</p> <p>A. Geographic Coverage</p> <p>For local currency business, the geographic restriction will be phased out as follows: ... Within 5 years after accession, all geographic restrictions will be removed.</p> <p>B. Clients</p> <p>For local currency business, within 2 years after accession, foreign financial institutions will be permitted to provide services to Chinese enterprises.</p> <p>Within 5 years after accession, foreign financial institutions will be permitted to provide services to all Chinese clients.</p> <p>Foreign financial institutions licensed for local currency business in one region of China may service clients in any other region that has been opened for such business.</p> <p>C. Licensing</p> <p>Qualifications for foreign financial institutions to engage in local currency business are as follows:</p> <p>– 3 years of business operation in China and being profitable for 2 consecutive years prior to the application, otherwise, none.</p>	<p>(3)</p> <p>Except for geographic restrictions and client limitations on local currency business (listed in the market access column), a foreign financial institution may do business without restrictions or the need for case-by-case approval, with foreign-invested enterprises, non-Chinese natural persons, Chinese natural persons and Chinese enterprises. Otherwise, none.</p>

⁴⁴ Committee on Trade in Financial Services, Communication from Japan, Restricted S/FIN/W/58 10 October 2007, at [7]; S/FIN/W/64 10 November 2008, at [7].

⁴⁵ Committee on Trade in Financial Services, Communication from the United States, Restricted S/FIN/W/61 29 October 2007, at [12]; S/FIN/W/68 27 November 2008, at [9].

⁴⁶ Committee on Trade in Financial Services, Communication from Canada, Restricted S/FIN/W/62 30 October 2007, at [4].

⁴⁷ Committee on Trade in Financial Services, Communication from European Communities, Restricted S/FIN/W/59 22 October 2007, at [8]; S/FIN/W/66 14 November 2008, at [4]; S/FIN/W/70 12 October 2009, at [5]; S/FIN/W/81 13 October 2011, at [7].

⁴⁸ Trade Policy Review Body, 19 and 21 April 2006, Trade Policy Review People's Republic of China Minutes of Meeting Addendum, WT/TPR/M/161/Add.1, 15 June 2006, 143.

⁴⁹ Trade Policy Review China Minutes of Meeting Addendum, WT/TPR/M/199/Add.1, above n 28, 121.

⁵⁰ *Ibid* 254.

⁵¹ Trade Policy Review China Record of the Meeting Addendum, above n 56, 29.

A 1 Million RMB Requirement for Accepting Deposits from Chinese Citizens

Article 31 of the Regulation states that branches of foreign banks in China may only accept retail deposits from Chinese citizens in excess of 1 million RMB. Regarding the 1 million RMB requirement, the United States claimed that this would be inconsistent with the Schedule after December 2006 as China committed to eliminate national treatment and market access limitations relating to geographical, client and scope of business factors within five years of its WTO accession. The GATS-consistency assessment with respect to the banking services at issue can be conducted in two steps, to determine whether China has undertaken commitments and whether China has fulfilled those commitments.

1 Whether China has Undertaken Commitments

The Schedule includes banking services of acceptance of deposits and other repayable funds from the public, so that foreign bank branches engaging in local currency business is one of banking services committed by China. The banking services of concern are provided through a bank branch (Mode 3 the commercial presence) in the territory of China.

With respect to limitations on market access under Mode 3, China made the commitment that within five years after accession, foreign financial institutions would be permitted to provide services to all Chinese clients. The issue at hand seems to be inconsistent with conditions agreed and specified in the Schedule, because all limitations were eliminated after five years of China's accession. However, the list of measures under Article XVI:2 is exhaustive⁵² and the type of clients receiving foreign services is not covered by the second paragraph of Article XVI:2. Thus, the relevant issue does not fall under Article XVI.

With respect to limitations to national treatment under Mode 3, China committed to 'none' except for geographic restrictions and client limitations on local currency business (listed in the market access column); it also made the commitment that foreign financial institutions could do business without restrictions or the need for case-by-case approval with foreign-invested enterprises, non-Chinese natural persons, Chinese natural persons and Chinese enterprises. The term 'none' is a GATS scheduling convention that means 'no limitations'—in other words, a full commitment.⁵³ The words 'none except' indicate that a Member intends to make a full commitment subject only to the

⁵² See general, the first four sub-paragraphs concern quantitative limitations on service suppliers, transactions or assets, operations or outputs, and total number of natural persons; the fifth covers measures that restrict or require specific types of legal entity or joint venture; and the sixth identifies limitations on the participation of foreign capital.

⁵³ Scheduling of Initial Commitments in Trade in Services: Explanatory Note. MTN.GNS/W/164 3 September 1993, at [24]. See also the 2001 Guidelines Schedules, above n 29, at [42].

limitation described.⁵⁴ According to the relationship between market access and national treatment, the discriminatory measures listed in the market access column also apply to national treatment. When the discriminatory measures in market access are eliminated within five years after accession, restrictions and limitations shall also be eliminated from the national treatment column. China has therefore undertaken a full national treatment for the commercial presence supply of the service at issue since December 2006.

The Schedule uses the term ‘foreign financial institution’ instead of explicitly naming foreign bank branches or exemplifying the scope of foreign financial institution. Other Members interpreted this to mean that China was committed to eliminating national treatment and market access limitations for financial institutions providing banking services, regardless of whether these institutions operated as branches or subsidiaries.⁵⁵ However, China appears to treat branches of foreign banks as legal entities separate from foreign financial institutions, as it applies more restrictive requirements to foreign bank branches than to subsidiaries. In this sense, it is necessary to decide whether foreign financial institutions are entitled to include branches of foreign banks.

Article 2 of the Regulations on Administration of Foreign-funded Financial Institutions⁵⁶ (the valid law defining foreign financial institutions before and at the time of China’s WTO accession) defines foreign financial institutions by listing five types of institution that have been approved to be established to operate within the territory of China, including branches of foreign banks. Overall, China has committed to provide full national treatment to branches of foreign banks.

2 *Whether China Has Fulfilled Commitments*

To assess whether the measure at issue is inconsistent with China’s national treatment commitments under Article XVII of the GATS, it is necessary to determine (a) whether services at issue are inscribed in the Schedule; (b) whether the measures at issue affect the supply of these services; (c) the extent of China’s national treatment commitment, including any conditions or qualifications, with respect to these services entered in its schedule; and (d) whether these measures accord less favourable treatment to service suppliers of other Members than to like domestic suppliers.⁵⁷

With respect to (a), it has already been established that the services at issue are indeed within the scope of banking services inscribed in the Schedule, and are therefore subject to any national treatment commitment that China may have

⁵⁴ Mexico—Measures Affecting Telecommunication Services Report of the Panel WT/DS204/R, 2 April 2004, at [7.75].

⁵⁵ Committee on Trade in Financial Services, Communication from the United States, Restricted S/FIN/W/68, 27 November 2008.

⁵⁶ 外资金融机构管理条例, promulgated according to the Order of the State Council No. 148 on 25 February 1994, was invalidated by the Order of the State Council No. 340 and came into force on 1 February 2002; was invalidated by the Regulation of the Administration of Foreign-funded Banks on 11 December 2006.

⁵⁷ Report of the Panel, China—Publications and Audio-visual Products, above n 28, at [7.1272].

indicated. With respect to (b), as the measure at issue directly governs the suppliers (branches of foreign banks) of the services at issue, this affects the supply of retail lending from foreign bank branches as questioned by other WTO Members under the TRM and TPR, and China has not argued otherwise. With respect to (c), China has committed to introduce or maintain limitations on national treatment for local currency business listed in the market access column. China committed to full national treatment for the services at issue as discussed above, because geographic restrictions and client limitations on local currency business in market access were eliminated within five years after the accession and China has inscribed 'otherwise, none'.

And finally, with respect to (d), while branches of foreign banks can only take RMB deposits from Chinese citizens of more than 1 million RMB, branches of non-foreign banks (including Chinese banks, wholly foreign-owned banks and joint venture banks established in the territory of China) can accept deposits of any size from Chinese citizens. This difference in treatment is based exclusively on the national origin of the service supplier; domestic and foreign suppliers under the measure at issue are like suppliers, as they are all branches of banks. Moreover, branches of foreign banks are prevented from accepting individual deposits of more than 1 million RMB from Chinese citizens, whereas domestic like service suppliers (branches of non-foreign banks) are permitted to do so. The measure at issue thus imposes a discriminatory prohibition on foreign service suppliers, which clearly modifies conditions of competition in favour of domestic suppliers. Thus, the measure at issue accords to foreign service suppliers' treatment that is less favourable than that accorded to domestic like suppliers. Overall, in the author's view, Article 31 of the Regulation, stating that branches of foreign banks in China may only accept retail deposits from Chinese citizens in excess of 1 million RMB, is in violation of Article XVII of the GATS.

B Prudential Measures

China has responded that relevant requirements for foreign-funded bank branches conducting local currency business were of a prudential nature and that Members were allowed to protect depositors' interests and maintain the soundness and stability of domestic financial systems by introducing prudential measures.⁵⁸ However, it is difficult to identify which measures are prudential and which are not, because of the lack of a definition on prudential measures or a clear distinction between prudential and non-prudential measures.

1 The Prudential Carve-out

In the WTO system, paragraph 2(a) of the Annex of the GATS only provides reasons for prudential measures by stating that:

⁵⁸ China's Response 2006, S/FIN/M/53, above n 9, at [26]; Trade Policy Review Body 21 and 23 May 2008, above n 24, 255.

Notwithstanding any other provisions of the Agreement, a Member shall not be prevented from taking measures for prudential reasons, including for the protection of investors, depositors, policy holders or persons to whom a fiduciary duty is owed by a financial service supplier, or to ensure the integrity and stability of the financial system. Where such measures do not conform with the provisions of the Agreement, they shall not be used as a means of avoiding the Member's commitments or obligations under the Agreement.

This regulation is known as the 'prudential carve-out', but it does not define prudential measures and the reasons provided are only illustrative.⁵⁹ It only provides a non-exhaustive list of prudential reasons to justify the adoption of domestic measures that may go against a Member's WTO obligations. Moreover, the Annex does not mention that any international standards or the role of international organisations may be referred to in order to determine prudential measures.

Apart from the prudential carve-out in the *Annex*, China also argued that according to the Basel Committee on Banking Supervision (BCBS), the banking sector regulators of all countries were entitled to stipulate and utilise prudential regulations to control risks to prevent banks from reckless risk-taking, as long as these regulations were intended to protect the depositors' interests, mitigate banking risks and ensure the safe and sound operation of the banking system.⁶⁰ The BCBS 'is the primary global standard-setter for the prudential regulation of banks and provides a forum for cooperation on banking supervisory matters'.⁶¹ Seeking to identify measures that could be characterised as prudential, the BCBS set forth principles relating to prudential regulations and requirements in the Core Principles for Effective Banking Supervision (September 2012 edition).

The principles include typical prudential measures such as the requirement for capital adequacy ratio, asset risk concentration and affiliate transactions. However, the BCBS documents have no legal force, and are developed and issued by the agreement of Members with an expectation that individual national authorities will implement them.⁶² For example, the Australian Prudential Regulation Authority implemented the Basel III in Australia through revisions to its Prudential Standard APS 112 Capital Adequacy: Standardized Approach to Credit Risk, which took effect on 1 January 2013.

To clarify the difference between prudential and non-prudential measures, some scholars⁶³ suggest analysing whether the real purpose of an alleged

⁵⁹ Régis Bismuth, 'Financial Sector Regulation and Financial Services Liberalisation at the Crossroads: The Relevance of International Financial Standards in WTO Law' (2010) 44:2 *Journal of World Trade* 489, 496; Also see, Éric H Leroux, 'Trade in Financial Services under the World Trade Organisation' (2002) 36:3 *Journal of World Trade* 413.

⁶⁰ Report of the Meeting Held on 27 November 2006, above n 58, at [26].

⁶¹ Basel Committee on Banking Supervision Charter, Bank for International Settlements 2013, I.1.

⁶² History of Basel Committee, Bank for International Settlement, updated 1 October 2015, <<http://www.bis.org/bcbs/history.htm>>.

⁶³ Sydney J Key, *The Doha Round and Financial Services* (American Enterprises Institute,

prudential measure is trade restrictive or prudential. The second sentence of 2(a) under the Annex appears to imply that the purpose of defining prudential measures is that they shall not be used as a means of avoiding a Member's commitments or obligations under the agreement. The WTO Secretariat also states that 'Article VI:4 and 5 may not be applicable to prudential measures; questions may remain as to whether they are based on objective and transparent criteria, or are not more burdensome than necessary'.⁶⁴

Although the objective of avoiding a Member's GATS obligations is difficult to clarify because of the absence of evidence of willingness, the situation has improved following rulings in the recent dispute *Argentina—Measures Relating to Trade in Goods and Services* (hereinafter *Argentina—Financial Services*),⁶⁵ which was the first official WTO decision to address the prudential carve-out. The panel in *Argentina—Financial Services* found that two measures setting requirements relating to reinsurance services and for access to the Argentina capital market are not justified under paragraph 2(a) of the Annex, because they were not taken for prudential reasons in the absence of a rational relationship of cause and effect between the measures and the prudential reasons.⁶⁶

Before analysing the requirements that constitute the legal standard under paragraph 2(a), the panel defined that 'it constitutes a justification for measures that are inconsistent with the GATS and is therefore in the nature of an exception'.⁶⁷ The panel also considered that 'paragraph 2(a) covers all types of measures affecting the supply of financial services and not only those measures that could be characterised as 'domestic regulations' within the meaning of Article VI of the GATS',⁶⁸ which was confirmed by the Appellate Body. The panel then set forth three requirements for examining whether measures at issue could be shielded under the prudential exceptions: that measures (1) are 'affecting the supply of financial services'; (2) were taken 'for prudential reasons'; (3) have not been used 'as a means of avoiding commitments or obligations' under the GATS.⁶⁹

Proceeding to examine 'for prudential reasons', the panel analysed the meaning of the concept 'prudential reason' and then examined what was

Washington DC, 2003) 29; Mamiko Yokoi-Arai, 'GATS Prudential Carve Out in Financial Services and Its Relation with Prudential Regulation' (2008) 57 *International and Comparative Law Quarterly* 613, 640; Joel P Trachtman, 'Addressing Regulatory Divergence through International Standards: Financial Services' in Aaditya Mattoo and Pierre Sauvé (eds.) *Domestic Regulation and Service Trade Liberalisation* (World Bank/Oxford University Press, Washington DC, 2003) 27, 30; and Régis Bismuth, above n 59, 495.

⁶⁴ Council for Trade in Services, *Financial Services*, Background Note by the Secretariat S/C/W/72, 2 December 1998, at [35].

⁶⁵ *Argentina—Measures Relating to Trade in Goods and Services* DS453, hereinafter *Argentina—Financial Services*, complainant Panama, Respondent Argentina, request for consultation on 12 December 2012, Panel report 30 September 2015, Appellate Body report 14 April 2016.

⁶⁶ *Argentina—Measures Relating to Trade in Goods and Services*, Report of the Panel, WT/DS453/R 30 September 2015, at [7.919].

⁶⁷ *Ibid* at [7.814].

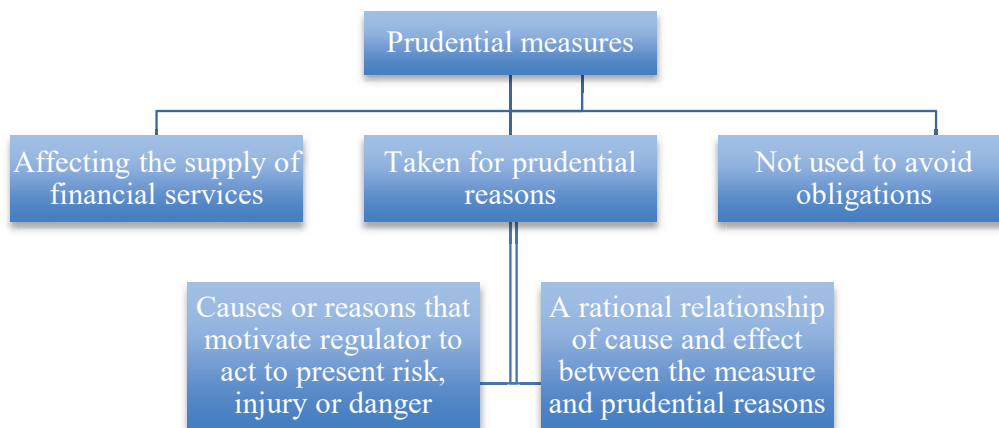
⁶⁸ *Ibid* at [7.847].

⁶⁹ *Ibid* at [7.851].

meant by a measure having been taken for prudential reasons. The panel concluded that the expression ‘prudential reasons’ referred to ‘those “causes” or “reasons” that motivate financial sector regulators to act to present a risk, injury or danger that does not necessarily have to be imminent’, and the list of reasons in paragraph 2(a) should be regarded as indicative but not exhaustive.⁷⁰ The Member who is taking the measure has the burden of proof to demonstrate whether the measure’s design, structure or architecture seek to justify under paragraph 2(a) and the prudential reason provided, which can only be determined on a case-by-case basis taking account of the particular characteristics of each situation.⁷¹

The central aspect of a rational relationship of cause and effect between the measure and prudential reasons is the adequacy of the measure with respect to the prudential reasons; that is, whether the measure contributes to achieving the desired effect.⁷² With regard to the third requirement, the panel considered it unnecessary to continue the examination because Argentina had failed to demonstrate that measures were taken for prudential reasons within the meaning of paragraph 2(a).⁷³

Figure B: Legal Standard of Prudential Carve-out



2 Assessing Measures at Issue

Based on the panel’s analysis in *Argentina–Financial Services*, this study examines whether the 1 million RMB limit in relation to foreign bank branches is a prudential measure under paragraph 2(a) of the *Annex*. The first requirement that China has to meet is that the measure at issue is one affecting the supply of financial services in accordance with paragraph 1(a) of the

⁷⁰ Ibid at [7.868] and [7.879].

⁷¹ Ibid at [7.891].

⁷² Ibid at [7.905].

⁷³ Ibid at [7.945].

Annex.⁷⁴ The measure at issue is about providing services through foreign bank branches, which refers to Mode 3—the commercial presence of Article I:2. Moreover, acceptance of deposits is specifically listed under the definitions of financial services in paragraph 5(a) of the Annex, and all services subsequently listed in paragraph 5(a) are services of a financial nature. Consequently, the measure requiring that foreign bank branches accept a minimum of 1 million RMB in any deposit by a Chinese citizen is a measure affecting the supply of financial services within the meaning of paragraph 1(a) of the Annex.

This study proceeds to examine whether China has also demonstrated that the measure at issue is a measure taken for prudential reasons. China maintained that the prudential purpose of the measure was to protect the depositors of foreign bank branches because the Chinese government was unable to supervise and control the risk arising from the parent bank of a foreign branch. In terms of the order of debt repayment, many Members prescribe that domestic depositors enjoy priority over overseas depositors, so that if the parent bank encounters liquidity risk or payment crisis, depositors at the branch in China may not be guaranteed priority in repayment.⁷⁵ Also, international coordination of bankruptcy liquidation has proved to be a tough process.⁷⁶ Many foreign banks in China are multinationals, and the Chinese government is unable to supervise and control the risk arising from the parent bank of a foreign branch, and is also unable to isolate that risk from its branch in China.⁷⁷ The above reasons identified by China for protecting depositors of foreign bank branches and controlling the risk arising from the parent bank seem to be prudential in nature and in conformity with the expression of prudential reasons in paragraph 2(a) of the Annex.

Finally, it remains to determine whether there is a rational relationship of cause and effect between the measure and these prudential reasons. In the same regulation as the concerned measure, the conditions under which China is considered to protect depositors of foreign bank branches and strengthen the supervision and control have already been laid down. Article 8 of the Regulation states that a wholly foreign-owned bank or a Chinese–foreign joint venture bank should allocate at least 200 million RMB or a freely convertible currency of the equivalent value to each of its branches as operating capital. This large amount of operating capital can be regarded as a guarantee for depositors from China. To cope with liquidity risk or a payment crisis, Article 44 requires 30% of operating capital to be interest-bearing assets allocated by the banking supervisory institution of the State Council, and Article 46 prescribes the minimum ratio of current assets and current liabilities as 25%.

Moreover, Article 9 regulates that a foreign bank that plans to establish a branch or representative office must meet the following requirements: it must (1) have the capability to make profits continuously and retain a good credit

⁷⁴ See, paragraph 1(a) of the *Annex*: Reference to the supply of a financial service in this Annex shall mean the supply of a service as defined in paragraph 2 of Article I of the Agreement.

⁷⁵ Report of the Meeting Held on 27 November 2006, above n 58, 26.

⁷⁶ Trade Policy Review China Minutes of Meeting Addendum 2008, above n 49, at 255.

⁷⁷ China's Response 2007, S/FIN/M/55, above n 10, at [50].

standing and have no record of gross violation of any law or regulation; (2) have international financial experience; (3) have an effective anti-money laundering system; (4) be under the effective supervision of the financial regulatory authority of the country or region in which it is located, and its application to establish a branch must have been approved by the financial regulatory authority; (5) meet other prudent conditions and have a perfect financial regulatory system; its financial regulatory authority must have a good mechanism for cooperation with the banking regulatory institution of the State Council. To establish a branch, a foreign bank must not only meet the requirements as described in Article 9, but also satisfy the requirements stated in Article 12: (1) its total assets must not be any less than 20 billion USD at the end of the year prior to the filing of its establishment application; and (2) its capital adequacy ratio must meet the requirements of the financial regulatory authority and the banking regulatory institution of the State Council.

The above requirements allow the financial regulatory institution to effectively supervise and control the risk arising from the parent bank of a foreign bank branch. Articles in the Regulation already performed functions like those China claimed to achieve through the measure at issue. These articles can act to present a risk, injury or danger that does not necessarily have to be imminent, without limiting the business scope of foreign service suppliers. In doing so, the Chinese supervisory agency would be able to safeguard depositors' interests as well as maintain the supervision and control of risk.

Further, the measure at issue does not directly impose specific requirements on preventing liquidity risk or a payment crisis and strengthening of the supervision of the parent foreign banks. The prudential reasons claimed by China are a side effect of the measure at issue, but the direct effect of applying the measure is to establish boundaries for foreign bank branches and then persuade foreign banks to establish local subsidiaries in China according to Chinese law and regulations. Under the TRM, China responded to other Members' concerns regarding China encouraging foreign banks to establish local subsidiary entities to transform existing branches into subsidiaries, because a locally incorporated subsidiary of a foreign bank would be subject to supervisory requirements with respect to capital adequacy, loan loss provisions, large exposures, cross-border capital flows and deposit repayment capacity.⁷⁸ It appears that the effect of the so-called prudential reason is to transform branches into local subsidiaries.

It is rational that prudential objectives can be directly achieved without any limitations on foreign services and service suppliers, but it is irrational to apply a measure having only an indirect effect to achieve a certain prudential objective when the objective can be satisfied by other measures. As the measure in question is not taken for prudential reasons, it is unnecessary to continue the examination on whether the measure has been used as a means of avoiding commitments or obligations under the GATS.

⁷⁸ Report of the Meeting Held on 27 November 2006, above n 58, at [26].

In light of the foregoing discussion, the measure at issue does not have a rational cause and effect relationship with the prudential reasons identified by China. China also claimed the 20% shareholding limitations on single foreign investment institution in Chinese-funded banks as a prudential carve-out. Similar to the 1 million RMB requirements, this measure affects the supply of financial services, but it was not designed for prudential reasons and thus does not contribute to achieving the desired effect of prudential causes.

IV TRANSPARENCY

Since China's WTO accession, other WTO Members have recognised that China has made notable improvements in transparency, 'particularly through the many notifications that it has made to the WTO's councils and committees as well as through its use of numerous official journals, other publications and the Internet to publicize new or modified trade-related laws, regulations and other measures'.⁷⁹ Nevertheless, they also concede that there remains much to be done to ensure transparency obligations committed in the Accession Protocol and the Working Party Report. Under the TRM and TPR systems, Members have expressed concerns about transparency since 2002, immediately after China's accession.

With regard to transparency in financial services, Members' concerns under the TRM can be categorised as one general expectation, two main themes and three follow-up issues. For the general expectation, from the 2006 to the 2011 TRM Japan consistently held the view that there was room for further improvement on regulatory transparency in China. The two main themes of transparency are the publication of laws, regulations and policies relating to trade and the public comment/consultation procedures on draft laws, regulations and other measures, which have been questioned by Canada (2004),⁸⁰ the United States (2006, 2007, 2008 and 2009)⁸¹ and the European Communities (2011).⁸² Specifically, Canada requested procedures or laws to promote a standardised public consultation process; the European Communities considered there still appeared to be inconsistencies with regard to the publication and provision of adequate opportunities for interested parties to comment; the United States indicated that trade-related measures issued by other ministries and agencies were not published in China's nominated official journal (the Ministry of Commerce's *MOFCOM Gazette*) and that some proposed measures only allow periods as brief as 7 or 14 days (rather than 30 days) for comment.

In addition, Members are concerned about three issues relating to transparency: vague provisions, with unspecified criteria, referring to

⁷⁹ Communication from the United States, S/FIN/W/53, above n 53, at [36].

⁸⁰ Committee on Trade in Financial Services, Communication from Canada, Restricted S/FIN/W/37 5 November 2004, at [6].

⁸¹ Communication from the United States, above n 53, S/FIN/W/53 18 October 2006, at [36–38]; S/FIN/W/61 29 October 2007, at [24] and [25]; S/FIN/W/68 27 November 2008, at [15] and [16]; S/FIN/W/72 23 October 2009, at [12] and [13].

⁸² Communication from the European Communities, above n 55, S/FIN/W/81, at [5].

unspecified laws and regulations regarding foreign-funded insurance companies (European Communities 2002); insufficient notice on revision of regulations and reporting requirements imposing undue costs and burdens (Canada 2005 and 2006); and transparency in licensing requirements and procedures. Further, WTO Members consistently query transparency under the TPR system, but these concerns relate to transparency as a general policy for all trade.

The China—Financial Information was caused by the state censorship on media, in which the government exerts strict censorship and control over the media through the Xinhua News Agency. China—Publications and Audiovisual Products also referred to limitations on media products such as reading materials, sound recordings, films for theatre release and other publications and audiovisual products in electronic and physical forms. These two disputes seem likely to be related to China's deficiencies in transparency, but the transparency obligations under the WTO are narrower than in the transparency discussed in daily life. Hence, this research first clarifies China's transparency obligations before assessing GATS-consistency.

A Transparency in the GATS and China's WTO Commitments

Transparency is a very important element in ensuring competitive markets and also a cornerstone of the multilateral trading system.⁸³ It may facilitate international trade by providing a predictable regulatory system; the less transparent the regulatory environment, the more likely that anti-competitive markets will remain.⁸⁴ The GATS recognises the importance of transparency in its Preamble and in Articles III and VI.

Paragraph 2 of the Preamble stipulates one of the GATS objectives as 'wishing to establish a multilateral framework of principles and rules for trade in services with a view to the expansion of such trade under conditions of transparency and progressive liberalisation and as a means of promoting the economic growth of all trading partners and the development of developing countries'.⁸⁵ The transparency principle under Article III requires each Member to publish all relevant legislation and international agreements affecting trade in services by the time they come into force at the latest, and to respond to all requests for specific information on any measures affecting trade in services. Accordingly, transparency encompasses the publication of laws and regulations, procedural fairness in decision-making, judicial review and the non-discrimination principle.⁸⁶ In addition, transparency is a criterion for good governance in administration and implementation, such as the

⁸³ The Fundamental WTO Principles of National Treatment, Most-Favoured Nation and Transparency, Background Note by the Secretariat WT/WGTCP/W114, 14 April 1999.

⁸⁴ Shanker Singham, *A General Theory of Trade and Competition: Trade Liberalisation and Competitive Markets* (Cameron May Publisher, London, 2007) 399.

⁸⁵ The Preamble of the GATS.

⁸⁶ Paolo D Farab, 'Five Years of China's WTO Membership: EU and US Perspectives on China's Compliance with Transparency Commitments and the Transitional Review Mechanism' (2006) 33:3 *Legal Issues of Economic Integration* 263, 268.

process of decision-making by governments and the process by which decisions are implemented.⁸⁷ The obligation under Article VI:4 provides not only the negotiating framework but also the basic principles that Members should transform into domestic disciplines.⁸⁸ It also calls upon Members to develop domestic disciplines based on the principles of necessity, transparency and equivalence.

In addition to Article III, it has been specified in the Accession Protocol that China shall publish all WTO-related laws, regulations and other measures; make drafts of all such documents available for comment for a reasonable time prior to enforcement; establish or designate an official journal to publish on a regular basis all these measures; and establish a joint enquiry to reply to requests for information relating to these measures within a certain number of days.⁸⁹ In the Working Party Report, the representative of China confirmed that China would make available to WTO Members translations into one or more of the official WTO languages (English, French and Spanish) of all relevant laws, regulations and other measures, in no case later than 90 days after the enforcement;⁹⁰ China would also publish a list of all organisations responsible for authorising, approving or regulating services activities through granting of licences or other approval, as well as the procedures and conditions for obtaining such licences or approval.⁹¹

B Problems of Transparency

Prior to China's WTO accession, some Members were concerned about the lack of transparency and the difficulty in locating and obtaining WTO-related legislation;⁹² some even identified a lack of transparency as China's main problem.⁹³ After more than 10 years of trying, the Chinese government has made noticeable progress on transparency. Foreign investment and trade-related laws and regulations have been published in an official gazette since 1993 and the Chinese government lists seven official journals that contain WTO-related information.⁹⁴ In addition, the Ministry of Foreign Trade and Economic Cooperation established three entities: the Department of WTO Affairs, the China WTO Notification and Enquiry Centre, and the Fair Trade

⁸⁷ Padideh Ala'i and Matthew D'Orsi, 'Transparency in International Economic Relations and the Role of WTO' in Padideh Ala'i and Robert G. Vaughn (eds) *Research Handbook on Transparency* (Edward Elgar Publishing Limited, 2014) 368, 369.

⁸⁸ WPPS Background Information on the Agreement on Technical Barriers to Trade and the Agreement on Import Licensing Procedures S/WPPS/W/6, 29 February 1991, at [2].

⁸⁹ *Accession of the People's Republic of China* WT/L/432, 23 November 2001, at [Part I, 2 (C)].

⁹⁰ Working Party on the Accession of China, Report of the Working Party on the Accession of China, Restricted WT/ACC/CHN/49 1 October 2001, at [334].

⁹¹ *Ibid* at [332].

⁹² *Ibid* at [324].

⁹³ Christopher Duncan, 'Out of Conformity: China's Capacity to Implement World Trade Organisation Dispute Settlement Body Decisions After Accession' 18:2 (2002) *American University International Law Review* 399, 460; Also see, Sylvia Ostry, 'China and the WTO: The Transparency Issue' (1998) 12:3 *UCLA Journal International Law & Foreign Affairs* 1.

⁹⁴ Karen Halverson, 'China's WTO Accession: Economic, Legal, and Political Implications' (2004) 27 *Boston College International and Comparative Law Review* 319, 351; Also Report of the Working Party, above n 90, at [325] and [330].

Bureau for Import and Export.⁹⁵ In 2006, China adopted a single official journal, the *MOFCOM Gazette*, administered by the Ministry of Commerce for the publication of all trade-related laws, regulations and other measures. In 2008, the Provision on the Disclosure of Government Information⁹⁶ was promulgated to establish the processes for information disclosure.⁹⁷ Currently, the Department of WTO Affairs and the China WTO Notification and Enquiry Centre operate within the Ministry of Commerce. The Ministry of Commerce has established a website⁹⁸ to disseminate information and has also organised a China/WTO website for WTO/Free Trade Agreement (FTA) consulting.⁹⁹

However, other WTO Members' concerns reveal problems with China's implementation of its transparency obligations, including publication and consultation. In 2015, the US–China Business Council indicated that transparency was consistently cited as a top concern in the annual survey on China's business environment, including the openness of government decision making, the public availability of information, and the solicitation of broad public feedback during the drafting of new laws and regulations.¹⁰⁰ In general, China's deficiencies in its transparency obligations comprise 'obligations concerning the publication and notification of relevant measures and obligations concerning the administration and application of measures'.¹⁰¹

1 Transparency on Publication and Consultation

During the negotiation of China's WTO accession, 'some Members noted the difficulty in finding and obtaining copies of regulations and other measures undertaken by various ministries' and they also suggested using 'the Internet and other means to ensure that information ... at all levels could be assembled in one place and made readily available'.¹⁰² Until now, neither a single official journal nor a website has published legal information from all legislatures at the central level. The *MOFCOM Gazette* publishes most government entities' trade-related measures, but publication is less common for measures such as

⁹⁵ 'China Establishes WTO-related Organisations' *Xinhua News Agency-CEIS* (United States, 31 October 2001).

⁹⁶ Provision on the Disclosure of Government Information, adopted at the 165th Executive Meeting of the State Council on 17 January 2007 and entered into force on 1 May 2008.

⁹⁷ As indicated in Article 1, the purpose of this regulation is to safeguard legal access to government information by citizens, legal persons and organisations, improve the transparency of government work, promote administration according to the law, and take full advantage of government information on serving, living, social and economic activities.

⁹⁸ Ministry of Commerce of the People's Republic of China Department of WTO Affairs (China WTO Notification and Inquiry Centre), <<http://www.sms.mofcom.gov.cn>>.

⁹⁹ China and WTO, <<http://www.chinawto.mofcom.gov.cn>>. 'It includes basic knowledge about the WTO, its documents and agreements, the new round of WTO negotiations, China's trade policy and information on WTO Members', see 'China to Open Official WTO Website' *Economic Review* (Shanghai, 13 September 2002).

¹⁰⁰ The US–China Business Council, 'China 2015 Regulatory Transparency Scorecard' March 2015, <<http://www.uschina.org/reports/china-2015-regulatory-transparency-scorecard>>.

¹⁰¹ Markus Krajewski, *National Regulation and Trade Liberalisation in Services: The Legal Impact of the General Agreement on Trade in Services (GATS) on National Regulatory Autonomy* (Kluwer Law International, Hague, 2003) 125.

¹⁰² Working Party Report, above n 90, at [330]

opinions, circulars, orders, directives and notices.¹⁰³ The large quantity of these departmental rules, issued by more than 60 departments and agencies of the State Council, increases the difficulty of publication and public accessibility to all.¹⁰⁴ In 2014, only 75% of regulatory documents were posted by the State Council, even though the rate of published regulations has increased 50 percentage points from 2013 and 2014.¹⁰⁵

The Legislation Law of the People's Republic of China (hereinafter the Legislative Law) and its relevant regulations¹⁰⁶ require that drafts of regulations, rules and local decrees be made available to the public and the opinions of relevant authorities, other organisations and citizens be collected, but 'many of China's ministries have not been consistent in publishing draft departmental rules for public comment'.¹⁰⁷ In the *2012 Trade Policy Review Report*, the Secretariat said, 'it would appear that not all departmental rules have been published for public comment'.¹⁰⁸ From January to December 2013, the State Council posted less than 10% of its own administrative regulations and department rules for public comment through the State Council Legislative Affairs Office (SCLAO); other government agencies did no better and only a small fraction of relevant documents were posted for comment on either the SCLAO (less than 10%) or their respective agency websites (less than 17%).¹⁰⁹ During 2014, just three of nine laws passed or amended by the National People's Council were posted for public comment.¹¹⁰

At the sub-national level, no official journal publishes local decrees and rules, and administrative practice involves the use of informal and unpublished regulatory documents.¹¹¹ According to Article I of the GATS, measures affecting trade in services include measures issued by regional or local governments and authorities. According to the Legislative Law, the local people's congress of a province, autonomous region, municipality or major city has the right to make local decrees or rules. The numerous local decrees and rules are not published in official journals and websites at the central level, and some of them may not be published on local governments' websites.

Although the Legislation Law states that local decrees and rules must be published in the bulletin and newspaper,¹¹² local decrees only sporadically appear on the websites of local governments. It is difficult to locate local

¹⁰³ United States Trade Representative '2012 Report to Congress on China's WTO Compliance' December 2012, 11.

¹⁰⁴ Sijie Chen, 'China's Compliance with WTO Transparency Requirement: Institution-Related Impediments' (2012) 4:4 *Amsterdam Law Forum* 25, 42 and 43.

¹⁰⁵ The US-China Business Council, above n 100.

¹⁰⁶ Trade Policy Review Body, Trade Policy Review Report by the Secretariat China Restricted WT/TPR/S/264, 8 May 2012, at [11]. The Regulations on Procedures for Formation of Administrative Regulations (State Council Decree 321), and the Regulation on Procedures for Formation of *Departmental Rules* (State Council Decree 322).

¹⁰⁷ United States Trade Representative, above n 103, at [11].

¹⁰⁸ Trade Policy Report, above n 106, at [12].

¹⁰⁹ The US-China Business Council, 'China 2014 Regulatory Transparency Scorecard' March 2014.

¹¹⁰ The US-China Business Council, above n 100.

¹¹¹ Christopher Duncan, above n 93, at 464.

¹¹² Article 70, *Legislative Law*.

decrees and rules relating to the services trade, and virtually impossible for anyone to know exactly which rules apply.¹¹³ For example, the website of the China Legislative Information Network System¹¹⁴ mainly publishes the central government's trade-related legislation and the website 'China Trade in Services'¹¹⁵ publishes laws, regulations and departmental rules relating to trade in services; however, most local decrees and draft measures for comment are not published on websites. Moreover, legislative and administrative action at the local level still operates with limited supervision from the central government, which creates virtually no transparency.¹¹⁶ Administrative interference and improper administrative action persist and is usually used to achieve local protectionism and revenue policy.

At both the central and local levels, most legislation is only published in Chinese. This may compromise China's transparency obligations under the Working Party Report in which China promised to make available all measures pertaining to or affecting trade in goods or services, intellectual property, or foreign exchange control in one or more of the official WTO languages no more than 90 days following implementation.¹¹⁷ Although the English editions of laws and some regulations can be found, most newly published regulations and local rules relating to trade in services are published only in Chinese. As the legislation adopts professional and technical terminology in Chinese characters, it is difficult for foreign services suppliers to understand them well. Chinese lawyers can undertake bilingual consulting for foreign investors, but this may increase cost and ambiguity because different lawyers may have different understandings. Further, a lawyer's translation can only be used as a reference; it has no legal effect. Even though it is important to make translations of legislation available to WTO Members before measures are implemented or enforced, China has not yet established the infrastructure to produce translations of trade-related measures.¹¹⁸

Regarding the reasonable period for comments before implementing measures, Article 37 of the Legislative Law legalised a 30-day public comment period, but only for bills on the agenda of the session of the Standing Committee. For other laws, regulations and measures promulgated by other legislative bodies, the 30-day reasonable period is just a soft law: the *Interim Measures on Solicitation of Public Comments on Draft Law and Regulations* states that draft regulations would generally be released for public comment for no less than 30 days.¹¹⁹

¹¹³ Ranall Peerenboom, 'Ruling the Country in Accordance with Law-Reflection on the Rule and Role of Law in Contemporary China' (1999) 3:11 *Cultural Dynamics* 315, 327.

¹¹⁴ Legal Affair Office of the State Council <<http://www.chinalaw.gov.cn>>.

¹¹⁵ Ministry of Commerce <<http://tradeinservices.mofcom.gov.cn/index.shtml>>.

¹¹⁶ Sylvia Ostry, above n 93, at 13.

¹¹⁷ Donald C. Clarke, 'China's Legal System and the WTO: Prospects for Compliance' (2003) 2:97 *Washington University Global Studies Law Review* 97, 113. Also See, Working Party Report, above n 90, at [334].

¹¹⁸ United States Trade Representative, above n 103, at 11.

¹¹⁹ Article 6 of the *Interim Measures on Solicitation of Public Comments on Draft Law and Regulations* 法律法规草案公开征集意见暂行办法, promulgated by the State Council on 29 March 2007, and revised on 30 January 2008 and 22 July 2011.

In 2008, 2011 and 2012, the State Council of China pledged during bilateral dialogues with the United States to release drafts of all economic and trade-related administrative regulations and departmental rules for at least a 30-day public comment period.¹²⁰ During 2014, only 37.3% of broad regulatory documents posted to other government agencies' websites were posted for at least 30 days, and these documents had an average comment period of fewer than 20 days.¹²¹ The Organisation for Economic Co-operation and Development (OECD) made comments regarding China that public participation in policy formulation was 'informing the public rather than collecting opinions for improving policy making'.¹²²

2 *Transparency on Administration and Implementation*

The requirements of transparency, due process and efficiency for the implementation of domestic regulations are regulated as the procedural rules under Articles VI:2 and 3 of the GATS. Transparency under Article VI is not about publication and comments to measures affecting trade in services under Article III, but is about objective and impartial procedures for administrative decisions and the provision of information at the request of an affected service supplier. Article VI also requires administration relating to trade in services to be in accordance with due process and efficiency standards. Due process 'calls for procedural justice in the national jurisdiction of all Members, and thus creates a procedurally levelled playing field with respect to domestic administrative law provisions tracking trade in services'.¹²³

The efficiency standards require authorities to complete the consideration and to inform the applicant within a reasonable period of time. In the Working Party Report, China also committed that it would publish a list of all organisations granting licence or other approval, procedures and the conditions for obtaining such licences or approval. Transparency under Article VI permits markets to function effectively and reduces the opportunity for officials to engage in trade-distorting practices behind closed doors.¹²⁴

Other WTO Members also expressed concerns about transparency in licensing, approval requirements, procedures and timelines under the TRM and TPR. The 2014 Trade Policy Review Report on China also indicated that 'many aspects of China's trade and investment policy regime remain complex and opaque, leaving scope for administrative discretion and corruption'.¹²⁵ Specifically, problems of transparency in administration manifest in three ways: unpublished internal notices; reference to unspecified laws and regulations; and lack of efficiency caused by vague procedures.

¹²⁰ The US–China Business Council, above n 100.

¹²¹ The US–China Business Council, above n 100.

¹²² Ibid at [14], see also OECD 2010-B-Producer Support Estimate (PSE) and Related Indicators by Country.

¹²³ Panagiotis Delimatsis, *International Trade in Services and Domestic Regulations: Necessity, Transparency and Regulatory Diversity* (Oxford University Press, Oxford, 2007) 109.

¹²⁴ United States Trade Representative, above n 103, 11.

¹²⁵ Trade Policy Review Body WT/TPR/S/264, II Trade Policy Regime: Framework and Objective (1) Institutional and Legal Framework (i) at [4].

The Legislative Law stipulates that ministries, commissions, the PBC, auditing agencies and a body directly under the State Council have the right to enact administrative rules within the scope of their authority, to regulate matters that concern implementing laws and administrative regulations.¹²⁶ It also authorises the government of a province, autonomous region, municipality or major city to enact local rules to implement laws, administrative regulations or local decrees.¹²⁷ For these legislative bodies, lack of transparency resulting from unpublished internal notices is not a new issue; it has been discussed by scholars since China's WTO accession.¹²⁸ Internal notices are known as the normative documents that have the general binding force of legislation. They are adopted extensively by administrative bodies, especially at the local level, and encompass many forms, such as decisions, notices and provisions.¹²⁹ As normative documents are not publicly available, they make governments' decisions impossible to comprehend, especially in the administration of licensing or approval.¹³⁰ However, the publication requirements outlined in the Legislation Law do not apply to normative documents, as they are not regulated in the Legislation Law or other relevant laws.¹³¹

China's laws and regulations regarding licensing or approval requirements commonly apply 'and other relevant regulations' as the supplementary requirements at the end of articles. This creates loopholes enabling the Chinese government to enact unknown requirements for administrative decisions. In the Regulation, eight articles (Articles 9, 14, 17, 20, 27, 29, 31 and 34) refer to unspecified laws and regulations. For example, regarding the requirements of a shareholder planning to establish a foreign-funded bank, Article 9 lists four detailed requirements along with a fifth item stating other prudent conditions as prescribed by the banking regulatory institution of the State Council.

With regard to due process and efficiency, concerns remain in lengthy approval procedures and ambiguity in the application processes. In the Rules for Implementation, the timeline for the CBRC to decide has been stipulated in some licensing applications but not all. For example, to establish a branch by a wholly foreign-owned bank or joint venture bank, Article 15 of the Rules for Implementation only requires the banking regulatory bureau of the location

¹²⁶ Article 71, Legislative Law.

¹²⁷ Article 73, Legislative Law.

¹²⁸ Sarah Biddulph, 'Through A Glass Darkly: China, Transparency and the WTO' (2001) 3:1 *Australia Journal of Asian Law* 59; Ljiljana Biukovic, 'Selective Adaptation of WTO Transparency Norms and Local Practices in China and Japan' (2008) 11:4 *Journal of International Economic Law* 803; Paolo Davide Farah, 'Five Years of China WTO Membership: EU and US Perspectives about China's Compliance with Transparency Commitments and the Transitional Review Mechanism' (2006) 33:3 *Legal Issues of Economic Integration* 263; Hubert Bazin, 'Transparency and National Treatment under the Chinese Flag: A Lawyer's View of the Decade of WTO Membership and Legal Reforms' (2012) 1 *China Perspectives* 79; Thomas E Volper, 'TRIPS Enforcement in China: A Case For Judicial Transparency' (2007) 33:1 *Brooklyn Journal of International Law* 309.

¹²⁹ Sijie Chen, above n 93, 44.

¹³⁰ Tobias Bender, 'How to Cope with China's (Alleged) Failure to Implement the TRIPS Obligations on Enforcement' 9:2 (2006) *The Journal of World Intellectual Property* 230, 235; also see, Sijie Chen, above n 104, 44.

¹³¹ *Ibid* 46.

where the branch to be established to submit its examination opinions to the CBRC within 20 days, but does not regulate how long it will take for the CBRC to decide. The lack of timeline for establishing a branch reflects China's standpoint of encouraging the establishment of locally incorporated subsidiaries of foreign banks instead of branches, which reverberates the issue of the 1 million RMB minimum deposit requirement from Chinese citizens as discussed above.

In general, regulatory transparency is an important step to help China achieve its economic and trade goals of being a major global economy and playing a leading role in setting global trade policy. Lack of transparency may destroy the chances of creating a predictable policy environment and the confidence of global investors, thereby negatively affecting China's ability to achieve its goals.

V CONCLUSIONS

To identify potential inconsistencies, this paper reviewed all issues related to China's financial services under the TRM and TPR. The review of questions under the TRM and TPR reveals several ever-present concerns of other Members, including the 25% share limitation on multiple foreign financial institutions in a Chinese financial institution; the 20% share limitation on a single foreign financial institution in a Chinese financial institution; the 1 million RMB limitation on foreign banks' local currency business; and the lack of transparency in publication, consultation, administration and implementation. To examine the GATS-consistency of these questions, this research applied the general rules of treaty interpretation to relevant terms; assessed the domestic measures being challenged; interpreted the GATS provisions for market access, national treatment and domestic regulation; and examined the facts behind the concerns raised through the application of legal standards. Moreover, the preliminary analysis, selective method, comparative method and hermeneutic, explanatory, deduction and analogy approaches were employed to achieve the research purpose. As a result, this paper finds that the 25% cap on shareholding by multiple foreign financial institutions is not a violation of China's commitment to eliminate restrictions on ownership.

However, other concerns are inconsistent with China's WTO obligations. The 20% cap on shareholding in a Chinese-funded bank by a single foreign financial institution represents a limitation on foreign equity participation in terms of regulating the maximum percentage limit to foreign shareholding under Article XVI:2(f) of the GATS and is contrary to China's commitments in its Schedule. The 1 million RMB minimum for foreign banks' local currency business is in violation of Article XVII of the GATS because the measure imposes a discriminatory prohibition on foreign service suppliers, clearly modifies conditions of competition in favour of domestic suppliers, and accords to foreign service suppliers treatment less favourable than that accorded to like domestic suppliers. Regarding these limitations, China has claimed that the relevant requirements are of a prudential nature.

This research recognises that these measures only have an indirect effect on achieving a certain prudential objective when the objective can be reached by other measures, so that measures at issue do not have a rational relationship of cause and effect with the prudential reasons. Further, China still has not complied with its transparency obligations under the Accession Protocol and Working Party Report in terms of the following: publication is insufficient for measures promulgated by departments and local governments; most legislation is only published in Chinese and not in other official WTO languages; regulatory documents are not posted for consultation for a certain period of time; and there is a lack of transparency on licensing and approval requirements, procedures and timelines.

China's compliance with the GATS in financial services is significant not only for the Chinese government, but also for other Members who already have or want to have close trade relations with China. GATS-inconsistencies may impede foreign investment in financial services and impede China's trade relationship with other Members. It may also interfere with opening up the service market and thereby hold back overall development. Moreover, GATS-inconsistencies may lead to WTO disputes against China, with related costs. Becoming involved in a dispute may cost considerable time, effort and money. There are also opportunity costs in terms of other tasks not carried out. An imponderable cost is national reputation, if a WTO dispute settlement proceeding finds against a defendant WTO Member.¹³² More to the point, inconsistent measures may lead to the chilling of foreign efforts to supply services to China because of the unwarranted expenses or difficulties in doing business.

For service suppliers from other WTO Members, this research may provide a better understanding of China's legal situation affecting financial services, allowing them to predict the difficulties and extra expense of providing services in the territory of China. If service suppliers agree with the identified inconsistent measures, they could estimate economic benefits and undertake the additional legal research necessary to convince their governments to pursue a case.

¹³² Digby Gascoine, 'WTO Dispute Settlement: Lessons Learned from the Salmon Case' (Conference on International Trade Education and Research, Managing Globalization for Prosperity, Melbourne, 26 and 27 October 2005).