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**COMMUNICATION FROM THE UNITED STATES**

Transitional Review Mechanism Pursuant to Paragraph 18 of the Protocol of Accession of the People's Republic of China ("China")

The following communication, dated 16 October 2006, from the delegation of the United States is being circulated to the Members of the Committee on Trade in Financial Services.

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Questions from the United States to China concerning Financial Services

## I. INSURANCE SERVICES

1. The United States understands that insurance companies operating in China at the time of WTO accession may, but are not required to, continue to operate under the conditions existing, and pursuant to the approvals granted, prior to more recently issued regulations and implementing rules, including with regard to form of establishment, operations, financial structure and capital. Is that correct? If not, please explain how any divergence from this policy would be consistent with China's WTO obligations?

2. The United States notes that China's commitments for non-life insurance provide companies the freedom of choice to establish as branches, subsidiaries or joint ventures. The United States believes that all such companies should have the same rights of internal expansion (additional branches or sub-branches) in China, irrespective of their initial form of establishment. We are concerned that China may be somehow viewing the initial branch structure differently than a company established as a subsidiary.

3. Some insurance companies that initially established as a branch may be interested in converting such branch to a subsidiary. However, such companies have been encountering long delays while the China Insurance Regulatory Commission (CIRC) and other Chinese government agencies review their conversion applications. Without these approvals, such insurers cannot expand internally. CIRC's own regulations (the Notice Concerning Issues Relating to Conversion, issued in December 2005) require the CIRC approval process to be completed within two months of receiving a formal request.

(a) Why is CIRC not adhering to its own regulations, including the two-month time frame for approving conversion applications?

(b) Please explain CIRC's plans to work with other agencies to expedite the conversion approval process.

4. The United States understands that China will allow non-life insurers already established in China (whether as a branch or otherwise) to open branches and sub-branches even if they do not first establish as a subsidiary. Is that correct? Are there any limitations on this right? If so, please explain how China justifies this treatment in light of China's WTO commitments.

5. The United States remains concerned that China appears to grant internal expansion (branch and sub-branch) approvals for foreign insurers consecutively (meaning one at a time) rather than concurrently (meaning more than one at a time), while established and start-up Chinese insurers are able to receive concurrent approvals to open multiple branches and sub-branches. Please explain how China justifies this treatment in light of China's WTO national treatment commitments.

6. The United States understands that for foreign insurance providers, China requires RMB 200 million registered capital for initial establishment either as a branch or subsidiary. It is also our understanding that for those companies that have chosen to establish as a branch, China requires RMB 200 million in registered capital for each additional sub-branch, and, for those companies that have established as a subsidiary, China requires an additional RMB 20 million in registered capital for each location (or branch) of that subsidiary until total registered capital for the company reaches RMB 500 million.

(a) What is the prudential basis for these capitalization requirements?

(b) Please explain why it would not be possible for CIRC to rely on the financial reserves of the parent company in the case of firms establishing as a branch, and of the initial subsidiary in the case of firms establishing as a subsidiary.

(c) Please provide information on any plans to remove or modify these capitalization requirements.

7. Companies supplying non-life insurance have reported problems obtaining approval to introduce certain products, for example, political risk insurance. This had led some to observe that CIRC has delayed approving such applications because it wants to provide a competitive edge to a state-owned company that is already providing such products. Please explain how China justifies this inaction in light of its WTO commitments, including those on national treatment.

8. With regard to the reinsurance sector, the United States is concerned that the 2005 Regulations on the Administration of Insurance Business give domestically admitted reinsurers a right of first bid for 50 per cent of a foreign direct insurance company's reinsurance business. These regulations also seem to place limitations on the ability of a foreign direct insurer to cede insurance to a parent or affiliate company. The United States notes that China agreed as part of its WTO accession commitments to phase out limitations applying to the reinsurance sector. We understand that China's position is that these regulations do not impose a requirement that direct insurance companies have their business reinsured in China, do not restrict cross-border reinsurance service, and will not have any substantial impact on the reinsurance business conducted by foreign insurance companies within China. Is that correct? If not, please explain how China plans to implement these regulations in a manner consistent with China's WTO obligations.

9. There are reports that the Chinese government is considering injecting additional capital into the China Reinsurance Company as part of a broader effort to improve its competitiveness against international reinsurers.

(a) Please describe China's plans in this area. In addition, please specify the operations of China Reinsurance which would receive this additional capital. The United States understands that China Reinsurance is a holding company with at least three subsidiaries.

(b) Please explain how implementing this capital infusion would be consistent with China's WTO obligations, including those relating to national treatment.

10. CIRC recently issued the *Measures on Administration of Chinese Representative Offices of Foreign Insurance Institutions*. Article 18 of that measure imposes a number of onerous requirements on general and chief representatives. These representatives are required to be principally stationed at their offices, to spend a minimum of 240 days in China, not to absent themselves from China for more than 30 days at a time, and to submit a report to CIRC and designate a substitute whenever they are absent for more than 14 days. These requirements seem to go beyond what is needed for prudential reasons. What is China's rationale for these requirements?

11. CIRC's *Provisional Measures on the Administration of the Overseas Utilization of Insurance Foreign Exchange Funds*, issued in August 2004, establish a qualifying threshold (e.g., total assets of RMB 5 billion) for insurers to be able to invest their foreign exchange funds in overseas funds or equities. Even though this limitation applies to both domestic and foreign insurers, in practice, only the very largest insurers, i.e., domestic companies, will have the level of assets necessary to qualify for such treatment unless, as we have requested, CIRC recognizes the assets of the parent foreign insurer when determining the asset level of a foreign-invested insurer. Please justify this differential treatment in light of China's WTO commitments.

12. In June 2005, CIRC announced that local insurance companies would be allowed to invest their foreign currency in stocks listed on exchanges of "mature" markets overseas. Initially, insurance companies would only be allowed to invest in Chinese companies listed abroad, but this restriction could be relaxed later, according to regulators. Insurers would be required to cap investments in overseas shares at 10 per cent of the total foreign-exchange investment quota already allotted by regulators. Insurers must also limit their investments in a single company to 5 per cent of its total stock.

(a) Does this rule apply only to wholly-Chinese owned companies? If so, why?

(b) If foreign-invested insurers have foreign exchange assets, may they invest similarly? If not, please justify the differential treatment in light of China's WTO commitments.

(c) China has announced plans for reviewing its policies regarding overseas investments. Does China plan to relax its cap on investment in overseas shares? Does China plan to allow investments in companies other than Chinese companies listed abroad?

(d) Does China plan to still limit investments in a single company to 5 percent of its total stock?

13. Pursuant to Article 8 of CIRC's *Interim Regulations for Insurance Assets Management Companies*, which because effective on 1 June 2004, only insurers that have held licenses for more than 8 years are permitted to apply to establish and insurance asset management company. It appears that this provision applies only to insurers that have been operating in China for those 8 years, which would exclude all foreign insurers entering China's market since China's WTO accession. China has previously stated that this limitation applies to both domestic and foreign insurers. Nevertheless, given the disproportionate impact of this limitation on foreign insurers, please justify this differential treatment in light of China's WTO national treatment commitments.

14. Could China please clarify its views on whether foreign insurance companies would in any circumstances be required to outsource asset management to local asset management companies? Could China also clarify whether a decision not to outsource might affect insurance companies' choice of investment options?

15. In December 2004, CIRC allowed foreign companies to provide comments on the proposed revisions to the Insurance Law. Please report on the status of CIRC's review of the Insurance Law and plans for implementation of any revisions.

## II. BANKING AND RELATED SERVICES

16. In the Services Schedule accompanying its Protocol of Accession, China committed to phase out geographical, client (including for local currency business) and scope of business limitations for foreign financial institutions providing banking services within five years after its accession, or by 11 December 2006.

(a) What is the view of the Chinese Government regarding the recent proposal by the China Banking Reform Commission (CBRC) that would require foreign banks to incorporate in order to enter the retail RMB business? If China is considering enacting this proposal, please explain how this would be consistent with China's Services Schedule after 11 December 2006.

(b) We understand that China is considering establishing a deposit insurance system. Can you update us on the status of this effort and on how foreign bank branches would participate? Please confirm that in any case foreign banks would still be able to take uninsured deposits. We also understand that in current draft banking regulations deposits under RMB 1 million are defined as retail deposits. This amount seems unusually large, relative to both China's deposit structure and what we understand to be the level being considered for coverage by the deposit insurance system (i.e., RMB 100,000). We would like to know if there are plans to review this definition of retail deposit.

(c) Please also clarify how the CBRC proposal mentioned above would affect retail lending from foreign branches and how that would be consistent with China's Services Schedule after December 2006?

17. At last year's transitional review before this Committee, China stated "that in general there was no limitation on the share of foreign banks in financial institutions." However, it is widely understood that China currently maintains a policy limiting the equity share of a single foreign investor in a Chinese-foreign joint venture bank to 20 per cent, with the proviso that the equity share of the total foreign investment be lower than 25 per cent. China further limits this type of investment to no more than two existing state-owned companies for any given investor.

(a) Could China clarify this policy and cite examples of acquisitions in excess of the limits described above?

(b) Please provide the basis under Chinese law for this policy.

(c) How does China reconcile this policy with the fact that, under the banking services section in the Services Schedule accompanying its Protocol of Accession, China committed that qualified foreign financial institutions would be permitted to establish Chinese-foreign joint banks, and China did not schedule any limitation on the percentage of foreign ownership in these banks?

18. The United States appreciates the responses provided at last year's transitional review of China before this Committee with regard to China's capital requirements for establishing commercial banks in China. The United States continues to be concerned, however, because China imposes additional capital requirements on internal branches, on a branch-by-branch basis, that are extremely high.

(a) What is the rationale for having such high capital requirements for internal branches of existing banks?

(b) What is the status of the review of these capital requirements by CBRC?

19. In the Services Schedule accompanying its Protocol of Accession, China committed to lift by 11 December 2006 any remaining non-prudential measures restricting ownership, operation and juridical form of foreign financial institutions, including with regard to internal branching and licenses. What preparations has China made for the removal of remaining non-prudential measures?

20. In the Services Schedule accompanying its Protocol of Accession, China committed to allow unrestricted market access and national treatment for "payments and money transmission services, including credit, charge, and debit cards," with this commitment becoming effective with regard to the RMB business of retail clients no later than 11 December 2006. China also committed to allow unrestricted market access and national treatment for "advisory, intermediation, and other auxiliary financial services" for other financial services listed in its schedule, including payments. China's Services Schedule further provides for open market access for the "provision and transfer of financial information, and financial data processing ... by supplier[s] of other financial services." Nonetheless, certain officials at the People's Bank of China (PBOC) have stated that they support the proposal that China Union Pay be designated as a monopoly provider of electronic payment services for Chinese consumers, and that no other electronic payment providers be able to enter this market.

(a) What is the view of the Chinese Government regarding this proposal? If China is considering enacting this proposal, please explain how this would be consistent with China's Services Schedule after 11 December 2006.

(b) Please explain the steps that China is taking to ensure that all its commitments in the electronic payments and related sectors are met. For example, how will China ensure that international electronic payment providers can process domestic electronic payment transactions in China?

(c) How will China ensure that foreign financial institutions can issue the payment cards of their choice (whether Chinese-, foreign- or co-branded) for domestic transactions?

(d) How will China ensure that financial institutions are able to issue foreign electronic payment cards for international transactions?

21. The United States understands that China is considering requiring all financial institutions that issue electronic payments cards to adopt the Bank Identification Number (BIN) format of China Union Pay on all cards. However, if mandated, this requirement would have the effect of forcing other brands of payments cards out of the market, including the dual-brand, dual currency cards that are currently issued in China. Please explain how a requirement that foreign financial institutions adopt the CUP BIN format would satisfy China's WTO obligations.

## III. SECURITIES AND RELATED SERVICES

22. China made commitments in the Services Schedule accompanying its Protocol of Accession with regard to advisory, intermediation and other auxiliary financial services without scheduling any limitations on foreign ownership. Taking into account that these commitments include credit reference and analysis, investment and portfolio research and advice, and advice on acquisitions and on corporate restructuring and strategy, please explain how China justifies proposing a 49-percent foreign equity cap for credit rating agencies.

23. The China Securities Review Commission (CSRC) has reportedly imposed an informal moratorium on sales of existing state-owned securities companies to foreign entities. However, while China made commitments in the Services Schedule accompanying its Protocol of Accession with regard to securities services, it did not schedule any national treatment limitations. Please explain the nature of this moratorium, whether it is consistent with China's WTO obligations and China's plans for ending the moratorium.

24. In mid-September, the CSRC announced that it was imposing an official moratorium on providing new securities licenses, including for foreign joint ventures. Please advise when this moratorium will be lifted, since its imposition effectively denies foreign entry into the securities industry.

25. Does China have any plans for bringing its capital requirements for fund management companies into line with those found in other WTO Members? Please explain.

26. Please describe CSRC's policy with regard to circulating proposed measures and providing opportunities for public comment. Please also explain how CSRC coordinates with other Chinese regulators when proposed measures involve more than one regulator, as is the case with qualified domestic institutional investor (QDII) rules.

27. China's new rules governing mergers and acquisitions (M&A) provide some much needed clarity on the procedures to be followed when foreign firms enter into M&A transactions. However, these rules have also raised concerns. For example, there are broad review criteria, such as national economic security and potential loss of control over local brand names, which can be used to decide whether a merger or acquisition should be approved. Can China explain how these new review criteria will be used?

28. Earlier this year, China announced the launch of a QDII program permitting commercial banks to pool RMB from domestic institutional and individual investors into foreign exchange for investment overseas. When does China plan to implement similar rules for securities firms?

29. The United States urges China to increase the permitted share of foreign investment in asset management companies beyond 49 percent. Could China please inform us of any such plans?

30. The United States urges China to increase the permitted share of foreign investment in brokerage companies beyond 33 percent and allow these foreign-invested companies to trade in "A Shares". Could China please explain whether it has any such plans?

31. Is China considering permitting securities firms to engage in the domestic derivatives markets to the same extent as banks? If so, what is China's timetable? If not, why not?

## IV. FINANCIAL INFORMATION SERVICES

32. As the United States explained in questions that it submitted in connection with last year's transitional review before this Committee, in paragraph 309 of the Working Party Report accompanying its Protocol of Accession, China committed that "for the services included in China's Schedule of Specific Commitments, relevant regulatory authorities would be separate from, and not accountable to, any service suppliers they regulated, except for courier and railway transportation services." One of the services addressed in the Services Schedule accompanying China's Protocol of Accession is the "provision and transfer of financial information, and financial data processing and related software by suppliers of other financial services." Nevertheless, Xinhua is both a major market competitor of, and the regulator of, foreign financial information service providers in China. The United States re-submits the following questions, to which China did not respond at last year's transitional review before this Committee:

(a) When will China implement this commitment and create an independent regulator in the financial information services sector?

(b) Has China considered modelling an independent regulator in this sector after CIRC, CBRC or CSRC?

33. On 10 September 2006, Xinhua issued the *Administrative Measures on News and Information Release by Foreign News Agencies within China*. This measure abolished the *Measures for Administering the Release of Economic Information in China by Foreign News Agencies and Their Information Subsidiaries*, which had been issued on 15 April 1996. Among other things, under the 2006 measure, Xinhua now precludes foreign providers of financial information services from contracting directly with or providing financial information services directly to domestic Chinese clients. Instead, foreign financial information service providers must now operate through a Xinhua-designated agent. The one agent designated to date is a Xinhua affiliate. These new restrictions do not apply to domestic financial information service providers and, in addition, contrast with the rights previously enjoyed by foreign information service providers since the issuance of the 1996 measure, well before China's accession to the WTO on 11 December 2001. Under the 1996 measure, foreign information service providers had the right to contract directly with and provide financial information services directly to domestic Chinese clients, subject to an application and approval process administered by Xinhua.

(a) Please explain how China justifies the 2006 measure's restrictions on the market access of foreign financial information service providers in light of China's commitment to remove market access limitations relating to the "provision and transfer of financial information, and financial data processing and related software by suppliers of other financial services" upon China's accession to the WTO.

(b) Please explain how China justifies the 2006 measure's imposition of restrictions on the market access of foreign but not domestic financial information service providers in light of China's commitment to remove national treatment limitations relating to the "provision and transfer of financial information, and financial data processing and related software by suppliers of other financial services" upon China's accession to the WTO.

(c) Please explain how China justifies the 2006 measure's new restrictions on market access and national treatment in light pf the horizontal "acquired rights" commitment that China made in the Services Schedule accompanying its Protocol of Accession.

(d) Is China currently enforcing the 2006 measure, or is it necessary for implementing rules to be issued before the 2006 measure can be enforced? Please explain.

## V. PENSIONS

34. Please provide further details on the application and approval processes for "enterprise annuities." In order to offer pension annuities services, banks, securities firms, asset management companies and insurers must apply with their appropriate sectoral regulator (CSRC, CBRC and CIRC) as well as with the Ministry of Labor and Social Security (MOLSS). Please describe how China will maintain a level playing field among banks, securities firms, asset management companies and insurers in the application and approval process, given that an applicant must first secure approval from its appropriate financial services regulatory body before securing approval from MOLSS.

35. Please report on the current licensing of companies to offer enterprise annuities services, including numbers of domestic and foreign companies applying and licensed to offer these services.

## VI. TRANSPARENCY

36. In China's Protocol of Accession and accompanying Working Party Report, Members recognized the overriding importance of transparency through a host of provisions. Since China's accession, China has made notable improvements in the transparency of its trade regime, 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. Nevertheless, there remains much to be done to further improve transparency in China, as China itself has acknowledged. Transparency is a critically important area, both from a governmental perspective and from a business perspective.

37. In Section 2(C) of its Protocol of Accession, China specifically committed to establish or designate an official journal dedicated to the publication of all trade related measures, including, *inter alia*, "all laws, regulations and other measures pertaining to or affecting trade in ... services." The term "laws, regulations and other measures" is defined broadly as "laws, regulations and other measures of the central government as well as local regulations, rules and other measures issued or applied at the sub-national level."

38. During past transitional reviews, China has stated that its official journal was the "China Foreign Trade and Economic Cooperation Gazette," now published by MOFCOM and known as the MOFCOM Gazette. Until March 2006, however, only trade-related measures issued by MOFCOM, either on its own or jointly with other ministries or agencies, were published in the MOFCOM Gazette; trade-related measures issued by other ministries and agencies were not published in the MOFCOM Gazette. In March 2006, China's State Council issued a notice directing all central, provincial and local government entities to begin sending copies of all of their trade related measures to MOFCOM for immediate publication in its Gazette.

(a) Please provide an update on the progress being made by central, provincial and local government entities in fulfilling the State Council's directive to send measures pertaining to or affecting trade in financial services to MOFCOM for publication in the MOFCOM Gazette. As part of that update, please identify the government entities that regularly send their services measures to MOFCOM for publication in the MOFCOM Gazette. Please also describe the types of financial services measures (e.g., laws, regulations, rules, measures, notices, decisions, etc.) regularly being sent to MOFCOM for publication in the MOFCOM Gazette.

(b) With regard to measures pertaining to or affecting trade in financial services, please describe any progress that China has made during the past year in implementing the commitment that it made in Section 2(C) of its Protocol of Accession to provide a reasonable period for public comment on new or modified measures before implementing them, except in certain specified instances.