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TRANSATLANTIC BUSINESS COUNCIL

January 14, 2013

RE: EU and U.S. call for input on regulatory issues for possible future trade agreement; sector-specific submission on financial services

Dear Sir/Madam:

The Transatlantic Business Council is pleased to submit suggestions on financial services in a potential agreement between the EU and the U.S. to liberalize trade, investment and services.

Should you have any questions, please contact the TBC Secretariat.

With kind regards,

TBC Secretariat

The Transatlantic Business Council supports a deeper integration of the EU and U.S. economies through trade, investment and regulatory cooperation. We support the ongoing effort on both sides to identify those issue areas in which further cooperation would bring substantial gains to both sides.

Financial services is such an issue area and should be part of negotiations going forward that involve traditional trade and investment provisions pertaining to the General Agreement on Trade in Services, horizontal issues that are of general importance to a broad range of industrial or services providers and regulatory issues which might have market access implications. The latter is of particular importance in order to avoid regulatory fragmentation of EU and U.S. financial services markets, which would frustrate efforts of international bodies such as the Financial Stability Board that have been charged by the G20 to find ways to make national financial regulatory systems more consistent and harmonious.

The process of up-grading the framework for financial regulation is well under way in G20 countries and beyond. The G20 reform effort effectively addresses shortcomings in financial regulations and market infrastructures and products. In the process of legislation and rule-making on those issues, regulatory cooperation between the EU and the U.S. should play a significant role in the process of setting international standards and best practices related to financial markets regulation and oversight. It is essential that the EU and the U.S. continue to coordinate and collaborate on finding the best approaches to financial markets regulation in order to drive down regulatory duplication costs for companies operating on both sides of the Atlantic. A framework for regulatory cooperation within existing forms of dialogue that take place on both a transatlantic and global basis should be the most effective way forward and should add transparency to regulatory differences and commonalities.

As well as the existing dialogue, the broader EU-U.S. negotiation on a trade agreement would also be a useful avenue for pursuing deeper transatlantic cooperation in financial services regulation. The interim report of the High-Level Working Group on Growth and Jobs stated:

> "[...] the two sides [...] seek to negotiate: [...] Horizontal disciplines on regulatory coherence and transparency for goods and services, including early consultations on significant regulations, impact assessment, upstream regulatory cooperation, and good regulatory practices"

and

> "[...] provisions or annexes containing additional commitments or steps aimed at promoting regulatory compatibility over time in specific, mutually agreed sectors."

TBC fully supports this objective. In the potential EU-U.S. negotiations on trade, investment and regulatory cooperation, an effort should be made to improve upon the current institutional, regulatory and policy status quo on financial services, which after all represents a services sector that already displays high volumes of cross-border activity, in the form of both commercial presence and cross-border services trade. Improving dialogue to enhance compatibility between the EU and U.S. financial regulatory environment would help decrease the opportunities for regulatory arbitrage and reduce the cost of duplicative regulation as well as provide legal clarity on prudential, market infrastructure and product issues for financial market participants on both sides of the Atlantic. It would also enhance the ability of financial supervisors to effectively monitor cross-border financial markets activities.

The Financial Markets Regulatory Dialogue (FMRD) works to pursue these goals and the importance of its work is increasing, as legislation and rule-making in implementing G20

principles in the EU and in the U.S. have in some cases increased barriers to trade in the transatlantic financial market. Often times when this happens, explicit legislative or other official action is necessary to facilitate barrier-free access to each other's financial market. Also, there is no explicit mandate on either side to strive for such an objective.

Therefore, we propose consideration of legislative mandates for agencies of financial regulation on both sides of the Atlantic to explicitly strive for EU-U.S. regulatory cooperation, based on the working assumption that common standards, equivalence or mutual recognition should be reached. In clearly limited circumstances, in which, due to profound differences in constitutional, institutional or legal contexts, none of these objectives seems attainable, a comply-or-explain approach might be pursued to explicitly lay down why neither of both seems feasible.

Adding a specific mandate would encourage regulators on both sides of the Atlantic to consider the impact on the transatlantic financial market at every step of rulemaking process in line with the general recommendations of the HLWG quoted above.

We recognize that there may be issues for which regulatory harmony cannot be reached and that some topics would be more effectively dealt with as part of trade negotiations. That said, this should not prevent trying to achieve negotiations on other issues where agreement can be reached. We would suggest categorizing financial services issues by means of four boxes. The first two boxes would represent trade domains and need not necessarily be dealt with within the framework of the FMRD, whereas the third and fourth box issues would be dealt with in that framework. For example:

(1) The first box would include traditional trade and investment provisions consistent with the four modes of delivery in the GATS.

- The EU and the U.S. should work towards strengthening the national treatment of financial institutions, a binding of current levels of market access and removing remaining restrictions to trade at either the EU and federal U.S. level or at the EU member state level, respectively at the U.S. state level (cross-border supply).

- The EU and the U.S. should also work towards establishing and binding free access via foreign direct investment of EU- and U.S.-domiciled financial institutions across the Atlantic (commercial presence) and as well as strong investment protection rules.

- The EU and the U.S. should also improve current practical arrangements on the temporary movement of qualified persons by improving the status of qualified persons not only but also in financial services, by reducing administrative burdens and by providing mechanisms similar to the APEC Card for business visitors or by broadening the U.S. Visa Waiver Program.

(2) The second box would include horizontal business issues that are of importance to financial services firms. These include cross-border, intra-corporate use of data and the interoperability of legislation pertaining to data protection and security, cyber security and also consumer protection issues.

(3) The third box would include some financial regulatory issues which create difficulties in mutual market access and are, in principle, for legal, political and economic reasons, viable areas for on-going regulatory cooperation (for example, rule-making on derivatives). All of these topics are presumably at issue in the FMRD which would be the right body to address these topics. In addressing these topics, the FMRD should use the following principles as a guide:

- Undertaking consultation in advance of proposing and adopting legislation or regulation;
- Avoiding to the greatest extent possible the imposition of extraterritorial requirements, and wherever possible, recognizing the equivalence of regulatory regimes that share objectives but differ in approach;
- Adopting international standards and global best practices, and promoting the development of high quality international standards by global bodies; and
- Supporting closer coordination among regulators in the oversight of entities regulated in both markets to enhance oversight while avoiding overlap and duplication.

(4) The fourth box would include jointly agreed prudential carve-outs of such provisions that cannot be subject to considerations of mutually assured market access. These issues must mostly be those clearly dominated by financial stability, investor and/or client protection considerations and which, due to insurmountable differences in constitutional or legal provision on either or both sides of the Atlantic, cannot be bridged in the foreseeable future by either common standards, mutual recognition, "substituted compliance", "equivalence decisions" or similar legal methods. While accepting the pre-eminence of supervisory concerns on both sides of the Atlantic, even in these cases there is scope for progress to be made in further talks improving supervisory conditions and practices across the Atlantic, in particular with respect to an efficient division of labour between host and home regulators. In addition, there should be some consideration paid to the issue of proportionality of financial supervisory and market access considerations. The FMRD should pursue measures that would limit to the extent possible negative spill-over impacts of regulation.

While the first box should not contain particularly controversial issues but may well lead to demanding legal drafting of GATS-consistent provisions, the second box would potentially require legislative changes on both sides of the Atlantic of those horizontal sets of rules which present or threaten to present barriers to market access.

While issues in the first two boxes may not require continuous consultation with financial services firms once brought into force, on-going regulatory cooperation may well have to be based on a more elaborate consultation process involving industry input, a structured legislators' dialogue as to determine whether general financial services legislation rather than financial regulation and rule-making are at issue and high-level political oversight. Also, enhanced transparency of efforts to align regulatory approaches would be welcome, both in terms of work-streams, schedules, objectives (in broad categories as described above) and progress to reduce the potential for regulatory fragmentation.

Concerning the third and fourth box, governments and regulatory agencies on both sides of the Atlantic should establish a working programme to identify which types of issues should be put into which type of treatment, and how market access issues arising from inconsistent legislation or implementation can be rectified. The default, in all of these questions, should be that issues be treated in the third box with a view to achieving mutually agreed and compatible regimes.

Rather than describing the numerous issues of partly inconsistent or conflicting rule-making in the EU and the U.S. in the field of banking and securities (see Report of the EU-U.S. Coalition on Financial Regulation on "Inter-jurisdictional Regulatory Recognition", June 2012, attached) or in other sectors of financial services, we would like to highlight only the most important areas requiring additional efforts of aligning regulation on both sides with the aim of maintaining an integrated transatlantic financial market while deepening it in the medium-term.

Banking and securities

Enhancing capital and liquidity standards

- Most jurisdictions, including the EU and the U.S., are well advanced in implementing the recommendations of the Basel Committee on Banking Supervision (BCBS) on capital and liquidity standards (Basel II, II.5 on the trading book and complex securitizations and Basel III). The U.S. is implementing Basel II, having approved final rules covering the market risk elements of Basel II.5 in June 2012 and publishing draft Basel III rules on capital. The EU is in the process of finalizing its legislation on all aspects of implementing Basel II.5 and III. Liquidity rules proposed by the BCBS are also in the process of being implemented, but not in the short term. Different approaches to implementation are discussed in the U.S. and the EU, and a harmonized approach would clearly be desirable.
- It will remain important to harmonize the implementation of capital and liquidity rules in the EU and the U.S. to avoid costly and complex adherence to divergent rules. Particular emphasis should be given to the potential extraterritorial impact of certain U.S. legislative or rule-making provisions under discussion given the divergence of either side with the global approach of the BCBS with a view of limiting the impact to the greatest possible extent.

Improving banking resilience

- Coherent implementation of rules for significant institutions: Specific rules for globally systemically important banks (G-SIBs) should be implemented in a similar manner. We urge the EU and the U.S. to make it clear that the definition of criteria, the supervisory tools and the requirements regarding the loss-absorbency capacity on systemically important financial institutions be implemented consistently. Similarly, rules on the potential winding down of such institutions in case of failure should be aligned in order to avoid competitive distortions stemming from differences in treatment. A proper assignment of the task to the home country supervisor is an important element in an efficient framework.
- Going forward, close cooperation between the EU and the U.S. will be important in determining and regulating global systemically significant insurance companies and other financial institutions.

Establishing bank resolution regimes

- Resilient regimes: TBC supports on-going efforts to establish legal frameworks of bank resolution, including cross-border dimensions, additional prudential capital requirements, clearly defined rights of, and procedures for, supervisory authorities to intervene early on, orderly preparations of resolution plans by financial institutions and a strengthening of market infrastructures. Also, cross-border crisis management groups as well as co-operation arrangements have to be built for G-SIBs.
- Legal frameworks for cross-border resolution: U.S. and EU authorities should continue their work towards establishing comprehensive and harmonized legal frameworks for the resolution of financial institutions including harmonized international rules to cope with cross-border issues in resolution. The respective legal issues pertaining to the proper resolution of financial contracts subject to various U.S., EU member state and third country jurisdictions poses particular problems which should be addressed comprehensively.

Infrastructure

OTC derivatives reform and compatibility of regulation

- Core policy objectives towards a sounder framework for derivatives clearing should be set in line with G20 commitments. The U.S. and the EU are well advanced in implementing the G20 action plan. Both sides are strongly committed to ensure that most standardized OTC derivative contracts are traded on exchanges or electronic trading platforms and cleared through central counterparties, that derivative contracts are reported to trade repositories and that non-centrally cleared contracts should be subject to higher capital requirements. Work on minimum standards for margining of the latter contracts is moving forward.
- Current regulatory efforts pose fragmentation risks and avoidable costs. We are concerned that current efforts of rule-making on both sides may effectively result in overly burdensome regulatory costs because of divergent implementation. Also, the compatibility of emerging EU and U.S. rulebooks is not assured which has the potential to lead to complex and conflicting legal provisions for the centralized clearing of contracts. We are concerned that users of derivatives may face an unnecessarily costly reality while providers may have to cope with conflicting regulatory settings for certain products, such as swaps. We recommend that efforts at regulatory cooperation be strengthened with a view to reaching mutually consistent solutions that meet the regulatory objective while avoiding overly costly and conflicting legal provisions.
- Regulation of central counterparties. Of equal importance is the regulatory approach to central counterparties. We support the FSB work on providing a regulatory environment with fair and open access for market participants, cooperative oversight arrangements, effective resolution and recovery regimes and appropriate liquidity arrangements. Also, due consideration should be given to the proper supervisory structure in the emerging new EU supervisory architecture as well as in the U.S. context.

Insurance

Transatlantic trade and investment between the United States and European Union is the most dynamic economic relationship in the world. With products and services across industries and sectors imported and exported across the Atlantic, insurance is particularly important to U.S.-EU trade. Premiums generated from insurance and reinsurance total well over $185 billion annually, representing over two-thirds of the current global premium volume. The significance of our bilateral insurance and reinsurance relationship to transatlantic trade cannot be overstated.

In the Interim Report, the HLWG addresses a number of regulatory areas and non-tariff barriers that affect the insurance industry. The report specifically cites bilateral mechanisms for addressing these trade issues, which arise from technical regulations, conformity assessment procedures and standards. TBC welcomes this as an important step to cementing the progress already being made through the FMRD and the U.S.-EU Insurance Dialogues.

Regulators and policymakers on both continents essentially acknowledge that regulatory barriers are as much of a hindrance to cross-border trade (and growth) in financial services as other non-tariff barriers. In order to best tackle such regulatory barriers, we urge that the

FMRD and the U.S.-EU Insurance Dialogues not be "silo" activities separate from the mission of the HLWG.

TBC firmly believes that support for financial services and insurance issues at the highest levels of government would lead to greater coordination and better regulatory outcomes. We feel that political support would help U.S. and EU insurers become more competitive in rapidly maturing insurance markets, which we hope is a desired goal for policymakers on both sides of the Atlantic.

TBC also welcomes the Interim Report's request that negotiators include "provisions or annexes that might contain additional commitments or steps aimed at promoting regulatory compatibility over time in specific, mutually agreed sectors." We believe that the insurance sector would benefit from such actions. Otherwise, negotiators would simply consider technical regulatory discussions as loosely related to the Jobs and Growth Initiative, making any productive and significant outcomes from these negotiations less of an imperative.

TBC's comments herein are rooted in the overriding objective of growing and maintaining the largest bilateral insurance trade and investment relationship possible. With that in mind, we want the European Commission and U.S. Administration to consider these thoughts:

- Regulatory Awareness: U.S. and EU regulators and policymakers should recognize different supervisory methodologies (e.g., state-based versus country-level), but agree to analyze these methodologies based on outcomes and whether or not those outcomes are equivalent. This approach (and mindset) should achieve similar levels of protection for policyholders. A practical example of the lack of deeper mutual recognition between U.S. and EU regulators occurs in a situation where a national supervisor demands a more holistic view of an entire insurance group's operations. The natural reaction is usually for the regulator to request additional information, including complex data from the parent entity. As local regulators become increasingly sophisticated, such requests can be expected to multiply (absent any global or regional attempts to rationalize the process). This is a troubling trend for companies with a large global presence. In order to address this, we would encourage efforts by the U.S. and EU to design an approach for each jurisdiction to recognize robust group supervision conducted in another jurisdiction in order to prevent duplicative regulatory requests.

- Global Policy Coordination: Efforts by leaders in the U.S. and the EU should be coordinated with other global policy setting institutions such as the G20, the Financial Stability Board (FSB) and the International Association of Insurance Supervisors (IAIS), especially as the G20 efforts approach an establishment of uniform global standards. From TBC's standpoint, a single transatlantic voice would be most influential to communicate with such institutions.

- Industry Perspective: Consultative meetings with private sector corporations should be scheduled regularly, with the goal of bringing increased transparency to the process and ensuring that policymakers' decisions are informed by industry-based perspectives and experiences.

- Reinsurance Collateral Requirements: EU and U.S. policymakers should set a goal of achieving full parity of treatment for reinsurers trading on a cross-border basis between the EU and U.S. so that there are no statutory collateral requirements for approved reinsurers under either supervisory regime when trading into the other's jurisdictions. This goal can be achieved by the conclusion in the first instance of a "covered agreement" (to use Dodd-Frank terminology) on reinsurance prudential issues between the EU and the U.S. to enable mutual recognition of each other's

reinsurance supervisory regimes to occur, the removal of all discriminatory rules currently applicable and the forestalling of new discriminatory rules.

- Pensions Policy: Pensions policy is very much a national policy matter for the U.S. and individual EU Member States informed by national employment, contract and other policies. It is not an area which requires regulatory or policy harmonization. It is however a sufficiently important area to ensure that proposals by the EU Commission or U.S. Government do not have major impacts on a transatlantic basis. For example, EU proposals to apply solvency norms, targeted at insurance instruments, to occupational pensions schemes (IORPS Solvency II) would negatively impact on the attractiveness of investment and job creation in the EU by U.S. and European companies. The additional call on capital into corporate-sponsored pensions, notably in Germany and the UK, would divert significant funds from investment in growth and jobs.

In conclusion, we believe that the fundamental goal of the insurance industry—to protect policyholders from risks while ensuring financial security—is consistent with the stated goals of the U.S. and EU political leadership when it formed the HLWG. Insurance is a fundamental ingredient for creating a robust and seamless economy that can sustain growth and job creation on both sides of the Atlantic. As such, we hope that the above recommendations will be seriously considered.

Accounting and Auditing

With respect to financial reporting and audit, achieving regulatory convergence would yield numerous benefits that would contribute to the efficient and effective functioning and stability of transatlantic financial markets and could stimulate economic growth and create jobs. These include:

- Improved comparability of financial information, which not only provides investors and borrowers a stronger basis for decision-making, but also facilitates the mobility of capital which would increase cross-border economic activity and trade;
- Decreased capital raising costs due to reduced transaction costs and information asymmetries that arise from divergent accounting and audit regimes due to increased risks in translation errors;
- Mitigating systemic risks by improving information flows, thus, reducing threats of irrational market behaviors, such as over-confidence and extreme risk-aversion, which could cause misallocation of resources and sustained imbalances;
- Improved transatlantic regulatory cooperation, which could reduce risks associated with conflicting regulatory conclusions that confuse investors and others who rely on audited financial statements, and lead to more consistent future policy development;
- Reduced costs of compliance with regulatory requirements, for example, in reducing the number of financial reports required of multinational companies; and
- Reduced risk of regulatory arbitrage in which companies seek out jurisdictions with less rigorous regulation and lower compliance costs to gain economic advantage.

Accounting

With regard to accounting standards, adoption and implementation of International Financial Reporting Standards (IFRS) on both sides of the Atlantic would bring significant benefits in terms of transparency and confidence in capital markets as well as lower financial reporting and capital costs. These are all important steps towards the eventual goal of a barrier-free

transatlantic market. We continue to support the objective of a single set of high-quality accounting standards used, without modification, throughout the world, including the U.S. We recognize, however, it will take time to achieve this goal and countries may go about achieving it in different ways.

Based on the above observations, we encourage the EU and U.S. to agree to support the following:

- Encourage countries around the world to adopt IFRS without modification.
- Consistent application and interpretation of IFRS around the world, discouraging local modifications or interpretations.
- Support the objective of the IFRS Foundation in developing an Accounting Standards Advisory Forum so national and regional standard setters remain involved in the process of setting IFRS.
- Continuing timely endorsement of IFRS by the EU mechanism so that European companies can fully retain access to and comply with global accounting standards without any legal impediment, "carve-outs" or undue delay.

Auditing

Audit quality and auditor independence are vital to the public interest and to the efficient functioning of transatlantic capital markets. Audit quality and auditor independence are best secured by strong corporate governance, independent regulation of the auditing profession, the adoption and implementation of the International Standards on Auditing (ISAs), as well as professional adherence to the Code of Ethics promulgated by the International Ethics Standards Board for Accountants (IESBA).

We therefore encourage the EU and U.S. to support the following measures to promote enhanced regulatory compatibility in the oversight of auditors and high quality audits between our markets:

- Adopting and implementing International Standards on Auditing (ISAs). We believe the adoption and implementation of ISAs will provide consistency, further improve the quality of audit, and further reduce regulatory barriers. The EU and U.S. should encourage the International Auditing and Assurance Standards Board (IAASB) and national standard-setters to coordinate and converge their standards.

- Encouraging adherence to strong professional independence standards by audit firms and individual auditors as set out in the IESBA Code of Ethics, which provides for the application of safeguards to potential threats to independence, periodic rotation of the audit partner (a minimum of seven years), and restrictions on personal and business relationships with audit clients.

- Eliminating cross-border barriers, such as those that impose firm ownership requirements or restrict the mobility of professionals, the elimination of which could help further develop a transatlantic audit market.

- Promoting the establishment of appropriate collaborative arrangements between national audit oversight bodies and develop a clear roadmap towards mutual reliance.

- Developing a common framework for two-way communication between auditors and prudential regulators to improve cross-border regulatory cooperation in respect of financial institutions.

- Developing a transatlantic regulatory framework for auditors of companies listed in the U.S. and the EU – such a framework would establish common practices and standards, common inspection approaches, and common standards for public reporting of inspection results.

- Supporting strong and independent audit committees composed of highly qualified and competent non-executive Directors with clear articulation of their responsibilities. Responsibilities of audit committees should include the review of the performance, independence and objectivity of the external auditor and recommending the appointment or re-appointment of the auditor to the Annual General Meeting. The role of the audit committee also should include the pre-approval of permissible non-audit services to be provided by the auditor. Effective oversight of the independent auditor by the audit committee promotes good governance and investor confidence.

We also encourage the EU and the U.S. to move away from proposals currently under consideration in the EU and also subject to debate in the U.S. that would be harmful to audit quality, such as those that would impose mandatory firm rotation, restrict audit tenure, further limit non-audit services, mandate audit-only firms, or otherwise weaken the role of the audit committee. If implemented, we strongly believe these provisions will not improve audit quality and will increase costs to companies. As part of its responsibility for overseeing a company's financial reporting, the independent audit committee should continue to oversee a company's engagement with its external auditor, including recommendations regarding auditor appointment, remuneration and provision of permissible non-audit services.