Digesting the Regulatory Layer Cake in the North American Insurance Market: Integrating Trade Agreements in the International Expansion Plans of Insurance and Reinsurance Companies

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Summary

We analyze how the interaction of the NAFTA and the WTO with federal and state regulation affect risk reduction and market entry strategies in the North American insurance market. While the strategic benefits of international diversification are well known, there has been no analysis of how international trade agreements affect the strategic planning process of international insurance companies. We conclude that market entry through foreign investment in Mexico provides the best strategy for overcoming the challenge of existing market entry barriers in Canada, the United States and Mexico.

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Page 3+

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Why does an insurance company need to expand internationally?

Globalization of insurance companies has become a reality. With a few exceptions (for example, insurance companies in Japan), in most OECD countries the largest domestic insurance companies are either a subsidiary of a global giant or an affiliate of a global insurance company. These firms lower risk through geographic diversification and enhance long-term growth through demographic diversification.

The race for mergers and acquisitions is on. For example, on May 12, 2001, AIG announced a takeover of American General[1] a deal worth $23 billion. With demutualization providing shares to use as acquisition currency, the process of takeover has taken a new dimension in the insurance industry.

Why merge?

Success in the insurance business is very scale dependent. The larger the company, the greater the chance of higher profitability. Simple ways of expanding the size of the company is through mergers and acquisitions. For example, ING exercised the option of buying the remaining part of the Mexican insurance company Seguros Comercial America (SCA) on June 4, 2001 to consolidate its position in the Mexican insurance market. SCA now has 29% of the insurance market in Mexico. Even though SCA has a market value of less than $2 billion (compared with the market value of ING

[1] *New York Times,* Insurance Mergers Likely in Scale Race, May 12, 2001, p. 12.

at $453 billion), it is the sum of all these relatively small deals across the globe that adds value to the company.

Domestic mergers and acquisitions in a mature market are often not enough. Developing markets with rapidly expanding insurance business are often the best place to improve profitability. For example, the biggest return on investment of AIG comes from emerging markets.

How does an insurance company decide where to expand?

It is not enough for a company to decide to expand internationally. It has to make decisions about where and how. To expand in uncharted territories, it has to weigh in the risks along with the potential rewards. When entering a new market, a company needs to know what legal barriers it might encounter.

Regulations in international financial services are changing. Global deregulation has a major impact on risk management and strategic choices. In this paper, we explore international changes in regulation and how it can and does affect international expansion in the insurance business. While the strategic choices and risk management strategies may be well-known, we take an innovative look at how they are affected by international trade agreements and what the future of global trade in insurance services may be.

Why the North American markets?

With economies of scale in insurance business, it is clear why a company needs to get bigger. International expansion brings risk reduction. Entry into the North American market allows a company to operate in Mexico (a rapidly developing market) in addition to the United States and Canada. Although the latter are more mature markets, their

aging baby boomers make them the fastest developing annuity markets[2]. Thus, a company with business in all three countries can expand the sales of traditional insurance products (such as life and auto) in Mexico, and sell complementary products like annuities in the United States and Canada. This diversification reduces risk.

The NAFTA plays a big role in risk reduction by protecting foreign investment. Therefore, a combination of Mexico and the US/Canada is not the same as combining the US/Canada with some other country, such as China or Indonesia, where such explicit protection is not available.

Mexico also plays the role of a gateway. As an integral part of NAFTA, it can serve as an entry point for a non-NAFTA company to enter the US/Canada market. Mexico has also signed a free trade agreement with the European Union. Thus, companies in the US/Canada might find it easier to enter the European Union through Mexico. Mexico has also signed free trade agreements with nine countries in Latin America, and is participating in hemispheric negotiations. Thus, Mexico might be a convenient entry point for North American or European companies to enter other Latin American countries through Mexico. Mexico is also a member of APEC (Asia Pacific Economic Cooperation). Thus, it will become an entry point for the Asia-Pacific region when APEC completes its negotiations. Indeed, Mexico has the unique distinction of participating in all major regional trade blocks.

Description of the North American Markets

The US insurance market is the largest in the world. To understand the NAFTA market for insurance, we can look at its place in the top ten markets in the world. Mexico

[2] Among the developed countries, Canada has the fastest growing population over 65 (see, for example, Robert Brown *Economic Security for an Aging Canadian Population,* Society of Actuaries Monograph No.

does not feature there, but Canada does. Thus, in global scheme of things, NAFTA represents a small extension of the US market. The US market represents 34% of the global market and Canada has just over 1.8%, in the eighth place. Mexico appears as a blip in 24th place, with 0.35% of the market. However, in regulatory reform, NAFTA represents a giant leap. It has brought together three countries: a large developed market (US), a small, developed market (Canada) and a small but potentially large developing market (Mexico).

Table 1: Insurance market share, density and premium

Item	*Mexico*	*US*	*Canada*	*G7*	*EU*	*NAFTA*
Share of World	0.35	34.22	1.80	80.27	30.24	36.37
Insurance Density (US$)	84.60	2921.10	1375.30	2,693.60	1,805.90	2121.10
Insurance Penetration (%)	1.52	8.65	12.09	9.01	7.99	8.11

Insurance Density (premium per capita) consists of the premiums written divided by total population. Insurance penetration (premiums as a share of GDP) measures the significance of the insurance industry relative to the country's entire economic production. Life Insurance penetration typically increases in line with personal income (Source: World Insurance in 1999, Sigma, 9/2000).

It is probably unfair to think of the US insurance market as one single market. Given that state insurance commissioners have strong influence on policy making in each of the fifty states and state governments regulate insurance, it might be instructive to think of each state as a separate market. Table 2 shows the results of this exercise. Among the top ten markets in the world, four states of the US come in (New York, California, Texas and Florida). Among the top 20, another five states join in. Among the top 50, 30 states of the US find a place. Thus, by global standards, each state of the United States represents an important piece of the insurance market.

M-RS99-2, p. 10 (Table 2.3))

Table 2: How big are world insurance markets compared with States of the US

rank	*Country/State*	*premium*	*rank*	*Country/State*	*premium*
1	Japan	$519,589	26	Virginia	$16,020
2	Germany	$152,218	27	Taiwan	$15,827
3	United Kingdom	$137,061	28	Washington	$15,822
4	France	$136,841	29	Wisconsin	$15,365
5	New York	$71,390	30	Belgium	$15,323
6	California	$66,702	31	Brazil	$15,029
7	South Korea	$62,470	32	Missouri	$14,742
8	Texas	$48,685	33	Connecticut	$14,621
9	Florida	$44,079	34	Maryland	$14,234
10	Italy	$43,911	35	Minnesota	$14,129
11	Illinois	$39,923	36	Austria	$13,608
12	Canada	$36,196	37	Tennessee	$13,536
13	Netherlands	$36,139	38	Sweden	$13,057
14	Australia	$33,103	39	Colorado	$12,379
15	Switzerland	$32,994	40	Arizona	$11,721
16	Michigan	$30,502	41	Denmark	$11,118
17	Spain	$30,200	42	Alabama	$10,579
18	New Jersey	$29,959	43	Louisiana	$10,106
19	Ohio	$29,487	44	Finland	$10,105
20	Pennsylvania*	$28,016	45	China	$9,622
21	Massachusetts	$26,389	46	Oregon	$9,315
22	Georgia	$19,951	47	Iowa	$8,289
23	South Africa	$19,578	48	Kentucky	$8,188
24	North Carolina	$17,769	49	South Carolina	$7,807
25	Indiana	$16,199	50	Kansas	$6,615

Premium volumes are in millions of US dollars. Data are for 1996. Source: Sigma 4/1998 and NAIC database. *Pennsylvania data does not include HMO and HMDI premiums.

Interaction of Strategies and Regulation

The law relating to insurance is complex. Not surprisingly, international agreements reflect this complexity. NAFTA and WTO add international layers to domestic laws. Insurance firms that wish to expand internationally must wade through a dizzying array of rules to determine what services they may provide, how they may deliver those services, and where.

International and domestic regulations affect the strategies available to firms. The degree to which a firm can achieve economies of scale through the centralization of operations is affected by the modes of service delivery that are available in a given market. The exploitation of new technologies to improve service and lower costs is also limited by the mode of delivery that may be employed. The degree of control over international operations is restricted where market entry is available only through a minority equity stake in local firm. Thus, strategic business alliances may be a necessity, rather than a choice to be made. Even hiring and promotion decisions are limited by the degree of mobility that is allowed for natural persons. Restrictions on the movement of natural persons may also affect the transfer of knowledge and expertise from one operation to another.

Decisions regarding international expansion and business strategies can not be made without a careful review of state, federal, regional and global laws affecting international trade and investment in the insurance industry. This article analyzes interactions between these four layers of regulation as they apply to the insurance industry in North America. We then apply this analysis to international expansion strategies.

International Agreements on Insurance Services

NAFTA restricts the way Canada, the United States and Mexico may regulate insurance companies.[3] Chapter 11 governs foreign investment and Chapter 14 covers international trade in financial services. Of the 140 members of the WTO, 104 have made commitments to liberalize financial services regulation, including Canada, the United

[3] *North American Free Trade Agreement between the Government of Canada, the Government of the United Mexican States and the Government of the United States of America*, January 1, 1994 [hereinafter NAFTA].

States and Mexico.[4] WTO rules on financial services are found in a labyrinth of seven intersecting agreements: the Agreement Establishing the World Trade Organization; the Understanding on Rules and Procedures Governing the Settlement of Disputes; the General Agreement on Trade in Services (GATS); the GATS Annex on Financial Services; the Financial Services Agreement; the Schedules of Commitments on Financial Services; and the Understanding on Commitments in Financial Services. All WTO members are bound by the first four agreements. Mexico is bound by the first six agreements. Canada and the United States are bound by all seven. We will refer to these agreements collectively as the WTO.

NAFTA versus non-NAFTA firms

Canada, Mexico and the United States have two sets of international obligations that apply to insurance regulation. In principle, firms from outside the NAFTA region are only entitled to WTO treatment. However, they may be able to use the access acquired under the WTO to enter the North American market and gain NAFTA treatment.

NAFTA applies to "persons" of a NAFTA country, which includes an enterprise (corporation, trust, partnership, joint venture and other forms of business organization) constituted or organized under the law of a NAFTA member.[5] Thus, as long as a company from outside the NAFTA region is able to meet the requirements for incorporation (or other forms of business organization) and complies with foreign investment laws, it may become a NAFTA company. For example, it may acquire an

[4] See United States of America, Schedule of Specific Commitments, Supplement 3, GATS/SC/90/Suppl.3, 26 February 1998(authentic in English only); México, Lista de compromisos específicos, Suplemento 3, GATS/SC/56/Suppl.3, 26 de febrero de 1998(auténtica en español únicamente); Canada, Schedule of Specific Commitments, Supplement 4, GATS/SC/16/Suppl.4, 26 February 1998(authentic in English and French only); and Canada, Schedule of Specific Commitments, Supplement 4, Revision, GATS/SC/16/Suppl.4/Rev.1, 6 June 2000(authentic in English and French only).

[5] Articles 201, 1139, and 1416.

existing firm, establish a wholly-owned subsidiary, or create a joint venture in one of the NAFTA countries.

Scope and operation of NAFTA and WTO

Both NAFTA and WTO cover all types of insurance.[6] Their obligations apply primarily to federal governments.[7] However, under international law, a country may not invoke the provisions of its internal law as justification for its failure to comply with international treaties.[8] In addition, NAFTA and WTO both make it clear that national governments are responsible for the actions of their states or provinces, as well as self-regulatory organizations that play a role in market access for the financial services industry.[9].

General rules

Both agreements set out general principles, general exceptions, and exceptions specific to financial services regarding exclusivity of government social programs and prudential regulations required for the protection of consumers or the financial system. In addition, each sets out a series of specific exceptions – regarding specific laws or sectors -- to the application of the general principles. This latter type of exception – referred to as reservations – are set out in annexes for each country. All insurance regulations must either comply with the general principles, qualify as exceptions, or be listed as reservations in the annexes.

NAFTA uses a "negative list" of reservations, listing specific measures that do not comply with the general rules. This serves two key functions. First, it prevents the

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[6] NAFTA, Article 1416, Annex on Financial Services, Article 5.
[7] NAFTA, Article 1401, GATS Article I.
[8] Vienna Convention on the Law of Treaties, Article 27.
[9] NAFTA, Articles 105 and 1402. GATS, Article I(3).

governments from creating future restrictions that violate the general rules, except where such restrictions qualify under the exceptions. This limits the circumstances under which governments may create further restrictions on the sale of insurance. Second, the listing of non-conforming measures makes them easier to identify, simplifying future negotiations to eliminate them.

NAFTA thus encourages innovation by providing insurance firms with an incentive to create new services that are not restricted by the negative list. The NAFTA clarifies that this is the case by specifically prohibiting governments from discriminating against firms from the other members in the provision of new types of financial services.[10]

WTO uses the exact opposite of the NAFTA approach to liberalize trade in insurance services. Whereas NAFTA uses a “negative list” of reservations to set out specific areas that are *not* being liberalized, WTO sets out individual “positive lists” of services that *are* being liberalized. Thus, under WTO, if a WTO member has not made a specific commitment to liberalize a particular aspect of the insurance industry, it is under no obligation to do so. Even when a general commitment is made to liberalize a particular mode of delivering a specific type of insurance, the country in questions may submit lengthy lists of reservations for measures that contradict the commitment.

Relationship between WTO and NAFTA

WTO members may create free trade areas that go beyond their WTO obligations, even though this results in differential treatment among members.[11] If there is a conflict

[10] NAFTA Article 1407(1).
[11] GATS Article V, GATT Article XXIV.

between WTO and NAFTA, as a general rule NAFTA will prevail.[12] All three NAFTA countries are members of WTO and have made commitments thereunder. Should one of the NAFTA countries make WTO commitments that are better than the commitments they previously made to the other NAFTA members, NAFTA requires that the better commitment be immediately extended to its NAFTA partners.[13] It is thus not possible for a NAFTA member to give more favorable access to its insurance market to a non-member than it does to a NAFTA member. Indeed, NAFTA opens up the financial services markets to a greater degree than the WTO financial services agreements.

Non-discrimination

In NAFTA, two principles of non-discrimination, national treatment and most-favored-nation (MFN) treatment, prohibit discrimination against insurance firms on the basis of nationality. Under national treatment, foreign investors and firms must be treated no worse than domestic firms.[14] However, this does not entitle them to identical treatment. Rather, national treatment for financial services is defined as treatment that affords equal competitive opportunities. Differences in treatment are permitted as long as they do not put foreign insurance companies at a disadvantage as compared to domestic insurance companies. While differences in market share, profitability or size do not in themselves constitute proof that equal competitive opportunities are being denied, they may be used as evidence of such.[15] At the state or provincial level, governments must treat member country firms no worse than they do firms from other states or provinces.

[12] NAFTA Article 103. Within the NAFTA itself, conflicts between Chapter 11 and other chapters will be resolved in favour of the latter. See NAFTA Article 1112.
[13] NAFTA Article 1406.
[14] NAFTA Article 1405.
[15] NAFTA Article 1405(5), (6), (7).

Under MFN treatment, the firms and investments from a member country must be treated no worse than those from any other country.[16]

WTO only applies the principle of non-discrimination with respect to MFN treatment.[17] Unlike NAFTA, the general obligations of WTO in financial services do not include market access or national treatment. Instead, members decide the conditions to set in these areas and specify those conditions in its schedule of commitments for each service sector.

These market access commitments must be applied without discrimination to all WTO members unless exceptions are listed in an Annex on MFN exemptions.[18] Mexico has not submitted any MFN exemptions that affect trade in insurance services. Canada and the United States each have one exemption. The United States commitments do not apply to any WTO members that restrict the expansion of existing operations, prevent the establishment of a new commercial presence or compel a person of the United States, on the basis of its nationality, to reduce its share of ownership in an insurance firm. Canada's MFN exemption permits Ontario to grant preferential access to non-resident individual insurance agents from all states in the United States.

Countries may use their WTO schedules of commitments to place limits on market access and national treatment. However, the limitations only apply to existing measures that would otherwise be inconsistent with these obligations, effectively freezing their restrictions so that future measures they might take will not be more restrictive. For example, a country might permit foreign insurance companies to establish a commercial

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[16] NAFTA Article 1406.
[17] GATS, Article II.
[18] GATS, Article II.

presence, but maintain a limit on national treatment by preserving a foreign investment law that limits the percentage of an insurance firm foreigners may own.

Key Exceptions

WTO exceptions override any obligations a member may commit to with respect to trade liberalization. However, they may not abuse the exceptions to create disguised restrictions on trade in services or to arbitrarily discriminate between countries. Key exceptions permit laws against deceptive and fraudulent practices and aimed at the collection of taxes or the avoidance of double taxation.[19] NAFTA contains more detailed rules than WTO with respect to the application to taxation measures to financial services obligations.[20]

Both agreements allow prudential measures to protect consumers, maintain the integrity of insurance firms and ensure the stability of the financial system.[21] While the governments are generally prohibited from interfering in transfers and international payments[22], NAFTA permits non-discriminatory transfer pricing rules to maintain the safety, soundness, integrity or financial responsibility of insurance firms.[23] This exception would apply to regulations regarding minimum deposit and capitalization requirements, for example. However, governments may not use the prudential exceptions to avoid their obligations.[24]

Dispute Settlement between Governments

Disputes between governments over the compatibility of domestic laws with the agreements are resolved through arbitration if they can not be settled through

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[19] GATS, Article XIV.
[20] NAFTA Article 2103.
[21] NAFTA Article 1410(1).
[22] NAFTA Article 1109.

consultations. If the arbitration panel rules in favor of the complaining party, and the other party does not take steps to comply with the panel's ruling, the complaining party may retaliate against the financial services sector of the other party.[25] These types of disputes can only take place between the member governments.[26] Insurance companies must persuade their own government to file a case against another member government when the latter violates its obligations. Unlike NAFTA decisions, WTO panel decisions can be appealed.[27]

NAFTA Dispute Settlement between Private Investors and Governments

Unlike the WTO, NAFTA provides for dispute settlement for foreign investors from one NAFTA country to sue the host government of another NAFTA country for compensation in the event of expropriation or measures equivalent to expropriation. In addition to seeking compensation, this process may be used to seek the repeal of the legislation that led to the expropriation.[28]

Any expropriation must be for a public purpose, nondiscriminatory, follow due process of law, and pay compensation at fair market value, plus interest. These rules provide NAFTA investors with the power to demand compensation whenever government measures interfere with business activities to such an extent that it prevents the use, enjoyment or disposal of their property. A mere reduction in profits does not constitute a sufficient degree of interference to constitute expropriation.[29] However,

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[23] NAFTA Article 1410(4).
[24] Annex on Financial Services, Article 2(a).
[25] NAFTA Article 1414(5).
[26] GATS, Article XXIII.
[27] See WTO *Understanding on the Rules and Procedures Governing the Settlement of Disputes*, available at wto.org.
[28] NAFTA Article 1401(2).
[29] See *In the Matter of an Arbitration under Chapter Eleven of the North American Free Trade Agreement between Pope & Talbot Inc and the Government of Canada*, Interim Award by Arbitral Tribunal (The Hon.

government regulations can be applied in a way that would constitute "creeping expropriation", where they have the effect of "taking" the property in whole or in large part, outright or in stages.[30]

Claims for compensation represent a powerful tool for insurance companies to use to dissuade NAFTA governments from implementing legislation that is harmful to their investments. Even if a claim is ultimately unsuccessful, the mere threat of a claim can be used as a bargaining tool.

Modes of Supply

Both NAFTA and WTO determine market access by four modes of supply:

- Cross-border supply (when a service is provided in one country to a customer in a second country without either party traveling, for example by internet)
- Consumption abroad (when the customer travels to the service provider's country to purchase the service);
- Presence of natural persons (where the service provider travels to the customer's country on a temporary basis to provide the service); and
- Commercial presence (where the service is provided by foreign investment).[31]

Comparison of WTO Commitments

In WTO, Canada has liberalized insurance trade the most and Mexico the least. Canada has liberalized all four modes of supply. The United States has liberalized three, leaving out presence of natural persons. Mexico has only liberalized commercial presence. In terms of reservations for state restrictions, the United States has the most,

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Lord Dervaid, The Hon Benjamin J. Greenberg Q.C., and Mr. Murray J. Belman) (June 26, 2000), available on the web at www.dfait-maeci.gc.ca/tna-nac/dispute-e.asp#chapter11 [hereinafter Pope & Talbot].

[30] *Third Restatement of the Foreign Relations Law of the U.S.*, s. 712, comment (g), cited with approval in Pope & Talbot, ibid.

Canada has fewer, and Mexico has none at all. This reflects the constitutional structures of the three countries.

In terms of the kinds of services that have been liberalized, Canada is the most open, followed by the United States and Mexico. State restrictions in the United States limit the delivery of insurance services to a far greater extent than Canada's provincial regulations. Mexico's commitments cover a broad range of services, some of which are unique to the Mexican insurance industry. However, foreign firms may only deliver these services through a minority investment in Mexican-controlled insurance firms. Canada and the United States are more open to foreign investment in the insurance industry than Mexico, but state and provincial restrictions on residency and citizenship of firms mitigate that openness to varying degrees.

The following table compares obligations by mode of supply.

Table 3: Modes of Supply in Canada, US and Mexico

Mode	NAFTA	Canada(WTO)	USA(WTO)	Mexico(WTO)
Cross-border Supply	YES	YES	YES	NO
Consumption Abroad	YES	YES	YES	NO
Commercial Presence	YES	YES	YES	YES
Presence of Natural Persons	YES	YES	NO	NO

[31] GATS, Article I(2).

Comparison of NAFTA and WTO by Mode of Supply

The following table shows which agreement provides market access in each country by mode of supply.

Table 4: Comparing NAFTA and WTO by Mode of Supply

Mode	Canada	United States	Mexico
Cross-border Supply	NAFTA WTO	NAFTA WTO	NAFTA
Consumption Abroad	NAFTA WTO	NAFTA WTO	NAFTA
Natural Persons	NAFTA WTO	NAFTA	NAFTA
Commercial Presence	NAFTA WTO	NAFTA WTO	NAFTA WTO

Because NAFTA permits restrictions on soliciting and "doing business" for firms that seek to supply their services via cross-border supply and consumption abroad[32], the least restricted method of entering the market is through the establishment of a commercial presence. Restrictions on soliciting mean that the customer must initiate the transaction, thereby limiting marketing activities. While WTO also permits restrictions on soliciting, it does not permit restrictions on "doing business". However, this advantage may be negated by the extensive WTO reservations for federal, state and provincial measures submitted by Canada and the United States. In the case of Mexico, the market may only be entered through a commercial presence for non-NAFTA firms.

For a foreign investor, NAFTA provides better treatment than WTO because WTO has no equivalent to NAFTA Chapter 11. Moreover, WTO applies no general

national treatment requirement to trade in services. Finally, there are fewer foreign investment restrictions in NAFTA.

Non-NAFTA firms may acquire rights under NAFTA by investing in one of the NAFTA countries. This means that such firms should first establish a commercial presence in the NAFTA country that has the fewest foreign investment restrictions for non-NAFTA firms, then expand into the other NAFTA countries from that establishment.

The restrictions that exist at the state level in the United States are protected by reservations under WTO and make entry into the U.S. market more complicated than entry into Mexico, which has no state regulations for insurance. Moreover, the only mode of entry Mexico provides for WTO members is by way of foreign investment. If a non-NAFTA firm establishes a commercial presence in Mexico, it can expand into the United States through foreign investments that enjoy NAFTA protection. As a Mexican enterprise, it may take advantage of NAFTA provisions permitting the entry of natural persons who are citizens of a NAFTA country, and the entry of senior managerial and other essential personnel of any nationality. Once established in Mexico, it can serve the Mexican market without being impeded by Mexican restrictions on cross-border supply and consumption abroad. Finally, Mexico's numerous trade agreements provide potential access to markets in Europe, Asia and Latin America.

The main drawback of adopting this strategy is that it may not work in Canada, since Canada has reserved the right to require that a company from a NAFTA member be controlled by residents of that member to be entitled to NAFTA benefits. This provision was designed to get non-NAFTA firms to enter NAFTA countries through Canada. Canada has liberalized its market under WTO more than the United States or Mexico.

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[32] NAFTA Article 1404(2).

The Canadian market is being opened further by the introduction of new financial services legislation. Thus, Canada is competing with Mexico in its efforts to attract foreign investment. However, Canadian restrictions that limit both foreign and domestic shareholders to a non-controlling minority interest in insurance companies, together with its relative paucity of trade agreements compared to Mexico, make it a less attractive gateway.

For European firms, Mexico provides the added advantage of the Mexico-European Union Free Trade Agreement (MEUFTA) and Bilateral Investment Treaties (BITs). The MEUFTA contains provisions for financial services that mirror those of NAFTA. However, it contains no equivalent to NAFTA Chapter 11. Nevertheless, 13 of the 15 members of the European Union (all except the United Kingdom and Ireland) have negotiated BITs with Mexico that provide substantially the same protection for foreign investors as NAFTA. Mexico's MEUFTA reservations limit foreign investment in insurance firms to 49%. However, Mexico allows European investors to avoid this restriction by establishing or acquiring a financial holding company, through which they may establish or acquire insurance firms.

Conclusion

The benefits of increasing growth and diversifying risk through expansion into developed and developing markets with different demographic and economic profiles are obvious to global insurance companies. However, a major challenge lies in integrating the rules of international trade agreements into the strategic planning process. This paper has analyzed how two major agreements affect market entry strategies in the world's largest and most economically diverse insurance market. We have reached the conclusion

that the challenge of regulatory barriers to entry can be mitigated by entering the market through foreign investment in Mexico to take advantage of the market entry and investment protection provisions of NAFTA.

Under both NAFTA and WTO, Canada, Mexico and the United States have demonstrated a preference for foreign investment as the market entry mode for foreign firms. This is due to the perception that foreign investment is more beneficial than allowing imports of insurance services. However, they also want their firms to be able to export their services. To open other markets to exports, they have to open their markets to imports. We can therefore expect to see increasingly liberalization of cross-border trade in insurance services, which will provoke further consolidation in the industry and widen the selection of market entry strategies available to firms.

NAFTA has important implications for the international expansion plans of insurance firms. First, it is a trail-blazer that provides clues as to the direction other agreements will take. As a regional agreement involving only three increasingly integrated economies, NAFTA can move the liberalization process further and faster than larger agreements, such as the proposed Free Trade Agreement of the Americas (FTAA) and APEC, both of which are twenty years behind. As NAFTA moves forward, its members also push for more rapid global liberalization in WTO that will mirror the achievements of NAFTA. Secondly, NAFTA plays a role in risk reduction. With investment in Mexico as the optimal entry mode, the combined protection foreign investors enjoy under NAFTA Chapter 11 and Mexico's Bilateral Investment Treaties reduces the risk of investment loss in all three countries.

NAFTA also reduces political and economic risk in Mexico by locking in the regulatory reforms that have been made, integrating the Mexico economy with Canada and the United States, and improving Mexico's long-term growth potential. NAFTA brings a wide range of trade and investment rules under one roof, so Mexico can not backtrack on one set of commitments without pulling out of the agreement entirely. Because NAFTA is so important to Mexico's economy, this is highly unlikely to happen. Finally, as NAFTA widens to include the rest of the hemisphere under the FTAA, Mexico will push for a deeper integration of the original three members in order to maintain better access to Canada and the United States than other developing countries have. This will lead to a further reduction in barriers to trade in insurance services, yet again blazing a trail for other agreements to follow.

Mexico thus enjoys several strategic advantages as a gateway for the international expansion of insurance firms. For non-NAFTA firms, it provides a means to enjoy NAFTA benefits in the North American market. For example, ING invested in Mexico and used its Mexican subsidiary to enter the California market rather than using its New York subsidiary. Once licensed in California, it was able to expand more easily into Arizona. Thus, even for NAFTA firms, there are benefits. Due to the regulatory segmentation of the US market, a firm from one US state may choose to enter another US state via a Mexican subsidiary, in order to gain foreign investor protection under NAFTA and thereby challenge barriers to trade in insurance services between states. In addition, with the GDP Mexican-American population of the United States approaching that of Mexico itself, entering the US market with a Mexican brand-name may overcome cultural marketing barriers. Finally, Mexico's enthusiastic pursuit of foreign investment

and trade agreements in all corners of the globe will continue to enhance its potential as a gateway to not only the North American insurance market, but the emerging global market as well.