Committee: Policy & Resources Committee – For Decision	Dated: 25 February 2016
Subject: Referendum on the UK's Membership of the European Union	**Public**
Report of: Director of Economic Development	**For Decision**
Report author: Giles French, Assistant Director of Economic Development	

Summary

This report is about the UK's membership of the European Union (EU) and seeks a view from Members on whether or not to recommend to the Court that the City of London Corporation should adopt a corporate position on the matter.

As Members are aware, a referendum has been called on 23 June 2016 at which voters will be asked to decide on the following*: "Should the United Kingdom remain a member of the European Union or leave the European Union?"*

To assist Members in this process, this report provides some broad background information on the UK's renegotiation with the EU agreed at the European Heads of Government Summit on 18 & 19 February 2016, and the City Corporation's existing position on the matter.

In addition, set out in Appendix A is some relevant opinion and analysis on the UK's membership of the EU from the Government's study of the Balance of Competencies, as well as the financial and professional services industry.

Recommendation: Members are asked to decide if the Committee should recommend to the Court that the City of London Corporation should adopt a position on the UK's membership of the EU and if so, what that position should be.

Main Report

Background

1. In January 2013, the Prime Minister, David Cameron, gave a speech at Bloomberg's headquarters in London where he committed a future majority Conservative government to an "In / Out" referendum on the United Kingdom's membership of the European Union (EU). However, the Prime Minister said in the same speech that it was not the right time to hold a referendum as, "a vote today between the status quo and leaving would be an entirely false choice". He said that the EU was in flux, and the Government had not had a "chance to put the relationship right".

2. In the last Parliament, between 2012 and 2014, the then Coalition Government conducted a comprehensive review of the Balance of Competences between the EU and the UK in all relevant areas of business, government and civil society. This review included a dedicated section on financial services and capital markets. The overall conclusion of this section of the review was “the balance of competences is broadly appropriate, but often undermined by poor policy-making”.

3. At the General Election held in May 2015, the Conservative Party was elected as a majority government, with a manifesto commitment to hold an “In / Out” referendum after negotiating a new settlement with the EU.

The UK’s renegotiation with the EU

4. The Prime Minister set the objective of negotiating a new settlement with the EU, attempting to address four key areas:

   - Economic governance: ensuring that nothing is done to discriminate against those countries that are not in the Eurozone;

   - Sovereignty: ensuring that “ever closer union” provisions “do not compel all Member States to aim for a common destination”;

   - Competitiveness: strengthening the internal market and cutting the burden of regulation;

   - Benefits and free movement: restrict in-work benefits of new migrants for up to four years.

5. The two key reforms of greatest relevance to the financial and professional services sector are *Economic Governance* and *Competitiveness*. Both of these reforms were highlighted by the Chancellor of the Exchequer at his speech in Mansion House to the Bankers’ and Merchants’ dinner in June 2015.

6. The draft deal was presented to the 28 Member States on the 2 February 2016 by Donald Tusk, President of the European Council. The draft was discussed at the European Heads of Government Summit in Brussels on the 18 & 19 February.

7. At the conclusion of the Summit and the agreement to the renegotiated settlement, the government recommended that the UK should vote to remain in the European Union. The date of the referendum was confirmed for Thursday 23 June 2016 at which voters will be asked to decide on the following*: "Should the United Kingdom remain a member of the European Union or leave the European Union?"*

Existing Position of the City of London Corporation

8. At a meeting of the Policy & Resources Committee on 27 June 2013, the following key messages were agreed to inform our engagement with EU policy makers:

   - Promote London to policy makers as Europe's international financial and business centre;
   - Explain the role of financial services in supporting the wider economy;
   - Europe needs to reform to be more competitive in the global economy;
   - Strengthen and complete the Single Market;
   - The UK needs to be fully engaged in EU policy making.The City Corporation's approach since then has been to take forward these principles, with City Corporation representatives reflecting the view of City businesses.

9. Following the conclusion of the UK's renegotiations, the agreement of those terms by the Member States of the European Union, and confirmation that the referendum will take place on 23 June, Members may consider it an appropriate time to decide whether the City of London Corporation should have a position in the referendum debate.

Conclusion

10. Members are asked to decide if the Committee should recommend to the Court that the City of London Corporation should adopt a position on the UK's membership of the EU and if so, what the position should be.

Giles French
Assistant Director of Economic Development
T: 020 7332 3644
E: giles.french@cityoflondon.gov.uk

APPENDIX A

Government's Study of the Balance of Competences – Financial Services and the Free Movement of Capital

1. Between 2012 and 2014, HM Government conducted a comprehensive review of the EU's competences. It was an audit of what the EU does and how it affects the UK. It included a section devoted to Financial Services and the Free Movement of Capital.

2. The review's Executive Summary states the following:-
   Responses to the Call for Evidence, suggest that the balance of competences is broadly appropriate, but often undermined by poor policy-making. The EU should undertake significant reform of the existing EU policymaking framework and processes, take a more proportionate approach to legislation in all subsectors, and give greater consideration to the principle of subsidiarity in retail market sectors.

3. This is supported by evidence that:

   - Access to the single market in financial services and the Free Movement of Capital provides significant benefits for the UK financial services industry and for consumers – the UK's access to the Single Market has been a reason to locate in the UK and further deepening of the Single Market would bring additional benefits;

   - There are significant weaknesses in the EU's current approach to harmonisation and policy-making - the existing policymaking framework has been inadequate for the type, volume and pace of legislation experienced in the last five years, and the quality of consultations, impact assessments and drafting of detailed rules to have not been sufficiently high;

   - Focused reform is required to ensure the success of the Single Market and justify the current balance of competences – a programme of reform is achievable and could correct current deficiencies, although wide concerns related to the development of the euro area and the banking union implied that Treaty change should remain an option, while some respondents argued for a repatriation of powers.

   - There was broad consensus in evidence and analysis that the UK financial services sector and the broader UK economy benefit from the Free Movement of Capital, which is protected by EU Treaty, and it is important that exceptions to the freedom exist only where necessary;

   - The international framework of regulatory standard has been significantly rewritten since the crisis and have provided the context for the EU's recent approach to regulation. Evidence emphasised that the UK needs to ensure it has adequate influence in financial services at both the global and EU level. There were also strong calls for the EU to ensure it facilitates access for financial services firms between EU and non-EU markets and does not adopt a protectionist approach;

- The establishment of the banking union following the euro area crisis has been considered to be necessary but concerns have been raised about the possible implications for the integrity of the Single Market and the UK's national interest. There were a number of calls for the EU to ensure that the development of the banking union does not come at the expense of Member States that choose not to participate.

The Views of UK-based Financial and Professional Services Industry

4. The following information relates to the opinions, comments and analysis of major UK-based financial and professional services firms and their trade associations in relation to the EU referendum debate.

5. Clifford Chance, the London-based international law firm, produced a report for TheCityUK in 2013 examining the alternative legal arrangements to full EU membership and the impact on the financial services industry. A synopsis of the alternative arrangements is below:

   - European Economic Area / European Free Trade Area (arrangement in place for Norway):

   - maintain access to the Single Market, but lose all legal influence over EU legislation while still having to implement most of it;

   - implement EU rules that ignore or damage UK interests (particularly in financial services as EU legislation develops);

   - own external trade policy subject to the EU's Common External Tariff rules, in particular in relation to rules of origin (ROO) requirements;

   - contribute less to the EU budget, but still pay a substantial amount;

   - permit the free movement of persons from other EEA member states.

6. Switzerland option:

   - based on 120 sectoral agreements, none on financial services (other than some access for branches and agencies of non-life insurance business) not considered viable by the EU on a continuing basis;

   - UK exports would have to comply with all EU standards;

   - Swiss EMEA investment banking business goes through subsidiaries set up in the UK.

7. Free Trade Agreements - a single agreement instead of sector by sector agreements:

    - financial services are excluded/free to regulate its own financial services sector;
    - free to conclude FTAs with third countries;
    - exports to the EU would have to comply with all relevant EU standards;
    - lose the right to influence the rules of what is currently the home market.

8. Customs Union (arrangement in place between the EU and Turkey):

    - follow decisions on tariffs made by the EU and limited to trade in goods;
    - accepting large sections of the acquis communautaire including competition and state aid;
    - reduced access to the internal market;
    - lose its right to provide services, including financial services, on equal terms.

9. The World Trade Organisation (WTO) rules - the purest form of the "out" scenario:

    - outside FTAs negotiated by the EU with 60 non-EU countries or organisations;
    - access to the EU market similar to that of Russia and China (both lack FTAs with the EU);
    - risk of losing the trading advantages for financial services as EU regulators would take all measures necessary to intervene in trade between UK, and EU financial services.

10. The models adopted by Norway and Switzerland provide for access to the Single Market, but require financial contribution to the EU budget and participation in the Free Movement of People. The other models do not provide the same level of access to the Single Market, but do not require budgetary contributions or adopting the Free Movement of People.

11. The report concluded that all of the alternatives failed to provide a satisfactory arrangement for financial services, and risked damaging them through reduced market access and a loss of influence in shaping regulatory policies.

Importance of ‘Passporting’ in Financial Services within Single Market

12. Many of the financial services firms located in the UK identify ‘passporting’ as a key benefit of EU membership. This is the ability of businesses authorised in the UK, of whatever national origin, to offer services across the other 27 EU Member States on the same terms as in the UK. The passport enables service providers that are authorised in one EU Member State to offer services in the rest of the EU without seeking separate authorisation from other National Competent Authorities. This has enabled cross-border transactions, payments and investments.If UK-based firms were to lose the benefit of the passporting regime, they would lose the automatic ability to supply services in the EU from the UK.

Business for Britain report “Change or Go: How Britain would gain influence and prosper outside an unreformed EU”

13. In June 2015, Business for Britain, a group of Britain’s business community who want to see fundamental changes made to the terms of our EU membership, published a report *“Change or Go: How Britain would gain influence and prosper outside an unreformed EU”*. The report examined all different sectors of the economy, and included a dedicated chapter on the possible impact of Brexit on the financial services industry.

14. The chapter on financial services concludes that there are many opportunities for the sector if the UK leaves the EU: businesses from around the world would still come to the City of London for financing options, and the UK could potentially have a stronger voice on key international regulatory bodies.

15. Other key points made in the “Change or Go” report are as follows:

    - Centres such as Frankfurt, Paris and Amsterdam have attempted to compete with London in the past and have failed;

    - UK companies are already finding ways to set up local EU subsidiaries without financial passporting;

    - It is unlikely that the EU would try to deny the City access to European capital markets, as the EU itself would be harmed;

    - Access to EU capital markets is not dependent on EU membership: a commitment to allowing firms access to capital markets is enshrined in the General Agreement on Trade and Services (GATS);

    - By leaving the EU, the UK could introduce its own consultation mechanisms on EU rules.

Facts & Figures on the Relationship between UK-based Financial & Professional Services and the EU

- The EU is the UK's biggest market for exports of financial services generating a trade surplus of £19.9 billion – over a third of the UK's trade surplus in financial services in 2013.

- TheCityUK's 2012 report "Driving Competitiveness", which examined the location decisions of 147 UK based financial services firms, identified that 40% of decision makers cited access to the EU as a core reason for choosing the UK over other centres.

- Around 35% of the EU wholesale financial services activity takes place in London.

- Twice as many Euros are traded in London as in Eurozone countries combined. Eurotrading has increased fivefold over the last decade. The UK accounts for 44% of global Euro dominated trading (up from 34% a decade earlier).

- Foreign ownership of UK financial services businesses at the end of 2014 – 489 from the US and 183 from Europe.

- All 10 of the top EU law firms are headquartered in London.

- 126 companies form other EU member states are listed on the London Stock Exchange.

- The UK attracts more foreign direct investment (FDI) than any other EU member state and financial services attracts more FDI than any other sector.

- 8,838 businesses from other EU member states have a presence in the UK (5,493 in the US); 10,142 UK businesses are located in the EU, (3,306 in the US).

- Creating a single market for digital could create an extra £250 billion in growth for the EU. The UK stands to benefit disproportionately from this boost.

- Completing the single market could be worth an additional 5% to EU GDP or as much as 8% in the long term – equivalent to between £500 billion and £800 billion. The UK could benefit by £110 billion or £4,100 per a household.

- The UK's share of EU trades:
    - 78% of Forex turnover
    - 74% of interest rate OTC derivatives
    - 85% of hedge fund assets managed
    - 64% of private equity funds under management
    - 59% of international insurance premiums

Views of Senior Practitioners in UK-based Financial & Professional Services on UK Membership of the EU

The following quotes from senior practitioners of the financial and professional services sector and their trade associations on the UK's membership of the EU is intended to be representative of the balance of opinion, but not an exhaustive list of all comment.

Trade Associations

- The Association of Foreign Banks: *"believes that the UK's interests, with regard to financial services, are best served by continuing to be an inner member of Europe and by helping to develop its regulatory framework."*

- Alternative Investment Management Association (AIMA), Jiri Krol, Deputy Chief Executive: *"I would disagree with the fact that there is some kind of benefit to the hedge fund industry emanating from Brexit."*

- Association of British Insurers, Huw Evans, Chief Executive: *"The risk of a British exit from the European Union is causing major political uncertainty for the insurance industry."*

- British Bankers' Association, Anthony Browne, Chief Executive: *"Membership of the single market has served the British people well for decades. Now is the time for intelligent reform, sensitive legislation and closer engagement from the UK to ensure that we can continue to profit from the EU for many decades – if not centuries – to come.*

- British Insurance Brokers' Association: *"A British exit from the EU would be disadvantageous overall to the insurance broker sector" because "it would lead to uncertainty for businesses which would have an adverse impact on the insurance market, investment and customer groups and the existing system of insurance companies 'passporting' into the UK could cease, potentially leading to a reduction in choice for UK consumers."*

- Investment Association, Guy Sears, Interim Chief Executive*: "Leaving the EU would complicate doing business without significantly cutting compliance costs."*

- The Law Society of England and Wales produced a report in October 2015 which stated: *"Even in the short term, the position is unpredictable. Uncertainty will, itself, have a business impact, as clients and business decision-makers seek to mitigate their risks."*

Financial Services Firms

- Standard Life, Sir Gerry Grimstone, Chairman, one of the UK's largest pensions groups, said: *"We believe that access to the EU Single Market is in the best interests of our customers and clients. The principle behind the Single Market – to encourage the free movement of goods and services – has created an environment that gives individuals and businesses the confidence* *to invest for the long term and it would be potentially damaging to the UK economy and therefore to companies such as Standard Life if the UK were to leave it".*

- HSBC, Douglas Flint, Chairman: *"I think business has a responsibility to speak up on economic matters. The evidence is that Britain has benefitted from being in the EU. Britain is stronger in a reformed Europe and Europe is better with Britain."*

- HSBC, Stuart Gulliver, Chief Executive: "If the UK leaves the EU it could have a significant impact on our non-ring-fenced bank … a number of jobs would leave the UK. I could imagine 20% of those [5000 jobs] would move to Paris."

- Goldman Sachs, Gary Cohn, President: *"I think for the UK it's imperative to keep the financial services industry in London. I think that having a great financial capital of the world staying in the UK and having the UK be part Europe is the best thing for all of us."*

- Morgan Stanley, Colm Kelleher, President: *"Were Great Britain to leave the EU, you would see significant backlash against London as a global financial centre."*

- Barclays and TheCityUK, John McFarlane, Chairman: *"Our opinion is that the City will be significantly worse because the rest of the world wants Britain to remain in the EU."*

- MMC, Dan Glaser, Chief Executive: *"I absolutely think it would be a big mistake economically, politically and strategically for the UK to leave the EU."*

- JP Morgan, Jamie Dimon, Chief Executive: *"Britain's been a great home for financial companies and EU membership has benefited London quite a bit. We'd like to stay there, but if we can't, we can't."*

- Lloyd's of London, John Nelson, Chairman: *"I can't emphasise too strongly the importance of the UK's relationship with the EU, not only for Lloyd's but also the rest of the UK economy."*

- Woodford Investment Management, Neil Woodford, Founding Partner: *"It is plausible that brexit could have a modest negative impact on growth and job creation. But it is slightly more plausible that the net impacts will be modestly positive."*

- Newton investment Management, Helena Morrisey, Chief Executive*: "On the contrary, I have great confidence that Britain and the British people could thrive outside the EU. I am not afraid that all will be lost. Indeed, I am confident we have much more to gain from the outward-looking, entrepreneurial spirit that has long defined us, than if we stay bickering, fighting and losing within a passé political structure that is wholly unnatural to us."*

- ICAP, Michael Spencer, Chief Executive: *"I am a Eurosceptic, but if he (David Cameron) gets a fair deal I can still envisage us staying in."*

- UBS, Alex Weber, Chairman: *"I don't think it would completely undermine the financial sector of London.The UK would probably be able to negotiate a favourable deal giving it access to the single market." [WSJ Nov 2015].*
  "The UK will have limited access to the EU's financial services if it leaves the Union. Firms would have to consider moving employees so that they can deal with clients who are EU-located." (LSE Jan 2016)

- Schroders, Michael Dobson, Chief Executive: *"As far as Brexit is concerned, I wait to see what is on the table when the referendum comes round. I think it unlikely we will vote to leave. If we do, we will reach an accommodation with the EU after a couple of years, one that works for both sides. Talk of economic suicide or catastrophe is very wide of the mark."*

Opinion Polling

The following opinion polls illustrate the position of the UK-based financial and professional services sector and other relevant business constituencies.

- TheCityUK, Ipsos Mori, 2015 (Senior leadership of financial services firms):
  - 84% Remain in the EU
  - 84% EU membership important for UK competitiveness
  - 10% Leave EU, but remain in Single Market

- Institute of Directors, EU Survey, 21 February 2016:
  - 60% Remain in the EU
  - 19% More likely to vote Remain since the EU Agreement
  - 54% EU Agreement makes no difference either way
  - 42% Would vote to remain in the EU anyway

- British Chamber of Commerce, 2015:
  - 63% Remain in the EU
  - 27% Leave the EU

Giles French
Assistant Director of Economic Development
T: 020 7332 3644
E: giles.french@cityoflondon.gov.uk