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| Committee | Dated: |
| Public Relations and Economic Development Sub-committee – for decision | 14 December 2017 |
| Subject: Future EU/UK trading relationship in financial services | Public |
| Report of: Damian Nussbaum | For Decision |
| Report author: Dan Turnbull, EDO | |

Summary

The International Regulatory Strategy Group has proposed that the UK should seek a deep and comprehensive Free Trade Agreement, including financial services, as the basis for the future trading relationship with the EU after Brexit. This paper seeks your approval to use the Corporation's key spokespeople, and the efforts of EDO officers, to promote the IRSG's proposals with key decision-makers during this crucial period.

The proposal respects the position of both the UK and the EU. Taking the UK and the EU's aligned regulatory regimes as a starting point, access should be based on mutual recognition and regulatory co-operation; it should deliver mutual market access rights as close as possible to those currently available.

In particular, the proposed approach includes:

- Mutual market access to be maintained, subject to ongoing regulatory alignment.
- A Forum for Regulatory Alignment as the EU and UK develop their rules.
- A system for supervisory cooperation, clarifying roles and responsibilities.
- A shared dispute resolution panel, which would rule on whether material divergence had occurred under the FTA (crucially, this would not be the ECJ).
- Material divergence means loss of access only in the affected area, not right across financial services.
- A degree of certainty for firms, with build-in procedures and timelines for withdrawal of access, or complete withdrawal from the FTA.

We now propose to engage with key UK and EU decision-makers, through a full engagement programme deploying the Lord Mayor, Chairman of Policy and Chair of IRSG.

Recommendation

It is recommended that Members note the content of this report, and approve the policy stance and engagement strategy it proposes.

Main Report

Background

1. The UK's vote to leave the European Union, has created considerable uncertainty about how UK-based Financial and Professional Services firms will be able to access the EU market, and vice versa, after Brexit. Currently, UK firms make use of "passports" across a wide range of financial services activities, allowing UK-authorized (i.e. licensed) firms to serve customers in the EU without need for further authorisation in the host country. The consensus view is that membership of the Single Market is a necessary condition for benefitting from passporting; given HM Government's position that we will be leaving the Single Market, the strong expectation is that passporting for FPS firms will fall away.
2. The high level of cross-border business conducted by UK-authorized firms inside the EU means that the question of what will replace passporting is very significant. In a low-access scenario, firms would need to establish subsidiaries inside the EU, and supply them with sufficient capital, liquidity and senior staffing to satisfy local regulators. This fragmentation would impose costs on firms that would need to be passed on to investors and/or customers, making UK-based firms less competitive compared with firms in other global financial centres.
3. The International Regulatory Strategy Group – a senior practitioner-led group co-sponsored by the City of London Corporation and TheCityUK – has considered this issue through a series of three reports, culminating in A New Basis for Access to EU/UK Financial Services Post-Brexit, published on 26 September. This report argues that the UK should seek a deep and comprehensive Free Trade Agreement with the EU-27, including financial services. Taking the UK and the EU's aligned regulatory regimes as a starting point, access should be based on mutual recognition and regulatory co-operation; it should deliver mutual market access rights as close as possible to those currently available.
4. In particular, the proposed approach includes:
 - Mutual market access to be maintained, subject to ongoing regulatory alignment.
 - A Forum for Regulatory Alignment as the EU and UK develop their rules.
 - A system for supervisory cooperation, clarifying roles and responsibilities.
 - A shared dispute resolution panel, which would rule on whether material divergence had occurred under the FTA (crucially, this would not be the ECJ).
 - Material divergence means loss of access only in the affected area, not right across financial services.
 - A degree of certainty for firms, with build-in procedures and timelines for withdrawal of access, or complete withdrawal from the FTA.
5. Engagement that has taken place regarding the IRSG proposal is set out in the Appendix.

Current Position

6. Currently the UK Government and European Commission are engaged in a negotiation around the “Phase 1” issues: the UK’s financial settlement, the rights of citizens and the status of the Irish border. If the European Council on December 14th-15th judges that sufficient progress has been made against these issues, discussions can formally turn to the future EU/UK trading relationship.

Proposals

7. The proposal has been broadly welcomed as the most significant intellectual contribution to thinking on the future EU/UK trading relationship by any sector, although it is recognised that it is an ambitious proposal, which will be politically challenging to achieve.
8. Planned future engagement regarding the IRSG proposal is set out in the Appendix.
9. We therefore recommend that Members adopt the IRSG proposal and associated engagement strategy. This approach is favoured by the IRSG, and reflects the current of opinion within the UK-based FPS sector.

Corporate & Strategic Implications

10. This work is the key project that EDO is pursuing to deliver against its Business Plan objective to achieve the best possible outcome from the Brexit negotiations and can be achieved with existing resources.

Conclusion

11. No issue is more vital to the short-to-medium-term competitiveness and performance of the City’s FPS sector than the post-Brexit access agreements with the EU. We therefore recommend that you support the adoption of this policy, and the use of the City’s key spokespeople and resources to promote it with decision-makers as we enter the most crucial phase of the negotiations.

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