Written evidence submitted by the City of London Corporation (FSMB45)

FINANCIAL SERVICES AND MARKETS BILL

PUBLIC BILL COMMITTEE

KEY MESSAGES

1. The City Corporation's 'State of the Sector' report, produced in partnership with the Treasury, records that the UK is perceived as having the world's preferred regulatory regime for financial services. The report notes the importance of three characteristics that support the UK's attractiveness as a global financial centre that the regulatory environment is
    a. agile,
    b. coherent,
    c. and competitive.

2. The report notes key statistics on the importance of the sector, it:
    a. accounts for 12% of the UK economy,
    b. contributes well over £70bn annually in tax revenue,
    c. provides one in 14 of all UK jobs, or a total of 2.2 million people, two thirds of whom are employed outside London across the regions and nations of the UK. A map showing the distribution of jobs is annexed to this briefing.

3. The City Corporation welcomes the Bill as it contains a number of pragmatic measures to enhance openness, innovation and competitiveness. The City Corporation[1] welcomes proposals to ensure that regulators exercise their new powers in the service of public policy objectives set by Parliament that maximise the industry's contribution to society.

4. As part of the transition process from EU to UK regulation, the Government and the regulators should provide commitments on
    a. the type of the rules that might be changed during transition,
    b. that changes will be subject to consultation,
    c. and indicate the minimum consultation period.

[1] The City Corporation is coordinating its response to the Bill with the leading financial services trade associations and representative bodies, including those in the banking, investment, insurance and fintech.

5. The City Corporation welcomes moves to build, in collaboration with industry, a robust regulatory regime for digital assets. The Bill’s approach, which broadly reflects the successful use of sandboxes elsewhere, would allow designated firms to trial new clearing and payment technologies in temporary pilot schemes.

6. Moves to support digital innovation on distributed ledger technology (DLT) are welcomed. This is a good example of policy nurturing innovation and therefore helping the UK maintain its international competitiveness.

7. The UK’s regulatory framework is internationally well regarded and makes a positive contribution to the UK’s standing as a global financial centre. In this context, the Bill’s targeted changes are broadly welcomed. In contrast, wholesale changes to the regulatory architecture could disadvantage the attractiveness of the UK as a financial hub.

8. A secondary competitiveness objective has been a long-standing priority for the sector. The City Corporation supports the Bill’s introductions of a secondary objective which is framed to support a strong regulatory regime whilst helping to promote the UK as a global financial centre.

9. As a secondary objective, economic growth and international competitiveness will remain subordinate to the goals of promoting competition, preserving stability, and protecting consumers. Regulators will advance secondary objectives so long as this supports their primary objectives.

10. Secondary competitiveness or growth objectives are common in sophisticated and mature financial centres. Regulators in Australia, Hong Kong, Japan, the EU, Canada and the United States have analogous objectives, for example.

11. The Cost Benefit Analysis panel is a welcome and important reform in regulatory decision-making.

12. Mutual Recognition Agreements, which are intended to simplify trade and regulatory arrangements between two or more countries, are

important to the UK's future trading arrangements. It is important to have a swift method of implementation in domestic law. For instance, the MRA with Switzerland is a top industry priority.

13. The Bill's provisions on net zero are positive steps and a way of supporting the UK's attractiveness in green services and products.

1. THE STATE OF THE SECTOR

a) Financial services is a global industry. From a UK base it provides a wide range of services to customers and clients both domestically and across the world, helping individuals to manage their finances and businesses to raise capital and manage risk.

b) The UK-based financial and related professional services industry is a significant national asset, accounting for 12% of the UK economy, contributing well over £70bn annually in tax revenue, and providing one in 14 of all UK jobs, or a total of 2.2 million people, two thirds of whom are employed outside London across the regions and nations of the UK[2].

c) The City Corporation consider that the realignment of the UK's financial services regulatory architecture offers a once-in-a-generation opportunity to become more nimble, agile and proportionate [3]. The UK's framework for financial services regulation is internationally respected and plays a major role in the UK's attractiveness for global businesses. With market-leading ideas such as regulatory sandboxes[4] and open banking, the UK has been a pioneer in embedding innovation in regulatory frameworks[5]. The opportunity should now be taken to ensure the regulatory framework in the UK stays agile, coherent and competitive, while delivering better outcomes for consumers and businesses[6]. Seizing this opportunity requires expert and professional regulators with adequate resourcing and efficient supervisory processes.

[2] State of the Sector, Pages 17, 45, 46
[3] Ibid Pages 27,30
[4] Ibid Pages 7, 27
[5] Ibid Page 33
[6] Ibid Page 27

2. **TRANSFERRING RETAINED EU LAW TO WITHIN THE REGULATORY PERIMETER (clauses 1-7)**

   a) The Government's intention is that many of the provisions in retained EU law (and therefore currently part of the regulators' rulebooks) will be replaced by UK regulators directly into their rulebooks, rather through legislation.

   b) The Bill provides provide the Treasury with a wide-ranging power to "restate" part of retained EU law into either primary or secondary domestic legislation. As an example, key definitions that make up elements of the financial services regulatory framework might be "restated" under this power. The Bill places some limits on this power, for example the power can be used when the purpose of a modification is to protect and enhance the stability and integrity of the UK financial system, or when a modification would promote the safety and soundness of financial services firms. Moreover, the Bill requires that the reason for a modification must be closely allied to regulators' objectives.

   c) Subject to certain safeguards, the broad objective of moving retained EU law onto the UK regulators' rule books is positive as it should make it easier to create rules bespoke for the UK financial services sector.

   d) Clarity and predictability are important to the UK's attractiveness to global institutions. The Government should give four commitments at an early stage of the parliamentary process:
      - To provide a full explanation of the limits of the proposed power,
      - To describe the consultation process that will be used prior to any rule change
      - Indicate that there will be minimum duration of each consultation
      - Be transparent about the sequencing and timing of the rules being transferred.

3. **INNOVATION**

   a) The Bill proposes several changes regarding use of new technologies in financial services, with a focus on cryptocurrency. The City Corporation welcomes moves for the UK to build a robust regulatory regime for digital assets, in collaboration with industry.

***Regulatory sandboxes* (clauses 13-15)**

b) The City Corporation supports proposals to establish regulatory sandboxes for financial market infrastructure (FMI) to allow firms to experiment with new technologies and practices. This sandbox approach is modelled on the existing FCA Regulatory Sandbox, but designed for FMI. In particular, it is intended to allow testing of the use of Distributed Ledger Technology (DLT) by FMI. The Bill does not make any changes to the FCA's Regulatory Sandbox.

c) This move will help the UK to remain at the forefront of the next wave of digital innovation on DLT. It is a good example of policy nurturing innovation and therefore helping the UK maintain its international competitiveness.

d) The City Corporation has a strong track record of running sandboxes in partnership with the FCA. Between November 2021 and March 2022, in partnership with the City of London Corporation, the FCA ran a second digital sandbox pilot focused on solving data and disclosure regulatory challenges related to Environmental, Social and Governance.

***Regulation of stable coins* (clause 21)**

e) The Bill will create a new category of 'digital settlement assets' which includes stablecoins and other crypto assets and brings them within the payment and electronic money system. Reflecting sandboxes used in fintech and elsewhere, designated firms will be allowed to trial new clearing and payment technologies in temporary pilot schemes.

4. REGULATORY FRAMEWORK

a) The UK's regulatory framework is an important factor in making the UK an attractive global financial centre. Business passes through the UK and entities base themselves in this jurisdiction because, in part, of the UK regulatory arrangements. In this context, policy stability is an important aspect of international competitiveness, and it is important to have a targeted approach to change. Taking this approach should help to maintain investor confidence.

b) Wholesale changes to the regulatory architecture would, however, disadvantage the attractiveness of the UK as a financial hub.

c) A critical part of the Bill is the implementation of the earlier Future Regulatory Framework (FRF) Review. The Review's proposed changes, including on the UK prospectus regime, capital raising on public markets, and secondary market rules, were positively received by the industry as maintaining high standard regulatory frameworks while supporting competitiveness[7].

d) An overarching consideration in relation to regulatory architecture is the importance of policy stability and regulatory independence. These factors are important to the UK's international competitiveness as a financial centre. These aspects of the Bill will help to address the issues raised in the [Corporation's benchmarking study](https://www.theglobalcity.uk/PositiveWebsite/media/Research-reports/CoL-Our-global-offer-to-business.pdf)[8] which stated that: "Financial services executives world-wide perceive the UK as having the most favourable regulatory regime for financial services…However, facing global challenges, the UK's government needs to return to being perceived as more predictable, stable, and strategic."

***New international competitiveness and growth objective for the PRA and FCA*. (Clause 24)**

e) The most important element of the FRF, and the Bill overall, is the introduction of a new international competitiveness and growth secondary objective for the PRA and FCA. Regulators will be required to give primary importance to the existing objectives of promoting domestic competition, preserving stability and protecting consumers. The secondary objective set out in the Bill will be advanced by regulators where is supports the primary objectives. This will require the regulators to promote, subject to aligning with relevant international standards, the international competitiveness of the UK economy (including, in particular, the financial services sector) and its medium to long term growth.

[7] Ibid Page 25
[8] https://www.theglobalcity.uk/PositiveWebsite/media/Research-reports/CoL-Our-global-offer-to-business.pdf

f) This approach is welcomed as it seems probable that the proposal will enhance the UK's reputation for strong and predictable regulation and give firms additional confidence to invest. High quality, well implemented and effective standards are key components of the UK's competitive advantage as an international financial centre.

g) The UK's pre-eminence as a financial services centre - and the associated tax and employment benefits that brings - should not be taken for granted. Whilst the UK is a major international hub, financial services firms are free to choose where they will be based. A secondary competitiveness objective is, therefore, timely as it will help to support the UK's international position as a global financial services centre.

Regulation and competitiveness

h) Regulation is an important determinant of competitiveness. Regulators already have an obligation under the Financial Services and Markets Act 2000 to have regard to the desirability of sustainable growth in the UK economy in the medium or long term, but this does not require them to consider the effect of their interventions on international competitiveness.

i) Competition, consumer protection and financial stability should and will remain the clear primary focus of the regulators. A secondary growth and international competitiveness objective will ensure they are incentivised to create proportionate rules that promote the UK in comparison with other global financial centres, to the benefit of the economy and consumers alike. The secondary competitiveness objective will help to ensure that the cultural approach of regulators acknowledges that regulatory decisions effect the economy and the international competitiveness of the UK's financial services sector. In turn, this will enhance the UK's reputation for strong and predicable regulation. The move is also welcomed as it should support regulators to consider innovation, the cost of doing business and consumer choice.

j) Regulators should set out in a public document and to parliamentarians, at regular intervals, how they have balanced potentially competing objectives. Regulators should face parliamentary scrutiny on how they implement the objectives.

International Precedents

k) There are many international examples of regulatory competitiveness objectives. Regulators in other countries regularly manage consideration of international competitiveness and/or economic growth without undermining their core mission of competition, financial stability and consumer protection.

l) Relevant financial regulators in Australia, Hong Kong, Japan, and the United States have competitiveness or growth as a regulatory objective. Canada's statutory objective is formulated as protecting the interests of consumers while having due regard to competitiveness. The European supervisory authorities – the European Banking Authority, the European Securities and Markets Authority and the European Insurance and Occupational Pensions Authority – are each required to take due account of the impact of their activities "on the Union's global competitiveness". Many of these jurisdictions have adjusted their regulatory objectives and their implementation of them since the global financial crisis without abandoning competitiveness as a key objective.

5. NET ZERO (Clause 25)

a) The Bill introduces a new regulatory principle for the FCA and the PRA, requiring them to have regard to the need to contribute towards achieving compliance with section 1 of the Climate Change Act 2008 (for the UK to achieve Net Zero by 2050).

b) The UK remains the only global financial centre that leads in both conventional and green financial centre rankings. The Bill's proposal should, therefore, help to develop and strengthen the UK's attractiveness as a market where global participants can find the fullest spectrum of 'green' services and products.

c) The City Corporation supports the net zero ambition and recently held a Net Zero Delivery Summit designed to:

- Maintain momentum on key policy initiatives for finance from COP 26;
- Present as best practice, the role of FPS in helping the wider economy achieve net zero;
- Secure London's role as a strategic leader on sustainable finance.

d) Voluntary Carbon Markets could be an important contributor to net zero. At scale, a liquid voluntary carbon market (VCM) could allow billions of dollars of capital to flow from those making net zero commitments into the hands of those with the ability to reduce and remove carbon, significantly contributing in the transition to net zero. The City Corporation is leading the development of VCM by:
   - serving as the secretariat to the UK Voluntary Carbon Markets Forum.
   - being selected as a founding sponsor of a new governance body for VCMs, The Integrity Council for Voluntary Carbon Markets (IC-VCM). The IC-VCM launch marks a significant step towards high-quality and scaled VCMs.

6. COST BENEFIT ANALYSIS (CBA) PANEL

a) The Bill requires the regulators to publish statements on their approach to CBA and to require the FCA and the PRA (with the Bank) to establish new panels to support the development of their CBA.

b) This is an important and welcome reform as it will require the use of cost benefit analysis in the decision-making process within the regulators. The move will help keep the UK an attractive financial services centre in relation to the cost of doing business.

7. OPENNESS: Mutual Recognition Agreements (MRA)

a) The Bill gives the Treasury a power to make changes to domestic legislation necessary to ensure that MRAs can be fully implemented, using secondary legislation. This includes the ability to grant any additional powers to the financial services regulators that are required to give effect to MRAs.

b) Because MRAs are designed to improve joint working between regulators, they should reduce the cost of doing business and produce more cost effective client offerings. It is understood that this aspect of the Bill will be used at an early stage to implement the MRA on financial services which is currently being negotiated with Switzerland.

c) Currently, finalising the MRA with Switzerland is a key industry priority. The MRA represents a genuine opportunity to develop a gold-standard bilateral financial services relationships based on mutual recognition. It will bring UK and Swiss governments, regulators, and firms together forming a deeper financial services partnership. The MRA will embed high regulatory standards.

Office of the City Remembrancer
October 2022

APPENDIX 1. Employment in UK based FPS

Figure 2: Employment in UK-based financial and related professional services, 2020

Source: TheCityUK calculations based on data from Nomis and the Northern Ireland Business Register and Employment Survey