



Select Committee on the European Union

Sub-Committee on EU Services

Uncorrected oral evidence: Financial services after Brexit

Thursday 29 October 2020

10 am

[Watch the meeting](#)

Members present: Baroness Donaghy (The Chair); Lord Bruce of Bennachie; Lord Cavendish of Furness; Baroness Couttie; Lord McNally; Baroness Neville-Rolfe; Baroness Prashar; Lord Sharkey; Lord Thomas of Cwmgiedd; Lord Vaux of Harrowden.

Evidence Session No. 1

Virtual Proceeding

Questions 1 - 13

Witness

I: Sir Jonathan Faull, Partner and Chair of European Public Affairs, Brunswick (Brussels).

USE OF THE TRANSCRIPT

1. This is an uncorrected transcript of evidence taken in public and webcast on www.parliamentlive.tv.
2. Any public use of, or reference to, the contents should make clear that neither Members nor witnesses have had the opportunity to correct the record. If in doubt as to the propriety of using the transcript, please contact the Clerk of the Committee.
3. Members and witnesses are asked to send corrections to the Clerk of the Committee within 14 days of receipt.

Examination of witness

Sir Jonathan Faull.

Q1 The Chair: Good morning. Welcome to the EU Services Sub-Committee's public evidence session as part of its ongoing inquiry into financial services after Brexit. This session is being broadcast on parliamentlive.tv and a full transcript is being taken and will be made available to you to make any corrections shortly after the session.

I welcome Sir Jonathan Faull to the meeting. I, as Chair of the Committee, will open with the first question. How important is achieving a deal to the UK financial services sector and what progress has been made in negotiations on financial services in recent months? There have been comments in the newspaper that up to £1.2 trillion of investment has already gone to other capitals in Europe. Over to you, Sir Jonathan, and welcome.

Sir Jonathan Faull: Thank you and good morning. It is very important that an agreement be reached in respect of financial services. If you are asking whether that will happen, I frankly do not know. I do not think anybody knows at the moment. It seems that a great deal of effort has been devoted to goods, customs issues and tariff issues, which, of course, are not directly relevant to services or to financial services in particular. It is an important economic sector in its own right and it is an important driver of the economy more widely in the United Kingdom and the European Union. So it is important. There are mechanisms in place, however unsatisfactory some of them may seem, which provide for some links even in the absence of an overall agreement, but at this stage we simply have to wait and see what transpires in the next few days and weeks.

The Chair: Thank you very much. How would you comment on some of the newspaper reports at the weekend about the amount of investment that is already going to other European capitals in the uncertainty?

Sir Jonathan Faull: There has been a long period of uncertainty and financial institutions have had contingency plans. Clearly, some of them are now implementing some aspects of those plans. There are some activities that are relatively easy to move from one place to another, and that has been happening. There is no single city in the European Union with the financial services capacities of the City of London, but there is a wide range of cities with considerable experience of parts of them; I think of Paris, Frankfurt, Dublin, Amsterdam and Luxembourg. All those places have seen some activities moving that until now have been conducted in London.

Q2 Lord Sharkey: Good morning, Sir Jonathan. Earlier this week, UK Finance's head of Brexit said that a positive EU equivalence determination for CSDs was probable in the next couple of weeks, but went on to say that, outside that and the existing extension for the clearing houses, we are unlikely to see more come to fruition.

What would be the consequence for the financial services sector if the UK failed to secure positive equivalence determinations from the EU?

Sir Jonathan Faull: In any area not covered by an equivalence decision and not covered by some other sort of general agreement, the consequences would be that the suppliers, the providers of those services, would have to comply with two different sets of rules as they diverge in the coming months and years. There would be British rules in the UK, European rules in the EU, and no obvious bridge between them; there would just be two separate jurisdictions. That would create additional cost and friction, and no doubt it would create some further displacement of activities and would be harmful in the sense that the situation that we have known for the last decades, which still prevails today, would simply disappear and be replaced by a wholly different one.

There are various types of equivalence and various types of financial service to which equivalence rules are applied, and some say there should be more. Sometimes, confusingly, there are related issues—we may come to them later—such as adequacy, which is another Euro word used that does not sound very good to English-speaking ears.

There is also a system of recognition of foreign jurisdiction rules for data transfers. Many financial services these days are data driven and require data transfers, so that is another area that will need careful attention.

Lord Sharkey: Could you point us to parts of the financial services sector for which the lack of an equivalence decision is likely to have dramatic consequences?

Sir Jonathan Faull: Quite simply, the passport for banking services, which provides that if you meet the rules for obtaining a banking licence in one country you can branch out from that country into the other 26 now—27 when we were still members—requires something like an equivalence determination. There are wide areas of share trading and insurance where, without an equivalence determination, there will be friction.

Q3 **Lord Bruce of Bennachie:** The issue of equivalence has obviously been central to the discussions for the whole period of negotiation. The political declaration specifically quotes that the future relationship “could include appropriate consultation and structured processes for the withdrawal of equivalence findings, to facilitate the enduring confidence which underpins trade in financial services”.

That looks like a positive declaration, but the fact is that, at the moment, the EU has a unilateral right to terminate any equivalence agreement within 30 days, which pretty well everybody who has given evidence to this Committee has said is untenable as a practical working basis. How important is it that there should be a properly negotiated process of applying or disapplying equivalence? What chance do you think there is of that being secured?

Sir Jonathan Faull: It is very important, extremely important. The abrupt change in the terms or, indeed, withdrawal of equivalence can have devastating effects, and nobody should want that to happen. You need agreement of a governance system and a structured form of regular dialogue so that both sides know what the other is intending to do in advance. Above all, you need mutual trust; you need confidence in each other. I do not want to make a polemical or political point, but trust has been impaired recently. It will be very important across the board, but in this area as well, to restore high levels of trust at all levels.

The sort of dialogue you need goes from, if I may say so, people such as yourselves, Parliament to Parliament, Government to Government, Ministers to Ministers. Equally important in a way, however, is financial supervisors to financial supervisors. These are people who, within the EU framework, met via NetMeeting all the time, met their British counterparts all the time, got to know each other, were seconded from one place to another, had often studied together and had common concepts, languages and objectives. That needs to be maintained or restored somehow, and people need to talk to each other, not only the Europeans and the British but more widely across the world.

Lord Bruce of Bennachie: Are you aware of the extent to which those kinds of discussions have been prioritised? You make a valid point about the mood music and the atmosphere, but the Committee gets a lot of evidence that suggests that there is a lot of detail going on behind the scenes and a lot of very confrontational rhetoric out in the public domain. Do you have any insight as to whether, from either side, there is a serious desire to get to a better place of trust and understanding? We have had comments from the EU in the last few days that it does not know what the UK's intentions are and that that makes it difficult. What is your take on where we are with that and what the chances are?

Sir Jonathan Faull: I do not know what is going on behind the scenes—by definition, I am not behind the scenes—but I am perfectly sure that the regulators, the supervisors and the central bankers all want to do their jobs together in the interests of financial stability, as they have been throughout the crises of recent years. I am sure no one would say, “We want to have a bust-up”, but it might happen inadvertently. A great deal of attention will need to be given to the forms of governance surrounding not only the wider relationship but, in this particular area, the administration of this equivalence system or whatever it may be called. It is of great importance to the financial sectors themselves, and it is also of great importance politically for the wider relationship.

Lord Bruce of Bennachie: It has had difficulties with Switzerland, and one of the arguments has been the worry that giving the UK some kind of special arrangement, given the importance of the City, might open up demands from other third countries. Do you think that is a consideration for the EU, or might what you have just said about the importance of working together trump that?

Sir Jonathan Faull: I hope it will. Relations with Switzerland below the surface—or behind the scenes, to use your expression—have continued to be reasonably good over the years. There have been political issues between the European Union and Switzerland, but the Swiss financial sector is important—obviously not as important as the British—and there are Swiss financial institutions trading all over the EU and vice versa. Ways can be found to pursue a harmonious relationship, and they will have to be found in this case.

Q4 **Lord Vaux of Harrowden:** You covered this to quite an extent in the previous question, but it goes beyond just the pure equivalence side of things. What is your view on the UK and EU proposals for regulatory co-operation? How do you think the future regulatory dialogue should be structured?

Sir Jonathan Faull: There are various models. There is the Swiss model and there is the EU-US model. When I was working in this field in the European Commission, we had regular meetings with foreign countries. Those meetings had all sorts of different names, but “structured dialogues” are sometimes what they are called. They will be necessary and will need to be regular, friendly and frank, and they will need to have some understanding about what happens if things go wrong. It should not be beyond the wit of the people concerned to devise sensible arrangements.

The politics will be what they are, the framework agreements will be what they are, but people will continue to have to deal with each other. There are financial institutions with considerable activities in one place and the other, so the supervisors have to work together. These people will meet in all sorts of meetings in Basel, in New York—when people can actually start meeting again; I hope soon—in the infernal, eternal round of discussions in the international financial world. The British will no doubt continue to play an important role in that and the Europeans, too.

Lord Vaux of Harrowden: You mentioned the Swiss model and the US model. What do you think are the relative merits of those two approaches?

Sir Jonathan Faull: They are fine as far as they go, but the EU-British relationship is a different one. The UK was a member, it is very close, and it is a major financial centre. European countries and European companies are used to dealing with, in and through the City of London. So I do not think you can take one of these models and just replace Switzerland with the United Kingdom.

It will be sui generis to a certain extent, but the fundamental issues are simple. People need to meet regularly and need to have some confidence in each other. They need to be given some leeway by their political leaders to talk to each other and to suggest changes where they think they are necessary. There will be confidentiality issues, as there always are, but as far as I know they are always respected. They need to be able to say, “We are considering doing X, Y, Z. We are minded to do X, Y, Z.

We'd like to discuss with you the impact of that on you and what you might do in response".

If those dialogues work properly, given the interpersonal relationships that exist already, I think some measure of confidence is justified.

Q5 Baroness Prashar: Good morning, Sir Jonathan. Building on your previous answer, what do you think are the key risks and opportunities for potential regulatory divergence after the transition period?

Sir Jonathan Faull: The risks—they are not hard to think of—are friction, delay, rows, spillovers of rows to other areas, and obstacles to trading access where there were lower obstacles, if any, before.

What opportunities are there? Well, seeing what other ideas might work, diversification of activities and geographical markets. A lot of that is possible already. The EU system is not really a straitjacket. The City of London prospered during the UK's membership and the UK has been in a leadership role in many of these fields internationally and in Europe.

There are risks and there are some possible advantages. One thing we can say for certain is that it will be different. Brexit as it is consummated will be an undoing of integration at the stage it reached in 2019-20.

Baroness Prashar: Will the risks be the same if we are not totally following the rules but aligned to the regulatory framework?

Sir Jonathan Faull: They would be different if we were aligned. Of course, there would be the risk that we—we British, I am now saying—would be taking rules in the making of which we had had very little say, and historically we have had a huge say in the development of European rules. We would be taking rules that had not been thought through in a British way or with the interests of the City of London. I keep saying City of London, but I mean the British financial sector more generally; I am aware that it is not only London. So alignment without participation in the process is obviously an uncomfortable and risky process.

Could you repeat the second part of your question? I am sorry.

Baroness Prashar: If we were aligned, what are the risks and opportunities in that area?

Sir Jonathan Faull: The opportunities coming with alignment will, I assume, be ease of access. Something like the access to European markets, which was enjoyed as a member, will be available to British exporters of financial services.

Q6 Baroness Neville-Rolfe: It is very good to see you again, Sir Jonathan. What is your assessment of the Financial Services Bill introduced on 21 October and the financial services future regulatory framework review, which is in a consultation paper published last week? Do you agree with the Minister, John Glen, that we need to ensure that our regulatory regime has the agility and the flexibility to respond quickly to emerging

challenges and to seize new global opportunities, a sentiment that I think was behind some of those documents?

Sir Jonathan Faull: Who could be against agility and the ability to react to events? I must admit to a slight concern about a competitiveness criterion in financial services legislation, because the balance between being competitive and ensuring financial stability is a delicate one. Whatever legislation ensues will have to be very clear in the remit it gives to the regulators and supervisors in that respect.

That, in a way, anticipates what I imagine will be a subsequent question. The balance between parliament, government, financial supervisors, regulators and authorities is a delicate one. It is different from place to place and different from time to time, and, of course, it depends on the constitutional structure of the country or jurisdiction concerned.

The UK has a balance. The UK had a balance as an EU member state to which it contributed. It is now striking out on its own and will have to find a new balance in a rather changed and difficult world. We have had a major financial crisis very recently and we are probably in or having another one of a different nature now as a result of Covid-19 and the economic consequences thereof, in so far as we can see them yet.

So, yes, the UK has an opportunity provided by the reconstruction of its financial architecture after Covid-19 and after Brexit. I think the issues are well known. There is no off-the-shelf, simple template to be used, but, to repeat myself, the balance between your House, the House of Commons, Her Majesty's Government and all the regulators, who is giving instructions to whom, who is accountable to whom and what ends up in the courts and what does not are very important issues at the design stage, which will have untold consequences in the future.

Baroness Neville-Rolfe: Thank you for that. As you say, we will talk a little bit more about scrutiny.

Could I loop back on to this balance point, which I very much agree with? We have financial regulators who have shown themselves to be quite effective on the stability agenda and, indeed, helped Brussels to develop that across the EU. However, there are, as we know because we have had evidence from them, smaller financial services operations, perhaps not operating across the EU, and it is important that their dynamism and growth is supported.

Is there some potential there in this domestic legislation and, if so, are there any criteria or suggestions that you would give us to try to pursue in that wider interest? Jobs in financial services stretch right across the UK, as you said earlier.

Sir Jonathan Faull: It is a time of change. There is the digital challenge opportunity for the financial sector. One big decision that needs to be made is whether one has rules applicable to all financial service providers, whatever their size, or whether one has a threshold and rules

for the big ones that are different from the ones applicable to the small ones. Those are very important issues.

Obviously, the international implications are extremely important for the big ones and less important for the small ones, although the small ones will hope to grow and no doubt grow overseas in due course. I suppose the consumer protection issues will be the same for all of them, but perhaps the capital requirements, for example, will not be the same for all of them.

There are opportunities to think again about this, and no doubt the European Union over in Brussels will be doing something similar at the same time as the UK is charting its own course. This is another reason to have a dialogue between the two of them, because if they go too far apart there will be friction.

Baroness Neville-Rolfe: Thank you very much. I could not agree with you more about the need for dialogue, which is a point that EU Committees have made often.

Q7 Lord Thomas of Cwmgiedd: I want to return to this question of a balance, with a particular focus on the power that is being given to the regulators and what Parliament should do to ensure that they are held to account for the rules they develop and the way they enforce them.

I will ask you a very broad question first of all. What views do you have about the Government's wish to delegate so much more to unaccountable regulators?

Sir Jonathan Faull: There are a few principles that should be uncontroversial. Financial legislation can never anticipate all the challenges which those charged with implementing it have to face. Even your House, with its enormous store of wisdom and experience, will never produce—and should not seek to, by the way—perfectly detailed legislation applicable in all foreseeable, or indeed unforeseeable, circumstances. A margin will always be left to regulators.

You used the word “unaccountable”. How accountable or unaccountable they are is a matter of political choice in the design of the system. In some places, parliaments have a say in the appointment of regulators, have regular hearings with them and seek to constrain or at least to influence their activities quite considerably; in other places, less so. That depends on the tradition and constitutional arrangements of the country, but there are various ways of doing it.

What you want to have—this is easy to say and very hard to achieve—is the agility on the part of the regulators and supervisors to cope with what can be emergencies on a Sunday afternoon and things having to be done before the markets open. I say “markets open”, but that is very old fashioned; markets are never closed these days. They need to be fleet of foot when they have to be, but they need to be fleet of foot within parameters that are set by democratic systems, politicians and parliaments. This is all very trite, and the design devil is in the detail. It

will seem satisfactory and need correction at various times along the road and, if I may say so, you should build in correction possibilities so that things are not cast in stone for ever.

In 2008, 2009 and 2010, when I was representing the European Commission in Basel and all the international bodies where people came together to deal with the financial crisis, we thought when we were doing well that we were leaving our great-great-grandchildren with a toolkit to deal with the next crisis. Actually, the next crisis may be happening in our lifetimes, within a few years of the one that we thought we were dealing with, and it is already clear that some of the things that were done in the heat of the years following the financial crisis of 2008 need to be looked at again.

Building some flexibility into the parliamentary framework for which you are responsible seems to be a very sensible approach.

Lord Thomas of Cwmgiedd: Drawing on your own experience of dealing with the European Parliament in these areas, what would you advise us to look for in proper parliamentary scrutiny of the dialogue and of the regulators' activities?

Sir Jonathan Faull: I can tell you what the European Parliament does. It has and seeks a greater say in the appointment of people to these bodies. It is concerned about their professional qualifications. It is concerned about their diverse origins and, of course, the European Union is a complicated place with 27 countries. It hauls the leaders of the supervisory and regulatory bodies back into committees, sometimes even into plenary sessions, for discussions and interrogations, followed up by all sorts of further requests in writing.

On the part of the regulators and supervisors at the European level, there is a sense that they are accountable to the European Parliament, not in their daily activities but for the major policy-related determinations which they find they have to make.

Lord Thomas of Cwmgiedd: Thank you very much. We had better move on to someone else. I have a lot more I would like to ask you, but there is no time.

The Chair: You can always ask a supplementary. Any member who feels that there is something they would like to ask can email the clerk.

Sir Jonathan Faull: I do not know whether you provide for this, Chair, but if there is provision for writing answers to questions, I would be happy to do so.

The Chair: Excellent, thank you very much. Lord McNally has lost his connection. We will have to come back to him.

Q8 Lord Cavendish of Furness: Thank you, Sir Jonathan. I have learned hugely from what you have told us this morning, for which I am grateful. A recent report on the future UK-EU relationship in professional and

business services found that these sectors have been largely overlooked in the future relationship negotiations. What do you think the knock-on effects of this might be on financial services?

Sir Jonathan Faull: As I said initially, I think the focus has been on physical goods for the time being, and perhaps it has taken longer to conclude the negotiations on those aspects than people initially thought it would.

One way of answering your question is to say that if there is no agreement and there is a certain bitterness in the relationship, it will make life very difficult from 1 January onwards. If there is an agreement, even if it does not cover financial services explicitly, there is reason to hope that the good will that will have been created—and, to be honest, the relief that Brexit has a chance at least of leaving the front pages and becoming a matter of normal business between the British Government, the European institutions and the member states—will be helpful in dealing with the nuts and bolts of equivalence, adequacy and all the other things we have talked about in a new balanced relationship in which both sides can consider that they have things to gain. A lot depends on the outcome of these negotiations and whether they deal with financial services. If there is a setback, there will be a setback in the overall relationship.

Lord Cavendish of Furness: Doing my homework, I saw an interview you gave in March 2019 in which even then you pointed to the prioritising of goods over financial services. First, do you think there has been quite a lot of catch-up and, secondly, do you think there is a perception that financial services have such agility they can look after themselves?

Sir Jonathan Faull: Some people might think that. Of course, they are less visible and less spectacular. There are no lorries at Dover and there is no customs official in the middle of the channel stopping a financial service. There may be a tendency to think that it is all about pressing a button.

One of the extraordinary things I learned from the beginning of this whole Brexit process was how services are nearly as proximity dependent as goods. I sort of understood intuitively that most countries in the world traded in goods mostly with their neighbours, but it turns out that in services, even though we are talking about pressing buttons rather than shifting physical goods, there is also a considerable proximity factor.

If I knew that, I think everybody knew that, and no doubt the Brexit talks have taken longer and made less progress than was initially hoped. The focus has been on physical goods, customs, tariffs and what happens at a border. You can stand at a border all day and you do not see a financial service coming through. If people settled for that and put services to one side, I think they were making a mistake.

I think there has been progress in the last six, nine, 12 months. People continue to talk to each other. There have been helpful unilateral moves

on both sides to keep financial services flowing, but there is still a lot of work to be done. It is also true that within the European Union itself—and the British were always the first to remind their European counterparts of this—the European Union made progress on goods and has achieved largely a genuine internal market for goods but that is certainly still not true of services. It is still pretty hard to provide services. I am not talking only about financial services. Try sweeping chimneys in Germany if you do not have the right paperwork.

The Chair: Lord McNally, have you managed to reconnect?

Q9 Lord McNally: Yes, I hope so. Sir Jonathan, you will be very surprised to learn after that experience that I was Minister for Data Protection for three years.

Sir Jonathan Faull: You were protecting your own data very effectively there.

Lord McNally: During that period, I saw just how much influence we had, not in my skills but in the skills of our officials, in creating the GDPR. We pretty smoothly transferred it into British law. Evidence from Ministers on committees I was on two years ago said that data adequacy would be like flicking a switch; it would be so smooth that it would not really be a part of the negotiations at all.

However, in the last few months it all seems to have soured, and some of the evidence we have had from Ministers has been that it will be all right on the night. How important is a positive data adequacy decision for the financial services industry? Stephen Jones of UK Finance said, “Many financial institutions, banking and otherwise, rely on cross-border data flows, and therefore data adequacy designations in both directions are very important”. Was he right?

Sir Jonathan Faull: Yes, he was. Data are the coal and steel of the 2020s. If the EU was starting out today, that would be its primary focus, I am sure. Financial services are data driven. Every company in almost every sector engaged in any sort of international activity is transferring data across borders all the time without necessarily realising it, so it is of huge importance. It is also, of course, of huge importance to the general public, consumers and citizens that data be properly protected. You can argue about where balances are struck and whether a particular piece of legislation strikes a balance correctly, but it is a very important area.

The EU is very proud of its data protection legislation. It is not simply a policy choice. The Europeans say that it is a fundamental right and a fundamental value. You are right, Lord McNally, that the British contributed quite considerably to the development of that policy and that legislation. It comes with this “adequacy” notion, which is a bad translation from French, a so-called false friend, by the way. “Adequate” to our ears sounds just about okay. In French, “adéquat” means something like appropriate or suitable. I remember arguing about this with the Americans, who were terribly insulted when I told them that we had to assess the adequacy of their data protection rules.

It is very important that the UK remains part of the European data protection area. The European system, which is the equivalent of equivalence, is adequacy, which means at the moment that the Europeans look at the foreign country's rules and determine whether they are good enough. If they are, the data flow and, if they are not, the data do not flow.

The problem with that—this has been very controversial in recent years—is that data are also of enormous importance to law enforcement and intelligence communities. There is a great deal of very useful evidence to be found in all the data that we generate about ourselves and our activities all the time. The role of the state through its law enforcement and intelligence agencies in having access to data in certain circumstances is, unsurprisingly, controversial. There have been difficulties in the EU-US relationship, and I am afraid there are likely to be issues in the EU-UK relationship, but they need to be sorted out. We are all members of NATO. The UK is a European country facing the same challenges as the other European countries in so many areas. It would be tragic, counterproductive and foolish for the data protection issue not to be sorted out.

Is it being used as a bargaining chip in the wider negotiation? I cannot rule that out. I do not know. The simple answer to your question is that this is a very important issue and it is essential that agreement be found.

Lord McNally: Most of the Ministers we talk to and a lot of opinion is that it is of such overwhelming mutual self-interest that it is really a no-brainer. It may be being used as a bargaining chip—well, you have more experience than me of EU brinkmanship—but, on the other hand, we have all seen Theresa May, from her experience of security when she was in the Home Office and from her premiership, pulling faces of disbelief behind Michael Gove when he assures us again that it will be all right on the night. Do you think the security issue will be the real blocker to adequacy and that the other is simply mutual self-interest?

Sir Jonathan Faull: I hope it is not, because I think the common security interest is very important as well as all the other economic interests, but that is just me speaking. It is very important. Things that we may think of as no-brainers sometimes happen or do not happen when we think they should, and these negotiations have an emotional side to them, as we have seen, which can get out of hand. Things have happened in the last five years that, frankly, I would have said were no-brainers and would not happen at any stage throughout those five years.

I am not sanguine about it. I think it requires hard work and attention. I am sure the security communities on both sides are determined that their co-operation should continue and they have some influence over their Governments, but at the end of the day the negotiation is an overall settlement and they are still talking.

Q10 **Baroness Couttie:** Good morning. We have talked a great deal this morning about the importance to the financial services sector of getting a

deal, and I think everybody in this Committee is entirely behind that. In the scenario where we do not get a deal, do you think that there are some potential opportunities for the UK perhaps to strengthen regulatory co-operation with other key global financial centres, maybe even to take a leadership role in developing common global standards?

Sir Jonathan Faull: I think the UK has a leadership role in developing global standards, which it had throughout its membership of the EU. I saw it with my own eyes—a leadership role both within the EU and as a member of the EU in the wider world. I do not think that needs to be found or restored, because there is already a strong tradition with it.

Obviously, if there is no deal between the UK and the EU, both sides—sticking to the financial services sector—will have to rethink how they regulate financial services and how they obtain financial services—where they buy them and where they sell them. That goes to the structure of European banks. It goes to the way in which securities derivatives are cleared.

If I may add to your question, if there is no deal but everything stays the same for a considerable period of time, perhaps things will calm down. If there is no deal followed by deliberate divergence, or accidental or inadvertent divergence, reactions on both sides will set in, people will begin to do business in different ways in different places, and coalitions of leadership in the international bodies in which so many of these standards are set will be different.

I am not making a Brexit point—it is too late for that—but the UK in the international bodies where I saw it at work was comfortably part of the European club and part of the Anglosphere club, with very close relationships with the Americans, the Canadians, the Australians and the Europeans—and, where necessary, talking to the Chinese and the others as well.

That leadership role would be different, but apart from the overall impact on the economy, on the pound and on the standing of the City of London—there would be an effect on all of those—there is no reason why the UK should not continue to contribute greatly to the way in which financial services are regulated, supervised and produced, bought and sold across the world.

Baroness Couttie: What you basically said in that response was that you do not think there will be a diminution of the UK's influence in working with other regulatory bodies across other countries. Do you think that there may be potential opportunities for the UK with other global markets? Currently, obviously we are working across the globe in our financial services, but do you think there will be greater opportunities, having come out of the EU, or do you think that that will have no real material impact?

Sir Jonathan Faull: I do not think that membership of the EU impeded those international opportunities, so I do not see why they should be

greater or better. They are there and the record shows that they are there. The City of London is an international trading centre; it is not only a European one. A lot will depend on the overall standing of the country, its economy, and its international relations. It will be different, but I do not think it will create new opportunities that could not be created today.

Baroness Couttie: Not even with perhaps free trade agreements on financial services with third countries, which obviously we would not be able to have currently because of our relationship directly with Europe?

Sir Jonathan Faull: I do not want to turn back the clock in any way. As a member state of the European Union, the British were very important players in the European trade negotiations, particularly in respect to financial services. So what was possible was possible then, too. The UK may, in its trade agreements as a non-EU member, be able to secure opportunities which the EU is unable to secure. Clout counts for a lot in this world, and the 27 as a whole offer in international negotiations—as the 28 did—a sophisticated market in producing and consuming financial services. It is not an easy thing to do, but it cannot be ruled out hypothetically.

The Chair: Sir Jonathan, if you have time, we have two supplementaries from members of the Committee.

Sir Jonathan Faull: With pleasure.

The Chair: Thank you very much.

Q11 **Lord Vaux of Harrowden:** Sir Jonathan, I want to ask a little more about divergence. There is a tendency when we talk about divergence to think about it as being something the UK will do away from Europe, but divergence obviously goes both ways. Since we are not going to be at the table to influence the direction the EU takes any more, do you see areas where the EU is likely to diverge that might impact on our industry?

Sir Jonathan Faull: Yes, definitely. I think that the EU without us will be a different place, and is already becoming a different place with different policy objectives. This is speculative, of course, but one can certainly speculate about the EU's desire to build an autonomous sovereign financial sector around its common currency, the euro, which may lead it to regulate financial services in ways that would not have been possible or at least as easy with the UK still at the table and, of course, not taking account of UK concerns.

That said, the UK was not alone in its positions around the EU table and was usually quite masterful in husbanding coalitions and majorities for some of the things it wanted. There is a tendency to think that Europe is Paris or Europe is Paris and Berlin. It is more complicated than that, but there will be divergence. The buzzwords of autonomy, sovereignty, reshoring, onshoring, and building European capacity are all over Brussels, and I think decisions are already being made that might have been different if the UK had still been at the table.

You are absolutely right, Lord Vaux, that divergence is a two-way street. It will be deliberate on both sides, it will occasionally be inadvertent on both sides, and it will require very hard work to make sure that it does not create unnecessary friction in the relationship. I am not one of those who think, although I respect the intellectual argument that the euro was the great game changer, and once Europe, or most of it, had the euro as a currency, the UK simply no longer had a place, because inevitably EU financial services policy would be geared to defending, sustaining and promoting the euro.

I think the record shows that the UK, by dint of hard work, fought its corner very successfully in the design of financial regulation with the City of London and the pound sterling outside the eurozone. I do not think there is any deterministic inevitability about that, but now that we have gone, the risk of divergence on both sides is very considerable.

Lord Vaux of Harrowden: Are there any specific areas within the sector that you are particularly concerned about where you see divergence coming from that would impact on us?

Sir Jonathan Faull: There are people who want to build a European capital market, a European capital markets union, a capital market sector. There are people who want to bring about through mergers the creation of a large eurozone-based investment bank to rival the big American, British and other investment banks. There are all sorts of policy instruments available that can go some way to achieving that process.

It is not smooth; there is no unanimity. and we have to see what the world looks like when we emerge from Covid-19. Nobody knows yet when that will be or what that world will look like. But we will be doing these things separately now, and unless we get the bridges right there are considerable dangers of divergence sending us off into a world of friction and the fragmentation of financial markets and of capital, ultimately to the detriment of the economy for all of us.

Q12 Lord Thomas of Cwmgiedd: Sir Jonathan, maybe you could help us with this in writing, but I assume that in your position after 2010 you were heavily involved in dealing with the financial fallout of the crisis of 2008-09 and the necessary changes that had to be made to the capital adequacy requirements.

I would greatly appreciate, and I think we might find useful, guidance as to the way the Parliament interrelated with the Commission and the Council in developing policy nationally and internationally, and the role the Parliament played when that policy came to be put into directives. Obviously, it was a very important series of events, and as we may face the same in a year or two, it would be useful to have some feel of the influence Parliament had and its ability to take into account the kinds of considerations that Baroness Neville-Rolfe made of trying to make certain that different sectors of the economy, particularly SMEs, were taken into account. I would be very happy if you could write something, if that is not

too great a burden.

Sir Jonathan Faull: I would be delighted to. Very briefly, there is an international level of international organisations—the Financial Stability Board—where there is considerable concern that there is not much parliamentary scrutiny, or much transparency even, about their operations. These are central bankers and senior treasury officials meeting often on Sunday afternoons, usually in Basel—at the time, nobody ever thought we would not be meeting in person. A lot of the standard-setting work is done at that international level. Then it comes back down to individual countries or jurisdictions—the EU for the EU, where it has competence in the area—and the normal legislative process takes place involving parliaments.

However, it has to be said—this is controversial, of course—that, a lot of the time, the principles, and indeed some of the details, have been agreed internationally and parliaments are simply told by executives, “We’ve agreed to that, and the question now is how to do it. We can’t go back and undo it very easily”.

There is an accountability democratic problem there. I was the senior civil servant. My commissioner—the equivalent of a Minister—my staff and I would appear regularly before parliamentary Committees, and at the member state level the same thing would be happening before the national parliaments. I was not always sure whether parliaments found that satisfactory.

Then, of course, the detail, which is often mind-numbingly complicated, with pages of algebra, calculations and so on, is the subject of the legislative process, often in a hurry.

Lord Thomas of Cwmgiedd: Obviously that was a huge experience, and it would be very helpful, Sir Jonathan, as long as it is not too much of a burden for you, to see how it worked in practice in that last great crisis, possibly in preparation—we hope not—for the next one in a short order of time.

Sir Jonathan Faull: Will someone contact me and explain how I should do it and to whom I should send it?

The Chair: We will certainly do that, but we are inviting you, as a Committee, to add anything you want arising from Lord Thomas’s question or from any other areas that were raised.

Q13 **Lord Cavendish of Furness:** I am rather haunted, Sir Jonathan, by the status of our diplomatic voltage after we leave. After all, we have to rebuild a relationship with the EU but also with the individual countries. You cannot invent diplomats overnight. Do you think we have enough strength in that department for the next year or two?

Sir Jonathan Faull: I am not sure I am the right person to judge that. I am quite impressed by and proud of the diplomatic voltage, but it needs to be rechannelled and there are big changes under way and coming.

Most of the diplomats I have known in my now 42 years in Brussels have spent time here, in home departments and in embassies overseas, in Washington and in central banks, and have networks of contacts garnered throughout their careers that prove extremely useful. We will miss some of that now. Bank of England staff will not spend a few months inside the European Commission or vice versa on secondment, which used to happen all the time.

The British diplomatic core is of high calibre; it has a fine reputation. We speak what has become the world's language, we write it reasonably well most of the time, but we will have to rebuild relationships, networks and, to a certain extent, reputation. The last five years, frankly, have not been great. Without making a polemical point, the internal market Bill, which I think is before your House at the moment, has raised concerns across Europe and more widely.

There is a job to be done. It should not be taken for granted, and we should look again, no doubt constantly, at the way our diplomats are recruited and trained, where we send them and what sort of experience we want. They need to be financially savvy as well as doing war and peace.

Lord Cavendish of Furness: Do you think the culture of the Foreign Office is currently right for that task?

Sir Jonathan Faull: I am afraid I will duck that one. I have never worked in—what is it called now?—the Foreign, Commonwealth and Development Office. I have many friends who I admire enormously who have and do, but I really cannot judge its culture very well.

The Chair: Sir Jonathan, we have benefited greatly today from your experience and your knowledge. You have covered all the areas and we are very grateful to you. We will drop you a line about the areas of follow-up that Lord Thomas asked. Thank you very much for your time.