

European Scrutiny Committee

Oral evidence: Regulating after Brexit, HC 125

Wednesday 3 May 2023

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Members present: Sir William Cash (Chair); Richard Drax; Margaret Ferrier; Mr David Jones; Greg Smith.

Questions 156-165

Witnesses

I: Charlotte Clark CBE, Director of Regulation, Association of British Insurers; Barney Reynolds, Partner and Head of Financial Institutions, Shearman & Stirling LLP; Kerstin Mathias, Regulatory Affairs and Policy Director, City of London Corporation.

Examination of witnesses

Witnesses: Charlotte Clark CBE, Barney Reynolds and Kerstin Mathias.

Q156 **Chair:** Good afternoon. It is very nice to see you here. Thank you for appearing to give evidence. We have an expert panel of witnesses for today's session, and we are hoping to gain a better understanding of post-Brexit UK financial services regulation, and of how and where the UK has freedom to regulate differently after Brexit. We also intend to look at how, if at all, the UK's financial services sector has been impacted by post-Brexit changes in international co-operation, including losing EU equivalence. We will also explore whether the UK's finance sector has enough international influence outside the EU to become an international leader on regulatory reform. We will also look at one or two other areas. The Windsor framework has of course recently been agreed, but we shall touch on that only in passing, if we have time. Before we get started, for those watching at home would you briefly introduce yourselves?

Barney Reynolds: I am Barney Reynolds, a partner at the global law firm Shearman & Sterling. It is US headquartered. I am based in London, and I co-head the financial institutions business, which is about half the firm's business.

Charlotte Clark: I am Charlotte Clark, the director of regulation at the Association of British Insurers.

Kerstin Mathias: Good afternoon. My name is Kerstin Mathias. I am the director of regulatory affairs and policy at the City of London Corporation.

Q157 **Chair:** Thank you very much indeed. I shall ask the first question. What is the potential impact of the Financial Services and Markets Bill, and the planned revocation of retained EU law in this area?

Barney Reynolds: Generally, it moves inherited EU legislation, because EU regulation was done at a legislative level, into the regulator rulebooks for the regulators to manage going forward, so it is largely an empowering Bill. It does some other things, but that is the main thing that it achieves. Obviously, that does not mean that the outcome is going to be what is desirable. There is a lot of work to be done subsequent to that by the regulators in combing through the rulebooks, removing unnecessary rules, and re-couching things in a more calibrated way to business, which is needed to complete the job. The Bill enables that, and I think is welcome.

Charlotte Clark: We are very supportive of the Financial Services and Markets Bill. I will not repeat what Barney said about what it practically does. Where there are advantages, bringing in wider objectives to the regulators on things like competitiveness and growth should bring benefits, partly because as regulators they are taking on greater responsibility. The ability to balance public policy decisions, if they are essentially the rule-making body, is crucial to make sure that we get the right balance between protection, financial stability, competitiveness and growth. In terms of the specifics of the Bill, there is a lot of responsibility. Obviously, it is brought back to the UK. Some of it sits with Parliament. A

lot of it sits with the regulators. One of the things that we have been challenging and discussing as the Bill goes through is whether the framework is right for accountability and transparency. One of the big themes is how this will actually work in practice.

Kerstin Mathias: I strongly agree with what has been said so far. We are also very supportive of the Bill. It is a very good piece of legislation. The one thing that I would also like to draw your attention to is the new structure that it creates for how we regulate the industry in the UK post Brexit. As Charlotte said, a lot of new powers are moving to the regulators, which in principle is a good thing because it will allow us to benefit from the enhanced flexibility and agility that we will now have post our departure from the EU. The other side of the coin is that we need to make sure that there is sufficient accountability for that flexibility, and that we use it in the right way. I guess that that is in part what we are here to discuss.

Q158 **Greg Smith:** Good afternoon. Can you take us through what progress the UK Government have made so far in terms of new regulation in the financial services area, and what impact it has had on the sector?

Barney Reynolds: Lots of small changes have been made—small in the scheme of things—that accumulate to make quite a significant change. There have been lots of welcome steps. I can list them all, but to shortcut that, embedded in the statutory system that we have, and that we will have under the new Act, there is a consultation process. The Government and the regulators have been consulting on changes. Today we got some of the listing rules. There have been proposed changes to Solvency II. Any of these changes involves a proposition, and soundings being taken from the industry and users of the markets. Basically, I think the system works on that, so that has all been good.

To frame it in the wider context, there is an awful lot more to be done if we are to get back to where we need to be, in my view, which is a very competitive City. To get to that there needs to be more real examination of the inherited *acquis* and a finetuning of it for today's markets. Some of that is going on. For instance, the markets are shifting. Assets are becoming digitised. There are proposed new rules. There is a proposed new scheme for that, which is welcome, but a thorough look is needed not only substantively, which is what has started and needs to carry on in earnest—I think the Government and the City Minister have been doing a good job on that—but in terms of method.

As soon as the regulators have their powers, they need to be combing through and redrafting things on a common law method, which basically involves far fewer rules, with the same high standards if not higher, which you can achieve with much more predictability as to how the rules operate. A lot of them are poorly drafted at the moment. Why does that matter? It is because a lot of the competitiveness of the City comes from the ability of firms not to have to go and ask permission from a regulator, but to look at a rule and say, "I understand that I can't do that, but I can do the rest of these things." That is where we need to get to.



To finish the picture on that, getting back to the regulator accountability point that has been flagged, which I agree with wholeheartedly, in my view the solution is to bring the courts back into the regulatory system, so that regulators are obliged to apply the rules that they make in a predictable way. That would be fixed by making minor changes to the processes and rules around the upper tribunal. Case law precedent would fill in the detail of how some higher-level regulator rules, such as the consumer duty or integrity, apply in practical situations; we get that from our case law system. That can be brought into the system by allowing largely private disputes between consumers and firms to be heard in a forum that creates precedent. That would mean a minor adjustment to the ombudsman scheme to make it an adjudication scheme, and introducing, as per the recommendation of the Treasury Committee, a first-tier tribunal that creates precedent. Once you have that, you will have fewer rules and legal certainty. Then I think you will start seeing some real results.

Greg Smith: Thank you. Charlotte, from the insurance perspective?

Charlotte Clark: In terms of progress, it would be quite difficult to change the rules until the Financial Services and Markets Bill got Royal Assent. Obviously, for us the big debate has been around Solvency II, changing the rules there, and diverging from what the EU does. I am sure that we can get into that in a bit more detail, but until the Bill is passed, changes to the rules cannot take place.

As Barney says, there is an awful lot of consultation on different areas. The whole Treasury programme around smarter regulation, and its approach to replacing EU law in tranches, and to prioritising, makes a lot of sense. It is a mammoth task, going through the whole of financial services regulation and thinking about the areas where you might want to diverge, and where alignment is better. I don't think any of us will say that we want to rush that. It will take careful thought; we have to ask, "Right, how do you do that?", and try to get the benefits of divergence, if at all possible.

Kerstin Mathias: I would agree. Government has looked to move at pace, and that is welcome, but it has resulted in, I think, 143 initiatives on something called the regulatory initiatives grid, which is what all the financial services regulators annually publish. While change is welcome, and it is right to look into where we can make changes so that the system works better for the UK, we need to bear in mind that there is only so much capacity for change in the system, in both the private and public sectors. We do not want to rush the reviews and ultimately end up with an outcome that is not right because there were too many initiatives happening at the same time. Prioritising is absolutely crucial. We strongly believe that there are two areas that we should prioritise, because they are where we see the greatest growth potential: the area of sustainable finance regulation, and anything to do with technology and information.

Chair: Thank you. I ask David Jones to ask questions 7 and 12.

Q159 **Mr Jones:** Kerstin, you have already partially answered my question. I



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was going to ask you how and where the UK should diverge from EU financial services law. Also, should any particular retained EU financial services laws be kept?

Kerstin Mathias: To start with the first question, on divergence, I am not totally sure that that is the right way to look at the matter, because it assumes that one system is static and the other is moving, and of course that is not the case. The UK and the EU, and frankly any other regulatory framework in any jurisdiction, are evolving. We are all evolving in parallel as we look to solve many similar problems. We are solving them in different contexts, and that is why sometimes a different approach is justified and necessary. There isn't, I'm afraid, a very clear answer, yes or no, on divergence, because we need to look at issues case by case, and make the decision that is right for the UK market and the actors that operate here.

Secondly, the UK has the most international financial services sector. That is fantastic, and we should be very proud of that. In part, that is because our internal market is much smaller than that of our greatest competitor, the US, but we are none the less the greatest international financial centre, and that is the mindset that we need to apply as we look to protect, enhance and grow the competitiveness of the sector. That does also mean that we need to pay greater attention to what our competitors are doing, and to what some of these international businesses that will be operating not just in the UK but in the US, Singapore and elsewhere would like to see. Many of them would like to see coherence in the framework, because it simplifies doing business in a global industry.

Charlotte Clark: As to areas where divergence would be helpful, we have already mentioned Solvency II. The purpose of the divergence is not for its own sake; the UK insurance sector is different from the insurance sector in the EU, and a lot of our insurance has to do with long-term savings. Clearly, we have a general insurance market as well, but so much of where the money is and the importance of the investment side of Solvency II is in the long-term savings market, which is different from how it would be in the EU.

Other areas where I think divergence would be helpful are the rules around advice and guidance—the definitions are very fixed within EU law—and thinking about what UK consumers need in getting advice and guidance, whether that is personalised guidance or trying to make sure that they get the right products rather than those that are necessarily specified in regulation. There is something like PRIIPs, which is also on the list for consideration. There are areas such as disclosure: how do you give people information, and what is the right way of giving people information? Barney mentioned the consumer duty. That gives an overarching responsibility to firms, or it will do when it comes in, to make sure that customers have the right understanding. There are also things like very specified disclosure rules: while some of them will be necessary, that is an area that I think could be looked at.



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You asked about which ones could be kept. There has to be a purpose to divergence. Kerstin made the point that this is a global industry and we do not want cost for the sake of cost, so divergence really has to add something. One of the other points to make is that the UK was very influential in designing financial services regulation. We were by far the biggest financial services market in the EU, and so a lot of the things in those regulations are things that we have argued for over many years. It is about making sure that we are looking at those areas where divergence makes sense to the UK market and to UK consumers.

Barney Reynolds: I think the method is key. When we talk about divergence, many of the standards in the EU acquis that we have inherited are standards that we set; it is just that they are written out in a way that is not our way. I would not dispute the need to comply with many of those standards, but we can do it differently. What we should be doing is looking at encapsulating those desired outcomes in the fewest words possible and applying them consistently. I agree we need to be careful to go through our normal processes of consultation and do everything properly. I do think we can and should move faster, and we have taken a long time to get to this stage. It is a long gestation period, and we are starting to see some changes, but I think we now need to see an awful lot more flowing through. This is just the beginning.

We need more regulator efficiency. One of the other differentiators with other places around the world is not just the rules, but the supervisors. In most countries, the supervisory quality is very low. We have got very high-quality supervisors. That, and not just the rules, is a selling point for the market. The supervisors need to up their game in terms of being quicker and more efficient in processing things and deciding whether to accept or reject an application, because that has become a bit slow.

In making all these changes, we should not be looking over our shoulder. We have set the standards, some of them in conjunction with the US, but generally around the world for financial services we have been at the core of many choices. The reason for that is the customers come to the market, and they come to where their money is looked after in the safest and most predictable way. It is not without any risk at all—they recognise that things can go wrong—but generally in a sensible way. That is where we should refocus our efforts, and the magnet, as it were, of our system will then take care of an awful lot of the rest.

I am concerned about the consumer duty and the principles, because they are too vague. Our system does not operate on the basis of vague rules. We have all sorts of debates over the ECHR where people take different views on vague rules. It causes huge problems in this country. Our system is based on much more clarity as to what is or is not permitted, and we have accepted ways of understanding things. You can debate those, and there is a whole democratic process of changing things if they are unsatisfactory. We need to apply that to these principles of regulation, because Parliament is delegating power to the regulators, and the regulators then make a set of rules known as principles that essentially



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say, "Go forth and do no evil." Nobody could disagree with that, but the financial market is unbelievably complicated, and the consumer duty is effectively a drag on innovation and business, which is in no one's interest. The solution I propose is to bring the courts in and very quickly build up precedent as to what it means, and then if the regulators see that the courts have gone in the wrong direction, they can tweak the rules.

Finally, I do not think we should be chasing equivalence by saying, "What rules would you like us to have in order to grant equivalence?" Equivalence is based within the EU scheme, and the UK was very instrumental in coming up with this whole scheme. It is based on outcomes. Monsieur Barnier himself, who rolled out a lot of these things when he was financial services Commissioner, went round saying that this was an outcomes-based regime. We should not therefore and in any event start tailoring this market's rules to someone else's scheme. We should be regulating on the basis of high standards, as we always have done. The market will come here, and then other places will want to give us equivalence in order to have access to the cheapest services from here on the basis of the outcomes we achieve. There are already decisions on equivalence for over 100 countries around the world, including Mexico, Singapore and Bermuda for reinsurance, that do not depend on identical rules to the EU, so we must get out of that way of thinking. It has been a misleading cul-de-sac that people have been led up after 2016.

Q160 Mr Jones: You have anticipated my next question, because I was about to ask you whether the financial services sector's desire to align with or diverge from EU rules has been influenced in any way by the reluctance of the European Union to grant equivalence to the UK.

Barney Reynolds: I think it has. If the EU had at the moment of Brexit offered equivalence for keeping all the same rules and working in some committee with it on new rules, the industry would have been very keen on that. The good thing is that the EU has not said that, because what some of the political stuff around equivalence has done, in a way, is force people to start thinking afresh for themselves about what our rulebook should look like. I think equivalence will then follow anyway, once the politics has quietened down. That is how I see it happening.

I am sure there are still many in the industry who hanker after the idea that we can have one single rulebook and get equivalence. I do not think it is realistic, and I do not think it is actually in the UK's interests or the City's interests. We have progressively suffered a dampening of competitiveness since before the Brexit referendum to do with this massive prescriptive rulebook—a rulebook that we were party to making ourselves, but it has dampened our competitiveness vis-à-vis New York, and we need to lift that off, think again and see the sky.

Mr Jones: Kerstin, do you want to add to that?

Kerstin Mathias: Yes, I am happy to. I agree that equivalence is not a priority for the industry at the moment. They have dealt with the consequences of the UK's departure from the EU. They have made their



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necessary investments. They have restructured where they had to, so that money has been spent. The priority is now to make sure that operating in the UK market is as efficient and easy as possible, including from the perspective of global institutions, as I said, and coherence plays a role in that. Equivalence is not a priority any more.

There are two exceptions. One is the CCP equivalence. We still have that. It is a temporary equivalence at the moment. Everyone is very, very keen to keep that, and we strongly believe it would be in the interests of UK competitiveness to keep that equivalence decision. Of course, politics unfortunately comes into play here, but it would be a very good outcome for the market to keep that. The other one is not called an equivalence decision, but it is the same principle, and it is something called data adequacy, which allows the cross-border transfer of data. The UK has currently been granted that from the EU, and in our view, that is also a very important one to keep.

Q161 **Mr Jones:** Charlotte, do you agree?

Charlotte Clark: Yes. There is probably not very much to add. Equivalence, as colleagues have hinted at, is largely a political decision rather than a practical one. The fact that we haven't got equivalence, I think people have got on with. Forces bigger than us will make decisions on whether equivalence will happen in the future, but I don't think that it is a question of slavishly following the rules in order for that to happen. It is about relationships.

Chair: Your remarks are interesting for many reasons, but I will pick up on two of them. On the question of harmonisation, there has always been a call for it. Today, as it happens, is the 39th anniversary of my entering Parliament.

Charlotte Clark: Congratulations.

Kerstin Mathias: Congratulations.

Chair: It was in 1984, and I went straight on to the European Select Committee, and I have been on it ever since. I mention that for a very simple reason: harmonisation was the keystone of the single market for political reasons because they wanted to move towards a greater degree of integration and political union—*[Interruption.]* I am going to suspend again, I'm afraid, for a Division, but I want to reflect on that, and on the interpretation by the courts.

So long as the European Court was in charge, the object of purposive rule was that of ensuring that you had movement towards a greater degree of harmonisation and political union, so the question of how we interpret EU retained law within the framework of the UK is very important. We need to change the basis of interpretation away from the purposive, which takes you towards harmonisation, and more, I would suggest, to the question of how you manage to do it by the common-law precedential system, which we call *stare decisis*. At that point, I am going to suspend the meeting for yet another 10 minutes. We will be back soon.

Sitting suspended for a Division in the House.

On resuming—

Q162 **Chair:** There was one further question I wanted to ask. There have been reports in the press that loosening any degree of financial services regulation will lead to too much risk. Looking back at the history of the City of London and asking a really big question about competitiveness, which is related to the point I was making earlier about harmonisation—harmonisation was designed to remove a degree of a level playing field, but there never was one; there was never a level playing field to speak of, because there was regulatory collusion. I am just asking the question about risk. Would you like to comment on that in relation to the Financial Services and Markets Bill? Barney, do you have any thoughts on that?

Barney Reynolds: The financial markets are unbelievably complicated, and they get ever more complicated all the time. They involve lots of different people doing different things. They are intrinsically risky, to some degree, because with more risk comes more profit and so on. People do not have to come here; they will go and make their profit somewhere else if we make it too difficult for them. I think the key is to make sensible rules that allow firms, if they do fail, to fail safely.

In the wholesale markets, we need to recognise the power of market discipline and the fact that sophisticated buyers will do a level of analysis themselves that no regulator can replicate or protect them from. They do not want to pay for the regulator to be protecting them from things; they want to be able to decide for themselves, so we need fewer rules in the wholesale sector, but focused on ensuring that firms here can fail safely and that they operate to certain basic standards. Obviously, the thing that was missing in oversight before 2007-08 was the oversight of the system as a whole for systemic risk, which needs to be there. It was actually a responsibility of the Bank of England, but essentially no one anywhere in the world was looking at the system as a whole. That must not happen again, and I do not think it will.

Then there is the retail sector, where you have customers who cannot look after themselves to the same degree and you do need more protection from risk, but the “do no evil” approach of the consumer duty is way too simple. The problem with that sort of approach is that financial firms are not going to innovate or take any risk at all with consumers in that environment, where they are effectively responsible even if something loses money. We need to allow for the fact that even consumers may lose a certain amount of money if products go the wrong way. There are different levels of things. Certain investments, like pensions, obviously cannot lose money, but certain other types of investments can be more speculative. People have small amounts in them, but we need to recognise that a system can operate where people can win big but also lose a little bit.

Chair: Charlotte, do you have any thoughts on that?

Charlotte Clark: In terms of the regulatory system, your original question was about press coverage, which seems to suggest that we want some sort of race to the bottom. That is just not true at all. Actually, the UK benefits from very high regulatory standards, and that is one of the reasons why people want to do business here.

Where we are talking about divergence, we are talking about smarter regulation; we are talking about regulation that is better focused on the UK market and its specifics. I do not think that the caricature that somehow this is lower standard than something like Solvency II—I have certainly seen articles that suggest that—is the case at all. It is about changing the rules so that insurers can invest in things that may be more beneficial to society than, say, Government gilts. It is about ensuring that the system works for the UK economy rather than sticking to the rules because those were the rules previously.

I want to make a point about the consumer duty, because we have talked about it a few times. That is not an EU rule; that is a UK Government rule. It is something that has come in since we left the EU. Just for clarification, that is not an EU issue.

Chair: Kerstin?

Kerstin Mathias: A globally leading financial centre needs a globally leading regulatory framework and globally leading supervision. That is the way it works, and we have plenty of evidence to support that statement. Do I agree, though, that we have a little bit of a problem in terms of how we approach risk in the industry? Yes, I think that is correct. The pendulum has probably swung just a little bit too far. We should have a conversation about how we might be able to better calibrate our approach to risk. At the end of the day, London is a global risk management centre; we have the expertise to manage that here, and that is what it is about in many ways. There is an inherent risk involved in taking no risk at all, and it seems like that fact has been forgotten in parts of the ecosystem. It certainly does not feature strongly enough in the debate at all.

The final point, and Barney has made this already, is that we need to strongly distinguish between wholesale and retail activity, because there is a much greater need to protect retail customers from risk. Again, it is not about no risk at all, because that is also risky.

Q163 **Margaret Ferrier:** The UK is the second largest destination for fintech investment. Do you think the UK could lead the way in devising regulations in this area without being too concerned about what is happening at an EU level? I will come to you first, Barney.

Barney Reynolds: Yes, I do think there is a fantastic opportunity for the UK here, and in fact it may be the sector that allows us to move forward into our traditional way of doing things, as it were—moving forward to go backwards—quickest.

There is an element of luck in it, but we moved very slowly on fintech, or crypto and digital assets. We moved thoughtfully, and we shut out a lot of



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players, many of which turned out to be rather dangerous. FTX is an example. I had better not name some of the others, because they are still in business. We shut out some people correctly. We possibly could have allowed some people in as well, more than we have done, but that does not matter much now.

In the meantime, the US allowed FTX and some other businesses to operate onshore in an environment where there was no clear regulatory regime. There has been an awful lot of litigation, with very severe consequences, and that is ongoing. The US, I think, feels burned by what has happened. I suppose the fact that the US is psychologically burned by it, the fact that they have a fragmented regulatory system where they have not agreed yet who does what, and the fact that they are so punitive in relation to some of the ancillary aspects of digital assets and so on is putting people off.

The EU has applied its code-based method. It has done that true to type, so it has come up with some new concepts: an e-money token, where the concept of e-money itself is already very slippery and difficult to apply; and an asset-referenced token, which is, again, a new and slightly vague concept where you may have to have legal opinions as to which bucket things fall into. The beauty of our system is that we do not apply that method; it is much more transparent, easier to apply and more intuitive.

The final group of countries in this scheme are the offshore centres and the wannabe centres that have produced untested rules. As FTX showed in the Bahamas, the sophistication of the supervisory element of it is questionable.

I think there is a flight to quality phenomenon. We are hearing from clients and the industry that people are now putting on hold their plans to set up anywhere else—in the EU or anywhere else—pending seeing what the UK does, and if the UK gets it right, they will come here. That is the opportunity. We are going about it in the right way. There is a thoughtful Treasury consultation out there, and as long as we put the effort in, I think we will come up with a very good system. We could do that, if we move quickly, by the end of the year.

Kerstin Mathias: I think we should be very proud of our fintech sector here in the UK. Of course, that is linked to the strength of the traditional financial services sector, but you might be aware that we currently have 10% of the global market share in fintech. We attracted \$12.5 billion of investment in 2022, in well over 500 deals. That is in part because of the regulatory approach that we have taken and the approach to encourage innovation, and maybe also coming back to what we said earlier on risk—accepting that there might be some risk in looking to encourage growth in that sector—but it has definitely paid off.

We were proud, at the City of London, to support the delivery of the Kalifa review, the implementation of which is making excellent progress. The question is now what comes next. First, I think we need to acknowledge that we now have a much more mature, bigger and more competitive



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fintech sector here in the UK than we had a couple of years ago, so we need to spend much more time thinking about how we can fund those businesses and help them to grow and scale. That is beginning to happen with an initiative such as the scale box, which the FCA is currently implementing, but there is a wider conversation that we need to have on the funding side.

Then, on the regulatory and policy side, we need to focus on the new and emerging topics, some of which Barney has already mentioned. The two others that I would maybe include are AI and smart data. If we get the framework for those right, the fintech sector will benefit, and of course other parts of the ecosystem will too.

Margaret Ferrier: Charlotte, do you have anything to add?

Charlotte Clark: Probably not. There is an insurtech sector, but it tends to be focused more on improving support for customers than on regulatory changes on things like crypto. While we certainly benefit from the fact that we have a vibrant fintech sector in the UK, it is probably less of a regulatory issue. As Kerstin says, issues like AI have pretty revolutionary impacts. How we regulate those will be quite a big challenge going forward, but I think it is the same in every jurisdiction—understanding AI, its possibilities, its risks and making sure that they are managed appropriately.

Q164 **Chair:** Good. How do you think the Government's proposed overhaul of Solvency II will benefit the insurance and reinsurance sector?

Charlotte Clark: We clearly welcomed the announcements in the autumn statement, which changed the risk margin of Solvency II. There has been lots of debate, and there is a very similar debate in the EU as to whether or not that was calibrated in the right way. The changes in the UK are likely to be very similar to the ones in the EU.

Where the UK debate is perhaps a bit more specific has been around the matching adjustment. The matching adjustment in Solvency II is about what investments can be held—when you are investing longer term, how can you hold those in an appropriate way? The proposed changes are about expanding the sorts of assets that can be held in insurers' matching adjustments. We estimate that the changes will mean £100 billion of investment in the UK over the next 10 years. We have definitely welcomed the approach.

What has not changed, though, is the way these things are calculated. At certain points the regulator, the PRA, has argued that we should be tightening up the regime. Solvency II is about the most prudential and cautious regulatory regime in the world. Trying to make it even more cautious would have been a mistake and would certainly have been to the disadvantage of the UK. Keeping the rules as they are is a good balance. It is a system that very much protects policy holders, but hopefully with the changes to the assets that can be held—one of our constant lines was that it was easier to invest in a coalmine than it was in a wind farm. Allowing

some of these changes in what can be held in terms of investment is really crucial for the UK economy and issues like net zero moving forward.

Q165 Chair: Any other comments, Kerstin or Barney? If not, I will ask a final question. Having given us the benefit of your great experience in these financial matters, do you believe that the post-Brexit financial services sector in the United Kingdom is capable of greater opportunities and that the City of London will therefore effectively maintain its position? After all, a lot of commentary goes on that is based rather more on political judgments about whether Brexit was a good idea or not, which then gets translated into negative thinking. In other words, do you see benefits as a result of what has been going on with Brexit in terms of the financial sector? We are still, I believe, No. 2 in the world to New York, and from what you have said greater opportunities appear to be prospective. Could you wind up on those thoughts?

Kerstin Mathias: We at the City of London conduct our own annual benchmarking study, which we released a couple of weeks ago. It was a tie for first position between us and New York. I know that other studies are out there, such as the Z/Yen one, which puts London in second spot. What is clear is that we are still a—if not “the”, depending on which study you believe—major financial services centre, but it is also fair to acknowledge that we have faced quite a lot of headwinds in the last couple of years. That includes covid, for instance. It also includes having to deal with the impact of new technologies and embracing that. It includes the major task of reskilling the workforce and having access to the right talent, domestically and internationally, in order to maintain this thriving international financial centre.

We have every confidence in who we are and what we will be in the future, but it is equally important that we do not rest on our laurels, and that we fight to protect and enhance what we have here. It has often been referred to as the crown jewels in the UK economy. I will be honest: it does not always feel that way when we look at the public debate and at the policy clarity and certainty that we are facing and engaging with as an industry. Those would be my high-level views.

Charlotte Clark: My remarks would be similar. The UK insurance sector is still the fourth biggest in the world after the US, China and Japan. It is probably the most global insurance sector, if you think about areas like Lloyd’s of London and others. It is an incredibly important part of the UK ecosystem, as well as the UK economy. That said, it would be wrong to suggest that there have not been headwinds over the last few years, and there is something about making sure that we are addressing those. I do not think that we can be complacent and think that our position in the world is just going to remain as is. There are improvements that need to be made. We have talked quite a lot about regulatory culture. That is one area where we have largely the right rules; it is about how we make sure that we have the right culture of regulation in the UK to make sure that financial services can thrive.

Barney Reynolds: The opportunities are huge because financial centres are centres—they are national things, ultimately, and we are sitting on the second biggest. In my view, it can easily be the biggest again. We have some very good regulators. It is a very delicate thing to be navigating through the current situation. A financial crisis is potentially brewing in the banking system of some countries. We have seen things going on in the US that are troubling. There has been a merger of the two biggest Swiss banks. That could easily spread to the eurozone and the UK. Financial business can breed contagion risk.

It is a risky environment for financial business. At the same time, we need to be competitive for the right bits of it. We must not allow the fact that there is risk around to stop us doing all the other stuff that we have been talking about, and we need efficient regulation on all topics, including what are essentially political topics, such as ESG regulation, where the EU have very much politicised it. We need to take it out of the political arena and allow market discipline as much as possible to apply, just providing disclosures for that.

The other linked point I could make is that the REUL Bill, for other sectors of the economy, is linked to our success.

Chair: You mean the Retained EU Law (Revocation and Reform) Bill, for the benefit of our viewers.

Barney Reynolds: Yes, exactly. The Retained EU Law Bill is relevant to it because really we should be doing everything that we are talking about in the financial sector, in terms of the revamp, across the inherited acquis—across the whole economy—to allow for greater competitiveness and growth. That includes looking again at topics like data and others to make sure that they are optimised and that we are as competitive as can be. I think we can go a lot further on most of those topics.

Finally, the culture of the firms, if we are going to see the full benefits of regulatory reform, needs to adjust to operate in this common-law environment that we are creating, where they are able to innovate with clear rules. That will involve a change within some large firms. At the moment, some of them are looking over their shoulder at what other firms are doing and saying, “Okay—that is the proper interpretation, but I can’t take that view unless other firms are doing it too.” It is the flock of sheep phenomenon. We need to change that as well, so that people and firms can start innovating and thinking for themselves, and taking the opportunities that arise from law and regulation to innovate and be entrepreneurial, and be even more successful for national benefit.

Chair: Good. Thank you very much for coming. It has been very interesting, and goes to show that having a good balance of interests in terms of your professional capacities helps us to understand better what is really going on in the field. Thank you very much.