HOUSE OF COMMONS

Treasury Committee

Oral evidence: The economic and financial costs and benefits of UK membership of the EU, HC 499

Wednesday 3 February 2016

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Watch the meeting

Members present: Andrew Tyrie (Chair); Mark Garnier, George Kerevan, John Mann, Mr Jacob Rees-Mogg

Questions 610 - 692

Examination of Witnesses

Witnesses: **Andrew Bailey**, Deputy Governor for Prudential Regulation, Bank of England, and Chief Executive Officer, Prudential Regulation Authority, and **Tracey McDermott**, Acting Chief Executive, Financial Conduct Authority, gave evidence.

Q610 Chair: Thank you very much for coming to give evidence this afternoon. It could not be timelier; in fact, one might say it is almost too timely, with the Prime Minister still on his feet answering questions and providing clarification on the very thing that we would like to explore with you this afternoon. The issue at stake is very large—it is right at the heart of the negotiations—which is: what protections does Britain need as a non-member of the eurozone for the conduct of its economic policy generally, and particularly for its financial services industry, which is much larger than those of other member states?

Can I begin by asking you, Mr Bailey, what protection you think is afforded by what you have seen in the Tusk document and the accompanying documents that have come with it? Perhaps you could just summarise those in a few headings and then, on the basis of your headings, we will go through them.

Andrew Bailey: Yes, I will do that. As you understand better than we do, this is very much a continuing process and a continuing negotiation; that is the first thing I would say. The second thing is that we only saw these documents when you did, which was quite well into yesterday, so we have had a bit under 24 hours to look at them. With that in mind, as you know, the Bank of England published its report on the Bank of England and the EU in the

course of last year. In that report, we made the point that there is a need for safeguards. I think that is the spirit and point of your question.

The question for all of us, then, in this context, is how effectively we think the safeguards that we think are sensible will be provided for under this. As I say, it is early; we cannot reach any definitive conclusion on this, but I can set out what, to me, anyway, are the relevant headings. I would set out a number. There is no significance to the order, by the way. I would start with subsidiarity which, of course, is the subject of one of the draft declaration documents. There is a one-page document in there on subsidiarity. I think that is important because—

Q611 Chair: If you do not mind—sorry to interrupt—perhaps it would be helpful if we could get the headings, and then we will go through them one by one.

Andrew Bailey: Yes. I would start with subsidiarity.

Chair: That is one.

Andrew Bailey: Heading 2 would be proportionality. Heading 3 I would term as taking up brakes and cards. Heading 4 I would broadly call carve-outs. Heading 5, to borrow a procedure that is going on at the moment, I would term the call for evidence review process, which I will come back to, because that piece is going on at the moment and sits alongside those things. Those are the headings that I would come up with to start.

Q612 Chair: That is very helpful. Maybe we should take subsidiarity and proportionality together, since they are so closely related. What comfort should we take from this text? Has much been advanced here from where we were by what is in the text?

Andrew Bailey: As you know, subsidiarity is explicitly covered in the treaty. The question, then, is how effectively it is put into practice when you set it against the ever closer union argument. Drawing on my own experience of European processes over quite a few years, there is sometimes quite a strong pressure, as we have seen in the past, for the ever closer union argument to trump the subsidiarity argument. Speaking from my own experience, if you asked me, "What do you want to see out of the language in here?", it ought to be that, at the point of initiation of legislation—I define legislation quite broadly here, because Tracey and I are both involved with level 1, level 2 and level 3 rules through our respective involvement in the ESAs, the European supervisory authorities—the question is properly asked: what is appropriately done at the Union and what is appropriately done at the national level? The test of this is whether that question is going to be robustly asked.

Q613 Chair: Because it is not being robustly asked at the moment?

Andrew Bailey: I do not think it has had enough prominence, no.

Q614 Chair: So what we have at the moment is not working. I think everyone who has thought about that in this debate is agreed on that. The question is whether what we have in front of us is adequate to make it work, in your view.

Andrew Bailey: It is a set of statements and commitments. The test of it is whether it will be put into practice.

Q615 Chair: What does that mean, "Will it be put into practice"?

Andrew Bailey: I do not think you can honestly take this piece of paper and say, "I understand exactly how this will work in the future", but this is an early stage of the negotiation. That is not a point of criticism; that is a point of what needs to happen.

Q616 Chair: There is one aspect of this document that offers a ray of hope, it seems to me. I would like you to comment on this. If you look at the first line of the subsidiarity document, 7/16, ***it*** says, "The Commission will establish a mechanism to review the body of existing EU legislation"—that is, the acquis communautaire—"for its compliance with the principle of subsidiarity and proportionality". The question is: what is this mechanism?

Andrew Bailey: Yes. That is a good start.

Q617 Chair: As you know, I did a bit of work on that and, indeed, wrote a book about what that mechanism should be.

Andrew Bailey: I have not read all of it.

Chair: I am appalled. You are one of the few. Right at the heart of it is that, if the Council is not given robust advice about what constitutes or might constitute something that should now be reviewed or reconsidered in the acquis, it certainly will not be done. I suppose my question to you, in this area, is whether you, as the Bank, think there is merit in the Government pressing vigorously to establish what that mechanism would consist of before this document is signed off.

Andrew Bailey: These are the right words, as you say. Let us now flesh them out.

Q618 Chair: They are words. They may be better than nothing.

Andrew Bailey: There are always words in there. This, of course, is the way European processes work. They are the right words. They are, as you said when you read them out, pretty explicit, but the devil is in the detail. Is it a process that has substance? One of the things we have seen in the last year, or a bit less, is a greater desire coming from the EU to review legislation.

Q619 Chair: Of course, that might be temporary, on the grounds of: "Well, we are in negotiation with the Brits, so we had better be a bit careful. Let us throw in something to review."

Andrew Bailey: That is one perspective you could put on it. Another one is that there has been something of a shift of the emphasis from re-regulation, post-crisis, to growth, particularly in the euro area context, which is causing a desire to review. That is a reasonable interpretation to put on it as well. We have seen that, and that is helpful and encouraging. In the last couple of days, we have responded to the European Commission's call for evidence on the regulatory framework for financial services. We published it literally in the last day. You can download it, but I can send it.

Q620 Chair: Why do you not just discuss whether you think the call for evidence part has improved a bit? That was your fifth. You listed five and we have addressed two so far. The fifth one was the change in the so-called call for evidence approach. Outline what you see as the old system and what we have now that you think is improving.

Andrew Bailey: The process is working better at the moment than it has before. It was not really a process, in my experience, that had much substance to it before. It is working better. In terms of the role of that safeguard, it is designed to do two things. First, it handles the review mechanism when, quite reasonably, you could have some change in the priorities. Secondly, it should handle unintended consequences of legislation. When you go through a very complex legislative process, you implement it. Solvency II is a good example of this.

Q621 Chair: Is this not because we have a more receptive Commission at the moment? Is there not a risk of this just being reversed? Do you think this document in any way entrenches the shift towards a more transparent call for evidence approach to law-making?

Andrew Bailey: It gives you a pretty explicit peg to hang it on.

Q622 Chair: I do not want to be too cynical, but I sort of hear no, and at the same time get the words "we will see".

Andrew Bailey: The simple answer is yes, for the reason that the words you read out are clear. The qualification coming out of the discussion we have just had is that you have to put flesh on to that as part of the next stage of the process.

Q623 Chair: We need an entrenchment of this call for evidence approach.

Andrew Bailey: It is that and the point of subsidiarity that we were discussing. We need to entrench both of them, because they are slightly different.

Q624 Chair: Let us have a go at these brakes and cards that you have described. What do we have to show for that?

Andrew Bailey: Well, you have language on both.

Q625 Chair: How much store do you set by that to offer the Bank protection?

Andrew Bailey: Having read it—and I have not been part of the process; I am, in a sense, an observer like you on this—I think that could do a few things. It could help with subsidiarity, because you have a sort of back-up process there that says, if the commitment to subsidiarity does not translate into what we think it should, you could play the card or the brake, as it were. It should also work in the context of what I might call poorly conceived legislation, where there is a pause in the process to reflect and hopefully change direction. As I have observed, there is a lot of talk about brakes and cards. They are, to my mind, one of a series of safeguards. They are not, in any sense—

Q626 Chair: Are they things on which you think you can rely? That is the question I asked you a moment ago.

Andrew Bailey: They are useful. My point is that you should not rely on them on their own; they have to sit alongside the other things we have been discussing. This framework has to fit together as a whole.

Q627 Chair: Let us now turn to these carve-outs. We have a carve-out that enables the FPC to operate. That is the CRD IV macroprudential carve-out. That seems to be intact, but not in Solvency II.

Andrew Bailey: No. The carve-out is important. The way I think about the carve-out, to step back to monetary policy for a moment, is this: monetary policy is conducted at the level of the currency area. In our case, of course, that is also the nation state; in the euro area, it is not. That is not subject to EU process and EU rule-making. In the crisis, we learned bitterly that, alongside monetary policy, we have to have macroprudential tools. The logic of the fact that monetary policy operates at the currency level, as it must do, is that macroprudential tools must be there in parallel; that is the logic of carving out. As you say, we and the Government of the day argued very hard in the context of CRD IV to get that, and we got something that works.

In the call for evidence, we have also set out the argument that, although insurance is not in what you might call the front line of macroprudential at the moment, there is a case for having the same or a similar carve-out. I can give you a real-life experience case study of this.

Chair: This is on Solvency II.

Andrew Bailey: It is on insurance, actually.

Q628 Chair: We might come back to that later on, because I think other colleagues want to ask in more detail about insurance. That would be very interesting. Can I point out that we have just had an exchange that, frankly, even well informed members of the public would find, I expect, very difficult to understand. One wonders how democratic accountability can hope in function in

an institution with such recondite processes as this. I thought I might ask a few simple questions before I move to John Mann to discuss consumer protection.

These proposals contain a mechanism to protect the interests of the euro-outs from the euro-ins. When you start to look at the language, it is framed in a way that does not really offer very much. It says, for example, only that the Council must discuss the issue; it says that the President only must try to facilitate a wider agreement. As I understand it, a simple majority in the Council can close down even the discussions that are enabled by these provisions, and that would be the end of the matter. What store do you set by that, in a sense, crucial part of this agreement?

Andrew Bailey: I am looking at document 4/16 now, section A, "Economic Governance", at page 5. There is a fairly crucial phrase in the second paragraph, which is that the "rights and competences of the non-participating member states"—that is, the non-euro area—will be respected.

Q629 Chair: What does that mean? That is exactly what I have just asked you. We have got as far as it being respected. "Respected" seems to mean you can get a discussion at the Council, which can be closed down by a simple majority, and you are, in the meantime, relying on the President to facilitate an agreement. It does not sound like a great deal of protection.

Andrew Bailey: Yes. We are back to the same question we have been discussing of how much substance there has to be around that. I would just make one point: you presented the euro area thing as asymmetric. I think it is actually symmetric, because it is important—and we strongly take this view, in the light of the banking union—that the ECB single supervisory mechanism can put into effect what it needs to put into effect within its area without us being an issue there. Symmetrically, it works in reverse, and obviously it is the symmetrical and reverse point that is crucial to this, but it actually is symmetrical. In many ways, if you talk to the SSM, the issue they are facing is how to take the members of the euro area currency union, create the single supervisory mechanism and put in place common approaches. It is pretty difficult.

Q630 Chair: Would you have preferred a specific period of delay, which would at least mean that there is a broader discussion, or a permanent block of some sort, rather than what we have here, which is this proposal for a discussion in the Council? Effectively, all we are offered here is that it can be forced on to the Council agenda. In other words, if you, as the Bank, do not like something, you go to the Treasury and you say, "This is a disaster." The Treasury then trot along to No. 10 and they say, "This is a disaster." No. 10 says, "Okay, we had better make sure this is on the European Council agenda by triggering this mechanism."

Incidentally, elsewhere in this document, you will find that there is a blank with respect to the number of countries that are required in order to secure even that discussion. Even that is up for negotiation. Rather than this rather weak protection—I may be mistaken, but that is how it looks—would you see merit in at least a mandatory delay period?

Andrew Bailey: What we need out of this is an effective mechanism by which, when the euro area says, "We want and need to do this thing in order to make our approach more effective", we can say, "That is fine; that is for you", and they have the governance to do it within the euro area, but they do not have to put it on to the full EU membership. We also need an effective mechanism to say, "You do not need to do that." Moreover, you would have to apply a test that says "You do not need to harmonise across the whole of the EU for the sake of the single market."

Q631 Chair: We do not have that now, do we, in here?

Andrew Bailey: Again, it is back to the whole discussion of what lies behind this and what flesh can be put around it. That is for the negotiation, not for me.

Q632 Chair: But, in the absence of that flesh, what is the answer?

Andrew Bailey: As everybody has said, and as I have seen the Prime Minister say, there is a way to go yet.

Q633 Chair: Yes, but you are saying you think that the way to go has to include some more things, if you are to have the protection you feel you need.

Andrew Bailey: I do not think, from anything I have heard, that there is any real question about what we are aiming for here. In a sense, I think there is common ground.

Chair: But I did not ask you that.

Andrew Bailey: No, you did not. It is where that negotiation takes it in terms of achieving those ends. By the way, when the process comes to an end, the Bank of England having published its report on the Bank of England and the EU, we will come back and revisit the points in that document and share them with you.

Chair: That is a very helpful clarification.

Andrew Bailey: I talked to Mark Carney this morning and we agreed to say that to you.

Chair: Mentioning Mark Carney, so far this afternoon you have played a straight bat that even he, although he is a Canadian, would be impressed by.

Q634 John Mann: Ms McDermott, on financial products, do UK consumers have better quality consumer protection than in other EU states?

Tracey McDermott: It is difficult to give a single answer to that question. There is a wide range of financial products sold across the EU. The retail financial services markets tend to be significantly more domestic, rather than across the EU as a whole, so products are sold that are very much specific to individual countries. Some consumer protection regimes apply across the EU, for instance in relation to funds under the UCITS directive,

and those are standardised protections that apply across the EU. We believe that we give UK consumers the protections they need in the products they buy, which may be different products with different distribution mechanisms to those sold in other member states.

Q635 John Mann: Let me repeat the question: do UK consumers have a higher quality of consumer protection than in other EU member states, in your judgment?

Tracey McDermott: In terms of products where there is a harmonised regime, for instance in relation to UCITS, they would have the same types of protections as those in other member states. There will be other products where there are protections in the UK that do not exist in some other member states. There will also be products sold in the UK that are not sold in the EU more widely and so on. There are a range of different answers to that question, so I cannot give you a straight yes or no, I am sorry.

Q636 John Mann: Do you identify some countries where there are specific problems for UK consumers within the EU?

Tracey McDermott: Practically speaking, most retail financial services markets remain domestic markets, so most UK consumers are buying UK products. There is the ability to passport across the EU, using the EU passport. There have been some issues in terms of firms passporting into the UK from other jurisdictions. The comments about contract for difference providers passporting in are well known. There have been some issues around insurance, on which we have recently published an enforcement action. There are some interactions with UK consumers from the rest of the EU, but it is on the wholesale side that EU integration is currently much more relevant.

Q637 John Mann: Do you have concerns about products being marketed to UK consumers from countries such as Cyprus or Malta?

Tracey McDermott: One focus of the ESAs, the European supervisory authorities, is on how to ensure that there is supervisory convergence. Where there are products that can be marketed across the EU, and there are a set of rules that apply to that, how do you ensure that those are being applied and supervised in the same way in different jurisdictions?

As I mentioned, spread betting and CFD providers have been marketed into the UK and, indeed, into other European jurisdictions, and there have been discussions at ESMA around that in particular, as to whether or not the rules have been applied in the same way in all those jurisdictions. That process happens through ESMA. In relation to insurance specifically, as I said, there have also been questions around the provision of insurance services into the UK from other jurisdictions. That is also being focused on in EIOPA, to ensure that the right protections are in place to do that.

Q638 John Mann: Your organisation spokesperson told *The Daily Telegraph*, "There is nothing we can do. This is EU regulation", when posed with such a question. Is that a problem for UK consumers, therefore?

Tracey McDermott: I do not know the context of the specific quote.

John Mann: Passporting of investment products from Cyprus and Malta.

Tracey McDermott: The right to passport in is certainly a right that exists under EU legislation, so we cannot prevent firms from passporting in, but if we think they are not treating UK consumers properly we have some powers, as the host regulator, to take action in relation to that.

Q639 John Mann: In terms of convergence across the EU, are we watering down our standards in order to match inferior European standards?

Tracey McDermott: In terms of retail financial services, which I think is where your question is focused, a lot of European legislation in the retail space builds on UK standards. There are aspects of MiFID that implement things related to the retail distribution review. The mortgage credit directive, which comes into force next month, is built largely on aspects of the mortgage market review, so there has tended to be more of the UK introducing standards, which are then spread across the EU, rather than vice-versa.

Q640 John Mann: I raised in the House this week the question of currency convertors and that, despite the fact that the Advertising Standards Authority had specifically ruled on 17 September against a lot players in the industry, the FCA, as regulator, refused to even look and investigate the case. Is that not an indication, on potential cross-border possibilities, that we are lessening our standards?

Tracey McDermott: In relation to currency convertors, the relevant piece of European regulation there is the payment systems regulation, and FX trading is not necessarily caught by that. We are in discussion with the Advertising Standards Authority in relation to that specific issue, in terms of who is best placed to take that forward. I think the specific issue that you raised is not particularly something around EU passporting.

John Mann: I am glad the issue is still live; I hope it will remain so in the future, Mr Bailey. I am glad you are nodding.

Andrew Bailey: It will.

Q641 John Mann: This is not prying inappropriately. I am interested in whether the referendum decision date is going to impact on your transfer of engagements.

Andrew Bailey: I have to say, I had never thought about that until you mentioned it. No, I think, is the answer. The situation is this: the process to find my successor at the PRA has started. Obviously, as Mark Carney would say if he was here, we want to get that done as quickly as possible. Tracey has very kindly agreed to continue as interim CEO during that period. I have promised her that that will not go on beyond the end of June, and that is a

matter of public record; I have said it elsewhere. The referendum date is interesting. You mentioned it, and it had never entered into my thinking on this.

Q642 John Mann: Can I just probe a bit further? I never want to over-compliment people who are appearing in front of the Committee but many people would be quite comfortable that, if there needed to be a delay, there was a delay. Whether there will be a referendum in June, as people seem to be speculating, I have no idea. No one else seems to have any idea round this table.

Andrew Bailey: We do not.

Q643 John Mann: But that has been widely discussed and, if the UK was to leave, would your current job not be rather critical in the immediate term, in response to such a decision? If the UK chose to stay, there would not seem to be a specific significance. If the UK chose to leave in a referendum, it would seem to me that that would be a factor.

Andrew Bailey: It is an interesting point. Let us think forward to that situation. The first set of issues arising would be contingency planning around what I might call the financial market and broader macroeconomic fallout from the decision. As you know, I am one of the governors of the Bank of England; I am involved in those discussions, but I am by no means the only governor who is involved in financial market decisions and that broader fallout. Of course it would be important that that got put through prudential supervision. That would be the first set of issues.

I think I am right in saying that there is at least a two-year period in terms of the actual process for whatever happens next. The important thing to say here is—and I think none of us know the answer to this question, either—that what happens after that very much depends on other decisions that are made, post that outcome in the referendum, about what the UK's future relationship with the EU is. None of us knows the answer to that, and that has a very big bearing, from the point of view of the framework of supervision, on what happens next.

Of course, in the first instance nothing happens, because the whole European framework is implemented in UK legislation. That UK legislation is there—I think you had a previous discussion in another hearing on this—and remains intact whatever the outcome of the referendum. You are right that there would be a lot of contingency planning; there would be a lot of attention on it. In the first instance, it would be on financial markets and broad macroeconomic issues, and the other governors of the Bank of England are also well versed and involved in that. Then there would be a rather longer period in terms of what happens next.

John Mann: That is helpful.

Q644 Chair: During this period of what happens next, I take it that there is a good deal of contingency planning going on in the Bank.

Andrew Bailey: I set them out in the order I did deliberately, because the first set of issues are around the financial market reactions and what the impact of that would be, and that is

obviously an immediate issue. We are very dependent, as I said, on the answer to the big question, which is: what would the UK's relationship with the EU be thereafter? You know as well as I do that you can have a range of answers to that question. There is what I call a Norwegian outcome, which means we have exactly the same set of European legislation implemented into UK law; we would not be really involved in the process of creating it in Europe, but we would end up with the same set of things, actually. At the other end of the spectrum, we would be far more free-standing, and there would be a whole set of issues around what bilateral arrangements we have with the European Union. We just do not know the answer to that.

Q645 Chair: On a prudential basis, are you in discussions with major financial institutions to make sure they are doing the necessary preparation?

Andrew Bailey: If you split it into the two things I did, we certainly observe financial market developments; we are already observing them, frankly and we then map those on to the exposures of the particular institutions.

Q646 Chair: Is this an explicit part of your discussions with institutions on prudential grounds at the moment?

Andrew Bailey: I will just give you one example.

Q647 Chair: Just to be clear, I wanted an answer to that point. When you turn up at HSBC or Barclays, are you taking a look at their contingency plans?

Andrew Bailey: Since Christmas, there have been some quite marked changes in the pricing of sterling FX options, often called risk reversals. When you look across the term structure of those, it is quite marked, so we obviously then go back to institutions and question what their exposure to this is. As you know, at the moment there is a lot else going on in the world of financial markets, so it is only one of several things going on that we have to pay a lot of attention to. The oil price and the whole emerging market one are in some ways much bigger issues at the moment.

Then you get to what I might call the more structural issue, where I would say that, because of the lead time post-referendum and the open question about the future relationship, that, frankly, is much more unplanned at this stage.

Q648 Mr Rees-Mogg: When the Governor was here, he mentioned some of the risks in relation to the UK economy if we left the European Union, and some of the modelling that the Bank of England did in relation to that. I wonder what work the Bank of England has done in relation to the risks of our staying in the European Union.

Andrew Bailey: In a macroeconomic sense—and I cover here both the FPC and the Monetary Policy Committee—that, currently anyway, would be far more in what I might call the more central outcome. Take the FPC, of which I am a member, so I am better able speak about that. The Governor talked about the risk to the current account from leaving

the European Union and a change in the risk premium, leading to a change in exchange rates and possibly interest rates as well, because of the correction of the current account. In a sense, the other side of that argument, by assumption, is that if we do not vote to leave then we are more into the central case, as at the moment. There, the broader issue is about the fact that the current account deficit is at one of its widest points and about its sustainability. That comes down to the question about how it is financed.

Q649 Mr Rees-Mogg: You may remember that, when we signed up to the Maastricht treaty, we had an opt-out from stage 3 of monetary union, but not from stages 1 and 2. You mentioned that exchange rate policy was entirely national competence; that is not quite accurate. Stage 2—and this is now partly under Article 142 of the treaty—is that exchange rate policy is a matter of common interest. I just wonder whether the Bank has given any consideration to the European Union or the Commission bringing enforcement proceedings to ensure that we follow the requirements of stages 1 and 2, and what risks that might have.

Andrew Bailey: That is a good question. I am dredging my memory now as well. I think we have, if I remember rightly, certain notification requirements. If we were to use foreign exchange intervention as a tool—which of course we have not done since the exit, other than a few little bits a long time ago on a co-ordinated G7 basis—on our own, then there are notification requirements. I certainly know there are notification requirements in the context of the ECB. Have we done anything about that? No, other than knowing they exist because, frankly, as you know, foreign exchange intervention has been just off the table for a long time.

Q650 Mr Rees-Mogg: We are in the strange position that there are these treaty commitments that we have, which no one has tried to enforce since we left the exchange rate mechanism. It does specifically say that members "shall take account of the experience acquired in co-operation within the framework of" the exchange rate mechanism, which at least implies that we are meant to be in it, as part of stage 2. I wonder whether the Bank has done any work on what might happen if the Commission decided to come back to us on that or whether it is just being left in the relatively long grass.

Andrew Bailey: That is interesting subject. As you probably know, the interesting case in point there is Sweden, because Sweden does not have an opt-out, but it has chosen not to go through the stages, as it were. If I am honest with you, to coin a phrase, that is more in the "sleeping dogs lie" camp.

Mr Rees-Mogg: That is helpful. I am grateful for that answer.

Andrew Bailey: I am sorry, I am really dredging ancient—

Mr Rees-Mogg: I am sorry to go back to that.

Andrew Bailey: It is well known now. I have been at the Bank for over 30 years.

Q651 Mr Rees-Mogg: You remember it all. To come on to some of the other future risks, as I am sure you know, 10 countries have agreed to follow enhanced co-operation for the financial transaction tax. The situation is, as I understand it, that, if we are a member of the European Union and a trade takes place through London in an equity or a bond that relates to one of the countries involved, we would have the duty to collect the tax and then pass it to the relevant Government. If we are not a member of the European Union, we would have no obligation to collect that tax. Has the estimate been done as to what extent of UK business would be in that category, and therefore—depending obviously on the level of the tax—what risk there might be of those transactions going to Singapore, New York or other areas outside EU control?

Andrew Bailey: I am not aware, no. The answer to that is no. The difficulty I feel when discussions of the financial transaction tax come up, which is not very often, I have to say, is that I find it very hard to work out how it would be implemented. You need to have some idea of how it would be implemented to understand the answer to your question, because it depends on how you would implement it and how you would in practice levy the tax. It is very hard. This is the question that always comes up, when it gets sketched out, as to how it would work.

Q652 Mr Rees-Mogg: There are proposals. Ten countries have agreed to go forward with it. I just wonder whether this ought not to be an area that the Bank looks into, because there is clearly a risk that transactions related to those 10 EU countries would move out of the City of London if it was implemented.

Andrew Bailey: It is a risk. If I am honest with you, I think the general view has been that we have not yet seen something that was near enough to seeing the light of day—in other words, that could work to get there.

Q653 Mr Rees-Mogg: I am slightly prodding, because the Bank has done the work on the risks of leaving, and it seems to me it is quite important, as this is going to be a very contentious political debate, and obviously the Bank wishes to be independent from the political fray, that it does the countervailing work on the risks of staying.

Andrew Bailey: Yes. You may know the answer to this question. I go back to my point about what choice the UK would make as to what its relationship would be with the EU after leaving. If we remained within the European economic area, would we still be subject to the mechanism? I do not the answer to that question.

Mr Rees-Mogg: I do not know the answer to that.

Andrew Bailey: That would be relevant.

Q654 Mr Rees-Mogg: Indeed, but I am not sure that is a good answer. I am rather keener on your complete independence line.

Andrew Bailey: We have not. Look, I will be quite honest with you on this. From our perspective, we have not seen a proposal for a financial transactions tax that seemed to have enough substance to it to be able to work through the answer to the question you asked.

Q655 Mr Rees-Mogg: I will ask you about one other area of concern, and that is TTIP. As you know, financial services have been excluded from TTIP, as I understand it at the Americans' insistence rather than ours. Why do you think the Americans excluded financial services?

Andrew Bailey: I do not know for certain. I would observe—and I would observe this in the context of quite a few international processes in terms of financial services, so we see this in some aspects of post-crisis regulation—that there is quite a strong pressure from the US, and in particular from Congress in the US, to have US solutions. Probably the most notable case of this at the moment is in the world of insurance and the whole question about globally significant insurers and the designation of them. That is a domestic designation. This has been and still is a very heated issue in the US. That is a good example of the resistance. I think that is, to a degree, what lies behind it.

Q656 Mr Rees-Mogg: It has been rumoured in the press that it is the quid pro quo for the French insisting on protecting French films; that the US has said, "If you are protecting films we are not going to do financial services." As far you know, is that so? You do not know that.

Andrew Bailey: No.

Q657 Mr Rees-Mogg: Fair enough. The other suggestion is that the Americans do not want to the take the risk of opening up their market to Greek banks and so on. If it were a deal with a UK it would be very much easier to do because they recognise the high quality of the City of London compared to some of the peripheral EU financial services.

Andrew Bailey: I do not know.

Q658 Mr Rees-Mogg: Again, I wonder if it is something the Bank ought to look into as a matter of risk of remaining, because we might be cutting ourselves off from a free trade deal in financial services with the United States. That is potentially of huge advantage because the City is so important to our overseas earnings. For the Bank to have a view on it might be extremely helpful.

Andrew Bailey: I will take that back.

Mr Rees-Mogg: Thank you very much.

Q659 Stephen Hammond: Good afternoon. We have taken evidence from a number of other people about the City and London and its competitive position. It is going the other way. We have heard about the City of London and its competitive position. We are keen to understand how far the intrinsic advantages of the City of London—law and language, which drive competitiveness and agglomeration of talent—have been the key driver of the success of the City of London over the last 30 years, as opposed to membership of the single market in financial services? I am interested to hear from both of you as to how you see that balance.

Tracey McDermott: It is impossible to give a definitive answer to that. Clearly, the UK has significant advantages in terms of an established and well regarded financial services market. It has advantages in terms of expertise, time-zone advantages and so on. But the growth of trade in the past 30 years with the EU, in terms of financial services, has been significant. It has been our biggest market for UK financial services, at around £16.5 billion. It is not possible to isolate one rather than the other.

Andrew Bailey: You do see network effects. If you get a sizable enough concentration of activity, you get benefits in terms of networking. People often say that now about FinTech. If you see hear the numbers quoted for the number of jobs in FinTech in the London and the south-east area, it is pretty big. You ask the question, "What is driving that?" There is a network and agglomeration effect. The Treasury did something on this when they did the five tests on euro membership in the previous Government.

Q660 Stephen Hammond: The key point that we are trying to tease out in evidence is, while you cannot give a definitive balance one way or the other, you saw huge numbers of international banks joining the City of London before we had membership of the single market in financial services. Has membership accelerated that trend, or were there things in place beforehand? You are tending to suggest, Mr Bailey, that, as a lot of people believe, the agglomeration of professional services widely in the financial services sector, not just banking, makes London an attractive financial centre. When Mark Astaire from Barclays came before us, he made the point that we thrived inside the EU, but his view was that London would continue to thrive outside the European Union.

Andrew Bailey: The two interact, of course. If you get the agglomeration effects and you are in a large free trade area, you will get the interaction of those two things. You will have an even larger benefit; that is true. The economics of it would tell you that is true. The imponderable question, of course, coming back to what the relationship between the UK and the EU would be in a post-exit context, is how much of that would be jeopardised by leaving. For that reason, that is a hard question to answer.

Q661 Stephen Hammond: Given that the bulk of euro currency trading is already done in London, is that not evidence to suggest that Brexit would not be a major threat to the City of London?

Andrew Bailey: It depends what comes next after that.

Q662 Stephen Hammond: Do you mean a change in regulatory regime?

Andrew Bailey: No, it would be the change in trade relationships. It goes back to Mr Rees-Mogg's point about TTIP. There is an open question about what the UK's trade relationship would be with the EU post-exit. That is probably the first thing to cover on that question.

Stephen Hammond: We clearly cannot answer that.

Andrew Bailey: No, sorry.

Tracey McDermott: It may be worth saying that there are 5,300 or so firms that passport out of the UK into the EU. To Andrew's point, whether or not that would still be possible would depend entirely on the arrangements that were put in place in the event of a vote to leave. Passporting arrangements are currently widely used by firms based in the UK to enable them to do cross-border business.

Q663 Stephen Hammond: Could I test with you a couple of statements that have been made by either side of the argument? The campaign group, Leave, for instance, has made the proposition that EU regulation is the reason why the eurozone has so few financial centres. Would either of you agree with that assessment?

Tracey McDermott: The UK is also subject to EU regulation, and we are quite a big financial centre.

Andrew Bailey: That is illogical.

Q664 Stephen Hammond: Broadly, you do not accept that. They have made that statement, but that is not one that either of you would share.

Andrew Bailey: It is just inconsistent, as Tracey has said. The UK is subject to the same regulation.

Q665 Stephen Hammond: Business for Britain has stated that the general consensus is that "the UK's influence over financial laws has declined dramatically since the 2008 financial crisis". Again, is that something either of you would agree with or is that not applicable?

Andrew Bailey: I do not think so, no. One important thing to note is that—this is particularly true in the banking area—in the prudential area, much of the framework starts in Basel, in the international context, and is subsequently implemented into EU law. The EU does not always implement all of it exactly, and that is sometimes an issue. But, if you are asking the question about influence, that influence starts, for us, in the degree of the role that we play in the broader international body, which in the banking context is

primarily focused on the Basel Committee and the Group of Governors and Heads of Supervision, which sits above it.

Q666 Stephen Hammond: Leading on from that, your general assessment is that the UK is significant in influencing the regulatory agenda inside the EU to its own advantage.

Andrew Bailey: We have had some significant achievements. One that is live at the moment is the work we have done jointly with the European Central Bank on reintroducing a simple and transparent securitisation regime, which is more robust than past examples.

Q667 Stephen Hammond: Paragraph 5 of the "Economic Governance" section is all about whether or not there is supremacy of the EU as opposed to the eurozone. I do not know whether you have read that section. In that context, one of other people giving evidence to us, Mr Chu of HSBC, said it was inevitable, whatever happened, that the eurozone would become more influential in banking supervision in a way it had not been before.

Andrew Bailey: Yes, because that is the whole logic of creating the single supervisory mechanism in the ECB for the eurozone, or the banking union, which at the moment is the eurozone. That is something we welcome, because we think it is appropriate for there to be a supervisory authority at the level of the currency area. Frankly, some of the experiences we had during the previous depths of the euro crisis were quite difficult. The SSM is obviously a body we deal with extensively, because in a sense it is a parallel body to us, as a supervisor. We have already seen real benefits from the creation of the SSM in the last year or so since it has come into existence. That is a good thing from my perspective.

Stephen Hammond: There is no inherent contradiction at all in that.

Andrew Bailey: No, it is sensible. Frankly, we have welcomed having the ECB in that capacity as a counterpart to us.

Q668 George Kerevan: Good afternoon. I want to look, broadly, at the relationship between our financial regulatory organisations and European ones and at how we co-operate. You are both members of the European Banking Authority and the European Securities and Markets Authority.

Tracey McDermott: I am a member of the European Securities and Markets Authority, as Andrew is of the EBA.

Andrew Bailey: Formally, I am a member of two: I am a member of the European Banking Authority and the European Insurance and Occupational Pensions Authority. One of my colleagues, Sam Woods, actually takes my role on EIOPA, because two ESAs is quite a lot to do. I actively play a role in the EBA, yes.

Q669 George Kerevan: I was just interested in pursuing how the EBA operates. I know there are votes, but is it largely by consensus? If it is by consensus, can we always guarantee that, if we have a particular issue that is important to British financial institutions, we are listened to and given good credence? How does it work?

Andrew Bailey: You are right that more things than not are done by consensus, because there are agreements. Nowadays, there are probably votes at most board of supervisors meetings. Obviously, some of the well known and quite well publicised issues tend to attract votes frequently; they rarely do not attract them. Voting is there.

In terms of our influence—we can both speak to this—we put a lot of resource and effort into the ESAs because they are important. There is a huge volume of level 3 rule-making coming out of the EBA and EIOPA. EIOPA has obviously been on the front line with Solvency II. Therefore, frankly, we take the view that it is very important that we are in there. We may not always like what goes on, but we have to be in there. You can speak about ESMA, Tracey.

Tracey McDermott: I would say the same. Obviously, there is the formal role on the board of supervisors, but an awful lot of the work that is done by the authorities is done in various working groups and taskforces. Certainly, from an FCA perspective, we are represented on pretty much all of them.

Q670 George Kerevan: They are staffed by professionals from your organisation?

Tracey McDermott: Yes, from our organisation. Actually, although Andrew has a seat on the board of supervisors for the EBA and EIOPA, we also have involvement in working groups related to those issues as well. Currently, we have 18 people on secondment to various European institutions. We have around eight at ESMA and eight at the Commission. Those numbers may be slightly off, but it is around those sorts of numbers. We also have a team of people based in the UK who primarily interact with Europe. We invest quite a lot of resource in that.

Q671 George Kerevan: When the argument is made that banking and financial regulation is imposed on us by Europe, that is a rather one-sided view, because we have staff from our organisations there involved in making the rules.

Andrew Bailey: Yes, but I would distinguish two parts to that argument. There is the point that the Chairman questioned me on earlier about how the legal framework works. Then you raise the second issue: yes, but is it all populated by other people? As Tracey rightly says, no, we have both taken the view that, given the importance of this, it was important to be in there in terms of our own staff representing us and to provide them with secondees.

Tracey McDermott: It is clearly correct to say that the UK is influential within the ESAs, particularly because we have the widest spread of financial markets out of all the members

of the European Union. Obviously, we are one of a number. We are influential, but we are not the only voice is around the table.

Q672 George Kerevan: Where I am going is the obvious direction. As the eurozone moves to a banking union and the ECB becomes more and more dominant as a regulator, to what extent, therefore, does the ECB become the dominant player within the regulatory bodies and then the Bank of England, the FCA and our other agencies become bit players? Even though the City is huge in terms of its economic impact within Europe, the dominance of the ECB and the eurozone members within the decision-making bodies will ultimately dwarf our influence, will it not?

Andrew Bailey: That is an interesting view. It is really for the EBA, because, in the other two, the ECB is not playing that role. Obviously, that was extensively discussed at the time. That is why the double majority voting system operates in the EBA—as a protection for that. The other thing to say is that it is another reason why we have a very close relationship with the ECB, because, on the whole, we think it is better to try to sort these issues out with them in the context of the EBA, as well as having a very close relationship with them outside.

I have to say—other people have said this—all my experience so far is that the euro countries do not speak with one voice. That could change. This is why the double majority protection is important. In the EBA, they do not speak with one voice, but that could change as time goes by and the SSM becomes more institutionalised.

Q673 George Kerevan: You have anticipated where I am going: to test the validity of the double majority voting, whether it actually works in practice. It did not work in practice when it came to bank bonuses, precisely because everybody except the UK—

Andrew Bailey: You have to have some supporters.

George Kerevan: Exactly. The double majority thing only works if, broadly speaking, the non-eurozone countries operate as a bloc. That did not happen in a key issue that has affected the City. With banking union, you could foresee, increasingly, the smaller non-eurozone countries operating in the ECB's orbit. The point is this: how big a defence is the double majority voting? It has not worked on occasion.

Andrew Bailey: It cannot overcome the fact that, if we have no other supporters, we are going to lose, frankly. You raise an interesting question about the position of some of the countries that are not in the eurozone. I do not know. In the remuneration case, to be honest with you, for some of them it is just not the issue it is for us, because they come from systems that do not have remuneration structures anything like the ones we have.

George Kerevan: You are arguing that was a one-off?

Andrew Bailey: No, it could happen again.

Q674 George Kerevan: I have sat with Mr Schäuble, the German Finance Minister, in Göring's former office. He clearly wants to extend the bank transaction tax, not only in the eurozone but to other countries. I could foresee a situation in which all other countries want to support a bank transaction tax.

Andrew Bailey: This goes back to the other question. If there were to be a bank transaction tax, his argument is, "I do not want it just in our area. I want everybody in it."

Q675 George Kerevan: Ultimately, double majority voting is not a defence.

Andrew Bailey: It works in some circumstances. As we were saying, it will work in a circumstance where there is potentially a delineated view between the euro area and the non-euro area. That is where it will work. It will not work in other circumstances, and that has always been known.

Q676 George Kerevan: That is very fair. Now, we come to the current negotiations the Prime Minister and the Government have been pursuing. To quote the Chancellor, "Among the principles we seek to establish in this re-negotiation are these simple ones: fairness between the euro-ins and the euro-outs enshrined, and the integrity of the single market preserved." Have we got that?

Andrew Bailey: It goes back to the question of the Chairman. We have words that can be used to create that, but flesh has to be put onto the bone. That is consistent with things I have heard said in the Chamber today.

To put a bit of context around it, what does that mean in terms of the euro area? The issue the ECB has is that it has a system of supervision with all its member countries, but, of course, there has been no harmonisation of legal provisions. If you are a supervisor in the SSM, if you are doing my job in the SSM and you have a series of cases before you, first of all you have to work out which legal system you are operating in. You have to say, "For this one, I am operating in this legal system, and for that one I am in that one."

That is complicated enough as it is. What follows from that, then, is that—in a sense, this is at its most acute at the moment, because of the transitional arrangements in CRD IV, with the framework—there are a lot of national discretions in there that are being used. The position the ECB is well known to have taken is to say, in introducing the SSM, they want to reduce those national discretions. A good part of that they can do without any involvement from the rest of us. The protection in that context is to say there are some where you might think the way to solve that is to change EU law. That is where the issue lies.

George Kerevan: That has to be in the negotiations, then.

Andrew Bailey: That is what lies behind a lot of the text in the "Economic Governance" section.

Q677 George Kerevan: You are the regulator; you are an independent governor. I am trying to get a sense of whether what the Prime Minister has delivered provides that.

Andrew Bailey: It is continuing. We are still in negotiations. Well, we are not in negotiations. He is in a negotiation.

As I said earlier, the language in this document about "safeguarding the rights and competences of the non-participating member states", taken in isolation, is a good piece of language. As the Chairman was saying to me earlier, however, where is the substance? In some respects, I have no doubt that is still being negotiated.

Tracey McDermott: To echo what Andrew said, there is explicit recognition in the "Economic Governance" section that discrimination based on which currency you use is prohibited. That is quite a strong statement of intent. The practicalities of how all this works in practice is, obviously, where the detail is. However, the intention that there will not be an inequality inbuilt between euro and non-euro countries is stated quite clearly in there. There is also explicit recognition in the context of banking that that may mean there are two different sets of rules, some of which will apply within the banking union and some of which will apply more broadly across Europe. It says quite a lot about that balance between the euro and the non-euro countries.

Q678 George Kerevan: But that is an aspiration. If you have banking union here and the UK there, is it not inevitable that the needs of the banking union will dominate what happens across the entire market?

Tracey McDermott: The document we have, in terms of what it says is the intention, is quite explicit that there should not be discrimination based on what currency you use. It explicitly recognises that that may mean different legislative frameworks applying to banks in the euro and banks outside the eurozone. In terms of whether that means there is a stronger voice in the banking union part of it than the other, that is a slightly different question that is much more about how it operates in practice. But the statement of principle is a helpful statement of principle.

Q679 Chair: To go back to Solvency II, the colleague who was thinking about following up on that has left to participate in the debate that is taking place on the Floor of the House at the moment. **The** Parliamentary Commission on Banking Standards had a letter from you in 2013 that was highly critical of Solvency II. You called the history of the EU process on Solvency II "shocking", the legislative proposals "vastly expensive" and "lost in detail". On reading that, it seemed to me that Solvency II was an object lesson on how not to make good law. Do you agree with that?

Andrew Bailey: Yes. It went on for a very long time. You can get different estimates on when Solvency II started; it was way before my time being involved in this. It was not just that. The problem—in a way, this is a cost issue—was that there were many false dawns in

terms of when it would end and move into implementation. The consequence of that was that a lot of pressure was put on to begin implementation before the thing was landed. The thing was only finally landed not that long ago. I look at the amount of money that the FSA and, to a degree, we then spent on Solvency II. I can give you the numbers, actually. Going back to about 2011, the FCA set a framework and estimated that it would cost between £100 million and £150 million for them to implement Solvency II.

Chair: That is their cost of implementation?

Andrew Bailey: Yes, that is their cost. The number is a lot bigger in the industry.

Q680 Chair: ***Yes. Do you*** know ***roughly by what multiple that would be?***

Andrew Bailey: No. I have heard a lot of numbers.

Chair: Is it two, three or five?

Andrew Bailey: A few billion pounds often comes out as the number.

Q681 Chair: This is a process that has cost several billion pounds?

Andrew Bailey: It could well be. We do not know the exact number. We know for certain what we have spent. We know the big firms have probably spent more than we have.

In 2011, the FSA said £100 million to £150 million. The final number, we think, is £105 million; it is not quite done yet. Quite a big part of the eventual £105 million would have been sunk by the time we got to 2011-12. I am not saying all of that was wasted, because we needed an infrastructure, but it probably gives you a sense of how this process of pushing to implementation before it was finished led to a pretty front-loaded expenditure. It begs the question as to how much it would have been with a different process. That is one thing.

The second thing is something we discussed one of the times I was here with David Belsham from the PRA board. He is quite articulate on this because he is an actuary and he had long experience of this in his previous life at Prudential. We got it implemented at the end of last year. We are now ready, as we have put in the call for evidence paper, which I will send on to you, highlighting—this, again, is a point David raised—issues that need addressing. This falls into the "unintended consequences" area, where there are some elements of Solvency II that frankly do not look very sensible, as implemented.

It has led me and my colleague Sam Woods, in particular, who runs insurance supervision for me, to be quite public in saying, as we said last time, "Be very careful in comparing Solvency II capital numbers, because there are big differences in terms of the treatment of different types of insurance business." Of course, life insurance markets, for instance, are very different across EU countries, because the product offering is quite different. This goes to Tracey's world as well. There are very different products. The UK is relatively unusual in having a large annuities market. Other countries have different forms of guarantee structures on long-term savings.

Frankly, we see things that do need dealing with. Now, the question is about how much you could have avoided that by having a better structure of regulation and a better process in Europe, and how much you need the call for evidence mop-up type process in the safeguards. You need both, is the answer.

Q682 Chair: The short answer to my question is that this was an object lesson in how not to make law.

Andrew Bailey: Yes. Important and big though it is, for it to have been going on for well over a decade at that expenditure seems implausible.

Chair: We are not even sure about the timeframe, because it is lost in the mists of time. We are not even sure where it really began.

Andrew Bailey: There are different views. I am sure there is a reasonably objective answer to it.

Q683 Chair: Does the European Commission grasp the scale of the mistakes that were made with this?

Andrew Bailey: I do not know. One of the things I would observe in Europe—

Chair: That is worrying in itself, that you say you do not know.

Andrew Bailey: We have seen some of this with CRD IV as well. It is rightly—I use this word advisedly—a political process to agree these things. As the bodies that then have to implement them—Tracey and I are both in this position—you sometimes feel that there is a huge process of agreement and then it is chucked over the wall and you have to implement it in a year. That is very hard sometimes.

Q684 Chair: Is there anything you want to add before I move on to another aspect of Solvency II, Ms McDermott?

Tracey McDermott: No, nothing specifically in relation to Solvency II.

Chair: You had a hand in it.

Tracey McDermott: I would make a general point in terms of the Commission. Andrew has already referred to the call for evidence. One of the areas that the PRA and we have focused on in the call for evidence is the question around implementation timetables, overlapping implementation, reporting requirements, definition consistency and so on. To that extent, the Commission, having initiated the call for evidence, has recognised that there is a challenge here that needs to be looked at.

Q685 Chair: At the very least, what we need by way of clarification from these negotiations, which are not yet complete, is that this call for evidence process be entrenched in a meaningful way that we can understand and that cannot be

resiled from. It sounds to me like, using this as a case study, you are telling us that you would conclude that, had you had that process in place, you might have been spared quite a lot of time and money, and dealt, to some degree, with this front-end loading problem to which you alluded. Is that correct, in a nutshell, Mr Bailey?

Andrew Bailey: Yes. The general point is that we can get better outcomes.

Q686 Chair: Might it be worth finding out how much Solvency II cost the industry? It might be worthwhile. I do not want to impose another burden on everybody by asking the question, but it might be worth us knowing publicly what the cost was and, if firms were able to make an estimate with your supervision of it, what they feel would have been necessary anyway. In other words, you made the valid point that some of this work was not wasted, because we would have had to have done some of it anyway. That would also be helpful: a gross cost and a net cost.

Andrew Bailey: We should be able to get that. I am sure there will be something.

Q687 Chair: Could you say whether you are content with the current arrangements now in place—they were implemented only a few weeks ago at the beginning of the year—for Solvency II? Do you have remaining concerns? Now is the time to articulate those.

Andrew Bailey: Again, in the call for evidence paper, we have set out, mainly, the things David Belsham and I covered in the hearing before Christmas. We covered the question of what often gets called the ultimate forward rate, which is the question of which curve is used. David covered the so-called risk margin.

Chair: We had an extensive exchange on that.

Andrew Bailey: Yes. We take the view that it is too interest-rate sensitive.

Q688 Chair: How are we going we take these forward? Do these now fall into the category?

Andrew Bailey: They are in the call for evidence category, yes.

Q689 Chair: Can we do a bit of forward thinking and, for a moment, go back to what I was discussing at the beginning? This is now existing legislation. This is now part of the acquis communautaire. Now we want to have a look at this recondite and rather vague document we have just been presented with and assured is great stuff on the Floor of the House. What we need to know now is whether that review mechanism that was set out—the mechanism in particular—is robust enough to enable statutory review to take place.

Andrew Bailey: Yes, absolutely.

Chair: I do not want to put words in your mouth, but it seems to me that we do not have the information at the moment to hand, to have the remotest idea as to whether it would help or not. Is that correct?

Andrew Bailey: We have a vision as to how it could work. We have some examples of how it has been put into effect recently, which are encouraging, but, as you said earlier and I would agree, that does not mean it is cemented in, and it should be. We agree on that.

Chair: Whenever I hear the word "vision"—

Andrew Bailey: You begin to recoil.

Chair: Yes, I recoil a little and I tend to think of theological analysis.

Andrew Bailey: I apologise if I pick up some of these documents and sound pejorative. Solvency II is quite interesting, because, if I am honest with you, I sometimes hear from those who are involved in the process—this is including in the European Parliament—that this was a very delicate political compromise and you unpick this at your peril. This is often said. Then you get the other side of it. As you will see in the paper we published, we say, "Look, I am sorry, but some of these things just do not work properly." We need to sort these things out, because it does have a real impact on the industry.

Q690 Chair: On the one hand we are told, "This is a Ming vase. Do not move it from the mantelpiece", and on the other hand, if we try to put anything in it, like some liquid, we find it has a hole in the bottom.

Andrew Bailey: Or it is, "Do not take the machine apart, because you will not be able to put it back together." You can use both those analogies, yes.

Q691 Chair: I just want to close with an examination of one other aspect of this debate, on which you have particular expertise to bring. I mean both of you—please chip in, Tracey McDermott, if you are the right one to aim this at. Certainly for part of it, you are.

Open Europe have put the annual cost of the top 100 most burdensome EU rules at £33 billion. I have a list here: the capital requirements directive, AIFMD, MiFID, financial services and so on. Have you made any effort to take a look at these figures? Are figures purporting to measure the cost of regulations in this way—I am juxtaposing this with what I have asked you to do in respect of Solvency II—largely meaningless without an understanding of how the EU would choose to regulate the industries in the absence of membership?

Andrew Bailey: I do not know how they calculate the figures, but I can certainly have a look at them. The one thing I would say—this is probably most apposite in terms of bank capital regulation—is that it depends on what counterfactual you use. The idea that we would have very little bank capital regulation or go back to what we had before the crisis would obviously be disastrous, and the cost could be understood in that context. However, I would honestly have to look at how those numbers were derived.

Chair: It might be worth the Bank and the FCA having that look.

Andrew Bailey: Yes, I could do that.

Q692 Chair: To the extent possible, you might feel—without wanting to be drawn into the grubby world of politics, in which those of us on this side of the room live—that we could get a bit of clarity on what kind of numbers might or might not be plausible.

Related to that, some people are arguing that there would be a bonfire of red tape with an even more permissive regulatory environment, were we to leave. Is there plausibility in what they might say? In other words, you described two scenarios or extremes of what the world might look like. Of course, it is very difficult to assess, perhaps, what it might look like. Even taking that broad spectrum into account, is this "bonfire of red tape" imagery adding much light as opposed to heat in the debate?

Andrew Bailey: It is an interesting question. Let us go back to Mr Rees-Mogg's line of questioning on TTIP for a moment and imagine we had to negotiate equivalent agreements with the US, which we probably would, actually, to get to that world. You then have to consider where that ends. If you go to the US structure, you have Dodd-Frank; you have Sarbanes-Oxley; you have state-based insurance regulation in 50-odd states. It has been stated a number of times in peer reviews. The last one the IMF did commented that we were rather light in terms of supervisory resources compared to non-EU countries.

You would not immediately assume that there is a golden world out there where it is all different. Sometimes I ask major US banks how many supervisors they have. The problem is they have to count the number of agencies first. If you talk to a major US bank about the number of supervisors they have, they can easily run up over 100. If you add up the resources Tracey and I have, that is a lot more.

Tracey McDermott: There is relatively little, if anything, in EU regulation where there would be no regulation at all. For instance, Andrew has talked about capital, but you cannot imagine a world where there is no market-abuse oversight. That is currently derived from EU regulation. If we were outside the EU, we would still have that. Undoubtedly, there would be some things you would do slightly differently. There may be some things you would do, to Andrew's point about Solvency II, in a more streamlined way. However, domestically, we would want quite a lot to cover the ground covered by most EU regulation anyway.

Chair: Those are helpful answers. I would like to end by making one more request of both of you. If you can do it jointly, that would be even better. Think through what this mechanism might be that seems so crucial now to at least part of this process. After all, it is not just how rules are made; it is about what happens to them once they are there: how they added to, amended or altered, or how unintended consequences develop as a consequence of changes in behaviour in the marketplace and the regulated community. A mechanism that can review existing law, the acquis communautaire, is of particular importance in a mature institution such as the EU, which is what it is now.

I would be grateful if you could go away and give a little bit of thought to that. I have had a go off my own back, but you have dozens of high-powered people behind you thinking about

these issues. I am sure they will come up with something far better. It would be very helpful to have that sooner rather than later, too. These negotiations look as if they are in their final stages, so the sooner the better: days or weeks, rather than months.

Thank you very much for coming to give evidence. We are extremely grateful to you. I expect we will need to hear a good deal more from you on this subject before we are done. We are very grateful for the suggestion that you are going to come forward with a considered set of