

Select Committee on the European Union

Uncorrected oral evidence Brexit: Deal or No Deal

Tuesday 24 October 2017

4.20 pm

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Members present: Lord Jay of Ewelme (The Chairman); Baroness Armstrong of Hill Top; Lord Crisp; Lord Cromwell; Baroness Falkner of Margravine; Baroness Kennedy of The Shaws; Earl of Kinnoull; Lord Liddle; Baroness Neville-Rolfe; Lord Selkirk of Douglas; Baroness Suttie; Lord Teverson; Lord Whitty; Baroness Wilcox; Lord Woolmer of Leeds.

Evidence Session No. 3

Heard in Public

Questions 21 - 31

Witness

I: Mr Miles Celic, Chief Executive, TheCityUK.

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Examination of witness

Miles Celic.

- Q21 **The Chairman:** Mr Celic, we have had a bit of a discussion about how to pronounce your name but I hope that that will be satisfactory. Welcome. It is very good to see you here. We are also glad to have our friends from Bavaria sitting behind us. There may be a vote at any moment: the Bell may go, in which case some of us will have to leave and we will have to call proceedings to a halt for a moment.

We are very grateful to you for coming to give evidence to us. This meeting is being televised. It is a public evidence session. A full transcript will be taken and a copy will be sent to you after the session is over. This is the third evidence session in our inquiry into Brexit: deal or no deal, which is looking at the possibility of no deal and at the transitional arrangement and what that might consist of. Perhaps you could introduce yourself and your organisation and then we will go on to the first question. If you would like to make an initial statement, that would be fine. If not, we will press on with the questions.

Miles Celic: Thank you for the invitation, and I look forward to an interesting and, I hope, insightful discussion. I am the Chief Executive of TheCityUK, which is the business-led representative body for financial and related professional services. We represent about 2.2 million people around the UK within our industry. That covers everything from banking to insurance to asset management to accountancy, the law firms, the professional services firms—it is the whole ecosystem, about 13% of economic activity in the UK. We always make the point that two-thirds of those jobs are outside the M25. Obviously, Brexit is extremely high up the list of priorities for our companies and it is probably the issue of primary importance in our engagement at the moment. I am happy to move straight on to questions.

- Q22 **The Chairman:** Thank you very much. I will begin with a rather general question: what is your assessment of the Government's approach to Brexit negotiations so far? I might add that the Prime Minister's spokesman said yesterday that the Government were looking to finalise a deal all in one go ahead of the UK's exit in March 2019 and the start of any proposed implementation period. We would be grateful for your views on that, too.

Miles Celic: Sure. Probably our most urgent priority in terms of where the Government are, and indeed where the EU 27 are, is around the issue of transitionals. We have made a number of statements to that effect over recent months. We issued another statement on that last week. From our perspective, it is not much use getting to the end of the process and then being told that there is a terrific transitional agreement there, because any company that needs to make any decision about moving operations or staff or whatever it may be will have made that decision by that point. From the conversations we are having with the companies that we represent, I would say that there is a hope that there will be progress by Christmas and certainly within Q1 2018. Any company that needs to

have moved any operations or staff will have done so by that point. Companies cannot find themselves on 30 March 2019 being unable to serve customers on the continent of Europe, or indeed vice versa.

We welcomed the Prime Minister's speech in Florence when she focused particularly on transitionals. We said that that put the ball into the EU's court in terms of a response from the EU. It is disappointing that we have not seen that taken up yet. With regard to the pace of the talks—this is not something solely for the UK Government; there are two sides to this negotiation—it is disappointing that we have not seen further progress on to the issues that our companies are focused on. That runs the risk that from the point of view of this industry, you end up with a slight paradox of both a high-access and a low-access Brexit. My own view is that we will probably end up, because economic logic would suggest it, in a position where we have a pretty good deal—a good, comprehensive free trade agreement—between the UK and the EU 27 at the end of this process, but companies cannot wait for that. They cannot simply cross their fingers and hope that that is where we end up.

The Chairman: When you say the end of this process, do you mean 29 March 2019 or beyond that?

Miles Celic: Our vision of transition is that there are two stages. First, there is a bridging period between the end of the Article 50 process and the start of the new relationship, should that be required—and I will come back to that in a moment—and then an adaptation period. Typically any free trade agreement has an adaptation period for the various parts of the economy as they adapt to the new arrangements. The Prime Minister's view, judging by comments she made yesterday and previously, seems to be that everything can be sorted out in the remaining 12 months—and really it is about 12 months' worth of negotiation because clearly this will need to go to individual parliaments and so forth for ratification on the European side—and that full, comprehensive free trade agreement can be sorted out within the next 12 months. That is the Prime Minister's view. I have to say I think that is ambitious. If you look at CETA, that was a seven-year process. From recollection, the South Korean free trade agreement was a 12- or 14-year process. It would certainly be a matter of pride on both sides if we managed to achieve it in that time.

Q23 **Baroness Neville-Rolfe:** Obviously this is a vast and important sector. It is good to have your written evidence. I was very struck by the figure of nearly 11% of the UK economic output, and you mentioned the 2.2 million jobs. I am interested in the substance. What are the main stumbling blocks—those of substance—to agreement being reached in respect of financial services and how can those be overcome? On what terms and how long will it take to reach agreement? You have already said that it will take time. We are very keen to look ahead beyond the transition period to the substance and hear what we are aiming for.

Miles Celic: I believe that Mark Hoban appeared before a number of you relatively recently and set out our ambition for the end of this. Before I

get on to Mark's work and the work that the International Regulatory Strategy Group has done, which is effectively a joint venture between ourselves and the City of London Corporation, I will say that there are three priorities for the industry, which are set out in our submission. The first is the transitional period, which I have touched on. The second is that we end up with mutual market access as close as possible to the current situation—so the minimum amount of friction compared to where we might be. That is based on mutual regulatory recognition, which I will come back to in a moment.

The third is mutual access to talent. We did a piece of work with PwC which looked at the long-term vision for the industry once the UK is out of the European Union and once it has gone through any transitional period, both the bridging and the adaptation elements. We spoke to dozens of senior industry leaders, politicians, regulators and others. My own expectation had been that regulation and the regulatory framework would be the most important thing in terms of the long-term health of the UK ecosystem in financial and related professional services. It was certainly very important—it was the second most important issue. But marginally the most important issue was access to talent: the ability of the UK to bring the best and the brightest to the UK. That is not just intracompany transfers—not just being able to move somebody from the German operations of a financial institution or a law firm to the UK operations—but the ability to be open to entrepreneurial talent.

At the moment the UK remains the number one centre for fintech internationally. There are a number of reasons for that. It is a terrific accolade to have but it is one that we cannot be complacent about. It is built largely on the ability to bring people to the UK. There is a question mark about how we train people within the UK, and we are doing work on that. It is not just a European issue, although I appreciate the remit of the Committee. But if you look at Silicon Valley, for instance, 40% of the fintechs there were started by people born outside the United States and 44% of the staff of those fintechs were born outside the United States. The two main countries that provide entrepreneurs and staff to those companies are China and India. From that perspective, we need a global approach to immigration and to talent, as well as working up talent in the UK. Those are the three principles that we look at the Brexit negotiations through.

When it comes to the specifics—the substance, as you put it—there are a number of elements. The first is an overarching mutual regulatory recognition regime. A number of you will be familiar with that, but just to summarise, in essence we have a shared set of objectives for regulation—

The Committee suspended for a Division in the House.

The Chairman: We are not all here, but time is tight.

Baroness Neville-Rolfe: I have a final supplementary. You have told us about talent and fintech, and I think we understand that, but what would

be really difficult to get agreement on? Would it be passports or super equivalence, that sort of thing?

Miles Celic: On the substantive issues that you mentioned earlier, there are a variety of areas that we need to consider. There is an overarching element, a sort of umbrella. On equivalence, we are public and on record as saying that we feel that it does not work. It is designed for third countries that do not have a free trade agreement with the European Union, and the hope is that we will end up with a free trade agreement. That certainly seems to be the ambition on both sides.

There are a number of elements that are granular and specific, which are related to Brexit but can be addressed outside the negotiations. One of those is contract continuity; that is particularly important. We would look for some movement on that, and I think that there is an appetite for that in certain parts of government on both sides of the Channel and among certain regulators, certainly in the industry. It is one of those that is outside the control of industry; it is to a degree outside the elements of the negotiations themselves. But it could be done, and it would offer a great deal of reassurance to companies and customers.

An important caveat to that, and generally to all my comments today, is that there is an interesting division within industry between large and quite a lot of medium-sized companies, which understand these issues, are seized of them and have the resource to look after them, and what we are seeing with a lot of smaller companies, which either do not have the resources for this or are simply unaware. So my big concern would be with the inoperables that we will see through the withdrawal Bill process, but also with things such as contract continuity. That is something that quite a lot of smaller companies are unaware of, and they may risk being part of a disorderly Brexit if we do not get a grandfather on those sorts of issues.

Baroness Neville-Rolfe: Have you thought of ways of overcoming that?

Miles Celic: One thing that we are looking at is how we communicate those issues. We have spoken to regulators about this and to government, and there is definitely a recognition of more needing to be done.

The Chairman: Thank you. To some extent, some of Baroness Falkner's questions have been answered, but I hand over to the noble Baroness to have a go.

Q24 **Baroness Falkner of Margravine:** You have already indicated that you think that there will be an agreement—although I think that it is fair to say that you are not very clear as to when that might happen. Who will be the winners and losers from a failure to reach an agreement, if there is a cliff edge? I have read your paper carefully, where of course you elaborate on the fact that you think there will be quite a lot of losses. Is there any upside? In the light of that, you will, of course, be familiar with the speeches given at the Reuters Newsmaker event and in Berlin by

Andrew Bailey of the FCA. He struck a slightly different tone in saying that we have had very robust financial services dominance since the corn laws, and that Brexit is not the end of the world. How do you interpret that? From the perspective of where you sit, where do you think the truth of the matter is in terms of gaining and losing? Can you comment on clearing in that regard, too?

Miles Celic: I think there are a variety of levels in that. First, there is absolutely no complacency in the industry about its position. The UK and London specifically is the number one international financial centre; that is confirmed in independent survey after independent survey. We have seen in the most recent survey an increase in the lead over New York, so the industry is in a good position, but it is not complacent. As we are seeing in terms of some of the jobs and activity that is moving, London is proving to be quite sticky. People want to remain in the UK—they want to find reasons to remain in the UK. There is no particular desire to leave the UK if it is avoidable, but it may prove to be unavoidable. As I have said, companies will need to serve customers.

On the longer-term reaction, Andrew Bailey touches on something really important. This is not about having a checklist. We have not created the world's leading international financial centre by simply sitting down and deciding that we were going to do so and creating a list of activities that were ticked off, then turning round at the end of it and saying, "Voilà, here we are, the world's leading international financial centre". Instead, this goes back literally centuries. You can look at the corn laws and right back to what is recognised as the world's first joint stock company being created here in the UK in the 16th century. All these things have contributed to the ecosystem that has developed over time. One key element of that has been Europe as the domestic market, effectively, for London. Perhaps I can continue the answer after the Division.

The Chairman: We will have to suspend again. I am sorry about that, but there we are.

The Committee suspended for a Division in the House.

The Chairman: We are quorate, so Baroness Falkner, the floor is yours.

Miles Celic: I am happy to complete the answer, if that would be helpful. The other parts of your questions were about who the winners and losers would be, and you asked for a word on clearance. What I said before was as prologue, to say that it is not just London; as I say, it is the fact that you have an interconnected ecosystem that connects, say, the asset management industry in Edinburgh and the legal services and fintech in Manchester with the work that happens in London as well. That means that what we have here in the UK is extremely difficult to replicate.

As I said, there is no checklist. The guy sat in any other European centre cannot simply say, "We will get our checklist out and create an international financial centre". Actually, therefore, the loser in a no-deal Brexit is Europe. The studies we have seen across this confirm that there

will be greater economic inefficiency across Europe, more fragmentation, fewer jobs within the industry and less supply for consumers. The example people always use is the German manufacturer who gets a loan from their company in Düsseldorf and does not necessarily recognise that a lot of the deal is done in London and then goes back to the institution they are dealing with in Germany. The winners under that basis are New York and Asia, and we are seeing an element of this. There is therefore a logic that as you leave the primary financial centre, you go to the next international financial centre. To a degree, we are seeing companies thinking, "If we are going to move activity from London, we can move it to activities that we currently have in New York and scale those up".

The other thing we are seeing—there has been some press reporting of this recently, although we have seen it for a little while—is the growth of centres such as Hong Kong, Singapore and Shanghai. Again, when you think logically about where clients want to book business, where the greatest returns come from, where you see the growth of what will be the largest single portion of the global middle class, this is all in Asia. So naturally, as the economic centre of gravity shifts to the east, financial and professional services will follow that. As any country goes up the development curve, as I am sure all Members will be familiar with, you start with low-end manufacturing and move to high-end manufacturing, consumer goods and then services. In the event of a no-deal Brexit, that is where we see the winners.

A word on clearing—I am sure you will be familiar with the arguments. There is no economic rationale for moving clearing from London, and we would argue that there is very little to no regulatory rationale for doing it. Chris Giancarlo of the CFTC recently appeared before the House Agriculture Committee in Congress, in the US, and made precisely these points. He has said before that a body of water is no impediment to good regulation. There is certainly no appetite among any of the companies we have dealt with for moving clearing from London. It is economically inefficient and also extremely hard to do. You do not simply unplug euros and move them elsewhere. These are bundled together with other currencies and instruments, because that is where you get the compression and netting effects and the efficiencies of price that come with that. An economic cost would be associated with doing that.

Baroness Falkner of Margravine: Briefly, you talked about business moving to east Asia and New York, and we have just seen the big announcement about Hong Kong. But I wonder whether you foresee an element with regard to London trying to remain pre-eminent. Do you see a level of regulatory arbitrage?

Miles Celic: That is an important question, which opens up a whole list of issues. The first point is that there is absolutely no appetite among mainstream industry for a regulatory bonfire—a sort of wild west of regulation. If anything, one of the things that keeps the UK an attractive place to come to if you are a foreign institution is the high standard of regulation and supervision here. We have seen absolutely no appetite for that from government or from regulators. It would be a retrograde step.

For any short-term benefit you might accrue from that, there would be a long-term cost in that being seen to do business in London would not carry that stamp mark of quality.

- Q25 **Lord Cromwell:** The financial services are certainly a great British industry, so all of us would want it to thrive and be successful and to remain here. But I am getting slightly mixed messages from some of the things you are saying. When business energy and activity run into political complexity—I think you have acknowledged there is a great deal of that—there is always this thing about, “Just get on with it or you will pay the price”. Can we come back to this issue of relocating out of London? What is the reality? You said that it is difficult to replicate and that anyway there is a move of the economic centre to Asia, regardless of Brexit. What is the reality? Are businesses crying wolf? Are their plans already well in hand? Have they already done more than just establish a footprint office in country X? Can you also give us some sort of quantification of the impact of what you foresee happening? Finally—I quote from evidence, if I could just bring it up—you say: “Once businesses start moving, there is no reverse gear”. Could you just explore that for us a little?

Miles Celic: On the reality, this ties into a number of issues. The first is that Brexit has triggered and catalysed a number of decisions that probably would have been taken over a longer period. You have absolutely identified this economic shift of gravity. There is the impact of disruptive technological change and what that means, there is return on your capital—where you best place your people, and so on. So a variety of factors are all tied into that. Absolutely, it is difficult to replicate what you have in London. The report that we did with PwC that we launched in June, which looked at the future of the industry in the UK, identified in almost every category that London is in the top three globally within the various subsectors of the industry. The UK generally is also an attractive place to live: it is relatively straightforward; it is somewhere where you can come to; there is a strong cultural scene, which is an important part of making it attractive for people; the universities are an important element of this; and you have the connectivity and the use of the English language. All of these are organic elements of an ecosystem. The risk with that is that if you pull any element out, it is difficult to foresee the impact that that will have on the ecosystem overall. But it also, as I say, makes it difficult to replicate.

Lord Cromwell: With respect, you are having it both ways. Either we should be frightened that these companies are all going to get up and relocate, or they are not, because of the many attractions. Which is it?

Miles Celic: The point is that they do not want to. This is the point that I am trying to make, but perhaps not as clearly as I would like. They do not want to relocate, but ultimately they have to be able to service their customers. As I say, if they cannot service those customers on the first day after Brexit, that is a major issue for them; you are failing your shareholders, employees and your customers.

On quantification, as we said in the evidence we provided, we commissioned Oliver Wyman to run a completely independent study of this. I tend to dislike the terms “hard Brexit” and “soft Brexit”, as they are somewhat amorphous shorthand, so we spoke to Wyman and it produced a spectrum of high access to low access. At low access—effectively, WTO—the initial impact is about 75,000 jobs out of the whole ecosystem and about £18 billion to £20 billion of economic activity, which is about 40% of the European activity. As I say, a lot of this is bundled together, but it is about 40%. What is interesting in some of the conversations we are having with companies that are already members or with companies that are coming to the UK to seek to be members is that they are looking at the strengths of the UK as a domestic market—and it remains a major domestic market; it is for many still the third largest insurance market in the world, for instance—and they are looking at London as an international centre. I think that they are taking an option, if you like, on London as a European centre and will wait to see where Brexit gets them.

On what that therefore means for the longer term—this is what we are struggling with—it is very difficult to get a sense of what it means for the critical mass of London as a financial centre. That is the risk that I alluded to earlier with regard to the ecosystem. If you remove an element of it, you can quantify that impact in the short term, but over the longer term, does London lose a certain critical mass so that you end up with just a further fragmentation of the European economic and financial services ecosystem that currently exists?

Lord Cromwell: But to go back to my earlier point, part of what you are saying to us is that that will happen anyway; this may be the trigger moment, but Brexit is not actually that relevant to it. It will happen anyway because of the way the global economy is shifting. Could you also address my question about the reverse gear?

Miles Celic: On the trigger point and the impact, my own view is that we will probably see the emergence of three major international financial centres. That is what we are seeing: New York, Europe—I hope London, within that—and a centre in Asia. That effectively gives full coverage throughout the working day, across the entire globe. The challenge for the UK is to retain London as the international financial centre in Europe.

In a speech in February, Wolfgang Schäuble made the point that certainly in the short to medium term—we are thinking decades here—London will remain Europe’s international financial centre. If we can get to a Brexit deal that allows that to continue, because it is ultimately in the interests of both sides, then you can continue to play that role in the European economy which Britain has played predating the existence of the European Union.

On your point about a reverse gear, at this point, companies will need to make the minimal possible footprint that is a minimum credible presence in the markets that they need to be in. Anything else is the unnecessary expenditure of money, the unnecessary allocation of capital and either

moving people or employing people locally that could be avoided. This is all cost. One of the large institutions I spoke to costed the move that it would need to make—it is not one of the larger moves—at around £100 million in the first year and about £50 million subsequently. Any planning director who goes to their board and says, “I need to spend £100 million to move these people so we can guarantee that we can serve our customers on day one after Brexit”, will not be in a strong career position if they then go back, 12 months later, and say, “We need to spend a significant proportion of that moving everybody back”. It is much more likely—this is what we are seeing—that people will shift what they have to shift to be certain that they can guarantee that they serve their customers on day one. Then, depending on where the final deal moves to, you have the option of scaling up or keeping it at roughly the same level you are at.

The Chairman: Can I follow up one aspect of that? If you are in a bank and you are making these contingency plans, at what point do you decide that now is the moment to make the decision and move? Is it in November? Is it in January? What has to happen before that decision is made?

Miles Celic: That differs from institution to institution, often depending on how they are structured and what they might already have in the European Union. As I said earlier, most institutions will want to see significant progress this side of Christmas, and certainly in Q1 2018. I would have thought that that will be the trigger point—the point of no return for most companies.

What drives that decision is the need to apply for a banking licence if you are a bank; the need to apply for a particular form of insurance permission if you are an insurer; or whatever it may be if you are in any other part of the industry, whether that is legal firms, asset managers or whoever. You work back from that point. You work back from the day that the UK leaves the European Union. Getting a banking licence is usually a 12-month process, sometimes a bit longer. Ditto the insurance processes. You need to build in the following fact. Take, for instance, Dublin. In 2014-15, Dublin agreed a single digit number of new banking licences. That is the capacity that exists within the regulators. If you know that your competitors and peers are also going through that process, you want to build in time for that. You want also to build in time to get office space, which is often a long lead time and, in many of these centres, very limited. For example, Dublin has a limited amount of office space and Frankfurt is in a similar position. You want also to look at the people you need to move. Again, in many cases you are talking about people who might need to move families or get children into schools. These are all moving elements of the decision.

The Chairman: What would businesses and banks need the Government to have done by Christmas to prevent this move outside London from happening?

Miles Celic: We can do something to minimise that, which would require both sides to step outside the sequencing that currently exists in the talks and make a commitment that there will be a transitional period at the end of this. Pretty much everybody you speak to privately in the European Union accepts that there will almost certainly be a transitional period, if there is a deal. That is the nature of how these debates and negotiations happen. I think that that is now largely publicly agreed as well. Having that certainty means that financial institutions can decelerate their plans. It gives them additional time to scope out what they need to do. Some companies will take the view that the political risk is such that they will need to make those moves whatever; they will not be willing to bet on there being a deal. A number of companies have said that explicitly to us. However, most companies are looking for the opportunity to maintain the optionality and decelerate, and therefore slow down the process. What we cannot do is effectively create a transitional process that simply delays a cliff-edge effect. There has to be a transitional process that leads to a deal.

Lord Cromwell: I have a small supplementary on this, and I am thinking perhaps of folk looking in on your testimony. It may be an obvious question but it needs to be answered. Do most of the financial institutions that you are talking about not already have footprints all over Europe?

Miles Celic: Many of them do, but it is about the nature by which they are currently regulated. It is an important question. The nature of the passporting regime that currently exists allows a company that is based in the UK to conduct operations across the European Union, and vice versa, providing those services to customers. The nature of leaving the European Union and the single market means that we will lose access to the passporting regime, so we have to find an alternative that allows us to continue to serve customers.

The Chairman: We will have some further questions on the transitional period in a moment. But before that, Baroness Armstrong.

Q26 **Baroness Armstrong of Hill Top:** You mentioned no deal. There is a lot of debate about what no deal would mean, which is what we are trying to tease out in this inquiry. What action should the Government take to ensure that the financial services sector in the country as a whole is well prepared for the no-deal scenario? Is that a real issue in your sector? Are they thinking about it and, if they are, can you tell us what they are saying? Do you feel that the Government are fully engaged in the discussions you are having with your membership around that?

Miles Celic: This is an important issue and, as you can imagine, it is very high up the agenda for the companies that we represent. We have a very positive and constructive ongoing dialogue with our main sponsor department, the Treasury. It is seized of this and looking at it as an issue. We have had engagement with government departments across the piece, with Ministers and officials from all the key departments for the industry that we represent. But it is broader than government. As a heavily regulated sector, the role of regulators and supervisors is

particularly important. The PRA and the FCA have worked with companies to ensure that the financial stability and customer disruption risks are addressed, which is very important in this. As you will be well aware, the FCA and the PRA have been in touch with companies on this and we have looked at what needs to be done in order to make sure that clients can be served.

In any well-run, highly regulated industry, that is what we ought to be doing anyway. The risk management committees of all the companies that sit within our membership would be looking at this. They would have been exploring, before the referendum, the risks involved in this. There has been a huge amount of preparation within the industry for the potential ramifications of a no-deal scenario. That is what feeds into the need to potentially move some operations into the European Union to address that.

Going back to the point you mentioned earlier, one of the risks is that smaller companies are less engaged with this. As I said, we are looking at that to see how we can better communicate the need to engage. The flipside is that often most of those companies are more domestically focused, but that does not remove the need to address those issues.

The Earl of Kinnoull: Staying on that subject, I wonder whether you can give me some colour by sector. It strikes me that the different sectors are in very different states of preparedness and propensity for damage.

Miles Celic: First, there is a broader ecosystem point, as you say, which we have talked about. I can obviously speak only to the ecosystem that we are in, but the banks and insurers are dealing with the need to secure the licences or permissions that they will require. I think that asset managers are looking at this in their own way, partly because of the way that asset management works. But it is broader than just the financial institutions. In the accountancy or law firms, say, there is an important role in the permissions that exist for lawyers to be able to conduct legal work in the European Union. The law firms have been very engaged with that. From memory, in the last 12 months or so, 1,100 UK solicitors have registered in Dublin so that they can continue to provide services to clients on the continent. I would expect that to continue.

This all ties in to the nature of the recognition of professional qualifications and standards. You are right to identify that each subsector of the industry has its own challenges, as well as those that are common. With regard to which part of the industry is more developed and advanced, I do not get the sense that any particular part of it is further ahead than others. Because of the nature of the way that TheCityUK and the ecosystem operate, everybody is well developed on those priorities. The feedback we tend to get is that we are probably slightly further ahead than many other industries.

Q27 **Lord Teverson:** Forgive me for being late to this Committee, Mr Celic, and if you have answered this before then please say so. We seem to

concentrate so much, understandably, on UK-regulated businesses that have passporting into the rest of the EU 27. Should we not be doing more about those which I would have thought important to our ecosystem—I do not know how big they are; probably not as large—which are regulated from within the other 27 and passport into the UK? Are they not also important to the UK system, and what can the Government do about that? I do not know whether we could unilaterally offer equivalence but should we be—or are we—doing something about this?

Miles Celic: You have hit on an important issue, which ties into the nature of there being a European financial and professional services ecosystem. It is difficult simply to take the UK out as a module and ignore the existence of the 27. You have a significant amount of passport traffic in both directions and, as I said earlier, the UK remains a major domestic and international market. That is very appealing to a lot of European companies and the ability to access it from a European perspective is incredibly important. Most of those institutions that you talk about already have a significant presence in London. In the conversations we have had with the institutions in Brussels, in member state capitals and with counterpart organisations, we have certainly stressed that there is a lose-lose scenario from a European perspective if we get this wrong.

If you look at Europe in its totality, the financial and professional services industry is one of the few remaining industries where Europe is a global leader and globally competitive. A bad Brexit deal simply would undermine that—again, on both sides of the Channel. If you really want to have a champion European services sector that can compete with the Americans and the Asians over the long term, a positive and constructive Brexit deal will help to make that possible. A poor Brexit deal will make it much harder.

Lord Teverson: What about those companies and businesses that are passporting into the UK? Are they having to go through all those issues themselves and are we going to lose them as well?

Miles Celic: The passport, such as it exists—ultimately, as you will be well aware, there is no single such thing as the passport as it is tied into a number of directives; from recollection, there are 17 directives covering 39 effectively different passports—will be gone, once we are out of the single market. It is therefore a question of the best possible regime to replace that. We feel that that will be mutual regulatory recognition. We have taken that around European finance ministries, European institutions and European counterpart organisations. Typically, the feedback we get is, first, “That is ambitious but not unrealistic”; secondly, “If we were in your shoes, that’s pretty much what we would design, too”; and, thirdly, that the politics will be the difficult bit.

Q28 **Lord Whitty:** On the transition arrangements, hitherto most of the commentary has been about whether it will be a transition period to something that we know or a phased implementation period for something that is already agreed. You have, I think, been the first person

to say to us clearly that this should be a two-stage process, with a bridging agreement and then an implementation agreement as we feed into a free trade agreement. Could you give us more clarity about what you would expect to happen during the two periods? How much would you need to have agreed on the nature of those periods, possibly on length as much as anything else, by the first quarter of next year? You have already said that there will be less value to it, which presumably means that people will make decisions if we do not get an agreement by then.

Miles Celic: I think the Chancellor has described a transition period as a wasting asset; I absolutely agree with this characterisation. With every day that goes past it is worth less and less, hence the need for an early agreement on it. On the way we see the bridging and adaptation periods operating, and what needs to be achieved to make them happen, if everything can be agreed within the Article 50 process—as the Prime Minister has suggested—then there is no need for a bridging period. As I say, that would be an ambitious ask.

If we do not achieve that, the bridging period ought to be used to finalise the detail of what the comprehensive free trade agreement looks like. We can use the Article 50 process effectively to agree heads of terms: the broad principles under which the free trade agreement would operate and what would be included in it. From our industry's perspective, we would ideally like it to include services. Obviously, most free trade agreements have not included services to any meaningful extent, but this is an opportunity to do that.

On the bridging period itself, my point of view is that there is no time to design a bespoke transition period from scratch. Therefore, we would need a bridging period based on something that is, effectively, off the shelf. Whether that is EEA or EFTA, or something along those lines, remains to be seen. During that period, we would effectively have a stand-still arrangement. We are concerned that that period should not be excessively long and leave the UK as a rule-taker. We do not feel it appropriate that the world's leading international financial centre is a rule-taker during that period. You could not imagine New York agreeing to be a rule-taker for any significant length of time if it were in our shoes, so we would need a time-limited bridging period during which the FTA is agreed. We would then move into the adaptation period. The nature of FTAs is that you go through and agree them, then move to an adaptation period where it is effectively bedded in.

Lord Whitty: You are describing it as necessary for the interests of your financial sectors to gain that from a British point of view, but what is the balance of advantage or negotiating strength in terms of getting a transition agreement? Will the Europeans see it in the same light or is there a difference?

Miles Celic: I think a variety of factors play into this for the transition period and the comprehensive FTA. I can speak only on behalf of the financial and professional services industry but, in our view, this and the

mutual regulatory recognition that would underpin it would clearly be to the advantage of the entire UK economy, especially to highly regulated elements of the UK economy.

On the balance of advantage, from recollection the European Parliament issued an analysis relatively recently suggesting a €63 billion hit on the European Union from a no-deal Brexit. What we tend to hear from European audiences is: "We are willing to take a certain degree of economic pain to maintain the political aims of greater European integration, and to take a certain degree of economic pain to maintain the integrity and success of the single market". Our response is, "You don't need to. You can have both a transition period and a strong, comprehensive free trade agreement with the UK which do not undermine the single market in any meaningful sense whatever and would maintain the strong economic links between both sides".

The UK is about 15% of European GDP—I am sure you are familiar with that stat. The UK financial and professional services industry is about 40% to 45% of that entire activity in the European Union. One of the advantages of mutual regulatory recognition is that it will allow for that parity between the two. So it depends on a case-by-case basis, but broadly speaking our sense is that we can obviate an entirely unnecessary and avoidable economic risk by going down a more positive route.

Lord Whitty: May I add one more rider to that? I do not think that you covered this point in answer to Lord Cromwell. Would, as some commentators have suggested, a failure to get an effective transition period or having a half-baked one be to the main advantage not of Frankfurt, Paris or Dublin but of New York?

Miles Celic: That is absolutely right. The analysis that Oliver Wyman did for us last year suggested that New York and Asia would be the big winners of a no-deal Brexit. That is to the detriment not just of the UK but of the European financial and professional services ecosystem. There will be fewer jobs and less activity across Europe. This is not just some abstraction that impacts on the industry; it would mean less financing for European companies and it would be harder and more costly to get a mortgage, to invest in a business and to save for your retirement or to send your kids to university. Those are all impacts across the rest of the economy that are entirely avoidable.

Q29 **Lord Liddle:** I want to explore the notion that it is ambitious to have sorted out your sector by the middle of next year. You say that you do not want to be a rule-taker. Does that not mean that in practice the EU 27 will say that we have to go through all the financial legislation that there is and tell them where we want to diverge and why? They will say that they have to consider whether it puts them at a regulatory disadvantage to us. They will say, too, that their currency is the euro and that they have to make sure that they are satisfied with the stability of the financial institutions dealing in euros in London every day, because that could have a serious impact on the euro economy. Are those not

perfectly reasonable propositions on the part of the EU 27? If they are reasonable, how then would you think that in a six-month or eight-month period you can come to an agreement and sort all those issues out? You say that we cannot be a rule-taker because we are so important but, if there are disputes, how do envisage them being settled? What are you putting forward as a dispute resolution mechanism that would be binding on the EU 27 and the City of London?

Miles Celic: There are several segments to that.

Lord Liddle: It is a big agenda.

Miles Celic: It is a huge agenda, and one that will last for some time. On the rule-taker element, our proposal for a bridging period, which would take an off-the-shelf solution, would necessarily mean that the UK would be a rule-taker for a particular period. But there is a nuance to this; as with so many of these issues, it is not purely black and white. Many of the rules that will be implemented during that period are British designed. It is in the nature of European regulation in our industry in particular that, because we are home to Europe's international financial centre, there are a disproportionate number of British citizens in European supervisory authorities and a disproportionate influence in terms of the regulatory and legislative dynamics in Europe for our industry. So during the period that we are a rule-taker, we would be implementing, under the auspices of the EU, rules that were largely designed and created by the UK, with British MEPs involved in all this, and so on.

From recollection, the fastest reasonably we could get a new piece of legislation through the European Union would be about four years—and I suspect that that would be at a pretty break-neck pace. I was fortunate enough in my days in the insurance industry to work on Solvency II, which took 17 years from start to finish and, I suspect, paid for many mortgages during that time for an army of consultants and others. So I do not expect that there would be a vast slew of new rules coming in during the bridging period.

Once we move from being a rule-taker into a position of regulatory and supervisory equality, another issue is how we address and manage regulatory alignment and, indeed, divergence. The proposals that Hogan Lovells has helped us to work on, on mutual regulatory recognition, provide a framework for that. In essence, in simple terms, you say, "These are the shared objectives for our regulatory systems, around customer protection or financial stability or capital requirements, or whatever it may be. We accept—and it would certainly be the case on day one—that the rules are identical, and that the regulatory and supervisory systems are of comparable quality". Then you create a process that goes with the grain of what already exists, accepts minimum international standards where those are appropriate and builds on those.

The process would be to create, first, a forum where regulators and supervisors can continue to gather in exactly the same way as they

already do, to manage the ongoing alignment or divergence. Where divergence is created, there is a cost to that, which is worked through in collaboration with the regulatory authorities. It may be, just to pick an example at random, that the UK takes a different route on insurance, or the Europeans may adopt a different route on insurance over the longer period. What you end up with in that particular space may be a reduction or elimination of access, or greater capital or supervisory requirements being put in place, whatever the appropriate outcome would be.

On dispute resolution, typically, disputes—certainly in free trade agreements and on many regulatory issues—are dealt with in the lower foothills, before you even need to get to dispute resolution. However, we would envisage the creation of a specific dispute resolution body that would have both UK and EU judicial, supervisory and regulatory involvement, allowing for the resolution of any disputes that might arise. On activity that happens in the UK but which would be systemically or economically important, from a European perspective, the detail would be important but we would be broadly comfortable with the idea of supervisory visibility for European supervisors for any activity that meets those criteria.

Lord Liddle: So the ECB would remain in charge of that section?

Miles Celic: It would not be in charge. The precedent has already been set. If you are a British company with a large American operation that has economic or systemic significance, the FCA can currently go and look at your American operations. That is a principle and precedent that has already been enshrined at international level. We would be broadly comfortable with that although, as I say, the detail would be an important element in terms of supervisory visibility for European supervisors into the UK—and, importantly, vice versa, because the traffic will go both ways. That would go with the grain of ongoing regulatory and supervisory co-operation.

The Chairman: We should begin to move towards a close.

Baroness Neville-Rolfe: I have one point of clarification. You talked about the cost of no deal being £18 billion to £20 billion in revenue, from the Oliver Wyman report. Lord Teverson asked you a question about what would happen to Deutsche Bank and BNP Paribas. My question is how you have allowed for that in that number. Have you assumed that they will continue to have passports here, or have you assumed that they will not?

Miles Celic: The £18 billion to £20 billion is based on a WTO-terms Brexit, whereby we would leave the European single market and all the elements of the European Union. The model was based on moving to WTO and at that point having to look at the current third-country regimes that exist for countries that do not have a free trade agreement with the European Union.

Baroness Neville-Rolfe: On your scenario, would we allow Deutsche Bank a passport, or not?

Miles Celic: I would need to check what is in that—and I am perfectly happy to go back and double-check what the assumptions were in that model.

Q30 **Lord Woolmer of Leeds:** I have two questions. I assume that if no deal is agreed—that there is an agreement that there is no deal—you would still need a transitional period. I assume that is right. My broader question is this. You talked of the Government and the regulators being fully engaged in putting together a proposed deal and being fully prepared for no deal. You strike a note of great optimism, even though you think that the Prime Minister's aim of October next year is somewhat optimistic. Are you saying that the British are fully prepared for the negotiations coming up and are fully prepared for no deal? That is not the impression that the public or Parliament gets. Are you telling us that there is no reason for the Government not to be able to negotiate, because it is fully prepared and well engaged with the industry and that the only issue now is the political will on both sides to convert this into an agreement? Are you saying that it is not a question of agreements within the UK and that the Government and industry are well prepared for the negotiations? After all, transition has to be agreed by March next year and the whole deal has to be agreed within 12 months.

Miles Celic: Can I just clarify the first part of your question, which is that a transition period would be required in a no-deal scenario as well?

Lord Woolmer of Leeds: There will need to be a transition in some form.

Miles Celic: From our perspective, a no-deal scenario means that there is nothing to transition to, so there is no transitional period.

Lord Woolmer of Leeds: No adaptation period?

Miles Celic: Under that circumstance, there is no transitional agreement, because you have nothing to transition to; there is no agreement that you can move towards. You effectively just stop being a member of the European Union. At that point, you have to move to all the mechanisms that are in place for a third country, so there is no free trade agreement.

From the point of view of the UK financial and professional services industry, you are dependent in certain cases on the third-country regimes that exist, applying for individual equivalence decisions. Those decisions are political as well as regulatory; in fact, they are more political than they are regulatory. If the negotiations have fallen apart in an acrimonious way, that suggests that that political agreement might be harder to come by than would otherwise be the case. You are also dependent, if you are a lawyer, an accountant or another professionally qualified individual, on the European legislation in place on the recognition of professional qualifications. In some cases, that is also dependent on a state-to-state basis. So you have something that needs to be looked at both at European level and on a state-to-state basis. There might be certain things that could be done if the political will

existed on, say, contract continuity, but again that would be a significant risk. So there is no transition—there is nothing to transition to. That is what some people term “the cliff-edge effect”: effectively, you drop out of the European Union with no deal. That is economically entirely suboptimal and, I would argue, economically and politically entirely avoidable, if we play our cards right.

That goes to your second point, which is on whether we are comfortable that the UK Government has thought through what needs to be addressed and what needs to be done. I can only speak on the issues that we engage in with the Government. The Treasury, as our main sponsor department, has been extremely well engaged on the key issues that are important to this industry. The Chancellor’s Mansion House speech in June and what the Bank of England governor has said have been a fantastic recognition of the issues that the industry needs to deal with—the areas where the industry needs reassurance and the issues on which the industry needs progress. We were very encouraged by that. As to the engagement on the key issues at official level, from the City Minister, Stephen Barclay, and from the Chancellor himself, we could not ask for more.

The Chairman: Lady Wilcox?

Baroness Wilcox: We have had a good coverage of that, Lord Chairman, and I think that my questions have been answered, so we can move on.

Q31 **Baroness Falkner of Margravine:** I have a short question about what you were saying on the need for transition this side or the other side of Christmas. We are hearing that a political declaration at the end of the next European Council in the communiqué would give some reassurance. Would that be ample or would you want something legally written in?

Miles Celic: It would not be ample. In fact, I suggest that for many companies it would not even be sufficient. This is the conversation that we have when we are in member state capitals. People will say, “There’s a sequencing, which has been agreed. Monsieur Barnier has a mandate to discuss each individual element at each individual phase of the process. He does not have a mandate from the member states to discuss a transitional agreement.” Our contention has been, which is why we thought that the Florence speech was a useful step forward on the British side, that we should take it out of the sequencing. This is so important and so clearly in the interests of both sides that we should take it out of the sequencing and have a legally binding agreement between the UK and the EU 27 that there will be a transitional period. You can set out the principles of that transitional period. It would be difficult precisely to identify the granularity of it, but you could set out the principles under which that transitional period would operate. You could do that via a number of mechanisms. I would say that an MoU lodged at the UN, which is one of the possible measures, would give many companies the reassurance that they can not switch the engine off but at least, as I said, take the foot off the gas to a degree. The political risks around this mean

that every time there is an explosion of political disagreement or rancour on either side of the Channel—I am not finger-pointing at anybody in particular—companies doubt whether there will be a deal at all. At that point, the transitional process becomes academic.

Lord Selkirk of Douglas: You have answered all the questions that I wished to ask, but, for the sake of clarity, may I ask you to summarise what you believe are the most important elements of a strategy for a successful outcome?

Miles Celic: I would summarise them as follows. The immediate and urgent short-term priority is the agreement of a transitional period—a commitment to a transitional period between the UK and the EU 27. In the medium to longer term is the agreement and the securing of a comprehensive free trade agreement between the UK and the EU, based on mutual market access that is as frictionless as possible and as close to the current situation as possible. It needs to be a bespoke deal, specifically for the UK and designed for the relationship between the UK and the EU 27, which is unique and unlike any other in the world. It must build on the Prime Minister's commitment of a special and deep partnership with the European Union that is based on mutual regulatory recognition, as we have talked about during this session. On the broader dynamic, it should underpin the fact that, as I think has been said, the UK is leaving the European Union but is not leaving Europe and that the relationships—personal, commercial, strategic or Government to Government—that exist both at EU level and at nation-to-nation level will be a fundamental underpinning of prosperity and security for both sides as we go forward.

The Chairman: That is a good note on which to end. You have given us a huge amount to think about and a lot of valuable evidence, interrupted by two Divisions. Thank you very much on behalf of us all. I am glad to say that our Bavarian friends sitting behind you have been taking copious notes throughout your evidence. Thank you. We are most grateful to you.

Miles Celic: Thank you.