

31 January 2017

Rt. Hon Andrew Tyrie MP
Chairman, Treasury Select Committee
House of Commons
London
SW1A 0AA



Dear Mr Tyrie

Inquiry on the U.K.'s future economic relationship with the E.U.

The role of the Financial Markets Law Committee (the "FMLC" or the "Committee") is to identify issues of legal uncertainty, or misunderstanding, present and future, in the framework of the wholesale financial markets which might give rise to material risks, and to consider how such issues should be addressed.¹

The Committee regularly produces publications that are received with widespread approbation by both industry and public sector bodies, domestically and overseas. These are available on its website at www.fmlc.org. The Committee also regularly engages with members of the European Commission, Financial Stability Board and international regulators on matters of concern to the wholesale financial markets.

Following the result of the E.U. Referendum, the FMLC announced that it would work with experts in law and financial services to identify, analyse and address legal uncertainties relating to the U.K.'s withdrawal from the E.U. ("Brexit") and that it would establish a High Level Advisory Group ("HLAG") to give direction to the Committee's future work in this field. Its research programme is now well under way.² In this context, the FMLC welcomes the opportunity afforded by the Treasury Select Committee's inquiry into the U.K.'s future relationship with the E.U. to contribute to the ongoing discussions on securing the optimum transitional arrangements for an orderly withdrawal.

In a speech delivered on 17 January 2017, Prime Minister Theresa May offered an outline for the U.K.'s coming negotiations with the E.U., stating her intention to obtain a customs agreement with the E.U. that leaves the U.K. free to reach individual tariff schedules at the World Trade Organisation ("WTO") and to seek transitional arrangements for financial services. She observed that the U.K. "cannot possibly" remain within the European single market.

In accordance with this plan, at the end of the two-year Article 50 notice period, when the U.K. ceases to be a member of the E.U., it will automatically lose all access rights to the European single market in financial services and will become, from the perspective of E.U. law, a "Third Country". While there exist already under many E.U. regulatory measures Third Country regimes that allow financial services activities to be conducted on a cross-border basis, there remains uncertainty as to the conditions that the U.K. and British regulators will have to satisfy in order to be able to secure a

¹ In view of the role of HM Government in the negotiations for withdrawal, Sinead Meany, Stephen Parker and Sean Martin took no part in the preparation or discussion of this letter and it should not be taken to represent the views of the Bank of England, HM Treasury or the Financial Conduct Authority.

² The text of the announcement and further details of the FMLC's work in this area are available at: <http://www.fmlc.org/the-fmlcs-work-on-brexit.html>.

positive determination on access and the timescale within which such determinations might be made.

Given the uncertainties just mentioned, market participants in the U.K., who will lose their “passports” to the E.U. single market for financial services upon Brexit, regard it as essential that the U.K. and E.U. should agree transitional arrangements as early as possible. The FMLC is of the view that such arrangements would offer a valuable means of promoting legal certainty and minimizing the disruption which could occur if there is any *hiatus* between the availability of the financial services “passport” and the application of the Third Country regimes.

A *hiatus* of this kind could mean that U.K. providers of financial services would be—at least temporarily—deprived of access to key E.U. markets unless they were first individually to acquire authorisation (either for a subsidiary or for the U.K. firm “directly” *via* a branch). For many, this would require establishing a new entity within an E.U. Member State or otherwise restructuring the group.

Decisions of this kind must be taken well in advance of the point at which the U.K. withdraws from the single market and so the process of giving notice under Article 50(2) is likely to increase the pressure on firms to put restructuring decisions into effect. Transitional plans could ease this pressure by reducing practical uncertainty about access to the single market for a period beyond the two-year period specified in Article 50(3) of the Treaty of the European Union.


In light of these considerations, the question of transitional provisions would appear to be an urgent one. Nevertheless, given the complexity of the issues and markets at stake, the Committee takes the view that the question would benefit from as much careful research and analysis as time will afford. One way in which to reconcile the exigencies of the political timetable with the intricacy of the issues at stake would be to adopt a staged approach, starting with areas where the mutual benefit for both the E.U. and the U.K. in preserving current arrangements is clearest or the issue is otherwise uncontroversial. (One example of such arrangements that could usefully be made is the continued use of London-based financial benchmarks for valuation and reference rate purposes by E.U. supervised entities, and *vice versa*.)

Assuming that transitional arrangements are found to be desirable from a policy perspective, it will be important to consider the status under international trade law of any such arrangements. In particular, the General Agreement on Trade in Services (“GATS”) of the WTO contains “most favoured nation” (“MFN”) provisions, which require, subject to exceptions, WTO member countries not to discriminate between services and service providers from other WTO member countries. While the GATS, in effect, exempts certain mutual recognition agreements between WTO member countries from this strict version of MFN, there is legal uncertainty about the scope and ultimate effects of these provisions which should, therefore, be taken into account as any transitional agreement is designed and negotiated.

The FMLC is in the process of analysing and addressing legal uncertainties in the context of Brexit and has undertaken to publish, in particular, work in relation to Third Country regimes in European financial services regulation. The Committee expects to have further comments to make on transitional issues based on such future work. In the meantime, the Committee remains at your disposal should you require further clarification on issues of legal uncertainty arising from Brexit in the wholesale financial markets.

I and Members of the Committee would be delighted to meet you to discuss the issues raised in this letter. Please do not hesitate to contact me to arrange such a meeting or should you require further information or assistance.

Yours sincerely,

A handwritten signature in black ink that reads "Joanna Perkins". The signature is written in a cursive style with a large initial 'J'.

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