HMT Balance of Competences Single Market: Financial Services and the Free Movement of Capital Review

Barclays Response

17 January, 2013

Introduction

Barclays welcomes the opportunity to respond to the Balance of Competences Review – Single Market: Financial Services and the Free Movement of Capital Review ("The Review).

Barclays operates in multiple European countries, including the United Kingdom where we are headquartered, and undertake business with, and on behalf of, European and international clients within the Internal Market.

The Review comes at an important moment in the lifetime of the current EU legislature, with European Parliament elections and a new European Commission in 2014, as well as the first moves towards the Eurozone Banking Union, and an unprecedented amount of EU legislation both governments and industry have had to and are contending with. This provides an opportunity to reflect on where both Government and industry have come over the past 4-5 years.

Broadly we are happy with the balance of competences between the UK and EU – and we remain advocates of European rules. However, in answering the questions of the Review, we see a number of key principles as being common themes in our response. These we think go some way to ameliorating the EU legislative process, better serving governments and industry alike. These are:

- Simplifying the EU legislative process: The European policy making process is complex and revision should be prioritised to ensure there is adequate time for consultation and revision processes; and compelling impact assessments and proper cost benefit analysis is undertaken.
- Prioritisation: As a broad point, we believe that prioritisation of reform is crucial and that a focus on a few select reforms can disproportionately contribute to increased financial stability. Implementing G20 recommendations and agreeing the Banking Union are good examples of this. An effective cumulative impact of all current, and proposed, legislation would also act as a useful guide.
- Subsidiarity: Greater consideration should be given to principles of subsidiarity and proportionality. We have been unsatisfied that these criteria have been adequately complied with.

We would be happy to discuss any of this in further detail. Please contact Edmund Lakin, Assistant Vice President (Edmund.j.lakin@barclays.com)

Yours sincerely,

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Consultation questions

Question 1: How have EU rules on financial services affected you or your organisation? Are they proportionate in their focus and application? Do they respect the principle of subsidiarity? Do they go too far or not far enough?

The creation of the Internal Market has been a commendable and ambitious project since its inception in the Single European Act. In the field of financial services, the Financial Services Action Plan (FSAP) was the project that most clearly took the internal market commitment and brought it to fruition. The FSAP aimed to develop financial markets into one of the most integrated parts of the Single Market. Since at least 1999 EU rules have had a material impact on Barclays.

Post crisis and as a result of the G20 agreement, there has been a notable emphasis towards further regulation in financial services. The shift towards more regulation has become prominent as the guiding principle has shifted to financial stability rather than market integration.

Whilst the majority of the rules we consider to be proportionate, there are many cases where the regulations have had little or no market opening effect and may have even contributed to European and international market fragmentations.

The principle of subsidiarity already exists in the Treaty and is examined in the context of impact assessments. It is not clear, however, that it is given due consideration. It is crucially important and becoming more so that the subsidiary principle is adequately considered.

A recent example of where we see a proposal not complying with the subsidiarity principle is the Payments Account Directive. In this proposal the European Commission chose to favour legislation which would seek to create cross-border access to payment accounts & and switching, despite there being no such evidence to suggest there were major obstacles for consumers accessing a payment account or showing demand for cross-border bank accounts. This is an example where the issues should have been covered at a national level.

Question 2: How might the UK benefit from more or less EU action? Should more legislation be made at the national or EU level? Should there be more non-legislative action, for example, competition enquiries?

The UK has benefited a lot from EU action. The banking system, thanks to successive reforms of the capital requirements framework, is now considerably more resilient. Vital and important steps have also been taken to create a bank resolution framework (Bank Recovery and Resolution Directive) in the EU and we greatly welcome its conclusion. In addition, the steps being taken in building a Banking Union have helped to restore a sense of trust that the steps Europe is enacting are necessary to maintain financial stability.

What both the UK and EU would benefit from is the right EU action. In particular prioritisation is vital. The European Commission's drive to implement G20 recommendations and the steps taken so far on the Banking Union are a good illustration of this; and how a focus on a few select reforms can disproportionately contribute to increased financial stability.

Since the financial crisis, regulatory reform in the EU has been proposed at an unprecedented pace. At the end of 2013 there were over thirty proposals (relevant to financial services) being negotiated within the EU, with a lesser number in the pipeline, despite only a fraction of this number having been agreed during 2013. In particular, we would like to highlight the forthcoming EU Bank Structural Reform proposals which the current European Commissioner for the Internal Market is trying to finalise in the near term. Legislation on structural reform is very important to banks and bank investors, and any legislation here does draw attention to institutions. This raises the question of whether legislation of such complexity and importance should be proposed at this point in the life-cycle of the European institutions when, realistically, there is no chance of it entering legislative negotiations until 2015 at the earliest and reaching agreement until 2016-17. We would argue that in this instance, such legislation should wait to be proposed when there is a realistic chance of it commencing legislative negotiations – and the Commissioner proposing it is able to deliver it under his mandate.

Finally, the increased incidence of the use of Regulation rather than Directive – while welcome from the point of view of ensuring a Single Rulebook in areas subject to EU legislation – highlights the importance of weighing carefully the suitability of EU level rulemaking. In our view non-legislative action can be useful, especially where subsidiarity has been given due consideration. However, we believe that there is no need for the EU to undertake sectoral investigations into financial services, as it has done previously (e.g. 2005-2007), particularly given the increasing involvement of national regulators in competition in financial services.

Question 3: How have EU rules helped or made it harder to achieve objectives such as financial stability, growth, competitiveness and consumer protection?

Ideally EU rules, at all times, should seek to find a balance between financial stability, growth, competitiveness and consumer protection. However, in a post crisis world they have tended to focus on stability at the detriment of growth and competitiveness. This has been notable during the current European Commission where delivering the G20 recommendations and completing the Banking Union have taken precedent.

Financial stability

Where the EU has played a strong role is in the implementation of the G20 commitments, which have been of great importance. The Banking Union also provides another good example of where the EU is seeking to achieve the objective through greater pooling and coordination between the Members of the Single Currency.

Consumer protection

We strongly believe that the right level for consumer protection measures is at the national level, as consumer/ retail markets remain largely domestic. We consider that many consumer rules do not offer anything new or innovative for the end user.

Competitiveness & Growth

EU legislation should at all times aim to ensure that there is no detrimental effect on European firms in markets beyond the EU in which they operate. There should be a rigorous cost-benefit analysis of the global application of EU rules to EU firms. Latterly the European Commission has been focusing on developing more growth orientated policies around access to finance, but the effects of which won't be known for a while yet.

Question 4: Is the volume and detail of EU rule-making in financial services pitched at the right level? Has the use of Regulations or Directives and maximum or minimum harmonisation presented obstacles to national objectives in any cases?

We generally welcome the single regulatory rule book via maximum harmonisation, but as raised in Question 2, there has been a significant increase of EU legislation in financial services, the majority of which is highly detailed and complex. We believe that there should not be a preference for one form of legislative instrument over another, and at all times the best instrument should be used. In line with our answers to Q1 & Q2, prioritisation and subsidiarity treated effectively should deliver the right instrument. Importantly too, in the right instances minimum harmonisation provides a degree of flexibility that reflects differences among Member States.

In addition we think that there could be improvements made to the Level 2 & Level 3 rule-making. For example:

- Allowing sufficient time for Level 2 decision-making process
- Increasing certainty around entry into force of Level 1 rules, pending creation of Level 2 and Level 3 rule-making instruments,

Question 5: How has the EU's approach to Third Country access affected the ability of UK firms and markets to trade internationally?

We regard it as very important that the EU takes a balanced and non-discriminatory perspective to third country regimes, founded upon an approach that recognises other regulatory regimes which achieve similar outcomes to EU law. Taking the derivatives reform agenda as an example, reforms to legislative frameworks and implementing rules are still underway in many jurisdictions with few having frameworks in place that will support implementation of all the G20 reform commitments. This poses an important challenge to the EU in terms of ensuring policy coherence and requires work with international counterparts to create compatible regimes that avoid the erection of barriers that affect the ability of EU firms to conduct business internationally. Some examples:

G20 Reform Agenda

- Most FSB member jurisdictions have legislation in place to require reporting of OTC derivatives contracts to Trade Repositories and more than half of the jurisdictions have legislation in place that allows for adoption of clearing and trading obligations. Specific trade reporting requirements and Basel III capital requirements are each in force in about half of the member jurisdictions. However, in contrast mandatory clearing obligations and requirements to trade on organised trading platforms are each only partially in force in a small number of jurisdictions. Jurisdictions have not yet put in force margin requirements for non-centrally cleared derivatives, pending finalisation of international standards in this area.
- EU banks are required to clear through Qualifying CCPs (QCCPs) – authorised in the EU or recognised third country. In addition to the specific technical issues associated with EMIR and QCCP determination process, the capital requirement under CRD are also impacted, as they are dependent on CCP status. We found that the communication on how EMIR affects third country CCP operators has not been clear. The onus seemed to have been not only on the third country CCP to know it needed to meet EU requirements if it wanted to trade with EU counterparties, but also at the regulator-to-regulator level as country equivalence is a precondition for recognition of each CCP. Better communication with third countries by European Authorities would have been welcome.

CRA3

- The introduction of the CRA regulation imposed a restriction on banks use ratings from global CRAs for regulatory purposes to those that are issued by CRAs regulated and supervised in the EU, third country CRAs that are certified or issued by global rating agencies in third countries and endorsed. The process for endorsement was extremely challenging, with potentially material economic implications for the banking community, and gave rise to a number of issues.

Question 6: Do you think that more or less EU-level regulation in the area of retail financial services would bring benefits to consumers?

We see this as a broader question of retail financial services (bank accounts) and digital commerce (electronic selling of goods). In the former, retail financial services markets remain largely domestic. In general this is not due to regulatory barriers but to differences in consumer preferences and behaviour combined with underlying differences in consumer protection rules in difference member states.

Digital commerce however is a European market place with consumers buying goods and services from businesses across the Single Market without always being aware of which Member State those businesses are in, and expecting the same levels of consumer protection. Here, when consumers are buying from businesses across the EU you would want legislation that is pan-European – for example Distance Marketing Rules.

Extra care must be taken in the retail financial services sphere, therefore, when considering EU action. It is particularly important that cross-border liberalisation does not lead to a dilution of the ability of financial institutions to maintain know-your-customer standards or anti money laundering rules. Recent moves to legislate for access to a basic bank account (see response to Question 1), for example, include a cross-border element that risks damaging a bank's ability to exercise due caution, while providing little added value to the domestic (UK) situation, where access to a basic bank account is far advanced.

There are areas in which cross-border barriers may be realistically removed without a diminution in standards. These opportunities will most regularly lie in ensuring a (cross-border) level playing field for the corporate services that underlie consumer financial services. For example, cross-border acquiring (of credit card transactions) is currently subject to different national restrictions, while the regulatory focus is elsewhere.

Another factor mitigating against any increase in EU-level regulation is the increasing level of regulation at the national level in financial services (e.g. the UK's Payment Services Regulator which will become fully operational in 2015).

Question 7: What has been the impact of the shift towards regulation and supervision at the EU level, for instance with the creation of the European Supervisory Authorities? Should the balance of supervisory powers and responsibilities be different?

Significant progress has been made on institutional reform at the EU level under the ESFS framework, to deliver the safety and stability of the financial system after the global financial crisis. We believe that much has been achieved since the implementation of the ESFS and we continue to believe that it is essential for effective supervision that national regulators should perform, and continue to perform a direct supervisory role alongside the ESAs.

In our view, the ESAs should continue to be complementary to national regulators, and in addition to policy and rulemaking, should seek to play a strong co-ordination role fostering convergence and a level playing field across the EU. In particular by ensuring that single EU rules are implemented in an equivalent manner by all member states and where there are unanticipated divergences in approaches, ensure that these are addressed.

Question 8: Does the UK have an appropriate level of influence on EU legislation in financial services? How different would rules be if the UK was solely responsible for them?

The EU is a club of 28 Member States so there will always be a limit to one Member State's own influence, however within a policy area that that country is known for – or that is important to that Member State – that Member State should be influential.

We consider that the UK does maintain a level of influence, and in particular maintains a reputation as a source of technical expertise which provides it with an ability to lead discussion. The UK does though need to ensure that its strategy for influencing the EU keeps pace with other nations, recognising in particular the changes in the EU process and predominance of the G20 agenda at the EU level which require additional resource and input from Member States.

The UK also importantly plays a leading role in international fora where much of the EU regulatory agenda emanates from such as the Financial Stability Board, Basel Committee on Banking Standards, IOSCO and IASB.

For this reason, it begs the question how different UK rules would be if they were a purely national competence – the UK would still have had to implement Basel III, as well as trading and clearing obligations as referenced in the Pittsburgh G20 Communiqué. What the UK could have though is more flexibility over the application of the rules domestically – but given the importance of Europe as a trading bloc, it would be hard to imagine that there would be too many material differences between how the UK and an EU (minus UK) would implement global rules into their separate legislatures for reasons of equivalence. However, what the UK could have is more flexibility over timing given it was not required to wait until agreement had been made at the EU level – however even here the UK has flexibility to front-run currently. A recent example being the introduction of a statutory bail-in regime within the Banking Reform Bill, ahead of the final agreement on the Bank Recovery and Resolution Directive. Such examples of gold plating can have material impacts on UK firms, thereby impacting on the competitiveness of the UK.

Question 9: How effective and accountable is the EU policy-making process on financial services legislation, for example how effective are EU consultations and impact assessments? Are you satisfied that democratic due process is properly respected?

There are a number of areas where the EU policy making process can be improved, notably:

- <u>Consultation processes</u>: we believe that the European Commission should provide a minimum of three months per consultation for responses – this would provide adequate time for the sectors affected to assess and respond adequately. For example the Consultation on the recommendations of the "High-level Expert Group on Reforming the structure of the EU banking sector" (Liikanen) was open from 02.10.2012 to 13.11.2012 – a period of just six weeks.
- <u>Revision processes</u>: in general, while there may be exceptions, a suitable amount of time should pass between the adoption of a piece of legislation and its review. The pace of revision of legislation has increased year on year. The original UCITS Directive was adopted in 1985 with the first successful revision (UCITS III) taking place in 2001. UCITS IV was adopted in 2009 with a possible UCITS VI proposal in 2013. The European Commission is currently reviewing the Short Selling Regulation (SSR) which came into force on 1 November 2012, with a date to report to the European Parliament by 30 June 2013 on the appropriateness, impact and operation of the Regulation's requirements and restrictions. Only three months after its introductions businesses are being asked to comment, and given the short period of experience make assumptions on a Regulation which will then be used to guide the Commission's review.
- <u>Appropriate period for implementation of legislation</u>: It is of particular importance that adequate time is provided for the implementation of legislation. It is often the case that substantial change occurs to legislative texts during the trilogue period (such as CRD4) meaning assumptions as to the ways elements are likely to turn out will not always be right and there will need to be changes to systems to be fully compliant. A particular problem is around the introduction of binding technical standards twenty days after publication in the Official Journal.

- Trilogue processes: Prior to the 2004-2009 legislative period, two-reading processes were the norm in EU financial services policymaking. Since then, single readings have entirely replaced them and have resulted in the trilogue process assuming crucial importance in the legislative process. This centralises power in the hands of a smaller number of policymakers and politicians and is of questionable benefit in terms of speed or democratic accountability. A hard limit (for example six months) should be considered for first reading trilogues.
- Impact assessments: Impact assessments should form a critical part of ensuring an effective and accountable EU policymaking process. A thorough impact assessment should contain an in depth cost-benefit analysis, and should help reduce the risk of unintended consequences. The robustness of the impact assessment is likely to be enhanced if it is undertaken by an organisation that is separate from the institution that proposes the legislation. The example of the Commission's recent Financial Transactions Tax impact assessment is one that would have benefited from this more independent approach.

Question 10: What has been the effect of restrictions placed on Member States' ability to influence capital flows into and out of their economy, for example to achieve national public policy or tax objectives?

N/A.

Question 11: What may be the impact of future challenges and opportunities for the UK, for example related to non-membership of the euro area or development of the banking union?

The Banking Union does present an existential challenge to the UK, as there is the potential for diminished opportunity in the EU rule making process and a general marginalisation from the centre of influence.

The UK financial services sector relies on its access to the (Single) European marketplace as the basis of its world leading position in finance. It is therefore in the UK's, the Sector's, and Barclays' interests that we maintain pro-active, constructive engagement to ensure that marginalisation from the centre of influence does not become a self-fulfilling prophecy.

The UK has sought to ensure that the appropriate checks and balances are created within the Banking Union proposals to ensure that the integrity of single market decision making is maintained. This is important whether the Banking Union contains 17 members or whether it contains more than that. It is essential therefore that the UK spends less time looking for the challenges and more time looking at how best to work with the new relationship, for example ensuring that HMT and PRA/ FCA commit adequate resource to engagement with different Member States competent authorities and the ECB. It is also important that the UK works hard to ensure that the ECB is as open and transparent as possible with non-Banking Union countries.

Question 12: Do you have any further comments about issues in addition to those mentioned above?

We think it is important to emphasise the importance of the UK engaging more actively than it has been in the past, particularly given the emergence of the Banking Union. The UK needs to ensure it has a strategy to enhance its representation in the European Commission, support it's MEPs and engage at the earliest stage possible through seeking to build consensus. The key, if it is to be successful, is in bringing its technical expertise to the table and limiting purely political considerations in negotiations.