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**Treasury Select Committee  
Houses of Parliament  
Westminster  
London  
SW1A0AA**

Submitted online

**RE: Inquiry: Future of Financial Services**

BlackRock<sup>1</sup> is pleased to have the opportunity to respond to the Future of Financial Services Inquiry issued by the Treasury Select Committee

BlackRock supports a regulatory regime that increases transparency, protects investors, and facilitates responsible growth of capital markets while preserving consumer choice and assessing benefits versus implementation costs.

We welcome the opportunity to comment on the issues raised by this inquiry and will continue to contribute to the thinking of the TSC on any issues that may assist in the final outcome.

We welcome further discussion on any of the points that we have raised.

Yours faithfully,

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<sup>1</sup> BlackRock is one of the world's leading asset management firms. We manage assets on behalf of institutional and individual clients worldwide, across equity, fixed income, liquidity, real estate, alternatives, and multi-asset strategies. Our client base includes pension plans, endowments, foundations, charities, official institutions, insurers and other financial institutions, as well as individuals around the world.

## Executive summary

The UK begins life outside the EU with a world-leading, well respected financial services industry, underpinned by robust governance and high regulatory standards. The comparative advantage the UK has in this sector means it is well positioned to excel in the growth industries of the future. For example, by specialising in FinTech, becoming a centre for green finance, and more generally demonstrating the value of financial services to the wider public – for example through retirement provision.

The UK also has an opportunity to design a more tailored regulatory framework for financial services, while also adapting the system to ensure that it can handle the additional responsibility this entails for government, parliament, and the regulators. While the Financial Services and Markets Act model needs some adaptations to make it fit for purpose post-Brexit, we agree with HM Treasury's view that it continues to provide a reliable approach outside of the EU. Adaptations should include a mechanism for ideas and feedback to be sourced from industry and other stakeholders - consumer groups, think tanks, and civil society - in the course of both making and adapting regulation; and making sure Parliament, the civil service, and regulators have enough resource and expertise to carry out their responsibilities. We do not believe that the UK should seek to directly replicate the EU's model for drafting and scrutinising financial services regulation – for example by setting up a body akin to the EU's Committee on Economic and Monetary Affairs (ECON), which plays a role unique to the EU institutions – but do see benefit in introducing a financial services sub-committee of the Treasury Select Committee, supported by dedicated civil servants steeped in financial regulation

We also see benefit in expanding the set of objectives that currently underpin UK financial services regulation. The present set of objectives – financial stability, consumer protection, market integrity and competition – are undoubtedly crucial and should remain in place. But complementary objectives could help to realise the primary purpose of financial markets: funding the economy while providing end-investors with a means of generating returns. As such, we recommend a new objective for regulators to remove unnecessary barriers to investing in alternative and long-term asset classes; alongside an additional objective for regulators to not only protect those who are already saving or investing, but to encourage more people to start doing so.

Beyond this, the UK's ongoing success in financial services will depend in part on continued openness to overseas firms and investors. Access to new and innovative products spurs competition and productivity in the wider financial services ecosystem, making the UK financial centre more competitive internationally. Provided there are no financial stability concerns or consumer protection concerns, access to the UK market should not be contingent on reciprocity or level playing field concepts. And instead of maintaining an approach based on equivalence, we believe UK consumers would be better served by an open-market stance, relying on mutual recognition and deference to manage risks where relevant. Further, as the UK looks to strike more trade agreements with countries, we believe it will be important to increase the ease of doing business across borders through measures such as mutual recognition of qualifications and skills; as well as provisions to limit data localisation.

## Responses to questions

### **1. How can the UK financial services sector take advantage of the UK's new trading environment with the rest of the world?**

It's important to recognise that the UK is already a leading financial centre, and after Brexit should seek to consolidate its strengths: namely its existing advantages within financial services, international openness, access to talent, time-zone, business-friendly environment (common law legal system and sophisticated professional services ecosystem), and its internationally-respected expert regulators. Indeed, the UK's stable and proportionate approach to regulation is part of its appeal to international firms. The UK also has a significant and growing domestic market, constantly evolving to serve the needs of retail customers, as well as a considerable asset base in retirement savings being built through auto-enrolment.

During its time as a member of the EU, the UK played a leading role in designing financial services policy and has made major intellectual contributions to international standards as well. Going forwards, it should continue to lead the development of international standards, both through engagement in multilateral organisations and by building on bilateral agreements, such as the recent MOU on cross-border clearing between the Bank of England and the US Commodity Futures Trading Commission.<sup>2</sup>

Going forwards, the UK financial services industry will gain advantages relative to the rest of the world to the extent that it can excel in the growth industries of the future. For example, by specialising in FinTech (see question 6), becoming a centre for green finance, and more generally by demonstrating the value of financial services to the wider public – for example through retirement provision.

### **2. What changes should be made to the UK's financial services regulations and regulatory framework once the UK is independent of the European Union?**

We believe there are two main aspects to this question: changes to the governance structure for financial services regulation; and a new approach to regulatory objectives.

Leaving the EU gives the UK more scope to implement a governance structure that is agile, flexible, and able to respond to new developments. It can also be adapted to align more closely with the UK's legal framework, moving from a more prescriptive and process-driven model to one guided by principles and outcomes. The second phase of HM Treasury's Future Regulatory Framework Review has proposed an adaptation of the Financial Services and Markets Bill model that would, we believe, be a good first step towards this. Although it will be important to ensure that the model is augmented to provide a mechanism for ideas and feedback from stakeholders (such as industry, consumer groups, think tanks, and civil society) to be introduced into the development and ongoing scrutiny of policy.

The UK will also have the scope to evolve the objectives that underpin the regulatory framework. At present, the objectives are to maintain financial stability, protect consumers, and ensure market integrity and competition. These objectives are undoubtedly crucial and should remain in place. But we believe complementary objectives could help to realise the primary purpose of financial and capital markets: funding the economy while providing end-investors with a means of generating the returns they need to meet their objectives.

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<sup>2</sup> <https://www.bankofengland.co.uk/news/2020/october/cftc-boe-sign-new-mou-for-supervision-of-cross-border-clearing-organizations>

This should not come at the expense of providing a high-quality, high-standards regulatory environment; rather, this could mean an objective to remove unnecessary barriers to investing in alternative and long-term asset classes, such as infrastructure, renewable energy, and others. This has the dual benefit of providing capital to projects and companies that need it, driving economic growth; while also allowing end-investors with long-term horizons to benefit from the associated returns, notably DC pension savers.

It could also mean an additional objective for the FCA to not only protect those who are already saving or investing, but to encourage more people to start doing so – reviewing current and proposed regulation to that end. This is particularly important as the balance continues to shift from Defined Benefit to Defined Contribution pensions as the means of providing for UK citizens' retirement, emphasising the need to ensure people are saving enough and generating sufficient returns to provide adequate retirement income. The Bank of England has moreover estimated that between March and November 2020 household savings were £125 billion higher than the counterfactual had COVID restrictions not been in place, and that this will continue to rise over the course of this year.<sup>3</sup> It is therefore increasingly important to enable a wider range of people to benefit from the advantages of investing relative to keeping cash in bank accounts. Ultimately, the UK should look for citizens to have the same level of engagement with capital markets and personal investments (aside from property) as there is in countries such as Australia or the United States.

### **3. What should the Government's financial services priorities be when it negotiates trade agreements with third countries?**

The UK already hosts a world-leading financial services industry, concentrated in higher value-add activities. The Government should seek to maintain this status, using it as a base to build comparative advantage in future growth sectors: specifically sustainable finance and alternative asset classes. It should not seek to compete with or replicate well-established sectors, such as those specialising in fund domiciles.

Part of the UK's success in financial services also lies in its ability to attract talent from around the world. Trade deals should continue to facilitate this by including mutual recognition of skills and qualifications – particularly for accountants, lawyers, actuaries, and other professional services; and avoiding any frictions in cross-border working such as double taxation. This will enhance firms' capabilities to operate across borders. Early wins with jurisdictions like Australia and New Zealand could serve as proof of concept agreements with high levels of ambition for professional and other services.

Multinational firms' operations can be hampered by onerous restrictions on the storage of transfer of data. Any trade agreements should recognise this, and include provisions to limit data localisation. This benefits both the firms and their consumers – who are able to store data in the most secure or suitable location – and regulators – as firms are better able to comply with different regulatory requirements if they have more discretion over managing their data.

### **4. Should the UK open its financial services markets to external competition from countries outside of Europe, or should the UK maintain the current regulatory barriers that apply to third countries?**

Historically, part of the UK's success in financial services has been its willingness to remain open to overseas firms and investors. Going forwards, this openness should be maintained

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<sup>3</sup> <https://www.bankofengland.co.uk/-/media/boe/files/monetary-policy-report/2021/february/monetary-policy-report-february-2021.pdf?la=en&hash=3638A7091B34164428A54277B55BD6901709AA44>

unless there are material financial stability or consumer protection concerns. Even where these issues do exist, the appropriate action is to mitigate them through regulation, rather than via blanket barriers to access.

UK consumers benefit from access to new and innovative products, and this innovation spurs competition and productivity in the wider financial services ecosystem, making the UK financial centre more competitive internationally. Provided financial stability concerns are addressed and adequate levels of consumer protection are ensured, access to the UK market should not be contingent on 'reciprocity' or based on 'levelling the playing field' for the benefit of domestic providers. Rather than maintaining an approach based on equivalence – no access unless granted otherwise – UK consumers would be better served by an open-market stance, relying on mutual recognition and deference to manage risks where relevant.

All of this will help to ensure UK savers and investors continue to enjoy the substantial benefits of economies of scale, access to expertise, and innovation in financial markets that they currently do from an open marketplace. Regulation will also work best when it aims to achieve the best possible outcomes for end-investors, instead of seeking to manage competition between service providers.

## **5. What skills and immigration policy will the UK financial services sector need once the UK has left the European Union?**

As mentioned, part of the UK's success in financial services has depended on being able to attract the right skills and talent from across the world. An open immigration regime should therefore be comprehensive with regards to access, geographic coverage, and in terms of skills and income levels accepted. This includes the removal of any future quotas and a labour market testing requirement under the Skilled Worker visa category, as well as the development and expansion of technology to further streamline visa processing. It will allow financial services firms to quickly identify and establish long-term plans to retain talent at all levels, develop a diverse workplace, and deploy it in a multi-national operation. In addition, the government should further address the treatment of applications under the EU Settlement Scheme in light of COVID-19, including interpretive guidance that provides flexibility for individuals who spent time outside of the UK during the pandemic, as well as those who were not able to enter the UK before the end of 2020.

## **6. How can Government policy and the UK regulators facilitate the emergence of FinTech and new competition; develop new areas of growth for the financial services sector; and promote the UK as the best place to incubate new financial technologies and firms?**

A potential benefit of FinTech solutions are as a means of empowering individuals to engage more with their personal finances, savings, and investments. FinTech can be an enabler for financial inclusion and well-being in the UK, allowing many more people access to experience a better financial future. People are more likely engage with their finances if the process is truly digital (app-based), intuitive, and engaging. Therefore, one suggestion would be to acknowledge more openly that cash is not always a safer place to have your money relative to investments. This is particularly the case in the current environment where the longer-term effects of negative real rates are having a damaging effect on people's savings. Further to this, the Government could seek to build the digital infrastructure to underpin a domestic market for technologically-delivered financial services. The pensions dashboard, for example, has enormous potential as a proposition, but has been discussed for numerous years now without material progress: taking steps to, for example, digitise individuals' account statements and reports would be a good step forward.

Beyond this, if the government wishes to foster or attract FinTech companies to the UK market, there are a number of policies to consider, including: allowing companies to list with dual-class share structures for a strictly time-limited period; giving owners more control in the early stages of company development; avoiding strict minimum income requirements in the UK's immigration regime to facilitate equity remuneration; and revising the thresholds for entrepreneurs' tax relief. All of these could be improved to incentivise the type of entrepreneurs and companies the UK wishes to attract.

Finally, the government and the FCA may wish to consider how, post-Brexit, greater scope for experimentation and innovation can be facilitated via the regulatory sandbox.

## **7. Through what legislative mechanism should new financial regulations be made?**

HM Treasury, in Phase II of its Future Regulatory Framework Review, has proposed that financial regulation should be made using a refreshed Financial Services and Markets Act framework. We largely agree with this approach, which includes an increased role for Ministers to set the broad objectives and principles for financial services regulation. We suggest that, in addition to this, there should be scope for ideas and feedback to be sourced from industry and other stakeholders in the course of both making and adapting regulation.

## **8. What role does Parliament have to play in influencing new financial services regulations?**

Parliament's role should be to hold government and regulators to account on their stated objectives and principles; but also on other societal objectives, such as whether regulation is facilitating the financial services sectors' role of providing capital to the economy while also providing returns to individuals saving for their future.

## **9. How should new UK financial regulations be scrutinised?**

Going forward the UK will have more discretion around how it sets financial services policy. This in turn will create more responsibility and workload for its regulators. It will be important for the appropriate checks and balances to be put in place to ensure the appropriate level of scrutiny and challenge. The Treasury Select Committee (TSC) has been one of Parliament's leading committees in holding regulators and industry to account in forensic detail. As the committee for the Treasury, it is the proper place to weigh the Government's objectives for financial services against wider macro-economic and fiscal responsibilities. In order to ensure it is properly resourced to do this effectively, there could be scope for a financial services sub-committee with dedicated civil servants steeped in financial regulation.

## **10. What progress has the Government and regulators made in facilitating key financial services equivalence agreements with third countries; and would an alternative mechanism serve the interests of the UK market better?**

An alternative mechanism would probably serve the interests of the UK market better. Equivalence is a concept developed in the EU, that aims to reduce regulatory competition and 'level the playing field' for competing financial service providers. It stems from the need, which is to an extent unique to EU legislative order, to ensure that firms from Member States who have had to harmonise their regulatory regimes for the purpose of the Single Market, do not face competition from firms outside of it who have not been subject to that process. Outside of and with limited access to the Single Market, the UK has different policy drivers for determining access, and we believe the interests of the end user should be paramount in decision-making. As such, market access to the UK should be granted where it allows consumers to benefit from a wider range of improved services subject to adequate

consumer protection provisions, relying on outcomes-based assessments where necessary and without lowering standards.

More broadly, using equivalence as a process to ensure precise alignment in regulatory standards – as opposed to concepts of deference or mutual recognition, which rely on regulatory outcomes – hinders the integration of markets. If every jurisdiction insists on full equivalence with another before market access is granted, the tendency overall will be towards fragmentation. In turn, this undermines good work done to promote regulatory cooperation and convergence following the great financial crisis, to the detriment of end-users and financial stability.

## **11. How should financial services regulators be funded?**

Broadly speaking, the funding mechanism in place at present seems to work well. That said, UK regulators' burden will increase in the near future, as they take on more responsibility for the initiation of regulation, and also begin to adapt the EU acquis for the UK. At the same time, it is likely that it is not just regulatory bodies that will need additional resource, but Parliament and central government also: expertise and capacity for scrutiny that up until now has (in part) been embedded in EU institutions will have to be replicated in the UK. This includes ensuring the Treasury is adequately resourced to advise Ministers on the activities of the regulators and engage with them effectively at a working level.

A related issue is that of fees and levies applied to the financial services sector. If the UK is to remain competitive, it is important that any levies are not excessive, and proportionate to the risks they seek to address. The Financial Services Compensation Scheme (FSCS), for example, is not currently fit for purpose: ever-increasing fees are extracted from certain parts of the financial sector to compensate for unrelated failures in other sectors. The FSCS should be re-thought and re-worked on a 'polluter pays' principle.

## **12. Should the mandate and statutory objectives of the financial services regulators change to include wider public policy issues?**

As discussed under question 9, the current regulatory objectives in the UK are, broadly, financial stability, market integrity, and consumer protection. Going forwards, we believe these should be augmented with additional responsibilities to encourage more UK citizens to save and invest for their futures; and to better connect end-investors' capital with appropriate investment opportunities – for example by lowering barriers to deploying capital in alternative and long-term investments, particularly via DC pension schemes.

We do not believe UK regulators should be given an explicit objective to encourage the competitiveness of the UK financial services sector. A robust, expert, high-quality regulatory ecosystem will encourage investment and growth. An approach to regulation that makes changes solely with competitiveness in mind could ultimately undermine the integrity of markets, and compromise the UK's reputation in financial services. The power to decide how to strike the balance between pursuing competitive advantage versus maintaining alignment with other markets properly rests with government and Ministers, who should consider this on an issue-by-issue basis. For regulators, a more fitting objective is to monitor and reduce the cumulative impact and burden of regulation on firms; including by avoiding 'gold-plating' of international standards.

## **13. How important is the independence of regulators and how might this best be protected?**

The independence, expertise, and quality of the UK's regulators underpins the success and reputation of its financial services industry. It is a competitive advantage vis-à-vis other

finance centres and should not be undermined. The Financial Services and Markets Act is an appropriate mechanism for setting regulators objectives and holding them to account, and should continue to be so as those objectives are refined or expanded. As mentioned under question 9, it will be important to ensure regulators, parliament, and the government have adequate resource to protect the integrity of the FSMA mechanism. Investing further in recruiting talented PRA / FCA supervisory staff is important (as they are the regulators' interface with the market).

#### **14. How can the balance between lighter touch regulation and prudential safeguards be best secured?**

There is not necessarily a trade-off between each of these objectives: regulation can be 'light touch' in the sense that it is simple and easy to adhere to, while still maintaining high, robust standards. To take an example from another sector, simple capital buffer requirements for banks could be easy to adhere to while also providing a high level of prudential protection. This underscores the importance of making regulation that is principles-based and outcomes-driven, not prescriptive and bureaucratic.

#### **15. How should consumer interests be taken into account when considering potential regulatory changes?**

To do this, industry, consumer groups, and other stakeholders should be engaged early on in the policymaking process – continuing to use the current approach of seeking feedback through public consultations and acting on the responses.

Having the right conception of consumer interests is also critical: it should not be viewed solely as a risk-minimisation exercise – instead, it must be remembered that the ultimate objective of investment products is to generate an adequate return and meet the financial goals of end-investors. This has to be facilitated as well as ensuring a sufficient level of consumer protection. Indeed, as crucial aspects of individuals' financial security and wellbeing increasingly depend on investment returns – DC pensions being the most notable example – a re-evaluation of what investment exposures are appropriate may be needed, alongside a concerted joint effort from industry, government, and regulators to improve engagement with investment and financial education.

#### **16. What are the strengths and weaknesses of the European Union model of scrutinising financial services legislation?**

EU legislation has to apply equally and fairly throughout the Single Market, requiring a high degree of granularity. This in turn means that the European Parliament has a more significant role in the (re)drafting of detailed regulation than has traditionally been the case in the UK. The Committee on Economic and Monetary Affairs (ECON), for example, has historically provided robust scrutiny of EU financial service policy, which it has been able to do partly through access to dedicated civil servants helping it to engage with financial services regulation at a reasonable level of detail. While this model has some benefits – notably uniform application of EU law in the EU and more direct EU-level democratic and stakeholder oversight of detailed regulation, it can also mean complex and technical financial services regulation is drafted by the legislator instead of technical experts.

Regulators should instead be free to design the most effective means of achieving regulatory objectives – including determining how regulation impacts investors – set by politicians, with political oversight focused on what those objectives should be and the political trade-offs they may entail.



**17. Should the UK seek to replicate the EU's model for drafting and scrutinising financial services regulation?**

No, as this would import both the strengths and weaknesses of the EU system (see also question 16). However the UK should look to improve its own system by drawing on the strengths of the EU model: providing sufficient resource and expertise to support proper scrutiny, while ensuring technical experts remain free to devise detailed regulation in accordance with the objectives set by politicians. This could be achieved, as discussed above, by a dedicated financial services sub-committee of the Treasury Select Committee, supported by specialist civil servants.

**Conclusion**

We appreciate the opportunity to address and comment on the issues raised in this Inquiry and will continue to work with the Treasury Select Committee on any specific issues which may assist in review of the UK's regulatory framework.