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After Brexit - Looking towards closer regulatory cooperation

Now that the UK has left the EU, the financial services sector is looking ahead at what the future might hold. The UK is now a “third country” under the EU financial services regime, and UK banks have lost important access rights to the EU markets, in particular, the ability to freely “passport” financial services across EU member states. As a result, UK banks must now carefully navigate the regulatory framework in each EU member state in which they look to do business.

Looking ahead, it is possible to see that, notwithstanding Brexit, there may in the future be a return to close EU and UK regulatory alignment. It seems possible that the benefits of free market access which have been enjoyed by both the EU and the UK – making both the EU and the UK attractive international centres of business – may continue through bilateral “equivalence” arrangements.

“Equivalence”, however, depends on regulation achieving outcomes which are comparable between the EU and the UK, and it is up to the EU and the UK to agree equivalence in key areas. Although developments towards equivalence have so far taken place at a measured pace, it is hoped that an agreement on financial services will be reached between the EU and the UK in due course. In many areas, in particular, derivatives and securities business, there is otherwise the risk of fragmented markets which are inefficient and costly to navigate. Equivalence would not only benefit UK businesses, who would be able to easily access EU markets, but also European consumers and corporates needing liquidity.

Equivalence – although very important for financial services – is clearly only part of the picture. Regulatory cooperation in the purest sense means countries working together to determine the appropriate direction of regulatory policy, all the while being able to react appropriately to real-world events. This will create a positive environment for international business.

As a basic matter, it is hoped that the EU and the UK will continue to be “open” rather than “protective” financial services markets. Being “open to business” has made London, Frankfurt, and other European financial services hubs global centres of financial excellence. It is hoped that even outside of areas of regulation which are deemed “equivalent”, the EU and the UK will be able to work closely

together to formulate regulatory objectives which ensure broadly similar standards. Close co-operation going forward on the green agenda, for example, is a high priority.

While there are clear benefits to equivalence in being able to enjoy free market access across borders, this will always be subject to the possibility of equivalence being withdrawn by either the EU or the UK at short notice. Businesses, of course, need time to react effectively. Where equivalence is taken away, there may not be an easy solution to ensuring that businesses are protected from the adverse impacts of sudden regulatory change; in particular, where they have structured their business based on equivalence decisions.

Regulatory cooperation should therefore not just be an area-by-area assessment, but should be an exercise at the highest level of regulatory policy in financial services; closer cooperation will, hopefully, reduce the risk of the EU and the UK taking a radically different path from each other. Equivalence should, therefore, be easier to maintain. Where rules are broadly aligned, they are easier to understand, and they provide a more comprehensible basis for structuring international business.

The ultimate aim in close regulatory cooperation – across the full spectrum of financial services – is to create an environment which ensures the continued attractiveness of the UK and EU financial markets for international business.