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Members present

Lord Harrison (Chairman)
Earl of Caithness
Lord Carter of Coles
Lord Davies of Stamford
Lord Dear
Lord Flight
Lord Hamilton of Epsom
Lord Kerr of Kinlochard
Lord Shutt of Greetland

Examination of

developing. We will go on to look at many other questions related to this. Professor Véron, perhaps you could respond to this first point.

I am afraid it is a tiny point as we prepare for this session. I am not a professor, just Mr Véron.

The Chairman: I am always happy to elevate people, sometimes to the House of Lords.

Thank you. A lot of things have happened. No two crises are identical, so we know that the crisis that has happened since 2007 will not happen again, and that would be the case even if the EUj 25.2939 support industrial and

European level, because they were part of a globally considered response to the crisis. I do not think they preserve us from shocks generally. As measures, they were entirely effective in addressing the problems that gave rise to the last crisis and they do result in a more stable system.

Banking union is really nothing

Call me naive, but I think this is an area where in substance—I am not talking about the politics, obviously—the UK and its partners in Europe should be able to find common ground.

Market efficiency is the whole point of capital markets union. I suspect that we will come back to this so I will not dwell on it. Basically, what has been done is that some G20 initiatives have been implemented, particularly in the derivativesthe

temporary, and indeed this guarantee arguably lasted for the following four years, until 2012.

Then there was the second major mistake. It is very difficult to find a consensus view on what should have been done with Greece, but I think the Deauville declaration of October 2010 will remain a symbolic moment of the core member states of the eurozone removing any guarantee that was perceived before for the periphery countries, in a way that has created a lot of instability. It is a difficult area, and we may come back to it. Taken together, those two moments—guarantees on banks and the removal of sovereignis

It is quite interesting to look at the question, “What are the nothing wrong with any of those policies individually but, taken collectively, European Parliament has contributed to significant improvements, certainly in some of the first drafts of legislation which have appeared over the years.

The Chairman: Do you attribute that partly to Sharon Bowles?

Yes. It is unfair to name any specific individual, but there are quite a number of MEPs who are very engaged and very happy to take individual points. Neither the Commission nor the Council can take a list of 450 minor amendments and push through all of them, but among the various available MEPs, that can be done.

I agree with what Professor Gleeson said about Parliament. I do not think it is just Sharon Bowles. No disrespect to her, but it is much broader and something that is likely to stay after her. Irrespective of how the new chair of the Economic Committee plays out, we will see essentially the same form of constructive role of Parliament, at least on small things and incremental improvements, as Professor Gleeson just described.

In a way, it might be

Secretariat, but it was a high-level committee. It was mo00153 35.450ky

concerned with Mr Barnier. I agree that he clearly gave great impetus to particular bits, but the point about overall coherence is a very strong point, which I would like to press a little further. Did the creation of the permanent President of the European Council and the presence of the first incumbent make any difference? Did it make the problems of incoherence worse or did it provide some palliative to the situation in the Commission which you described?

The Chairman: Nicolas Véron, you wanted to pick up something else that Simon Gleeson said. In response to Lord Kerr's last point, do you you pick that the Commission will in the next five years do better than the one that we had over the last five years. Again, I make no particular attribution to individuals on this.

I wanted to respond to Professor Gleeson about this question of correcting legislation. It is a feature of legislation that only the legislator can correct legislation. If you compare this with the US, which is the obvious point of comparison, EU directives are easier to correct than Dodd-Frank. So in a way we have the advantage in this comparison. There is a big difference however in that there is much more in European legislation than there is in the equivalent US legislation, and there is more delegation to agencies in the United States than there is in Europe, for all the small print. I am cautiously optimistic about this as well. The creation of the European supervisory agencies, EBA, EIOPA and ESMA, and the banking union, will make us evolve towards a more US-like model, where Parliament will gradually, probably slowly, learn from its mistakes and the Council will learn from its mistakes—as well as the Commission learning from its mistakes, I hope—and we will have a more sensible division of labour between legislation and rule-making at the sub-legislative level. I do not expect this to happen quickly, but I think that we are broadly on the right path to correct that feature of our current process.

The Chairman: Simon Gleeson, could you respond to Lord Kerr—then we must rush on to Lord Hamilton?

All of this really comes down, I am afraid, to good old-fashioned institutional power politics. The reason [illegible] unlikely to abandon its stance that it is a legislator and a primary actor—and, if the Council disagrees with what it says, that can come out in trialogue. We have an almost complete centralisation of power in one entity at the moment and, unless there is a significant change to the constitution of Europe, which seems unlikely to happen, because it would probably require treaty amendment, we are probably stuck with that for the time being.

Q51 Lord Hamilton of Epsom:

businesses. It is quite right that the European banking system, given the regulatory architecture, is unlikely to be able to expand the flow of credit to European small businesses, so we need another piece of architecture. There is at least a proposal to provide one.

The Chairman: Nicolas Véron, could you respond to the growth agenda mentioned by Lord Hamilton. Lord Flight, could you make it brief?

Q52 Lord Flight: Very briefly, the French tax authorities came over here, looked at the EIS system, and put in an even more generous one in France. The amounts of

do that, you need a European chief accountant. I, for one, believe that this should be an agenda on which the UK and the continental nations could find common ground, but we do not have it at this point for a number of different reasons. Some are political, some are turf-related and some are private–interest reasons.

The Chairman: That is really helpful. I am anxious to pass on.

Q53 Earl of Caithness: Professor Gleeson, you have partly answered my question in responding to Lord Carter of Coles. As you rightly said, there are 40 different pieces of legislative enactment in recent years. Where are the contradictions, gaps and overlaps? What have these reforms done in the way of generating extra costs and inefficiencies in the financial sector? The third part of my question, therefore, is what are the unintended consequences of all this? Where has it led to extra costs, the transfer of risks off the balance sheet and that sort of thing?

We have talked about some of the individual instances. It might be helpful to talk about the biggest collective problem, which is not identifiable as any one directive but as an overarching point that goes across many of these 40. That is the fact that the European legislative process seems to have become somewhat disengaged from global consensus on a number of issues, andunumber these area( )Tj 33.74198439 0 9d (procei( )Tj 15.875 0 71 problems, the more you find yourself constructing obstacles to business between Europe as a whole and the rest of the world as a whole. Although I agree with everything M Véron says about the importance of developing the single market and creating more business within Europe, it is equally important for Europe to do more with the rest of the world. I would identify the biggest single

Back to your question about extra costs, gaps and overlaps and identifying them precisely the impact of banking union. The fact is that the ECB will become a very strong institution, much stronger than the ESAs, in producing or advising on rules, and I think that that will help the process. By the way, there was recently a very important ruling by the European Court of Justice—the UK against ESMA—which unfortunately the UK lost. The ruling clarifies the previous Meroni doctrine on what EU agencies can and cannot do. It gives them much more autonomy and the ability to delegate on matters where discretionary decisions are required than was thought to be possible before. At least, that is my understanding of the judgment. I think that it is a good thing and is exactly in the spirit of what Professor Gleeson said about having more of the detailed rule-making done at agency level; it makes it legally much more possible than it used to be.

Of course, I agree that the Commission has an incentive to retain its turf, but whether it will do so successfully in the way it currently thinks it can remains to be seen. I am slightly less deterministic than Professor Gleeson. Because of the heft of the ECB and possibly because of future reform of the ESAs themselves, we can look forward to a future in which more of the decision-making and rule-making will be done at the more competent agency level.

The Chairman: Simon [illegible]

precisely what causes the problem. It is an approach like that which basically makes these bodies really useless for amending and developing law and policy.

This is particularly alarming as we move towards MiFID, the markets directive, because market regulation above everything else is a process that involves a feedback loop. Although it would be much more efficient if a greater degree of power could [illegible] reintegrate the markets? Let us take, say, banking resolution. The central common funds for dealing with a failing bank are minuscule and grow extraordinarily slowly. We will see for some considerable time to come banks renationalised in the sense that they will go back to within their national frontiers. Was that inevitable or is there something that could still be done? I am struck by M Véron's opening remarks about how we are seeing the end of national banking. It seems to me that we are miles away from genuine banking union.

The Chairman: Do you want to respond to that?

Yes. The initial remark I made was definitely a forward observation. I was describing my expectation of what I am reasonably confident will happen rather than what has already happened. I think that banking union is the centrepiece of the EU effort to address market fragmentation, and so far what I am seeing on the ground makes me optimistic that it will work. At this point I cannot say that it has worked or even that it works because it is too early to tell. A timetable has been set and in barely more than a month's time we will have the results of the comprehensive assessment. They will give an early indication that goes beyond what we already know. I also suspect that in the second half of 2015 we will see the end of the wave of bank restructuring and recapitalisations immediately following the comprehensive assessment. I think that it will not be before the second half of 2015 that that particular cloud of dust will have settled. At that point we will know more about whether banking union does actually foster cross-border bank mergers and the sort of integration-friendly developments that the ECB says it wants to see. By the way, the ECB has been saying that very clearly.

The Chairman: Let us turn to Simon Gleeson. You responded very warmly to what Lord Kerr was asking.

other words, the shortcomings of banking union and its incompleteness in its current form are essentially unavoidable unless there is further progress in fiscal and therefore political union.

My take on this is simply to say that monetary union with a sort of half-way banking union is much more robust than monetary union without banking union at all and it is much more supportive of an integrated financial system. I see the positive side of it, but you are right that we are not yet there. It is not realistic for the next year or two to go for fiscal internationally developing? Finally, and most importantly, there is Basel and banks. To what extent is Europe going to come in line with that?

The first thing to say about that is if you imagine that none of the international hierarchy existed at all and that we simply had the PRA and the FCA in the UK that were completely and unrestrictedly sovereign, the rules that would come out of that process would be almost the same as the ones we have today.

Lord Flight: I understand.

What happens above them is almost a policy-making process. One of the things you notice if you look at FSB/G20 level is that most of the policy input is coming from the UK and

to be made here. I suspect

principle, which I very much believe is a good organising principle for those issues, may give you different answers. At the current juncture—

Lord Davies of Stamford: The subsidiarity principle may indeed be in opposition to the right degree of supervision—

No, the subsidiarity principle simply says that responsibility should be at the level where it is most effective. Basically, if things can be dealt with at the national level in an effective way then they should remain at national level. If they cannot, there is a case for bringing them to the European level. In the case of banking union there is a slightly hybrid level, the banking union area, which is likely to become larger than the eurozone very quickly but does not include the UK.

On structural separation, I reiterate my view that, at least for the time being, this is not a priority for legislation and therefore should be left for supervisors, which also means that inside the banking union area it will actually be consistent because it will be consistently implemented individual case. Everyone would agree with that—it has always been the position that any

Coming on to whether the balance is efficient, a good starting point would be that increased harmonisation is useful for activities that are inherently cross-border and less so otherwise. In the context of financial regulation, the specific point tends to be that retail savings products, for example, are sold very differently from country to country. An Italian saver buys an entirely different product in an entirely different way from a British or a German saver. It actually makes very little sense to harmonise the marketing of retail—

Lord Davies of Stamford: Ah,

That is at the retail level. If we look at the wholesale level, we are trying to achieve a different thing. The easiest way of putting this is to say that if London, for example, wants to be the European financial centre, Europe must feel that it is able to regulate it effectively. It goes beyond the question of how we generate the best regulation towards how we generate the regulation that allows this entity to perform the job that it wants to in the legal context in which it needs to perform it. It is not simply a matter of saying who is technically the best regulator; you are saying, “Who needs to feel that they have a hand in the regulation of this thing?”. To that extent, I would argue that the balance is wrong. We still do not have sufficient European control of the City of London to leave other European Governments happy with the fact that increasingly Europe has only one financial centre, and that is it.

I entirely agree with what Simon Gleeson has just said. It is probably easier for a continental such as me to say than for a UK citizen like him, but we are on the same page here. My way of putting it is that the City of London has in terms of functionality? There is not necessarily an indisputably obvious solution in each particular case.

That is true, and this is why all federations that I know are a constantly renegotiated arrangement where nothing is really in a steady state. You see that in the US, in Switzerland and in all federal organisations. That brings complexity but it might be better than the alternatives. On the assessment of what is sufficiently consistent and what is not, I also express my full agreement with Professor Simon Gleeson; enforcement is where the biggest problems are. That is not to say that there are none regarding the harmonisation of legislation, but there are many more in terms of enforcement. I mentioned accounting enforcement but I would also mention single-market enforcement. When you discuss with people inside the Commission’s internal market directorate, all those who I know agree privately that the European Commission has not done enough by a mile to enforce single-market legislation. It goes beyond Mr. Barnier.

Lord Davies of Stamford: Is that not a reflection of the fact that it is local national authorities that tend to be responsible for enforcement?

The European Commission has enforcement powers that it has not used to the extent that it should have; that is the assessment that they make, and I fully share it. Again, contrasting banking union with capital markets union, there is a bit of a paradox. As Simon Gleeson said, wholesale markets should be more integrated than retail markets, but with banking union we have segments of retail markets that are now more integrated than wholesale markets. There will be catch-up action here. Again, I give the example of accounting and auditing, which should be relatively uncontroversial, even though there are enormous vested interests. The ECB as a supervisor will supervise banks whose national operations are audited by fully independent national firms; of course, they are part of a network,

Q60 Lord Flight: The question is whether the my personal opinion that certain UK Government departments, particularly the Treasury, proceeded for far too long under the illusion that they were sovereign law-makers when in fact they were not. Over the last seven years, we have seen a rather violent correction of that illusion. In order to correct that, it is necessary for those who make financial policy in the UK to be clearly aware that financial policy is no longer made in Horse Guards Parade—it is made in Brussels—and to manage the making of policy on that basis.

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On the broader question about EU legislation, again, I want to see the bright side. The EU process can improve and the UK help to improve the EU process. The UK was instrumental when the Commission was committed to better regulation processes. There has been a pause in better regulation but there is no necessity the(...)Titter so I have sympathy for my friends in the UK in all parts of society and government who struggle with it.

Capital markets union—to use again the moniker that Jean-Claude Juncker has introduced—is a test of this. Can we find a positive agenda where the interests of the UK, those of other European countries, the common EU interest and the interest of the City of London are sufficiently aligned so that significant progress can be made towards more integrated capital markets, with appropriate enforcement, monitoring and supervisory mechanisms? I believe that it is possible. I see the UK government authorities, including but not only the Treasury, being tempted to stonewall and say, “Well, of course we love capital markets union; it should be an amendment to the directive on prospectus and some new legislative text on securitisation which will not have much substance”, which is another way of saying, “Let’s say we love capital markets union and do nothing on capital markets union, or so little that it will not make any difference”. I am not sure that this strategy—if it is a strategy—is aligned with the UK national interest. I cannot opine on the politics of it, not being a UK citizen myself, but I can certainly say on policy that I see much more scope on substance for a constructive agenda of capital markets union where the interests of the UK as a nation, of London as a financial centre and of the EU as a whole are broadly aligned. I hope this will materialise. I am not sure that it will. not —

reaction of my colleagues that this has been a very invigorating hour and a half, and we are most grateful to you both for coming in and starting our "September Song".