Briefing Paper:  
The Rule of Law:  
Brexit and Financial Services  

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Professor John McEldowney, University of Warwick with  
Professor Rosa Lastra, Queen Mary University of London  

Bingham Centre for the Rule of Law  
www.binghamcentre.biicl.org
The Rule of Law: Brexit and Financial Services

The rule of law is not an arid legal doctrine but is the foundation of a fair and just society and an important contribution to economic growth, as well as offering the best means yet devised for securing peace and co-operation


Introduction

The decision to leave the European Union, following the referendum in June 2016, highlights how economic and financial issues underpin much of how we are governed. When coupled with the global financial crisis, Brexit has considerable influence over our constitutional and political institutions. The disruption caused by the experience of 2007-2009 is likely to dominate events for the foreseeable future. Though market turbulence is hard to anticipate, the consequences of the uncertainty that surrounds the future health of the UK economy as the UK seeks to negotiate a new relationship with the European Union cannot be ignored.

Estimates of the economic impact of leaving the EU are hard to make but it is commonly assumed that the sensitivity of the UK financial sector is greater than other parts of the economy. The stakes could not be higher. London is the wholesale financial centre for the EU. It hosts nearly 360 banks, many of the major insurance companies and is the largest stock exchange in the EU. The three major credit rating agencies have their EU Head Offices in London and the list goes on. There are growing concerns that the UK may lose out to other market capitals such as New York. Brexit raises fundamental issues of national and international importance.

Britain depends on trade and the success of trade will be a major factor in assessing the effect of the UK’s departure from the EU. Financial services contribute around £130 billion annually to the UK economy and account for 7% of GDP, employing around 1.1 million people, the majority of whom live outside London. There are around 100,000 non-EU nationals and 60,000 EU nationals working in the financial sector in the UK. It is a highly skilled workforce with 50% educated to degree level or equivalent. The IMF concluded that “the growth in the UK’s financial sector owes much to the single market” with the UK trade in financial services much greater than the OECD average. It is estimated that one third of the UK’s financial and insurance services are with the EU and almost all the UK Banks’ investments are with the EU.

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1 We are grateful to Stephen Connolly, University of Warwick, for advice and help in writing this article.
3 The House of Commons debate suggests that there are many financial uncertainties in Parliament about the European Union (notification of withdrawal) Bill.
The referendum result in June 2016 has raised many questions about future arrangements for the UK’s financial sector which is the largest in Europe. Its significance has been given some prominence in the discussions about the consequences of leaving. But this discussion frequently concerns technical details and overlooks the constitutional importance of Parliament and the rule of law.

The run up to triggering Article 50 and the negotiations that will lead to the final exit arrangements provide an opportunity to take stock of what is at stake for the UK economy. Whatever the final exit arrangements are, the role of parliamentary scrutiny will become an important element in ensuring appropriate accountability of the UK government in its relations with the EU after exit. The role of the rule of law in ensuring checks and balances on the financial system also has wider constitutional significance in the long term for our system of government.

The single market in financial services and the four basic freedoms have been transposed in various Directives and Regulations over the last three decades. It is not easy to replicate or imagine that what has been achieved will be repealed as much of the current achievement has come from past experience and learning from mistakes and new events. This takes time and effort. This paper provides a synopsis of some of the emerging issues for financial services raised by Brexit and explores the challenges and opportunities that they present for the rule of law.

The rule of law and the economic context

The UK’s constitutional arrangements are vague and uncertain, especially if required to provide prescriptive and concrete answers to unforeseen or unexpected events, like Brexit. Leaving the EU involves many economic and legal issues as well as a redefinition of the role of Government and Parliament.

Economic development has given rise to a wide range of social and corporate issues that informed Parliament’s legislative developments over many centuries and the importance of law in the economic, social and political life of the country has been well recognised by leading constitutional writers including Dicey, Maitland and Holdsworth. Economic history provides evidence of the use of law to address issues such as the development of relationships such as landlord and tenant, between labour and employment, and companies and between

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9 A.V. Dicey (1835-1922).
10 F.W. Maitland (1850-1906).
wealth, capital and the population. Law has underpinned many of the conditions responsible for wealth creation as well as poverty.¹²

Brexit involves the use of law to redesign the financial system and the UK’s international financial relations on an unprecedented scale.¹³ Rule of law values should inform the redesign incorporating fair procedures, good practice and proportionate responses: For reasons that are both practical and principled, for this process to succeed, it must conform to the rule of law. Lord Bingham noted that the business and economic community requires certainty and predictability, values that are underpinned by the rule of law. All too frequently, the rule of law has been too narrowly confined to political or ‘pure’ legal issues, but adherence to the principles of the rule of law in all aspects of public life and economic development is essential for the future of the UK’s financial relationship with the EU, for securing the stability of the UK economy and for sustainable economic growth. Under the UK’s constitutional arrangements, Parliament plays a central role in securing the rule of law during Brexit and into the future.¹⁴

**Brexit and Financial Services**

Financial services constitute a key sector in the forthcoming negotiations between the UK and the EU,¹⁵ inextricably linked to the economic wellbeing of the country. Significantly there is a large element of “inter-linkage” between London and financial markets across the EU.¹⁶ A large number of foreign institutions participate in the UK and many non-EU financial institutions use the UK as a hub to access clients in the EU. Negotiations will need to address both how UK firms have access to EU markets as well as the needs of those firms from third states (non-EU countries) that use London as a platform and legal basis to access the whole European financial market.

The EU single financial market provides an example of financial integration and the removal of barriers has led to a situation that, paradoxically, has benefitted the City of London most. Indeed, the City has become a key exponent of the advantages of such single market. As acknowledged, under the single passport, a financial service provider authorised in one Member State may provide such services in any other Member State via branches and other forms of provision of services (such as online provision). Subsidiaries are different in that they become legal persons under the law of the country of incorporation. Because an authorised legal person in one Member State may offer financial services via this “passporting”, intra-EU cross border financial activities have flourished in recent years. Once the UK leaves the EU the operation of the single passport system will cease for UK firms and this will have

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¹² Sir William Holdsworth, “A Neglected Aspect of the Relations between Economic and Legal History” (1927) 1 Economic History Review 114-23. This point was also made at the time by Adam Smith and Henry Thornton.

¹³ The vote in favour of leaving the EU has resulted in setting up a large number of Government Departments alongside civil service teams set up for that purpose. House of Lords Library Note: Leaving the European Union: Machinery of Government Changes LLN 2016/070 (16 December 2016). The new government departments include the Department for Exiting the European Union and the Department for International Trade. There are a number of Cabinet Committees, the European Union Exit and Trade Cabinet Committee, the Joint Ministerial Committee on EU Negotiations.


¹⁵ House of Commons Library, Briefing Papers Number 07628 Brexit and Financial Services (1 November, 2016).

¹⁶ CityUK, Key Facts about the UK as an international financial centre 2016 (1 November, 2016).
considerable significance. Distinctions are made between basic financial services such as banking, investment services and insurance that form a core area and non-core areas such as clearing, settlement, hedge funds and financial data that developed separately. Each will need to be specifically addressed.

There have been talks that suggest that the current passport may be replaced by an equivalence regime. According to this equivalence doctrine, a third country’s legal and regulatory framework can be considered equivalent to the EU and thus granted market access as long as certain conditions are met. However, this regime has limited application since it does not encompass all financial services providers and is subject to negotiation and changes over time. Since it does not apply across all sectors and could be revoked, it is considered by many as an imperfect replacement of the single passport. Thus, relying on equivalence once the UK leaves the EU is not ideal.

The EU has also played a key role in the development of standards formulated by the Financial Stability Board and the Basel Committee on Banking Supervision. The role of these international standard setting bodies is critical in the continuation of systems of adequate prudential regulation, including markets which are fundamental for the City of London such as derivatives and their clearing.

A number of subtle but important points must be considered:

- UK financial market infrastructures (FMIs) will have to decide how to take matters forward. Will it be possible to continue to offer access to incoming firms seeking to use the financial infrastructure or will it be necessary to operate with an EU-based entity? Clearing of euro-dominated business is likely to be relocated to the euro area after Brexit.
- Alternative investment fund managers may be restricted from managing EU based-funds. Authorisation on a state by state basis is likely to be complicated.
- Many of these effects may be side-stepped by shifting offices to an EU Member State thus mitigating any immediate effects. This of course can have negative consequences for the City of London.

Opinions diverge on the consequences and advisability of leaving the EU. The mixture of difficult technical issues and political division raises the prospect of unintended consequences as well as unforeseen outcomes. Opinions are clearly divided as to the benefits and potential detriments of UK exit. Setting that debate to one side, the key question is how best to manage

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17 See the detailed analysis provided by Karel Lannoo, Chief Executive of CEPS, a leading European Think-Tank, “LSE Brexit: When it comes to financial services, the UK has much to lose and little to gain from leaving the EU” http://blogs.lse.ac.uk/brexit/2016/10/04/when-it-comes-to-financial-services-the-uk-has-much-to-lose-and-little-to-gain-from-leaving-the-eu/.
18 See the analysis of the evidence given to the House of Lords EU Financial Affairs Sub-committee on Brexit Financial Services November – December 2016 (HM Treasury Written Evidence (BFS0005)).
19 Post-trading refers to the activities that take place after an exchange of securities has been agreed upon. This includes clearing and settlement. As acknowledged, clearing and settlement is the term used to describe the processes and the infrastructures required to finalise a transaction. Efficient and safe post-trade infrastructures are a key element of a well-functioning financial market. See https://ec.europa.eu/info/business-economy-euro/banking-and-finance/financial-markets/post-trade-services/financial-markets-infrastructure-policy_en.
the new relations between the UK and the EU and between the UK and the rest of the world after the UK leaves the EU.\textsuperscript{20}

Underlying this question are issues about how to secure predictable and stable relations in the financial sector. The importance of financial services comes from the fact that there are over 56,000 financial service firms engaged in financial markets in the UK. A large proportion have to be regulated within the UK.\textsuperscript{21} This is a technically complex operation as it requires consistency and fairness as well as cooperation between the different regulatory authorities and standard setting bodies. This cooperation is not only within the EU but also worldwide, reflecting as it does that financial markets are international.\textsuperscript{22}

There is also the dynamic of open markets, favoured by some countries against the protectionist policy of others. Underpinning regulatory approaches are the need for consistency and the application of common regulatory standards. Financial markets are also sensitive to sudden changes or unanticipated shifts in regulatory policy. Their economic vulnerability to turbulence in the market exposes the sector to shocks that may create wider financial problems. The shadow of the 2008 financial crisis hangs over the sector as a whole. Mitigating market fears and over-reactions is essential if financial regulation is to be effective.\textsuperscript{23}

All of this raises important legal and constitutional issues, not least in terms of the procedures for scrutiny of the process of Brexit. The outcome of the negotiations will have implications for the long-term outlook of UK economy as well as the stability of its constitutional and political institutions.

\textbf{Membership of the European Economic Area (EEA)}

The EU maintains different types of agreements with different countries, such as the Agreement on the European Economic Area with EFTA countries (the Norwegian model), a series of bilateral agreements with Switzerland (the Swiss model) or the customs union agreement with Turkey (the Turkish model). But there is no obvious Brexit model. The terms and conditions for accessing the EU single market post Brexit will only become clear after an intensive period of negotiations, which will commence with the formal trigger of Article 50.\textsuperscript{24}

Authorised financial firms are currently entitled to trade under the relevant single market directive within an EEA area and provide services. As explained earlier, passporting is based on the assumption of an authorisation by a competent authority in one Member State and

\textsuperscript{21} The Financial Conduct Authority regulates over 24,000 of the firms within the UK. See the letter from Andrew Bailey to Andrew Tryrie, Chair of the Treasury Committee, House of Commons (28 October 2016).
\textsuperscript{22} House of Lords Library Note: Leaving the European Union: Global Free Trade LLN 2016/3.
notification to the competent authority in the other Member State/s where the firm wishes to do business.

There are limits on what is included in the passport arrangements but the principles underlining the passport system are important as they provide framework, giving firms certainty and predictability as to the rules and “tradability” of assets.

These arrangements are specific to the various individual financial service providers. There is no single passport that applies to all financial services. In some types of financial services the option of the passport system does not apply, for example in the case of a consumer credit agreements. When no passport scheme operates, firms must either rely on their direct rights under the Treaty on the Functioning of the European Union arrangements to operate on a cross-border basis or apply to the specific regulatory body for authorisation. The UK’s regulatory scheme would need to be permitted to authorise UK firms or the UK firms would need to seek authorisation through the regulatory system of the Member State they are hoping to trade in. (It is worth noting that there is a related form of passporting concerning prospectuses. This benefits capital market securities listings and the creation of a capital markets union.)

Since the single passport is predicated on the basis of free movement, there have been talks about using other regulatory models as noted above, notably third country ‘equivalence’, which refers to the possibility of market access to groups or entities based in countries who can show that their financial sector regulation is equivalent. This possibility is set out in a patchwork of rules, including Markets in Financial Instruments Directive II (MIFID II) and other pieces of EU regulation governing financial trading, but covers a narrow range of services, and thus it is a partial solution for certain parts of the financial industry. For most banks equivalence may not prevent them from relocating their operations. There have also been suggestions of having a “tailored deal” or “bespoke deal”, but this is likely to require some concessions on freedom of movements and budgetary contributions.25

The UK is a member of the WTO as well as the EU (though currently its WTO membership is subject to the membership of the EU). Leaving the single market with no Free Trade Agreement in place would leave the UK’s access to the EU’s market be governed by WTO rules. Settling these arrangements is likely to be complex and time-consuming and lack of access to passport arrangements will leave considerable uncertainty for many firms. Their retreat from London is a likely consequence. The negotiation of WTO agreements will also be complicated by the fact that the UK will have to seek “equivalence” arrangements or to make use of third country passports whenever possible or even authorisation from each regulator of the jurisdiction where financial business is being transacted.

Andrew Bailey of the Financial Conduct Authority (FCA) in a letter to Andrew Tyrie, Chair of the Treasury Committee warns:

Furthermore, in a complex landscape analyses should be based upon an understanding of the links and dependencies across and between these factors, whereby the withdrawal of passporting rights under one Directive may have associated effects in other areas.26

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25 Ibid.
26 Andrew Bailey letter to Andrew Tyrie, Evidence to the Treasury Committee (28 October 2016).
Changes in the UK’s relationship with the EU are likely to lead to a lessening of the UK’s influence in the way rules are written and created. Addressing such challenges will require technical dexterity as well as sound economic analysis from regulators and the UK government. Transparency and oversight are necessary to ensure that there is public confidence in the outcome and parliamentary scrutiny as the arrangements are developed seems essential.

**Non-EEA agreements and UK financial institutions – Switzerland and Canada**

Two models are currently being considered as possible “fits” for the arrangements that are negotiated between the UK and EU: Switzerland and Canada. The former relies upon a number of bilateral agreements that give firms certain rights similar but not the same as the single market. However, the Swiss model does not cover financial services with the limited exception of non-life insurance and is unlikely to be offered by EU negotiators because of its complexity and the incentives it may give to other Member States in allowing the possibility of cherry picking. Moreover, even in this case the arrangements do not amount to the equivalence of passporting. This is not an ideal model. It leaves considerable uncertainty as well as complexity in the working out of arrangements.

The Canadian model is based on the EU-Canada Comprehensive Economic and Trade Agreement (CETA) which makes trade in financial services possible through the World Trade Organisation (WTO) and the General Agreement on Trade in Services (GATS) principles. This means that passporting rights do not apply and financial companies in Canada face the same challenges as other non-EU firms in negotiating authorisations. In fact the requirements of authorisations represent a major problem for many non-EU firms that cover a wide spectrum of companies and their activities.

It will require careful negotiation to determine a successful outcome for such companies. The outcome may also have an impact on competitiveness and also on the financial choices that consumers may have.

Underlying the challenges that face the UK are also the likely consequences on markets. In evidence to the House of Lords European Affairs Sub-Committee on Financial Services, the Financial Conduct Authority concluded:

> There may be risks to market integrity, particularly if the price formation process were rendered less efficient if, in transition, market liquidity fragmented between the UK and EU27 financial centres. This would be a risk both for the UK and the EU 27 as this fragmentation could lead to systemic risk.

One important, but perhaps too readily overlooked consequence is that regulatory cooperation and continuity will be difficult to achieve especially in a period of unforeseen changes. It is not easy to know how post-Brexit UK regulators will be regarded and how much influence they will have in shaping the future of financial regulation. This is a key question in terms of reputation as well as future political influence. Though hard to quantify or calibrate it is essential for the UK to maintain a strong influence in international organisations and institutions.

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28 The Financial Conduct Authority (FCA) written evidence to the House of Lords European Affairs Sub-Committee November 2016 evidence BFS0003.
WTO and EU Frameworks

The UK is an original member of the WTO, so leaving the EU does not mean that it will have to renegotiate its accession to the WTO. However, UK trade concessions to other WTO members are currently part of the EU schedule of concessions in goods and services. Once the UK leaves the EU, a process will have to be observed to disentangle UK’s trade concessions from the EU’s schedule of concessions annexed to GATT 1994 and GATS, followed by a certification of the new UK schedules by other WTO members. Leaving the single market with no deal in place would leave the UK’s access to the EU market be governed by WTO rules. Settling these arrangements is likely to be complex and time-consuming and lack of access to passport arrangements will leave considerable uncertainty for many firms. Their retreat from London is a likely consequence. The negotiation of WTO agreements will also be complicated by the fact that the UK will have to seek “equivalence” arrangements or to make use of third country passports whenever possible or even authorisation from each regulator of the jurisdiction where financial business is being transacted.

There is a framework for market access in financial services under the GATS arrangements for WTO members. There are a number of important aspects that should not be overlooked.

To begin, GATS provides a schedule of commitments that apply, for example, to asset managers. The UCITS (Undertakings for the Collective Investment in Transferrable Securities) Directives require that the funds are managed by an EU manager with an EU depository. This has implications for the fund arrangements. There has to be a managed company established in the EU and also a depository in the Member State of the UCITS. The arrangements also extend to EEA states that are not in the EU such as Norway, Iceland and Liechtenstein. There are passporting arrangements but these are limited to EU Alternative Investment Fund managers (AIFMDs), that are authorised under an EU regulator. The latter is a key element in being able to manage financial Alternative Investment Funds (AIFs) in another Member State on the basis of establishing a branch in that Member State or on a service basis. The role of the AIFMDs is to offer the prospect of a third country passport for managers and funds that are outside the EU. The AIFMD system is deeply unsatisfactory when it comes to passporting non-EU AIFMDs. US fund managers regularly complain that they must obtain multiple authorisations to ensure compliance. This is an ongoing matter for discussion and the arrangements are not yet in place. In July 2016, the European Securities and Markets Authority (ESMA) published advice on future regulation but it has not been acted upon yet.

The Role of UK Financial Regulators after Brexit

Brexit has significant implications for the role of UK Financial Regulators both during the negotiations leading to Brexit and thereafter. Ensuring cross-border access is a key objective. Close co-operation with other regulators is also an important goal. The aim is to minimise the risks of regulatory arbitrage and fragmentation in financial markets. Co-operation between regulatory authorities is thus essential for safety and soundness and establishing a robust

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29 As acknowledged, WTO rests on the General Agreement on Tariffs and Trade (GATT) and on the General Agreement on Trade in Services (GATS).

30 See also http://www.ictsd.org/opinion/nothing-simple-about-uk-regaining-wto-status-post-brexit
regulatory and supervisory framework is key in this regard. However, achieving this outcome will require considerable effort and activity.

Withdrawal from the EU does not change the statutory arrangements of the FCA, Prudential Regulation Authority (PRA) and Bank of England but it will inevitably change the way markets operate and this will need to be factored into the work of these regulatory bodies. The future is uncertain but it is clear it is likely to have consequences that will need to be addressed very carefully.

Overall the question of continued co-operation and influence is likely to be essential for effective regulation but this is also necessary for any prospect of influence over financial standards globally. That influence is likely to be the key to future success and ultimately effective regulation.

Finally, the effectiveness of many UK financial firms as well as regulators will depend on recruiting a skilled and well-trained workforce. This is essential for competitive financial firms as well as regulatory influence. The role of the US is critical in terms of international regulatory agreements and if it retrenches from global arrangements this may well effect the prospects for the UK after Brexit.31

Operating outside the EU will bring many new challenges and opportunities. The FCA in particular will have intervention powers for incoming passporting firms that are regulated within the EU or the EEA. This will require co-operation with the European Supervisory Authorities (EBA, ESMA and EIOPA) and national regulators and supervisors in other Member States. Furthermore, the issue of the location of EBA, currently based in London, will have significant consequences for the City’s influence in the design of European banking rules.32 Working outside the EU regulatory framework may also give rise to greater flexibility but remains to be seen. It is worth considering the market that will allow new players to engage. There will be some practical limitations on such flexibility as there are responsibilities under the Basel Committee on Banking Standards Supervision.

Underlying any assessment of prospects for the future are uncertainties and difficulties that will accompany future planning and strategy. At risk are many of the UK’s most important financial firms and economic relations. The future influence of UK regulators in the global economy and their contribution to setting regulatory standards is also important, perhaps more than ever before in an uncertain world.

Economic Uncertainties and the Brexit process and the importance of the rule of law and Parliament’s role

In periods of potential economic turbulence and uncertainty the need to uphold the values of the rule of law is paramount. One aspect of the rule of law is that it has an overarching

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influence as to how Parliament should behave.\textsuperscript{33} This is particularly important in light of the recent Supreme Court decision in the Miller case,\textsuperscript{34} requiring an Act of the UK Parliament to authorise leaving the EU.

This is a period where politics are highly contested after the unexpected referendum result. The major political parties, including the Government, having campaigned to remain, are faced with the difficulty of leaving and of being scrutinised more than at any time in recent constitutional history. Lack of clarity about the legal effects and the policy consequences of Article 50 negotiations leaves considerable discretion in the hands of the Executive and the negotiating arrangements undertaken by the EU institutions. Policy making is likely to have to operate through contingency planning. Even the date of the conclusion of Brexit is uncertain. Assuming that Brexit is commenced at the end of March 2017, it is possible that the Brexit arrangements will be concluded by March 2019. This date may be extended by a unanimous agreement of the EU 27.

The UK Parliament has responded eventually to the uncertainty, after some months of inertia. At least 30 inquiries are being undertaken by Parliament, 13 in the House of Lords and 18 in the House of Commons. Some are in the process of being prepared while others have been published.\textsuperscript{35} The House of Lords European Union Committee 9th Report on Brexit: Financial Services\textsuperscript{36} provides important recommendations and analysis of the issues facing financial services. This is against a backdrop of stubborn government resistance to any parliamentary scrutiny. Parallel to the UK’s Parliament activities, the EU Parliament, whose assent is needed for Brexit, will also be engaged in substantial scrutiny and information gathering about the negotiations and their completion. MEPs are likely to be given access to the EU Commission’s meetings and to the progress of the negotiations. This will leave MEPs potentially better informed and knowledgeable than their counterparts in the UK Parliament. The contrast between the two Parliaments could not be clearer.

The main benefit of parliamentary scrutiny is that the full significance of the many complex areas of discussion, particularly financial and economic, will receive a wide canvass of expertise and analysis. Select Committees, empowered since the election of independent chairs, could provide a resilience that will empower negotiation rather than enfeeble it. Parliamentary scrutiny can also give the final agreement legitimacy, leading to its ratification by the UK Parliament. The necessary connection between the intensity of scrutiny and information available in the UK Parliament and the EU Parliament is one that cannot be avoided. If the EU Parliament is better informed than the UK Parliament, UK parliamentarians would be unfairly treated and less able to engage properly than their EU counterparts. Moreover, the legitimacy of the process in the UK may be undermined.

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\textsuperscript{34} R (Miller) v Secretary of State for Exiting the European Union See note 7.
\textsuperscript{35} House of Lords Library Note: Leaving the European Union: Machinery of Government Changes LLN 2016/070 (16 December 2016) There are a number of key committees involved with Brexit: in the House of Commons they include the Exiting the European Union Committee, the International Trade Committee as well as many other specialist committees covering sectoral issues such as agriculture; in the House of Lords they include the Liaison Committee, the European Union Committee. There are a number of specialise committees and sub-committees including human rights as well as police and security cooperation.
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Parliamentary select committees have also an important opportunity to develop their methodology and techniques of inquiry beyond the mainly retrospective analysis that is too often the norm. Setting proactive terms of engagement will facilitate finding evidence, evaluating data and engaging with analysis that will not only bring government to account but simultaneously empower the government of the day to negotiate in a more effective manner. Empowerment will also come from engagement with other stakeholders and MPs. It has the potential to offer a wider perspective on financial and economic sectors and a substantial improvement in the negotiations. There are powerful incentives. Summoning witnesses, hearing evidence and questioning ministers should not be undervalued. There are also opportunities that hold their own rewards. Engaging with the public and media has the potential to enhance Parliament’s reputation and provide an important connection with public concerns. Financial sectors require assurances that their voice is being heard.

There are, however, concerns that the large number of select committee inquiries may dissipate their effectiveness. The solution is to co-ordinate the findings and collate the evidence. Two Committees may prove decisive: The Liaison Committee and the Brexit Committee. The Liaison Committee is pivotal in ensuring co-ordination of the various inquiries. This can be taken forward by effective communication between the various committees and a pro-active approach to management. It might also be possible to identify and address any gaps in the inquiries as well as ensuring coherence in the findings and recommendations of the committees. There is also a need to give particular priority to certain sectors, particularly in the area of finance and economics. Taking this approach is tied to engagement with appropriate expertise and information and has a broad appeal of strengthening Parliament as well as the Government’s negotiation strategy. The Brexit Committee, set up to monitor the Brexit department responsible for the co-ordination of Brexit negotiations, is also likely to be pivotal. This is a new committee with untried membership and an unprecedented remit. The work of the Committee is ongoing and it has engaged with monitoring the Government’s policy on Brexit. 37

Finally, but also important is the role of the courts and their significance is far from clear. The Supreme Court decision in the Miller case 38 has made clear that debate in the UK Parliament and an Act of Parliament are necessary to authorise triggering Article 50 to leave the EU. In many cases UK courts have acted with self-restraint, especially when policy and economic matters are being discussed. This was clearly illustrated in the aftermath of the 2008 financial crisis. In R (application of SRM Global Master Fund LP) v Treasury Commission (The Nationalisation of Northern Rock), 39 claimants sought judicial review of the decision to nationalise Northern Rock. The standing of the claimants was that they were all share-holders of Northern Rock. Their complaint was that the valuation of Northern Rock at the date of nationalisation was unfair. Northern Rock was a going concern, although insolvent and that the conditions of the support provided by the Bank of England as the Lendor of Last Resort imposed high interest rates on Northern Rock for the monies provided by the Bank of England. This had the effect of making the valuation of the mortgage portfolio of Northern Bank unfairly benefit the Government through providing a profit for the Bank of England loans. The financial support provided by the Bank of England deprived shareholders of their

38 R (Miller) v Secretary of State for Exiting the European Union. See note 7.
39 [2009] All ER (D) 139.
profits and the provisions for compensation to existing shareholders was unfair. The case argued by the claimants was that through the economic device of loans and guarantees, the Bank of England secured for the taxpayers expropriation through nationalisation of Northern Rock but without adequate compensation to the Northern Rock share-holders. The case made out by the claimants was rejected. Stanley Burton LJ held that without Bank of England intervention Northern Rock would have ceased trading. The Government through the Bank of England could have withdrawn support – there was no duty to provide financial support and no legitimate expectation to do so. There was no requirement to give such support and the compensation scheme for the shareholders had to accept Northern Rock’s valuation based on the loans provided. The claim was dismissed. This is a good illustration of the self-restraint shown by the courts in matters of policy and economics.  

Another example is when the courts are invited to consider matters relating to public spending particularly how the public purse is best protected. The decision of the Supreme Court in the HSE v Wolverhampton City Council\textsuperscript{41} considered the responsibilities of public authorities when deciding to exercise a discretionary power to achieve a public objective. The main question was whether or not costs to the public ought to be taken into consideration. The Supreme Court considered the responsibilities on public bodies and their application to the case in question. Planning permission for a block of four student residences had been applied for and granted. In the course of construction, the Health and Safety Executive (HSE), concerned about gas storage on site, applied for an order to revoke planning permission against Wolverhampton Local Authority. In refusing the application, the Council considered costs and came to the view that, if planning permission were revoked, the cost of compensation that would be payable would be high. It consequently refused the HSE’s application. The HSE brought judicial review proceedings against the Council. The High Court refused that part of the claim. The Court of Appeal allowed the HSE appeal and held that the Council has to make its decision in isolation from the economic circumstances of the decision. The Supreme Court adopted a different approach, and decided that a public authority was entitled to take into account the cost to the public purse. Section 97 required the authority to satisfy itself that revocation is expedient including consideration of the development plan and other “material considerations”. As the payment of compensation is a relevant matter, the cost to the public purse has to be considered. In general principle, a public body has to take into account public spending. 

It is to be expected that tackling financial and economic disputes will require considerable dexterity but judicial oversight will be paramount in ensuring the rule of law is upheld. 

Conclusions 

Linking debates about Brexit to the overarching concerns of the rule of law is timely. The rule of law provides an essential framework for the discussion of many aspects of Brexit including 

\textsuperscript{41} HSE v Wolverhampton CC [2012] UKSC 34.
the role of Parliament, the importance of the courts and the values of justice and fairness, especially legal certainty.

In the *Miller* decision,\(^{42}\) the Supreme Court affirmed the importance of prior authorisation by Parliament through debate and an Act of the UK Parliament. Some years earlier, Lord Bingham noted the historical importance of the rule of law to the earliest commercial life of the nation. History has a resonance with the present. Over 250 years ago, Lord Mansfield made some pertinent observations: “The daily negotiations and property of merchants ought not to depend upon subtleties and niceties; but upon rules easily learned and easily retained, because they are the dictates of common sense drawn from the truth of the case.” Later he concluded that in “all mercantile transactions the great object should be certainty: and, therefore, it is of more consequence that a rule should be certain, than whether the rule if established one way or another. Because speculators then know what ground to go upon”.\(^{43}\)

Setting the agenda for the future will require careful consideration of the many potential implications of Brexit for the financial sector.\(^{44}\) The Institute for Government has identified four main options for UK and EU relations after Brexit.\(^{45}\) The first is *EEA membership* but this requires acceptance of freedom of movement. The benefits of EEA are that Member States provide services to other Member States without having to be concerned about regulatory equivalence. The merits of this option will ensure that the UK will be able to maintain financial services.

Second, the operation of a *Free Trade Agreement*. This would involve several different permutations. There are many service sector agreements. Settling on the appropriate arrangements for financial services will take some time and effort. For example the trade agreement between the EU and Canada does not include financial services. There are other models such as Switzerland for insurance and public procurement but there is not one for financial services.

The third option is *membership of a Customs Union*. The benefits are restricted as none of the Customs Union arrangements cover services and are confined to trade in goods. Membership does not give any preferential access to the EU’s services market.

The fourth option, in the event of a “hard Brexit” would be adopting *World Trade Organisation (WTO)* rules. The UK might lose its passporting rights and will then require acquiring authorisation from each individual member state. This will take some time and cost to achieve. Selecting the most appropriate option is a matter for public debate as well as government negotiation.

There is also the option of *unilateral free trade*. The option of a trade agreement with the USA is actively being pursued with an uncertain outcome.\(^{46}\)

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\(^{42}\) *R (Miller) v Secretary of State for Exiting the European Union*. See Note 7.

\(^{43}\) T. Bingham, *The Rule of Law* p. 38.

\(^{44}\) There is also a question of Brexit having differential impacts on the different nations. See: Akash Paun and George Miller, *Four-nation Brexit* London: Institute for Government (October 2016).


The House of Lords European Union Committee in its recent 5th Report concluded that there should be a transitional arrangement and that the government should focus on its future trading relations with the EU and WTO. One option is to trade under WTO rules but this is not straightforward. An early decision should be made about the value of a Customs Union such as where there are trade arrangements under WTO rules are likely to take some time to finalise. The EU has been influential in developing WTO rules and this influence is one that will need to be considered in any negotiation. The same House of Lords European Union 9th Report on Financial Services pointed to the imperative that “the Government gains a detailed understanding of how firms are likely to be affected by changes to their rights of access to EU markets”.

The main passporting arrangements are complicated and many firms do not realise the extent to which they are reliant upon the current arrangements. Underlying the uncertainties are questions about future relationship with the EU especially in areas of insurance and banking. Access to and maintaining international standards is a key element in any future relationship. Staffing is also critical and having the ability to hire the most qualified staff will inevitably require access to skilled migrants.

The House of Lords Committee emphasised the need for certainty and clarity over how the interests of various stakeholders are to be met. The value of UK financial services to the EU also needs to be fully researched and presented as a clear negotiating strength. This note does not consider the special implications that the UK decision to exit the EU will have for the devolved nations. However, it is likely to impact on their economy as well as financial relations within the UK and needs to be properly assessed.

Underpinning future strategy is the desire to set up free trade agreements that will encourage the UK to participate in global free trade. Setting high expectations underscores the need for suitable and rigorous forms of accountability and oversight. Upholding the rule of law in the Brexit process can define the future of the UK in a way that rekindles the spirit of our constitutional inheritance. Unchartered change, increasing uncertainty and fragility in economic markets are certain to raise questions about additional costs and added burdens from Brexit. Deciding on whom the many burdens should fall and how the distribution of costs might be fairly weighted sets new and unexplored challenges for existing institutions and values. In this uncertain time adhering to fundamental values of justice and fairness can help set priorities and become a predictable and useful guide to how the future might be enjoyed in a tolerant society that lives up to the spirit of the law. The rule of law should prevail and protect citizens especially the poorest and most vulnerable.

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48 Ibid. para 2 p. 39.
49 Ibid, para 20 p. 41.
52 Swati Dhingra, Gianmarco Ottaviano, Thomas Sampson and John Van Reenen, The Consequences of Brexit for UK trade and living standards LSE: London; Centre for Economic Performance, March 2016.