Standard Life

Review of the balance of competences

Single Market: Financial Services and the Free Movement of Capital

Response to the Call for Evidence

Standard Life welcomes the opportunity to provide evidence to the Government review of the Balance of Competencies between the United Kingdom and the European Union in relation to Financial Services and the Free Movement of Capital.

About Standard Life

Established in 1825, Standard Life is a trusted provider of long term savings and investments to around six million customers worldwide, with a further ten million customers in our joint ventures.[1] The Standard Life group includes savings and investments businesses, which operate across the UK, Canada, Europe, Asia and Middle East; workplace pensions and benefits businesses in the UK and Canada; Standard Life Investments, a global investment manager, which manages over £179bn globally; and its Chinese and Indian Joint Venture businesses. At the end of September 2013 the Group had total assets under administration of over £237bn.[2]

Standard Life plc is listed on the London Stock Exchange and has approximately 1.3 million individual shareholders in over 50 countries around the world.[3] It is also listed in the Dow Jones Sustainability World Index, ranking it among the top 10% of sustainable companies in the world.

Standard Life has operations in several member states in the EU, and is the leading provider of workplace pension schemes in the UK, where we administer group schemes with over one million members. The content of our response reflects the significant role we play in the financial services sector within Europe, and beyond, and our desire to encourage greater levels of long-term savings and investments in all territories.

Standard Life recognises the significant benefit to our industry of access to the single market as well as the associated challenges of working within a dual layered regulatory and legislative system. We need to protect and promote the single market and work to ensure the EU's regulatory structures and systems work effectively. UK firms, like Standard Life, need to maintain our role in proactively informing and shaping the EU policy agenda, particularly where challenges exist, with an open, constructive, and thoughtful approach.

Framework

The EU can be an impetus for greater objectives – protecting a wide consumer base and shaping complex policy initiatives. Standard Life views the Single Market as an opportunity to access a wider market and provide our services thanks to rules that make cross border activity possible and more affordable to consumers. The Single Market is not perfect. The rules that govern it are being drafted as a reaction to 2008; sometimes they are viewed as being too detailed and sometimes

[1] These figures are correct as of January 2014
[2] The figures in this paragraph are correct, as at 30 September 2013
[3] This figure is correct as of January 2014

they are viewed as too broad. However, we would counter that on the whole, the EU and the Single Market provide our business with the opportunity to provide our customers with a wider range of options. The EU and the Single Market provides all its Member States access to markets that would otherwise be surrounded by tariff barriers. Being part of this barrier-free union allows the UK to act as portal to third countries who want access to EU markets.

Financial services in the UK act as hubs because the UK can offer market access to the EU whilst providing the infrastructure, labour and technical know-how that international firms require. The relationship with the EU benefits not only our business, but also the whole of the UK.

It is impossible to make an assessment of the UK's relationship with the EU without looking beyond our borders. EU rules have made it easier for financial stability to gain more solid footing in the wake of the crisis. Bodies such as the ECB, G20 and international supervisory agencies have given us a forum to come up with international solutions to international problems. The financial crisis has not been limited to the UK alone. During the crisis, more agreements and actions have been made possible by the participation of these international bodies. Our business is international; our regulations need to have an international dimension as well.

Consumer protection is of central importance to Standard Life. The EU is working on creating a Single Market that provides greater choice and protects more than 500 million citizens. It is not a perfect system, nor is it complete. We engage with the EU to highlight best practice from across the EU and third countries where we operate. The single rulebook must be finalised to ensure that customers from across the EU are equally protected. That being said, it also needs to remain flexible to ensure that it can deal with the particularities of individual markets. The UK has a significant role to play in the future with promoting this.

Q1. How have EU rules on financial services affected you or your organisation? Are they proportionate in their focus and application? Do they respect the principle of Subsidiarity? Do they go too far or not far enough?

DEPTH OF LEGISLATION

For Standard Life, effective regulation promotes genuine harmonisation within the EU, is proportionate and does not breach the principle of subsidiarity. Examples of regulation that do not appear proportionate are CRD IV and Solvency II. In both cases, we strongly agree with the principle of the intended purpose of these prudential regulations. However, we feel that lengthy rule books that run into the thousands of pages and are at an extremely granular level of technical detail may not be helpful and may even constrain market access to new entrants.

SUBSIDIARITY AND PROPORTIONALITY

We note that the UK is consulted on legislation that has an element of subsidiarity. Indeed, all national parliaments have the opportunity to assess and register opinions with the EU if they feel that legislation risks breaching subsidiarity.

In terms of EU legislation being proportionate in focus and application, the volume of legislation going through the institutions leads to considerations of the interoperability, both within the EU and externally. There could be unintentional distortions in the Single Market. Externally, dossiers like Solvency II and CRD IV resemble work that is going on at the international level, but there will need to be extensive negotiations to ensure that firms are able to continue doing business across borders and that EU and global developments are well aligned.

For Standard Life, the effectiveness of regulation's ability to protect customers and provide them with real benefits is paramount. Whilst acknowledging the prudential regulation is both technically complex and very important, especially following recent banking issues, we feel that a more proportionate approach to both the volume and level of detail in these regulations is likely to result in better regulation and a safer industry.

Q2. How might the UK benefit from more or less EU action? Should more legislation be made at the national or EU level? Should there be more non-legislative action, for example, competition enquiries?

On the whole, the UK benefits from EU action. Market access is of central importance to financial services and Standard Life is no different. We welcome the completion of the Single Market to ensure that consumers are protected equally across borders. We also look for the EU and its supervisory authorities to take action in ensuring that directives are implemented equally across all Member States.

Naturally, inconsistencies within the Single Market have led to uneven levels of certain measures. The example of the Retail Distribution Review in the UK is an area where the UK has implemented a higher level of standards than the Commission's initiatives. This may result in UK firms being at a possible disadvantage to those EU firms that passport services in the UK. On the other hand, the UK has benefited from EU regulation such as from the National Private Placement Regime.

TAXATION

Another area where the UK may benefit from more EU action is concerning tax. The reserved nature of tax law can cause the Single Market to act in a suboptimal manner and can act as a de facto restriction on capital flows into and out of Member States. This can be demonstrated with respect to both the Third Life Directive and UCITS. The freedom of movement of capital is the fundamental freedom that has most often come into conflict with local tax policy across Member states. There is extensive case law, both at Member State and ECJ level, which have found that local tax policy acts in a discriminatory way and acts as a restriction to the freedom of movement of capital. An example would be ECJ case law concerning withholding taxes (typically applied cross border but not locally) and the tax treatment of dividends (e.g. local dividends exempted but non-local subject to tax). Other cases have dealt with issues concerning freedom of establishment.

Whilst the courts have generally found in favour of taxpayers, the fundamental freedom has clearly not been reflected in Member States' tax law. This has effectively acted as a de facto restriction even if the courts have subsequently found that the fundamental principle trumps local tax law. This can only have a detrimental impact on the ability to offer cross border savings products, either due to differing treatments of the products themselves or differing treatment of the underlying investments.

Any action taken by HMG on tax issues should not violate rules set out in Article 113 TFEU and should support the fundamental principles of the freedom of movement of capital and freedom of establishment.

FTT

Although the FTT is not a settled matter, the proposal as it currently stands will create a barrier to transacting in investments and will also create a barrier within the EU given the limited number of Member States which will join the FTT zone.

NON-LEGISLATIVE ACTION

Non-legislative work done at the EU level could be considered in one of two ways – that it is beneficial, and guides the Commission in its legislative work. In a sense, it is taking the pulse of the European Parliament before it issues legislative work (as is its right of initiation). On the other hand, non-legislative work can often be controversial, and may divert limited resources away from badly needed legislative work that will complete the Single Market. Prior to any non-legislative dossiers being initiated, there should be a broad assessment made as to whether or not there is capacity to provide resources. Any work undertaken, however, may provide another piece of the Single Market puzzle.

Q3. How have EU rules helped or made it harder to achieve objectives such as financial stability, growth, competitiveness and consumer protection?

LONG-TERM PLANNING AND FINANCIAL STABILITY

On the whole, the UK benefits from financial stability, growth and competitiveness that comes from global solutions that are being sought out in forums such as the EU, the G20 and others. When we are presented with concrete proposals and definitive timelines, we are in a better position to forward plan. This in turn results in our ability to invest in the wider market, leading to growth of the economy.

As a customer-driven company our planning needs to be as secure as possible to deliver what we have promised to our consumers. The EU regulatory process can present challenges to our long term goals. Given the technical nature of the legislation that is currently making its way through the EU institutions, a small change in wording in a draft can result in a significant redesign of a planned system change, business process redesign and redesign of information provided to consumers.

GROWTH

Development of EU regulation can be lengthy and unpredictable. The complexity of the network of players is also extensive. Surprise last-minute development can unravel business response plans. These are the very reasons that that the UK should stay engaged with the process of EU rulemaking. Many businesses rely on long-term planning and when capital requirement directives and regulations are being drafted, there may be instances of capital being tied up unnecessarily or not being able to procure and assign adequate or appropriately skilled resource. Last minute changes can also mean capital and resources are inefficiently assigned which could have cost implications and consequently filter down to the real economy. The UK must be involved heavily with the decision making process to ensure that their expertise in complex financial services legislation is captured.

INVESTMENT AND COMPETITIVENESS

An example of a successful EU wide product is UCITS funds. Currently UCITS funds domiciled in one member state can be successfully distributed across all others. The UCITS license and brand has been successful in creating a standardised fund structure that can be promoted across the EU.

Naturally, there are some drawbacks when examining the details of the regime. This problem highlights the incompleteness of the Single Market. Standard Life's experience has demonstrated that funds domiciled in certain EU Member State can be used more widely. For instance, Luxembourg SICAVs appear to be the most easily distributed across Europe and further afield into Asia. Ireland is also a popular domicile for some types of UCITS, such as money market funds. Much of the preference appears to have been in the tax transparent nature of Luxembourg and Irish funds. Until recently, UK funds were disadvantaged by their tax arrangements and so the uses

of Luxemburg and Irish UCITS vehicles have allowed us to distribute our products more widely. Our position on tax harmonisation is set out in question two.

Although we have noted a discrepancy in the ability to invest in UCITS licensed countries, our experience has shown that the regime as a whole is extremely useful in driving investment. We also note that many international investment firms have set up in London, perhaps with a view to having access to a UCITS licensed domain. More broadly speaking, our investment business has more avenues to explore as a result of EU membership. In turn, our customers are able to have more choice. Standard Life Investments' operation has benefited from standardisation across the EU and indeed do benefit from global standardisation.

EU AND GLOBAL STANDARDISATION – BOLSTERING THE UK ECONOMY

An area that benefits from the weight of a common EU position in the global regulatory environment is that of capital requirements across the banking and insurance industries. These regimes may act as a template for action taken by international regulatory bodies. Furthermore, firm action taken by international actors bolsters confidence in markets, which in turn contributes to recovery in our local economy.

Examples such as EMIR and some parts of MiFID fall into this category. When dealing with investments, it is done on a global basis and ideally this could be done with common standards across all markets. It is, however, beneficial for the EU to approach global regulatory standards setting bodies with a united voice. The implementation of EMIR brought standardisation of handling OTC derivatives trading across the EU. Standardised requirements in these areas would help us to invest on a global basis.

Q5. How has the EU's approach to third country access affected the ability of UK firms and markets to trade internationally?

Standard Life's experience with third country access is of particular interest to us, considering that we have six million customers worldwide and a further ten million customers in our joint ventures.[4] Our ability to offer products whilst remaining compliant is of paramount importance. The shifting sands of the regulatory field have caused many issues in the industry with forward planning.

Legislative processes take time; however major alterations in policy can cause disruptions in planning. In terms of Solvency II, the procedures that have led to the EU's approach to third country access for EU insurers operating in third countries is an example of this. The rules pertaining to third country access were set in 2009, only to be altered significantly in 2013.

Another example of where the EU rules may not be helpful on third country equivalence pertains to the lack of details at level one in Solvency II. For example, the Deduction and Aggregation consolidation method was referenced only in passing in the final level one text in 2013 and a detail-light reference in the 2009 level one text. This is a model that many firms use when accounting across borders.

EQUIVALENCY AS A TOOL

It should be noted that certain third countries have their own reasonable plans to modernise their regimes along more global lines, independently of Solvency II and have no intention of applying for

[4] These figures are accurate as of January 2014

equivalence. Such is the case with the approach Canadian regulators set out to the Commission during the negotiations of Omnibus II.

Recent global developments have emerged aimed at introducing a new global solvency standard for the insurance industry. The EU's apparent desire to push Solvency II out beyond the EU, using the equivalence route, now risks being overtaken by more global developments and events. Solvency II may be a piece of EU legislation that will be eclipsed by international regulatory developments.

We feel that a more pragmatic and consensual mutual recognition approach to third country access should be pursued going forward. This would facilitate the road ahead for EU insurers to trade fairly and successfully in global markets.

Q6. Do you think that more or less EU-level regulation in the area of retail financial services would bring benefits to consumers?

Consumers benefit from a completed Single Market. EU regulation should be suitable and appropriate, taking into account not only the end goal, but the potential impact on consumer choice and competition in the market. A fractured Single Market is highly detrimental to consumers.

In recent years, there has been a wide array of legislation that has originated from the EU; it very much highlights that the Single Market is far from being complete. In some instances, rules have been made to address specific issues that occurred in specific Member States. An example of this is the introduction of AIFM which may have been designed to deal with current events having an impact in one Member State alone, rather than being drafted with all Member States in mind. Unfortunately, the broad scope of AIFM creates a regulatory environment that covers many product types in which no issues of consumer detriment occurred. An example of this is the significant increase in requirements for Investments Trusts in the UK which have operated successfully over many decades. It is not obvious that the additional requirements will bring improved consumer protection to investors in investment trusts.

The European Parliament's adopted resolution on vulnerable consumers is an example of policy direction with unlimited scope for interpretation. Their position is that financial services as a sector is so complex that almost any consumer could be vulnerable at some point. We believe that consumer protection can be targeted and delivered effectively at the national level.

Q7. What has been the impact of the shift towards regulation and supervision at the EU level, for instance, the creation of the ESAs? Should the balance of supervisory powers and responsibilities be difference?

The ESAs provide an excellent forum for sharing information, developing a single rulebook and harmonising application of directives. Because they are empowered to look across different countries, they are better positioned to be able to examine issues that may arise. They are also able to flag up inconsistent application of directives. They play a central role in ensuring that the wide range of regulation that has come from the EU in the last five years is applied accurately and consistently.

Standard Life supports the current arrangements for ESRB oversight and the current ESFS, including powers given to the ESAs; that being said, the policy direction of moving towards pan-EU regulators and supervisors raises a number of practical questions. The ESAs have been presented

with highly technical detailed requirements that need to be delivered to NSAs and the EU institutions in a timely manner. In many instances, they are understaffed for the volume of work that they are being tasked with. There is a risk of inherent conflict with the processes of delivering a substantive programme of financial services legislation. We would prefer more detailed legal ESA guidelines. There is also a question of flexibility. We want the ESAs to retain some flexibility when examining national markets; in certain instances, different markets produce different consumer needs.

Capacity issues may come to the forefront in the coming years. The review of the ESAs due out in 2014 will hopefully identify areas where the ESAs could be fine-tuned. As ever, we continue to push for clearer legislation that delineates where the NSA has competence and where the ESA has competence. Thanks to secondment and various supervisory working groups, there is overlap between the NSAs and ESAs, but more can be done in this area. Clear competence areas will help especially in the area of directives.

Q9. How effective and accountable is the EU policy making process on financial services legislation, for example how effective are EU consultations and impact assessments? Are you satisfied that the democratic due process is properly respected?

The effectiveness of the EU has been discussed in several of the previous questions, but there are some matters that present challenges. At the moment, there is not a formal process of reflection and critical assessment of legislation or non-legislative proposals (e.g. non-papers or review clauses) that fall within a particular policy area. For example, MiFID/R, PRIPs and IMD2 may be reviewed individually in the future, but there may not be a review that examines them together and identifies issues, e.g. gaps in scope or inconsistencies in legal definitions. A process for reviewing sectoral legislation should be put in place urgently as the instances of conflict and ambiguity are increasing. Inconsistencies in work being done to complete the Single Market may defeat the original policy objective.

Lack of synchronisation in EU legislation can result when lead pieces of legislation are under development whilst a related regulation has already been completed, as with the case of MiFID II and EMIR. A similar situation is developing with MiFID, MiFIR, PRIPs and IMD2. Given that there is so much legislation in the field of financial services, there should be a heavy focus on ensuring that legislation is not drafted in silos – that is to say, the contents of the legislation need to be consistent.

EU processes can result in solid outcomes, although these processes present challenges – opaque negotiations, red tape, delays in procedure. Whilst we want coherent legislation, delays and lack of information can lead to problems if the actors involved are not aware of commercial realities faced by industry. In the Solvency II process, we have found that certain elements have been effective (such as impact assessments) but lacking in other areas (such as short consultation periods).