Getting Brussels Right: “Best Practice” for City firms in a post-referendum EU

A CSFI Report
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Preface

In early 2016, CSFI decided to review and update the findings of the report that Malcolm Levitt had written for us in 20101. This was made possible by the presence of our Fellow in Brussels (on a career break from the UK’s Foreign and Commonwealth Office) who has been with us since 2015. The work was proceeding apace, when everyone – on both sides of the Channel – was caught unawares by the unexpected result of the June 23 referendum.

Whether one is pro or anti-EU, whether one voted for or against ‘Brexit’, there is no doubt that the referendum ushered in a very difficult, delicate and (potentially, at least) dangerous phase in relations between London and Brussels – and, since financial services are so important to the City, between the City and the EU institutions. Hence, the work that we were doing to update Malcolm’s paper took on a new urgency – and, indeed, some re-interviewing of people we had already spoken to.

The result is a series of recommendations that take as their starting point the recommendations that Malcolm made six years ago. The new report is a communal effort, but I would like to thank the excellent (and much appreciated) assistance of our Brussels Fellow. I would also like to thank Malcolm and all the other interviewees in London and Brussels for their help. Of course, all mistakes are entirely the CSFI’s responsibility.

Andrew Hilton
Director
Centre for the Study of Financial Innovation

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Getting Brussels Right: “Best Practice” for City firms in a post-referendum EU

Foreword

This important Report stresses that “getting Brussels right” is more urgent than ever. Although the post-Brexit world is unknown, being dependent on negotiations yet to begin, how the City engages with the EU is, the Report stresses, crucial and needs attention both during the period up to exit and thereafter.

Its starting point is my 2010 report, the conclusions of which (summarised below) are claimed in this document to be “even more relevant and urgent than before the referendum.” Regrettably, those who were in denial about the 2010 report’s somewhat critical findings did not attend its CSFI launch where very senior officials who understood and regulated or supervised the City made their endorsement of it crystal-clear.

Now, it is essential to recognise that business as usual is not an option: without the UK, the EU risks adopting very different policy outcomes with direct implications for internationally-operating firms. EU advocacy work in the City has never been more important and needs CEO engagement, which the Report finds lagging by comparison with Continental competitors.

The Report’s authors note that the context within which the City engages with the EU is more difficult now, because of the reduced influence of the UK Government in negotiations of concern to the City - including being “frozen out”, the falling influence of British EU officials and MEPs even prior to exit, and the weakening of City links with current key Ministers and officials, including Number 10, who need to be educated without delay. The Report also comments that other Member States are determined that the UK should not be perceived to benefit from Brexit so as not to encourage domestic leavers. It also warns of the risk that “protectionist” countries see the opportunity to seize the initiative.

In several respects, matters have improved since 2010, and the Report quotes non-British interviewees who admire the quality and professionalism of City lobbying efforts. Even so, it also suggests room for improvement regarding the need:

- to adopt CEO-led engagement with the EU, where City firms still lag behind Continental competitors;
- to approach the EU in a spirit of compromise;
- to build alliances across industries and borders at firm and trade association levels;
- to recognise that the tone of engagement matters at least as much as substance, hence the need to avoid perceptions of arrogance which have been exacerbated by the Referendum;
- to be there - whether directly or through a third party (e.g. trade association, consultant);
- to stress the benefit to the real economy of City activities and to avoid appearing self-serving;
- to recognise the threat to City cooperation if firms decide to go their own way;
- to recruit non-British representatives to embrace linguistic and cultural pluralism; and
- to engage with other capitals.
I would add the following suggestions:

• We must acknowledge that past reliance on HMG for EU lobbying needs to be swiftly mitigated by direct engagement with policy-makers in other capitals, including appreciation of their political dynamics.
• This is reinforced by the need to recognise that new national alliances will emerge and will need to be assessed. The power of smaller, sympathetic potential allies will remain important, but the role of the big EU players, potentially friendly or hostile, will, in the absence of the UK, increase.
• The UK must become more involved with think-tanks in London and Brussels, and with those in national capitals where firms have operations - as well as with relevant NGOs and the media.
• We must also recognise the risk that – notwithstanding the above - the myriad of working groups, associations and individual firm activities risks drowning out key messages.
• We must engage the support of major corporates – who are the end users of City services - to stress the usefulness of the City.
• We should recognise the potential contribution of new, technology-driven, entrants to the financial services sector, who also have an interest in better regulation.

Malcolm Levitt
Senior Adviser
Kreab, Brussels
1. Introduction

Background

In 2010, Malcolm Levitt, a long-time euro-watcher who had worked as an EU advisor to Ernst & Young, IBM, and Barclays and in the European Commission, wrote a paper for the CSFI entitled *Getting Brussels right: “Best practice for City firms in handling EU institutions”*. His motivation for writing this was a belief that the UK financial services industry was failing to realise its potential in influencing the EU institutions. This was in the context of a period of unprecedented regulatory and supervisory challenge from the EU, stemming in part from the global financial crisis of 2007/8, but also from what Malcolm identified as a 'battle of philosophies and competition between financial centres'. He argued that - given that the City's success was believed to be predicated on an advantageous regulatory and supervisory system - there was inevitably going to be a confrontation of interests between the UK and the rest of Europe. The crisis of 2007/8 provided the spark for this.

In this context, Malcolm outlined nine 'lessons to be learnt' for City firms, based on 68 interviews and years of experience in Brussels and the financial sector. Whilst most read his conclusions and felt that they fairly captured the main features which characterised the UK approach to Brussels, for some those conclusions were more controversial. Malcolm and the CSFI were surprised to find that many within the industry felt hard done by - or that they believed Malcolm's characterisation of the tension between Brussels and London was unfair. This led to a lively debate in both capitals, and gave both audiences food for thought.

Six years on, the CSFI decided it was time to look again at these conclusions and to use them as a means of shining a spotlight on the UK financial services industry's relationship with Brussels today, in late 2016. A significant amount has changed in the time since Malcolm wrote his paper - including the UK referendum on EU membership, the increased strength of the European Parliament, changes in regulatory mechanisms and the passing into EU law of major pieces of legislation affecting the City.
Aims and objectives

This paper explores how City firms should engage with the EU institutions if they want to have the greatest impact in a post-referendum world. It takes Malcolm's paper as a starting point, but it looks at how the context has altered since the UK referendum, and how this has changed the importance of Malcolm's recommendations. The aim of the paper is partly to help firms think about the direction and nature of their engagement with the European institutions in preparation for a situation where the UK is no longer an EU member state. But it is also designed for those working in Brussels to consider what more they could do to understand where UK firms are coming from, and the limitations they will be working under in a post-referendum (and post-Brexit) world. Maintaining a healthy and constructive two-way communication flow between the UK’s financial services industry and the rest of the EU is to everyone's benefit.

To achieve this, the paper takes Malcolm's recommendations, and highlights those that have grown in importance since 2010. It examines the specifics of the post-referendum world, which may have changed the relative importance of those recommendations, highlighting some of the changes to the context in Brussels and London that we are already witnessing, and which will have a significant impact on the nature of engagement with the EU. It then returns to Malcolm's recommendations and outlines which are more relevant now, in light of the changed context, and what other areas need to be considered given the UK referendum result.

Most of those who were interviewed in 2016 agreed that we can already see clear indications of trends which are changing the context for UK engagement in Brussels - and also suggested that firms need to begin adapting to these straight away, before it is too late.

What this paper deliberately avoids doing is focusing on the content of City firms' interactions with the EU, either in the negotiating period or post-Brexit. Those who contributed to this paper were almost unanimous in saying that, at the time of writing, it is 'too soon to say' what will substantively change for the City in a post-Brexit world, because we do not yet know what will be negotiated between the EU and the UK. And in both Brussels and Westminster there is a broad consensus that the UK's relationship with the EU will not follow any predetermined blueprint, since it has no precedent. Norway, Canada and Switzerland are often mentioned as possible models; but the uniqueness of the UK itself and the UK's history with the EU means that we cannot take any existing arrangement as a starting point.

In addition, much has already been written about the potential negotiating outcomes which could affect the City, with the main emphasis having been placed on whether the UK is able to maintain its right to clearing euro-denominated derivatives and whether the UK retains the so-called “passport” which allows it to access the...
European single market without restrictions. Given that there is a wealth of analysis on the likely impact of such issues for EU and for UK financial services, this paper avoids delving into the 'what ifs' of this debate; rather, it focuses on the fact that City firms need to look afresh at how they handle Brussels in terms of the manner and structure of their engagement, regardless of the outcome of the Brexit negotiations.

When we talk about the nature of City firms' engagement, we are talking more about tone, language and approach than about the hard facts which are going to need to be hammered out in UK-EU negotiations during the coming years. As one non-British long-time euro-watcher commented in 2016: “In terms of lobbying, the UK are some of the best in the world...(However) although they are usually right on the substance, when it comes to playing a political game, they should understand that the substance is often less important than the tone and language.”

We can already detect trends and changes in the context for engagement which will mean that getting this right will become even more important. At a time of high emotions, high political stakes and an uncertain future for Europe and the UK, it may be that the nature of engagement becomes as important as the content of it if we are to maintain a constructive and open two-way communication channel between the City of London and Brussels.

Malcolm's recommendations

For his 2010 paper, Malcolm conducted 68 interviews with firms, officials, MEPs, non-City corporates and consultants, and drew on his career of experience in the City and in Brussels to conclude that City firms need to raise their game to the best practice of their peers and non-City firms.

He argued that they could do this:

• by ensuring earlier engagement, as well as through better quality submissions and representations;
• by upgrading the skill-set devoted to EU issues to embrace public affairs/government relations staff, business experts and those familiar with the authorities in other capitals;
• by developing a formal, CEO-driven process to ensure that businesses respond in a timely and rigorous manner to major regulatory developments, and that their heads are held to account for their performance on significant regulatory issues;
• by improving the persuasiveness of firms' arguments in terms of tone – avoiding self-serving pleading, engaging end-users and other interested parties earlier, and using external economic or other professional consultants;
• by developing relationships with authorities in other capitals;
• by developing alliances with Continental firms on issues of common concern;
• by recognising the benefits of building relationships – not just turning up only when a firm wants something specific;
• by putting more resources into providing data and high-quality input into the UK authorities; and
• by recognising the benefits of being “proactive”.

Malcolm also outlined ‘best practice’ for City firms and ‘lessons to be learnt’ (listed in Annex A), but these broadly correspond with his conclusions as outlined above. So, for the purposes of this paper, we use these as the starting point. The following chapter takes a closer look at how the operating environment in Brussels is changing since the UK referendum and what this means for the context in which City firms are operating. Our findings are based on thirty further interviews with MEPs, consultants, bankers, trade associations and officials, conducted on the basis of anonymity, throughout the Summer of 2016.
2. Post-Referendum: How has the context changed?

Since June 2016, it has become clear that the operating environment for the City in Brussels will be characterised by two phases: - the pre-deal (negotiation) phase; and the post-deal (Brexit) phase.

These two phases call for different ways of working and a certain scale of effort. As one senior banking official put it, "the pre-leave period is vital. Now is the time to put every shoulder to the wheel. We need to maximise our interests in order to set the baseline for negotiations. We need to be all-in, influencing the UK government and Brussels. Working as hard as we can before we get kicked out."

We will come to the question of how this work should be carried out in the following chapters, but first we need to examine how the operating environment will change given the referendum result. We can summarise these changes in three categories:

- A reduction in the number and seniority of Brits in Brussels (traditionally, the City has relied on British MEPs and, to a lesser extent, Brits in the Council and Commission or elsewhere in Brussels, to exert influence on the EU);
- A reduced role for the UK government in European-level discussions (the UK government has been an important lever of influence for City firms wanting to influence or block EU decisions on financial services); and
- Heightened competitiveness, with EU countries looking for any advantages from the post-referendum fall-out.

Whilst it is still too early to draw definitive conclusions on any of these points, it is already possible to detect trends and to make predictions for how the operating environment will be different post-Brexit - and even once Article 50 is invoked.

A reduction in the number and seniority of Brits in Brussels

The UK has never been as heavily represented in Brussels as most of the of the other major EU member states. Indeed, the European Commission’s own figures show that, as of February 2016 (i.e. before the referendum), British nationals constituted just 3.8% of EU staff, compared to 10.2% for France, 17.8% for Belgium (which is understandably over-represented) and 4.8% for Poland. That said, there are plenty of other Brits in Brussels – lawyers, lobbyists, accountants, management consultants – all of whom have more than a passing interest in how the next few years pan out.
Since the UK referendum on June 23, those Brits, whether within the European institutions or observers, have been forced to consider the impact of the referendum result and Brexit on their careers and on their influence in Brussels. A small minority says that little has changed and that it is too early to say if anything will, but the majority agrees that the access and influence that Brits enjoy in Brussels is already diminishing.

For the purpose of this paper, we can divide Brits with influence in Brussels into three broad categories:

- those working in the institutions (Commission and Council officials, MEPs and those supporting MEPs);
- those working in one of the vast array of organisations that are formally independent of the EU institutions and the UK government, but which are trying in one way or another to influence them; and
- those working in the UK Permanent Representation in Brussels.

Brits in the EU institutions

The number, access, and potential status of Brits within the institutions will play a significant part in the negotiations between the EU and UK. Immediately following the referendum, the President of the European Commission, Jean Claude Juncker, the President of the European Parliament, Martin Schulz, and the Secretary-General of the Council, Jeppe Tranholm-Mikkelsen, wrote letters to their staff assuring them that they would support the interests of British nationals during any negotiations. Juncker's letter to Brits in the European Commission was blunt. It said: “You are Union officials. You work for Europe. You left your national 'hats' at the door when you joined this institution and that door is closing on you now.” He promised to “support and help you in this difficult process. Our staff regulations will be read and applied in a European spirit”.

Despite this, most of those interviewed agreed that, over time, the number and seniority of Brits within the EU institutions will diminish, although some pointed out that the influence of Brits had been shrinking in any case over the last fifteen years - with the notable exception of a brief period after Lord Hill's appointment as Commissioner for Financial Stability, Financial Services and Capital Markets Union.

Any further decrease in the number of Brits within the Commission will inevitably have an adverse effect both on the EU and on the City. For the EU, it will mean a loss of expertise which will be felt most keenly in financial services. As one non-British former European Commission official commented, 'the fact that the UK officials will have to leave will be hugely damaging... [on financial services] people often deferred to Brits because they knew Brits had the knowledge.'
For the City, it will mean fewer Brits within the institutions with whom one might exploit national loyalties - something that has been a key feature of the power-play in Brussels since the EU began. For City firms, those loyalties matter most within the European Parliament, where British MEPs are a natural first port-of-call. But to a lesser extent (and despite Juncker’s protestations), national loyalties also play a role in building relationships with fonctionnaires in the Commission. As a former European Commission official commented, “The UK has extremely efficient links between City firms and the British members of the European Commission. Germany is far less efficient at this, whilst French EU officials tell their government everything.” “Efficient” may be a strange way of putting it, but the meaning is clear. Another senior consultant characterised the links between national governments and their officials as follows: “French and Germans are more systematic in their nurturing of their officials. France (under François Hollande) has been less influential in the Commission, but usually France uses its officials well. The Germans are hit and miss, but are currently on a high in terms of influence”. All this points to the importance of having one’s own nationals in influential positions in order for governments (and companies) to maximise their levers of influence.

Lord Hill’s resignation as EU Commissioner the day after the referendum result was perhaps the most tangible and immediate hit to City firms’ ability to influence the European Commission. Lord Hill’s Cabinet had been a natural starting point for any City firm looking to understand or influence Commission decisions. As the Financial Times reported the day after Lord Hill left his post, ‘his departure is the most tangible sign of British political influence in Brussels evaporating after its referendum vote to leave the EU, with power draining away from Brits in the EU institutions and the European Parliament.”

There is anecdotal evidence that triggering Article 50 will accelerate the decline in both the number and influence of British officials within the European institutions that we are already starting to see. And, as noted, this is taking place in the context of an already disproportionately low number of British officials in the European institutions. Within the institutions themselves, rumours abound about the freezing of recruitment of Brits in certain divisions and about informal direction that existing British EU officials should not be allowed to move into more senior or sensitive roles. Many British EU officials who are currently in place worry that if they stay in Brussels, their career prospects will be severely restricted. In any case, there will be no new generation of Brits to replace them as recruitment of British nationals to the European institutions as permanent members of staff will almost certainly cease after Brexit. In the interim, however, seconded national experts continue to be posted to Brussels, and the institutions continue to accept applications from British stagiaires (generally considered the next generation of EU policy experts). However, they do so with no confidence that those they recruit will be able to apply for a permanent job in the EU as long as they only hold British nationality.

2. The Financial Times. 25 June 2016. “UK’s EU commissioner Lord Hill quits as British departures begins’.”
The status and continuing presence of the 73 British MEPs in the European Parliament will be key to City firms' engagement with the EU, since British MEPs are usually the first stop for those in the City trying to influence the Parliament and its myriad Committees. Their future role will form part of the EU-UK negotiations, but it is safe to say that, post-Brexit, the UK will have no MEPs in the Parliament.

The big unknown is whether British MEPs will stand in the European elections that are scheduled for 2019. This is a key date from Brussels's perspective in view of the two-year limit on negotiations after the triggering of Article 50 - which, if done in the first quarter of 2017 (as Prime Minister Theresa May has indicated), would mean negotiations being finalised in the first quarter of 2019. One MEP recently suggested (in a public forum) that, regardless of the timing of any deal, it would be highly unlikely that the UK would hold new European elections in 2019 – though it is possible that those British MEPs still in place could be extended in post to fill the gap between the European elections and the finalisation of an accord.

However, as the recent High Court judgement suggests, things may well change before then. For the time being, the situation of MEPs in the pre-deal phase is unclear, but there is already pressure from some sides for British MEPs to step down completely, to absent themselves from any discussions relating to the future of the EU 27, or to abstain from voting. Some interviewees for the present paper pointed out that, even if the British MEPs were to stay in position, they would almost certainly not be appointed to the more influential posts, notably that of rapporteur (an MEP elected by fellow MEPs when one of the Parliament's Committees is tasked to draft reports on legislative proposals).

All these potential changes to the British presence in the European Parliament come at a time when the Parliament has never had such power. Even compared to when Malcolm was writing in 2010, its influence has grown. The Lisbon Treaty of 2009 designated the so-called “co-decision procedure” as the principal decision-making method for the EU - and extended it to 45 new legislative areas. It also put the European Parliament on an equal footing with the European Council in deciding the direction of the EU and how it spends its money. And it obliged the Council to nominate a candidate to head the European Commission “taking account of the elections to the European Parliament” - which paved the way for the Parliament to insist that only a candidate from its list of “Spitzenkandidaten” or (“top candidates”) should be chosen, thus resulting in the appointment of Jean-Claude Juncker to become President of the Commission in 2014, despite objections from the UK.

Back in 2010, Malcolm had recognised that the City had to do more to make its case within the European Parliament. But, as we will examine in the next chapter, the new context makes this all the more urgent.
Brits outside the institutions

On the second category of Brits in organisations independent of the EU institutions and the UK government (many of whom work for organisations whose job it is to represent City interests), there are also early signs that Brexit, and/or the triggering of Article 50, will reduce their numbers and influence.

Whilst there is little reason to think that Brits working for think-tanks or NGOs will have their career prospects hurt significantly, there is anecdotal evidence that those working in jobs which are directly involved in lobbying are already experiencing problems. One senior consultant confided that, within weeks of the UK referendum result, a major foreign client delegation visiting Brussels had made it clear that its preference was to work with only non-British consultants. Another described how some Brussels-based lobbying firms hiring for new posts over the Summer are now routinely rejecting British CVs because of a perception that Brits can no longer be as effective as their European counterparts in influencing the EU. This view was not shared by all those interviewed, but a significant minority provided specific examples of where clients or hiring managers were hesitating before engaging Brits to represent their interests in Brussels.

Diminishing role of the UK government in European-level discussions

The UK government has always been a crucial lever of influence for City firms in getting their arguments across to the EU. If the UK government's ability to shape the thinking of the rest of the EU diminishes, so too does that of the City.

For the time being, the UK Permanent Representation to the EU in Brussels continues to attend all routine meetings that any other member state attends, and the UK government has made it clear that it remains a full member of the European Union until its official withdrawal. However, as the EU-UK negotiations get underway, it is inevitable that the UK will be frozen out of more and more discussions that it would otherwise have been able to influence. This trend will likely begin in earnest after Article 50 is triggered, but there are already some signs of the UK government's diminishing role in European-level discussions.

On September 19, for instance, the 27 European member states held their first Heads of State meeting without the UK in Bratislava, to discuss the future of the EU post-Brexit. They issued a statement on the back of this meeting which asserted that:
“Bratislava is the beginning of a process.....the Heads of the 27 will meet informally at the beginning of 2017 in Malta. The March 2017 celebrations of the 60th anniversary of the Rome Treaties will bring together Heads in Rome and will be used to round off the process launched in Bratislava, and set out orientations for our common future together.”

This statement, which was superficially similar to normal European Council communiqués, referred to issues on which the UK would usually have considerable influence, including defence, immigration and economic and social development - demonstrating that the UK will no longer be guaranteed a seat at the table when issues are discussed which are fundamental to its interests. More recently the European Council announced that the EU 27 would meet without the UK in the margins of the December European Council to discuss the Brexit process.

Another sign of the UK government's declining influence over EU decision-making was its decision - under pressure from the EU27 – to relinquish the rotating Presidency of the European Council in the second half of 2017. In normal circumstances, the EU Council Presidency is a key source of influence for member states; in this case, the UK will no longer be able to take advantage of it.

Meanwhile, the context has also changed in terms of the UK government's own structure in dealing with Brussels.

The Department for Exiting the EU (DExEU) now sits alongside the Foreign and Commonwealth Office, the Department for Trade, and the Treasury as the primary departments involved in the EU debate.

It is perhaps too soon to say what impact this will have in terms of the UK's influence in Brussels, but it could be significant. For the time being, the staff in UKREP are broadly the same as they were before the referendum - so, in a town where personal relationships are key to influence, they continue to enjoy much the same access and influence as they did before. However, when new staff arrive to replace existing civil servants, and after Article 50 is triggered, they may find it much more difficult to build a trusted network of counterparts in the institutions and among the civil services of other member states at a time when EU-UK negotiations are in full force.

Whilst all those who were interviewed in 2016 were in no doubt of the quality of the individuals in the UK Representation, most suspected that, once Article 50 was invoked, access to the institutions (or to the other Permanent Representations) would become more difficult, exacerbated by inevitable changes in personnel.

The civil service has also been struggling to recruit the number of experts with the right skills required for the task of negotiating Britain’s exit. Most significantly, a lack of trade negotiators - owing to the UK having been forced to rely on the EU for all its trade deals in recent years - is proving a challenging gap to fill.
More immediately, several of those interviewed in 2016 commented on the weakening of links between the City and the UK government since the reshuffle of Ministers which followed the referendum. There was particular concern about the impact that the change of Ministers was having on their ability to influence the UK government, and thus to influence Brussels. One senior British banking expert commented that there is a perception in the City that 'Brexit' Ministers both distrust the City and do not understand it. Others lamented the lack of links between the City and the civil service, with one interviewee from the City stating that 'with the exception of UKREP, there are very few left in the civil service whom we know or trust - particularly in Number 10.” Those interviewed stressed the need for the City to educate the new government in the potential consequences of different Brexit scenarios.

Since these interviews, much progress has been made, and there is now a growing body of analysis from legal firms and large consultancies which attempts to outline in simple terms (for Ministers, as well as the public) the different scenarios for the City and the impact on the UK economy of different negotiation outcomes.

The importance of City firms educating the UK government was highlighted by almost all those interviewed, but there were different interpretations of exactly what the message should be - often along national lines.

For example, one non-British MEP was emphatic that the most important thing City firms could do at present would be to lobby the UK Prime Minister to invoke Article 50 sooner rather than later, in order to avoid prolonging a period of uncertainty which was felt to be detrimental to both the UK and the rest of Europe. In a similar vein, a member of the senior leadership of a non-British bank said that if he had one piece of advice for City firms, it would be to encourage the Prime Minister to provide a clearer signal on her willingness to negotiate and to compromise with the rest of the EU, as this would calm the nerves of those already thinking of investing elsewhere.

In examining how the context for engagement with Brussels has changed, it is worth looking ahead to the post-Brexit world - in which the UK will no longer be represented at European Council discussions. This will bring with it significant changes to the dynamic within the Council that will have a long-term impact on decisions relating to financial services. This was a concern for many of those interviewed in 2016, who generally believed that the absence of the UK from European Council discussions would lead to decisions that would adversely affect the City.

It is broadly accepted that, when it comes to financial services, there are three camps within the European Council. Whilst these are fluid over time, they are broadly characterised as:

- The Anglo-Saxon camp, representing a pro-market and pro-innovation attitude. This camp is traditionally headed by the UK, and is broadly supported by
Scandinavian countries, Ireland, some of the Benelux countries, a handful of Eastern European countries and Malta.

- A more protectionist camp, led by France and supported by the Mediterranean countries (affectionately labelled ‘Club Med’).
- The euro-zone “core” - led by Germany and often supported by Austria, Finland, Slovakia, Croatia, some Eastern European countries and the Netherlands.

In the absence of the UK – given that Sweden is unlikely to take over the UK’s leadership role - those countries instinctively aligned with the pro-market, pro-innovation economics of the UK will find themselves under pressure from the other two camps, which may result in a zero-sum game. For financial services, in which Germany traditionally takes less of an interest than France, the risk for UK firms is that decisions at European Council level will quickly begin favouring the more protectionist, less liberal bloc. The UK government, because it is no longer in the room, will be unable to shape, mitigate or veto any proposals affecting the financial services industry. As one banking official put it: “The Northern liberal bloc is about to have a big shock. The Southern Mediterranean integrationists will get a boost.”

An increasingly competitive and politicised atmosphere

Brussels has always been characterised by competition, both along national lines and between firms from the same sector. But the prospect of Brexit exacerbates this for a number of reasons.

First and foremost, almost immediately after the UK referendum, other member states began trying to woo business from London - hoping to find some economic advantage for their capital city. National leaders, several of whom are facing difficult elections, look to the negotiations with the UK as an opportunity to win business and votes. At the same time, the political message from the majority of member states - fuelled by a fear that Brexit may be contagious - is that the UK must not be seen to ‘gain’. Indeed, even those countries for which Brexit is not an immediate preoccupation are clear that the UK must be seen to be worse off outside the EU than within it, in order to deter others from following the UK’s example.

At the same time, within the UK, the political elite is under pressure to demonstrate to its electors that it is taking their concerns around immigration, globalisation and sovereignty seriously.

The Conservative leadership has a party to unite and a population to appease, and protecting the City's interests has rarely won votes.
For better or worse, this is the context in which City firms will be presenting their ideas to Brussels, Westminster and other national capitals. In the next chapter, we look at ways in which the City could draw on Malcolm’s recommendations from 2010 to help them continue to be effective in this post-referendum context.
3. What does this change in context mean for Malcolm's recommendations?

All of the people interviewed in 2016 agreed that Malcolm's recommendations to City firms written in 2010 still broadly hold true today. But some of his recommendations have already been accepted, or are now considered business-as-usual, whilst others are felt to be even more important now, particularly post-referendum. And a few new recommendations and considerations were highlighted by interviewees that were not emphasised in Malcolm's paper.

2010 conclusions broadly being met in 2016

The quality of UK submissions and representations was raised a number of times by those who were interviewed in 2016, and the overwhelming sentiment was that the City now routinely 'punches above its weight' in the EU. Almost everyone interviewed in 2016 emphasised that British expertise, particularly in the lobbying domain, is second to none, and that the analysis done by British firms is of a very high standard. One non-British interviewee acknowledged that UK lobbyists are now the best in the world, insisting that “their position papers are the most robust and they engage in evidence-based lobbying. This is particularly appreciated given the Better Regulation agenda.” There was also praise for the culture of accountability in the UK, where clear targets and openness to challenge help in the formulation of more robust analysis and policies.

One non-British MEP commented that, in the realm of financial services, “the British already have a great deal of influence in Brussels: when you're the most powerful, you are listened to.” So, whilst Malcolm's recommendations rightly highlighted room for improvement, the starting position for the City and its representatives in Brussels, at least in 2016, is a strong one.

Similarly, on the issue of upgrading the skill-set devoted to EU issues, many of those interviewed in 2016 felt that City firms and the UK civil service (particularly UKREP) are in a better position now than five years ago. One senior consultant commented that there has been an improvement in in-house capacity, that organisations such as the Financial Conduct Authority and the Bank of England have become more open to foreigners, and that British companies are now more inclined to value experience of the EU institutions. This is partly because firms have realised
the importance of EU relations, but also because posts which dealt directly with the EU are no longer considered a career back-water in the way they may have been five to ten years ago. In terms of government, this is even more true post-referendum, at a time when the civil service is creating hundreds of new jobs - all of which require a detailed understanding of the EU. This skill-set will become prized in a way that it was not when Malcolm was writing back in 2010.

Almost without exception, those interviewed in 2016 agreed on the importance of a CEO-driven process to coordinate UK financial firms' engagement with the institutions. Some argued that this is already being done, and that it has probably improved since 2010. But others believed that UK firms continue to lag behind their main competitors. For smaller firms from smaller financial capitals, such as the Scandinavian countries, CEO engagement tends to be more regular, and that has paid dividends. In contrast, expectations in Brussels about the engagement of larger UK firms is often higher - whereas the actual level of CEO engagement does not always match expectations, and continues to lag behind Continental competitors.

Most of those interviewed in 2016 mentioned the value of CEO engagement in terms of influencing Brussels. But they also mentioned the benefits it creates within the firms themselves. By ensuring that those responsible for engagement with Brussels sit centrally within a firm, directly or indirectly reporting to the CEO, those who deal with the EU institutions on a regular basis can more easily access the resources and expertise they need from other parts of the business.

The importance of this has really come to light in those firms in which 'European affairs' are still the responsibility of compliance teams (which sets the wrong tone, by portraying Brussels only as the creator of regulation which has to either be complied with or not) or in 'government relations' departments. In contrast, when EU engagement sits centrally within an organisation, it is easier to reach consensus quickly and to deliver consistent messaging - and, as Malcolm pointed out, that has allowed those working on EU affairs to secure the whole-hearted engagement of the business. Sitting centrally also allows those people working on European issues to have better exposure within the business. This is something that can be important in terms of career progression and attracting talent to the area.

A word of warning on this point, however. Whilst a certain number of CEO visits to Brussels (and national capitals) each year is considered valuable, one consultant specifically warned against allowing this to become a 'box-ticking exercise', in which those tasked with EU engagement organise a certain number of senior visits with a certain number of officials each year - without the flexibility to respond to Brussels's erratic timing or to build a deeper relationship with European counterparts. This links with Malcolm's observation in 2010, that City firms need to focus more on 'effectiveness and proactivity', rather than on meetings for the sake of meetings. The vast majority of City firms interviewed in 2010 admitted that they were more “reactive” than “proactive” in dealing with the EU: “The focus generally appears to be on the number of meetings held with officials or MEPs, and on the papers...
submitted'. Malcolm wrote of the need to evaluate effectiveness of engagement, something which is difficult but not impossible to do.

This is even more important when it comes to CEO engagement, with interviewees in 2016 noting that such involvement needs to be proactive, and not simply a reaction to problems as they arise. In that way, relationships can be built from the bottom up, and are not simply used to resolve problems once they have arisen.

2010 conclusions needing greater emphasis in 2016

Malcolm was particularly concerned about the timeliness of UK firms' engagement with the EU institutions, noting that officials and MEPs repeatedly stressed the importance of engaging in the debate during the drafting and legislative stages of policy development.

The timing of engagement continues to be considered an area needing further improvement. The main issue brought up by interviewees in 2016 was the need to engage with the institutions even when one's immediate interests are not at stake. As one senior lobbyist put it, 'UK firms often expect a return overnight, but they need to think medium to long term and know that engagement will pay off one day'.

Of course, this takes resources both in terms of man hours and infrastructure, but as one consultant said “sometimes smaller companies are better at lobbying even though they have less money, because they are more engaged and the ramifications of EU policies are closer to (their) business.” The Swedes were cited as being particularly strong in this regard, and at providing a consistent message over time.

This links with another theme which came up repeatedly during interviews in 2016: the need for City firms to engage with the EU in a spirit of compromise. Given the changes in context outlined in Chapter Two, this point takes on even greater importance.

One former MEP was particularly emphatic on the need for British firms to approach Brussels in a spirit of compromise, offering this advice:

“When outlining your priorities, don't make them binary. Articulate your second and third - best positions, impart enough knowledge that these come into play. Firms can be reluctant to do this, and consequently can lose completely.”

The issue of banking bonuses was given as an example of where, in the eyes of those working in the EU institutions, UK firms could have achieved a better result if they
Compromise, coherence, consistency and dialogue

had been willing to compromise. Similarly, when making points to MEPs and those in the Commission, it is important to understand the counter-arguments being put forward by others. The same former MEP pointed out that “You need to understand the position of non-like-minded firms. Compromises come from understanding the other point of view.”

This spirit of compromise links closely with the overriding sentiment that City firms need to build alliances both across industries and across national boundaries.

Almost all those interviewed in 2016 agree that this is even more important in a post-referendum world, where differences between firms from the same sector can be exploited. Whilst most agreed that City firms had generally done well in building alliances across the industry since 2010, several interviewees warned that this progress could well be threatened. In particular, there is a risk of fracturing the lobbying effort as different financial institutions and trade associations try to find ways to stay relevant - and therefore to distinguish themselves from others. One experienced banking official said that a lack of clarity from the UK government after the referendum risks creating in-fighting between firms as everyone “goes for the lifeboat’ rather than thinking 'big picture” - which is what is required in a period of crisis. “Everyone is reassessing their allies. All are talking about consensus, but everyone is aware of the possibility of 'first mover advantage'. The danger is that the City loses the benefits of cooperation which it has already accrued.”

All of this is occurring at a time when regulatory cohesion and consistency are extremely important - as highlighted by a senior banking expert: “Coherence of international regulation will be so much more difficult now - previously it was just the US and EU that we had to worry about, now the UK as well. Regardless of how it works out, it's vital that there are advocates of cohesion to remind people of the basic principles which the UK stands for.”

In the light of this, almost all those interviewed in 2016 commented on the renewed importance of trade associations and the role of the City Corporation and of City UK in helping the industry to share ideas and find commonalities.

Alliances across national boundaries are also increasingly important in a post-referendum world, where arguments which benefit only British interests carry even less weight than before.

Several of those interviewed pointed to the importance of “dialogues” between the City of London and its equivalents in other member states, which are designed to promote commonality. Similarly, one trade association official, stressing the need for City firms to be active members of European trade and investment associations, said there is a risk that, because UK firms are often more effective at lobbying or can move more quickly, they are sometimes tempted to 'go it alone'. Whilst this may seem beneficial in the short term, in the long term (and particularly in a post-Brexit world), this will be counter-productive since UK firms needed to bring partners with them.
As well as involvement with trade associations, an overwhelming number of respondents pointed to the importance of City firms actually being present in Brussels - reacting to events as they unfold, seizing opportunities and building a network.

This was described well by one MEP: “Be present. This is the only way to find common cause with others in the industry. Post-Brexit this will be even more important, as it will allow you to get wind even earlier of consultations.” Many of those interviewed in 2016 commented that other nationalities often did this better than UK firms - with the Irish and the Swiss being considerably more pro-active than the UK, despite their relatively small size. That said, most agreed that 'being present' could mean different things, whether it meant having a strong public affairs department (something large banks and the London Stock Exchange are doing very well) or using consultants who are on the ground all the time and whom you can trust to get your points across. A word of caution for any firm relying too heavily on government came from a former MEP, who insisted that “you cannot rely on government because the government can drop your issue, even if they agree with it, if other priorities come up.”

This is crucial in a post-referendum world, where the UK government has competing objectives, many of them political, and cannot afford to spend too much time on any one issue.

A key concern for Malcolm back in 2010 was the need for City firms to improve the persuasiveness of firms' arguments in terms of tone - with particular emphasis on avoiding self-serving pleading. Of all Malcolm's 2010 recommendations, this drew by far the most attention when re-examined in 2016. And it is the one which merits the closest examination in the context of the UK referendum and a potential Brexit.

The issue of 'British arrogance', which was touched upon by Malcolm back in 2010, came up time and time again in 2016 - not as an accusation, but rather as an acceptance by both the buyer and seller that there is a risk that Brits engaging with MEPs and other EU officials may come across as arrogant. One non-British interviewee commented that although this 'arrogance' is largely perception rather than reality, perceptions matter a great deal when trying to get one's point across. As he put it, they can lead to “asymmetry of engagement”. Three areas were highlighted as contributing to this perception:

- Language: Many British representatives from the City engaging with Brussels either do not realise or tend to forget that they are dealing with people for whom English is their second (or third) language. Advice from another non-British interviewee is clear: “Anglo-Saxons should think about slowing down, using simple language and understanding that their interlocutor is not a native speaker.” Also on the language issue is a tendency for Brits (often those based in London) to refer to 'the Europeans' as though this does not include the UK. This can give an impression of Brits deliberately distancing themselves from the European project, both within City firms themselves and when engaging their Brussels interlocutors.
• Substance: There was little doubt amongst those interviewed that the UK, as the leader in financial services in Europe, produces experts with excellent technical knowledge and expertise. Whilst this is, of course, an advantage in many ways, it also brings a risk that British interlocutors fail to fully explain, in non-technical terms, their points to an audience which often does not have the same expertise as they do. Another interviewee went further by insisting that Brits “know what they're doing and therefore don't feel the need to accommodate other views. Although they are usually right on the substance, when it comes to playing a political game, they should understand that the substance is often less important than the tone and language.”

• Difference in legal systems: This was highlighted as possibly contributing to the perception of arrogance amongst Brits in Brussels. Given that the application of UK law is to the letter, Brits spend much more time than their Continental counterparts on finding the perfect wording - which can come across as arrogant especially if, as often happens, it involves law firms (which means conversations often get technical pretty quickly).

The potential for City firms to be perceived as arrogant has significantly increased in the post-referendum world. Back in 2010, Malcolm pointed out that the City's mantra that “we are global, not simply European” was taken by many MEPs and Commission officials to reveal an unacceptable degree of dismissiveness in London towards EU ambitions and concerns. In view of the UK referendum, during which so much of the political rhetoric focussed on the UK as a 'global trading nation', this risk was greatly exacerbated - and the potentially adverse reaction to the City's emphasis on its global position is, therefore, much greater.

Whether London is (or continues to be) a global capital or not, the importance of City firms respecting both the European project and the power of the EU is even greater now, and it calls for a degree of humbleness. One trade association official pointed out that “the UK has to realise that, in some domains, it is no longer the major player. For example in consumer credit, personal finance and leasing they are small players. The likes of BNP, SocGen and Santander have much more influence. So if the UK comes in preaching on these issues, then they're not really seen as credible, and they risk being laughed at.”

UK firms' propensity to engage in self-serving pleading was named by many of those interviewed as one of the areas in which a different approach is necessary.

Inevitably, it is the job of any company representative or lobbyist to explain their specific interests to their Brussels interlocutors – and, generally, British arguments and analysis are sound. However, the tendency for these arguments to come across as self-serving came up time and time again. A senior member of a London hedge fund, for instance, gave this advice to City firms: “Do not be arrogant. Try to understand the public policy imperatives to which the Commission is trying to respond. That way you avoid giving the impression of “special pleading.”
This need to avoid special pleading will be even greater as Brexit approaches, since arguments that are based on advantages which might accrue to the British economy will be significantly weakened. Almost all interviewees stressed the need for City firms to shift away from an emphasis on maintaining the competitiveness of the City towards an emphasis on the “real” economy - and on the mutual advantages which will accrue to both the UK and the EU.

Some suggested that the perception of special pleading by City firms is exacerbated by the constant stream of scandals involving the financial services industry and by the tendency of some Brussels officials to use London (and big banks in particular) as “a scapegoat for all sorts of vices”. Several interviewees argued that British firms need to demonstrate an 'alignment of interests' when they go to see Brussels officials - something that is, arguably, made more difficult as a result of London's bonus culture. As one non-British interviewee argued, whilst firms can say that a certain piece of legislation will hurt their institution (and therefore the economy), if their interlocutor knows that they are incentivised by bonuses, then this reduces the potential impact of the argument. Whilst, in the UK, government officials are more likely to understand the value of corporate revenue and taxes, in Brussels non-British interlocutors may not take the time to make the link between big banks, big bonuses and corporate revenues. This makes the need to demonstrate an 'alignment of interests' all the more important.

Back in 2010, Malcolm concluded that “Most City firms appear not to engage governments or financial authorities in other capitals on EU policy and legislative developments.”

Interviewees in 2016 generally accepted that some improvement had been made in terms of engaging on the regulatory side - for example, with ESMA in Paris, and with the ECB and SSM in Frankfurt and, to an extent, with national capitals (particularly the Tresor in France). But all accepted that much more needs to be done in this regard, and that engaging other national capitals will become all the more important since City firms have to convince other players who will have a seat at the European table when the UK government does not. As one banking official commented, City firms 'Need to read the direction of travel and work with those liberal countries who would usually be on our side'. Another senior consultant commented that firms need “clear recognition that France and Germany will be the drivers now and will be cutting deals behind the scenes.....These countries respond to different priorities beyond competitiveness of the City, and they need much more real economy and domestic reasons to move.”
4. Conclusion - What to do about it?

Much has changed for the EU, the UK and the City of London since Malcolm Levitt wrote his report on City firms’ engagement with the EU in 2010 - the UK referendum result and the increased role of the European Parliament being the most important.

In order to prepare this paper, we began talking to people before the UK referendum. Even at that stage, it was possible to discern those of Malcolm's recommendations which had been more or less internalised by the City, and those on which the City still had some way to go. However, the referendum result and the prospect of Brexit have obviously changed everything. The “operating environment” for City firms in Brussels will be even more difficult over the next couple of years (and beyond) than we had envisaged when we set out on our task. That said, it is also very clear that Malcolm’s recommendations are even more relevant – and their adoption more urgent – than before the referendum.

In Chapter Two, we outlined how the environment for City firms engaging with the EU had changed in terms of the number (and seniority) of Brits working in Brussels, the diminishing influence of the UK government and the heightened competitiveness between national capitals, firms and politicians. Given how the context is changing, it is remarkable that Malcolm managed to capture so many of the principal issues which can form the basis of an engagement strategy today – though some merit more focus and others need re-prioritisation in view of the changes that have occurred.

Having taken Malcolm's conclusions as a base, we put forward some recommendations for firms to be thinking about as they engage Brussels in the pre and post-Brexit phases of the negotiations:

1. Be present in Brussels: The likes of the BBA, UKREP, and City firms' representations in Brussels must grow and must grow quickly, before the playing field changes completely. Whether the aim is to gather intelligence or to protect one's interests, these things are best done on the ground. This will provide the flexibility to be pro-active, and to build deeper relationships which are not just based on solving ad hoc problems as they arise.

2. Use the pre-Brexit period to maximum effect: “Now is the time to put every shoulder to the wheel.” It is important to protect and nurture the levers of influence that the City still has. In particular, the City and government must support British MEPs to maintain their positions for as long as possible, must encourage UKREP officials to stay in place, must build networks with non-Brits in Brussels and elsewhere which can survive Brexit, and must build financial expertise amongst EU staff while the UK is still a member state.
3. **Educate, educate, educate:** City firms must focus on educating their new UK Ministers, so that the government enters negotiations with its eyes wide open. The City must also actively share expertise with the burgeoning Civil Service involved in EU negotiations. Of course, how effective this is will depend in large part on how open UK Ministers and the Civil Service are to the City. They have every reason to want to listen and learn, but the arguments need to be presented in a measured and objective fashion, based on fact and linked to the impact on the real economy. The City must also use its expertise to educate non-British MEPs and Commission officials, not just on areas of immediate concern, but on the financial services sector more generally. They should stay engaged with the Capital Markets Union initiative, and show willing to contribute to the debate despite Lord Hill's absence.

4. **Be humble and bring the audience with you:** When you are the biggest fish in the pond and have special technical expertise and resources, there is a danger that you will be perceived as arrogant. In a post-referendum or (post-Brexit) world, remaining EU members will have less patience with this - and less obligation to put up with it. Whilst most in Brussels recognise that UK expertise will still be needed (perhaps more than ever) post-Brexit, they will not accept it at any cost, and it will be incumbent upon City firms to explain why they should still have a role. Anyone engaging with Brussels needs to be careful that characterisations of the City as 'global' do not appear to undermine the European project.

5. **Take Brussels and the “European project” seriously:** Whether they are pro or anti EU, understanding and respecting what the 27 other member states are trying to achieve and the challenges they face will make City firms more effective in getting their points across. As one former European Commission official said: “The City must be the body that shows itself to be firmly in favour of the EU succeeding. There needs to be a fundamental change in attitude along these lines, not a competition between the two.” This may be harder to do from the outside when one's country has made a democratic choice to leave, but it is all the more important that the City should be intelligently supportive.

6. **Engage with the other EU 27 - build alliances:** The City will need to call on its North European, economically liberal friends to represent its pro-market, pro-innovation interests in Brussels - and will need to do so with a concerted effort that has not hitherto been seen. The Swedes and the Danes will be key to protecting many of the interests the City holds so dear when the UK is not in the room. Investing in those relationships for the long-term will require considerable time and effort. It may involve a bigger representation; it will certainly entail a permanent presence or regular visits to capital cities and better utilisation of subsidiaries in other European capitals.
7. **Recruit the necessary people and value EU expertise:** A surprising number of those interviewed in 2016 suggested that City firms would not only need more people to handle the EU, but may need to recruit more nationals from the remaining EU member states to help them maintain their influence in Brussels and to build relations with other national capitals. That also means that those existing employees with special knowledge of the EU institutions and networks in Brussels should be nurtured and encouraged to share that expertise with others.

At a time when many in the City feel they face crisis after crisis, the recommendations above may seem like an unwelcome distraction from the business of damage limitation and/or of maximising opportunities, in which City firms are currently engaged. It is natural that most energy should be focussed on prioritising arguments to be presented to the UK government and the EU; but it may pay dividends in the longer run to take a moment to focus on how those arguments can best be presented - and on how the context in which they will be heard has changed.
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