CITY OF LONDON

THE GLOBAL CITY

London and the UK's global offer to business: Enabling regulatory & legal environment

Enabling regulatory & legal environment

With an effective government, a competitive and simple tax system, and low barriers to international trade, Singapore is the financial centre with the most enabling regulatory and legal environment. Of the major economies, the UK's regulatory framework is leading. It sets international standards, is at the forefront of innovation, and offers the lowest corporation tax rate of all G20 economies.

However, facing global challenges, the UK's government needs to return to being perceived as more predictable, stable, and strategic. This will reinforce businesses' confidence that the UK is a market worth investing in.

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Metrics

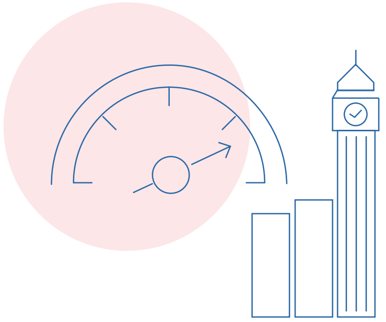
1. Government effectiveness
2. Regulatory quality
3. Control of corruption
4. Regulatory coherence
5. English common law (yes/no)
6. Financial centre = political centre (yes/no)
7. Regulatory sandbox (yes/no)
8. Open banking (yes/no)
9. Perception of favourability of financial services regulatory regime
10. Total tax and contribution rate
11. Individual income tax rate
12. Tax complexity
13. Size of international tax treaty network
14. Additional financial services taxes (yes/no)
15. Services trade restrictiveness
16. Cost of regulatory barriers to financial and professional services trade
17. Controls of the movement of capital and people
18. Number of fintech bridges and regulatory cooperation agreements

Regulatory stability and innovation

Financial services executives world-wide perceive the UK as having the most favourable regulatory regime for financial services. The UK's regulatory environment is at the forefront of innovation and provides the financial and professional services sector with an environment in which they can access regulatory expertise and effectively test their products and services. The UK's financial centre is in close proximity to its political centre, and English Law is the world's business law. However, facing global challenges, the UK's government needs to return to being perceived as more predictable, stable, and strategic to reinforce businesses' confidence that the UK is a market worth investing in.

Facing global challenges, the UK's government needs to return to being perceived as predictable, stable, and strategic. Only then will businesses have renewed confidence that the UK is a market worth investing in.[1]

Of all comparator global financial centres, the UK's government is rated the least effective. When asked about perceptions of the quality of public services, policy formulation and implementation, and the credibility of a government's commitment to such policies, executives rate the UK at 1.4 on a scale of -2.5 to 2.5. This is down from 1.7 five years ago. Singapore is in the lead with a rating of 2.2. The ability of the UK's government to formulate and implement sound policies and regulations to promote private sector development is better perceived than its overall effectiveness: Experts give the UK's regulatory quality a score of 1.6. This is better than scores of the US and Japan, but behind Germany, Hong Kong, and Singapores. In the last two years these ratings show more fluctuation. Recent events may also have an impact on government effectiveness and regulatory quality perception, with the US' handling of the COVID-19 pandemic being criticised, the UK's EU trade negotiations strategy questioned, and Hong Kong's future openness thrown into doubt. Whilst the fact that the UK's financial centre is in close proximity to its political centre facilitates direct communication channels between industry and government stakeholders, the UK's government needs to return to being perceived as predictable and strategic. Only then will businesses have renewed confidence in the UK and perceive it as a location to invest in.

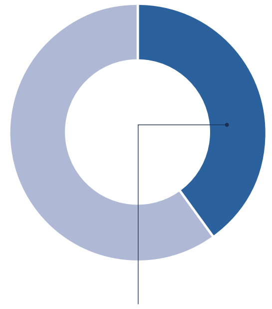


1.4

Executives rate the UK at 1.4 on a scale of -2.5 to 2.5 for its quality of public services, policy formulation and implementation, and the credibility of a government's commitment to such policies

Businesses located in the UK benefit from the best legal advice in the home of the world's business law.[2]

English common law is the preferred governing law for business transactions world-wide, and firms located in the UK are where the world's business law is home. It is well-known, well-developed, and predictable. 40% of all corporate arbitrations globally use English common law. The law is commonly used even for contracts that do not have any geographical connection to the UK, demonstrating its high reputation. All other financial centres use amended English law, mixed legal systems, or civil law.



40%

40% of all corporate arbitrations globally use English common law

Central Square, Leeds

The UK's regulatory environment is at the forefront of innovation and provides businesses with an environment in which they can access regulatory expertise and effectively test their products and services.[3]

Innovation in financial and professional services in the UK benefits from a supportive regulatory environment. The UK is the first global financial centre that pioneered both a regulatory sandbox and open banking. In the World Trade Report 2019, the World Trade Organization highlights the UK Financial Conduct Authority's regulatory sandbox as a prime example for both facilitating an effective regulator-innovator dialogue and cooperation between different markets. In 2020, the Financial Conduct Authority and the City of London Corporation began piloting an additional 'digital sandbox' to support innovative firms tackling challenges caused by the COVID-19 pandemic. Such regulatory cooperation reduces costs and provides an environment in which innovation can be effectively tested. There is further opportunity for the UK to extend 'open banking' into 'open finance', extending open banking principles to cover a wider range of financial services.

The **UK is the first global financial centre** that pioneered both a regulatory sandbox and open banking

Sources

[1] World Bank 2019.
[2] Own analysis.
[3] Own analysis.

The UK, Singapore, and Germany are most aligned with the Basel III recommendations on strengthening bank capital requirements, providing businesses with a reliable operating environment.[4]

The Basel Committee on Banking Supervision provides a forum for regulatory cooperation on banking supervisory matters, aiming to provide guidelines and standards to enhance the quality of banking supervision world-wide. The committee's Third Basel Accord, set out in response to the 2008 Global Financial Crisis, is designed to strengthen bank capital requirements. Whilst the framework is voluntary, adoption by markets provides banks with clear regulatory frameworks. In particular multinational banks benefit from reduced regulatory compliance costs if they find comparable regulatory standards in the markets they operate in. Of all global financial centres, the UK, Singapore, and Germany have made the most progress in recent years to align their regulatory frameworks for banks with Basel III recommendations. The UK and Germany have made particular progress between 2018 and 2019 in the areas of capital, leverage, liquidity, and disclosure. This regulatory alignment and coherence increase a market's attractiveness. As of now, the US is the least aligned market. Whilst the UK has followed European Union legislation in the past, this changes after the UK's EU exit. Further clarity needs to be provided to the sector on divergence from or coherence with European Union legislation and regulation.

The UK, Singapore, and Germany have made the most progress in recent years to align their regulatory frameworks for banks with Basel III recommendations

The UK is perceived to have the most favourable regulatory regime for financial services.[5]

The perception of a financial centre's regulatory strength plays an important role: The stronger international stakeholders perceive a centre's regulatory framework, the more likely they are to retain or increase investment there. In 2020, a majority of financial services executives – 30% – stated that the UK would have the most favourable regulatory regime for financial services. At 26%, the US made second place, followed by Singapore with 18%.

30%

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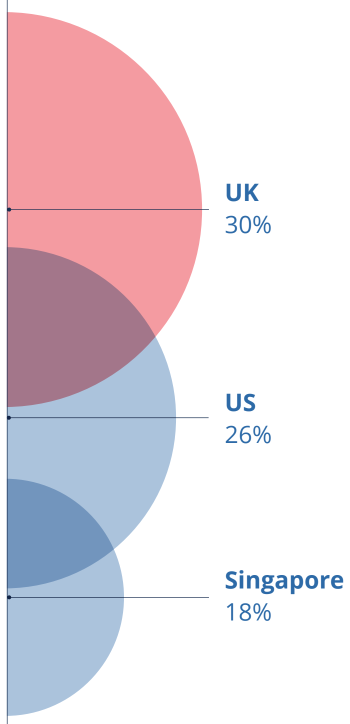



The Royal Exchange, London

"London's position as fintech capital of the world has been hugely beneficial to Global Processing Services' growth journey, owing to its standing as an attractive fintech investment hub, its pool of exceptional tech talent enabling operational excellence, and a forward-thinking regulator. This combination of factors uniquely positions London as a prime incubator of tech and financial services cross-pollination, which is further illustrated by the 174 authorised e-money institutions in the UK – more than any other jurisdiction in the EEA and most of whom are based in London. With the support of the Department for International Trade and the Singaporean Economic Development Board's Fintech Bridge, we were able to effectively navigate the regulatory complexities involved in expanding internationally and bring the UK & European fintech revolution to APAC, launching our Singaporean and Sydney offices last year, and powering some of the biggest fintech players in the region including WeLab Bank, Razer Fintech and Revolut. As the tectonic plates of influence shift from West to East, there is a massive opportunity for UK fintechs to cement the UK's place as a global fintech powerhouse, whilst extending their reach into the APAC region to capture the immense potential of the market.

Joanne Dewar
Chief Executive Officer,
Global Processing Services (GPS).

Sources

[4] Bank for International Settlements 2020.
[5] Duff & Phelps 2020.

Tax

Singapore and Hong Kong are the two global financial centres with the most competitive tax systems, but their economies are based on different fundamentals than the UK, US, Japan, and Germany. Of these major economies, the UK has the most competitive tax framework. With the lowest corporation tax rate of all G20 economies, a simplified tax system, and a large international tax treaty network, the UK is a broadly more attractive destination for financial and professional services firms than the US, Germany, and Japan. However, because of the UK's bank levy and corporation tax surcharge, corporate and investment banks located in London pay higher total tax rates than their counterparts in New York City or Frankfurt.

Whilst Singapore and Hong Kong have lower corporation and individual income tax rates, the UK has the most competitive tax rates of all major economies that are a global financial centre. Any tax policy changes in response to COVID-19 need to ensure that the UK's tax framework retains its competitive position.[6]

For both business and individual income tax and contribution rates, the UK is the most competitive major economy of all global financial centres. Singapore and Hong Kong have more competitive rates, but their economies are based on different fundamentals than the UK, US, Japan, and Germany. Research shows that the total tax and contribution rate of firms in the UK lies at 30.6% of a business' commercial profits, followed by the US (36.6%), Japan (46.7%), and Germany (48.8%). With 2018's tax cuts, the US have made the most progress in increasing the competitiveness of their tax system in recent years. However, at 19% the UK's corporation tax rate is still the lowest and most competitive rate of the G20 economies. Individual income tax rates show a similar picture: Singapore and Hong Kong have the lowest overall marginal tax rates, but of the major economies, the UK is the most competitive market with a highest marginal tax rate of 45%. At 55.95% – including local inhabitant tax – Japan's highest marginal tax rate for individual incomes is the highest. Foreign direct investment into the financial services sector is particularly responsive to a market's tax system. Tax rates and frameworks affect the choice amongst alternative locations when setting up new foreign financial services entities. Any tax policy changes proposed by the UK government in response to the economic fallout caused by COVID-19 need to ensure that the UK's tax framework remains competitive in the future to ensure lasting prosperity, growth, and job creation.

The UK is the most competitive major economy for both business and individual income tax and contribution rates

The UK has the least complex tax framework of all major economies that are a global financial centre.[7]

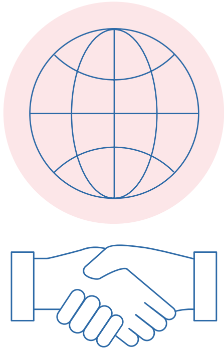
When assessing the time to comply with a market's tax framework in hours and the number of taxes paid per financial year as a proxy for a market's tax complexity, the UK again is the most competitive financial centre of the major economies. Whilst Hong Kong's tax system is the least complex, followed by Singapore's, the UK's is much simpler than those of the US, Germany, and Japan. On average, businesses in the UK spend between 105 and 114 hours preparing and paying taxes, and make 9 payments. Businesses in the US spend 175 hours on complying with the country's tax framework and pay 11 taxes per year. In contrast, entities in Hong Kong spend just 34.5 hours on preparing and paying taxes, and pay 3 taxes. This assessment does not account for additional taxes that apply to the financial services sector, e.g. bank levy or corporation tax surcharges.

Of all comparator global financial centres, the UK has the largest international tax treaty network.[8]

International double tax treaties help to avoid the double taxation of profits from foreign sourced income. Businesses located in markets that have signed tax agreements with many other countries have an advantage over firms in locations with a more limited treaty network. Individuals working in multiple locations benefit from these treaties as well. With 132 double taxation agreements with other markets at the end of 2019, the UK has by far the largest international tax treaty network – and the number consistently grew over the past 5 years. The market with the next-largest tax treaty network is Germany with 96. At just 42 tax treaties, Hong Kong's network is the smallest.

Due to bank levies and corporation tax surcharges, the UK does not provide banks with such a competitive tax environment.[9]

The UK and Germany are the only comparator markets in which additional taxes apply to the financial services sector, affecting banks in particular. Both markets introduced bank levies after the 2008 Global Financial Crisis to discourage banks from relying on risky forms of borrowing and provide a further source of tax revenue. In addition, the UK introduced a further 8% corporation tax surcharge for banks in 2015. Whilst the UK has a generally competitive tax system, banks do not benefit from it: A typical corporate and investment bank in London has a total tax rate of 47.1% – 13.6 percentage points higher than in New York City and 2.4 percentage points higher than in Frankfurt.



132

The UK has by far the largest international tax treaty network, with 132 double taxation agreements with other markets

Sources

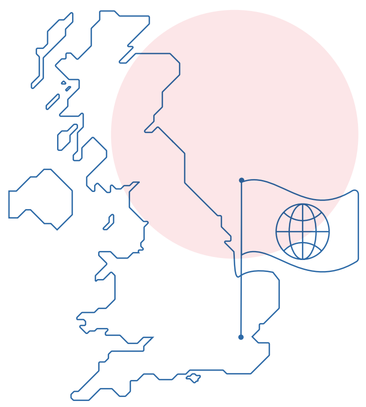
[6] PwC/World Bank 2020, KPMG 2020, Merz/Overesch/Warmser 2017.
[7] PwC/World Bank 2020.
[8] Own analysis.
[9] UK Finance 2019.

Market access

Financial services firms located in Singapore and Hong Kong have the best access to international markets. Singapore in particular stands out and achieves a top score for regulatory coherence, number of fintech bridges and regulatory agreements, and few controls of the movement of capital and people. The UK is more open than Germany, Japan, and the US. Of these major economies, the UK's regulatory framework is most aligned with international standards. Low restrictions on services trade mean policy-induced trade costs for financial services firms located in the UK are lower than in most other markets. However, depending on the future path the UK will choose after the EU exit, this competitive advantage could be at risk.

The UK has less controls of the movement of capital and people than the US and Germany, which makes it a more open global financial centre and supports businesses to trade internationally.[10]

Financial and professional services firms depend on low regulatory barriers to trade internationally. In the annual Economic Freedom of the World report, the UK demonstrates a good performance for controls of the movement of capital and people. Based on an assessment of the country's restrictions on foreign ownership and investment, capital controls, and the freedom of foreigners to visit for short-term business purposes, the UK is much more open than the US and Germany. However, it is less open than Japan, Singapore, and Hong Kong; with the latter two being the most open jurisdictions.



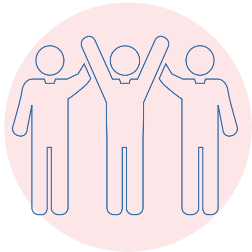
The UK is a more open global financial centre than the US and Germany and supports businesses to trade internationally

There is potential for the UK to establish more fintech bridges and agreements on regulatory cooperation with international partners to help UK-based businesses access other markets.[11]

More regulatory cooperation facilitates better market access for businesses located in cooperating markets. In 2016, the UK and Singapore established the world's first fintech bridge. This type of regulatory cooperation is designed to coordinate regulatory issues in the areas of technology and innovation and enable each market's fintechs to access the other market. Between 2016 and 2019, Singapore grew its number of fintech bridges and regulatory cooperation agreements to 28. This is a higher number than Hong Kong, the UK, Japan, and the US' combined. With 7 agreements, the UK is the financial centre with the third-most fintech bridges and regulatory cooperation agreements. Germany is the only centre that has not yet established dedicated fintech regulatory cooperation agreements with other markets. These numbers serve as a proxy: Cooperation agreements are particularly beneficial when they support businesses to access other markets through e.g. fast-tracked licensing.

Sources

[10] Fraser Institute 2020.
[11] Own analysis.



The UK has **7** fintech bridges and regulatory cooperation agreements, making it third in the financial world

Right: Paternoster Square, London

Lower services trade restrictions mean lower costs businesses need to bear

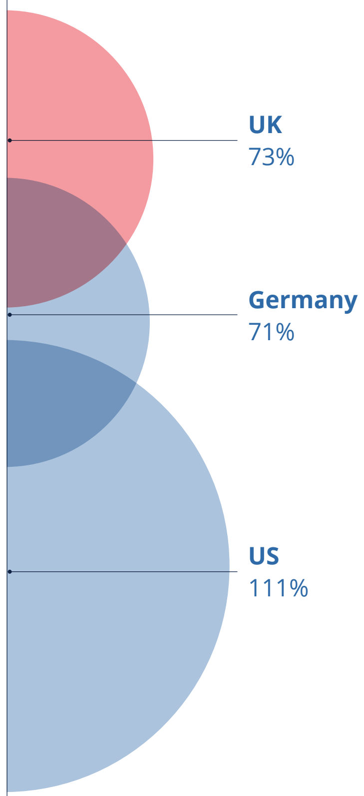
Lower services trade restrictions mean lower costs businesses need to bear. The UK is one of the best global financial centres to conduct international services trade from, but could lose this competitive advantage after the EU exit.[12]

Based on an OECD assessment of restrictions on foreign entry, restrictions to movement of people, other discriminatory measures, barriers to competition, and regulatory transparency, the UK is one of the best global financial centres to conduct international services trade from – second only to Germany. Both centres are more open than the US and Japan. Despite global trade tensions, this assessment has only slightly changed in recent years. Financial and professional services firms benefit from low restrictions in services trade as they reduce compliance costs. According to further OECD analysis, financial and professional services firms located in Germany and the UK need to bear lower policy-induced services trade costs than their counterparts in Japan and the US. In the UK, average policy-induced services trade costs are 73% of the total value of financial, business, and insurance services. This share is slightly lower in Germany, at 71%; but it is much higher in the US, where the share is 111%. Across all markets, policy-induced services trade costs are highest for financial services, followed by insurance and business services trade. The costs for services trade within the European Economic Area are much lower: 7% on average for businesses located in the UK that trade with other European Economic Area parties. This is a competitive advantage the UK could lose after the EU exit.

Source

[12] OECD 2019, 2020.

In the UK, average policy-induced services trade costs are **73% of the total value of financial, business, and insurance services**. This is a competitive advantage the UK could lose after Brexit



Right: MediaCityUK, Salford Quays, Manchester

About the Global City campaign:

The Global City campaign is The City of London Corporation's overarching initiative to promote the UK as a world-leading international financial centre. It showcases the UK as a great place for financial and professional services firms to invest, locate and grow.

theglobalcity.uk

About the City of London Corporation:

The City of London Corporation is the governing body of the Square Mile dedicated to a vibrant and thriving City, supporting a diverse and sustainable London within a globally successful UK.

We aim to:

- Contribute to a flourishing society
- Support a thriving economy
- Shape outstanding environments

By strengthening the connections, capacity and character of the City, London and the UK for the benefit of people who live, work and visit here.

www.cityoflondon.gov.uk

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