FORUM

EDITED BY TOM WELSH

Why Brexit won't take away London's fintech crown

THE VOTE for Brexit may not have led to the economic meltdown we were told to fear, but it certainly gave rise to a feeling of disbelief, as the political models and expert commentators many had put their faith in were proven to be way off the mark.

Bankers and fintech entrepreneurs alike looked on with horror on the morning of the result, and all were concerned about the future of passporting, investment and access to talent. These critical issues haven't gone away. But nearly two months after the event, the outlook is brighter and some entrepreneurs are starting to see some brass in the muck.

First, we must confront the brutal facts. Tech startups will likely see a drop in investment in the short term. We will also most likely see a squeeze on immigration and the possible loss of passporting, which will make it a lot more difficult to access European markets.

But the resulting instability will not lead to an exodus of talent from the sector. Entrepreneurs are attracted to the fintech sector because of its informality, freedom and sense of possibility. If they were interested in security, they would be working in finance for a guaranteed salary and a prestigious job. So the uncertainty of Brexit will not turn away these mavericks, and the loss of London banking jobs may even attract a few more bright young minds to fintech, just like in 2008 when the financial crash led to the sector's creation.

The EU comfort zone is gone. Stripping this away will mean the loss of easy exporting and undoubtedly the loss of a few startups. But it will also force London's fintech firms to adopt a new mindset, becoming global in their outlook from inception. At a time when the world's growth is concentrated in emerging markets on the other side of the world, this could be just the shake-up that the sector needs.

We enjoy the world's best regulatory framework in the UK, and the FCA's expertise in working with the sector is what led to the creation of passporting in the first place. In the medium term, Britain may well continue with a similar relationship with the EU than at present. This will allow fintech companies to continue to service European markets while being left in no doubt that they need to go global and look at new markets as a priority.

Many, for example, may start to examine the opportunity that exists for the "next billion" internet users, concentrated in developing markets. These consumers are different from those in Europe and the West, as they will operate exclusively on mobile devices and many will never own a bank account. A fintech sector that is reliant on Europe will not see the opportunities that exist in these markets, whether it is offering microfinance for small businesses or university funding for gifted students.

Political instability is at its highest level in our lifetimes. But for every investor buying up tinned food for their bunker, there is another using it as a litmus test for which startups are willing to explore new opportunities as they present themselves.

Cameron Stevens

> **The EU comfort zone is gone – but at a time when the world's growth is concentrated in emerging markets on the other side of the world, this could be just the shake-up the sector needs**

Customer bases dwarfing those of the European Union are opening up across the globe. These are harder to reach, but offer more potential in the long run.

London is the global capital of fintech, and the jewel in the crown of UK technology. This has as much to do with the city's culture and history as it does with its universities and investors. The things that make London great did not disappear when the country voted to leave the European Union. The easier export opportunities for London fintechs will probably go, but no companies ever became great by the availing of easy opportunities.

None of this will be easy, and things are not bound to improve as a result of Brexit. Making a success of this new environment will require an enormous effort from a group of highly intelligent and single-minded entrepreneurs. It will require those with safe options to take risks. And we will need to lobby hard to ensure that the shortfall in talent from the EU is made up elsewhere. This means championing the sector internationally through trade missions and recruiting from emerging markets that would benefit the most from our fintech products.

But entrepreneurs love a challenge and anything is possible. After all, in less than a decade, London has created the world's top fintech hub from scratch, becoming a true urban rival to Silicon Valley.

Cameron Stevens is chief executive of Prodigy Finance.

DEBATE

Q: Will government plans to fine firms who give advice on aggressive tax avoidance backfire?

Mark Davies

YES

HMRC's proposals will fail because they don't address the fundamental issues. First, consider motive. Nobody likes to pay tax and it is lawful to arrange our affairs to pay the least amount of tax. Second, there is an opportunity to avoid tax because our tax system is mind-blowingly complicated. Tax avoidance relies on mistakes and gaps in the law, tax reliefs and that different taxes have different tax rates. Simplifying our tax law would do far more to lessen the opportunity to avoid tax and lessen the motive to avoid if the tax payable appears to be fair and reasonable. The ability to penalise anybody who benefits from a tax scheme, from the designer, to anyone who markets it or assists with the implementation, is disproportionate and sloppy law-making when it is the existing tax law at fault. Unacceptable tax avoidance is difficult to define and often determined after years of litigation. Law makers should do more to simplify the tax code, and introduce a system of pre-clearance which would prevent uncertainty.

Mark Davies is managing director of Mark Davies & Associates.

Tessa Lorimer

NO

Tax avoidance schemes will continue to proliferate until the government holds culpable accountants, lawyers and other intermediaries to account. It is not right that taxpayers (many of whom were not sophisticated investors and ought never to have been targeted by their advisers) should be penalised for their roles, when the people who structure and sell these schemes, and receive sizeable commissions for doing so, get away scot-free. As with everything, the devil is in the detail and a cross-agency approach will be essential. The Financial Services and Markets Act 2000 should have prevented the general marketing and mis-selling of these schemes, but through a lack of proper enforcement, has never acted as a strong deterrent. These proposed penalties could be substantial in many cases and, along with naming and shaming those involved, would serve as a powerful disincentive to professionals and intermediaries who otherwise may be tempted to design, promote and facilitate avoidance schemes.

Tessa Lorimer is special counsel in Withers' tax investigations team.

"Brexit means Brexit" means something very different to what many people think

WHAT does "Brexit means Brexit" mean? When Theresa May uttered these words, she almost certainly didn't know what they will actually mean in practice, and she probably still doesn't.

The conventional wisdom says there are four potential ways forward for the UK. First, stay in the Single Market by remaining in the European Economic Area (EEA). This is the Norwegian model. Second, sign a free trade agreement of some form. This is the Swiss model. Third, agree another form of bilateral deal, such as a customs union agreement. This is the Turkish model. Lastly, we have the WTO model whereby we would trade under World Trade Organisation rules.

When you scratch each option, however, the conventional wisdom is revealed to be too simplistic. The eventual reality will almost certainly be some form of hybrid model. Let's examine why.

The EEA option is probably the most favoured in Whitehall and Westminster. From an economic perspective, it is the closest option to existing EU membership. It provides continued tariff and non-tariff barrier free trade with the EU, and covers goods and services, as now.

The problem with the EEA option is mainly political. The price of access to the Single Market would almost certainly be free movement of people. It is hard to imagine the rest of the EU allowing free movement of goods, services and capital, without the fourth freedom, people. But continuing with free movement of people would almost certainly be a bridge too far, politically, in the UK.

The political stumbling blocks with the EEA don't stop there. The other price of access to the Single Market would be a budgetary contribution of some form also. Throw in the problem of regulation without representation, and the UK having to abide by Single Market rules it had no say in (and which might be worse in the future), and the political hurdles to EEA membership appear too high. Moreover, even if the UK were to seek the EEA option, there is no guarantee it could achieve it. Because EEA membership requires EU or European Free Trade Association (EFTA) membership, there is the possibility of a veto by an EFTA country.

Graeme Leach

The free trade agreement option is less attractive in terms of access, given that it is likely to only cover goods, with minimal coverage of services. The experience of the Swiss also shows that even limited access to the Single Market requires the free movement of people. Switzerland doesn't have an EU agreement for financial services either. Throw in issues of complexity and timing (the Swiss have 120 bilateral agreements established over many decades), and the free trade agreement model has its own set of challenges.

The customs union model, illustrated by Turkey, is just another form of bilateral agreement. But remaining in the customs union would mean trade policy was still outsourced to the EU and that UK prices would remain higher than world prices, because of the European Union's Common External Tariff (CET). Both the Swiss and Turkish models were agreed by the EU because of an expectation these countries were on a transition into the EU. Reverse the direction, and it is not at all clear that the EU would accept such agreements for countries leaving – the carrot would be replaced by the stick.

So we're thrown back towards the WTO model, but in my view with a twist. The twist is that we wouldn't revert to tariffs on goods imported into the UK. Instead the UK would trade tariff free with the world – unilateral free trade. We'll examine the how and why next week.

Graeme Leach is chief executive and chief economist of macronomics, a macroeconomic, geopolitical and future megatrends research consultancy.