

Agenda Supplement – External Affairs and Additional Legislation Committee

Meeting Venue:

For further information contact:

Video conference via Zoom

Alun Davidson

Meeting date: 10 December 2020

Committee Clerk

Meeting time: 14.00

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– Supplement

Please note the documents below are in addition to those published in the main Agenda and Reports pack for this Meeting

5.2 Paper to note 2: Correspondence from Lord True, Minister of State at the Cabinet Office to the Chair regarding the UK Internal Market Bill – 9 December 2020

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Attached Documents:

Correspondence from Lord True, Minister of State at the Cabinet Office to the Chair regarding the UK Internal Market Bill – 9 December 2020





Agenda Item 5.2

Lord True CBE
Minister of State
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David Rees MS
Chair, External Affairs and Additional
Legislation Committee
Welsh Senedd
Cardiff
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Our reference: MC2020/18378

9 December 2020

Dear David,

Thank you for your time on 12 November. I sincerely apologise for the difficulties at our end that led to the late start to proceedings.

During the session, I committed to writing on a number of issues, which I will address in turn. I will also address the additional points you raised in subsequent letters.

Engagement with Welsh Government during the development of UKIM

UK Government officials worked closely with their counterparts in the Welsh Government and the Northern Ireland Civil Service in the years ultimately leading up to the publication of the White Paper that preceded the UKIM Bill. Those discussions considered the benefits and limitations presented by a range of options that could potentially address the issue of future divergence within the UK's internal market and ran parallel to, and within, the forums discussing the Common Frameworks.

Much of the specific discussion on the internal market was given to working closely together to understand the potential impact of divergence and the ways that existing policymaking tools might or might not be adequate to manage that risk. Proposals considered between officials ranged from wholly non-legislative options to statutory approaches similar to the core of the Bill that is now before the House.

At no point were these discussions considered to be binding, nor to be leading definitively to any specific approach. Welsh Government officials were clear in their view that their Ministers would be unlikely to welcome many legislative models.

Since the introduction of the UKIM Bill UK Government Ministers and officials have held a number of discussions to present their respective positions on the provisions as drafted, and subsequently to engage in more detail on amendments proposed by the Welsh Government and tabled by Baroness Finlay.

Difference in scope of regime between UK and EU (i.e. why is the scope different in Parts 1-3 of the Bill)

The questions at the session focused on the difference between the lists of exemptions that feature in the UK Internal Market Bill and those that are present in the EU's single market arrangements. However, I would appreciate this opportunity to set out a more detailed picture of the differences between the two systems and the reasons behind these.

It is worth highlighting up front that while the design of our principles has been informed by our experience as a member of the EU, we have also drawn inspiration from a number of other internal market systems from around the world.

For example, as set out in Clause 2 of the Bill, in order to qualify for mutual recognition a good must first meet the relevant regulatory requirements that apply in the part of the UK it was produced in or imported into. This is drawn from the Australian mutual recognition principle and ensures that the devolved administrations (and the UK Government, acting for England) can continue to apply their own requirements to goods produced or imported into their own territories. This contrasts with the EU's system, whereby goods qualify for mutual recognition if they have been lawfully placed on the market in another EU Member State. If that system applied in the UK, it would permit goods produced or imported into Wales to be sold in Wales even if they complied with the regulatory requirements of another part of the UK (e.g. England); the goods would simply need to have been 'placed on the market' in England and would then qualify for mutual recognition. This would give businesses a largely free hand in choosing which regulatory requirements to comply with and would prevent the devolved administrations (and the UK Government, acting for England) regulating their own producers and importers.

This is just one example but illustrates the wider point that in designing a system that is suited to the UK context we have looked to a number of examples rather than simply copying from the EU's particular experience.

This difference, and the others set out below, are consequences of the different contexts and starting points of the UK and the EU internal markets. The EU's internal market system was designed in the context of gradually integrating a large number of countries with diverse histories, cultures and competing market priorities. In the UK we have a distinct history of devolution and an already highly integrated market, which we are looking to preserve rather than integrate further. This starting point has informed every aspect of our system, including the types of regulation within scope, the exemptions and the institutional arrangements supporting the principles.

For example, we will not be replicating the role of the Commission in challenging the adoption and implementation of new regulatory requirements for goods by the devolved administrations, provided they are acting within their areas of devolved competence. In the UKIM system, we have made clear that there will be no such unelected body, as the Office for the Internal Market will have a purely advisory role.

There are a number of other key points of contrast between our system and the EU's which I have set out below, starting with Part 1 of the Bill.

Part 1

1. Narrower scope of UKIM system and clear distinction between principles

The two market access principles apply to clearly defined sets of regulatory requirements on goods which are tightly focused on sale. Broadly speaking, mutual recognition applies to requirements in scope of the list in clause 3(3) which *prohibit sale if not complied with*, and non-discrimination applies to requirements in scope of the list in clause 6(3) which *apply to or in relation to goods sold* in the territory in question. Requirements will clearly be captured by the mutual recognition principle or the non-discrimination principle, or by neither (this will depend on whether they meet the clearly defined criteria) and this removes any uncertainty as to how the principles interact.

- For example, as Ministers have identified, reasonable legislation relating to the pricing of certain goods (such as minimum unit alcohol pricing) will clearly be within scope of the non-discrimination principle rather than the mutual recognition principle. Other legislation, such as that affecting how a consumer is permitted to use a good, or how a good is otherwise dealt with *after* its been sold (e.g. how it is recycled) will generally be out of scope of the principles all together.

This contrasts with the scope of the EU's system which, through Article 34 of the TFEU, introduces a significantly vaguer and more wide-ranging principle relating to the free movement of goods. Through case law the principle has been found to apply to "*all trading rules enacted by Member States which are capable of hindering, directly or indirectly, actually or potentially, intra-Community trade*¹"; and in recent years has been found to capture measures which simply *hinder access* to the market of a Member State, even if the measures do not disadvantage imports in any way (e.g. use restrictions).

Whether a requirement is caught by Article 34, and how the EU principle of mutual recognition interacts with the wider principle relating to the free movement of goods and non-discrimination, is therefore more complicated and less certain under the EU system.

2. Process for implementing new regulatory requirements for goods

The UKIM system does not introduce an equivalent to the EU's pre-notification and standstill requirements for technical regulations. This notification period in the EU, which can be extended if there is a dispute or if the EU is planning to legislate in the same field, can introduce significant delays in the implementation of new legislation. Member States may also find themselves unable to implement new legislation at all, if Member States or the Commission (or ultimately the CJEU) find that the legislation is contrary to the free movement of goods principle.

Under the UKIM system, there is an expectation that, in Common Framework areas, if one part of the UK wishes to diverge from a foundation approach, a discussion will take place between the devolved administration(s) and the UK Government to identify whether a common approach can be achieved that meets the desired outcomes. However, there is no notification or justification process which would prevent a DA from enacting legislation in their areas of competence. Indeed, the market access principles do not prevent UKG or the DAs from adopting and implementing divergent rules for goods; they simply create limits on the extent that they can enforce new requirements against traders from other parts of the UK. The market access principles will therefore ensure that any divergence does not damage the ability of UK companies to trade with every part of the UK.

¹ *Procureur du Roi v Dassonville (Case 8/74)* Pack Page 3

This design reflects our view that a decentralised system is more appropriate for the UK and is more respectful of the devolution settlements.

3. Areas where a single set of rules apply

The approaches to mutual recognition in the EU and UK share a key similarity in that they have limited application where a single set of rules applies. In the EU system the mutual recognition principle does not affect “harmonised matters” for goods and services. In the UK, similarly, issues where “whole-of-UK” approaches exist (e.g. through reserved matters or through a consistent approach agreed through a Common Framework), will not in practice be affected by mutual recognition.

4. Clear focus in the UK system on commercial markets

The UKIM system clearly provides that supplies of goods by public bodies will only be in scope if they are supplied for purely commercial purposes. It achieves this through the definition of sale. The position is less clear at an EU level.

5. Exemptions from Mutual Recognition

It is true that the EU system has more exemptions than the UK system, however this again reflects our different circumstances and starting points. In the UK we have a shared commitment to high regulatory standards and effective mechanisms for regulatory co-operation for example through Common Frameworks. This reduces the need for exemptions in contrast to the EU, which includes 27 nations with far more diverse approaches to regulation.

Furthermore, the EU’s own experience shows that exemption mechanisms can undercut the effectiveness of mutual recognition in practice. The Government’s view is that new barriers to trade should be limited where possible, and other means of fulfilling policy aims sought, and our approach to exemptions reflects this.

We have however excluded certain specific areas of regulation where mutual recognition would not be appropriate. The limited exclusions allow, for example, specific environmental issues to be taken into account when authorising a chemical for use in a part of the UK. In addition, the Secretary of State has a power to amend this list of exclusions in the future to ensure that it remains up to date and responsive to changes in technology and unforeseen challenges in the operation of the principle.

Finally, as I pointed out above, our mutual recognition principle has a narrower scope than comparable EU provisions. For example, the EU mutual recognition system captures certain ‘life-cycle’ requirements which can significantly influence the composition or nature of goods (e.g. requirements relating to use, recycling or disposal), whereas the UK’s mutual recognition principle generally only captures requirements which actually prohibit sale if not complied with.

6. Exemptions from Non-discrimination

As has been pointed out, our list of legitimate aims for discrimination are narrower than the comparable EU lists. The broad rationale for this is the same as set out above for mutual recognition, however there are some additional points for non-discrimination specifically.

Crucially, the tests for discrimination in the UKIM system are significantly more difficult to meet than in the EU system, meaning that rules are less likely to be caught by the UK's non-discrimination principle in the first place. In particular, the test for direct discrimination requires a rule to *actually* place incoming goods at a disadvantage compared to local goods, and the test for indirect discrimination requires a rule to *actually* place incoming goods at a disadvantage in a way that causes a significant adverse effect on competition. This contrasts with the EU approach, where rules will be caught by Article 34 simply if they have the *potential* to hinder inter-state trade. This higher bar means that fewer exemptions are needed.

Furthermore, while our list of legitimate aims for justifying indirect discrimination is narrower than the EU's list, we are not applying the EU's stringent proportionality test, but our bespoke test of whether a measure can 'reasonably be considered necessary' to fulfill a particular aim.

Part 2

Part 2 of the Bill applies the Bill's market access principles of mutual recognition and non-discrimination by drawing on similar principles to the Provision of Service Regulations 2009, which transposed the EU Services Directive in the UK. The Mutual Recognition Principle in the Bill is very similar in effect to a mutual recognition principle in Regulation 15(5)-(5E) of the 2009 Regulations. The new intra-UK Non-Discrimination Principle replaces EU non-discrimination principles in the 2009 Regulations that are to be revoked at the end of the Transition Period.

Under the mutual recognition principle in the 2009 Regulations, a part of the UK could justify not applying the mutual recognition principle on the basis of an overriding reason relating to the public interest in Regulation 15(5D). This exemption, derived from the EU law, has been considered many times by the CJEU and covers a broad and continually expanding range of policy reasons. To provide the necessary clarity for UK businesses and minimize burden on the UK courts, the UK Government's approach is that instead of an expansive exemptions regime, we have a clearly defined list of exclusions on the face of the Bill, with a power to amend that list of exclusions to adapt to changing requirements of the UK Internal Market.

In turn the exclusions from Part 2 of the Bill, which are found in Schedule 2, are substantially similar to matters out of scope of the 2009 Regulations as a result of regulations 2 and 5 of the 2009 Regulations. Additionally, we have looked to matters listed in Regulation 25 of the 2009 Regulations (derogations from the freedom to provide services for providers from another EEA State) as the starting point for areas excluded from scope of the new intra-UK non-discrimination principles.

The Government is committed to keeping the list of exclusions under close review. If, following further examination, it was clear that further exclusions for Part 2 are necessary, or matters excluded should be brought within scope of the principles in the future, then there is the possibility to make a change to the exclusions in Schedule 2 via regulations using the power in the Bill for the Secretary of State to amend the Schedule.

Part 3

Part 3 does not operate an exclusions schedule in the same way as Parts 1 and 2. This is in recognition that professional qualifications operate differently to goods and services. Instead of an exclusions schedule, if the relevant authority considers that automatic recognition is not appropriate for that profession - because of a difference in policy environment or specific regulatory needs in that part of the UK - it is possible for them to disapply this by putting in place

an alternative recognition process which complies with the principles set out in clause 24 of the Bill.

Only if the applicant demonstrates they meet the required standards for that profession in that part of the UK, does the relevant authority have to allow access to the profession. This means that all parts will still have control on who can access the profession in their jurisdiction based on their professional standards.

In sum: there are differences between the UK and EU's approach – of course, but an assessment should not be done on a simplistic basis. The market access principles as developed in the core of the Bill have been designed for the UK's specific situation, devolution arrangements and legal approach, with clear parameters and concepts, and will only curtail new rules to the extent that they create unnecessary barriers to trade.

Government amendments concerning the relationship between the Bill and devolution

During constructive and detailed debate in the House of Lords, and considerable engagement with the Welsh Government, the Government listened carefully and subsequently proposed amendments to the Bill in the following areas:

Firstly, building upon the constructive amendments put forward by the Welsh Government (and later tabled by Baroness Finlay), the Government offered concessions that enhance the existing provisions to explicitly ensure the UK internal market works in the interest of all administrations on an equal basis. This is delivered primarily through enhancing the accountability structures of the Office of the Internal Market (OIM) in Part 4:

An amendment to Clause 29, Part 4 clauses included explicit references that the OIM operates in the interests of all four nations of the UK on an equal basis, as is already set out in its functions.

Introducing a time-bound consent requirement to ensure that the SoS must seek to obtain DA consent in respect of the chair and panel of the OIM within a period of one month, after which SoS can proceed unilaterally. If this were to happen, the amendment would also require the Government to outline its reasons for proceeding without your consent or the consent of the other DAs. This in turn ensures that there is an enhanced role for the DAs in the OIM. This government amendment reflects amendments 28 and 29 as put forward by the Welsh Government in their list of proposed amendments to help strengthen the Bill.

Including a review after 5 years by the Secretary of State into whether the CMA remains the most appropriate body to carry out the functions described in Part 4. This would include the DAs as statutory consultees.

Introducing a non-legislative commitment to hold Ministerial meetings, on an annual basis, to discuss matters relating to the UK internal market.

Secondly, a further proposed amendment involved an addition to Clause 29, Part 4 to ensure that the OIM functions for the benefit of consumers across the UK.

Thirdly, we have added an extra clause imposing a duty to consult the DAs in advance of publication of the response to the forthcoming domestic regime consultation.

And finally a series of amendments – both legislative and non-legislative – were proposed to improve accountability and transparency in the Bill in relation to the power to provide financial assistance and the delegated powers.

On the power to provide financial assistance, the Government brought forward an amendment at Report to introduce a legislative requirement for Government departments to report annually to Parliament following use of the power. This adds a requirement in legislation to provide a summary on use of the power for scrutiny by Parliamentarians and the wider public and will ensure that key partners, such as those in Welsh Government, can see where the money has been spent. We hope this will further support our commitment to work collaboratively with all our partners.

On DA involvement and engagement in UKIM machinery, in order to strengthen the role the DAs play in the shaping of the UKIM system, we proposed to add in a statutory consultation requirement for UKG to consult with the DAs before using delegated powers (within Parts 1 to 3 of the Bill) - for example, to amend the list of legitimate aims for indirect discrimination and the Schedule of exclusions. Going further, we introduced a one-month consent period for DAs before using the power to amend the list of relevant requirements for non-discrimination, amend the list of legitimate aims, amend the list of exclusions, or to issue, revise, or withdraw statutory guidance.

We also proposed adding a duty on the Secretary of State to review the exercise of the delegated powers in Parts 1 and 2, covering both goods and services.

The Government's intention with these amendments was to help strengthen the Bill and ensure that devolved administration interests are taken into consideration.

Applicability of OIM Non-Compliance Fines to the Senedd Commission

The Government has acknowledged concerns that devolved legislatures may be in scope of the penalties the CMA can levy in the event of non-compliance with an information notice. I wish to note first of all that the information-gathering powers in question mirror section 174D of the Enterprise Act 2002, ensuring consistency across the CMA's functions. I also wish to stress that the Government is committed to not taking any steps to bring financial penalties into effect by regulation until there is clear and credible evidence that there is a need to do so to enable the CMA to fulfil its internal market functions.

As you note, the CMA will not be able to levy a penalty against the UK Government or the devolved administrations. It is correct that the devolved legislatures themselves are not excluded from the same provision and this is because it is improbable that they would hold relevant economic information with regard to detrimental effects on the internal market. In practice therefore the CMA is highly unlikely to impose a fine on the Senedd or any of the devolved legislatures.

More broadly, the anticipation of the Government and the CMA is that the vast majority of the information-gathering necessary will be conducted on a voluntary basis and that the imposition of fines will only be used as a last resort.

UK Shared Prosperity Fund

On Wednesday 25 November the Government announced further details on the UK Shared Prosperity Fund as part of the Spending Review. This fund will help to level up and create opportunities for people and places across the UK, and will at least match current EU receipts -

on average reaching around £1.5 billion a year. The Government will set out further details of the UKSPF in a UK-wide investment framework published in the spring.

The Government believes this Bill is vitally important for our businesses and citizens as we leave the Transition Period, and I hope the explanation I have set out in this letter therefore is helpful to deepen understanding of our approach and is reassuring for you and your colleagues in the Senedd.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'True', with a long horizontal stroke above the first letter.

Lord True CBE