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European Scrutiny Committee

Fourth Report of Session 2017–19

Documents considered by the Committee on 6 December 2017

Report, together with formal minutes

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Notes

Numbering of documents

Three separate numbering systems are used in this Report for European Union documents:

Numbers in brackets are the Committee's own reference numbers.

Numbers in the form "5467/05" are Council of Ministers reference numbers. This system is also used by UK Government Departments, by the House of Commons Vote Office and for proceedings in the House.

Numbers preceded by the letters COM or SEC or JOIN are Commission reference numbers.

Where only a Committee number is given, this usually indicates that no official text is available and the Government has submitted an "unnumbered Explanatory Memorandum" discussing what is likely to be included in the document or covering an unofficial text.

Abbreviations used in the headnotes and footnotes

AFSJ	Area of Freedom Security and Justice
CFSP	Common Foreign and Security Policy
CSDP	Common Security and Defence Policy
ECA	European Court of Auditors
ECB	European Central Bank
EEAS	European External Action Service
EM	Explanatory Memorandum (submitted by the Government to the Committee)*
EP	European Parliament
EU	European Union
JHA	Justice and Home Affairs
OJ	Official Journal of the European Communities
QMV	Qualified majority voting
SEM	Supplementary Explanatory Memorandum
TEU	Treaty on European Union
TFEU	Treaty on the Functioning of the European Union

Euros

Where figures in euros have been converted to pounds sterling, this is normally at the market rate for the last working day of the previous month.

Further information

Documents recommended by the Committee for debate, together with the times of forthcoming debates (where known), are listed in the European Union Documents list, which is published in the House of Commons Vote Bundle each Monday, and is also available on the parliamentary website. Documents awaiting consideration by the Committee are listed in "Remaining Business": www.parliament.uk/escom. The website also contains the Committee's Reports.

*Explanatory Memoranda (EMs) and letters issued by the Ministers can be downloaded from the Cabinet Office website: http://europeanmemoranda.cabinetoffice.gov.uk/.

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Meeting Summary

The Committee looks at the significance of EU proposals and decides whether to clear the document from scrutiny or withhold clearance and ask questions of the Government. The Committee also has the power to recommend documents for debate.

Brexit-related issues

The Committee is now looking at documents in the light of the UK decision to withdraw from the EU. Issues are explored in greater detail in report chapters and, where appropriate, in the summaries below. The Committee notes that in the current week the following issues and questions have arisen in documents or in correspondence with Ministers:

Law enforcement cooperation—EU/Canada Agreement on Passenger Name Record Data

- Whether the Government rules out any "grandfathering" of existing EU PNR agreements with third countries during a transitional period, so that these would continue to apply while the UK negotiates new bilateral agreements to take effect at the end of a transitional/implementation period.
- Whether the Government considers that the absence of a grandfathering arrangement would create risk and uncertainty for carriers and how it intends to mitigate this risk.
- Whether the Government accepts that the scope for the UK to diverge from the EU template for PNR agreements with third countries will be extremely limited and that, the greater the degree of divergence, the higher the risk that the UK will be unable to conclude its own PNR agreement with the EU.

Citizens' rights—The European Citizens' Initiative

- Whether the Government expects to use its correcting powers under clause 7 of the EU (Withdrawal) Bill to make clear that UK nationals would no longer be entitled to take part in European Citizens' Initiatives (ECIs) once the UK leaves the EU.
- How Brexit will affect the involvement of UK nationals in ECIs (either as organisers or as signatories) which were initiated before Brexit day.
- Whether the Government intends to seek transitional arrangements to ensure that their participation would count towards meeting the requirements for registering an ECI and securing sufficient statements of support for formal examination by the Commission.

Single EU VAT Area

- The implications of the UK leaving the common VAT area as part of Brexit, which means that VAT will need to be collected at the border to avoid the risk of large-scale tax evasion. It is unclear how the ambition for "free and frictionless trade", and the absence of any physical infrastructure at the Irish border in particular, are compatible with leaving the EU's VAT system.

EU-Norway VAT Agreement

- The EU and Norway have negotiated a new agreement on tackling cross-border VAT evasion and fraud. The new Agreement, which is the first of its kind negotiated by the EU, could form a template for future UK-EU relations in this area. The Committee has therefore asked the Treasury some further questions about its position.

Emissions Trading System

- The impact on UK operators of proposed changes to the EU's Emissions Trading System, from 1 January 2018, in order to protect its integrity in the event of an abrupt UK exit.

Anti-microbial resistance

- The implications of divergence from the EU's veterinary medicines regulatory framework, including measures to tackle anti-microbial resistance.

Digital Single Market: ENISA/the EU Cybersecurity Agency

- The range of means by which third countries currently participate in, or cooperate with, ENISA, including through the NIS Directive and its supporting institutional arrangements.

Vehicle type approvals

- Precedents for vehicle certification authorities outside the EU and EEA being able to issue European type approvals which are recognised within the EU.

Summary

EU/Canada Agreement on Passenger Name Record Data

The Government informs the Committee that the Justice and Home Affairs Council on 7/8 December is expected to agree a proposed Council Decision authorising the Commission to negotiate changes to a draft PNR Agreement with Canada which would bring it into line with a recent Court of Justice Opinion. The Government says it is "minded to opt into the Council Decision" and to support its adoption, even though the three-month period available to the UK to decide whether to opt in has not yet expired. The Committee asks the Government to justify its early opt-in decision and requests further information on the implications of the UK's exit from the EU for its ability to share PNR data with third countries.

Not cleared from scrutiny; scrutiny waiver granted; further information requested; drawn to the attention of the Home Affairs Committee and the Committee on Exiting the European Union.

EU participation in Council of Europe Convention and Additional Protocol on the Prevention of Terrorism

The Commission has proposed two Council Decisions authorising the EU to conclude (ratify) a Council of Europe Convention and Additional Protocol on the Prevention of Terrorism. Decisions authorising the EU to sign these instruments were adopted in 2015. The UK did not opt in and the Government indicates that it is "not minded" to opt into these proposals "at this stage". The Committee asks the Government to clarify its position on the Court of Justice exercising jurisdiction over national security matters; explain whether it considers that the Convention and Additional Protocol concern areas of exclusive or shared competence (the distinction matters because it determines whether the Member States are free to act individually or only the EU can act) and how this should be reflected in the proposed Decisions; provide some indication of the views of other Member States; clear up any ambiguity about the possibility of the UK opting in post-adoption; and indicate how soon the Government expects the UK to ratify the Convention and Additional Protocol.

Not cleared from scrutiny; further information requested; drawn to the attention of the Home Affairs Committee.

The European Citizens' Initiative

The European Citizens' Initiative (ECI) was introduced by the Lisbon Treaty and is intended to give EU citizens a direct say in shaping the laws that govern them. The Commission considers that there is scope to clarify and simplify the existing rules to make ECIs more accessible for EU citizens and less burdensome for their organisers. Most of the changes proposed are designed to streamline the ECI process. They would also give young people aged 16 and above the right to support an ECI (currently they have to be of voting age). The Government raises no concerns about the substance of the changes proposed but alludes to "timing and implementation" issues connected with the UK's exit negotiations. The Committee requests further information. It also asks whether it is the Government's position that UK nationals will cease to be EU citizens on Brexit day and what implications this will have for their participation in ECIs initiated before the UK leaves the EU.

Not cleared from scrutiny; further information requested; drawn to the attention of the Committee on Exiting the European Union.

Single EU VAT Area

The European Commission has proposed to end the EU's "transitional" system for collecting VAT on cross-border sales of goods between Member States, under which businesses who buy goods from another EU country effectively have to charge themselves VAT. The Commission has proposed to establish a "definitive VAT system", under which cross-border sales would be treated the same as domestic sales, with VAT to be collected in the Member State of the buyer but accounted for by the supplier. However, the Commission proposal only legislates for the intent to establish such a system, leaving the detail to be fleshed out in further draft legislation in 2018.

The Committee has serious concerns about the complexity of the reforms proposed by the Commission, as well as the various derogations from the new "definitive system" to reduce the administrative burden on suppliers. In addition, the Minister has not addressed the significant consequences of the UK's exit from the common EU VAT area, as it means UK businesses will no longer benefit from supplying or receiving goods from EU countries without VAT being collected at the border. It is unclear how the Government's ambition for "free and frictionless trade" with the EU after Brexit, and the absence of any physical infrastructure at the Irish border in particular, are compatible with leaving the EU's VAT system. The Committee has asked the Minister to address its concerns that, in the absence of physical VAT controls, the UK Treasury could lose significant amounts of tax revenue due to the VAT evasion on imports from the EU.

Not cleared from scrutiny; further information requested; drawn to the attention of the Business, Energy & Industrial Strategy Committee, the Northern Irish Affairs Committee and the Treasury Committee.

EU-Norway VAT Agreement

The European Commission has negotiated an agreement on addressing cross-border VAT fraud with Norway, which is awaiting ratification by EU Finance Ministers. The Committee considered the new Agreement politically important, as it could constitute a template for UK-EU cooperation in this area after Brexit. Although the Government described administrative cooperation as "one of the most effective tools for fighting cross-border VAT fraud", it has refused to indicate whether this EU-Norway Agreement could set a useful template when the UK leaves the common VAT area.

Cleared from scrutiny.

Coordination of social security systems

The Committee again considered a proposal to amend the Social Security Regulation, which governs the way in which EU citizens access the social security system of their host Member State if they exercise their freedom of movement rights. It granted a scrutiny waiver to enable the Employment Minister to support a Council agreement on certain aspects of the new legislation, but awaits further clarification from the Minister about both the substance of the proposals and their implications for the Brexit process. These were contained in a previous Committee Report on 13 November 2017.

The proposal is particularly important because the UK and EU have agreed that the Social Security Regulation will be "grandfathered" into the Article 50 Withdrawal Agreement for EU citizens already resident in the UK before Brexit and vice versa, including a bilateral mechanism to update the Withdrawal Agreement in light of future amendments adopted to the Regulation after the UK ceases to be an EU Member State.

Not cleared from scrutiny.

Sanctions on Venezuela

The Committee discussed the EU's new sanctions regime for Venezuela, which was approved by Foreign Affairs Ministers in November in response to the country's socio-

economic crisis and the repression of political dissent by the Venezuelan Government. The new sanctions framework imposes an arms embargo on Venezuela, and the EU may also in the future impose travel bans and asset freezes on high-ranking Venezuelan officials.

Cleared from scrutiny; drawn to the attention of the Foreign Affairs Committee.

Aviation Emissions and EU Emissions Trading System

The Committee considered proposals on the next phase of the EU Emissions Trading System (ETS) and on the specific arrangements for aviation within the ETS. Satisfactory agreement on both proposals has been overshadowed by EU proposals to future-proof the ETS against an abrupt UK exit from the EU. Concerned by the impact of that scenario on the carbon market, the EU has proposed that emission allowances issued by the UK from 1 January 2018 would be marked as such and would be invalid where the obligations on operators are "lapsing" due, for example, to the withdrawal of the UK from the ETS. The Committee notes that UK allowances could potentially be worthless and asks the Government for its analysis of the impact on UK operators.

Not Cleared/Cleared; further information requested; drawn to the attention of the Business, Energy and Industrial Strategy Committee.

Veterinary Medicinal Products

The Commission proposed in 2014 to amend legislation on veterinary medicines and medicated feed in order to improve its effectiveness and safety. Negotiations on these proposals are likely to culminate in agreement shortly after three years of discussions. The Committee waives the scrutiny reserve in order that the Government might give agreement, but raises a number of Brexit-related queries on: the amount of trade in veterinary medicines and medicated feed between the UK and EU-27; the implications for the UK of separation from the EU's veterinary medicines regulatory framework, including the restrictions to tackle anti-microbial resistance, the proposed new common database and the requirements on authorisations and mutual recognition; and whether the UK would be likely to choose to maintain alignment with EU standards post-Brexit in any case.

Not cleared; scrutiny waiver granted; further information requested.

Digital Single Market: ENISA/EU Cybersecurity Agency Regulation

The Commission proposes to give the European Union Network and Information Security Agency (ENISA) a permanent mandate. ENISA would acquire a role in the development and implementation of EU cybersecurity policy, as well as overseeing a new EU-wide "cybersecurity certification framework". On Brexit, the Minister states that the UK derives less value from membership of ENISA than smaller Member States. He accepts that the UK will need to enter into negotations with the EU to clarify its future relationship with ENISA. A number of third-country provisions exist in the NIS Directive and its implementing acts which should make some level of ongoing cooperation possible. The Committee seeks further information on these points.

Not cleared from scrutiny; further information requested.

Vehicle type approval

The UNECE World Forum for Harmonization of Vehicle Regulations, or Working Party 29 (WP.29), is a regulatory forum in which states agree to mutually recognise their vehicle type approval processes based on common standards, to reduce technical barriers to trade. Leaving the EU will mean that the UK will vote on these matters itself, instead of the Commission registering the bloc's position (pre-agreed by qualified majority in Council). Although many vehicle regulations are harmonised globally at UNECE, a significant proportion are not. At present this is not an issue when exporting from the UK to the European market, as the EU Regulation on type approvals means that certifications issued by the Vehicle Certification Agency (VCA) are recognised within the EU. However, the UK's withdrawal from the EU means that (in the absence of an agreement) the EU Regulation on type approval would no longer apply to the UK, meaning that UK-based manufacturers would have to use other European approval authorities. The Committee seeks further clarifications about the implications of withdrawal from the EU for UK participation in WP.29 and recognition of VCA certifications within the EU.

Not cleared from scrutiny; further information requested; drawn to the attention of the Transport Committee.

Rail passengers' rights and obligations

The European Commission has proposed a recast of an existing regulation covering rail passengers' rights and obligations. The proposal reduces the scope of current exemptions from the regulation, clarifies and strengthens a range of protections - particularly in relation to people with disabilities or reduced mobility - and introduces a force majeure clause for operators as well as a 'right of redress'. The Minister is supportive of EU action to achieve the objectives given, but concedes that the Government has yet to undertake a detailed analysis of the proposal's impacts. On Brexit, the Minister says that the rights put in place by this proposal would apply equally to all rail passengers and therefore benefit rail passengers who are not EU/EEA citizens. The Committee seeks further clarification of the proposal and its Brexit implications, particularly in relation to cross-border rail services on the island of Ireland.

Not cleared from scrutiny; further information requested; drawn to the attention of the Women and Equalities Select Committee.

Documents drawn to the attention of select committees:

('NC' indicates document is 'not cleared' from scrutiny; 'C' indicates document is 'cleared')

Business, Energy and Industrial Strategy Committee: EU Emissions Trading System 2021-2030 [Proposed Directive (C)]; Aviation emissions [Proposed Regulation (NC)]; Single EU VAT Area [(a) Proposed Directive (NC), (b) Proposed Regulation (NC), (c) Proposed Regulation (C), (d) Commission Communication (C)]

Exiting the European Union Committee: The European Citizens' Initiative [Proposed Regulation (NC)]; EU-Canada Agreement on Passenger Name Record Data [Recommended Decision (NC)]

Foreign Affairs Committee: Sanctions on Venezuela [(a)Proposed Decision (C), (b) Proposed Regulation (C]

Home Affairs Committee: EU participation in council of Europe convention and Additional Protocol on the Prevention of Terrorism [Proposed Decisions (NC)]; EU-Canada Agreement on Passenger Name Record Data [Recommended Decision (NC)]
Northern Ireland Affairs Committee: Single EU VAT Area [(a) Proposed Directive (NC), (b) Proposed Regulation (NC), (c) Proposed Regulation (C), (d) Commission Communication (C)]

Transport Committee: Vehicle type approvals [Proposed Decision (NC)]

Treasury Committee: Single EU VAT Area [(a) Proposed Directive (NC), (b) Proposed Regulation (NC), (c) Proposed Regulation (C), (d) Commission Communication (C)]

Women and Equalities Committee: Rail passengers' rights and obligations [Proposed Regulation (NC)]

1 Aviation emissions

Committee's assessment	Politically important
Committee's decision	Not cleared from scrutiny; drawn to the attention of the Business, Energy and Industrial Strategy Committee
Document details	Proposal for a Regulation of the European Parliament and of the Council amending Directive 2003/87/EC to continue current limitations of scope for aviation activities and to prepare to implement a global market-based measure from 2021
Legal base	Article 192(1) TFEU; QMV; Ordinary Legislative Procedure
Department	Business, Energy and Industrial Strategy
Document Number	(38508), 5968/17 + ADDs 1–2, COM(17) 54

Summary and Committee's conclusions

1.1 International agreement on reducing aviation emissions was eventually reached in October 2016, when the International Civil Aviation Organisation (ICAO) Assembly agreed to implement a Global Market–Based Measure (GMBM) from 2021 to 2035.

1.2 The EU had previously taken its own action to reduce emissions by including flights between aerodromes within the European Economic Area ("intra-EEA flights") and flights between aerodromes in the EEA and aerodromes in third countries ("extra-EEA flights") in the EU's main measure to reduce emissions—the Emissions Trading System (EU ETS)—from 2012.

1.3 The scope of the EU's measure was temporarily reduced to intra-EEU flights in response to international opposition. In the light of the recent international agreement, the Commission proposed to make that reduction in scope permanent.

1.4 The predecessor Committee last considered the proposal at its meeting of 25 April, when it granted a scrutiny waiver in advance of possible adoption of a General Approach. It was decided to retain the proposal under scrutiny while the position of the European Parliament developed.

1.5 Since then, the Minister of State for Climate Change and Industry (Claire Perry) has written to confirm that the Council adopted its position on 21 June as expected and that the agreement did not differ significantly from the original Commission proposal. She wrote again on 14 November, setting out the agreement reached in "trilogue" negotiations with the European Parliament.

1.6 She notes that one amendment agreed in the European Parliament and in the subsequent negotiations aims to protect the environmental integrity of the EU ETS in case of an abrupt UK exit from the EU in March 2019. The issue has arisen because permits for emissions in the previous calendar year are surrendered on 30 April. This would mean that, in the event of an abrupt exit, UK companies would not need to surrender their allowances for emissions in 2018. Instead, they could sell their allowances, possibly

flooding the market and thus potentially distorting the carbon price. To overcome this issue, it has been agreed that allowances issued by the UK from 2018 would be marked as such and would be invalid where the obligations for operators are "lapsing" due, for example, to the UK's exit from the System.

1.7 While the Government supports most of the agreement, it has indicated its intention to oppose the text due to the Brexit amendment and an amendment on the use of auctioning revenues which, it argues, goes against fiscal sovereignty by not making clear that it is for Member States to decide how to use their revenues.

1.8 The agreement is likely to be signed off by the Council on 19 December.

1.9 **We note the measures taken by the EU to protect the environmental integrity of the EU ETS and we address this aspect in our separate chapter on wider reform of the System.**

1.10 **We note the Government's intention to oppose the text, but we would welcome confirmation of the Government's final approach and its reasons. The proposal remains under scrutiny.**

Full details of the documents

Proposal for a Regulation of the European Parliament and of the Council amending Directive 2003/87/EC to continue current limitations of scope for aviation activities and to prepare to implement a global market-based measure from 2021: (38508), 5968/17 + ADDs 1–2, COM(17) 54.

Background

1.11 The introduction of the "full scope" Aviation EU ETS in 2012 (i.e. all flights to and from EEA airports) provoked widespread international opposition, in response to which the EU legislated to temporarily reduce the scope of the Aviation EU ETS to intra-EEA flights only. Full information on the background and content of the proposal were set out in the previous Committee's Report of 8 March.[1]

1.12 At its meeting of 8 March, the previous Committee raised a number of Brexit-related queries. In response, the then Minister of State for Climate Change and Industry (Nick Hurd) noted that the UK's future involvement in the EU ETS would be dealt with separately as part of the wider Brexit negotiations. As for the post-Brexit application of any market based emissions reduction measures to UK non-domestic flights, the Minister set out the various elements of uncertainty. The Minister concluded that it was not yet clear whether the UK could feasibly take separate action on UK flights to and from the EEA after EU Exit, to avoid a situation where these flights are not covered by a market based measure.

1.13 Despite the uncertainty, the Government's guiding principle in making decisions and participating in negotiations would be ensuring the best possible outcome for the UK aviation industry and continuing to take action to address aviation emissions as cost effectively as possible. The Minister also set out the UK's strong engagement in the development of the international mechanism.

1 Thirty-fourth Report HC 71–xxxii (2016–17), chapter 3 (8 March 2017).

1.14 At its meeting of 25 April, the previous Committee waived the proposal from scrutiny in advance of a possible General Approach and requested an update on discussions in both the Council and the European Parliament.

The Minister's letter of 12 July 2017

1.15 The Minister confirmed that the Council adopted its position on 21 June as expected and noted that the agreement did not differ significantly from the Commission proposal published on 3 February 2017.

The Minister's letter of 14 November 2017

1.16 The Minister explains that the European Parliament agreed its position on 13 July, including a series of more stringent approaches than adopted by the Council. There was also a last-minute amendment to invalidate allowances, issued from 2018, which are issued by a Member State where the obligations for aviation operators and other operators are "lapsing". This, explains the Minister, would make the allowances issued by the UK from 2018 invalid for compliance in the EU ETS, due to the UK's withdrawal from the EU before the compliance deadline for 2018 emissions (30 April 2019). The objective of this amendment was to protect the environmental integrity of the EU ETS in the event of an abrupt UK departure from the System in March 2019.

1.17 Political agreement between the Council, the European Parliament and the Commission was reached on 18 October. The Minister summarises the main elements of the deal as follows:

- the end date for the derogation reducing the scope to intra-EEA flights is set at 31 December 2023;
- an annual reduction (the Linear Reduction Factor) will be applied to the Aviation EU ETS cap from 2021;
- the exemption for non-commercial operators emitting less than 1,000 tonnes carbon dioxide per annum will continue to the end of 2030 (it would otherwise have ended in 2020);
- aircraft operators with emissions of less than 3,000 tonnes carbon dioxide per annum will benefit from simplified verification procedures;
- the European Commission will undertake a review on the implementation of Carbon Offsetting and Reduction Scheme for International Aviation (CORSIA) and the future of the Aviation EU ETS within 12 months of the rules on the CORSIA being adopted in ICAO;
- deletion of the text: "It shall be for Member States to determine the use to be made of revenues generated from the auctioning of allowances", which does not go as far as the European Parliament's position that it should be mandatory to spend such revenues on tackling climate change; and
- agreement to the proposed amendment to invalidate allowances issued from 2018, which are issued by a Member State where obligations are lapsing (see above).

1.18 Following political agreement, the text was presented to Member State representatives at the COREPER meeting on 27 October. The UK supported the main elements of the agreement, says the Minister, but stated its intention to vote against the deal for the following reasons:

- "The UK opposes the amendment to invalidate allowances from 2018, which could have negative impacts on the EU ETS carbon market in general and specifically on the UK.
- "The compromise text on revenues from the auctioning of aviation allowances goes against fiscal sovereignty by not making clear that it is for Member States to decide how to use their revenues."

1.19 On the amendment designed to protect the EU ETS from an abrupt UK departure from the System in March 2019, the Minister notes that the Commission has proposed a draft regulation to amend the EU ETS Registry Regulation to implement the amendment. She adds:

> "We will continue to work closely with our European counterparts. The UK Government is working closely with the EU Institutions to explore alternative solutions that would be better for the EU and the UK, and to this end published a consultation on bringing forward the 2018 compliance deadline for UK EU ETS operators to before the date of EU Exit on 6 November."

1.20 It is expected that the final compromise will be signed off by the Environment Council at its meeting on 19 December. The Minister seeks scrutiny clearance in order to vote against the package, but emphasises that the text is likely to be agreed in any case.

Previous Committee Reports

Fortieth Report HC 71–xxxvii (2016–17), chapter 8 (25 April 2017); Thirty-fourth Report HC 71–xxxii (2016–17), chapter 3 (8 March 2017).

2 The European Citizens' Initiative

Committee's assessment	Legally and politically important
Committee's decision	Not cleared from scrutiny; further information requested; drawn to the attention of the Committee on Exiting the European Union
Document details	Proposed Regulation on the European citizens' initiative
Legal base	Article 24 TFEU, ordinary legislative procedure, QMV
Department	Cabinet Office
Document Number	(39040), 12307/17 + ADDs 1–2, COM(17) 482

Summary and Committee's conclusions

2.1 The aim of the European Citizens' Initiative (ECI) is to give EU citizens a direct say in shaping the laws that govern them. Introduced by the Lisbon Treaty, the ECI empowers EU citizens of voting age and acting together—there must be at least one million drawn from no fewer than seven Member States—to invite the Commission to use its right of initiative in any policy areas where it has powers to act under the EU Treaties. The Commission may propose new laws or other non-binding policy measures. The procedures and conditions for implementing the ECI are set out in a 2011 Regulation which took effect in April 2012.[2] Since then, around eight million statements of support have been collected for various causes but only three of the 47 ECIs that have been registered have reached the final stage of the procedure where they are formally examined by the Commission to determine whether and how to act.[3]

2.2 Following a process of review and consultation, the Commission has concluded that the ECI has not met its full potential. It is not well-known amongst the public, around a third of initiatives do not meet the criteria for registration—the first step towards collecting statements of support—and the procedures are complex and burdensome for organisers. Without changes, the Commission considers that the ECI could eventually become obsolete.[4] It is therefore proposing a new Regulation to replace the 2011 Regulation, remove "bottlenecks" in the operation of the ECI and clarify the rules and conditions governing its use.[5] The Commission's aim is to foster debate and participation in the democratic life of the EU by making the ECI more accessible for EU citizens and easier to use for organisers of ECIs and their supporters. Young people aged 16 and above would be entitled to support an ECI, even if they have not reached voting age in their home Member State. The proposed Regulation is expected to take effect in January 2020, although some preparatory provisions will be implemented earlier.

2.3 The Parliamentary Secretary to the Cabinet Office (Chris Skidmore) considers that the changes proposed by the Commission are "likely to improve the operation of the ECI in practice" and make it easier for EU citizens to "participate in EU democratic processes".

2 See Regulation (EU) 211/2011 on the citizens' initiative.

3 The Commission has taken follow-up action on two of the successful ECIs—"Right to Water" and "Stop vivisection". See the Commission Staff Working Document (ADD 2) for further details.

4 See p.8 of the Commission Staff Working Document—ADD 2.

5 See p.3 of the Commission's explanatory memorandum accompanying the proposed Regulation.

Lowering the age at which EU citizens are able to support an ECI to 16 "is not a priority issue for the Government" as it will not affect the franchise for elections in the UK. The Government intends to "engage openly and cooperatively with our EU partners" on the Commission's proposed changes "while it [the UK] is obliged to do so as a Member State". In the longer term, he indicates that the Government will "consider all our obligations and take decisions in relation to the timing and implementation of these proposals as required during the exit negotiations period", adding that relevant factors include:

> "[…] whether any changes to the current domestic implementation of the ECI are required, also in line with the implementation process and process for exiting the European Union."

2.4 **The Minister raises no concerns about the substance of the changes proposed by the Commission. He makes clear that while the UK remains a full member of the European Union, the Government will "continue to negotiate, implement and apply EU legislation". We ask the Minister how rapidly he expects negotiations to progress and whether the proposed Regulation is likely to be agreed before the UK leaves the EU.**

2.5 **We would welcome further analysis of the "timing and implementation" issues alluded to by the Minister. We note that the proposed Regulation envisages the staggered implementation of its provisions. Some will take effect shortly after the proposal has been formally adopted by the Council and European Parliament; most—including the repeal of the 2011 Regulation—will only take effect from 1 January 2020, after the date on which the UK expects to leave the EU. Depending on the pace of negotiations, it is possible that both the 2011 Regulation and its successor Regulation will apply to and bind the UK on Brexit day. Under the European Union (Withdrawal) Bill, directly applicable EU Regulations which are "operative immediately before exit day" will form part of domestic UK law "on and after exit day".[6] It seems clear that the 2011 Regulation will therefore form part of domestic law "on and after exit day". We ask the Minister whether the proposed successor Regulation (if adopted before exit day) would also be regarded as "operative" for the purposes of the Bill and form part of the body of retained EU law which would apply in the UK post-Brexit, even though it contains provisions which may only take effect after exit day.**

2.6 **The European Citizens' Initiative is only available to EU citizens—that is, the nationals of EU Member States. We ask the Minister:**

- **whether it is the Government's position that UK nationals will cease to be EU citizens on Brexit day; and**
- **if so, whether the Government would need to use its correcting powers under clause 7 of the EU (Withdrawal) Bill to make clear that UK nationals would no longer be entitled to take part in European Citizens' Initiatives.**

2.7 **We also ask the Minister to explain how Brexit would affect the involvement of UK nationals in ECIs (either as organisers or as signatories) which were initiated before Brexit day. Does the Government intend to seek transitional arrangements to ensure**

6 See clause (1) of the Bill.

that their participation would count towards meeting the requirements for registering an ECI and securing sufficient statements of support for formal examination by the Commission?

2.8 **Pending further information, the proposed Regulation remains under scrutiny. We draw this chapter to the attention of the Committee on Exiting the European Union.**

Full details of the documents

Proposed Regulation on the European citizens' initiative: (39040), 12307/17 + ADDs 1–2, COM(17) 482.

The proposed Regulation

2.9 Many of the rules and procedures contained in the 2011 Regulation would remain unchanged. So, for example, the organisers of an ECI must be of voting age and resident in at least seven different Member States to ensure that the ECI is representative of opinion across the EU. The ECI must not be "manifestly abusive, frivolous or vexatious" or "manifestly contrary" to EU values, and it must cover areas in which the Commission is empowered to act under the EU Treaties. To reach the stage of formal examination by the Commission, the ECI must attract the support of at least one million EU citizens and achieve a minimum number of signatories in at least a quarter of all Member States—the qualifying threshold for signatories in the UK is currently 54,000 (this would increase to 54,750 under the proposed Regulation).[7]

2.10 Following extensive consultation with stakeholders, the Commission identifies a need for changes in the following areas:

- the registration process;
- the ECI "lifecycle" and time limits;
- the setting-up and certification of online collection systems; and
- personal data requirements for ECI signatories and the responsibilities imposed on organisers.

2.11 The proposed Regulation would reduce the burden on organisers of an ECI by:

- setting up a helpdesk service and online collaborative platform to provide a forum for discussion and source of information and advice on ECIs;
- providing a free translation service to ensure that the content of the ECI is available in all the EU's official languages once it has been registered;
- ensuring that each Member State has one or more contact points to assist organisers in setting up an ECI;

7 The threshold for signatories corresponds to the number of MEPs elected in each Member State, multiplied by 750 (roughly approximating to the total number of MEPs—751—in the European Parliament).

- allowing a legal entity (such as an organisation) to manage an ECI and clarifying the legal liability of organisers of ECIs;
- requiring the Commission to set up and operate, by 1 January 2020, a central online collection system which would be available free of charge to the organisers of a registered ECI; and
- clarifying that each Member State is responsible for verifying and certifying statements of support for a proposed ECI signed by its own nationals, even if they are resident in another Member State (currently, the UK and some other Member States choose only to verify and certify statements of support made by individuals resident in their territories).

2.12 The Commission-run, central online collection system would be optional—organisers of an ECI would be free to set up their own individual online collection systems but these must comply with common technical security features and (as now) be certified by the Member State(s) in which the data are held once the proposed ECI has been registered.

2.13 The Commission recognises stakeholders' concern that a significant (but declining) proportion of proposed ECIs do not meet the criteria for registration or fail to achieve sufficient statements of support (at least one million within a year of the ECI being registered). To meet this concern, the proposed Regulation would:

- allow organisers to amend their ECI if the initial request for registration is refused;
- provide for partial registration if "a substantial part" of the proposed ECI (including its main objectives) falls within areas where the Commission has the power to act under the EU Treaties (severing the non-qualifying parts);
- enable organisers to choose the start date for collecting signatures, provided it is no later than three months from the date of registration;
- clarify that statements of support for an ECI may be signed online or in paper form and limit the personal data that may be collected; and
- extend participation by establishing 16 as the age at which an individual can support an ECI.

2.14 At the end of the process, the organisers of ECIs which have secured sufficient statements of support are entitled to a public hearing held in the European Parliament. The proposed Regulation seeks to ensure that there is "a balanced representation of relevant public and private interests" to counteract concerns that the hearing provides a platform for the organisers rather than promoting "dialogue and participation and exchange of views" amongst interested stakeholders.[8] The proposal also extends (from three to five months) the time available to the Commission to publish its "legal and political conclusions" on the ECI and "the action it intends to take, if any, and its reasons for taking or not taking action".[9]

8 See Article 14 of the proposed Regulation and p.40 of the Commission's Staff Working Document (ADD 2).

9 See Article 15 of the proposed Regulation.

2.15 The proposed Regulation includes stronger provisions on transparency—information on the sources of support and donations exceeding €500 (£459)[10] per sponsor must be published in the register of ECIs and regularly updated—and on the protection of personal data to ensure that the collection of statements of support complies with updated EU data protection laws.[11]

The Minister's Explanatory Memorandum of 14 November 2017

2.16 The Minister sets out the Government's approach to EU legislative proposals following the outcome of the referendum on UK membership of the EU:

> "On 23 June 2016, the EU referendum took place and the people of the United Kingdom voted to leave the European Union. The Government respected the result and triggered Article 50 of the Treaty on European Union on 29th March 2017 to begin the process of exit. Until exit negotiations are concluded, the UK remains a full member of the European Union and all the rights and obligations of EU membership remain in force. During this period the Government will also continue to negotiate, implement and apply EU legislation."

2.17 He notes that the changes proposed to the operation of the ECI are "consistent with other Commission initiatives, reflecting the political guidelines of the Juncker Commission, aiming at enhancing citizens' involvement and participation in EU policy-making". On the substance of the changes proposed, the Minister observes:

> "The UK Government shares the Commission's priority of increasing the democratic legitimacy in the EU through enhanced citizens' involvement and participation (Priority no 10—A Union of Democratic Change). It also supports proposals that are intended to make it easier for EU citizens to participate in EU democratic processes and for competent authorities to administer the ECI. We believe that the Commission's proposal is likely to improve the operation of the ECI in practice. The proposal may also ease requirements on Member States, notably through the creation of a Commission-run data collection system.
>
> "The lowering of the age at which someone may sign an initiative—from 18 to 16—is not a priority issue for the Government. This is because this proposal will in no way affect the rights of citizens to vote in elections in line with existing law on the franchise.
>
> "The Regulation places a small number of obligations on Member States, notably the requirement to certify statements of support for initiatives. In the UK, this is not an onerous process. The Cabinet Office has recently streamlined its processes for certification and the requirement to do this in three months of receipt of statements of support is acceptable. (This requirement is unchanged from the existing Regulation)."

10 €1 = £0.91973 or £1 = €1.08728 as at 1 September 2017.

11 The General Data Protection Regulation will take effect in May 2018, ahead of the proposed changes to the ECI process—most are expected to take effect in January 2020.

2.18 Turning to the conduct of negotiations, the Minister comments:

> "The UK Government will continue to engage openly and cooperatively with our EU partners on the proposed reforms to the EU Regulation on the ECI whilst it is obliged to do so as a Member State.
>
> "Importantly, the UK Government will consider all our obligations and take decisions in relation to the timing and implementation of these proposals as required during the exit negotiations period. These include consideration of whether any changes to the current domestic implementation of the ECI are required, also in line with the implementation process and process for exiting the European Union."

2.19 He estimates the cost of implementing the proposed ECI Regulation domestically as "essentially zero".

Previous Committee Reports

None.

3 Digital Single Market: ENISA / EU Cybersecurity Agency Regulation

Committee's assessment	Legally and politically important
Committee's decision	Not cleared from scrutiny; further information requested
Document details	(a) Proposal for a Regulation of the European Parliament and of the Council on ENISA, the "EU Cybersecurity Agency", and repealing Regulation (EU) 526/2013, and on Information and Communication Technology cybersecurity certification ("Cybersecurity Act"); (b) Communication from the Commission to the European Parliament and the Council: Making the most of NIS—towards the effective implementation of Directive (EU) 2016/1148 concerning measures for a high common level of security of network and information systems across the Union; (c) Report from the Commission to the European Parliament and the Council on the evaluation of the European Union Agency for Network and Information Security (ENISA); (d) External Action Service Joint Communication to the European Parliament and to the Council: Resilience, Deterrence and Defence: Building strong cybersecurity for the EU
Legal base	Article 114 TFEU; ordinary legislative procedure; QMV
Department	Digital, Culture, Media and Sport; Foreign and Commonwealth Office
Document Numbers	(a) (39045), 12183/17, COM(2017) 477; (b) (39021), 12205/17 + ADD 1, COM(17) 476; (c) (39022), 12208/17, COM(17) 478; (d) (39050) 12211/17, COM(17) 450

Summary and Committee's conclusions

3.1 As part of its Digital Single Market Strategy, the Commission has brought forward a 'Cybersecurity package' which proposes to make the European Union Agency for Network and Information Security (ENISA) permanent and to update its mandate to reflect current and future needs in the field of cybersecurity.

3.2 The principal changes proposed involve granting ENISA enhanced roles in EU-level cybersecurity policy development and implementation, entrusting it with coordinating responses to large-scale cross-border cybersecurity emergencies, and asking it to implement a new "cybersecurity certification framework" which seeks to minimise market fragmentation. This would avoid (for example) smart meter providers having to pay standards organisations in different Member States large sums in order to have their products accredited in different jurisdictions.

3.3 The main elements of the package were trialed in a December 2016 communication on "strengthening Europe's Cyber Resilience System and Fostering a Competitive and

Innovative Cybersecurity Industry".[12] The Commission received support in its approach from the European Council's conclusions in June 2017.[13] The Council of Ministers had also previously called upon the Commission to take further steps to specifically address the issue of cybersecurity certification at the European level.[14] The package of proposed changes is also informed by a report evaluating the effectiveness of ENISA's performance,[15] which concludes that ENISA remains relevant, but has been inhibited by its lack of a permanent mandate as well as its limited resources relative to its broad mandate.

3.4 The legislative component of the package is the proposed revision of the existing ENISA Regulation[16] (hereafter "the Regulation"). In addition to making ENISA's mandate permanent, the Regulation proposes to shift the emphasis of ENISA's activity somewhat in the direction of the wider stakeholder community, particularly market-based operators.

3.5 Specific changes that are proposed include:

- giving ENISA an advisory role in EU-level cybersecurity policy development and implementation, meaning that it will issue independent opinions and undertake preparatory work in relation to the cybersecurity implications (e.g. of EU legislative proposals across a wide range of sectors);
- strengthening ENISA's role in operational cooperation and crisis management, through the creation of an 'EU cybersecurity blueprint' which envisions ENISA playing a coordinating role in response to large-scale cross-border cybersecurity incidents; and
- giving ENISA a role supporting EU policy development in the ICT standardisation and ICT cybersecurity certification areas, including through the introduction of a proposed EU framework for cybersecurity certification schemes.

3.6 The Regulation emphasises that EU cybersecurity certification schemes for ICT products would make use of existing standards and would not develop the technical standards themselves, and also that participation in European certification schemes will remain voluntary (unless legislation laying down security requirements for ICT products were to require otherwise).

3.7 Despite these changes there is a high degree of continuity with ENISA's former mandate and activities, which retains a strong focus on supporting the Member States by facilitating cybersecurity cooperation between them, sharing best practice and assisting in capacity building.

3.8 The Minister (Matt Hancock) does not provide a detailed analysis of the policy implications of the proposal, and states that officials will assess policy implications, including the Government's position on subsidiarity, during negotiations. The Minister

12 Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee, and the Committee of the Regions: Strengthening Europe's Cyber Resilience System and Fostering a Competitive and Innovative Cybersecurity Industry.
13 European Council meeting (22 and 23 June 2017)—Conclusions.
14 Council Conclusions on Strengthening Europe's Cyber Resilience System and Fostering a Competitive and Innovative Cybersecurity Industry—15 November 2016.
15 REPORT FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT AND THE COUNCIL on the evaluation of the European Union Agency for Network and Information Security (ENISA).
16 Proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on ENISA, the "EU Cybersecurity Agency", and repealing Regulation (EU) 526/2013, and on Information and Communication Technology cybersecurity certification (''Cybersecurity Act'').

states that a certain degree of EU coordination is beneficial to manage cross-border cyber risks, and that "the current flexibility in the text means that the Government is content that the proposed measures remain proportionate to the need". Despite the Commission's use of the word "operational" to describe the role envisaged for ENISA in cybersecurity crisis management, the Minister suggests that this does not actually amount to a traditional operational role.

3.9 On Brexit, the Minister acknowledges that the UK will need to enter into negotiations to agree its future relationship with ENISA after the UK leaves the European Union. He states that negotiations on the proposed regulation will commence at the end of October, and are unlikely to conclude before the UK leaves the EU in 2019. The Minister adds, in a separate memorandum on a Communication on the implementation of the Network and Information Services (NIS) Directive,[17] that the Government is looking at how it can limit disruption should the UK assume third country-status.

3.10 Our initial assessment is that the proposed Regulation does not fall within the scope of the UK's JHA Opt-In Protocol, because, like the existing ENISA Regulation, the proposal has a Single Market legal base (Article 114 TFEU), the Court of Justice has rejected a previous UK challenge of this base.[18] The increased focus on market actors envisaged in the Regulation would appear to bring ENISA's activities further into the ambit of its current Single Market legal base.

3.11 In parallel to the Commission's proposed reforms to ENISA, the European External Action Service has issued a Communication[19] regarding the external dimension of cybersecurity. Recommended actions include factoring cyber security into trade and investment policy, encouraging the uptake of IPv6,[20] and intensifying EU-NATO cooperation on cybersecurity. The Minister for Europe and the Americas (Sir Alan Duncan) at the Foreign and Commonwealth Office (FCO) indicates that the Government supports the Communication's overarching goal of making the EU proactive instead of reactive on cybersecurity issues, but outlines a number of areas of possible concern, including the impact of the EU certification framework on trade and investment, as well as possible conflicts between the operational role that is envisaged for ENISA and national processes.[21]

3.12 **We thank the Government for its Explanatory Memoranda in relation to these cybersecurity-related documents. We note that the Government has not yet provided a detailed analysis of the policy implications of the proposed Regulation (12183/17), and states that it will develop its position during negotiations. We therefore request further clarification on the following points:**

- **The Government previously told the Committee that it would "challenge any proposals that seek to create EU-only standards, or standards where the**

17 EM 12205/17.

18 EU law blog: ENISA, legal base and Case C-217/04 http://eulaw.typepad.com/eulawblog/2006/05/enisa_legal_bas.html (accessed 30 October 2017).

19 COMMUNICATION FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT AND THE COUNCIL Making the most of NIS—towards the effective implementation of Directive (EU) 2016/1148 concerning measures for a high common level of security of network and information systems across the Union.

20 Internet Protocol version 6 (IPv6) is the most recent version of the Internet Protocol (IP), the communications protocol that provides an identification and location system for computers on networks and routes traffic across the Internet. It provides a variety of security benefits relative to IPv4, its predecessor. See: IPv6 (accessed 26 October 2017).

21 EM 12211/17.

associated conformity checking can only be performed by/under the control of European bodies".[22] We ask the Government to clarify whether, and to what extent, the Commission's proposal realises these concerns.

- **Has the BSI been consulted in preparation of this Explanatory Memorandum? If so, what is its opinion of the Commission's proposed approach?**
- **What scrutiny will there be by the Member States and the European Parliament of any Commission-developed implementing regulations which would create individual cybersecurity certification schemes that required the repeal of national schemes?**
- **The FCO expresses concern about prospective EU interference with national operational activities in the field of cybersecurity, whereas DCMS cautions that the Commission's use of the term "operational" to describe ENISA's proposed coordinating role in cross-border cybersecurity emergencies does not actually amount to an operational role in the UK usage of the term. What is the Government's considered view on this aspect of the proposal?**
- **The ENISA evaluation report concluded that ENISA's effectiveness had been hampered by its limited resourcing relative to its broad mandate. To what extent do the proposals reflect these findings? Is ENISA's mandate sufficiently reduced in scope in some areas to offset its new obligations? Alternately, is a major increase in resources proposed?**

Brexit implications

3.13 **Regarding the implications of the UK's impending withdrawal from the EU, we note the Government's assessment that membership of ENISA itself is less valuable to the UK than it is for smaller Member States, and that the UK will need to enter into negotiations to agree its future relationship with ENISA after the UK leaves the European Union.**

3.14 **In relation to the provisions of the NIS Directive, we note the Government's assessment that the main impacts of withdrawal, if there is a transition to third country status, will be on the UK's membership of the Cooperation Group and CSIRT network; mandatory annual incident reporting requirements on Member States; and the potential impact on UK digital service providers. We note that the Government is looking at ways in which it can maintain membership of the Cooperation Group and CSIRT network, amending incident reporting to make it either voluntary or remove the requirement to report to EU institutions, as well as minimize any negative impacts on digital service providers.**

3.15 **Regarding the Brexit implications of the proposal, we ask the Government to provide:**

- **a clear account of the means by which third countries currently participate in / cooperate with ENISA, including through the NIS Directive and its supporting institutional arrangements;**

22 EM 11013–16.

- **a fuller account of the anticipated impacts of a shift to third country status for the UK and UK-based operators with regards to the main provisions of the ENISA Regulation and the NIS Directive (e.g., what would the impact be on digital service providers?);**
- **an explanation of the Government's concerns about the potential impact on trade and investment of the proposal for an EU certification framework, and how this might affect the UK when it assumes third country status;**
- **clarification of whether, given that the UK may end up having to apply the EU acquis during a transitional / implementation period, (i) the Government shares the Committee's assessment that the JHA Opt-In Protocol does not apply, or (ii) if the Government disagrees, the factors it will take into account in deciding whether or not to opt into the proposed Regulation.**

3.16 **We ask the Government to respond to these questions, and to provide an update of any progress that has been made in the Council, by 20 January 2018 (or earlier, if progress in Council requires it), with DCMS coordinating input from the FCO where necessary. In the meantime we retain this proposal under scrutiny.**

Full details of the documents

(a) Proposal for a Regulation of the European Parliament and of the Council on ENISA, the "EU Cybersecurity Agency", and repealing Regulation (EU) 526/2013, and on Information and Communication Technology cybersecurity certification ("Cybersecurity Act"): (39045), 12183/17, COM(2017) 477; (b) Communication from the Commission to the European Parliament and the Council: Making the most of NIS—towards the effective implementation of Directive (EU) 2016/1148 concerning measures for a high common level of security of network and information systems across the Union: (39021), 12205/17 + ADD 1, COM(17) 476; (c) Report from the Commission to the European Parliament and the Council on the evaluation of the European Union Agency for Network and Information Security (ENISA): (39022), 12208/17, COM(17) 478; (d) External Action Service Joint Communication to the European Parliament and to the Council: Resilience, Deterrence and Defence: Building strong cybersecurity for the EU: (39050) 12211/17, COM(17) 450.

Background

ENISA

3.17 The European Union Agency for Network and Information Security (ENISA) was established by Regulation (EC) No 460/2004[23] to contribute to the overall goal of ensuring a high level of network and information security within the EU. The Agency has its administrative seat in Heraklion (Crete) and its core operations in Athens. ENISA is a small agency with a low budget (€11.25m) and number of staff (84) compared to other EU agencies. It is headed by an Executive Director and governed by a Management Board and Executive Board made up of EU Member States and Permanent Stakeholders. An informal Network of National Liaison Officers facilitates outreach with EU Member States.

23 Regulation (EC) No 460/2004 was subsequently amended in 2008 and 2011 to extend the duration of its mandate. It was later superseded by Regulation (EU) No 526/2013 (the ENISA Regulation).

3.18 The ENISA Regulation sets out the ENISA's current mandate, which is due to expire on 19 June 2020. ENISA's main task is to enhance capability to prevent and respond to network and information security problems within the EU by building on national and Union efforts. It does so through a series of activities across five areas, which are:

- Expertise: provision of information and expertise on key network and information security issues.
- Policy: support to policy making and implementation in the Union;
- Capacity: support for capacity building across the Union (e.g. through trainings, recommendations, awareness raising activities);
- Community: foster the network and information security community (e.g. support to the Computer Emergency Response Teams (CERTs), coordination of pan-European cyber exercises);
- Enabling (e.g. engagement with the stakeholders and international relations).

3.19 ENISA has also taken on specific additional roles and responsibilities in support of the implementation of Directive (EU) 2016/1148 on the security of network and information systems (the NIS Directive). It now provides the secretariat to the Computer Security Incident Response Teams (CSIRTs) Network and assists the NIS Cooperation Group in the execution of its tasks and is intended to assist Member States and the Commission by providing expertise and advice and by the facilitation of best practice.

3.20 In December 2016, the Commission published a Digital Single Market Strategy communication on "strengthening Europe's Cyber Resilience System and Fostering a Competitive and Innovative Cybersecurity Industry",[24] which proposed that the EU develop a series of initiatives concerning cybersecurity certification and labelling, and bring forward the Commission's evaluation of ENISA, which would address the need to modify or extend the mandate of ENISA. The Committee judged the file to be not legally or politically important and immediately released it from scrutiny.

ENISA evaluation report[25]

3.21 Article 32 of the ENISA Regulation requires the Commission to undertake an evaluation of ENISA by June 2018 to assess the impact, effectiveness and efficiency of the agency and to consider whether the current mandate should be extended. The Commission has now carried out that evaluation, which included a public consultation alongside various studies and workshops, and this report outlines the findings.

3.22 The report concludes that ENISA plays a valuable role but that its current mandate does not equip it to meet the increasing cybersecurity challenges faced within the EU. Specific conclusions are that:

- ENISA's objectives remain relevant—indeed, there is a need for a more coordinated approach to cybersecurity;

24 Doc 11013–16.

25 REPORT FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT AND THE COUNCIL on the evaluation of the European Union Agency for Network and Information Security (ENISA).

- ENISA met its objectives and implemented its tasks, however its limited resources (human and financial) limited its ability to deliver against a broad mandate; these difficulties were compounded by difficulties recruiting and retaining experts; and
- the lack of a permanent mandate inhibits ENISA's ability to offer long term planning and sustainable support to Member States.

ENISA Regulation

3.23 The Commission's proposed Regulation (12183/17),[26] which provides a new mandate for ENISA, proposes the following basic changes:

- (Permanent mandate) To grant ENISA a permanent mandate, which would make it the EU Cybersecurity Agency. ENISA's mandate, objectives and tasks would remain subject to regular review;
- (Focus on wider stakeholder community) The organisation and the governance of the Agency would be reviewed to make sure that the needs of the wider stakeholders' community are better reflected in the Agency's work.

3.24 The proposed Regulation also modifies the scope of ENISA's mandate in multiple respects, to better align it with experience of what has demonstrated clear added value (as reflected in the Report) as well as recent additions to its role, including those which are proposed in this Regulation.

3.25 The following are the main changes that are proposed to ENISA's mandate:

- (EU cybersecurity policy development) The proposal tasks ENISA with a role in the development and implementation of EU policy and for it to play a specific advisory role. This would primarily be in the area of network and information security, but would also apply to policy initiatives with cybersecurity elements in other sectors (e.g. energy, transport, finance). ENISA would undertake this work by providing independent opinions and providing preparatory work;
- (EU cybersecurity policy implementation) ENISA would assist the Member States in achieving a consistent implementation of the NIS Directive, particularly supporting the work of the NIS Cooperation Group. More generally, ENISA would provide regular reporting on the implementation of the EU Cybersecurity regulatory framework;
- (Capacity building, knowledge and information, awareness raising) ENISA would be tasked with contributing to the improvement of EU and Member State authorities' capability and expertise and to contribute to the establishment of information sharing and analysis centres. The proposal outlines a vision for ENISA to act as a knowledge and information sharing hub through the pooling

26 Proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on ENISA, the "EU Cybersecurity Agency", and repealing Regulation (EU) 526/2013, and on Information and Communication Technology cybersecurity certification (''Cybersecurity Act'').

of best practice from across the Union. Alongside this it is stated that ENISA should act as a point of guidance in the aftermath of cross border cyber incidents through the compilation of reports and guidance;

- (Research and innovation) ENISA would advise EU and national authorities on research and development priorities and the implementation of research and innovation EU funding programmes;
- (Operational cooperation and crisis management) The proposal identifies a role for ENISA in the context of crisis management, which would involve strengthening the existing preventive operational capabilities, in particular upgrading the pan-European cybersecurity exercises (Cyber Europe) by having them on a yearly basis, and a supporting role in operational cooperation as secretariat of the CSIRTs Network (as per NIS Directive provisions);
- (EU cybersecurity blueprint) Also related to cybersecurity crisis management, an 'EU cybersecurity blueprint' is presented as part of this package and sets out the Commission's recommendation to Member States for a coordinated response to large-scale cross-border cybersecurity incidents and crises at the EU level. ENISA would facilitate cooperation between individual Member States in dealing with a large-scale cross-border emergency by analysing and aggregating national situational reports based on information made available to the Agency on a voluntary basis by Member States and other entities;
- (Market-related tasks, including cybersecurity certification of ICT) ENISA would perform a number of cybersecurity market-related functions. It would operate a cybersecurity 'market observatory', which would analyse relevant trends in the cybersecurity market and support EU policy development. In relation to standardisation, it would facilitate the establishment and uptake of cybersecurity standards, including through the proposed EU framework for cybersecurity certification. More information on this framework is provided below.

EU cybersecurity certification framework

3.26 The Commission argues that cybersecurity certification frameworks are important for developing trust in ICT products and services, but that the current certification framework landscape is patchy and as a result companies are often required to undergo multiple processes in order to offer products across EU Member States. This fragmentation increases costs for businesses. The Commission adduces various examples to illustrate this point—for example, the cost of smart meter cybersecurity certification in the UK is almost €150,000, and costs a similar amount in France. Ultimately, consumers incur a proportion of these increased costs.

3.27 In response, the Commission proposes to introduce a framework which will govern the introduction of EU-wide cybersecurity certification schemes. The Regulation itself does not introduce certification schemes, but seeks to create a system which will allow such schemes to be established and recognised across the EU. The proposal outlines the

minimal content of what would be required under such schemes. Specific cybersecurity certification schemes would be adopted by the Commission in the form of implementing acts, with ENISA playing a central role in their development.

3.28 Where the Commission adopts a specific certification scheme, national schemes or procedures will immediately cease to apply. Manufacturers of ICT products or providers of ICT services would then be able to submit an application for certification of to an accredited conformity assessment body of their choice.

3.29 The proposal establishes the European Cybersecurity Certification Group (the 'Group'), consisting of national certification supervisory authorities of all Member States, with ENISA and Commission officials providing the secretariat of the group. The main task of the Group is to advise the Commission on issues concerning cybersecurity certification policy and to work with ENISA on the development of draft European cybersecurity certification schemes. ENISA would also liaise with standardisation bodies to ensure the appropriateness of standards used in approved schemes and to identify areas in need of cybersecurity standards.

3.30 Member States will be responsible for monitoring, supervisory and enforcement tasks, and to this end they will appoint a certification supervisory authority.

3.31 Important limitations to the scope of the proposed framework include that:

- EU cybersecurity certification schemes would make use of existing standards in relation to the technical requirements and evaluation procedures that the products need to comply with and would not develop the technical standards themselves, with international standards being used instead; and
- participation in European certification schemes will remain voluntary (unless, as with all certification schemes and standards, legislation laying down security requirements for ICT products were to require otherwise).

Communication on NIS Directive implementation

3.32 The Commission has also issued a Communication[27] on Member States' progress in implementing the NIS Directive, some background information on which is provided below.

NIS Directive

3.33 The Security of Network and Information Systems Directive (2016/1148),[28] commonly known as the "NIS" Directive, was adopted by the European Parliament on 6 July 2016, and is the first substantive EU legislation on cyber security. Member States have until 9 May 2018 to transpose the Directive into domestic legislation.

3.34 The NIS Directive provides legal measures to boost the overall level of network and information system security in the EU by ensuring that Member States have in place a

27 COMMUNICATION FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT AND THE COUNCIL Making the most of NIS—towards the effective implementation of Directive (EU) 2016/1148 concerning measures for a high common level of security of network and information systems across the Union.

28 Directive (EU) 2016/1148 of the European Parliament and of the Council of 6 July 2016 concerning measures for a high common level of security of network and information systems across the Union.

national framework to support and promote the security of network and information systems. It establishes a Cooperation Group, to support and facilitate strategic cooperation and the exchange of information among Member States and a Computer Security Incident Response Team ("CSIRT") network to promote swift and effective operational cooperation on specific network and information system security incidents and as well as the sharing of information about risks.

3.35 Under the NIS Directive, Member States are required to identify "Operators of Essential Services"—including operators in the energy, transport, water, financial services, banking, healthcare and digital infrastructure sectors. Certain digital service providers (search engines, cloud computing services and online marketplaces) will also have to comply with the security and incident notification requirements established under the Directive.

The Communication[29]

3.36 The Commission's brief communication:

- notes the establishment of the Cooperation group and the CSIRT network;
- highlights the need for national cyber security strategies to incorporate the NIS Directive, and for Member States to establish appropriate Competent Authorities and CSIRTs to ensure effective implementation;
- reiterates the need to ensure that CSIRTs are adequately funded; and
- encourages Member States to ensure consistency across the EU in identifying Operators of Essential Services.

3.37 The Annex which accompanies the main communication provides detailed guidance on how the Commission believes that elements of the Directive should be interpreted.

EAS communication on external dimension of cybersecurity[30]

3.38 In parallel to the Commission's proposed changes to the ENISA Regulation and the associated cybercommunications documents described above, the External Action Service (EAS) has published a Communication setting out its proposed approach to the external dimension of cybersecurity. This is a non-legislative document.

3.39 The EAS provides a series of proposals on which the EU (Member States, EU Agencies and Institutions) might focus on across a wide range of cyber policy areas. The principal intentions set out by the Commission in the Communication are:

- to build resilience to cyber attacks through strengthening the European Union Agency for Network and Information Security (ENISA);
- to develop the Digital Single Market by setting up an EU cyber security certification framework, factor cyber security into trade and investment policy, and encourage the uptake of IPv6;[31]

29 COMMUNICATION FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT AND THE COUNCIL Making the most of NIS—towards the effective implementation of Directive (EU) 2016/1148 concerning measures for a high common level of security of network and information systems across the Union.

30 JOINT COMMUNICATION TO THE EUROPEAN PARLIAMENT AND THE COUNCIL Resilience, Deterrence and Defence: Building strong cybersecurity for the EU.

31 Internet Protocol version 6 (IPv6) is the most recent version of the Internet Protocol (IP), the communications protocol that provides an identification and location system for computers on networks and routes traffic across the Internet. It provides a variety of security benefits relative to IPv4, its predecessor. See: IPv6 (accessed 26 October 2017).

- enhance research and development by establishing a new Research and Competence Centre;
- encourage growth of cyber security skills and training within Member States;
- promote cyber hygiene and awareness by creating a platform to share cyber awareness campaigns and encouraging Member States to make cyber awareness a priority;
- combat cybercrime by making EUROPOL a centre of excellence for cyber forensics and online investigations, committing €10.5million to fighting cybercrime;
- support law enforcement by making proposals on cross border exchange of e-evidence, and the role of encryption in criminal investigations;
- increase cyber defence by deepening EU-NATO cooperation on cyber security, hybrid threats and defence, and encourage Member State projects, creating a training platform, and research and development projects funded by the European Defence Fund;
- establishing an EU crisis response framework and investigation into an Emergency Response Fund to deploy expert teams during/post major cyber incident;
- improving international cooperation through bilateral dialogues, at which the establishment of a framework for conflict prevention and stability in cyberspace and the application of existing international law in cyberspace will be prioritised; and
- focusing capacity building on the EU neighbourhood and developing countries, by establishing an EU cyber capacity building network.

The Minister's Explanatory Memoranda of 18 October 2017 (ENISA)

3.40 On 28 September 2017 the Minister of State for Digital at the Department for Digital, Culture, Media and Sport (DCMS) provided the Committee with two explanatory memoranda: one in relation to the report evaluating ENISA and another regarding the proposed ENISA Regulation.

(i) ENISA evaluation report

3.41 In the Government's memorandum on the ENISA evaluation report,[32] the Minister states that DCMS "would largely agree with the findings of the report". He suggests that because the UK is has significant resources and capability in this field, the direct value it receives from ENISA is not substantial; the support ENISA provides smaller, less advanced Member States is nonetheless helpful in building capability and expertise across the EU. ENISA has also played a useful role in the implementation of the NIS Directive.

32 REPORT FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT AND THE COUNCIL on the evaluation of the European Union Agency for Network and Information Security (ENISA).

(ii) ENISA Regulation

3.42 In the Government's memorandum on the proposed replacement of the ENISA Regulation,[33] the Minister explains that a detailed analysis of the policy implications of the proposal has not been provided, and that:

> "Officials will assess the policy implications during the negotiations, which the UK will take part in while it remains a member of the EU."

3.43 On Brexit, in addition to the usual paragraph of legal boilerplate about the implications of exiting the European Union, the Minister states that negotiations on the proposed regulation will commence at the end of October, and are unlikely to conclude before the UK leaves the EU in 2019. He adds that the UK will therefore need to enter into negotiations to agree its future relationship with ENISA after the UK leaves the European Union.

3.44 The Minister does not express any clear subsidiarity concerns in relation to the proposed Regulation, stating that the Government believes that a certain degree of voluntary EU coordination is beneficial to manage the cross-border context of cyber risks. He states that "the current flexibility in the text means that the Government is content that the proposed measures remain proportionate to the need" and adds that the Government will further consider its position on subsidiarity during the negotiation process.

3.45 The Government's summary of the proposal notes that the role for ENISA in the context of crisis management, including the delivery of an EU cybersecurity blueprint for the delivery of cooperation in emergency cybersecurity incidents, is described as operational by the Commission and that this reference is likely to concern a number of Member States. However, the Minister notes that the detail of the text suggests that this is unlikely to constitute what the UK defines as a traditional operational role.

3.46 In a previous Explanatory Memorandum regarding the Commission's communication on cybersecurity, which trailed this initiative, the Government had expressed a strong preference for global standards developed in international fora:

> "With regards to the certification and labelling proposals, the UK has a long-standing position of support for open, global standards developed in international fora. We take this view because global standards enable UK industry to reach a global market, not just an EU market, and specifically in this instance because an EU standard will undermine an existing global standard. We would challenge any proposals that seek to create EU-only standards, or standards where the associated conformity checking can only be performed by/under the control of European bodies."[34]

3.47 It may therefore be appropriate to seek further information from the Government's views regarding the proposal, including its thinking about future UK-EU cooperation in the area of cybersecurity, as well as a clearer assessment of any tensions with global approaches to standardisation as well as the "operational" role that is envisaged for ENISA.

33 Proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on ENISA, the "EU Cybersecurity Agency", and repealing Regulation (EU) 526/2013, and on Information and Communication Technology cybersecurity certification (''Cybersecurity Act'').

34 EM 11013–16 Strengthening Europe's Cyber Resilience System and Fostering a Competitive and Innovative Cybersecurity Industry (Commission Communication) 11013/16, COM (16) 410.

The Minister's Explanatory Memoranda of 28 September 2017 (NIS)

3.48 In a separate memorandum on the Commission's communication on implementation of the NIS Directive,[35] the Minister (Matt Hancock) describes the Communication as "a brief commentary by the Commission on NIS Implementation [which] makes no substantive changes to our NIS implementation." He emphasises that the Government supports the overall aims of the NIS Directive—to increase the cyber security of member states across the EU and protect citizens and businesses online—and says that the Government is considering how best to implement the NIS Directive into UK legislation in a manner that delivers a more secure environment for the UK's essential services and digital service providers, balanced against a need to avoid placing unnecessary burdens on business. The UK's proposed implementation takes into account the issues raised by the Commission in their Communication.

3.49 On Brexit, the Minister states that the impact of the UK's departure from the European Union is being incorporated into the UK's transposition preparations. He states that the main impacts of departure are:

- the UK's membership of the Cooperation Group and CSIRT network;
- mandatory annual incident reporting requirements on Member States; and
- the potential impact on UK digital service providers if there is a transition to third country status.

3.50 The Minister states that the Government is looking at ways in which it can maintain membership of the Cooperation Group and CSIRT network, amending incident reporting to make it either voluntary or remove the requirement to report to EU institutions, as well as minimize any negative impacts on digital service providers.

The Minister's Explanatory Memoranda of 3 October 2017 (FCO)

3.51 Separately, the Minister for Europe and the Americas (Sir Alan Duncan) at the Foreign and Commonwealth Office has submitted an explanatory memorandum on the External Action Service's Joint Communication: Resilience, Deterrence and Defence: Building strong cybersecurity for the EU.[36]

3.52 The Minister states that the Communication is not a policy document but represents a recommended policy approach: Member States will subsequently give their view on the policy approach in the form of Council Conclusions. Any subsequent action requiring member state approval would be subject to the normal decision making procedures.

3.53 The Minister emphasises that the publication of this Communication demonstrates the importance the Commission is placing on cyber security, and states that this is something that the UK supports. The Minister adds that the overarching goal of the Communication is to make the EU proactive instead of reactive on cybersecurity issues and enumerates aspects of the strategy which the Government supports including: the

35 EM 12205/17.
36 EM 12211/17.

focus the Communication places on cyber resilience of the EU, Member States and the EU neighbourhood; improved international engagement to enhance our overall collective security, including with NATO; and cyber deterrence.

3.54 The Minister also highlights areas of possible concern, which include:

- the potential impact on trade and investment from the proposal for an EU certification framework;
- development of an operational role for ENISA where this may interfere with national processes; and
- the development of international law in cyberspace.

3.55 The Minister states that the Government will seek to influence the impact of these areas through the Council Conclusions, and also adds that there are areas of the Communication that are too vague to comment on at present, where the Government will seek to influence detailed proposals.

Previous Committee Reports

None.

4 Veterinary medicinal products

Committee's assessment	Politically important
Committee's decision	Not cleared from scrutiny; scrutiny waiver granted; further information requested
Document details	(a) Draft Regulation on the manufacture, placing on the market and use of medicated feed; (b) Draft Regulation amending Regulation 726/2004 on Community procedures for the authorisation and supervision of medicinal products; (c) Draft Regulation on veterinary medicinal products.
Legal base	(a) Articles 43 and 168(4)(b), Ordinary Legislative Procedure, QMV; (b) Articles 43 and 168(4)(c), Ordinary Legislative Procedure, QMV; (c) Articles 43 and 168(4)(b), Ordinary Legislative Procedure, QMV
Department	Environment, Food and Rural Affairs
Document Numbers	(a) (36338), 13196/14 + ADDs 1–3, COM(14) 556; (b) (36340), 13240/14, COM(14) 557; (c) (36344), 13289/14 + ADDs 1–3, COM(14) 558

Summary and Committee's conclusions

4.1 The European Union has in place a set of rules regulating the production, marketing, distribution and use of veterinary medicines and medicated feed. In response to concerns that the current rules were burdensome, were failing to deliver a functional single market and did not assure the availability of products, especially for small markets, the Commission proposed revisions in 2014.

4.2 The revisions aimed to:

- increase the availability of veterinary medicinal products;
- reduce administrative burdens;
- stimulate competitiveness and innovation;
- improve the functioning of the internal market; and
- address the public health risk of antimicrobial resistance (AMR).

4.3 Noting the Government's broad support for these proposals, the then Committee reported the proposals to the House as politically important in October 2014. Our predecessors then engaged in correspondence with the responsible Ministers.

4.4 Discussions proceeded very slowly until new impetus was given to the proposals by the Estonian Presidency. In the most recent letter, the Parliamentary Under Secretary of State (Lord Gardiner of Kimble) reports that consideration has accelerated. Agreement is expected at the Agriculture Council on 13 December.

4.5 The Minister indicates UK support for the overall package. He notes that the main concern for the UK is the requirement that veterinary medicines be dispensed only by qualified vets. This would mean that that the UK system allowing "Suitably Qualified Persons", as well as vets, to prescribe certain categories of veterinary medicines would need to be re-considered. The system is an important one for farmers in remote areas of the UK where there are insufficient numbers of vets.

4.6 The Government also has some concerns regarding proposals in the medicated feed legislation (document (a)) on limits for the "carry-over" of medicines into non-target batches of feed. While the Minister indicates support in principle, especially for antibiotics where carry-over may contribute to antibiotic resistance, there are concerns about increased costs. The UK's concerns are shared by other Member States and so the Minister remains hopeful that a sensible agreement can be reached.

4.7 The other significant provisions in the proposals are those pertaining to tackling anti-microbial resistance. The proposed provisions are in line with UK policy.

4.8 On the UK's exit from the EU, the Minister comments that it was now highly likely that the UK would leave the EU before the updated legislation must be applied. The medicated feed proposal is due to be applied one year after entry into force and the veterinary medicines proposal is due to be applied three years after entry into force. Noting that the UK is already at the forefront of the fight against antimicrobial resistance and this will continue to be a priority beyond the UK's EU membership, the Minister indicates that the Government would look carefully at the Regulations and the elements that it may be sensible to implement after the UK has left the EU.

4.9 **We consider these proposals to be very important, with potentially significant Brexit considerations. The provisions relating to anti-microbial resistance, bearing in mind the trade in animal products, and to restrictions on prescribing are of particular concern to us.**

4.10 **We note overall UK support for these proposals, but that the Government has concerns about proposed new restrictions on prescribing veterinary medicines and about the provisions on carry-over under the medicated feed proposal. We would welcome an update on the agreement reached on both of those issues at the Council meeting. We would also welcome a summary of the agreed provisions on anti-microbial resistance.**

4.11 **The Minister noted in correspondence that it was unlikely that the legislation would need to be applied before the UK's withdrawal from the EU, noting the one year and three year deadlines for the medicated feed and veterinary medicines proposals respectively. Given that the medicated feed proposal (document (a)) will need to be applied one year after entry into force, we ask the Government whether it accepts that this might need to be applied during a post-Brexit implementation period as proposed by the Prime Minister?**

4.12 **On the UK's withdrawal from the EU, we would welcome responses to the following additional points:**

- **the amount of trade in veterinary medicines and medicated feed between the UK and EU-27;**

- **the implications for the UK of separation from the EU's veterinary medicines regulatory framework, including the restrictions to tackle anti-microbial resistance, the proposed new common database and the requirements on authorisations and mutual recognition; and**
- **whether the UK would be likely to choose to maintain alignment with EU standards post-Brexit in any case.**

4.13 **We waive these proposals from scrutiny in advance of the Council meeting on 13 December. They remain under scrutiny pending responses to the issues raised above and an explanation of progress as well as the Government's expectations for negotiations with the European Parliament. We would welcome a response within four weeks.**

Full details of the documents

(a) Draft Regulation on the manufacture, placing on the market and use of medicated feed: (36338), 13196/14 + ADDs 1–3, COM(14) 556; (b) Draft Regulation amending Regulation 726/2004 on Community procedures for the authorisation and supervision of medicinal products: (36340), 13240/14, COM(14) 557; (c) Draft Regulation on veterinary medicinal products: (36344), 13289/14 + ADDs 1–3, COM(14) 558.

Background

4.14 Details on the background and content of the proposals, as well as on the Government's position, were set out in our Report of 22 October 2014.[37] The key points are summarised below.

4.15 When the then Committee considered the proposals at its meeting of 22 October 2014, it retained the proposals under scrutiny, noting the Government's support for them but awaiting further information on the progress of negotiations. Since then, our predecessors received update letters on 4 March 2015, 7 July 2015, 11 May 2016, 2 February 2017 and 28 March 2017.

Medicated Feed (document (a))

4.16 Medicated feeds containing antimicrobials and anti-parasites are an important way of treating disease in groups of farmed animals, especially pigs and poultry, as well as in domestic pets. The existing EU rules governing their manufacture, placing on the market and use were adopted before the creation of the single market. The freedom it provides Member States as regards national transposition has given rise to a number of problems.

4.17 The proposed revision would retain many of the previous provisions, whilst seeking to achieve greater clarity by measures such as: prohibiting the use of medicated feed containing microbials with the intention of preventing disease in food-producing animals, thus taking account of the severe public health risk posed by antibiotic resistance; and establishing maximum levels, related to the degree of risk involved, for the "carry-over" of active substances between different types of feed manufactured on the same production line.

37 Fifteenth Report (HC 219–xv) (2014–15) chapter 2 and chapter 3 (22 October 2014).

Veterinary Medicines (documents (b) and (c))

4.18 The EU rules which currently apply to the production, marketing, distribution and use of veterinary medicines are set out in two main instruments:

- Directive 2001/82/EC, which stipulates that such a medicine cannot be placed on the market of a Member State unless the competent authority has issued an appropriate marketing authorisation ("national authorisation"), and sets out the basis on which an authorisation granted in one Member State may be valid in other Member States ("mutual recognition"); and
- Regulation (EC) No. 726/2004, which sets out a centralised procedure under which products are simultaneously authorised by the Commission in all Member States on a pan-European basis.

4.19 The Commission proposed (document (c)) to repeal Directive 2001/82/EC, and put in place an up-to-date and proportionate body of legislation (as a Regulation) tailored to the specific needs of the veterinary sector. The new Regulation would also incorporate the centralised procedures for the granting of authorisations by the Commission. As a consequence, Regulation 726/2004 should be amended in order that it is focused wholly on human medicines (document (b)).

4.20 Much of the existing framework would be retained, with the application of a benefit-risk assessment continuing to be a key element in determining whether a product should be authorised, but the proposal would introduce a number of changes, including:

- the Commission would be empowered to establish rules excluding or restricting the use of certain antimicrobials in the veterinary sector;
- new restrictions would be imposed on the supply of antimicrobial veterinary medicines, a system would be set up to record and report on their use, and, where there is no authorised veterinary medicine for a particular species or disease, rules would be established for prescriptions, principally in order to address concerns relating to antibiotic resistance;
- rules would also be established for online sales (which would be encouraged in order to improve access to veterinary medicines);
- packaging and labelling simplifications;
- changes to the lengths of marketing authorisations—10–14 years for the initial authorisations, with particular flexibility for smaller markets, and renewals of unlimited duration;
- a single product database for all authorised veterinary medicines; and
- a harmonised EU procedure would be introduced for the authorisation of the clinical trials used to demonstrate a product's quality, safety and efficacy, and food producing animals used in such trials would not be permitted to enter the food chain, unless the product administered has already been authorised.

The Minister's letters of 20 July 2017

4.21 On the medicated feed proposal (document (a)), the Minister explained that the Estonian Presidency had proposed reopening discussions on the proposals in September 2017. The European Parliament had adopted its first reading position with 93 amendments to the proposal and focused on the controls surrounding the prescribing of antibiotics and the level of carry-over in batches of medicated feed.

4.22 Regarding the other proposals, a third "read-through" had continued under the Maltese presidency and the Estonian presidency had stated its intention to finalise the Council's position by October 2017 in order to start the negotiations with the European Parliament as soon as possible.

The Minister's letters of 1 November 2017

4.23 The Minister confirmed that discussions on the medicated feed proposal were re-opened in September. A Council position was expected to be agreed by the end of the year.

4.24 Progress on the other proposals had been slower than desired by the Presidency, but agreement was also still expected by the end of the year.

4.25 The Minister noted that removal of the veterinary aspects from Regulation 726/2004 on community procedures for the authorisation and supervision of medicinal products (document (b)) meant that it would be necessary to update the arrangements for adoption of tertiary legislation (delegated and implementing acts) related to human medicines to ensure consistency with the Lisbon Treaty.

4.26 On the UK's exit from the EU, the Minister commented that it was now highly likely that the UK would leave the EU before the updated legislation comes into force. He added:

> " The UK is already at the forefront of the fight against antimicrobial resistance and this will continue to be a priority beyond our EU membership. We will look carefully at the Regulations and the elements that it may be sensible to implement after the UK has left the EU."

The Minister's letter of 30 November 2017

4.27 The Minister notes that the Estonian Presidency has accelerated these negotiations, which have now lasted more than three years.

4.28 He notes that restricting the act of prescribing certain medicines to vets only is a new development in the negotiations, included in the latest draft text. The Minister explains that, under existing arrangements in the UK, "Suitably Qualified Persons" (SQPs) are able to write prescriptions for veterinary medicines classified as "POM-VPS"[38] but that the latest proposed changes would prohibit this. He adds:

> "At the time of writing, there are just short of 7000 trained and qualified SQPs registered in the UK and approximately 320 medicines classified as POM-VPS. These products generally prevent (i.e. vaccines) or treat endemic livestock diseases or parasite infestations, both internal (i.e. worms) or

38 Prescription Only Medicines able to be prescribed by a vet, pharmacist or suitably qualified person

> external (e.g. fleas, lice etc) that do not require a prior veterinary diagnosis (in the UK, SQPs also sell and give advice on similar products, classified as NFA-VPS, authorised for use in companion animals.)"

4.29 The Minister explains that, throughout the negotiations, the Government has made the case for provisions at EU level that are compatible with the existing, well-functioning UK distribution system for veterinary medicines. Circumstances vary across EU member states, although the UK is alone in openly allowing non-vets (i.e. SQPs) to prescribe certain veterinary medicines.

4.30 On anti-microbial resistance, measures are being introduced in both the veterinary medicines and medicated feed proposals to reduce the risk to the development of antimicrobial resistance:

> "The routine use of antibiotics to prevent disease will not be permitted. The Commission has proposed that the treatment of a group of animals to eliminate or minimize an expected outbreak of disease (metaphylactic use) will be allowed but routine prophylactic use (a medicine or course of action used to prevent disease) will not. There will need to be a change to a number of Summary of Product Characteristics (SPCs—detailed descriptions of a medicine's properties and the conditions for using it) as some antibiotics are currently indicated for preventative use. The proposals are consistent with the UK Antimicrobial Resistance strategy."

4.31 Regarding proposals in the medicated feed legislation on limits for the "carry-over" of medicines into non-target batches of feed, the Minister indicates support in principle, especially for antibiotics where carry-over may contribute to antibiotic resistance. The concern for the Government is the potential impact of the proposed carry-over limits on the economics of medicated feed production. While carry-over can be reduced, explains the Minister, by flushing the plant with un-medicated feed, this then becomes a waste product and therefore an added cost of production. Also of concern to the Government is the capacity of commercial labs to detect or quantify trace amounts of carried-over medicines when conducting regulatory compliance testing. Investing in such analytical capability may further add to the cost of manufacturing medicated feed. The Government's position is that carry-over should be kept to a minimum but the levels of permitted carry-over for each substance must be set according to sound science from the outset. The UK, and the majority of Member States, have argued for workable limits to be set and the UK remains hopeful that a sensible agreement can be reached.

4.32 While the UK continues to resist inclusion of the specific provisions highlighted above, the UK can still support the proposal as a whole.

Previous Committee Reports

Fifteenth Report HC 219–xv (2014–15) chapter 2 and chapter 3 (22 October 2014).

5 Mobility Package: road use charges

Committee's assessment	Politically important
Committee's decision	Not cleared from scrutiny; further information awaited
Document details	(a) Proposal for a Directive amending Directive 1999/62/EC on the charging of heavy goods vehicles for the use of certain infrastructures; (b) Proposal for a Directive on the interoperability of electronic road toll systems and facilitating cross-border exchanges of information on the failure to pay road fees in the Union ; (c) Proposal for a Directive amending Directive 1999/62/EC on the charging of heavy goods vehicles for the use of certain infrastructures, as regards certain provisions on vehicle taxation
Legal base	(a) and (b) Article 91; ordinary legislative procedure; QMV (b) Article 113 TFEU; special legislative procedure; unanimity
Department	Transport
Document Numbers	(a) (38792), 9672/17 + ADDs 1–4, COM(17) 275; (b) (38793), 9673/17 + ADDs 1–5, COM(17)280; (c) (38827), 10175/17 + ADDs 1–4, COM(17)276

Summary and Committee's conclusions

5.1 Different aspects of road charging are considered in these Mobility Package proposals, which seek to promote the Commission's high-level goals set out in its 2011 White Paper on transport. The broad principles of 'polluter pays' and 'user pays' run through these proposals, which are linked to the Energy Union package and other proposals related to low-emission transport.

5.2 **The Government has identified a number of issues in relation to these three proposals. One of these is the scope of the revisions on road charging, and whether it would run counter to the objective of countering congestion and air quality problems to make buses and coaches subject in principle to road charging. The case for bringing light commercial vehicles within the scope of the legislation is also questioned.**

5.3 **Other issues concerning the road charging proposals are whether the required phasing out of time-based charging would be appropriate for the UK, as it would lead to a loss of flexibility in policy options; and whether the higher costs that will be incurred by a wider range of vehicles can be justified, particularly when considering the role of the freight transport industry in the wider economy.**

5.4 **The Government notes that the UK's current time-based HGV levy, instituted in 2014, raises £200 million per year, of which EU drivers contribute around £50 million. The Government states that "it remains to be determined whether a distance based charging scheme could be designed that raises the same net revenue and be acceptable to stakeholders".**

5.5 **The proposals on European Electronic Toll Systems raise questions as to their relevance for the UK. The Government notes that the UK's geographical position in Europe may mean that providers may decide that there is an insufficient business case to extend services to the UK.**

5.6 **The Government also notes that it is possible that the Commission's proposals to standardise the type of road charging may end up becoming irrelevant if the goal of a single, interoperable electronic tolling system is achieved.**

5.7 **There is obvious uncertainty because of the UK's forthcoming exit from the EU as to whether these Directives will end up being applicable to the UK (although this could be the case if an implementation period extending the acquis is agreed). If the Directives do become applicable, the requirement in the EETS Directive to share vehicle registration data between Member States to aid better enforcement of toll charges across borders could raise data protection issues following the UK's departure from the EU. The extent to which the UK's future partnership agreement with the EU covers data sharing for such purposes would determine whether UK enforcement agencies will be able to receive and transmit vehicle registration data.**

5.8 **The Government also raises several subsidiarity questions, which it notes it will be considering in its consultations and impact assessment. The issues the Government identifies relate mostly to the proportionality of what is being proposed. They do not, in large, address whether the proposed actions are better taken at EU level rather than left to Member States. However, the various objectives of the proposals are inherently cross-border in nature and difficult for Member States to achieve on their own: for example, the equivalent reduction of high CO_2 emissions across the EU, tackling discrimination in respect of non-resident drivers, reducing costs and burdens arising from the non-interoperability of EETS across the EU and increasing fine enforcement and deterrence in relation to non-resident drivers using EETS. In the case of (a) and (c) the proposals simply seek to make more effective existing EU legislation. In any event the eight week deadlines for the House to submit a Reasoned Opinion to the EU on these proposals all expired in September before our formation as a Committee and we do not think there are clear subsidiarity grounds to justify entering into political dialogue with the Commission instead at this stage.**

5.9 **Of those subsidiarity issues we would be grateful for further clarification from the Government in the area of vehicle taxation. The Explanatory Memorandum states at one point that the Government "will be considering the longstanding UK position that EU Member States should have the flexibility to set tax rates unless there is a strong case for having EU rules, and whether this proposal is consistent with that principle".**

5.10 **However, elsewhere in the document the Government states that "the Commission argues that in the absence of EU action, Member States would continue to be obliged to apply the minimum vehicle tax even if they introduced or intend to introduce a more appropriate instrument to recover infrastructure costs, directly related to the individual use of infrastructure. The government agrees that this is the case".**

5.11 **This latter statement suggests strongly that the Government accepts the case for EU action in amending the rules on vehicle taxation. We would be grateful for confirmation as to whether this is the case.**

5.12 **Other questions of interest include whether it is justified to bring within the scope of the legislation occasional, foreign drivers; the necessity of requiring that EETS systems must be compatible with the EU's GALILEO system (and its potential implications for UK suppliers of such systems post-Brexit), and whether estimated HGV carbon emissions are a sufficiently accurate basis for varied road charging, given that the methodology for such estimates is not yet entirely reliable.**

5.13 **Given that the Government has not yet concluded its consultations on the proposals with interested parties, and will need to carry out an impact assessment as well as subsidiarity assessment, we retain these documents under scrutiny until the Government has reported back to us on the issues raised in its Explanatory Memorandum, as well as on the possible implications of data protection requirements post-Brexit.**

Full details of the documents

(a) Proposal for a Directive amending Directive 1999/62/EC on the charging of heavy goods vehicles for the use of certain infrastructures: (38792), 9672/17 + ADDs 1–4, COM(17) 275; (b) Proposal for a Directive on the interoperability of electronic road toll systems and facilitating cross-border exchanges of information on the failure to pay road fees in the Union : (38793), 9673/17 + ADDs 1–5, COM(17)280; (c) Proposal for a Directive amending Directive 1999/62/EC on the charging of heavy goods vehicles for the use of certain infrastructures, as regards certain provisions on vehicle taxation: (38827), 10175/17 + ADDs 1–4, COM(17)276.

Background

5.14 These three documents concern proposals to update EU legislation on road charging. They aim to promote sustainable and equitable road transport through wider application of the 'user pays' and 'polluter pays' principles – both longstanding EU policy objectives.

(a) Proposal for a Directive amending Directive 1999/62/EC on the charging of heavy goods vehicles for the use of certain infrastructures ('Eurovignette Directive')

5.15 The Eurovignette Directive established the legal framework for Member States that have distance-based and time-based user charges for heavy goods vehicles (HGVs). Its aim was to make HGVs pay for the damage caused to roads, and it set minimum levels of vehicle taxes and specified the variation of charges according to the environmental performance of vehicles.

5.16 The Commission has identified that road transport is responsible for 17% of the EU's CO^2 emissions, and that the current rate of uptake of low and zero emission vehicles is insufficient to meet its 2030 climate and energy targets. In addition it has found that the quality of roads in the EU is degrading, due in part to a 30% decrease in public spending on road maintenance between 2006 and 2013.

5.17 In addition, the Commission has concluded that the use by Member States of time-based road charges (vignettes), as well as being ineffective in reducing congestion or incentivising cleaner transport, also discriminates against occasional, foreign drivers.

While 24 Member States implement some form of road charging, the Commission's evaluation has found significant disparities in national road charging policies, and has concluded that this lack of harmonisation results in administrative burdens for public authorities and road users.

5.18 The proposals seek to contribute to the reduction of CO^2 emissions in transport via pricing; address degradation of road quality; ensure that road charging schemes do not discriminate against non-resident motorists; and use road charging as a more effective tool in reducing air pollution and congestion.

(b) Proposal for a Directive on the interoperability of electronic toll systems and facilitating cross-border exchange of information on the failure to pay road fees in the Union (recast) ('EETS Directive')

5.19 Directive 2004/52/EC mandated the establishment of a European Electronic Toll Service (EETS) by which road users could, through a single contract with an EETS provider, and using a single on-board unit, pay electronic tolls throughout the EU. The Directive was accompanied by Commission Decision 2009/750/EC, which further defined the EETS.

5.20 The objectives of the legislation were to establish technical, contractual and procedural interoperability of electronic tolls throughout the EU, which would have the benefit of:

- reducing for road users the bother and costs of compliance with the requirement to pay tolls when travelling in the EU;
- reducing for road operators the costs of set up, operation and administration of electronic fee collection systems;
- encouraging the integration of on-board units with other standardised on-board equipment such as digital tachographs; and
- allowing future generations of tolling systems to benefit from the flexibility of satellite-based tolling, through the European satellite positioning systems (EGNOS and GALILEO).

5.21 The EETS Directive specified that all new electronic toll systems requiring the installation of on-board equipment and brought into operation after January 2007 should use one of three specified technologies (satellite position, mobile communications or microwave technology). EETS was to be provided to heavy duty vehicles by October 2012 and to cars by October 2014.

5.22 Member States were required to put in place the necessary regulatory framework for the operation of EETS; toll chargers (road operators) were to accept on a non-discriminatory basis all interested EETS providers and their certified equipment; EETS providers were required to provide their services in all electronic toll domains in the EU within 24 months of their registration by their Member State of establishment, and EETS users (road users) were to ensure the accuracy of all data provided and to comply with their obligation to pay tolls.

5.23 The Commission conducted an evaluation in 2015 to 2016, which found that the legislation had failed to deliver on most of its objectives. A European Electronic Toll Service has not been set up, and there has been hardly any progress on interoperability; on-board units have not been integrated with other vehicle devices; and, despite a reduction in the cost of on-board technologies, the costs of electronic tolling for toll chargers and road users has fallen very little.

5.24 The evaluation identified the following causes for the failures of the legislation:

- EETS providers face many barriers to entry into national markets, including discriminatory treatment by authorities, cumbersome registration procedures, and differing technical specifications in each market;
- the requirement in the Directive that EETS providers must provide their services in all Member States within 24 months of official registration is an unworkable requirement which has deterred registration;
- lack of specification of respective obligations of toll chargers and Member States in relation to EETS providers, which has allowed national barriers to remain in place without infringing EU law;
- an obligation to provide the light-duty vehicle market with costly satellite-based on-board units, despite the fact that at present electronic tolling systems for such vehicles do not use satellite positioning;
- lack of provision in the legislation for enforcing tolls on vehicles registered in another country; and
- the EETS Directive and related Decision are inconsistent with each other, as each imposes different requirements on the parties responsible for deploying EETS: the Directive assigns responsibility to national governments and toll charges, while the Decision assigns it to EETS providers.

(c) Proposal for a Directive amending Directive 1999/62/EC on the charging of heavy goods vehicles for the use of certain infrastructures, as regards certain provisions on vehicle taxation ('vehicle taxation Directive)

5.25 The Eurovignette Directive sets minimum levels of vehicle taxes for HGVs. The Commission has concluded that vehicle taxes, which reflect registration by the taxpayer rather than use of infrastructure, are not effective in incentivising cleaner and more efficient road operations, or in reducing congestion.

5.26 The Commission believes that vehicle taxes may also act as an obstacle to the introduction of tolls. Since the promotion of distance-based tolls is a key feature of the revisions to the Eurovignette Directive, the Commission believes that giving Member States the ability to reduce charges relating to ownership is now required.

The Commission's Proposals

(a) 'Eurovignette Directive'

5.27 The Commission believes that new rules are necessary to contribute to the reduction of CO^2 emissions from transport. The key change is that all vehicles will be brought within the scope of the legislation. The Commission notes that while cars and vans cause less damage to road infrastructure than HGVs, passenger cars "are the source of about 2/3 of external costs (including the cost of climate change, air pollution, noise, accidents and other negative impacts) generated by road transport, or about 1.8–2.4% of GDP".

5.28 The other elements of the proposed changes are:

- removal of optional exemption for HGVs under 12 tonnes;
- phasing out of time-based charging by 2023 for HGVs and by 2027 for other vehicles, and their replacement by distance-based charges, as the former are not effective in encouraging cleaner transport or in reducing congestion;
- phasing out of charges based on the EURO emissions class of a vehicle, as this classification is expected to become obsolete by 2020;
- differentiation of charges by vehicles' CO^2 emissions levels, with zero emissions vehicles receiving a 75% discount;
- allowing for extra congestion charges, with revenues to be allocated for projects addressing the sources of congestion; and
- requiring Member States to report annually on the use of revenues from road charges, so as to incentivise the use of such revenues for the maintenance and development of transport infrastructure;

(b) 'EETS Directive'

5.29 The Commission proposes the following changes for a recast of the Directive:

- adding as an objective the facilitation of the cross-border exchange of information on failure to pay road fees in the EU, in addition to the original objective of ensuring the interoperability of electronic road toll systems. This would require national vehicle registration authorities to provide vehicle owner details on request to enforcement authorities in another Member State, and in this context, a procedure for the cross-border exchange of information on toll offenders is set out, adapting provisions of Directive (EU)2015/413 (on facilitating cross-border exchange of information on road-safety-related traffic offences) to the tolling context;
- clarification that the rules only apply to tolls which require the installation or use of on-board equipment, i.e. not 'barrier' tolls;
- removal of the obligation on EETS providers to make products suitable for all vehicles, with a choice now permitted between heavy-duty and light-duty vehicles;

- EETS providers to be permitted to provide light-duty vehicles with systems using appropriate, i.e. non-satellite or mobile communications, technology;
- removal of the requirement for EETS providers to have contracted with toll chargers in all Member States within 24 months;
- authorising the Commission to amend by delegated act the list of technologies that can be used for electronic toll transactions. This is in recognition of the fact that such technologies can become obsolete rapidly;
- requiring Member States to provide the Commission with the data necessary to evaluate the effectiveness of the system for exchanging information on those who fail to pay road charges; and
- an update of applicable definitions, to ensure clarity on respective roles and obligations.

5.30 The recast Directive maintains, however, the requirements that satellite equipment provided must be capable of working with the EU's GALILEO system.

(c) Vehicle taxation Directive

5.31 The Commission proposes to allow Member States more scope to lower vehicle taxes, by reduction of the minimum level set out in the Directive. The amendment enables the gradual reduction of the minimum level to zero, in five steps (20% reduction each year) taken over five consecutive years.

5.32 The Commission's Explanatory Memorandum notes that the need to minimise the risk of distortions of competition between transport operators established in different Member States means that the proposed reduction in taxation must be gradual.

5.33 The Commission notes that the EU shares competence with Member States to regulate in the field of transport, but that the gradual decrease of existing minimum taxation level fixed by the Union can only be amended by the Union itself.

5.34 It goes on to state that "without EU intervention, Member States would continue to be obliged to apply the minimum vehicle tax even if they have introduced or intend to introduce a more appropriate instrument to recover infrastructure costs, directly related to the individual use of infrastructure".

The Government's Explanatory Memorandum

5.35 Jesse Norman, Parliamentary Under Secretary of State for Transport, in an Explanatory Memorandum of July 2017, informs us that the Government has not yet been able to consult on these proposals, and will be seeking the views of the road transport industry, Devolved Administrations and other interested parties.

5.36 He notes, however, that:

> "the negotiations on road haulage will ultimately determine whether or not the road charging proposals apply to the UK, but if they were to do so there would be an impact on what sort of charges and tolls could apply in the UK. In particular, the existing HGV road user levy, introduced in 2014, would be impacted as it is a time-based charge that excludes HGVs under 12 tonnes."

5.37 The Parliamentary Under Secretary is also able to provide some initial views on policy implications:

Eurovignette Directive

5.38 The Government believes that the Commission's proposals "would probably mean higher charges, for a wider range of vehicles, because the running and set-up costs tend to be higher for distance based than for time based charging".

5.39 The Explanatory Memorandum states that the Government will consider the following questions as part of its analysis:

- Would the proposals provide Member States with sufficient flexibility to introduce road charging that is appropriate for individual needs, priorities and circumstances, in particular in relation to the phase-out of time-based charging?
- Would requiring buses and coaches to be subject to the same charges as HGVs be counterproductive, given their role in tackling congestion and air quality problems?
- Would requiring HGVs from 3.5 tonnes to be included in an HGV charging scheme place an unnecessary burden on small vehicle operators, with no significant gain?
- Would varying HGV road charges according to CO^2 emissions prove robust, given that the methodology for estimating these emissions is not yet proven?
- Could the Commission's objective of ensuring that charging schemes become more similar to each be unnecessary, given that a successful interoperable EETS would allow road users to use a single service that pays for all electronic tolls?

EETS Directive

5.40 The Explanatory Memorandum highlights the following questions:

- given that the UK is geographically on Europe's periphery, EETS providers may decide that there is no business case to include UK tolls and charges within their service;
- the requirement for information on vehicle owners to be shared across national boundaries to aid enforcement of road user charges could help ensure higher compliance rates for UK tolls and charges, but could also impose a cost to the Driver Vehicle and Licensing Agency. Should the costs of providing this information be borne by the DVLA or by the requesting enforcement authority; and
- will allowing EETS providers a choice over which tolls and charges to include in their service encourage a market-led approach and reduce barriers to entry.

Vehicle taxation

5.41 The Explanatory Memorandum notes that:

> "in reaching a view on these proposals, the Government will be considering the longstanding UK position that EU Member States should have the flexibility to set tax rates unless there is a strong case for having EU rules, and whether this proposal is consistent with that principle."

Subsidiarity issues

5.42 The Government agrees with the Commission that any adaptation of existing rules on road charging can only be carried out by the Union. The Explanatory Memorandum notes the Commission's arguments that the three sets of proposals comply with the subsidiarity principle and states that it will take the following points into account when assessing the issue:

- whether action at EU level is required to address the problems (air quality, CO^2 emissions, degrading road infrastructure and congestion) or whether EU action would be more effective than Member State action, since these problems are arguable local in nature;
- is the Commission's view that legislation is required to ensure foreign drivers do not face discriminatory charges proportionate?
- the Commission's justification for extending road charging rules to buses and coaches is on the basis that rail transport already faces charging for infrastructure use, but will not actually require buses and coaches to be charged;

5.43 On vehicle taxation, the Government states:

> "on the proposals relating to the removal of minimum rates for VED [vehicle excise duty] (and its equivalent in other countries) the Commission argues that in the absence of EU action, Member States would continue to be obliged to apply the minimum vehicle tax even if they have introduced or intend to introduce a more appropriate instrument to recover infrastructure costs, directly related to the individual use of infrastructure. The Government agrees that this is the case."

5.44 This appears to contradict the statement at paragraph 5.41, since the above suggests strongly that the Government accepts that Union-level action on vehicle taxation in this instance is the most appropriate.

5.45 In any event, the Explanatory Memorandum notes that the UK is "close to, or at, the current minimum levels of VED for some categories of vehicles".

5.46 On EETS, the Government notes the Commission's argument that EU action is justified because individual Member States lack incentive to improve the operation of tolling systems across national boundaries, and because cross-border enforcement of tolls has not been effective since it requires bilateral data-sharing agreements.

5.47 The Government is also considering whether the Commission's proposed requirement that electronic road toll systems be compatible with the GALILEO system is "proportionate or necessary".

Impact assessment

5.48 The Government states that its interim view of the Commission's impact assessment,

> "suggests that the modelling assumptions that underpin their work may be optimistic. The revenue projections seem high, as do the projected benefits, and it is not clear how they would apply to the specific circumstances of the UK."

5.49 The Explanatory Memorandum adds that it is unclear to the Government whether the Commission has properly considered the role that the freight transport industry plays in the wider economy, noting that hauliers may have only limited power to pass on increases in costs arising from the proposals.

Financial implications

5.50 The Government notes that if the UK were required to comply with the proposals, there would be costs involved in designing future road tolls and charging systems in particular ways.

5.51 It adds that the current HGV road user levy raises approximately £200 million from UK and foreign vehicles, with EU drivers contributing around £50 million of this sum. The Explanatory Memorandum states that:

> "it remains to be determined whether a distance based charging scheme could be designed that raises the same net revenue and be acceptable to stakeholders (the proposal to eliminate minimum VED levels would create more flexibility to do so however)."

Previous Committee Reports

None.

6 Rail passengers' rights and obligations

Committee's assessment	Legally and politically important
Committee's decision	Not cleared from scrutiny; further information requested; drawn to the attention of the Women and Equalities Select Committee
Document details	Proposal for a Regulation of the European Parliament and of the Council on rail passengers' rights and obligations (recast)
Legal base	Article 91(1) TFEU; Ordinary legislative procedure; QMV
Department	Transport
Document Number	(39062), 12442/17 + ADDs 1–3, COM(17) 548

Summary and Committee's conclusions

6.1 On 27 September 2017 the European Commission published a proposed recast of the existing Regulation on rail passengers' rights and obligations.[39] The proposal aims to increase the uniformity of the implementation of rail passengers' rights across the EU, make targeted improvements to the passenger protections afforded, and reduce certain burdens on rail operators so that rail is not at a disadvantage relative to other modes of transport.

6.2 The current EU legal framework in this area—Regulation 1371/2007[40] on rail passengers' rights and obligations—aims to protect rail passengers in the EU by establishing common minimum rules throughout Europe. At present, passengers have rights to information, reservations and tickets, assistance, care and compensation in the event of delay or cancellation, free-of-charge assistance (for persons with disabilities and/or reduced mobility), compensation in the event of an accident, and a system of complaint-handling national enforcement bodies (NEBs).

6.3 The Commission is concerned that these protections are not uniformly applied throughout the EU, because the Member States are permitted to exempt a wide range of domestic services (apart from certain mandatory requirements) from the Regulation's application: long-distance services may be exempted until 2024; urban, suburban and regional services may be exempted for an unlimited period; and services of which a significant part is operated outside the EU may be exempted for renewable periods of five years, indefinitely. The Government has applied all of these exemptions, although they were not renewed in 2014 in Northern Ireland, where Regulation 1371/2007 now applies in full.

6.4 The Commission observes that only five Member States currently apply the Regulation in full, with the others having exemptions in place to varying extents. They consider

39 Proposal for a Regulation of the European Parliament and of the Council on rail passengers' rights and obligations (recast) 12442/17, COM(17) 548 http://europeanmemoranda.cabinetoffice.gov.uk/files/2017/09/12442–17.pdf.

40 Regulation (EC) No 1371/2007 of the European Parliament and of the Council of 23 October 2007 on rail passengers' rights and obligations http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32007R1371&from=en.

that this deprives passengers of their rights, and that the scope for exemptions should therefore be restricted. The proposal therefore brings forward the removal of exemptions for long-distance services from the current date of 2024 to 2020. It also proposes removal of exemptions for *cross-border* urban, suburban and regional services.

6.5 The Commission states that its proposal seeks to strike a balance between strengthening rail passenger rights and reducing the burden on railway undertakings. It aims to strengthen rail passengers' rights through the introduction of a general clause prohibiting any form of discrimination; a requirement that basic information about rights be provided at booking and during the passenger's journey; a requirement that operators "make all reasonable efforts to make through-tickets available", including to other operators; giving passengers who purchase multiple separate tickets the same rights as if they had purchased a single ticket (unless informed otherwise); and clarifying the complaint-handling process.

6.6 The proposal modifies existing requirements in relation to persons with disabilities and reduced mobility (PRMs). Changes include improving rights to assistance on trains and in stations, making clearer the rights of PRMs to be accompanied by a personal assistant or assistance dog, and ensuring that, where information requirements apply, information is available in accessible formats. These changes align the regulation with the United Nations Convention on the Rights of Persons with Disabilities.[41]

6.7 To reduce the burden on railway undertakings, the proposal introduces a *force majeure* clause that applies in situations caused by "severe" weather conditions and "natural disasters". The Commission considers that the proposed amendment would help improve the competitiveness of the rail sector and reduce financial burdens. The proposed Regulation also enables railway undertakings to use a new right of redress if delays are caused by a third party's fault or negligence.

6.8 On 19 October 2017 the Parliamentary Under Secretary of State (Paul Maynard) submitted an Explanatory Memorandum to Parliament for scrutiny.[42] The Minister states that the Government shares the Commission's objective of strengthening the rights of rail passengers and supports, in principle, the proposal's aim of standardising and improving passenger rights. He states that the Government believes that it is appropriate for the Commission to legislate in this area.

6.9 In terms of the impact on UK stakeholders, the Minister observes, somewhat vaguely, that "most" of the requirements of the current (2007) Regulation are already met or exceeded through domestic rail provisions. However, the Minister does not provide a clear sense of the extent to which the proposal's provisions are covered by domestic rail provisions, or what its impact will be. He acknowledges that the Government needs to "consider carefully" the detail of the proposals, and to consult with external stakeholders.

6.10 In relation to the UK's withdrawal from the European Union, the Minister states that the rights put in place by this proposal would apply equally to all rail passengers and therefore benefit rail passengers who are not EU/EEA citizens.

41 Convention on the Rights of Persons with Disabilities (CRPD) https://www.un.org/development/desa/disabilities/convention-on-the-rights-of-persons-with-disabilities.html.

42 Explanatory Memorandum from the Department of Transport (19 October 2017) EM 12442/17.

6.11 No implementation period is envisaged, so the Regulation would enter into force almost immediately after its publication in the Official Journal of the European Union. Depending on how rapidly progress is made, it is therefore very possible that the Regulation will become directly applicable in the UK either before it leaves the EU or during the Prime Minister's proposed Implementation Period.

6.12 **The proposed recast of the rail passenger transport rights and obligations Regulation is a substantial update of the existing Regulation, which dates back to 2007. The proposal would scale back the exemptions that are currently allowed, in order to improve the uniformity of the implementation of rail passenger rights throughout the EU. The proposal seeks to clarify and strengthen many aspects of rail passenger rights, particularly for persons with disabilities or reduced mobility. Finally, the proposal seeks to reduce certain burdens on rail operators, by introducing a *force majeure* clause for railway undertakings (as for other modes of transport) and granting them a right of redress.**

6.13 **The Government indicates that it supports the proposal's objectives and considers it appropriate for the EU to legislate to achieve them. However, it also acknowledges that detailed work on the proposal is still required and that it is seeking input from a range of stakeholders. In the meantime, there is a distinct lack of clarity regarding the impact that the proposed Regulation will have in the UK. For example, although the Government observes that "most" of the requirements of the *current* Regulation are already met or exceeded through domestic rail provisions, it does not specify which of the new requirements, if any, are not, and would constitute an additional right/obligation. The Government does not explain what effect limiting the scope of the current exemptions would have, in terms of UK services to which the entirety of the Regulation would subsequently apply. No analysis is provided of provisions in Articles 22 and 23, which appear to require that assistance for PRMs be available at all times when rail services operate, both in station and on board—potentially a highly significant provision.**

6.14 **We therefore request:**

- **clarification of which currently exempted rail services in the UK will be brought into the scope of the proposal;**
- **a list of the specific additional requirements the proposed Regulation will introduce that are not met by current UK law;**
- **a summary of any specific rights or other benefits that the Regulation will provide to persons with disabilities and reduced mobility (PRMs) that are not currently provided by UK law;**
- **clarification of the apparent requirement, contained in Articles 22 and 23, that assistance for PRMs be available at all times when rail services operate, both in station and on board; and**
- **an assessment of whether the Commission's view that big market players, by selling through-tickets on their own services only, keep new entrants who cannot offer through-journeys out of the market, is applicable to parts of the UK rail market, and an assessment of the significance and likely impact of the proposed requirement in Article 10 that railway undertakings and ticket vendors "make all reasonable efforts to make through-tickets available".**

6.15 **We welcome the Minister's assessment that the Regulation would have benefits for non-EU/EEA rail passengers travelling in an EU or EEA Member State. Nonetheless, in view of the UK's impending withdrawal from the EU, we request a more detailed account of these implications. The Committee asks for:**

- **clarification regarding whether, when the Regulation ceases to be directly applicable to the UK, there could under any circumstances be a reduction in any of the protections the proposed Regulation would otherwise afford to UK citizens and/or their enforceability;**
- **clarification of whether, when the Regulation ceases to be directly applicable to the UK, UK railway undertakings will be subject to reduced legal obligations to EU citizens to whom they sell tickets and provide services, meaning that EU citizens would have reduced rail passenger rights in the UK; and**
- **an account of what impacts and implications exiting the EU raises specifically for stakeholders in Northern Ireland, given that a number of Northern Ireland-Republic of Ireland services are in operation, and (unlike the rest of the UK) Northern Ireland Ministers opted not to continue to apply the exemptions in 2014.**

6.16 **We ask the Government to provide the Committee with responses to the above questions, along with updates regarding the Government's developing policy position in relation to the proposal, as well as its financial implications, by 24 January 2017 (or earlier if progress in Council requires it). In the meantime we retain this proposal under scrutiny and draw it to the attention of the Women and Equalities Select Committee.**

Full details of the documents

Proposal for a Regulation of the European Parliament and of the Council on rail passengers' rights and obligations (recast): (39062), 12442/17 + ADDs 1–3, COM(17) 548.

Background

The 2007 Regulation[43]

6.17 Regulation 1371/2007 on rail passengers' rights and obligations aims to protect rail passengers in the EU. It has been in force since 2009. The chief effects of this Regulation were to:

- guarantee disabled persons and persons with reduced mobility non-discriminatory access to trains and assistance;
- strengthen rail passengers' right to compensation when their luggage gets lost or damaged (up to about €1285 per piece of luggage);

43 Regulation (EC) No 1371/2007 of the European Parliament and of the Council of 23 October 2007 on rail passengers' rights and obligations http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32007R1371&from=en.

- strengthen rail passengers' right in case of death or injury through an advance payment to meet immediate economic needs. This advance payment amounts to at least €21000 per passenger in the event of death;
- reinforce rail passengers' right to compensation in case their journey gets delayed or cancelled: the minimum compensation amounts to 25% of the ticket price for delays between one and up to two hours and to 50% of the ticket price for delays of two hours and more;
- give rail passengers the right to be informed comprehensively before and during their journey, for example about delays;
- make it easier for rail passengers to buy tickets;
- impose an obligation on rail companies and station managers to ensure passengers' personal security in railway stations and on trains;
- oblige rail companies to set up a complaint handling mechanism for the rights and obligations covered by the new regulation;
- oblige Member States to ensure that passengers can lodge a complaint to an independent body, if passengers consider that their rights have not been correctly implemented; and
- extend the existing rights of passengers under the Convention for the International Carriage by Rail (COTIF) which only covers international transport, in principle, to all domestic train services.

Exemptions

6.18 Member States were also allowed to exempt the following domestic services from the application of the Regulation (apart from certain mandatory requirements):

- Long-distance services, for a maximum of five years, renewable twice, i.e. until 2024;
- Urban, suburban and regional services, for an unlimited period; and
- Services of which a significant part is operated outside the EU, for a renewable period of five years (de facto no time limit).

The proposal[44]

6.19 The chief provisions contained in the proposed Regulation are:

> *Limitation of exemptions to ensure uniform application of the rules (Article 3)*—The Commission has noted that only five Member States currently apply the Regulation in full, with the others having exemptions in place to varying extents. They consider that this deprives passengers of their

44 Regulation (EC) No 1371/2007 of the European Parliament and of the Council of 23 October 2007 on rail passengers' rights and obligations http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32007R1371&from=en.

rights, and that the scope for exemptions should therefore be restricted. The proposal accordingly removes exemptions for *cross-border* urban, suburban and regional services; brings forward the removal of exemptions for long-distance services from the current date of 2024 to 2020; and, for services a substantial part of which are operated outside the EU, requires that Member States grant exemptions only if they can prove that passengers are adequately protected on their territory. Some core provisions of the Regulation (non-discriminatory conditions; availability of tickets, through-tickets and reservations; liability for passengers and luggage; persons with disabilities and reduced mobility) are never exempted;

- *Force majeure (Article 17)*—Railway undertakings currently have to compensate passengers for delays caused by force majeure. The proposal introduces a force majeure clause that applies only in situations caused by "severe" weather conditions and "natural disasters";

- *Prohibition of discrimination (Article 5)*—The proposal introduces a general clause prohibiting any form of discrimination, e.g. based on nationality, residence, location or currency of payment. This aligns rail with other modes of transport. Passengers who feel that their rights have be infringed can turn to national enforcement bodies (NEBs) rather than having to initiate court proceedings under Article 18 of the Treaty on the Functioning of the EU (the general principle of Non-discrimination);

- *Fuller information about passenger rights (Article 30)*—The proposal requires that they be given basic information on their rights at booking, e.g. printed on the ticket or electronically, and during their journey. Notices informing passengers of their rights have to be placed in prominent positions in stations and on board. This includes clarifying rights where passengers will use connected services for one journey, whether they buy one through-ticket or several separate tickets;

- *Through-tickets: greater availability and fuller information (Article 10)*—By selling "through-tickets" (one ticket that covers all legs of a multi-leg journey) on their own services only, big market players keep new entrants who cannot offer through-journeys out of the market. The proposal requires railway undertakings and ticket vendors to make all reasonable efforts to make through-tickets available, including for journeys across borders and with more than one rail undertaking. The proposal therefore provides for passengers to be given fuller information on through-tickets;

- *Multiple separate tickets: equivalent rights (Article 10)*—Selling separate tickets for journey segments allows railway undertakings to bypass obligations relating to compensation, re-routing and assistance. The revised Regulation establishes that customers who purchase separate tickets in this way are entitled to the same rights as if they had purchased a single through-ticket, unless the passenger is explicitly informed otherwise in writing. The railway undertaking must prove that it informed passengers where their passenger rights do not apply to the whole journey but only to its segments; and

- *Complaint-handling process (Article 33)*—The proposal would require ticket vendors, station managers and infrastructure managers of certain stations (as well as railway undertakings) to put in place procedures for complaint handling. It proposes a deadline for complaints (two weeks for acknowledgement, three months for completing the procedure, extendable to six months for complex cases) and clarifies the responsibilities and competencies of national authorities responsible for the application and enforcement of passenger rights. Passengers should complain to rail operators in the first instance and then, if necessary, to an alternative dispute resolution body or an NEB. The proposal specifies NEBs' responsibilities in cross-border cases and requires them to cooperate effectively.

6.20 A range of changes are proposed in relation to persons with disabilities and reduced mobility (PRMs), in Chapter V (*Articles 10 and 20–26*), as set out below:

- where there is no ticket office or accessible ticketing machine in the station of departure, PRMs shall be permitted to buy tickets on board the train at no extra cost *(Article 10)*;
- the proposal extends PRMs right to be accompanied to their personal assistant and/or assistant dog *(Article 20)*;
- if an undertaking exercises a derogation to sell a ticket to or make a reservation for a PRMs, subject to non-discriminatory access rules referenced in Article 20(2), it must make reasonable efforts to propose alternative transport options (*Article 21*);
- where information requirements apply, information must be provided in accessible formats in line with the requirements proposed in the European Accessibility Act[45] *(Article 22)*;
- assistance to PRMs must be available at railway stations and on board during all operating hours *(Articles 22–23)*;
- PRMs will be enabled to only make one advance request for assistance to cover their whole journey where their ticket allows separate journeys, with railway undertakings, station managers, ticket vendors and tour operators cooperating in order to facilitate this *(Article 24);*
- when railway undertakings/station managers cause loss or damage to mobility equipment, assistive devices and assistant dogs they are liable for and must compensate that damage, and provide temporary replacements. Member States can no longer exempt compensation for such equipment *(Article 25)*; and
- requiring railway undertakings to provide disability awareness training to staff and to PRMs and to organisations representing them, upon request. Training must be given to staff on recruitment by way of regular refresher training *(Article 26)*.

45 Proposal for a Directive of the European Parliament and of the Council on the approximation of the laws, regulations and administrative provisions of the Member States as regards the accessibility requirements for products and services COM/2015/0615 final—2015/0278 (COD) http://eur-lex.europa.eu/legal-content/EN/TXT/DOC/?uri=CELEX:52015PC0615&from=EN.

6.21 Other changes which are proposed include:

- *Use of Delegated Acts to ensure consistency with international rules (Articles 36 to 37)*—The EU is now a member of the Intergovernmental Organisation for International Carriage by Rail (OTIF). To ensure consistency with the Convention concerning International Carriage by Rail (COTIF) and the International Convention for the transportation of Passengers (CIV), the proposal gives the Commission the power to update Annex I to take account of amendments to the CIV. The Commission will also be enabled to adopt delegated acts to adjust the minimum advance payment amount payable in the event of death or injury in line with inflation;

- *Contingency plans for station and infrastructure managers (Article 18)*—Under the 4th railway package, railway undertakings have to draw up contingency plans to protect and assist passengers in the event of major transport disruptions. No such obligations exist for other actors. To reduce the burden on railway undertakings, the proposal obliges station and infrastructure managers also to have contingency plans. Member States will decide on the detail and coordination of the plans with national authorities, for example; and

- *Right to redress for railway undertakings (Article 19)*—Depending on applicable national rules, railway undertakings may have difficulties in obtaining redress from a third party responsible for a delay. The proposal enables railway undertakings to use a right to redress, in accordance with applicable law, if delays were caused by a third party's fault or negligence. The measure aligns rail passenger rights with air passenger rights.

The Government's view[46]

6.22 In an Explanatory Memorandum submitted on 19 October 2017, the Parliamentary Under Secretary of State (Paul Maynard) states that the Government agrees that it is appropriate for the Commission to legislate in this area in order to ensure that the Regulation is applied more consistently across the European Union. The Minister notes that the recast Regulation remains a minimum harmonisation Regulation, meaning that Member States would be able to retain domestic passenger rights provisions that are more generous than the minimum standards in the Regulation.

6.23 The Minister states that the Government "shares the Commission's objective of strengthening the rights of rail passengers" and therefore "support[s] in principle the proposal's aim of standardising and improving passenger rights, including by improving access for persons with disabilities or reduced mobility and the requirement for railway undertakings and station managers to ensure that staff have disability training and attend regular refresher training".

6.24 The Minister also states that it understands the Commission's objective to make rail passenger services comparable to other modes of transport, in order to provide a more level playing field. The Minister states that the Government supports the principle of improved provision of information about passenger rights, and the need for passengers to have basic information on their rights at the point of booking a ticket.

46 Explanatory Memorandum from the Department for Transport (19 October 2017) EM 12442/17.

6.25 The Minister acknowledges the concerns the Commission has identified on the extensive use of exemptions by Member States, and states that he can appreciate that the Commission is keen to see uniform application of this across Member States; however, he adds that the Government will need to consider carefully the detail of the proposals, in particular any potential costs, in consultation with external stakeholders. The Minister clarifies that the exemptions permitted under Regulation 1371/2007 were put in place by the Department for Transport for Great Britain and by Northern Ireland Ministers for NI (although the exemptions were not renewed in Northern Ireland, meaning that the Regulation has been in full effect in NI since 2014). However, the Minister states that most of the requirements of the current Regulation are already met or exceeded through domestic rail provisions such as the train operators' Disabled People's Protection Policies, National Rail Conditions of Travel and the Equality Act.

6.26 In terms of the financial implications of the proposal, the Minister states that some of the new requirements in the proposals may not necessarily produce new burdens for the rail sector, as in many areas UK domestic rail passenger rights requirements already exceed the minimum standards in both the existing EU Regulation and in the Commission's proposals. However, he states that the detail of the proposal will be examined to determine whether there are financial implications for the rail sector or for the taxpayer.

6.27 The Minister states that the Government will need to consider carefully the detail of the proposals, in particular any potential costs, in consultation with external stakeholders. He adds that the Government will be discussing the proposals informally with industry, passenger representative bodies and the ORR to inform our view of the proposals and their implications.

Brexit implications

6.28 In relation to the UK's withdrawal from the European Union, the Minister states that the rights put in place by this proposal, where it is in force, would apply equally to all rail passengers. It would therefore have benefits for rail passengers travelling in an EU or EEA Member State, who are citizens of countries outside the EU or EEA.

Previous Committee Reports

None.

7 Vehicle type approvals

Committee's assessment	Politically important
Committee's decision	Retained under scrutiny; further information requested; drawn to the attention of the Transport Committee
Document details	Proposal for a Council Decision on the position to be adopted on behalf of the European Union in the relevant Committees of the United Nations Economic Commission for Europe as regards the proposals for amendments to UN Regulations Nos 12, 14, 16, 17, 43, 44, 46, 48, 49, 110, 121, 129 and 134, to UN Global Technical Regulations Nos 6 and 15, to the Rules of Procedure of WP.29 and to the General Guidelines for UN regulatory procedures and transitional provisions in UN Regulations, and as regards proposals for three new UN Regulations, one new UN Global Technical Regulation and a proposal for a new Mutual Resolution
Legal base	Article 114 TFEU in conjunction with Article 218(9); QMV
Department	Transport
Document Number	(39142), 13120/17 + ADD 1, COM(17) 602

Summary and Committee's conclusions

7.1 The United Nations Economic Commission for Europe (UNECE) World Forum for Harmonization of Vehicle Regulations, also known as Working Party 29 (WP.29), is a regulatory forum which seeks to reduce technical barriers to trade. UNECE Rules, Regulations and Global Technical Regulations are agreed on a quarterly basis at WP.29.

7.2 The EU and its Member States, which are members of UNECE, have a shared competence in this policy area, as a result of which the Commission delivers the collective Member States' voting position on UNECE proposals. This position is formulated in advance in the Council of Ministers on a qualified majority voting basis.

7.3 On 19 October 2017 the European Commission adopted a proposal for a Council Decision[47] on the position to be adopted on behalf of the EU in the UNECE Administrative Committee in November, regarding a number of new Regulations and Global Technical Regulations, as well as amendments to existing rules. The Parliamentary Under Secretary of State at the Department for Transport (Jesse Norman) subsequently submitted an Explanatory Memorandum to the Committee on 15 October 2017, seeking clearance to support the proposal.[48]

7.4 The Minister explains that the proposals consist of some minor technical changes to UN regulatory procedures and provisions; new UNECE Regulations on Automatic

47 Proposal for a Council Decision on the position to be adopted on behalf of the European Union in the relevant Committees of the United Nations Economic Commission for Europe 13120/17, COM (17)602 http://europeanmemoranda.cabinetoffice.gov.uk/files/2017/10/ST-13120–2017-INIT-EN.pdf.

48 Explanatory Memorandum 13120/17 http://europeanmemoranda.cabinetoffice.gov.uk/files/2017/10/171024_-_International_road_vehicle_regulations.pdf.

Emergency Call Systems, Electric Vehicles and the Mutual Resolution on Vehicle Interior Air Quality, which will, in the Minister's assessment, reduce technical barriers to trade; and a proposed Global Technical Regulation (GTR) on International Whole Vehicle Type Approval, which is intended to bring harmonisation between the major blocs of EU and Japan.

7.5 The Minister states that the Government is content with the changes to be brought about as a result of the proposed EU Decision. He says that it is well-established that the EU signs up to UNECE and Global Technical Regulations as a body in order to maximise the benefits of harmonisation.

7.6 This proposal was considered by the Council of Ministers on 6 November. As the newly appointed European Scrutiny Committee had not met at this time and was therefore unable to consider the Government's Explanatory Memorandum before the meeting of the Council on 6 November, the Government abstained, to avoid overriding the scrutiny reserve. The UNECE Administrative Committee voted to adopt the proposed changes on 14 November 2017.

7.7 Regarding the implications of the UK's withdrawal from the EU, the Government observes that "After the UK has left the EU, our participation in the UNECE will continue, as our UNECE membership is independent of our EU membership, despite the need to collaborate whilst we are EU members." The Government does not provide an analysis of the implications for UK stakeholders of a shift from the current EU Single Market regime for type-approvals, under which the UK Vehicle Certification Agency (VCA) can issue European approvals, to that of a 'third country'. This is understandable in the context of the proposal; however, a rounded appraisal of the implications of Brexit for type-approval processes and the UK automotive sector requires that the issues be considered together.

7.8 **We note the Government's support for the proposed package of changes to UNECE rules, Regulations and Global Technical Regulations (GTRs), which will reduce technical barriers to trade globally and maximise the benefits of harmonisation. The Decision was adopted by the Council on 6 November 2017, and the Government abstained in order to avoid a scrutiny override.**

7.9 **When the UK withdraws from the EU, its membership of UNECE will be unaffected and it will deliver its own vote, as opposed to the current position where the UK vote forms part of the collective portion formulated by the EU (in the Council on a Qualified majority voting basis).**

7.10 **To accurately appraise the implications of withdrawal from the European Union in this policy area, the Committee considers that a fuller account of regulatory harmonisation at both UNECE and EU level, and their interaction, is necessary. We therefore request that the Government provide us with a detailed briefing on:**

- **the scope and legal effects of UNECE rules, Regulations and Global Technical Regulations in the area of vehicle regulation and type approvals, as well as the extent of global participation in these rules;**
- **how this framework differs from, and interacts with, EU vehicle regulation (including type approval) frameworks, including the proportion of EU type approvals that are not covered by UNECE rules;**

- **the extent to which UN regulation, in effect, promulgates EU rules globally; why some states' participation in UNECE rules is limited;**
- **whether, in its view, the UK leaving the EU will significantly modify the dynamics within UNECE; and**
- **whether it has made a clear decision to continue to sign up to UNECE regulations post-withdrawal, or whether this issue is undecided.**

7.11 **Currently, the UK type-approval authority—the Vehicle Certification Agency (VCA)—checks many motor vehicles before they are placed on the EU market to ensure they meet relevant standards. The UK's departure from the European Single Market will in principle result in the EU Regulation on type approval no longer applying to the United Kingdom, meaning that type-approval certificates issued by the VCA would no longer be valid in the EU27, and that UK-based manufacturers would have to use other European approval authorities. We ask the Government:**

- **for an update regarding the status of EU approvals that are currently being issued within the UK: will these be recognised during the Prime Minister's Implementation Period and following the UK's withdrawal from the EU?**
- **for an update regarding whether the VCA will retain its ability to issue EU approvals during the implementation period and following the UK's withdrawal from the EU;**
- **whether, in order for UK type approvals to continue to be accepted within the EU, after the UK leaves the EU, the Government is willing to continue to accept European approvals, and (by extension) to ensure continued alignment with EU regulations;**
- **whether there is any precedent for vehicle certification authorities outside EU and EEA countries being able to issue European type approvals which are recognised in the EU; and**
- **for the Government's assessment of the implications for the UK automotive sector of UK manufacturers having to send vehicles to other European authorities to secure approvals, and (reciprocally) for EU manufacturers having to send vehicles to the UK for UK approvals.**

7.12 **To allow the preparation of a thorough response, we give the Government until 7 February to respond—a period of approximately two months. In the meantime we retain this proposal under scrutiny and draw it to the attention of the Transport Committee.**

Full details of the documents

Proposal for a Council Decision on the position to be adopted on behalf of the European Union in the relevant Committees of the United Nations Economic Commission for Europe as regards the proposals for amendments to UN Regulations Nos 12, 14, 16, 17, 43, 44, 46, 48, 49, 110, 121, 129 and 134, to UN Global Technical Regulations Nos 6 and 15, to the Rules of Procedure of WP.29 and to the General Guidelines for UN regulatory

procedures and transitional provisions in UN Regulations, and as regards proposals for three new UN Regulations, one new UN Global Technical Regulation and a proposal for a new Mutual Resolution (39142), 13120/17, COM (17) 602.

Background

Harmonisation of vehicle regulations

7.13 Vehicles which are sold and put into service in a country have to meet the regulations and standards of that country. The registration procedure of that country requires the approval of the vehicle and/or its components. The existence of separate national regulations and approval procedures in the different countries requires expensive design modifications, additional tests and duplicating approvals. Thus, there is the need to harmonize the different national technical requirements for vehicles and to elaborate a unique international regulation. Once the vehicle or its equipment and parts are manufactured and approved according to that regulation, they can be internationally traded without further tests or approvals. These regulations have to be continuously adapted to the technical progress and to the new requirements regarding safety and environmental protection.

The World Forum for Harmonisation of Vehicle Regulations (WP.29)

7.14 In order to reduce international trade barriers and to promote the global trade of vehicles and their components, efforts are being made to have harmonized vehicle regulations worldwide. The major forum for this role is the World Forum for Harmonization of Vehicle Regulations (WP.29) under the United Nations Economic Commission for Europe (UNECE). Two international agreements provide the basis for much of this activity.

The 1958 Agreement and UN Regulations

7.15 The UNECE 1958 Agreement, revised in 1995 ("the Revised 1958 Agreement") was put in place to assist industry by removing technical barriers to trade within Europe. The Agreement:

- facilitates free trade by encouraging the development of harmonised requirements for motor vehicles;
- requires the mutual recognition by participating countries (known as "contracting parties") of vehicle system and component approvals (for example for vehicle braking systems); and
- provides for manufacturers with approved products to have access to the markets of all contracting parties.

7.16 The 1958 Agreement operates on the principles of type approval and reciprocal recognition. If a component is type approved according to a UN Regulation by any of the Contracting Parties to the 1958 Agreement, all other Contracting Parties who have signed the same Regulation will recognize this approval. This avoids repetitive testing and approval of components in various countries in which the latter are exported. This helps

to reduce the time and costs of design, manufacture and approval as well as the entering into service of vehicles and their components. This harmonisation of standards opens wider global markets to manufacturers and reduces development and production costs.

7.17 A UN Regulation in force is legally binding on all those Contracting Parties which signed the same Regulation.

7.18 There are over 100 UNECE Regulations covering various aspects of vehicle construction which have been developed under the 1958 Agreement. As of 2016, there were 62 signatories to the agreement, including non-EU UNECE members such as Russia, Ukraine, Serbia, Belarus, Kazakhstan, Turkey, Azerbaijan and Tunisia, South Africa, Australia, New Zealand, Japan, South Korea, Thailand and Malaysia.

The 1998 Agreement and Global Technical Regulations (GTRs)

7.19 In 1998, the 1958 Agreement was supplemented by the 1998 Agreement. This Agreement was aimed at facilitating easier trade between the principal global regions of USA, EU and Japan while recognising the growing markets for new vehicles of China and India.

7.20 The 1998 agreement establishes a process through which countries from all regions of the world can jointly develop UN Global Technical Regulations (UN GTRs) for vehicles and their components. GTRs do not provide for mutual recognition of type approvals. Contracting Parties to the 1998 Agreement can adopt any UN GTR in which they are interested, but are not obliged to do so.

7.21 The 1998 Agreement currently has 33 Contracting Parties and 14 UN GTRs that have been established into the UN Global Registry.

7.22 UNECE Regulations and Global Technical Regulations are agreed in technical working groups, and then enacted at the political level by WP.29.

EU involvement in WP.29

7.23 WP.29 predates the EU. However the EU and the Member States have shared competence arrangements in the work of the vehicle sector of the UNECE. The Lisbon Treaty sets out procedures on the interaction of the EU with international organisations and agreements and affects the specific rules covering EU participation in both international agreements on motor vehicles.

7.24 All EU Member States are part of UNECE and WP.29, and all EU Member States individually present their own positions at a technical level. However, the Commission presents the Council's technical position and also delivers the collective Member States' voting position, which is formulated in the Council on a qualified majority voting basis.

7.25 The EU and Member States must accept approvals in line with the latest updates (amendments) to the UNECE Regulations, to which they are party. But the question of whether to make the latest amendment compulsory for new vehicles in the EU is considered separately by the Commission and Member States—it does not happen automatically.

EU type approvals and authorities

7.26 The European approval scheme is based on the concept of 'type approval', which provides a mechanism for ensuring that vehicles meet relevant environmental, safety and security standards. As it is not practical to test every single vehicle made, one production vehicle is tested as being representative of the 'type'. A number of performance requirements will apply to a given vehicle type ranging from tyres through to exhaust emissions and braking systems. To ensure a consistent approach, the test methodology is outlined in relevant rules and the tests are carried out at an appropriate facility.

7.27 Within the EU, Directive 2007/46[49] sets out the safety and environmental requirements that motor vehicles have to comply with before being placed on the EU market. The Directive makes the European Community Whole Vehicle Type Approval (EU-WVTA) system mandatory for all categories of motor vehicles and their trailers. A large number of UNECE regulations are also made mandatory by the Directive.

7.28 Approval authorities are established or appointed by EU countries and notified to the Commission. The approval authorities have competence for:

- all aspects of the approval of a type of vehicle, system, component or separate technical unit;
- the authorisation process;
- issuing and, if appropriate, withdrawing or refusing approval certificates;
- acting as the contact point for the approval authorities of other EU countries;
- designating the technical services; and
- ensuring that the manufacturer meets his obligations regarding the conformity of production.

7.29 The Vehicle Certification Agency (VCA) is the UK type approval authority. It checks many motor vehicles before they are placed on the EU market to ensure they meet relevant standards. These vehicles do not need to be checked by local type approval authorities elsewhere in the EU, avoiding unnecessary duplication.

7.30 A certificate of conformity is a statement by the manufacturer that the vehicle conforms to EU type approval requirements. EU countries cannot refuse to register vehicles if they are accompanied by a valid CoC that proves their compliance with EU law. The Commission has proposed simpler rules for the motor vehicle registration of a car already registered on one EU country to be registered in another.

7.31 A technical service is an organisation or a body designated by the national approval authority as:

- a testing laboratory to carry out tests; or
- a conformity assessment body to carry out the initial assessment and other tests or inspections on behalf of the approval authority.

49 Directive 2007/46/EC of the European Parliament and of the Council of 5 September 2007 establishing a framework for the approval of motor vehicles and their trailers, and of systems, components and separate technical units intended for such vehicles (Framework Directive) http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32007L0046&from=EN.

The proposal[50]

7.32 The proposal defines the Union's position in the voting on:

- proposed amendments to existing UN Regulations Nos. 12, 14, 16, 17, 43, 44, 46, 48, 49, 110, 121, 129 and 134; and amendments to UN Global Technical Regulations (GTRs) Nos. 6 and 15;
- a proposal for a new UN Regulation on Accident Emergency Call Systems (AECS). This is intended to harmonise rules on systems which automatically contact the Emergency services in the event of a severe collision. It is based on EU requirements which recently became compulsory for newly designed cars;
- a proposal for a new UN Regulation on International Whole Vehicle Type Approval (IWVTA). This is intended to set up a new global "whole vehicle" approval regime, to permit manufacturers to approve cars for global sale. The Government's explanatory memorandum states that initially this International approval scheme will be optional and will only cover around 60% of the standards needed to sell a vehicle in Europe, meaning that manufacturers will still need final approval from a local regulator;
- a proposal for a new UN Regulation on ISOFIX anchorage systems of child seats. ISOFIX top tether anchorages and i-Size seating positions are not new requirements. To allow for their inclusion in the new system of International Whole Vehicle Type approval, existing requirements for these systems have been removed from regulations covering seat belt anchorages, and instead will form a stand-alone regulation;
- a proposal for a new UN Global Technical Regulation on Electric Vehicle Safety (EVS). The new global technical regulation on electric vehicle safety is intended to create a single global standard for this topic—currently EU, America and Japan have different standards. This is a comprehensive set of requirements, to take account of the fact that electric vehicles have now become mainstream, which will ensure a high level of safety;
- a proposal for a new Mutual Resolution (M.R.3) of the 1958 and the 1998 Agreements concerning Vehicle Interior Air Quality (VIAQ). This is intended to introduce harmonised specifications around testing interior air quality, in order to avoid the use in car interiors of materials that emit harmful chemicals (such as volatile organic compounds), particularly when they are new;
- a proposal for amending the General Guidelines for UN regulatory procedures and transitional provisions in UN Regulations. These are intended to set out best practice in the drafting of UN Regulations; and
- a proposal for amending the Rules of Procedure of WP.29, which will permit non-accredited bodies to attend the meetings of WP29 where their input may be relevant.

50 Proposal for a Council Decision on the position to be adopted on behalf of the European Union in the relevant Committees of the United Nations Economic Commission for Europe 13120/17, COM (17)602 http://europeanmemoranda.cabinetoffice.gov.uk/files/2017/10/ST-13120–2017-INIT-EN.pdf

The Government's view

7.33 On 24 October 2017 the Parliamentary Under Secretary of State at the Department for Transport (Jesse Norman) submitted an Explanatory Memorandum[51] to the House. The Minister indicates that the Government "is content with the changes to be brought about as a result of the proposed EU Decision", and, states that it is well-established that the EU signs up to UNECE and Global Technical Regulations "to maximise the benefits of harmonisation".

7.34 Summarising the overall impact of the proposed changes, the Minister clarifies that:

- adoption of the proposals will require EU Member States to issue approvals to vehicles that comply with the revised regulations, and to accept vehicles approved elsewhere to the standard set out in the revised regulations (Articles 2 and 3 of Annex I to Council Decision 97/836/EC); and

- none of the proposals is compulsory for UK manufacturers, as amending existing international regulations / introducing new regulations does not alter the minimum requirements that must be complied with to sell a vehicle in the EU, which remain unchanged. It would require an EU legal act to make these new or amended regulations compulsory for new vehicles within the EU. On this basis, the Minister concludes that there will be no immediate burdens imposed upon business or the voluntary sector.

7.35 In relation to the individual proposals, the Minister states that:

- proposed amendments to existing UN Regulations and Global Technical Regulations introduce minor technical changes to, or editorial clarifications of, existing technical requirements;

- the new Regulations on Automatic Emergency Call Systems, Electric Vehicles and the Mutual Resolution on Vehicle Interior Air Quality, aim to harmonise standards globally in these areas. The Minister indicates the Government's in principle support for these Regulations on the basis that adoption of harmonised regulations helps industry by reducing the risk of regulatory diversity, removing technical barriers to trade and ensuring a high level of safety;

- the proposed Global Technical Regulation on International Whole Vehicle Type Approval (IWVTA) is intended to bring harmonisation between the major blocs of EU and Japan. The Minister states that

  "if [the Regulation] is widely accepted outside those blocs, it will help European manufacturers by permitting them to sell around the globe using approvals issued by their local approval authority, without needing to engage with overseas authorities."; and

- the Minister states that the other two miscellaneous proposals—the proposal for amending the General Guidelines for UN regulatory procedures and transitional provisions in UN Regulations, and a proposal for amending the Rules of Procedure of WP.29—have no significant new policy implications.

51 Explanatory Memorandum 13120/17 http://europeanmemoranda.cabinetoffice.gov.uk/files/2017/10/171024_-_International_road_vehicle_regulations.pdf

Brexit implications

7.36 The Minister states that "After the UK has left the EU, our participation in the UNECE will continue, as our UNECE membership is independent of our EU membership, despite the need to collaborate whilst we are EU members".

Previous Committee Reports

None.

8 Coordination of social security systems

Committee's assessment	Legally and politically important
Committee's decision	Not cleared from scrutiny; further information requested
Document details	Proposal for a Regulation amending Regulation (EC) No 883/2004 on the coordination of social security systems and Regulation (EC) No 987/2009 laying down the procedure for implementing Regulation (EC) No 883/2004
Legal base	Article 48 TFEU; QMV, ordinary legislative procedure
Department	Work and Pensions
Document Number	(38400), 15642/16 + ADDs 1–8, COM(16) 815

Summary and Committee's conclusions

8.1 Regulation 883/2004 determines which EU Member State is responsible for the calculation and payment of social security benefits for mobile EU citizens who move within the Union. Such citizens are, in principle, entitled to use the local benefits system on the same basis as nationals of their host Member State, including unemployment benefit, child benefit and state pensions, as well as having a right to access short- and long-term healthcare.

8.2 In December 2016, the European Commission tabled a legislative proposal to bring Regulation 883/2004 in line with the case law of the European Court of Justice on access to benefits for unemployed EU citizens; clarify the rules for determining which EU country is responsible for payment of benefits; and to amend the provisions of the Regulation on access to unemployment benefit, salary-related family benefits[52] and long-term care benefits. The Committee has set out the details of this proposal in some detail in previous Reports in February[53] and November 2017.[54]

8.3 The amendments to the Regulation are unlikely to apply before the UK withdraws from the EU in March 2019. However, the Regulation, and this pending amendment, are nonetheless significant. The UK and EU have both agreed to maintain its provisions for EU nationals resident in the UK on "Brexit Day" and *vice versa* as part of any Withdrawal Agreement under Article 50 TEU. The two sides have also accepted the need for a mechanism to apply future changes to the Regulation, as agreed at EU-level, to citizens within the scope of the Withdrawal Agreement.[55] In addition, the Government is now seeking an "implementation period" for the immediate post-Brexit period, during which it is likely that Regulation 883/2004 would continue to apply as it did while the UK remained a Member State.

52 Salary-related family benefits are a form of social security intended to replace income during child-raising periods.

53 See our predecessors' Report of 8 February 2017.

54 See our Report of 13 November 2017.

55 See for more information on the implications of Brexit for social security coordination paragraphs 15.32 to 15.45 of our Report of 13 November.

8.4 The Government has been broadly supportive of the proposed amendments. On 23 October 2017, EU Employment Ministers agreed a partial general approach on the elements of the Commission proposal relating to equal treatment and the determination of applicable national legislation. The Committee considered the Council's position, and the Government's override of scrutiny to support its adoption,[56] at our meeting on 13 November. We retained the proposal under scrutiny and asked a number of detailed questions of the Minister of State for Employment (Damian Hinds) about the Government's position, including in the Article 50 negotiations.

8.5 On 22 November, the Minister informed us that the Estonian Presidency was also seeking to secure a second partial general approach on long-term care benefits and family benefits at the EPSCO Council on 7 December.[57] He noted that the Government was "prepared to accept the current text". He added that the proposed coordination of long-term care benefits "should not have any financial impact for the UK". As regards the inclusion of family benefits within the scope of the Regulation, the Minister confirmed that the UK "does not administer any benefits of this type", and so there should "only be a limited financial impact". To enable the Government to support this partial general approach, the Minister requested a scrutiny waiver in advance of the Council meeting.

8.6 The European Parliament's Employment & Social Affairs Committee, which will be responsible for negotiations with the Council on the final text of the amendments to Regulation 883/2004, has recently published a draft Report on the proposals.[58] It is expected to adopt its mandate for those negotiations in the first half of 2018.

8.7 **We are not content to grant the Minister a scrutiny waiver ahead of the EPSCO Council on 7 December, we expect a swift reply to our outstanding questions contained in our Report of 13 November. In light of his latest letter, we also ask him to include in his reply why the proposed rules on family benefits would have a "limited" financial impact in the UK, given that no such benefit is administered here. We also note that the provisions of the Commission proposal relating to access to unemployment benefit have not yet been covered by a Council general approach.**

8.8 **The Committee will consider the proposal further following receipt of the Minister's reply to our previous Report. We expect to be kept informed of further progress within the Council and the European Parliament on this file, and will follow any trilogue negotiations closely.**

Full details of the documents

Proposal for a Regulation amending Regulation (EC) No 883/2004 on the coordination of social security systems and Regulation (EC) No 987/2009 laying down the procedure for implementing Regulation (EC) No 883/2004: (38400), 15642/16 + ADDs 1–8, COM(16) 815.

Previous Committee Reports

Thirty-first Report HC 71–xxix (2016–17), chapter 8 (8 February 2017) and First Report HC 301–i (2017–19), chapter 15 (13 November 2017).

56 The scrutiny override occurred because the Committee had not yet been reformed following the general election.

57 Letter from Damian Hinds to Sir William Cash (22 November 2017).

58 European Parliament document PE612.058 (20 November 2017).

9 Single EU VAT Area

Committee's assessment	Legally and politically important
Committee's decision	(a) and (b) Not cleared from scrutiny; further information requested; drawn to the attention of the Business, Energy & Industrial Strategy Committee; the Northern Ireland Affairs Committee, and the Treasury Committees; (c) and (d) Cleared from scrutiny
Document details	(a) Proposal for a Council Directive harmonising and simplifying certain rules in the value added tax system and introducing the definitive system for the taxation of trade between Member States; (b) Proposal for a Council Regulation as regards the certified taxable person; (c) Proposal for a Council Implementing Regulation as regards certain exemptions for intra-Community transactions; (d) Communication from the Commission on the follow-up to the "Action Plan on VAT -Towards a single EU VAT area".
Legal base	(a) and (b): Article 113 TFEU; special legislative procedure; unanimity; (c) Article 397 of Council Directive 2006/112/EC; (d)—
Department	Treasury
Document Numbers	(a) (39085), 12882/17 + ADD1–2, COM(2017) 569; (b) (39083), 12880/17, COM(2017) 567; (c) (39084), 12881/17, COM(2017) 568; (d) (39077), 12617/17, COM(2017) 566

Summary and Committee's conclusions

9.1 Since 1993, with the complete abolition of intra-EU customs controls as part of the Single Market, the EU has operated a curious system of Value Added Tax (VAT) on cross-border business-to-business (B2B) sales of goods and services within the EU. Under this system, a supplier can make a sale to a customer in another EU country VAT-free, after which the customer effectively must charge VAT to himself and pay it to their national tax authority. However, the system was meant to operate only on a transitional basis, as it allows for substantial amounts of VAT to be fraudulently evaded. For imports into the EU from non-EU countries (including from the UK when it leaves the EU after Brexit), VAT must still be paid at the border before it can enter the EU's territory.

9.2 In October 2017, the European Commission tabled a legislative proposal to simplify the system, end its transitional status and tackle intra-EU VAT fraud, estimated to cost Governments up to €53 billion (£47 billion)[59] each year. In particular, it wants to make suppliers, and not buyers, responsible for VAT on cross-border purchases and expand the use of an EU-wide mechanism that allows suppliers to pay VAT on sales to any Member State in their own country. Simultaneously, it wants to mitigate any new burdens on suppliers by maintaining the current system where the buyer is considered a "reliable

59 €1 = £0.8821 or £1 = €1.336 as at 31 October 2017.

taxpayer". The Commission estimates that its plans, if adopted by the Member States, would result in a reduction in VAT fraud of €41 billion (£37 billion) and compliance costs for businesses by €1 billion (£890 million) annually.

9.3 At present, the Commission has only proposed to establish, in EU law, the intention to move to a new system of cross-border VAT for B2B sales, with further detailed draft legislation to follow in 2018. Initially, the new system would apply only to cross-border sales of goods, with its extension to supplies of services to follow after an evaluation. In the meantime, the Commission has also proposed, at the request of the Member State, several "Quick Fixes" to the current VAT system for cross-border sales of goods, to reduce burdens on businesses and to counter fraud.

9.4 We have set out the history of the current intra-EU VAT system, the implications of the Commission proposals, and the substance of the short-term "Quick Fixes", in more detail in "Background" below.

9.5 On 24 October, the Financial Secretary to the Treasury (Mel Stride) submitted an Explanatory Memorandum on the proposals.[60] He cautiously welcomes the proposals, but warns that further detailed consideration will be necessary. In particular, he highlights the creation of a parallel system depending on whether the buyer is a "reliable taxpayer" or not; the potential impact of changes to cash flow that both tax authorities and businesses may experience as a result of the proposed changes; and the need for further scrutiny to ascertain what new opportunities for VAT fraud the proposals might create. The Minister does not assess the implications for UK businesses, both buyers and suppliers, of leaving the EU's common system of VAT.

9.6 **The Commission proposals are a major development in the EU's common system of value added tax, as they are the first significant step in ending a system for cross-border VAT within the EU that was introduced nearly twenty-five years ago as a temporary measure.**

9.7 **We share the Minister's concern about requiring suppliers to deal with two parallel systems for VAT on cross-border sales, depending on the customer. In addition, our ability to effectively scrutinise what is being proposed is hampered by the fact the UK's place within the common system of VAT after March 2019 remains unclear (see below), and because the actual substance of the Commission's proposals will not follow until next year.**

9.8 **We therefore ask the Minister to keep us informed of progress in the deliberations within the Council on these important proposals. In particular, we are interested in:**

- **the Government's view on the merit of legislating for the *principle* of the new system in the VAT Directive, but leaving detailed implementation to a later stage;**
- **the position taken by other Member States on the "definitive system" proposed by the Commission, including the extension of the OSS and the introduction of the reverse charge mechanism where the buyer is a Certified Taxable Person;**

60 Explanatory Memorandum submitted by HM Treasury (24 October 2017).

- **the perceived accuracy of the Commission's impact assessment, especially the estimate that its preferred method for implementing the "destination principle" would result in a reduction in VAT fraud of €41 billion and compliance costs for businesses by €1 billion;**
- **the way in which applications for CTP status would be assessed and monitored, and the likely impact on the resources of national tax authorities including HM Revenue and Customs; and**
- **the Council's position on the "Quick Fixes", and whether these provisions could be split off from the negotiations on the "definitive system" of VAT, to ensure a speedier adoption and entry into force.**

Implications of Brexit

9.9 **We have also considered these proposals, and the EU's common system of VAT more broadly, in the context of the UK's withdrawal from the EU. Our starting point must be that, at present, there are no customs and VAT controls at either the UK or EU border on flows of goods between the two, as they are both part of a common jurisdiction on these matters under the Treaties.**

9.10 **With respect to this latest package of measures on VAT, these only concern intra-EU supplies of goods. As such, it does not appear they will have much significance for the UK once it is outside the EU's common system of value added tax. However, it is unclear whether the Government envisages the UK will stay in that system for the duration of the post-Brexit "implementation/transition period". We will therefore apply scrutiny under the presumption that the UK could be under a legal obligation to implement this new legislation, depending on the speed of its adoption and the length of the implementation/transitional period.**

9.11 **However, it is clear that any post-Brexit interim arrangement will only postpone rather than negate the "cliff edge" of the UK becoming a "third country" vis-à-vis the European Union. At that point, UK exports to the EU (like those from any other non-EU country)[61] will face customs and VAT controls which are currently absent, and the relevant duties and taxes will have to be paid by the importer before UK goods can be released into the EU.**

9.12 **Therefore, unless there is an unprecedented agreement to the contrary, VAT controls will also at some point become necessary at the border between Northern Ireland and Ireland. The Government has said that it will not accept any physical infrastructure at the border. However, it is not clear how waiving border controls in Ireland only would be consistent with the UK's obligations under the WTO's Most Favoured Nation principle.[62] Moreover, without the necessary infrastructure for VAT controls, it is not immediately apparent to us how the Government would collect domestic import VAT on goods coming into the UK from Ireland (whether the supplier**

61 The only current exceptions to this are the Isle of Man, the UK Sovereign Area Bases in Cyprus and Monaco. These are all considered part of the EU's common VAT area, because of their special links to EU Member States.

62 Under the MFN principle, a WTO member that unilaterally grants another country a special favour (in this instance no customs controls for goods coming into the UK at the Irish border) has to do the same for all other WTO members.

is EU-based or not). By default, Brexit means the UK ceases to be part of the EU VIES system[63] which alerts the tax authorities of the buyer to intra-EU supplies on which VAT is due. No non-EU country receives information via that system.[64]

9.13 **With neither a UK-EU VAT Information Exchange System nor border controls in place, there would be a widespread potential for VAT evasion, as the Government would not know about the importation of goods on which the tax had not yet been paid. The same applies where goods are bought by EU-based suppliers from the UK, and entering free circulation in the EU after passing the Irish border.**

9.14 **The Irish Government will be unable to unilaterally waive VAT and other EU border-related controls on goods entering Ireland from the UK, unless some form of derogation from Ireland's EU treaty obligation is negotiated and agreed by the other Member States. However, it is not clear to us if it is feasible for the Government to negotiate a replication of the VIES system for UK-EU trade only, so as to permit a continued absence of VAT controls at the Irish border. Even goods from the EFTA-EEA countries Norway, Iceland and Liechtenstein, which have the closest economic link to the EU without being a Member State, face customs and VAT controls.**

9.15 **Moreover, even *if* such a system could be negotiated and implemented in time, it would require the UK and the EU to adhere to a similar set of rules on cross-border VAT (for example in relation to the legal definition of the "place of supply", as well as the use of any reverse charge mechanism and of the One Stop Shop). We have not seen any concrete information about how such a joint system would operate in practice outside of the framework of the EU Treaties. We are concerned it would simply require the UK to accept the relevant EU legislation, without representation (and its current veto on tax matters) on the Council.**

9.16 **Therefore, in the absence of a detailed proposal by the Government to facilitate an agreement to the contrary, we must assume that VAT controls will eventually be imposed on UK exports to the EU (irrespective of whether the Government chooses not to impose such controls on exports to the UK via Ireland, bearing in mind the potential consequences of such a decision under the MFN principle).**

9.17 **We have set out our assessment of the VAT-related implications of Brexit in more detail in paragraphs 9.70 to 9.81 below. In light of this, we ask the Minister to set out in more detail the Government's proposals to mitigate the impact of any VAT controls on exports to the EU after Brexit (especially at the Irish border), and to clarify:**

- **the total value in 2016 of VAT collected by HMRC on intra-Community supplies purchased by UK traders;**
- **if the Government will seek to keep the UK in the EU's common VAT area for the duration of the "implementation/transitional period";**
- **how the Government would collect domestic import VAT on cross-border purchases transported into the UK via the Irish border in the absence of customs controls there;**

63 VIES is the VAT Information Exchange System. See paragraph 9.26 for more information.

64 The recent EU-Norway Agreement on value added tax does not give Norway access to VIES, precisely because VAT is collected at the EU-Norway border on importation of goods going in either direction.

- **what the implications would be for the UK's ability to impose border controls on imports from non-EU countries into any UK port under the MFN principle if it waives such controls for goods crossing the Irish border;**
- **what assessment has been made of the value of HM Revenue and Customs' participation in, and access to, the EU's various VAT-related systems, including VIES, and how it proposes to mitigate any adverse effects of leaving those systems;**
- **whether there is any scope for use of the proposed expansion of the One Stop Shop or the Certified Taxable Person status by UK companies after Brexit for business-to-business transactions; and**
- **if it has identified examples of other customs cooperation agreements between different customs and VAT jurisdictions, other than the EU, that provide for the complete abolition of customs and VAT controls on imports from outside each respective jurisdiction.**

9.18 **In anticipation of the Minister's reply to our questions, we retain the proposal for a Council Directive and the Council Regulation on the Certified Taxable Person (documents A and B) under scrutiny, and clear the proposed Council Implementing Regulation and the accompanying Communication (documents C and D). We also draw these developments to the attention of the Business, Energy & Industrial Strategy and the Treasury Committees, and in the context of the border question in particular, the Northern Ireland Affairs Committee.**

Full details of the documents

(a) Proposal for a Council Directive amending Directive 2006/112/EC as regards harmonising and simplifying certain rules in the value added tax system and introducing the definitive system for the taxation of trade between Member States: (39085), 12882/17 + ADDs 1–2, COM(2017) 569; (b) Proposal for a Council Regulation amending Regulation (EU) No 904/2010 as regards the certified taxable person: (39083), 12880/17, COM(2017) 567; (c) Proposal for a Council Implementing Regulation amending Implementing Regulation (EU) No 282/2011 as regards certain exemptions for intra-Community transactions: (39084), 12881/17, COM(2017) 568; (d) Communication from the Commission on the follow-up to the "Action Plan on VAT -Towards a single EU VAT area": (39077), 12617/17, COM(2017) 566.

Background

9.19 The EU has established a common system of value added tax (VAT) system which is currently governed primarily by Directive 2006/112/EC (the VAT Directive). For cross-border trade within the EU, VAT must be paid in the Member State where a goods or service is supplied, which ordinarily means in the country where the customer is based or takes possession of the goods.[65] The Directive however contains various exemptions to this general principle, for example, where services are supplied to a consumer (in which case VAT is normally paid in the Member State of the supplier irrespective of the location of the customer).

65 European Commission, "Cross-border VAT" (accessed 22 November 2017).

9.20 The current system, described in more detail below, was originally created in 1993 as a transitional measure following the creation of the Single Market. For cross-border business-to-business (B2B) transactions, which constitute the vast majority of all cross-border VAT-taxable sales in the EU, the tax must be paid in the country of destination, but by the buyer rather than the seller (in contrast to purely domestic transactions, where the seller is responsible for accounting for the VAT).

9.21 The European Commission has now proposed to move towards a "definitive system of value added tax" within the EU, based on the principle that VAT should be paid in the Member State of destination for goods and services by the supplier, to bring the intra-EU system in line with the way VAT is collected on domestic transactions. The proposals do not affect the VAT treatment of goods imported into the EU from outside the Union, for example from the UK after Brexit.[66]

The current system for cross-border VAT within the EU

9.22 Under the 1977 VAT Directive, value added tax on cross-border supplies of goods within the European Community was subject to a system of "de-tax and re-tax", also known as the "destination principle". Under this system, the exporter obtained a rebate for all VAT paid on its inputs from its national tax authorities, while the importer paid VAT at the applicable rate in their Member State. This system was largely the result of the persistent differences in national VAT rates. In this way, the destination principle prevented goods imported from another European Community country from benefiting from a lower rate of VAT than applicable to domestic supplies of the same good.[67]

9.23 Before the advent of the Single Market, Member States' customs authorities were crucial to the functioning of the system, as the goods had to be presented for inspection at the border of the exporting nation before they would authorise the VAT rebate to be paid to the supplier.[68] However, with the abolition of internal customs controls between EU Member States as part of the introduction of the Single Market on 1 January 1993, the paying of the rebate to an exporter could no longer be made subject to a physical inspection of their paperwork at the border.

9.24 In anticipation of this change, the Commission made a proposal for a new VAT system based on the "origin principle" in 1987, meaning that VAT would have to be accounted for in the country where the goods are when transport to another Member State begins or the sale is made, and then passed on to the Member State of consumption. Its key features were a harmonised tax structure with two rates of VAT; harmonisation, within two defined bands, of the rates applied by Member States; and a clearing mechanism for redistributing VAT receipts to the Member State where consumption took place.[69]

9.25 The Council could not reach agreement on these proposals, resisting the clearing mechanism for redistribution of VAT receipts, as well as the harmonisation of VAT rates. The Member States therefore decided to adopt transitional arrangements which allowed tax to continue to be collected in the Member State of destination of the goods at the rate

66 See paragraph 9.70 for more detail on the VAT-related implications of Brexit.

67 The alternative is a system based on the "origin principle", under which VAT is collected in the country of export and rebated to the importer in the country of destination.

68 In essence, this system was identical to the VAT-rebate process that EU shoppers experienced before the introduction of the Single Market.

69 See COM(1989) 260, 14 June 1989.

and under the conditions of that country. As a simplification, however, VAT had to be accounted for by the business buying the goods, to avoid the supplier having to comply with the VAT legislation of another Member State.[70]

9.26 The functioning of the destination principle, in the absence of intra-EU border controls and with responsibility to account for the tax lying with the buyer, means that cross-border intra-EU B2B transactions are split into a zero-rated, VAT-free cross-border supply (by the seller) and a fictional VAT-taxable cross-border acquisition (by the buyer, who effectively has to charge himself VAT).[71] To enable Member States to track cross-border supplies of goods in the absence of border controls, the VAT Directive requires suppliers to submit a monthly recapitulative statement via the VAT Information Exchange System (VIES),[72] showing intra-EU supplies made, including the VAT number of the buyer. However, under the case law of the Court of Justice, the zero-rate exemption of an intra-EU supply of goods cannot be refused solely because of the absence of a valid VAT identification number of the customer.[73]

9.27 The European Commission has therefore compared the current arrangement to a "customs system [which] lacks equivalent controls", generating new opportunities for VAT evasion. In particular, the ability to zero-rate a transaction based on the claim that the goods are being exported to another EU Member State, without the inspection at the border and coupled with the deficiencies of the VIES system, increased the opportunities for missing trader fraud and carousel fraud.[74]

9.28 For trade in goods with non-EU countries, the pre-1993 system of payment of VAT at the border still applies as such imports are not exempt from customs controls. This is clearly highly relevant in the context of the UK's withdrawal from the EU, and its future status of "third country" vis-à-vis the EU.

Efforts to reform the cross-border VAT system

9.29 The current system for cross-border taxation of the supply of goods was meant to be transitional. The Commission was initially supposed to present proposals for the "definitive VAT system", based on the origin principle,[75] by the end of 1994 for entry into force in 1997.[76] However, the proposals put forward by the Commission in the mid-1990s were not accepted by the Member States,[77] and the fundamental question about the application of either the origin or destination principle remained unresolved, including when the VAT Directive was recast in 2006.[78]

70 European Parliament, "Working Paper: Options for a definitive VAT system" (PE 165.529).

71 See Article 138 of the 2006 VAT Directive.

72 The recapitulative statement is usually referred to as the EC Sales List (ESLs).

73 See the judgments of the Court in cases C-273/11 *Mecsek-Gabona*, C-587/10 *VSTR*, C-24/15 *Plöckl* and C- 21/16 *Euro Tyre*.

74 Intra-EU missing trader VAT fraud takes place when the company buys goods from another Member State, because purchasing the goods is VAT-free. When selling the goods on domestically, the company receives the entire amount of VAT, which it pockets rather than transferring it to the Treasury. Because the company disappears, this type of fraud is called missing trader fraud. Carousel fraud takes this a step further: the same goods are bought and resold by the fraudster several times via middlemen, and each time the amount of collected VAT increases and the company either disappears or becomes insolvent before the tax authority can collect the accumulated VAT.

75 Under this system, VAT is paid in the Member State where the supplier is based irrespective of the location of the customer.

76 See article 28L of the VAT Directive as introduced by Council Directive 91/680/EEC.

77 In 1996, the Commission proposed for VAT to be collected in one single Member State, with the revenues redistribution based on official macroeconomic statistics to ensure that VAT receipts accrued to the Member State of consumption.

78 See Commission proposal COM(2004) 246.

9.30 To break the deadlock, in 2010 the Commission published a Green Paper on reform of the EU's VAT system.[79] In light of the responses received, the Commission issued a follow-up policy paper in 2011 on the "future of VAT", in which it concluded that efforts to underpin the EU's VAT system with the origin principle, as called for in the original 1967 VAT Directive, remained "politically unachievable".[80] It therefore announced it would "launch substantial efforts to devise alternative concepts for a properly functioning destination-based EU system of VAT", and make proposals to that effect "in the first half of 2014". In 2012, EU Finance Ministers unanimously expressed their support for a move to such a system.[81]

9.31 After further delays,[82] the European Commission published a new Action Plan on VAT in April 2016.[83] It concluded that the VAT system ought to be simplified and made more efficient; provide fewer opportunities for fraud; and rely on greater cross-border cooperation between tax administrations. To achieve these goals, the Commission reiterated its intention to publish legislative proposals for the introduction of a "definitive VAT system" for intra-EU cross-border trade based on the principle of taxation in the Member State of destination, at the first instance for trade in goods (the "first legislative step") and subsequently for services as well (the "second legislative step", ending the use of the reverse charge procedure for such supplies).[84]

9.32 The Commission concluded that that best option was to tax cross-border B2B supplies of goods within the EU in the same way as domestic supplies, meaning that suppliers should account for VAT in the Member State of destination.[85] It would end the zero rating of cross-border supplies which gives rise to missing trader fraud, as the supplier would have to account for the VAT for one taxable event, and no zero-rated supplies would be allowed.

9.33 EU Finance Ministers welcomed the VAT Action Plan in May 2016, but underlined that the thrust of the forthcoming Commission proposals was only one among various options available for reform of the VAT system.[86] In addition, in November that year, the

79 Commission document COM(2010) 695. Cleared from scrutiny by the 2010–2015 European Scrutiny Committee on 8 June 2011.

80 See Commission document COM(2011) 851. Cleared from scrutiny by debate in European Committee B on 23 April 2012.

81 ECOFIN Council conclusions of 15 May 2012.

82 Despite the delays in reforming B2B VAT, the Council did take steps to introduce the "destination principle" to taxation of cross-border business-to-consumer (B2C) supplies of goods and services (which account for far lower volumes of cross-border trade), which the first reforms taking effect in 1 January 2015 and further changes expected to follow in 2019 and 2021. We reported on these reforms separately in our Report of 22 November on the e-commerce VAT package.

83 Commission document COM(2016) 148. Cleared from scrutiny by debate in European Committee B on 21 February 2017.

84 The Action Plan also committed the Commission to other proposals, which have also since been published and several of which we will consider in due course. These include: modernisation of VAT rates policy (document X); a package of measures to simplify VAT accounting for SMEs (document Y) and a proposal to improve administrative cooperation between Member States' tax authorities (document Z).

85 The Commission ruled out the use of a generalised "reverse charge mechanism", where VAT is 'suspended' along the whole economic chain and is charged only to consumers (compared to the current fractionated system, under which VAT is paid by every intermediary in the supply chain and then deducted from their output VAT). It concluded that its general use would shift the entire VAT collection to the retail stage, making tax revenue flows less predictable, as well as providing new opportunities for fraud (e.g. fraudsters claiming to be businesses to obtain goods intended for final consumption VAT-free).

86 ECOFIN Council conclusions, 25 May 2016.

Council invited[87] the Commission to also bring forward short-term fixes to the common system of VAT while this "definitive new VAT system" is being negotiated, relating to the use of the VAT identification number, chain transactions and call-off stock.[88]

The Commission proposals

9.34 In October 2017, the Commission published three proposals to begin implementation of the "first legislative step" to formalise the use of the destination principle for cross-border sales of goods. These documents also contain four "Quick Fixes" to address known shortcomings of the VAT Directive in the short-term, while the new "definitive" system is put in place.

9.35 This package of measures consists of:

- A proposal for a Council Directive harmonising and simplifying certain rules in the value added tax system, and introducing the definitive system for the taxation of trade between Member States (document (A));[89]
- A proposal for a Council Regulation as regards the certified taxable person (document (B));[90] and
- A proposal for a Council Implementing Regulation as regards certain exemptions for intra-Community transactions (document (C)).[91]

Reinforcing the destination principle

9.36 The core of the Commission's proposals is document (A), which would establish, within the VAT Directive, the intention that the EU will replace the current system with "definitive arrangements based on the principle of taxation in the Member State of destination of the supply of goods or services", where liability to account for the VAT would rest with the supplier. Under this new system, cross-border sales would no longer be split into a non-taxed "supply" and a taxed "transaction". Instead, the concept of an "intra-Union supply" will be introduced as a single, taxable event.

9.37 It is important to note that the amendment proposed to the VAT Directive by the Commission in October 2017 would only set down the *principle* that VAT should be accounted for in the Member State of the buyer. As and when the Member States agree to establish this principle in law the Commission would table a proposal to "overhaul the whole VAT Directive". This further proposal, which the Commission hopes to put forward in 2018 for consideration by the Council, would apply only to sales of goods; a review will be published five years after entry into force of the new system, to help the Member States decide whether to extend it to the cross-border supply of services as well.

9.38 The Explanatory Memorandum for the proposed amendment to the VAT Directive and the Communication accompanying the Commission proposal (document (D))[92] set out, at high-level, how this new "definitive system" is envisaged to work in practice.

87 ECOFIN Council conclusions, 8 November 2016.
88 See paragraphs 9.51 to 9.63 for more information on these proposals.
89 Document A is COM(2017) 569.
90 Document B is COM(2017) 567.
91 Document C is COM(2017) 568.
92 Document D is COM(2017) 566.

The One Stop Shop

9.39 Firstly, to assist suppliers in accounting for VAT in Member States other than where they are based, they will be able to account for VAT for sales in any Member States through an extended **One Stop Shop** (OSS) via their national tax authority. This system would allow businesses to identify and account for VAT in their home Member State for all their sales in the EU, using the applicable VAT rate in the Member State of destination. Money paid to that Member State for sales in other EU countries is subsequently re-distributed to the relevant tax authority.[93]

9.40 As part of its extension to cross-border B2B supplies, the Commission foresees that the functionality of the OSS will be expanded to enable suppliers to use it to deduct their input VAT from the tax they have collected on sales rather than via a domestic VAT return.

Mutual assistance and cooperation

9.41 Secondly, the Commission recognises that increased use of the One Stop Shop would require more trust and **cooperation between tax administrations**, as the Member State where the goods arrive would have to rely, for the first time, on the Member State of departure to collect the VAT due on the cross-border supply, and redistribute it accordingly.[94] It has therefore also tabled separate proposals to increase statutory cooperation between the EU's tax authorities,[95] although the specific legislation on the functioning of the One Stop Shop under this new system will only be presented as the package of detailed measures in 2018.

Transitional measures and the "Certified Taxable Person"

9.42 Thirdly, the Commission proposes to mitigate the administrative impact of these changes on businesses, in particular the shift of liability for VAT from the buyer to the supplier in cross-border sales.

9.43 Notably, it seeks to introduce the legal concept of a "**Certified Taxable Person**" (CTP), in essence a business certified as a reliable taxpayer by their national tax authority (documents (A) and (B)). Such certification would be mutually recognised by all EU countries, and once granted would be entered into the VAT Information Exchange System so that traders across the EU could quickly verify whether a buyer or supplier is a CTP. In the context of the transition to the "definitive system" of VAT, where a buyer has CTP status, they would remain liable to account for VAT under a reverse charge mechanism, in derogation from the proposed principle that the supplier should have that responsibility.

9.44 The justification for continuing to place responsibility for VAT on the buyer, derogating from the new "definitive" cross-border VAT system, is that it would mitigate the initial impact on suppliers of having to account for the tax on cross-border sales, while limiting missing trader or carousel fraud because the goods would be supplied to a CTP, who would

93 The OSS is currently available only to businesses who sell electronic services to EU-based consumers, although the Council is currently considering expanding it to all cross-border sales to non-business consumers. See our Report on the e-commerce VAT package of 22 November 2017 for more information.

94 We note in this respect that Germany has already voiced concerns about increased use of the One Stop Shop for business-to-consumer supplies of goods and services. See our separate Chapter on the VAT e-commerce package for more information.

95 See Commission document COM(2017) 706. The proposal remains under scrutiny.

be "by definition (…) a reliable taxpayer". In these cases, there is no essential change in the way the VAT system works for cross-border supplies compared to the current situation. Depending on the status of their customers, suppliers would therefore need to administer two different systems to account for VAT on intra-EU supplies. It is unclear if the use of the CTP status in this way is meant to be transitional, or permanent.

Further simplification measures

9.45 Lastly, the Commission floats suggestions for future **simplifications of the cross-border VAT system**, for example through the abolition of the recapitulative statement of intra-EU supplies (the VIES listing) and new streamlined invoicing rules for cross-border supplies. It remains to be seen whether these will be taken forward in its detailed proposals in 2018.

Estimated impact of the proposals

9.46 In its impact assessment, the European Commission estimates that this new system for VAT on cross-border sales of goods could reduce annual volumes of missing trade fraud by €41 billion (£36 billion), a decrease of 83 per cent. It also says it would reduce administrative burdens on businesses by €1 billion (£890 million) a year, after the initial costs of shifting to the new system.[96] However, it is not clear if the Commission has considered any variations in the pattern of trade in goods that could result from the new system, or new methods or opportunities for VAT evasion that may arise.

The Government's view

9.47 The Financial Secretary to the Treasury (Mel Stride) set out the Government's position on the Commission proposals on the "definitive system" of VAT in his Explanatory Memorandum of 24 October 2017.[97] He welcomes the formal amendment to the VAT Directive to acknowledge that the objective is to ensure taxation at destination, as Member States stand to gain revenues through a reduction in missing trader fraud. However, the Minister adds that "any change from the current system should be justified on the basis of the benefits it brings to business and to the tax authorities, balanced against the burdens involved".

9.48 In his Memorandum, the Minister also cautions that both tax authorities and businesses would likely experience "cash flow gains or losses" if the new system is introduced. The supplier of a good will experience a new cash flow gain because they will hold the VAT paid by the buyer until the date of their One Stop Shop return, whereas the buyers—who can currently offset output VAT against input VAT on the same return, paying only the difference—"are likely to pay VAT before they are able to claim it back". Similarly, the buyer's national tax authority would no longer immediately receive the VAT due, but must wait for it to be redistributed by the Member State of the supplier.

9.49 While expressing the Government's support for the use of the One Stop Shop by businesses to quickly identify the correct VAT rate for a cross-border supply (reducing the administrative burden on suppliers), the Minister questioned the proposed expansion of the OSS' capabilities to include input VAT deduction by suppliers, as the current system

96 Commission Impact Assessment SWD(2017) 325, p. 59.

97 Explanatory Memorandum submitted by HM Treasury (24 October 2017).

was "not designed to fulfil such a role". He added that the VAT Refund Directive[98] already provides a mechanism for such refunds, giving HM Revenue & Customs and other national tax authorities the opportunity to "scrutinise claims and ensure validity or eliminate errors prior to re-payment being made". The Minister explained that "allowing an offset within a [One Stop Shop] VAT return will remove this opportunity and potentially open up the system to fraud and double claiming rather than making it more robust".

9.50 In relation to the new status of "Certified Taxable Person", the Minister stated the Government is "willing to explore the concept", provided that the "criteria used to assess whether a business qualifies for CTP status and how this status is monitored are effective". He expressed concerns, however, that the introduction of CTP status could create a "two-tier system for businesses and disadvantaging legitimate start up and smaller businesses who might find it disproportionally difficult or expensive to qualify for CTP status", and therefore miss out from the simplifications proposed as "Quick Fixes" before the new system takes effect (see paragraphs 9.51 to 9.63 below).

"Quick fixes" to the VAT Directive

9.51 In addition to enshrining the "destination principle" in the VAT Directive, the Commission has also proposed a number of technical "Quick Fixes" to the Directive in response to the EU Finance Ministers' request of November 2016.[99] These relate to increased use of the VAT identification number and new evidentiary standards for proof of intra-Community supply to reduce cross-border VAT evasion, and to the VAT treatment of call-off stock and chain transactions of goods.

Call-off stock

9.52 Call-off stock refers to a situation where a supplier transfers goods to a buyer's warehouse, without transferring legal title to the goods until the buyer chooses to take ownership. It is commonly used by online retailers, to ensure stock is available to fulfil orders placed through its website.

9.53 Under the VAT Directive, where call-off stock is provided to a buyer in a different Member State than the supplier, the latter makes a both a zero-rated supply and a (fictitious) intra-Community acquisition on arrival of the goods, and therefore has to register in the Member State of destination for VAT purposes. When the buyer subsequently takes ownership of the goods, a domestic transaction occurs. Some Member States have introduced simplification measures by which the fictitious intra-Community acquisition is eliminated, leading to a disjointed application of the VAT Directive.

9.54 To ensure a more uniform application of the rules, the Commission has proposed (in document (A)) that call-off stock arrangements should give rise to a single supply and acquisition, with the buyer accounting for VAT on that transaction when they take ownership of the goods. This would eliminate the need for the supplier to account for VAT on the fictitious intra-EU acquisition in all Member States.

98 Directive 2008/9/EC.

99 See paragraph 9.33.

Chain transactions

9.55 Chain transactions occur where multiple supplies of a good occur but there is only one cross-border transport within the EU (for example when supplier A sells its wares to buyer C via intermediary B, who employ transport company D to physically move the goods directly from supplier A to the buyer).[100] Under the current rules, tax authorities and companies often struggle to identify at which part of this chain the "intra-Community supply" occurs (which is the only element which can be zero-rated).[101]

9.56 The Commission has now proposed (in document (A)) that, ordinarily, the intra-Community supply should legally take place when the vendor supplies the goods to the first intermediary (provided that the latter is registered for VAT in a different Member State than where the transport of the goods begins, as that would constitute a purely domestic transaction). The VAT would then be due in the home country of the intermediary. If the intermediary is registered for VAT in the same country as where the transport begins, the intra-Community supply takes place when the goods are delivered to the final customer, with VAT due in the Member State of destination.

VAT identification number

9.57 To address the opportunities for missing trader and carousel fraud created by the current system, EU Finance Ministers asked the Commission to propose legislation requiring a supplier to provide a valid VAT identification number for the buyer on their EC sales list before the cross-border supply can be zero-rated. Currently, Member States can impose fines when the identification number is not supplied, but Court of Justice jurisprudence prevents them from refusing to grant the zero-rated exemption (see paragraph 9.26 above).

9.58 The Commission has therefore proposed (in document (A)) to make the provision of a valid VAT number for the buyer a substantive condition before the exemption can be granted.

Proof of Intra-Community supplies

9.59 As a second anti-fraud measure, the Council also asked the Commission to explore how suppliers might provide evidence to their tax authority of a cross-border sale of goods that qualifies for a zero-rate (in addition to the proposed new substantive requirement to provide the VAT identification number of the buyer as described above).

9.60 In response, the Commission has proposed an amendment to the VAT Implementing Regulation (document (C))[102] which would introduce the types of evidence a supplier could provide that a supply of goods to a buyer in another Member State had indeed

100 A more complicated variety of a chain transaction is a triangular transaction, where a business established in EU country A supplies goods to a customer in EU country B, but the goods are shipped directly to the customer from a third EU country (C).

101 See also the judgment of the Court of Justice in C-245/05, *Emag Handel*, in which it ruled that the intra-EU supply occurs where goods are "dispatched or transported by or on behalf of the vendor or the person acquiring the goods" from one Member State to another. This has been interpreted differently by different Member States.

102 The proposal relating to the evidentiary standard for intra-EU supplies is contained in a separate document because it requires an amendment to the Council Implementing Regulation, whereas the other "Quick Fixes" are amendments to the VAT Directive itself.

taken place, including a document certifying receipt of the goods, a transport company's invoice, or the VAT return of the buyer for that particular purchase. The same types of evidence could be used if the goods were transported by or on behalf of the buyer, if they provide the supplier with a written confirmation to that effect.

Restrictions on the "Quick Fixes"

9.61 The Commission has proposed that the improvements offered by its "Quick Fixes" relating to call-off stock, chain transactions and proof of intra-Community supplies will only be available where the supplier (and, in certain cases, the buyer or intermediary) has the new "Certified Taxable Person" status (see paragraph 9.43 above). The new substantive requirement relating to the provision of a buyer's VAT identification number to zero-rate a cross-border supply would be generally applicable.

The Government's view

9.62 In his Explanatory Memorandum, the Financial Secretary states that the details of the "Quick Fixes" will need to be "considered carefully", but has not made clear the Government's position on their substance. However, he makes clear that the Government does not believe the Commission had made a compelling case that the proposed changes relating to call-off stock, chain transactions and intra-Community supplies should be restricted to businesses with Certified Taxable Person status only.

9.63 With respect to making it a substantive requirement for a supplier to provide a valid VAT identification number for the buyer on their recapitulative statement before a cross-border sale can be zero-rated, the Minister states this "essentially confirms" the Government's interpretation of existing law, and it supports "putting this matter beyond doubt".

Next steps

9.64 In his Explanatory Memorandum, the Minister notes that detailed consideration of the proposals are unlikely to begin until early 2018. He adds that "rapid progress is not expected on this dossier", given the "expected diversity of views from Member States, the significant nature of the proposed changes and the need for unanimity". Similarly, the European Parliament has not yet established a timetable for the delivery of its non-binding opinion on the proposals.

9.65 The Commission's plan is that further legislative proposals will follow in 2018 to cover detailed rules for implementation of the destination principle. Separately, on 29 November 2017, it also published further draft legislation based on its VAT Action Plan, including proposals on the improvement of administrative co-operation between EU tax authorities; the modernisation of the VAT rates structure; and a package of measures to simplify VAT accounting for small businesses. We will consider these in a separate Report in due course.

Our assessment

9.66 The Commission proposals, and in particular the first formal steps towards full application of the destination principle which shifts responsibility back to the supplier in intra-EU trade, are a major development in the EU's common system of value added tax.

9.67 We are not convinced that the reforms proposed by the Commission can sensibly be described as a simplification measure. It would effectively create a new transitional system with two parallel systems for cross-border supplies of goods, where a buyer or supplier, depending on the Certified Taxable Person status of the counterparty, would have to apply different VAT rules.[103] The proposal, if implemented, would entail significant changes for the administrative burden on exporters, as they would become accountable for VAT (especially as and when the exemption where the buyer is a CTP is removed). More broadly, we question the value of enshrining the principles for the "definitive arrangement" for cross-border VAT in the Directive when proposals for the practical implementation of that system will not be tabled by the Commission until 2018, and we would be grateful for the Minister's view on legislating intent rather than practicality.

9.68 With respect to the "Quick Fixes" to the current cross-border VAT system, we await further information from the Minister about the Government's position on their merit and technical feasibility.

9.69 We ask the Minister to keep us informed of progress in the deliberations within the Council on these proposals. In particular, we are interested in:

- the position taken by other Member States on the "definitive system" proposed by the Commission, including the extension of the OSS and the introduction of the reverse charge mechanism where the buyer is a Certified Taxable Person;
- the perceived accuracy of the Commission's impact assessment, especially the estimate that its preferred method for implementing the "destination principle" would result in a reduction in VAT fraud of €41 billion and compliance costs for businesses by €1 billion;
- the way in which applications for CTP status would be assessed and monitored, and the likely impact on the resources of national tax authorities including HM Revenue and Customs; and
- the Council's position on the "Quick Fixes", and whether these provisions could be split off from the negotiations on the "definitive system" of VAT, to ensure a speedier adoption and entry into force.

Implications of Brexit

9.70 We have also considered these proposals, and the EU's common system of VAT more broadly, in the context of the UK's withdrawal from the EU. This package of measures—including both the elements related to the "destination principle" and the "Quick Fixes" to the current system—concern only the application of the VAT system to intra-EU supplies of goods. The Minister, in his Explanatory Memorandum, has not provided any indication that they are likely to have a material impact on the UK once it is outside the common system of value added tax.

103 The supplier would be accountable for VAT where the buyer is not a CTP, but if the latter is a CTP, they would be accountable for VAT. In addition, the Quick Fixes would only be available where both buyer and seller are CTPs.

Remaining in the common VAT area during the "implementation period"

9.71 We cannot yet be certain when the UK will actually leave the common VAT area. It remains unclear whether the Government expects—or indeed envisages—that the UK will stay part of that common system for the duration of the "implementation period" that the Prime Minister requested in her Florence speech, which would operate under the "framework" of "existing EU rules and regulations".[104]

9.72 The consequence of staying in that VAT area for an interim period would be that the current system of intra-Community supplies, and the related vulnerabilities to fraud, would continue to apply to UK businesses. Moreover, the proposals contained in the Commission documents we have discussed in this Report may come to apply in the UK, depending on the speed of their adoption and the length of the transitional period. We have asked the Minister to confirm whether it is the Government's intention to stay in the common VAT area for the duration of the "implementation period".

9.73 In any event, it is clear that such a transitional arrangement will only postpone rather than negate the implications of the UK becoming a "third country" vis-à-vis the European Union. We have briefly described these below.

VAT controls on imports

9.74 Goods imported into the EU from non-EU countries are subject to border controls, to make sure they meet EU standards before they are released into free circulation. In addition, these controls aims to ensure that all relevant taxes—including any customs duties and VAT—are paid.

9.75 UK businesses will therefore automatically face border controls and other trade restrictions placed on the export of goods into the EU by virtue of its Customs Union and Single Market. In the context of value added tax, when the UK leaves the common VAT area, the remaining Member States will have to apply border controls on UK goods exported to the EU to ensure VAT is paid.[105] Similarly, the Government is expected to collect VAT on goods imported from the EU as it does at present for imports from non-EU countries. This also applies at the border between Ireland and Northern Ireland. In the absence of customs controls, once the UK has left the VAT Information Exchange System, it is unclear how the Government would collect VAT due on goods bought from outside the UK transported into its territory via the Irish border. Moreover, even if the UK made a unilateral decision not to impose VAT or customs controls, Ireland does not have such leeway under its EU Treaty obligations unless the relevant sectoral legislation is amended.

9.76 The Chancellor has recently reiterated calls for "free and frictionless trade"[106] between the UK and the EU after Brexit, and the Government's paper on future UK-EU customs arrangements appears to suggest that the UK having to operate "standalone customs,

104 Speech by the Prime Minister (Florence, 22 September 2017).

105 Of course, VAT is only one of a range of tariff and non-tariff barriers that will automatically apply to UK exports to EU countries once the UK leaves the EU and its Single Market. Many of those relate to the UK's regulatory standards that will no longer be automatically recognised by the EU. This is likely to be the case under any UK-EU free trade agreement as well, as it results from the UK's exit from the Single Market.

106 HM Treasury, "Autumn Budget 2017: Philip Hammond's speech" (22 November 2017): "*My Right Honourable Friend the Prime Minister has been clear that we seek a deep and special partnership, based on free and frictionless trade in goods and services, close collaboration on security and strong mutual respect and friendship.*"

VAT and excise systems", including the imposition of customs duties and import VAT on exports going in either direction, is "not the Government's preferred outcome", and could be mitigated by "further facilitations or agreements".[107]

9.77 It is unclear if the Government aims to fulfil this by ambition by negotiating a system which avoids such border controls on UK-EU trade flows altogether, following the end of the "implementation period". This would, presumably, require a replication in some way of the VIES for UK-EU trade in goods which will enable VAT checks to be waived (even if that, in itself, would not solve the issue of other checks carried out at the border which also require physical inspection).

9.78 In the White Paper on the Customs Bill,[108] the Government alluded to the potential economic ramifications of the reintroduction of customs and VAT controls between the UK and the EU:

> "Many business sectors in the UK operate complex supply chains which can involve components crossing borders between EU Member States multiple times during the production process. Time-dependent supply chains (such as fresh foods, medical goods, e-commerce, or just-in-time manufacturing employed by, for example, the automotive industry) have benefitted from the absence of routine customs controls in intra-EU trade, because they are particularly sensitive to administrative burdens and delays caused by customs procedures."

9.79 However, although it underlines the value of the absence of customs and VAT controls on intra-EU trade, the Government then describes the use of the system of intra-Community supplies compared to border controls as a difference in "accounting treatment". We question the description of such a substantial difference in the way in which VAT is accounted for as such, given that the Government's own preferred outcome is to maintain "free and frictionless trade", and it has recognised the potential detrimental effects of border controls on businesses with "time-dependent supply chains".

9.80 Overall, we are not convinced that the imposition of VAT and customs controls between the UK and the EU after Brexit could be avoided through a negotiated settlement. The EU has not abolished border controls for VAT and customs purposes for imports from any non-Member State (including the EFTA-EEA countries Norway, Iceland and Liechtenstein, which are members of the Single Market, or Turkey, which has a customs union with the bloc). We are also unaware of the abolition of such controls between other customs jurisdictions, other than within the EU itself. Therefore, such controls are likely on UK-EU trade even if a trade or customs agreement is negotiated.

Other consequences of leaving the Common VAT Area

9.81 The UK's exit from the common VAT area, whether in March 2019 or at the end of any "implementation period", will also have important implications for the way the UK VAT system operates domestically, as well as for HM Revenue's participation in EU-level

107 DExEU, "Future Partnership Paper—future customs arrangements" (15 August 2017).
108 HM Treasury, "Customs Bill: legislating for the UK's future customs, VAT and excise regimes" (9 October 2017).

mechanisms for the exchange of information on VAT and fraud. We will return to these matters in more detail in our forthcoming Reports on the recent Commission proposals relating to VAT rates and mutual assistance between tax authorities.

9.82 In anticipation of the Minister's reply to our questions, we have retained the proposals for a Council Directive and the Council Regulation on the Certified Taxable Person (documents A and B) under scrutiny, and cleared the proposed Council Implementing Regulation and the accompanying Communication (documents C and D).

Previous Committee Reports

None.

10 EU participation in Council of Europe Convention and Additional Protocol on the Prevention of Terrorism

Committee's assessment	Legally and politically important
Committee's decision	Not cleared from scrutiny; further information requested; drawn to the attention of the Home Affairs Committee
Document details	(a) Proposal for a Council Decision on the conclusion, on behalf of the European Union, of the Council of Europe Convention on the Prevention of Terrorism (CETS No. 196); (b) Proposal for a Council Decision on the conclusion, on behalf of the European Union, of the Additional Protocol supplementing the Council of Europe Convention on the Prevention of Terrorism (CETS No. 217)
Legal base	(a) and (b) Article 83(1) and 218(6)(a) TFEU, QMV, EP consent
Department	Home Office
Document Numbers	(a) (39144), 13424/17 + ADD 1, COM(17) 606; (b) (39143), 13425/17 + ADD 1, COM(17) 607

Summary and Committee's conclusions

10.1 The Council of Europe Convention on the Prevention of Terrorism was adopted in the aftermath of the 9/11 terrorist attacks in the United States of America. Participating countries are required to criminalise behaviour which may lead to acts of terrorism, such as public provocation or incitement of terrorism, recruitment for terrorism and the provision of training for terrorism. These criminal offences must be accompanied by "effective, proportionate and dissuasive penalties" and implemented in a way which respects human rights obligations, in particular the right to freedom of expression, association and religion. There are specific provisions on protection, support and compensation for victims of terrorism. The Convention also includes rules on jurisdiction and on international cooperation in investigating and prosecuting terrorist offences.

10.2 The Convention has been supplemented by an Additional Protocol which gives effect to the criminal law aspects of UN Security Council Resolution (UNSCR) 2178 (2014) on *Threats to international peace and security caused by terrorist acts* and seeks to strengthen further the legal framework for preventing terrorism and tackling foreign terrorist fighters.[109] Under the Additional Protocol, participation in an association or group for the purpose of terrorism, receiving training for terrorism, and travelling abroad (or funding

109 UNSCR 2178 (2014).

or otherwise facilitating such travel) for the purpose of terrorism are to be made serious criminal offences and an around-the-clock contact point designated in each participating country to exchange information on foreign terrorist fighters.

10.3 The UK has signed but not yet ratified the Convention and Additional Protocol. In 2015, the Council adopted Decisions authorising the EU to sign both instruments.[110] These Decisions were subject to the UK's Title V (justice and home affairs) opt-in. The then Government contested the Commission's view that the EU had exclusive competence in areas governed by the Convention and Additional Protocol and said it was undertaking its own competence analysis. It accepted that the EU and Member States shared competence in relation to counter-terrorism measures and that the Council was entitled to authorise the EU to sign the Convention and Additional Protocol. Nonetheless, the Government decided *not* to opt in, and made clear that competence in this area should be exercised by Member States:

> "Security is a matter for national governments and national parliaments. Whilst cooperation across borders is important—indeed, often necessary—it is for the UK to judge what is best done in our national interest. Not opting into these proposals will ensure that the UK cannot be caught by any exercise of EU competence in this area […]."[111]

10.4 The final versions of the 2015 Council Decisions (unlike the Commission's original proposals) include a recital which makes clear that the EU is only authorised to act "as regards matters falling within the competence of the Union in so far as the Convention/Additional Protocol may affect those common rules or alter their scope" and that Member States "retain their competence in so far as the Convention/Additional Protocol does not affect common rules or later the scope thereof"—meaning that EU participation is limited to those (unspecified) provisions of the Convention and Additional Protocol for which the EU has acquired exclusive competence based on the adoption of internal EU rules.[112]

10.5 The Commission has now proposed two further Council Decisions which would authorise the EU to conclude (ratify) the Convention—document (a)—and the Additional Protocol—document (b). The Commission appears to accept that the Convention covers areas of shared competence as well as areas of exclusive EU competence. By contrast, it asserts that the EU has *exclusive* competence to conclude the Additional Protocol since all its provisions "overlap with" and are "covered to a large extent" by EU law.[113]

10.6 The Security Minister (Mr Ben Wallace) indicates that the Government is "not minded to opt in at this stage" as "it would not be in the national interest to do anything which could bind us to an exercise of EU competence in relation to counter-terrorism which could limit our future ability to act independently on terrorism legislation; or which could grant the Court of Justice of the European Union jurisdiction over national security matters in relation to the UK".[114]

110 See Council Decision (EU) 2015/1913 and Council Decision (EU) 2015/1914.

111 See the letter of 17 September 2015 from the then Security Minister (Mr John Hayes) to the Chair of the European Scrutiny Committee.

112 See recital (6) of Council Decision (EU) 2015/1913 and recital (5) of Council Decision (EU) 2015/1914.

113 See p.4 of the Commission's explanatory memorandum accompanying document (b).

114 See para 11 of the Minister's Explanatory Memorandum.

10.7 **In correspondence on a separate matter—law enforcement access to data held in the EU's asylum database (Eurodac)—the Immigration Minister (Brandon Lewis) told us:**

> **"Article 4(2) TEU [Treaty on European Union] expressly provides that national security remains the sole responsibility of each Member State. It is a Treaty provision which speaks for itself."**[115]

10.8 **We ask the Minister whether he agrees that Article 4(2) TEU "speaks for itself" in precluding any EU competence for matters of national security? If so, does he also agree that there is no basis in the EU Treaties for the Court of Justice to assert jurisdiction over matters of national security?**

10.9 **It is disappointing that the Minister provides no analysis of the division of competences between the EU and Member States in relation to terrorism, given that this was a major pre-occupation of the previous Government when examining the proposed Council Decisions on signature of the Convention and Additional Protocol in 2015. It is striking that the proposed Council Decisions authorising the EU to conclude (ratify) the Convention and Additional Protocol do not appear to constrain in any way the areas in which the EU is competent to act, unlike the earlier Decisions on signature. Does the Government intend to press for the inclusion of a recital limiting the EU's participation in the Convention and Additional Protocol to matters for which the EU has *exclusive* competence?**

10.10 **Since authorising the EU to sign the Convention and Additional Protocol in 2015, the EU has adopted a Directive on combating terrorism which covers much of the same ground as the Council of Europe instruments and which Member States are required to transpose into their domestic laws by 8 September 2018.**[116] **Although the UK has not opted into the Directive, does the Minister consider that it tips the balance towards establishing that the EU now has exclusive competence to sign the Convention and/or the Additional Protocol or does he consider that there remain areas of shared competence? Should the proposed Council Decisions include a recital setting out the internal measures (including the Directive) on which the EU's assertion of exclusive competence is based?**

10.11 **We would welcome a more detailed insight into the position of other Member States, particularly those that have already ratified the Convention and (in much smaller numbers) the Additional Protocol. Does the Minister expect Member States to exert pressure to include additional wording limiting EU participation in the Convention and Additional Protocol to matters falling within the exclusive competence of the Union, ensuring that Member States are free to act in areas of shared competence? If they were to succeed, would the Government consider opting in after the Council Decisions have been adopted, given that the Minister says that the Government is "not minded to opt in at this stage"?**

10.12 **The Minister tells us that the UK is fully compliant with the Convention and Additional Protocol, following the passage of the Counter-Terrorism and Security Act 2015, and that the Government intends to ratify both instruments. We ask him whether there are any remaining impediments and how soon he expects the UK to proceed to ratification.**

115 See the Minister's letter of 13 July 2017 to the Chair of the European Scrutiny Committee.

116 See Directive (EU) 2017/541 on combating terrorism.

10.13 **The proposed Council Decisions remain under scrutiny pending further information. We draw this chapter to the attention of the Home Affairs Committee.**

Full details of the documents

(a) Proposal for a Council Decision on the conclusion, on behalf of the European Union, of the Council of Europe Convention on the Prevention of Terrorism (CETS No. 196): (39144), 13424/17 + ADD 1, COM(17) 606'; (b) Proposal for a Council Decision on the conclusion, on behalf of the European Union, of the Additional Protocol supplementing the Council of Europe Convention on the Prevention of Terrorism (CETS No. 217): (39143), 13425/17 + ADD 1, COM(17) 607.

Background

10.14 The Committee's previous Reports (listed at the end of this chapter) provide details of the earlier Council Decisions authorising the EU to sign the Convention and Additional Protocol and the factors informing the Government's decision not to opt in.

The proposed Council Decisions authorising the EU to conclude the Convention and Additional Protocol

10.15 The Commission notes that the Convention came into force on 1 June 2007. All EU Member States and the EU have signed the Convention; 23 Member States have ratified it. The Additional Protocol came into force on 1 July 2017. The EU and 25 Member States have signed the Additional Protocol; only five Member States have ratified it. The remaining Member States and the EU may only ratify the Additional Protocol once they have ratified the Convention (or ratify both instruments simultaneously).

10.16 In its explanatory memorandum accompanying document (a), the Commission identifies 13 EU police and criminal justice measures—the latest being a Directive on Combating Terrorism adopted in March 2017—which establish the EU's competence to act in areas covered by the Convention. It says that these measures "highlight the need for Member States to act within the framework of the EU institutions when undertaking international commitments in the area of fighting terrorism".[117] The UK participates in more than half of these measures but has not opted into the Directive on Combating Terrorism.

10.17 The Commission appears to accept that the Convention covers areas of shared competence as well as areas of exclusive EU competence. By contrast, it asserts that the EU has *exclusive* competence to conclude the Additional Protocol since all its provisions "overlap with" and are "covered to a large extent" by EU law.[118]

10.18 Both proposed Council Decisions include an introductory recital stating that "the Union has already adopted measures in the different areas covered by the Convention/ Additional Protocol" but only one measure—a 2002 Council Framework Decision on combating terrorism—is specifically mentioned.[119] The UK does not participate in this Framework Decision, one of the EU police and criminal justice measures which ceased to apply to the UK from 1 December 2014. Neither of the proposed Council Decisions seeks to constrain in any way the areas in which the EU is competent to act. This contrasts

117 See p.4 of the Commission's explanatory memorandum accompanying document (a).
118 See p.4 of the Commission's explanatory memorandum accompanying document (b).
119 See recitals (3) and (4) in document (a) and recitals (3) and (5) in document (b).

with the Council Decisions authorising the EU to sign the Convention and Additional Protocol which include recitals limiting the EU's competence to provisions covering areas of exclusive EU competence—meaning provisions which may affect common rules adopted by the EU or alter their scope.

10.19 The substantive legal base for both proposed Council Decisions is Article 83(1) of the Treaty on the Functioning of the European Union (TFEU). This reflects the Commission's view that "the predominant purpose" of the Convention and the Additional Protocol is to introduce criminal offences relating to terrorism—Article 83(1) authorises the EU to establish minimum rules on the definition of particularly serious criminal offences which have a cross-border dimension. The Council is required to obtain the consent (approval) of the European Parliament before adopting the proposed Decisions.[120]

10.20 The Commission accepts that both proposed Council Decisions are subject to the UK's Title V (justice and home affairs) opt-in Protocol and that the UK will only be bound by them if the Government decides to opt in. This contrasts with the Commission's view that Ireland (also a beneficiary of the Title V opt-in Protocol) is automatically bound by the proposed Council Decisions because, unlike the UK, it continues to participate in the 2002 Council Framework Decision on combating terrorism.

The Minister's Explanatory Memorandum of 27 November 2017

10.21 The Minister says that following the passage of the Counter-Terrorism and Security Act 2015, UK law is "fully compliant" with the Convention and Additional Protocol. The UK did not opt into the 2015 Council Decisions authorising the EU to sign the Convention and Additional Protocol, has signed both instruments independently of the EU and "plans to ratify them".[121]

10.22 He notes that the Government will need to decide whether it wishes to opt into the proposed Council Decisions authorising the EU to conclude (ratify) the Convention and Additional Protocol. The three-month period for opting in at the negotiating stage and securing a vote will expire on 19 January 2018. The Minister continues:

> "The longstanding approach of the UK Government is that it would not be in the national interest to do anything which could bind us to an exercise of EU competence in relation to counter-terrorism which could limit our future ability to act independently on terrorism legislation; or which could grant the Court of Justice of the European Union jurisdiction over national security matters in relation to the UK."

10.23 In light of these concerns, he indicates that the Government is "not minded to opt in at this stage".

Previous Committee Reports

None on these documents, but see the Committee's earlier Reports on proposed Council Decisions authorising the EU to sign the Convention and Additional Protocol: First Report HC 342–i (2015–16), chapter 39 (21 July 2015); Third Report HC 342–iii (2015–16), chapter 27 (9 September 2015); and Fifth Report HC 342–v (2015–16), chapter 31 (14 October 2015).

120 See Article 218(6)(a) TFEU which sets out the procedures for concluding an international agreement.

121 See para 7 of the Minister's Explanatory Memorandum.

11 EU-Canada Agreement on Passenger Name Record Data

Committee's assessment	Politically important
Committee's decision	Not cleared from scrutiny; scrutiny waiver granted; further information requested; drawn to the attention of the Home Affairs Committee and the Committee on Exiting the European Union
Document details	Recommendation for a Council Decision authorising the opening of negotiations on an Agreement between the European Union and Canada for the transfer of Passenger Name Record (PNR) data to prevent and combat terrorism and other serious transnational crime
Legal base	Articles 16(2), 87(2)(a) and 218(3) and (4) TFEU, QMV
Department	Home Office
Document Number	(39151), 13490/17 + ADD 1, COM(17) 605

Summary and Committee's conclusions

11.1 The UK has been at the forefront of EU efforts to promote the sharing of Passenger Name Record (PNR) data both within the EU (a new EU PNR Directive will take effect next May) and externally through the negotiation of PNR Agreements with third countries. EU data protection law prohibits the transfer of personal data to third countries unless they ensure an adequate level of protection—in practice, protection "essentially equivalent" to that guaranteed within the European Union.[122] In an Opinion issued in July, the Court of Justice accepted that the transfer of PNR data to third (non-EU) countries was justified to protect public safety, but said that some of the provisions of a draft PNR Agreement between the EU and Canada were incompatible with fundamental rights and contrary to EU law. The proposed Council Decision would authorise the Commission to re-open negotiations with Canada to the extent needed to make the Agreement compatible with EU law. It is subject to the UK's Title V (justice and home affairs) opt-in Protocol (Protocol 21) and will only be binding on the UK if the Government decides to opt in.

11.2 In his Explanatory Memorandum submitted on 1 November, the Immigration Minister (Brandon Lewis) was unable to tell us when the three-month deadline for opting into the proposed Council Decision would expire, adding:

> "We will provide further advice to the Scrutiny Committees on when they will be expected to comment on the Decision and when the UK has to opt in to the measure in accordance with Protocol 21 once the deadlines have been published."[123]

122 See p.2 of the Commission's Explanatory Memorandum accompanying the proposed Council Decision.

123 See para 10 of the Minister's Explanatory Memorandum.

11.3 In reaching a decision on UK participation in the proposed Council Decision, he indicated that the Government would have "particular regard" to two aspects of the Court's Opinion: first, that the Canadian authorities should (in most cases) only retain PNR data on individuals for as long as they remain in Canada; and second, that the onward transfer or disclosure of PNR data should only be permitted to a third (non-EU) country which has concluded a PNR Agreement with the EU or has obtained a Commission adequacy decision.

11.4 We asked the Minister to:

- clarify the Government's concerns with these aspects of the Court's Opinion and indicate how readily they could be resolved;
- comment on the implications of the Opinion for existing EU/PNR Agreements with Australia and the US; and
- explain how the UK's exit from the EU would affect its ability to share PNR data with third countries.

11.5 We also asked the Minister to tell us at the earliest opportunity when the three-month opt-in deadline would expire so that we could consider whether to recommend an opt-in debate.

11.6 In his letter of 30 November, the Minister says that the Estonian Presidency intend to agree the proposed Council Decision at the Justice and Home Affairs Council on 7–8 December. He continues:

> "Given the UK's acknowledged leadership on PNR matters I am minded to opt into the Council Decision and vote in favour of its adoption."

He invites us to clear the proposal from scrutiny, adding that "future Council Decisions on signature and conclusion of the Agreement will be subject to scrutiny and the opt-in will apply in the usual way".

11.7 Turning to the questions we raised in our earlier Report, the Minister considers that the Government's concerns with certain aspects of the Court's Opinion could be met by applying a broad interpretation to some of the conditions set out in its ruling. To this end, he notes that the proposed Decision has been amended to give the Council greater oversight of the Commission's conduct of the negotiations with Canada. He anticipates that changes will need to be made to the EU's PNR Agreements with Australia and the US but says that the timing and substance of any renegotiation rests with the Commission. He also anticipates that the UK will need to negotiate its own PNR agreements with Australia, Canada and the US on exit, regardless of any transitional/implementation period. Whilst the EU's PNR agreements with third countries provide a template, "the UK is not tied to replicate these" in the agreements it negotiates with third countries. He expects the UK to "maintain equivalency with the EU on data protection" once it leaves the EU and says that "maintaining respect for fundamental rights will remain an integral element" of any PNR agreements the UK concludes with third countries or with the EU post-exit. He adds that the Court's Opinion will also be "an important consideration" in ensuring that PNR agreements are limited to what is strictly necessary to secure their public safety objectives.

11.8 **The Minister says that the Government is "minded to opt into" the proposed Council Decision and to vote for its adoption at the Justice and Home Affairs Council on 7/8 December, even though the three-month deadline for reaching an opt-in decision has not yet expired. He offers no explanation for the Presidency's haste in bringing the proposal to the Council for decision nor indicates whether he considers that there are special circumstances that justify curtailing the time available to scrutinise the Government's opt-in decision.**

11.9 **This is not an isolated incident. There is a depressing history of EU PNR Agreements being pushed through scrutiny with undue haste. We recall that a similar situation arose on a proposed Council Decision to sign a PNR Agreement with Australia in 2011. The Home Secretary at the time (Mrs Theresa May) told our predecessors on that occasion that "the UK was very clear that, under the Treaty, we should be allowed to exercise our option to allow Parliament to scrutinise the Agreement within our three-month window for opting in".[124] Later that year, she informed the Committee that the Government had decided to "waive its Treaty rights to three months' opt-in consideration" on a proposed Council Decision to sign a PNR Agreement with the United States of America, but only after the Home Secretary had made representations "at the highest level about our entitlement to a three month opt-in period".[125]**

11.10 **We recognise that the circumstances are different in this case. The proposed Council Decision is the first of several steps towards securing a revised PNR Agreement. Further Council Decisions—and separate opt-in decisions—will be needed to authorise the EU to sign and conclude the agreement that emerges from the negotiations with Canada, meaning that the UK will only be bound by the eventual outcome of negotiations if the Government chooses to opt in. We consider that the UK will be in a better position to influence the outcome of negotiations, which may well serve as a model for a future EU/UK PNR agreement, if it participates in the negotiations. Given these factors, we agree to grant a scrutiny waiver to enable the Government to support the adoption of the proposed Council Decision. We do so with some reluctance and ask the Minister to explain:**

- **whether the Government has made any representations to the Presidency to protest at its handling of the proposed Council Decision and its apparent disregard for the procedures set out in the UK's Title V opt-in Protocol;**
- **whether he considers an early opt-in decision to be "necessary" or "essential" in this case;[126] and**
- **whether the Government intends to make a minutes statement underlining the importance it attaches to full adherence to the three-month opt-in period provided for in the UK's opt-in Protocol.**

11.11 **Turning to the implications of the UK's exit from the EU, the Minister appears to rule out the possibility of "grandfathering" existing EU PNR agreements with third countries during a transitional period, so that these would continue to apply**

124 See Thirty-fifth Report HC 428–xxxi (2010–12), chapter 2 (29 June 2011).

125 See Forty-eighth Report HC 428– (2010–12), chapter 4 (7 December 2011).

126 Under the so-called "Ashton undertakings" made to Parliament in 2008, where the Government considers that an early opt-in decision is "necessary" or "essential", it will explain its reasons to the Scrutiny Committees "as soon as is possible".

while the UK negotiates new agreements to take effect at the end of a transitional/implementation period. The effect would seem to be the same as a "no deal" or a deal without a transitional/implementation period, with a gap arising between existing EU/third country PNR agreements ceasing to apply to the UK and the UK being in a position to conclude new bilateral PNR agreements. Does the Minister accept that there is likely to be a gap and that this would create risk and uncertainty for carriers? How does the Government intend to mitigate this risk?

11.12 **The Minister says that the EU's PNR agreement with third countries provide a "template" for future negotiations, but that "the UK is not tied to replicate these in any future UK-third country PNR Agreement". Given that the Government also says it intends to "maintain equivalency with the EU on data protection", we ask him whether he agrees that the scope for divergence from the EU "template" will be extremely limited and that, the greater the degree of divergence, the higher the risk that the UK will be unable to conclude its own PNR agreement with the EU.**

11.13 **Whilst we have agreed to grant a scrutiny waiver so that the Government can support the adoption of the proposed Council Decision at the forthcoming Justice and Home Affairs Council, we remind the Minister that the proposal remains under scrutiny. We ask him to report back to us promptly on the outcome of the Council and to provide us with the information we have requested as well as updates on the progress of negotiations. We draw this chapter to the attention of the Home Affairs Committee and the Committee on Exiting the European Union.**

Full details of the documents

Recommendation for a Council Decision authorising the opening of negotiations on an Agreement between the European Union and Canada for the transfer of Passenger Name Record (PNR) data to prevent and combat terrorism and other serious transnational crime: (39151), 13490/17 + ADD 1, COM(17) 605.

Background

11.14 Our earlier Report listed at the end of this chapter describes the current framework for the transfer of PNR data to Canada and the reasons why the Commission is seeking a mandate from the Council to re-open negotiations with Canada.

The Minister's letter of 30 November 2017

11.15 We noted in our earlier Report that the UK had participated fully in the negotiation of EU PNR Agreements with third countries (including, most recently, Mexico in June 2015). As the proposed Council Decision would instruct the Commission to negotiate a new Agreement with Canada containing all the safeguards specified in the Court's Opinion, we questioned how much scope this would leave to negotiate out any elements of the Court's Opinion that the Government disliked. We asked the Minister to clarify the Government's concerns about the safeguards envisaged on the retention of PNR data and their onward transfer to third (non-EU) countries and explain whether he believed they could be resolved whilst still complying with the Court's Opinion.

11.16 The Minister responds:

> "On data retention, in its Opinion the Court said that the Canadian authorities should only retain PNR data for as long as the passenger is in Canada and that the data should be deleted once the passenger leaves Canada, unless there is objective evidence from which it can be inferred that the data might make an effective contribution to combatting terrorist offences or serious transnational crime.
>
> "The Government assess that it is possible to resolve this issue in line with the Court's Opinion, if this condition is applied broadly e.g. setting a minimum data retention period where data can be used to build an intelligence picture to enable the Canadian authorities to identify the transit of foreign terrorist fighters through Canada or to identify the trafficking of people through Canada. If this condition is applied in a strict way e.g. deleted once a passenger leaves Canada this would seriously impede the Canadian authorities use of the PNR data for the purpose it was acquired as some subjects of interest, including victims of trafficking, would become undetectable after their onward departure from Canada."

11.17 Turning to the conditions for onward transfer of PNR data to third (non-EU) countries, the Minister explains:

> "[…] in its Opinion the Court said that the Canadian authorities may only transfer EU PNR to a third country with an equivalent Agreement with the EU or an adequacy decision of the Commission covering the authority to which the data is to be disclosed.
>
> "The Government assess that it would be possible to resolve this issue in line with the Court's Opinion, if the principles of Article 11 of the EU Directive on the use of PNR data (EU/2016/681) are followed. Article 11 allows the disclosure of PNR data to a third country only on a case by case basis when the transfer is necessary for the purposes of countering-terrorism and serious crime. If the Opinion of the Court were applied in a strict way, it would mean that the proposed Agreement would impose higher standards for protection of PNR data on third countries than those which EU Member States must meet under the Directive."

11.18 He says that changes have been made to the wording of the proposed Council Decision "as a direct result of concerns being expressed by the UK and some other Member States". The revised text makes clear that the Commission must conduct the negotiations with Canada "in consultation with the relevant Council Working Party and in accordance with the directives contained in the addendum, subject to any directives which the Council may subsequently issue to the Commission".

11.19 We asked the Minister whether changes would need to be made to the EU's PNR Agreements with Australia and the United States of America and to indicate how soon he expected the renegotiation process to be started. He responds:

> "The timing and the substance of any renegotiation of the EU PNR Agreements with Australia and the United States are a matter for the European Commission. However, I anticipate that the Commission will wish to renegotiate those agreements."

11.20 We invited the Minister to comment on the consequences for the UK of *not* opting into the proposed Council Decision and any subsequent Decisions on the signature and conclusion of a new PNR Agreement with Canada (or other third countries). Would this mean that there would no longer be a lawful basis for air carriers operating from the UK to continue to transfer PNR data to the countries concerned? The Minister replies:

> "The Government assess this transfer of PNR data will continue. Following the expiry of the EU-Canada PNR Agreement in 2009, the Canadian authorities provided assurances in a form of an official letter to Member States stating that they would continue to protect and use EU PNR data in accordance with the expired Agreement until a new Agreement had been ratified. In the event the UK decided to opt out of the Agreement(s), we anticipate similar assurances ahead of the UK entering into Agreement(s) with those countries."

11.21 We noted that the Minister had not explained how the UK's exit from the EU would affect its ability to share PNR data with third countries and sought answers to a series of questions. We asked whether the Government intended that existing EU PNR Agreements in which the UK participates should continue to apply during any transitional or implementation period following the UK's withdrawal and what mechanism was envisaged to ensure their continued application. The Minister draws our attention to the Government's future partnership paper, *The exchange and protection of personal data* (published in August) which sets out the intention to "maintain data protection standards equivalent to those of the EU".[127] He continues:

> "Given this position we anticipate that the UK will need to establish PNR Agreements with Australia, Canada and the United States in place of the current EU arrangements."

11.22 We asked what effect no deal or transitional/implementation period would have on transfers of PNR data to third countries currently covered by PNR Agreements with the EU. None, according to the Minister:

> "We do not anticipate that a no deal/implementation period will have an effect on the transfer of PNR data by UK carriers to third countries covered by the EU's PNR Agreements as the UK's own agreements will be negotiated separately and there are no dependencies on our negotiations with the EU."

11.23 We questioned, in the longer term, how much scope the UK would have to depart from the data protection requirements set out in EU PNR Agreements when negotiating its own agreements with third countries. We asked:

- whether the Government accepted that the data protection safeguards contained in UK PNR agreements with third countries would materially affect the UK's prospects in seeking to negotiate its own PNR Agreement with the EU or securing a Commission adequacy decision; and

127 See the future partnership paper. The Exchange and Protection of Personal Data.

- whether the Government also accepted that, whichever route it wished to take, a UK/EU PNR Agreement or adequacy decision would need to comply with EU fundamental rights and the requirements set out in the Court's recent Opinion.

11.24 The Minister responds:

> "Our aim with these agreements will be to ensure that third countries provide an adequate level of protection to UK PNR data and an effective operational capability to those countries to safeguard their national security. While the EU's PNR Agreements provide a template, the UK is not tied to replicate these in any future UK-third country PNR Agreement.
>
> "Given that the UK intends to maintain equivalency with the EU on data protection, I do not believe that the safeguards for these UK PNR Agreements will materially affect the UK's prospects in seeking to negotiate its own PNR Agreement with the EU or securing a Commission adequacy decision in respect of the processing of EU PNR data by the UK. Maintaining respect for fundamental rights will remain an integral element of whatever form of agreement is reached. The Opinion of the Court is going to be an important consideration both within the Council as the negotiation proceeds with Canada and for the UK's own negotiations, to secure agreements which are no more than is necessary for the purposes of the Agreement."

Previous Committee Reports

First Report HC 301–i (2017–19), chapter 28 (13 November 2017).

12 EU Emissions Trading System 2021–2030

Committee's assessment	Politically important
Committee's decision	Cleared from scrutiny (by Resolution of the House on 13/12/2016); further information requested; drawn to the attention of the Business, Energy and Industrial Strategy Committee
Document details	Proposal for a Directive amending Directive 2003/87/EC to enhance cost-effective emissions reductions and low-carbon investments
Legal base	Article 192(1) TFEU; QMV; Ordinary Legislative Procedure
Department	Business, Energy and Industrial Strategy
Document Number	(37003), 11065/15 + ADDs 1–3, COM(15) 337

Summary and Committee's conclusions

12.1 The EU Emissions Trading System (ETS) is a central component of efforts to meet carbon dioxide reduction targets in a cost-effective and technologically neutral way. Companies can either buy allowances giving the right to emit carbon dioxide or they can take action to reduce carbon dioxide and sell allowances to others. There is a fixed limit on the number of allowances available, reducing over time. Some allowances are auctioned and some allowances are available free.

12.2 In July 2015 the Commission put forward a proposal for a Directive which would set out the arrangements to apply in Phase IV (from 2021 to 2030), including measures to strengthen the effectiveness of the System.

12.3 The proposal was first considered by the Committee on 16 September 2015 and debated in European Committee on 12 December 2016, after which the document was cleared from scrutiny. During that debate, the then Minister for Climate Change and Industry (Nick Hurd) made it clear that no decision had been taken on the UK's future engagement in the EU ETS but that—regardless of future UK participation—a strong EU ETS was in the UK's national interest.

12.4 When our predecessors last considered the document, at their meeting of 25 April 2017, they expected the Government to have either arrived at a position on future arrangements or be close to that stage. They asked that, when the Government next wrote with an update, information on the UK's approach to the EU ETS post-Brexit should be included.

12.5 The Minister for Climate Change and Industry (Claire Perry) wrote on 12 July, informing the Committee that there had been little further progress in the negotiations. On Brexit, the Government was still considering a range of options, from remaining in the system to introducing a domestic alternative. The Government's guiding principle would

be ensuring an outcome which was in the best interests of the UK, including ensuring continued adherence to the carbon budgets, under the UK Climate Change Act, as cost effectively as possible and maximising industrial competitiveness.

12.6 The Minister has written again, explaining that agreement was reached among the institutions on 8 November. The Government was content with the compromise, noting that the agreement reached meets the UK's key objectives of increasing the strength of the carbon price signal, while ensuring industrial sectors are given adequate protection from the risk of carbon leakage.[128]

12.7 As to the UK's withdrawal from the EU, the Minister refers to the Brexit amendment made to the related aviation emissions proposal,[129] which sought to protect the environmental integrity of the EU ETS in the event of an abrupt Brexit. While the Minister understands the motivation behind the amendment, she believes that it would have significant negative impacts on the smooth operation of the carbon market. The Government is therefore working closely with the EU institutions to explore alternative solutions. To this end, the Government published a consultation on 6 November on bringing forward the 2018 compliance deadline for UK operators to before the date of EU Exit. The Minister hopes that, through these actions, a suitable, alternative solution for all parties and stakeholders can be found.

12.8 On wider post-Brexit considerations, the Government has still not reached any decision on post-Brexit arrangements.

12.9 **We note the final outcome of the negotiations on the future EU ETS, which demonstrate continued commitment to a strengthening of the System.**

12.10 **It is with some concern, however, that we monitor developments on future arrangements for the EU ETS post-Brexit. We too understand the EU's desire to protect the EU ETS. While the Government might be frustrated with the EU's approach, the last-minute rush to resolve the issue might have been avoided if the Government had set out its stall on potential future arrangements. Indeed, the Government's reluctance to do so has been frustrating to this Committee.**

12.11 **Our concern is now for UK operators and the position in which they find themselves, potentially taking on worthless allowances from 1 January 2018. We look to the Minister to set out developments in the Government's negotiations on this matter and to explain the impact of any resolution, or lack of it, on UK operators.**

12.12 **The document has already been released from scrutiny. We draw this chapter to the attention of the Business, Energy and Industrial Strategy Committee.**

Full details of the documents

Proposal for a Directive amending Directive 2003/87/EC to enhance cost-effective emissions reductions and low-carbon investments: (37003), 11065/15 + ADDs 1–3, COM(15) 337.

128 Generally energy-intensive industries, such as cement and steel, which might re-locate to countries which have a weaker (and therefore cheaper) regulation of emissions, thus simply transferring the emissions elsewhere rather than reducing them.

129 COM(17) 54—see earlier chapter of this Report.

Background

12.13 In 2014, the European Council agreed a 2030 policy framework for climate and energy, which included a binding target to reduce overall EU greenhouse gas emissions by at least 40% compared with 1990 levels, and it also took the view that, in order to achieve this target cost-effectively, the sectors covered by the EU ETS would have to reduce their emissions by 43% compared with 2005 (with a corresponding reduction of 30% from other sectors).

12.14 The Commission accordingly put forward these proposals relating to Phase IV of the ETS from 2021 to 2030, including:

- from 2021, the annual decrease in the EU emissions cap would rise from 1.74% to 2.2%; and
- 57% of allowances would have to be auctioned, with the remaining 43% given away free.

12.15 Further details on the proposals were set out in the previous Committee's Report of 16 September 2015.[130] In that Report, our predecessors concluded that the document was significant and had no hesitation in recommending it for debate in European Committee A. The debate took place on 12 December 2016, at which point the document was cleared from scrutiny.

12.16 The Minister wrote on 21 March 2017 to update the Committee on progress in both the European Parliament and Council, following adoption of their positions on 15 and 28 February respectively. In summary, both institutions supported changes designed to strengthen the carbon price signal. While both institutions supported measures designed to protect those industries at risk of carbon leakage, their approaches differed in the extent to which they divert funds from national budgets. Furthermore, the European Parliament wished to impose stricter emissions requirements for access to the Modernisation Fund for projects in lower income Member States. The aim was to avoid the provision of this funding source to coal-fired power stations. The Council text was significantly less stringent in this respect.

12.17 The previous Committee last considered this document at its meeting of 25 April 2017. It noted that the Government was yet to take a decision on the UK's participation in the Emissions Trading System (ETS) post-Brexit and that, as the EU ETS involves reciprocal arrangements, the default position in the absence of a negotiated agreement on future engagement would be non-participation. The Committee expected the Government to have either arrived at a position or be close to that stage. It asked that, when the Government next wrote with an update, information on the UK's approach to the EU ETS post-Brexit be included.

Minister's letter of 12 July 2017

12.18 The Minister informs the Committee that there had been little further progress in the negotiations. The Government would like to see agreement by the end of the year. On Brexit, the Government was still considering a range of options, from remaining in the

130 Fourth Report HC 324–iv (2015–16), chapter 1 (16 September 2015).

system to introducing a domestic alternative. The Government's guiding principle would be ensuring an outcome which was in the best interests of the UK, including ensuring continued adherence to the carbon budgets, under the UK Climate Change Act, as cost-effectively as possible and maximising industrial competitiveness.

Minister's letter of 15 November 2017

12.19 The Minister writes to update the Committee on the negotiations, following agreement between the institutions on 8 November, and on the work being undertaken to determine the UK's relationship with the system post-Brexit.

12.20 The Minister indicates that the agreement reached meets the UK's key objectives of increasing the strength of the carbon price signal, while ensuring industrial sectors are given adequate protection from the risk of carbon leakage. On the strengthening of the carbon price signal, the agreement includes the following to help drive up the price of allowances and incentivise greater investment in low carbon technologies:

- improvements to the Market Stability Reserve (MSR)[131] that will soak up a greater proportion of surplus allowances from the earlier start date of 2019; and
- measures to cancel surplus allowances in the MSR above a certain threshold from 2023 onwards.

12.21 The agreed package equally ensures that businesses who are operating in competitive international markets receive adequate protection to prevent the risk of carbon leakage:

- a conditional increase to the percentage share of free allowances by up to 3%, if needed, to prevent the application of a cross sectoral correction factor that would otherwise uniformly reduce free allocation to industry as the cap declines and there are insufficient allowances to cover all emissions;
- from the middle of the phase (2026), as the risk of a correction factor increases, a reduction in free allowances for those sectors deemed not at risk of carbon leakage, allowing free allocation to be more focused; and
- a conditional increase to the funding available for low carbon innovation projects, through the innovation fund, so that the total value is equivalent to 450 million allowances.

12.22 The deal does not include a central harmonised fund at EU level for compensation for indirect costs to industry, which would have compromised Member States' fiscal sovereignty.

12.23 Finally, in relation to the fund which supports lower income Member States' energy infrastructure modernisation, agreement was reached to rule out funding for projects using coal as a fuel, with the exception of district heating projects in Romania and Bulgaria.

12.24 Final adoption is foreseen by the Environment Council on 19 December.

131 The MSR is designed to avoid significant fluctuations in the carbon price. It will remove allowances at times of excess and release them when the number of allowances on the market dips below a fixed threshold or of there is a surge in the carbon price.

EU Exit

12.25 On the UK's exit from the EU, the Minister refers to the amendment designed to protect the EU ETS from an abrupt UK departure from the system in March 2019, which was proposed by the European Parliament on the aviation emissions proposal (see earlier chapter of this Report). The Commission has subsequently proposed draft regulations to amend the EU ETS Registry Regulation to implement this amendment.

12.26 The amendment aims to protect the environmental integrity of the EU ETS in case of an abrupt UK exit from the EU in March 2019. The issue has arisen because permits for emissions in the previous calendar year are surrendered on 30 April. This would mean that, in the event of an abrupt exit, UK companies would not need to surrender their allowances for emissions in 2018. Instead, they could sell their allowances, possibly flooding the market and thus potentially distorting the carbon price. To overcome this issue, it has been agreed that allowances issued by the UK from 2018 would be marked as such and would be invalid where the obligations for operators are "lapsing" due, for example, to the UK's exit from the System.

12.27 While the Minister understands the motivation behind the amendment, she is concerned that these proposals would have significant negative impacts on the smooth operation of the carbon market. The Government is therefore working closely with the EU Institutions to explore alternative solutions. To this end, the Government published a consultation on 6 November on bringing forward the 2018 compliance deadline for UK EU ETS operators to before the date of EU Exit. The Minister hopes that, through these actions, a suitable, alternative solution for all parties and stakeholders can be found.

12.28 The Minister sets out the longer-term approach in the following terms:

> "Looking further ahead, the Government continues to consider the UK's future participation in the EU ETS, or otherwise, after our exit from the EU. As set out in the Clean Growth Strategy, published in October, we remain firmly committed to carbon pricing as an emissions reduction tool, while ensuring energy and trade intensive businesses are appropriately protected from any detrimental impacts on competitiveness. Whatever our future relationship with the EU, we will continue to reduce emissions in the sectors covered by the EU ETS and will seek to ensure that our future approach is at least as ambitious as the existing scheme and provide a smooth transition for the relevant sectors."

Previous Committee Reports

Fortieth Report HC 71–xxxvii (2016–17), chapter 21 (25 April 2017); Fourth Report HC 324–iv (2015–16), chapter 1 (16 September 2015).

13 Stability and Peace Instrument

Committee's assessment	Politically important
Committee's decision	Cleared from scrutiny
Document details	Proposal for a Regulation amending Regulation (EU) No. 230/2014 of 11 March 2014 establishing an instrument contributing to stability and peace
Legal base	Articles 209(1) and 212(2) TFEU; ordinary legislative procedure; QMV
Department	Foreign and Commonwealth Office
Document Number	(37930), 11037/1/16, REV 1 + ADDs 1–2, COM(16) 447

Summary and Committee's conclusions

13.1 The EU's Instrument contributing to Stability and Peace (IcSP) is a €2.3 billion (£2 billion)[132] programme which funds the EU's rapid response to political instability in the developing world, as well as its longer-term conflict prevention, peace-building and crisis preparedness initiatives globally.[133]

13.2 In July 2016, the European Commission sent a legislative proposal to the European Parliament and the Council, with the aim of allowing €100 million (£82.65 million) of the Instrument's funds to be spent on "capacity building in support of security and development" (CBSD), essentially improving developing countries' military capacity to ensure they can adequately protect their civilian population. Rather than reducing the budget for the existing elements of the Instrument, the Commission proposed that the €100 million would be diverted from other parts of the EU budget for external affairs.[134]

13.3 The details of the Commission proposal, and the background to its consideration by the Council and Parliament, are set out in more detail in our Report of 13 November 2017.[135]

13.4 The Member States' representatives in COREPER agreed the Council's negotiating mandate for negotiations with the European Parliament on the legislative proposal in December 2016, but the Government did not alert us to this fact until May 2017. In October, trilogues led to an agreement on the final legislative text of the amendment which preserved the substance of the Commission proposal.

13.5 When we considered the state of play on the proposal following the trilogue agreement, we asked the Minister for Europe (Sir Alan Duncan) to explain the lengthy delay in informing the Committee of the existence of the negotiating mandate adopted by COREPER. We also asked him to clarify which existing EU budget lines would be

132 €1 = £0.91973 or £1 = €1.08728 as at 1 September 2017.

133 The IcSP was established by Regulation 230/2014. It was cleared from scrutiny on 12 February 2014.

134 The details of the Commission proposal, and the background to its consideration by the Council and Parliament, are set out in more detail in our Report of 13 November 2017.

135 See our Report of 13 November 2017.

reduced to fund the €100 million endowment for CBSD activities under the amended Regulation, and provide more information about UK-EU cooperation on foreign policy and international development more generally after Brexit.[136]

13.6 The Minister replied to our questions on 22 November.[137] He apologises for the administrative error which had led to the delay in informing the Committee of the adoption of the Council's negotiating mandate. He also explains that the funding for the new CBSD was likely to come from "redeployment of unspent funds among the instruments and budgets" under the EU budget's external affairs heading, but that the Parliament had secured a guarantee that no funding would be diverted from the EU's Development Cooperation Instrument for this purpose.[138]

13.7 With respect to the budgetary implications of the proposal in the context of the UK's withdrawal, and possible contributions to the EU budget in 2019, 2020 and beyond, the Minister states only that these "are being considered and will be resolved as part of the exit negotiations, where necessary" and that the Government "will seek a fair financial settlement in accordance with the law and in the spirit of our continued partnership with the EU". More generally, the UK's post-Brexit participation in external financing instruments—including the IcSP—"will be a topic for the negotiations". He addes that future UK-EU collaboration should be a "dynamic arrangement" which is "subject to UK standards on transparency, accountability and value for money".

13.8 The European Parliament adopted the Regulation on 30 November, and formal approval by the Council is expected to follow before the end of 2017.

13.9 **We thank the Minister for his swift response to our Report of 13 November, and accept his apology for the delay in informing the Committee of the COREPER negotiating mandate. We now clear the Regulation from scrutiny.**

13.10 **With respect to the implications of Brexit for UK cooperation with the EU on matters of foreign policy, it is clear the Government is considering whether, and if so how, the UK might continue to participate in the EU's external financing programmes, including the IcSP, after Brexit. The Minister has reiterated that it remains a matter for negotiations.**

13.11 **As the European Scrutiny Committee, we take a particular interest in the Government's approach to continued alignment with EU policy after Brexit, including potential financial contributions to specific EU programmes. We have yet to receive any substantive information from the Government about how its "deep and special partnership" would operate in practice, and what legal or institutional framework might be necessary to replace the structures in which the UK will cease to be represented in March 2019. Until we receive confirmation from the Government to the contrary, we will also presume that the "implementation period" sought by the Prime Minister would, in effect, maintain the UK's participation in, and contribution to, EU foreign policy instruments for its duration.**

136 Idem.

137 Letter from Sir Alan Duncan to Sir William Cash (22 November 2017).

138 The Development Cooperation Instrument was established by Regulation 233/2014, which was cleared from scrutiny by the previous Committee on 12 February 2014.

13.12 **We will continue to press the Government for more specific proposals about post-Brexit cooperation with the EU on matters of foreign policy and international development. If the Article 50 negotiations move to the framework for future UK-EU relations following the European Council in December 2017, we expect the Government to be more forthcoming about the details of its proposals, including the implications of the "implementation period" for the representation of the UK's interests in the EU's decision-making structures and the institutional mechanisms for UK participation in EU foreign policy programmes after the end of the transitional period. This will allow us to consider the appropriate methods for parliamentary scrutiny of such participation once the UK is no longer represented on the Foreign Affairs Council or its preparatory bodies.**

Full details of the documents

Proposal for a Regulation amending Regulation (EU) No. 230/2014 of 11 March 2014 establishing an instrument contributing to stability and peace: (37930), 11037/1/16 REV 1, + ADDs 1–2, COM(16) 447.

Previous Committee Reports

11037/16: Tenth Report HC 71–viii (2016–17), chapter 3 (7 September 2016) and First Report HC 301–i (2017–19), chapter 16 (13 November 2017).

14 Sanctions on Venezuela

Committee's assessment	Politically important
Committee's decision	Cleared from scrutiny; drawn to the attention of the Foreign Affairs Committee
Document details	(a) Proposal for a Council Decision concerning restrictive measures in view of the situation in Venezuela; (b) Proposal for a Council Regulation concerning restrictive measures in view of the situation in Venezuela
Legal base	(a) Article 29 TEU; unanimity; (b) Article 215 TFEU; QMV
Department	Foreign and Commonwealth Office
Document Numbers	(a) (39191),—; (b) (39195), 13694/17, JOIN(17) 39

Summary and Committee's conclusions

14.1 Venezuela's social, economic and political crisis drastically worsened in July this year, when President Maduro established a "Constituent Assembly" which has since usurped the legislative functions of the democratically-elected National Assembly.[139]

14.2 In view of the country's economic instability, the widespread repression of political dissent, and the numerous deaths at anti-government rallies, the EU's Foreign Affairs Council on 13 November approved a new legal framework for a sanctions regime against those "responsible for serious human rights violations or abuses or the repression of civil society and democratic opposition in Venezuela".[140] It also instituted an arms embargo against the country, and restricted the sale of equipment which could be used for internal repression. The proposals, which were drawn to our attention on 1 November, were adopted before the Committee had had a chance to scrutinise them.

14.3 The new sanctions regime has the support of the UK Government, which voted in favour of its creation at the Foreign Affairs Council. In an Explanatory Memorandum, the Minister for Europe and the Americas (Sir Alan Duncan) expressed the Government's concerns about "Venezuela's continued authoritarian slide", adding that "EU restrictive measures are a useful tool to encourage the Venezuelan Government to negotiate with the Opposition in good faith".[141]

14.4 **We thank the Minister for the information about the new sanctions regime and its political context, and we accept his explanation for the Government's override of scrutiny. Given the interest across the House in the situation in Venezuela, and considering this is an entirely new EU sanctions regime, we report these developments to the House and to the Foreign Affairs Committee in particular. Any further decisions by the Council to impose the tier II sanctions on specific people or bodies will be subject to scrutiny in their own right.**

139 House of Commons Library briefing, "Political situation in Venezuela" (1 September 2017).
140 See Council Regulation (EU) 2017/2063 and Council Decision (CFSP) 2017/2074.
141 Explanatory Memorandum submitted by the Foreign and Commonwealth Office (1 November 2017).

14.5 **We do not consider that these documents have any immediate implications in the context of Brexit. The Government has already introduced a Sanctions Bill to create the necessary legal framework to allow it to impose sanctions currently implemented through EU law.[142] The consequences of Brexit for the UK's cooperation with the EU on foreign policy more generally are less clear, and we await further clarification from the Minister in this respect in response to a previous Report on the Instrument contributing to Stability and Peace.[143]**

Full details of the documents

(a) Proposal for a Council Decision concerning restrictive measures in view of the situation in Venezuela: (39191),—; (b) Proposal for a Council Regulation concerning restrictive measures in view of the situation in Venezuela: (39195), 13694/17, JOIN(17) 39.

Background

14.6 Venezuela has been in the grip of a socio-economic crisis for several years, experiencing shortages of essential goods, hyperinflation and outbreaks of violence. A related political crisis, centred on the battle for legitimacy between the Government of President Nicolas Maduro and the opposition, came to a head in March 2017 when the Supreme Court—made up of supporters of the President—assumed the legislative functions of Congress after holding the latter "in contempt" of its powers. There have been numerous deaths at anti-Government rallies, as well as imprisonment of opposition figures.[144]

14.7 Within the EU, the situation in Venezuela is of particular concern to Portugal and Spain—whose citizens make up the majority of the 600,000 EU nationals in the country—and the Netherlands, which is responsible for the foreign relations of Curacao, an island off the Venezuelan coast. In May 2017, the Foreign Affairs Council called on both the Venezuelan Government and opposition to "work in a constructive manner towards a solution to the crisis in the country, in full respect of the rule of law and human rights, the democratic institutions and the separation of powers". It also called for the release of imprisoned political opponents and respect for constitutional rights, describing them as "crucial steps to building trust and helping the country to regain political stability".[145]

14.8 However, the situation deteriorated further over the course of the summer. Although the Supreme Court reversed its decision to take make itself the legislative branch, President Maduro subsequently announced that he would convene a "Constituent Assembly" to revise the country's constitution, despite widespread opposition. This new Assembly was elected at the end of July, with all seats taken by Government-supporting candidates after the other political parties boycotted the election. Since then, Assembly members have dismissed the Attorney General, voted to put opposition leaders on trial for treason, and given itself the power to pass legislation.[146]

14.9 With no end to the crisis in sight, the EU's High Representative for Foreign Affairs (Federica Mogherini) asked the Foreign Affairs Council in October 2017 to establish a

142 https://services.parliament.uk/bills/2017–19/sanctionsandantimoneylaundering.html.
143 See our Report of 13 November 2017.
144 House of Commons Library briefing, "Political situation in Venezuela" (1 September 2017).
145 Foreign Affairs Council conclusions on Venezuela (15 May 2017).
146 This latter development was strongly condemned by the Minister for Europe and the Americas (Sir Alan Duncan) on 19 August 2017.

new EU sanctions regime in view of the situation in Venezuela. The regime would enable travel bans and asset freezes to be imposed against "natural or legal persons, entities or bodies responsible for serious human rights violations or abuses or the repression of civil society and democratic opposition in Venezuela". Furthermore, in view of the risk of further violence against protestors from excessive use of force and human rights abuses by the security forces, the sanctions framework imposes economic (tier III) restrictive measures in the form of an embargo on arms from any Member State to Venezuela, as well as specific restrictions on the sale of equipment that may be used for internal repression.

14.10 The legal acts creating this new sanctions regime were approved by EU Foreign Affairs Ministers, including the Foreign Secretary, on 13 November. The Council has not yet put forward proposals to subject any specific persons or entities to the tier II sanctions, but the arms embargo has entered into effect.

14.11 The Minister for Europe (Sir Alan Duncan) submitted an Explanatory Memorandum on the High Representative's proposals on 1 November.[147] In it, he expresses the Government's concerns about "Venezuela's continued authoritarian slide". He adds that the Government expects the actions of the Constituent Assembly to "continue to worsen the lack of respect for democracy and human rights". He expresses his support for the new sanctions regime, arguing that "EU restrictive measures are a useful tool to encourage the Venezuelan Government to negotiate with the Opposition in good faith".

14.12 The sanctions regime will expire on 14 November 2018 unless a Decision is taken by the Council before that date to extend it further. Any such Decision would be subject to scrutiny in its own right.

Previous Committee Reports

None.

147 Explanatory Memorandum submitted by the Foreign and Commonwealth Office (1 November 2017).

15 EU-Norway Agreement on value added tax

Committee's assessment	Politically important
Committee's decision	Cleared from scrutiny; further information requested
Document details	(a) Proposal for a Council Decision on the signing of the Agreement between the EU and Norway on administrative cooperation, combating fraud and recovery of claims in the field of VAT; (b) Proposal for a Council Decision on the conclusion of the Agreement between the EU and Norway on administrative cooperation, combating fraud and recovery of claims in the field of VAT
Legal base	Articles 113, 218(5) and 218(8) second paragraph TFEU; unanimity
Department	Treasury
Document Numbers	(a) (39175), 13774/17 + ADD 1, COM(17) 624; (b) (39174), 13773/17 + ADD 1, COM(17) 621

Summary and Committee's conclusions

15.1 Fraud involving value added tax, for example through fictitious transactions, is a significant problem for tax authorities across the EU. In 2016, the European Commission released figures for the EU-wide "VAT gap",[148] estimating that nearly €160 billion (£44.5 billion)[149] in VAT revenues were lost in 2014. Although a framework is in place for cooperation between EU Member States to address VAT fraud (notably the Regulation on administrative cooperation and combating fraud in the field of value added tax[150] and the Directive on mutual assistance for the recovery of claims relating to taxes and duties),[151] the EU does not currently have administrative cooperation agreements with third countries specifically to address cross-border VAT fraud.[152]

15.2 However, in May 2017, the European Commission concluded two years of negotiations with Norway on the first such agreement, and in October presented the results to the Council for signature and conclusion (ratification). The new treaty will largely have the same scope and structure as the mechanisms for cooperation in this area as currently in force between EU Member States, including Norwegian participation in Eurofisc, the EU's mechanism for sharing information between tax authorities to combat organised VAT fraud.[153]

148 The VAT gap is the difference between the expected VAT revenue and the VAT actually collected by tax authorities.

149 €1 = £0.91973 or £1 = €1.08728 as at 1 September 2017.

150 See Council Regulation 904/2010.

151 See Council Directive 2010/24/EU.

152 http://europa.eu/rapid/press-release_MEMO-14–90_en.htm

153 The European Commission will also shortly issue a proposal to revise the operation of Eurofisc.

15.3 In his Explanatory Memorandum on the final agreement, submitted in November 2017, the Financial Secretary to the Treasury (Mel Stride) supported conclusion of the Agreement, saying it "will facilitate the exchange of information and administrative co-operation to better control and counter VAT fraud", which "is in the UK's interest".[154] He made no mention of the possibility of using the Agreement as a template for UK-EU cooperation on VAT after Brexit, although the Council has stated (apparently in the context of the UK's withdrawal) that the close nature of the cooperation with Norway in this area was linked to its membership of the European Economic Area and "will not constitute a precedent for future agreements in this area between the European Union and third countries".[155]

15.4 The Agreement must be signed and concluded by the Council, with both Decisions requiring a unanimous vote. In his initial Explanatory Memorandum, the Minister indicated that no timetable for this process had yet been set. However, it subsequently emerged that the Decision for signature would be put to the ECOFIN Council on 5 December 2017.

15.5 **We thank the Minister for his helpful overview of the contents of this new Agreement with Norway, and how it will facilitate the fight against VAT fraud. We consider that this new treaty between the EU and Norway is of political importance for two reasons: it is the first international agreement concluded by the EU on mutual assistance in the field of VAT, and it may form the template for a future UK-EU agreement on the same subject matter, following the UK's withdrawal from the Union.**

15.6 **The Minister's initial Explanatory Memorandum did not provide a timetable for adoption of the legal acts, meaning that we had not yet considered the proposals by the time the Decision to sign the Agreement was approved by the Council on 5 December. We await further information from the Minister on the Government's position during the vote, and the timetable for the adoption of the Decision concluding the Agreement.**

15.7 **More importantly, it is extraordinary that the Minister has not referred to the potential value of this Agreement as a possible template for future UK-EU relations on mutual assistance in the field of value added tax. By default, unless there is a legal agreement to the contrary, by March 2019 the UK, as a "third country", will have no formal structures in place for cooperation with the EU on tackling VAT fraud. Moreover, we have noted in the context of the VAT e-commerce package that such an Agreement would likely be a precondition for UK businesses to make use of the EU's simplified VAT accounting mechanism if they sell goods to EU-based consumers post-Brexit.[156] We are concerned, therefore, that the other Member States have already made clear that "this Agreement will not constitute a precedent for future agreements in this area between the European Union and third countries".**

15.8 **Upon withdrawal from the Union, the UK will, in principle, cease to participate in the system of exchange of information that underpins the EU's efforts to tackle VAT fraud. It is unclear whether the Government envisages that the temporary post-Brexit**

154 Explanatory Memorandum submitted by HM Treasury (16 November 2017).

155 See Council document 14703/17, p. 3.

156 The Mini One Stop Shop (MOSS) for VAT, which is due to be extended to the sale of certain goods by non-EU firms into the EU from 2021. See our Report of [date] for more information.

"implementation period",[157] should one be agreed, would preserve all of HM Revenue and Customs' EU-level rights and obligations in this regard for the full duration of the "implementation period".

15.9 **It is also clear that, despite the close economic relationship between the EU and Norway, this new Agreement will not obviate the existing requirement for checks of Norwegian goods presented at the EU border to ensure VAT is collected.[158] This will also be the default position of UK goods exported to the EU after Brexit, including at the Irish border, unless an agreement to the contrary is reached before March 2019, or before the end of any implementation/transitional period immediately following. We will return to this subject in more detail in our separate Report on the Commission proposals for a EU Single VAT Area.[159]**

15.10 **Given the above, we would like the Minister to clarify the following matters:**

- **What assessment has the Government made of the value to the UK of the cooperation and recovery mechanisms established by Regulation 904/2010 and Directive 2010/24/EU? What is the potential impact of ceasing to be part of those systems post-Brexit, including Eurofisc?**
- **Is the Government considering whether the EU-Norway Agreement is a possible template for a future UK-EU Agreement on tackling VAT fraud, in view of its position that "administrative co-operation and the exchange of information are still considered to be one of the most effective tools for fighting cross-border VAT fraud"?**
- **What is the Government's assessment in this regard of the Council statement that the EU-Norway Agreement does not set a precedent for future agreements with other "third countries" such as the UK post-Brexit? Did it consent to the inclusion of this statement in the Council minutes?**
- **Does the Government envisage that the UK will remain bound by Council Regulation 904/2010 and Directive 2010/24/EU during its proposed post-Brexit "implementation period"?**
- **What is the status of the Commission's talks with other international partners on VAT, including Russia, Canada, China and Turkey? With which non-EU countries does the UK already exchange information with respect to VAT on a bilateral basis?**

15.11 **As our questions do not relate to the substance of the EU-Norway Agreement as such, we are content to clear the draft Council Decisions from scrutiny and make this Report to the House. We ask the Minister to keep us informed of progress towards the adoption of the concluding Decision, as well as on discussions with Norway about its financial contribution under the Agreement (as the methodology and size of that arrangement are plainly of relevance to the UK if it would seek to negotiate a similar Agreement with the EU post-Brexit).**

157 Speech by the Prime Minister (Florence, 22 September 2017).
158 See European Commission, "Norway—Cross-border VAT" (accessed 20 November 2017).
159 See Commission document COM(2017) 569.

Full details of the documents

(a) Proposal for a Council Decision on the signing, on behalf of the European Union, of the Agreement between the European Union and the Kingdom of Norway on administrative cooperation, combating fraud and recovery of claims in the field of Value Added Tax: (39175), 13774/17 + ADD 1, COM(17) 624; (b) Proposal for a Council Decision on the conclusion, on behalf of the European Union, of the Agreement between the European Union and the Kingdom of Norway on administrative cooperation, combating fraud and recovery of claims in the field of Value Added Tax: (39174), 13773/17 + ADD 1, COM(17) 621.

Background

15.12 Fraud involving value added tax, for example through fictitious transactions, is a significant problem for tax authorities across the EU. In 2016, the European Commission released figures for the EU-wide "VAT gap",[160] estimating that nearly €160 billion (£44.5 billion) in VAT revenues were lost in 2014. €50 billion of that amount was likely to have been caused by fraud.[161] In the UK, the estimated VAT gap that year totalled €14.3 billion (£12.7 billion), as a result of fraud, insolvencies, administrative errors, and tax avoidance measures.[162]

15.13 At EU-level, Council Regulation 904/2010[163] and Council Directive 2010/24/EU[164] set down the current legal framework for cooperation between the Member States on preventing VAT fraud and recovery of VAT evaded. Among other things, this legislation:

- established the mechanisms for exchange of information between national tax authorities (both automatically and on request);
- granted authorities access to data on intra-EU operators and transactions stored in national databases via a secured electronic platform called VIES (the VAT Information Exchange System);
- gave national officials of Member States the opportunity to participate in administrative enquires in other Member States; and
- created Eurofisc, an instrument for multilateral exchange of information for the early detection of scheme of tax frauds, including a VAT observatory where Member States exchange best practices and information on fraud trends.[165]

15.14 The mechanisms created by the 2010 legislation applies only to EU Member States. However, VAT fraud is also perpetrated by exploiting weaknesses in the control of

160 The VAT gap is the difference between the expected VAT revenue and the VAT actually collected by tax authorities.

161 European Commission, "Study and Reports on the VAT Gap in the EU-28 Member States: 2016 Final Report" (23 August 2016).

162 Idem, p. 50.

163 Council Regulation (EU) No 904/2010 on administrative cooperation and combating fraud in the field of value added tax.

164 Council Directive 2010/24/EU concerning mutual assistance for the recovery of claims relating to taxes, duties and other measures.

165 The European Commission will shortly table a legislative proposal for reform of Regulation 904/2010, including the operation of Eurofisc. However, the proposed changes are not expected to enter into force before March 2019. The Committee will assess the implications of this proposal separately in a forthcoming Report.

transactions involving companies located in third (i.e. non-EU) countries.[166] Although the EU has an agreement with Switzerland to counter fraud and all other illegal activities affecting their financial interests,[167] it currently has no administrative cooperation agreements with third countries specifically to address cross-border VAT fraud.[168]

15.15 In December 2012, at the request of the European Council,[169] the European Commission published an Action Plan on tax fraud and evasion which confirmed its intention to negotiate mutual assistance agreements on VAT with non-EU countries.[170]

The Government's position

15.16 Initially, the Government expressed concerns that the Commission's proposals for agreements with non-EU countries on VAT fraud could lead to duplications. However, a subsequent survey established that very few EU countries had VAT administrative co-operation or information exchange agreements with third countries.[171] This also reflected the UK's situation, as the Government had only begun including VAT provisions in its model text for bilateral taxation treaties in 2008. In January 2015, the then Financial Secretary to the Treasury told our predecessors:

> "As Tax Treaty negotiations are usually resource intensive, slow and lengthy affairs, it could be another twenty or thirty years before the UK is able to put in place a comprehensive set of bilateral VAT information exchange arrangements with all its trading partners."[172]

15.17 Given the estimated scale of VAT evasion involving third countries, the Financial Secretary noted that "administrative co-operation and the exchange of information are still considered to be one of the most effective tools for fighting cross-border VAT fraud", adding that it would be "preferable that Member States have access to a legal gateway enabling them to share VAT information with their near neighbours or trading partners".

15.18 The Minister added that the EU's agreement with Switzerland on the protection of their financial interests, in contrast to the UK's unsuccessful attempts to negotiate a bilateral Anglo-Swiss anti-fraud treaty, "demonstrated that negotiating an EU wide agreement is more likely to succeed".

The EU-Norway Agreement

15.19 In February 2014, the Commission formally asked the Council for authorisation to start negotiations with Norway on administrative cooperation in the area of VAT fraud,

166 For example, goods imported from a non-EU country are declared as being in transit when they arrive in the EU. This means that they are not subject to VAT in the Member State of importation, but in the Member State of destination. In many cases, however, there is no such country of destination and the goods disappear without any VAT having been paid. HM Revenue and Customs is currently discussing the scale of such fraud in the UK linked to imports of Chinese textiles and footwear with the European Commission.

167 The EU-Switzerland Cooperation Agreement to combat fraud and any other illegal activity to the detriment of their financial interests. The Agreement has been applied in the EU since 8 April 2009.

168 European Commission, "Questions and Answers: Cooperating against VAT Fraud" (6 February 2014).

169 European Council conclusions, 1–2 March 2012.

170 See COM(2012) 722 (6 December 2012). Cleared from scrutiny by the previous Committee on 18 March 2015.

171 See SWD(2014) 39 (12 February 2014): "The very few Member States (BE, FR, SE and UK) that had an exchange of information with third countries, could not provide exact figures on the number of such exchanges."

172 Letter from David Gauke to Sir William Cash on "VAT Administrative cooperation with Norway" (8 January 2015).

given its level of economic integration with the EU and a history of close cooperation with the Union on tax evasion.[173] The Commission also noted it had started exploratory talks with Russia,[174] Canada, Turkey and China.[175] EU Finance Ministers authorised the Commission to begin negotiations with Oslo in December 2014.[176]

15.20 After the mandate was granted, the then-Financial Secretary to the Treasury, David Gauke, informed our predecessors that the Government believed it be "efficient and effective for the Commission to negotiate a multilateral framework agreement with Norway on our behalf".[177] The negotiations were conducted from summer 2015 to spring 2017, with the Member States' representatives in the Council's Working Party on Tax Questions being kept informed of progress. The Agreement was initialled in May 2017.[178]

15.21 In October 2017, the European Commission submitted the Agreement for signature and conclusion (ratification) by the Council. EU-Norway cooperation on VAT fraud will largely follow the same structure of the cooperation in this field as currently in force between EU Member States. This is laid down in Council Regulation 904/2010 and Directive 2010/24/EU, including automatic exchange of information and (limited) Norwegian participation in Eurofisc.[179] However, Norway will not be given access to the Member States' national VAT databases, nor the EU's VAT Information Exchange System (VIES) on intra-EU supplies.[180]

15.22 The Agreement also provides for a Joint Committee composed of the European Commission and Norway, operating under unanimity. The Committee will cover such areas as the amendment of forms for the submission of information; the categories for automatic information exchange; and the terms of Norway's financial contribution to the running of the system.

15.23 The Financial Secretary to the Treasury (Mel Stride) submitted an Explanatory Memorandum on the proposed Agreement on 16 November 2017.[181] He states that the Government "supports changes which will facilitate the exchange of information and administrative co-operation to better control and counter VAT fraud", as "an extension of existing intra-EU rules and tools to provide a legal means to co-operate with neighbours and close trading partners is in the UK's interest". With respect to the bilateral relationship between the UK and Norway, he adds that both countries "can currently ask for assistance of each other in the recovery of VAT debts under separate agreements", but that this new EU-wide Agreement "goes wider than this".

173 Although Norway has a system of VAT like the EU's, it is not subject to the VAT Directive as taxation is not included in the EEA Agreement. Any sale from a Norwegian business to a customer in the EU is considered an export from Norway, liable for import vat when it enters EU territory (and vice versa). At present, administrative cooperation with Norway on VAT matters is ad hoc and not institutionalised.

174 The Commission in February 2014 also requested a formal mandate to negotiate a VAT agreement with Russia. However, the mandate does not appear to have been discussed since May 2014 and has not been approved by the Council.

175 European Commission, "Tackling tax fraud: Commission proposes stronger cooperation with non-EU countries on VAT" (6 February 2014).

176 See the outcome of the ECOFIN Council meeting of 9 December 2014. The negotiating directives remain classified.

177 See footnote 15.13 for more information on Eurofisc.

178 https://ec.europa.eu/taxation_customs/node/949_en.

179 Norway will not have full access to the Eurofisc early warning system and cannot act as a Eurofisc co-ordinator or chair, neither will Norway be able to vote in Eurofisc decision making.

180 As VIES allows Member States to access information regarding intra-EU transactions, and it was not considered relevant in the context of the EU-Norway Agreement.

181 Explanatory Memorandum submitted by HM Treasury (16 November 2017).

15.24 He reiterates the Government's position that the negotiating of agreements on administrative cooperation in the field of VAT is "likely to be more efficient" at EU-level, because negotiating "can be slow and take up significant resources".

15.25 The Minister made no mention in his Memorandum of the possible value of this new Agreement as a template for UK-EU relations on VAT cooperation after Brexit. The Council, however, has stated publicly that the close nature of the cooperation with Norway in this area was linked to its membership of the European Economic Area and "will not constitute a precedent for future agreements in this area between the European Union and third countries":[182]

> "The Council recognises that the European Union and the Kingdom of Norway are neighbours, dynamic trade partners and are also parties to the Agreement on the European Economic Area, which aims to promote a continuous and balanced strengthening of trade and economic relations between the Contracting Parties.
>
> Due to these close relations, the Agreement between the European Union and the Kingdom of Norway on administrative cooperation, combating fraud and recovery of claims in the field of value added tax must be regarded as specific and hence the Council declares that this Agreement will not constitute a precedent for future agreements in this area between the European Union and third countries.
>
> In particular, in any possible future agreement concerning exchange of targeted information through the Eurofisc network established under Chapter X of Council Regulation (EU) No. 904/2010 should be limited to what is strictly necessary and possible to combat cross-border fraud between the Union and the third country."[183]

15.26 It seems reasonable to conclude that this statement was appended to signal the position of the other Member States that the UK, once a third country vis-à-vis the EU, cannot necessarily rely on enjoying a similarly close relationship with the EU as Norway on mutual assistance in VAT matters under this new Agreement, in particular as regards participation in Eurofisc.

15.27 To enter into force, the Agreement must be signed and concluded (ratified) by the Council, with both requiring a unanimous vote. In November, the Minister told us that no timetable for this had yet been set. It subsequently emerged that the Decision for signature was to be adopted on 5 December, before the Committee had had a chance to scrutinise the contents of the Agreement or its implications in the context of Brexit.

15.28 Adoption of the Council Decision authorising conclusion of the Agreement is yet to take place. The Agreement does not provide for provisional application; it will enter into force on the first day of the second month following its ratification by both parties.

182 See Council document 14703/17, p. 3.
183 See Council document 14703/17, p. 3.

Our assessment

15.29 We consider that this new treaty between the EU and Norway is of political importance for two reasons: it is the first international agreement concluded by the EU on mutual assistance in the field of VAT, and it may form the template for a future UK-EU agreement on the same subject matter, following our withdrawal from the Union. We have also taken note of the fact that the Government's view that the EU collectively is more efficient at negotiating these types of Agreement on mutual assistance than countries individually.

15.30 Upon the UK's withdrawal from the EU, both Council Regulation 904/2010, Directive 2014/24/EU and the EU-Norway Agreement (should it have entered into force by that stage) will, in principle, cease to apply to the UK. It is unclear whether the Government envisages that the post-Brexit "implementation period", during which the UK would operate within "the existing structure of EU rules and regulation",[184] would retain HMRC's rights and obligations regardingthe aforementioned legislation, or the benefits of the Agreement with Norway, for its duration. We await more information from the Government on its proposals for the interim arrangement, as well as the outcome of the European Council's preparatory work on the "framework for the future relationship and on possible transitional arrangements".[185]

15.31 However, either in March 2019 or after the end of a possible "implementation period", HM Revenue and Customs will, by default, lose the rights granted to Member State tax authorities. In particular, HMRC will no longer have a legal right to request data from other Member States on potential VAT fraud, and cease to participate in Eurofisc. The Government has not specified in detail what type of partnership it wishes to have with the EU on VAT-related matters after any interim arrangement ends.

15.32 In light of this, we have asked the Minister a number of questions about the relevance of the EU-Norway Agreement in the context of the UK's withdrawal. We may return to this topic once we have received his reply.

Previous Committee Reports

None.

184 Speech by the Prime Minister (Florence, 22 September 2017).
185 European Council conclusions, 20 October 2017.

Documents not raising questions of sufficient legal or political importance to warrant a substantive report to the House

Cabinet Office

(39115) 13184/17 COM(17)590	Report from the Commission to the European Parliament and the Council on the Assessment of the European Standard on electronic invoicing, according to Directive 2014/55/EU.

Department for Education

(39212) — —	Report on the annual accounts of the European Centre for the Development of Vocational Training for the financial year 2016 together with the Centre's reply.

Department for Exiting the European Union

(39214) — —	Report on the annual accounts of the Translation Centre for the Bodies of the European Union for the financial year 2016 together with the Centre's reply.
(39226) 14333/17 COM(17)652	Report from the Commission to the European Parliament and the Council on Progress in Bulgaria under the Co-operation and Verification Mechanism.
(39227) 14412/17 COM(17) 751	Report from the Commission to the European Parliament and the Council on Progress in Romania under the Co-operation and Verification Mechanism.

Department for International Development

(39198) 13999/17 COM(17) 644	Proposal for a Council Decision on the position to be taken on behalf of the European Union in the ACP-EU Committee of Ambassadors regarding the implementation of Article 68 of the ACP-EU Partnership Agreement.

Department for International Trade

(39234) 14474/17 COM(17) 668	Proposal for a Council Decision on the position to be taken on behalf of the European Union in the Ministerial Conference of the World Trade Organization as regards public stockholding for food security purposes, trade-distorting domestic support, including for cotton, export restrictions in agriculture, fisheries subsidies, domestic regulation in services, and SMEs/Transparency of Regulatory Measures for Trade in Goods.

Department for Transport

(39071)	Court of Auditors Report 13/2017 A single European rail traffic management system: will the political choice ever become reality?
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Foreign and Commonwealth Office

(38832)	Council Decision authorising the opening of negotiations with the Republic of Mali in order to conclude an Agreement on the status of the European Union CSDP Mission in Mali (EUCAP Sahel Mali) replacing the Agreement in the form of an Exchange of Letters between the European Union and the Republic of Mali regarding the status of EUCAP Sahel Mali.
(38865)	Commission Implementing Regulation (EU) 2017/970 of 8 June 2017 amending Council Regulation (EC) No 329/2007 concerning restrictive measures against the Democratic People's Republic of Korea.
(38866)	Council Implementing Decision (CFSP) 2017/975 of 8 June 2017 implementing Decision (CFSP) 2016/849 concerning restrictive measures against the Democratic People's Republic of Korea.
(39242)	Council Decision to provide support to States in the African, Asia-Pacific and Latin America and Caribbean regions to participate in the high-level fissile material cut-off treaty expert preparatory group consultative process.
(38251)	Council Decision (CFSP) 2017/… of [dd/mm/2017] amending Decision 2014/512/CFSP concerning restrictive measures in view of Russia's actions destabilising the situation in Ukraine.
(39252)	Joint Proposal for a Council Regulation amending Council Regulation (EU) No 833/2014 concerning restrictive measures in view of Russia's actions destabilising the situation in Ukraine.
(39261)	Council Regulation (EU) 2017/2062 of 13 November 2017 amending Regulation(EU) 2017/1509 concerning restrictive measures against the Democratic People's Republic of Korea.

HM Treasury

(39100) 12753/17 ADD 1 COM(17) 559	Proposal for a Decision of the European Parliament and of the Council providing further macro-financial assistance to Georgia.
(39146) 13485/17 COM(17) 604	Report from the Commission to the European Parliament and the Council under Article 29(3) of Regulation (EU) 2015/2365 of 25 November 2015 on transparency of securities financing transactions and of reuse and amending Regulation (EU) No 648/2012.

Home Office

(39145) 13478/17 COM(17) 608	Communication from the Commission to the European Parliament, the European Council and the Council Eleventh progress report towards an effective and genuine Security Union.

Formal Minutes

Wednesday 6 December 2017

Members present:

Sir William Cash, in the Chair

Douglas Chapman	David Jones
Richard Drax	Andrew Lewer
Marcus Fysh	Michael Tomlinson
Kelvin Hopkins	Dr Philippa Whitford

2. Scrutiny Report

Draft Report, proposed by the Chair, brought up and read.

Ordered, That the draft Report be read a second time, paragraph by paragraph.

Paragraphs 1.1 to 16 read and agreed to.

Summary agreed to.

Resolved, That the Report be the Fourth Report of the Committee to the House.

Ordered, That the Chair make the Report to the House.

[Adjourned till Wednesday 13 December at 9.30am.

Standing Order and membership

The European Scrutiny Committee is appointed under Standing Order No.143 to examine European Union documents and—

a) to report its opinion on the legal and political importance of each such document and, where it considers appropriate, to report also on the reasons for its opinion and on any matters of principle, policy or law which may be affected;

b) to make recommendations for the further consideration of any such document pursuant to Standing Order No. 119 (European Committees); and

c) to consider any issue arising upon any such document or group of documents, or related matters.

The expression "European Union document" covers—

i) any proposal under the Community Treaties for legislation by the Council or the Council acting jointly with the European Parliament;

ii) any document which is published for submission to the European Council, the Council or the European Central Bank;

iii) any proposal for a common strategy, a joint action or a common position under Title V of the Treaty on European Union which is prepared for submission to the Council or to the European Council;

iv) any proposal for a common position, framework decision, decision or a convention under Title VI of the Treaty on European Union which is prepared for submission to the Council;

v) any document (not falling within (ii), (iii) or (iv) above) which is published by one Union institution for or with a view to submission to another Union institution and which does not relate exclusively to consideration of any proposal for legislation;

vi) any other document relating to European Union matters deposited in the House by a Minister of the Crown.

The Committee's powers are set out in Standing Order No. 143.

The scrutiny reserve resolution, passed by the House, provides that Ministers should not give agreement to EU proposals which have not been cleared by the European Scrutiny Committee, or on which, when they have been recommended by the Committee for debate, the House has not yet agreed a resolution. The scrutiny reserve resolution is printed with the House's Standing Orders, which are available at www.parliament.uk.

Current membership

Sir William Cash MP (*Conservative, Stone*) (Chair)

Douglas Chapman MP (*Scottish National Party, Dunfermline and West Fife*)

Geraint Davies MP (*Labour/Cooperative, Swansea West*)

Steve Double MP (*Conservative, St Austell and Newquay*)

Richard Drax MP (*Conservative, South Dorset*)

Mr Marcus Fysh MP (*Conservative, Yeovil*)

Kate Green MP (*Labour, Stretford and Urmston*)

Kate Hoey MP (*Labour, Vauxhall*)

Kelvin Hopkins MP (*Independent, Luton North*)

Darren Jones MP (*Labour, Bristol North West*)

Mr David Jones MP (*Conservative, Clwyd West*)

Stephen Kinnock MP (*Labour, Aberavon*)

Andrew Lewer MP (*Conservative, Northampton South*)

Michael Tomlinson MP (*Conservative, Mid Dorset and North Poole*)

David Warburton MP (*Conservative, Somerton and Frome*)

Dr Philippa Whitford MP (*Scottish National Party, Central Ayrshire*)