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European Scrutiny Committee

Forty-first Report of Session 2017–19

Documents considered by the Committee on 24 October 2018

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:

- The future UK-EU energy relationship will be more complex than presented in the Government's White Paper
- The Government and the EU do not agree on how UK should be involved in future EU spending programmes

In relation to telecommunications:

- The EU regulatory framework for telecommunications will largely continue to function after EU exit;
- The price caps proposed for intra-EU international call charges (as distinct from roaming charges) will not apply to UK consumers, after the end of the implementation period;
- As the Government does not plan to maintain the EU's ban on mobile roaming charges domestically, some mobile operators may choose to re-introduce mobile roaming charges, and, even where they do not, the increased wholesale roaming charges they incur may be passed on to consumers indirectly.

A summary of some of the implications of EU exit for the digital sector are provided in the chapter on the Digital Single Market. Issues addressed include data flows (personal and non-personal), access to the international broadcasting market, roaming charges, international calls, geo-blocking, cross-border portability of online content, .eu domain names, venture capital, customs procedures affecting online cross-border sale of goods, and access to talent.

Summary

EU Sanctions for Chemical Attacks

The Committee has drawn the attention of the House to the adoption of the EU's new sanctions framework for perpetrators of attacks involving prohibited chemical weapons. It is the Government's intention to use the new framework to apply asset freezes and travel bans against those involved in such attacks, including those held responsible for the

Salisbury novichok attack. Although the overarching legal framework is now in place, a decision to apply the sanctions against specific people and organisations will need to be made at a later stage (requiring the unanimous agreement of all EU countries).

Cleared from scrutiny; drawn to the attention of the Defence committee, Foreign Affairs Committee and the International Development Committee.

European Defence Fund 2021–2027

The Committee has published its second report on the proposed European Defence Fund, which will provide an estimated €13 billion (£11.5 billion) of funding for research into and development of military technology by EU Member States from 2021 onwards. The Government is seeking participation in the Fund to enable the UK defence industry to be eligible for funding, but the Committee notes that the proposed legal text for the Fund would impose conditions — and limitations — on such participation, including limited influence over how any UK financial contribution would be spent, that may not be acceptable. It has retained the proposal under scrutiny in anticipation of further information from the Ministry of Defence about progress in the EU's legislative process.

Not cleared from scrutiny; further information requested; drawn to the attention of the Business, Energy and Industrial Strategy and the Defence Committee.

The European Electronic Communications Code

Trilogue negotiations regarding the recast of the European Electronic Communications Code—the principal regulatory framework for telecoms—have concluded. The principal change made in trilogues was the introduction of regulated price caps (16p/min and 5p/text) for intra-EU telephone calls. In effect, the EU has extended the limitations which previously applied only to mobile roaming charges to all intra-EU international calls, i.e. including where the caller is not using roaming services. This is on the basis that telecoms are charging mark-ups on the wholesale price of providing these services that is not justifiable. In exchange for supporting this European Parliament proposal, the Council extracted significant concessions on other issues, as a result of which all of the UK's negotiating objectives have been protected. The Minister states that the final text "meets all of the government's key negotiating lines".

On EU exit, although the Minister states that the EU regulatory framework for telecommunications is administered at national level and primarily consists of EU directives which are already implemented into UK law, meaning that UK telecommunications law will therefore largely continue to function after EU-exit, the Committee notes that the WTO General Agreement on Trade in Services (GATS) does not provide a like-for-like substitute for the EU regime. Furthermore, the Committee notes that UK consumers will not benefit from regulation of intra-EU international call charges, that it is probable that mobile roaming charges (abolished on an intra-EU basis) will return, and that, even where they do not, increased wholesale roaming costs incurred by UK providers may be passed on to UK consumers indirectly.

The Committee's decision: cleared from scrutiny

EU Clean Energy legislation

These proposals on energy efficiency, renewable energy and energy governance have been agreed, and cleared from scrutiny by the Committee. The Committee had challenged the Government to clarify its indication in its White Paper on the future EU-UK relationship that the UK may be willing to apply some sort of common rulebook for energy policy, but that this would not extend to wider environmental and climate change rules. In response, the Minister recognises that the legislation has multiple objectives, including energy, environment and climate change, thus appearing to support the argument that the White Paper is too simplistic in this regard. The Committee will monitor this issue as it scrutinises the outstanding elements of the Clean Energy Package (proposals on electricity market design).

Cleared; drawn to the attention of the Business, Energy and Industrial Strategy Committee

LIFE Programme (Climate and environment funding)

In its first Report on this proposal for the next iteration of the EU's climate and environment funding Programme (LIFE), the Committee raised issues regarding potential UK participation post-Brexit. In response, the Minister notes that the UK's preference is to negotiate strategic cooperative accords rather than participating in individual programmes on the basis of the generic third country arrangements for each programme. The Minister's statement is a presentation of Government policy, but it is not aligned with the EU's stated preferences. The Committee suggests that it would be prudent for the Government to engage in the design of the generic third country participation arrangements for this Programme. The Committee also re-iterates its query as to how any UK financial contribution would be calculated.

Not cleared; drawn to the attention of the Environment, Food and Rural Affairs Committee, the Environmental Audit Committee and the Business, Energy and Industrial Strategy Committee

Preventing the dissemination of terrorist propaganda online

The aim of the proposed Regulation is to introduce harmonised EU-wide rules to ensure that online terrorist content is identified and removed as quickly as possible whilst safeguarding freedom of expression and information. It would require online platforms to take proactive measures to prevent the dissemination of terrorist content; empower national authorities to issue a legally binding removal order to take terrorist content off the web within an hour; introduce penalties for platforms which fail to remove terrorist content promptly; and strengthen cooperation amongst Member States and with Europol. The Government welcomes the proposed Regulation, says it is consistent with its own plans to legislate on illegal online content and confirms that the UK will be bound to implement the proposal if it is adopted and takes effect before the UK's exit from the EU (on 29 March 2019) or during a post-exit transition period. The European Scrutiny Committee requests further information on: the Government's approach to negotiations and to the EU-wide harmonisation of penalties; the implications for freedom of expression; possible amendments to UK law; and consistency with other EU legislation applicable to online platforms.

Not cleared from scrutiny; further information requested; drawn to the attention of the Home Affairs Committee, the Justice Committee, the Digital, Culture, Media and Sport Committee and the Joint Committee on Human Rights.

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 Clean Energy legislation [(a), (b) Proposed Directives; (c) Proposed Regulation (C)]; DCMS Digital Single Market [(a) Communication (NC); (b), (c) Communications (C)]; EU Programme for the Environment and Climate Action [Proposed Regulation (NC)]; Ending seasonal changes of time [Proposed Directive (NC)]; European Defence Fund 2021–27 [Proposed Regulation (NC)]

Digital, Culture, Media and Sport Committee: DCMS Digital Single Market [(a) Communication (NC); (b), (c) Communications (C)]; Preventing the dissemination of terrorist propaganda online [Proposed Regulation (NC)]; European Electronic Communications Code [(a) Proposed Directive; (b) Proposed Regulation (C)]

Defence Committee: EU sanctions regime for chemical attacks [(a) Decision; (b) Regulation (C)]; European Defence Fund 2021–27 [Proposed Regulation (NC)]

Environment, Food and Rural Affairs Committee: EU Programme for the Environment and Climate Action [Proposed Regulation (NC)]

Environmental Audit Committee: EU Programme for the Environment and Climate Action [Proposed Regulation (NC)]

Exiting the European Union Committee: DCMS Digital Single Market [(a) Communication (NC); (b), (c) Communications (C)]; Ending seasonal changes of time [Proposed Directive (NC)]; Participation of Iceland, Norway, Switzerland and Liechtenstein in the EU's justice and home affairs IT agency, "eu-LISA" [Proposed Decisions (NC)]; European Electronic Communications Code [(a) Proposed Directive; (b) Proposed Regulation (C)]

Foreign Affairs Committee: EU sanctions regime for chemical attacks [(a) Decision; (b) Regulation (C)]; Neighbourhood, Development & International Cooperation Instrument 2021–27 [Proposed Regulation (NC)]

Home Affairs Committee: Money-laundering: powers of the European Banking Authority [(a) Amended Regulation; (b) Communication (NC)]; Preventing the dissemination of terrorist propaganda online [Proposed Regulation (NC)]; Participation of Iceland, Norway, Switzerland and Liechtenstein in the EU's justice and home affairs IT agency, "eu-LISA" [Proposed Decisions (NC)]

International Development Committee: EU sanctions regime for chemical attacks [(a) Decision; (b) Regulation (C)]; Neighbourhood, Development & International Cooperation Instrument 2021–27 [Proposed Regulation (NC)]

Joint Committee on Human Rights: Preventing the dissemination of terrorist propaganda online [Proposed Regulation (NC)]

Justice Committee: Preventing the dissemination of terrorist propaganda online [Proposed Regulation (NC)]; Participation of Iceland, Norway, Switzerland and Liechtenstein in the EU's justice and home affairs IT agency, "eu-LISA" [Proposed Decisions (NC)]

Treasury Committee: Money-laundering: powers of the European Banking Authority [(a) Amended Regulation; (b) Communication (NC)]

1 DCMS Digital Single Market

Committee's assessment	Politically important
Committee's decision	(a) Not cleared from scrutiny (b) (c) Cleared from scrutiny; Drawn to the attention of the Digital, Culture, Media and Sport Committee, the Business, Energy and Industrial Strategy Select Committee, and Exiting the European Union Committee
Document details	(a) Communication from the Commission: Completing a trusted Digital Single Market for all The European Commission's contribution to the Informal EU Leaders' meeting on data protection and the Digital Single Market in Sofia on 16 May 2018; (b) Communication from the Commission to the European Parliament, the European Council, the Council, the European Economic and Social Committee and the Committee of the Regions—Artificial Intelligence for Europe; (c) Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions: Tackling online disinformation: a European Approach
Legal base	—
Department	Digital, Culture, Media and Sport
Document Numbers	(a) (39779), 9403/18 + ADD 1, COM(18) 320; (b) (39669), 8507/18 + ADD 1, COM(18) 237; (c) (39680), 8578/18, COM(18) 236

Summary and Committee's conclusions

1.1 The European Commission has adopted a number of non-legislative communications providing an overview of progress with the implementation of the Digital Single Market (DSM) Strategy—the Commission's attempt to create an effective EU-wide single market for digital goods and services—as well as identifying further activity on artificial intelligence and online disinformation during the remaining period of the legislative cycle.

1.2 The overarching Communication[1] ("Completing a trusted Digital Single Market for all") reiterates the economic logic of the DSM: that the creation of a functional single market for digital goods and services within the EU could contribute €415bn per annum to the GDP of the EU28 by eliminating barriers to trade, encouraging digitisation of businesses, and creating trust in digital goods and services. The Communication notes that significant progress has been made to deliver the DSM Strategy across a range of

1 European Commission, Completing a trusted Digital Single Market for all COM(2018) 320.

legislative proposals. An annex[2] provides a detailed overview of the 29 initiatives which have already been adopted or where a political agreement is in place,[3] and those where the institutions have yet to reach an agreement.[4]

1.3 In a separate communication on tackling online disinformation,[5] the Commission describes the rise of disinformation—which it defines as misleading or outright false information that is created or shared online for malicious purposes—across the EU, as well as the drivers which amplify this content, including algorithms and click-based digital advertising models. The Communication states that such disinformation poses a threat in sowing distrust in institutions and building societal tensions, and that domestic and foreign actors can potentially manipulate policy making and societal attitudes through disinformation. It also states that measures taken by online platforms to date, particularly social media platforms, have not been sufficient to tackle the spread of disinformation online, necessitating EU action.

1.4 The most significant proposal to tackle online disinformation announced in the Communication was the development of an industry Code of Conduct. This Code, which is a voluntary and non-binding document which will apply to the industry stakeholders that choose to participate in it, was subsequently published on 26 September 2018.[6] The Commission will monitor its implementation by industry and, if the results prove unsatisfactory, propose further actions by the end of 2018, potentially including regulation. Other proposals include launching a study to examine possible gaps in relation to the identification of online sponsored content; creating an independent European network of fact-checkers; and using the Horizon 2020 work programme to mobilise emerging technologies to combat disinformation.

1.5 The Parliamentary Under Secretary of State at the Department of Digital, Culture, Media and Sport (Margot James) states that the Government is "broadly supportive of the EU's actions in this area, and do[es] not believe that such action will prevent the UK taking action in this area".[7]

2 European Commission, ANNEX—Digital Single Market legislative initiatives 2015–2018 COM(18) 320 final.

3 The Communication identifies the following initiatives as already adopted: Decision on the use of the 470–790 MHz frequency band; Regulation on cross-border portability of online content services; Regulation as regards rules for wholesale roaming markets; Regulation and Directive on permitted uses in copyright for print-disabled persons and implementing the Marrakesh Treaty; Regulation to promote Internet Connectivity in local communities (Wi-Fi4EU); Regulation on Consumer Protection Cooperation; Regulation addressing unjustified geo-blocking; Council Regulation and Directive on Value Added Tax for e-Commerce; Regulation on cross-border parcel delivery services; Audio-Visual and Media Services Directive. Since the publication of the Communication, the following initiatives have also been adopted or a political agreement between the institutions has been reached, meaning that they are expected to be adopted in the near future: Council Regulation establishing the European High-Performance Computing Joint Undertaking; European Electronic Communications Code; Body of European Regulators for Electronic Communications; Regulation on a framework for free flow of non-personal data; Regulation establishing a Single Digital Gateway; Council Directive on Value Added Tax for e-publications.

4 The Communication identifies the following files as ones where adoption has not yet taken place: Directive concerning contracts for the supply of digital content; Directive concerning contracts for the distance sales of goods; Directive on copyright in the Digital Single Market; Regulation on broadcasting organisations; Regulation on ePrivacy; Regulation on protection of personal data by the Union institutions and bodies; Regulation on the EU Cybersecurity Act; Directive on the combatting of fraud and counterfeiting of non-cash means of payment; Regulation on promoting fairness and transparency for business users of online intermediation services; Directive on the re-use of public sector information (recast); Regulation on the implementation and functioning of the .eu Top Level Domain name.

5 European Commission, Tackling online disinformation: a European Approach COM(2018) 236 final.

6 European Commission, EU Code of Practice on Disinformation (26 September 2018).

7 Explanatory Memorandum from the Government (tackling online disinformation) (21 May 2018).

1.6 In a separate Communication relating to artificial intelligence, the Commission set out a "European initiative on Artificial Intelligence".[8] To boost the EU's technological and industrial capacity and Artificial Intelligence(AI) uptake across the economy, the Communication states that the EU as a whole (public and private sectors) should aim to increase investment in AI to at least €20 billion by the end of 2020 and aim for more than €20 billion per year over the following decade.

1.7 To prepare for socio-economic changes brought about by AI, the Commission states that it will seek to support the efforts of Member States, which are responsible for labour and education policies, by setting up dedicated (re-)training schemes with financial support from the European Social Fund, gathering analysis to anticipate changes to the labour market and the skills mismatch across the EU to inform decision making, encouraging business-education partnerships to attract and retain AI talent and foster continued collaboration, and inviting social partners to include AI and its impact in their joint work programmes.

1.8 The Communication also notes that having an appropriate ethical and legal framework is important to facilitate trust in AI, and states that:

- 24 Member States, including the UK, through a Declaration of Cooperation,[9] have committed to entering into a strategic dialogue with the Commission in order to contribute to the development of a coordinated plan on AI by the end of 2018;
- the Commission will set up a European AI Alliance to develop draft AI ethics guidelines by the end of 2018; and
- the Commission will issue guidance on the interpretation of the Product Liability Directive by mid-2019 (the Communication is accompanied by a Staff Working Document which provides a mapping exercise regarding the liability challenges that occur in the context of emerging digital technologies).

1.9 In the Government's Explanatory Memorandum,[10] the Minister (Margot James) notes that the Communication is not a legislative proposal, no actions are required, and there are no financial implications for the UK or for UK businesses or the third sector arising from it. The Minister also notes that the UK's own AI report 'Growing the Artificial Intelligence Industry in the UK'[11] "sets out similar initiatives to those recommendations made in the [Commission's] AI Review". The Minister concludes that the Government will carefully scrutinise the implications of any detailed proposals which may arise from the Communication.

1.10 **We have taken note of the Government's views regarding these non-legislative Communications on progress of the Digital Single Market, Artificial Intelligence, and tackling online disinformation. We note the Minister's statement that the Government has "been a strong supporter of the DSM Strategy" and "supports swift agreement on the outstanding legislative issues of the DSM Strategy, in line with recent European**

8 European Commission, Artificial Intelligence for Europe (30 April 2018).
9 Declaration: Cooperation on Artificial Intelligence (10 April 2018).
10 Explanatory Memorandum from the Department of Digital, Culture, Media and Sport (artificial intelligence) (16 May 2018).
11 Professor Dame Wendy Hall and Jérôme Pesenti, Growing the artificial intelligence industry in the UK (15 October 2018).

Council conclusions." The Government is also supportive of the actions outlined in the Communication on tackling online disinformation (document b), we have taken note of the industry Code of Conduct regarding online disinformation.[12] We ask the Minister to ensure that the progress report on its initial implementation is deposited with the Committee for scrutiny when it is published. Regarding the Communication on Artificial Intelligence (document c), we note the Minister's assessment that proposed EU actions in this policy area is closely aligned with the Government's own findings, and that the Government has signed a Declaration of Cooperation with 24 other Member States to help develop a coordinated plan on AI by the end of 2018.

1.11 **On EU exit, the Government's intention to cease to participate in the Digital Single Market will mean that the legal arrangements which give effect to it will no longer apply to the UK. On the basis of our ongoing scrutiny of the wide range of Digital Single Market legislation, we have identified a range of effects that this will have:**

- **Personal data flows: Once the UK becomes a third country under EU law including the General Data Protection Regulation (2016/679) (GDPR)[13] it will cease to automatically benefit from the free flow of personal data with the EU27, and will have to establish alternative third-country arrangements as provided for in Chapter 5 of the GDPR. The Government's White Paper on the future economic partnership[14] indicates that "the EU's adequacy framework provides the right starting point for these arrangements". It is not automatic that the Commission would grant an adequacy decision and some further adaptation of domestic law may be necessary, particularly in relation to bulk collection of data for state surveillance. In the absence of an adequacy decision, UK cooperation in a wide range of EU information systems and databases would not be possible, and UK-based businesses would have to pursue other more bureaucratic and expensive alternatives provided for in the General Data Protection Regulation;**

- **Non-personal data flows: The UK will no longer participate in the EU's free flow of non-personal data framework,[15] meaning that even if an adequacy decision is concluded regarding personal data flows individual EU Member States will in principle be able to apply data localisation restrictions to UK-based operators,[16] which would require them to locate data processing facilities in the relevant EU Member State;**

- **Broadcasting: Outside the EU's mutual recognition framework for broadcasting—the Audio-Visual and Media Services Directive (EU) 2010/13[17]—a sector in which the UK is currently highly dominant within the EU, broadcasters who wish to retain their right to broadcast without**

12 European Commission, EU Code of Practice on Disinformation (26 September 2018).

13 Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, and repealing Directive 95/46/EC (General Data Protection Regulation).

14 HM Government, The future relationship between the United Kingdom and the European Union (July 2018).

15 European Commission, EU negotiators reach a political agreement on free flow of non-personal data (19 June 2018).

16 Free flow of non-personal data, chapter 28 (12 September 2018).

17 Directive (EU) 2010/13 of the European Parliament and of the Council of 10 March 2010 on the coordination of certain provisions laid down by law, regulation or administrative action in Member States concerning the provision of audiovisual media services (Audiovisual Media Services Directive) (Text with EEA relevance).

restriction to the EU27 from the UK (and who do not currently have a significant operational presence in another Member State) will have to locate a proportion of their staff in an EU27 Member State;[18]

- **Roaming charges: EU27 operators will be able to increase the wholesale roaming charges which UK mobile operators incur when UK citizens travel to the EU27. Although the Government will be able to limit the extent to which operators can directly charge UK consumers for these services, and some operators may not reintroduce roaming charges, the Government cannot prevent operators from incurring these increased costs, which may, over time, to be passed on to consumers by a variety of means (e.g. higher contract costs). Increases in wholesale roaming charges would have a significantly more harmful effect on operators which are not part of a group with a large commercial presence in Europe and Mobile Virtual Network Operators (MVNOs);[19]**

- **Intra-EU international calls: UK citizens will not retain the effects of the EU's forthcoming restrictions on charges for international calls, which will initially be capped at 16p/min and texts at 5p/text;[20]**

- **Geo-blocking: UK citizens and businesses will no longer benefit from protections afforded by the ban on discriminatory blocking or limiting customers' access to traders' online interfaces and redirecting them to another online interface: for example, if a British consumer wishes to access an online clothing shop's Italian website, the website will be allowed to block access to it and to redirect him/her to a British site with different pricing; similarly, if a UK citizen wishes to buy hosting services for a website from a business Swedish company they will no longer be entitled to the same terms of access as Swedish customers. UK operators selling to EU consumers will have to continue to comply with the regulation;**

- **Cross-border portability of digital content: UK citizens will no longer directly benefit from the provisions of the cross-border portability regulation, which allows consumers to access digital content. Due to the difficulty of navigating cross-border copyright issues, UK consumers may see restrictions to their online content services when they temporarily visit the EU;[21]**

- **".eu" domain names: When the UK leaves the European Union, and any transition period ends, UK persons and organisations will no longer be legally eligible to apply for .eu domain name registrations or to have existing ones renewed. The Commission has clarified in a notice to stakeholders[22] that the Registry for .eu will be entitled to unilaterally revoke such domain names. At present, there are 317,000 UK-based registrations for .eu domain names which potentially stand to be affected by these developments. Although businesses with a place of establishment in the European Union will be able to retain**

18 Thirty-Seventh Report HC 301–xxxvi (2017–19), chapter 6 (5 September 2018).
19 House of Commons Library, The abolition of mobile roaming charges and Brexit (6 July 2017).
20 See Letter from the Minister (DCMS) to the European Scrutiny Committee (16 July 2018).
21 HM Government, Copyright if there's no Brexit deal (24 September 2018).
22 European Commission, Notice to stakeholders brexit eu domain names.pdf (28 March 2018).

their eligibility, UK-based businesses will not be able to do so without having an establishment in the EU, and UK citizens will be unable to do so unless resident in an EU Member State;[23]

- **Country-of-origin principle: UK information society service providers providing services to the EU will no longer be able to rely on the country-of-origin principle in the E-Commerce Directive (EC) 2001/31**[24] **meaning that—unless they have an establishment in an EU27 country—they will be subject to the national rules of each EU Member State, thus increasing non-tariff barriers to trade and compliance costs; and**

- **Regulatory divergence and alignment: The UK will be able to adopt more distinctive and potentially more responsive approaches to regulating the digital economy, which may bring benefits in some cases. However, a more unilateral approach would also risk recreating the regulatory fragmentation that the Digital Single Market—of which the UK was the chief advocate—sought to eliminate, which would make it harder for businesses to grow their operations across national borders—a paramount concern for digital firms. Taking a distinctive approach to regulating the digital economy can also be challenging for individual countries because of the scale of the economic operators: for example, when Spain proposed to force aggregators to pay news publishers for their stories, Google News simply withdrew its service.**[25] **In practice, there may therefore continue to be significant alignment with EU policy on many digital issues.**

1.12 **Other implications of EU exit which are particularly salient for the sector, but which are not directly related to the Digital Single Market Strategy itself, relate to:**

- **Venture Capital: Between 2011 and 2015, the European Investment Fund (EIF) committed €2.3 billion to some 144 UK based venture firms, which amounts to approximately 37% of all venture funding raised in the UK during those years, according to data from Invest Europe, the trade association for European VC firms.**[26] **The Government has not yet clarified the type of relationship with the European Investment Bank that it seeks, but has recently suggested that it is "exploring options with the EU for maintaining a future EIB Group relationship as part of this second phase of negotiations".**[27] **If the supply of venture capital to UK-based digital firms were to be negatively affected, this would have a detrimental impact for the digital sector;**

  Customs procedures affecting online cross-border sale of goods: Unless the Government can secure arrangements as part of the future economic partnership which permit frictionless trade in goods, including preserving the effects of the intra-EU framework for cross-border VAT payments, the UK's exit from the Single EU VAT Area would mean that

23 Thirty Fifth Report HC 301–xxxiv (2017–2019), chapter 1 (11 July 2018).
24 Directive 2000/31/EC of the European Parliament and of the Council of 8 June 2000 on certain legal aspects of information society services, in particular electronic commerce, in the Internal Market ('Directive on electronic commerce'), OJ L 178, 17.7.2000, p. 1.
25 Guardian, Google News says 'adiós' to Spain in row over publishing fees (16 December 2014).
26 House of Lords EU Committee, Written evidence submitted by COADEC (October 2016).
27 Letter from the Chief Secretary to the Treasury to the Chair of the European Scrutiny (4 October 2018).

exports of goods from the UK to the EU and vice versa would be subject to physical custom controls to ensure the correct amount of VAT is paid at the EU's external border (in contrast to the current situation, where there are no such controls and movements of goods are monitored via the EU's VAT Information Exchange System).[28] This would potentially cause delays as well as cash-flow issues for businesses exporting to the EU. If other duties / customs procedures became applicable these would be likely to further increase costs and delays. UK consumers purchasing products from the EU27 would also be affected by delays and higher prices, as inbound parcels from the EU27 would be subject to the same customs processing as parcels from other countries and handling fees would be charged;[29] and

- **Access to talent: The free movement of persons within the EU currently provides the digital sector with access to a large base of skilled workers with minimal associated bureaucracy and costs. If the Government's future approach has the effect of restricting the supply of talent this is likely to have negative consequences for the sector: as Antony Walker of TechUK said: "If migration controls become too restrictive or too cumbersome, there is a risk that over time, tech companies will move to where talent is more readily accessible".[30]**

1.13 **As documents (b) and (c) are non-legislative, we clear them from scrutiny. We retain document (a) under scrutiny in order to keep a watching brief on the implications of EU exit for the UK digital sector. We draw these documents to the attention of the Digital, Culture, Media and Sport Committee, the Business, Energy and Industrial Strategy Committee and the Exiting the European Union Committee.**

Full details of the documents:

(a) Communication from the Commission: Completing a trusted Digital Single Market for all The European Commission's contribution to the Informal EU Leaders' meeting on data protection and the Digital Single Market in Sofia on 16 May 2018: (39779), 9403/18 +ADD 1, COM(18) 320; (b) Communication from the Commission to the European Parliament, the European Council, the Council, the European Economic and Social Committee and the Committee of the Regions — Artificial Intelligence for Europe: (39669), 8507/18 +ADD 1, COM(18) 237; (c) Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions: Tackling online disinformation: a European Approach: (39680), 8578/18, COM(18) 236.

Previous Committee Reports

None.

28 Twenty Third Report HC 301–xxii (2017–2019), chapter 3 (28 March 2018).
29 Financial Times, VAT: Brexit's hidden border dilemma (May 30 2018).
30 House of Lords EU Committee, Written evidence submitted by TechUK (November 2016).

2 EU Programme for the Environment and Climate Action

Committee's assessment	Politically important
Committee's decision	Not cleared from scrutiny; further information requested; drawn to the attention of the Environment, Food and Rural Affairs Committee, the Environmental Audit Committee and the Business, Energy and Industrial Strategy Committee
Document details	Proposal for a Regulation of the European Parliament and of the Council establishing a Programme for the Environment and Climate Action (LIFE) and repealing Regulation (EU) No 1293/2013
Legal base	Article 192 TFEU, Ordinary legislative procedure, QMV
Department	Environment, Food and Rural Affairs
Document Number	(39829), 9651/18 + ADDs 1–3, COM(18) 385

Summary and Committee's conclusions

2.1 "LIFE" is the EU's funding Programme for environment and climate action, aiming to contribute to the implementation, updating and development of EU environmental and climate policy and legislation. We first considered the Commission's proposal for the Programme over the period 2021–27, with a budget of €5.45 billion (£4.84 billion), at our meeting of 5 September 2018.[31] In our Report, we raised a series of queries about UK participation in the next Programme.

2.2 The Parliamentary Under-Secretary of State for the Environment (Dr Thérèse Coffey) has responded.[32] On future UK participation, she states that the UK proposes to collaborate with the EU through new cooperative accords that provide for a more strategic approach than simply agreeing the UK's participation in individual EU programmes on a case-by-case basis. Where such a cooperative accord was in place, she says, the UK would need to make appropriate financial contributions that would be agreed between both parties. There would also need to be governance arrangements that ensured both parties could shape the activity covered, recognising these will need to respect the autonomy of the EU's decision making. On the specific third country provisions for the next LIFE Programme, she says that the Regulation remains subject to the next Multiannual Financial Framework (MFF) negotiation and, therefore, the final detail is not yet available.

2.3 Concerning elements which might be helpful to the UK, the Minister observes that the proposed Regulation contains a number of sub-programmes which reflect domestic priorities, for example in relation to the 25 Year Environment Plan, the forthcoming Waste and Resources Strategy in England and the Clean Growth Strategy.

31 Thirty-seventh Report HC 301–xxxvi (2017–19), chapter 8 (5 September 2018)
32 Letter from Dr Thérèse Coffey to Sir William Cash, dated 11 October 2018.

2.4 Noting the Minister's comments on the future relationship between the UK and the EU, a recent speech by the EU's Chief Brexit Negotiator, Michel Barnier, is relevant. Responding to the Government's white paper on the future relationship, he expressed the EU's willingness to support future UK participation in EU funding programmes, such as research, but using third country cooperation mechanisms under the next MFF.[33]

2.5 **We asked the Minister about future UK participation in the LIFE Programme, including potential UK participation on the basis of the proposed third country arrangements, which include restrictions on decision-making and requirements on financial management. She responded by stating that the UK Government is not intending to participate in the EU's future programmes through established third country arrangements but by way of cooperative accords, allowing both partners a decision-making role. The Minister refrained from commenting on the third country arrangements in the draft LIFE Regulation as they are yet to be agreed.**

2.6 **We note the Government's position, but we also note that the EU—as expressed by Michel Barnier on 10 October—does not take the same view on arrangements for any future UK participation. While it may be possible to negotiate cooperative accords, it may also be the case that UK participation will need to be on the basis of the generic third country arrangements as agreed for each programme. We therefore believe that it would be prudent for the UK to engage actively in negotiations on this proposed Regulation with particular regard to the third country arrangements. We ask the Minister to set out the Government's negotiating approach as regards those elements of the proposed Regulation.**

2.7 **In our first Report on this proposal, we asked the Minister to set out the criteria that would be used to assess any financial contribution that the UK might make. Her response is silent on this question. We re-iterate the question and draw her attention to the Government's recognition in a letter[34] on future participation in ITER (the international nuclear fusion research project) that the starting point for the assessment of any UK contribution to that project would be "a standard GDP ratio-based mechanism".[35] If applied to the draft LIFE Programme for 2021–27, this could potentially require a UK contribution of €872 million (£774 million) over the seven years. We acknowledge that this figure is highly speculative.**

2.8 **We would welcome a response to the above queries and an update on the progress of negotiations within ten working days. The proposal remains under scrutiny. We draw this chapter to the attention of the Environment, Food and Rural Affairs Committee, the Environmental Audit Committee and the Business, Energy and Industrial Strategy Committee.**

33 Translation from French, as expressed by Michel Barnier in his speech at the closing session of Eurochambre's European Parliament of Enterprises 2018, 10 October 2018.

34 Letter from Sam Gyimah to Sir William Cash, dated 25 September 2018 regarding the Proposal for a Council Decision amending Decision 2007/198/Euratom establishing the European Joint Undertaking for ITER and the Development of Fusion Energy and conferring advantages upon it (9868/18, COM(18) 445).

35 The contribution by third countries for participation in EU programmes is typically calculated by taking their share of GDP of the total GDP of the EU and the third country in question combined (i.e. the EU-27 and UK), and multiplying it by the budget for the EU programme in question. The proposed LIFE Programme budget is €5.45 billion, and the UK's proportion of the combined GDP is 16%, this producing a total figure of €872 million (£774 million) and an annual figure of €125 million (£111 million).

Full details of the documents:

Proposal for a Regulation of the European Parliament and of the Council establishing a Programme for the Environment and Climate Action (LIFE) and repealing Regulation (EU) No 1293/2013: (39829), 9651/18 + ADDs 1–3 , COM(18) 385.

Previous Committee Reports

Thirty-seventh Report HC 301–xxxvi (2017–19), chapter 8 (5 September 2018).

3 Neighbourhood, Development & International Cooperation Instrument 2021–27

Committee's assessment	Politically important
Committee's decision	Not cleared from scrutiny; further information requested; drawn to the attention of the Foreign Affairs Committee and the International Development Committees
Document details	Proposal for a Regulation establishing the Neighbourhood, Development and International Cooperation Instrument
Legal base	Articles 209, 212 and 322(1) TFEU, ordinary legislative procedure; QMV
Department	Foreign and Commonwealth Office
Document Number	(39903), 10148/18 + ADDs 1–2, COM(18) 460

Summary and Committee's conclusions

3.1 In May 2018, the European Commission proposed to consolidate a number of the EU's existing funding instruments for international development assistance into a single legal framework: the Neighbourhood, Development & International Cooperation Instrument (NDICI).

3.2 With a putative budget of €89.2 billion (£78.5 billion) under the 2021–2027 Multiannual Financial Framework, this Instrument would fund EU development assistance worldwide, as well as finance other elements of the Union's foreign policy (for example, helping accession countries meet the economic, legal and political criteria for becoming EU Member States). Notably, the Commission has proposed to bring the European Development Fund– which provides assistance to 78 countries in Africa, the Caribbean and the Pacific–within the new Instrument, ending the current practice of administering that Fund entirely separately from the general EU budget.[36]

3.3 The Government, as part of its efforts to establish a new security and foreign policy partnership with the EU after Brexit, is actively engaged in the negotiations within the Council on the legal text underpinning the NDIC Instrument. In particular, it is seeking the insertion of a "third country" provision–missing from the European Commission's original proposal–that would allow the UK to become a contributor to the Instrument as a

36 The European Development Fund is 'off budget' because it has historically been funded by Member State contributions directly. Although managed by the European Commission, those contributions are not—in a legal or accounting sense—part of the EU budget. This ringfences money available for the ACP states from the EU's development assistance for other countries, and reduces the budgetary oversight of the European Parliament.

non-EU Member State. We first considered the NDICI proposal in September 2018,[37] and asked the Government to clarify in particular what conditions it would attach to any such financial contribution to the Instrument as a "third country".[38]

3.4 The Minister for Europe and the Americas (Sir Alan Duncan) replied by letter dated 1 October 2018, in which he explained that any UK contribution to the NDICI—should this become possible under a new 'third country' mechanism—would have to come with several levers of influence for the Government. The Minister "envisage[s]" that these would include[39] a right for the Government to be consulted about the practical implementation of the Instrument; agreed mechanisms for disbursement of EU funding; and eligibility for UK entities to bid for and receive funding from EU instruments to which the Government contributes.

3.5 The Minister also explains that no clear majority view has emerged yet among the Member States about the proposal to "budgetise" the European Development Fund from 2021 onwards, but that the Government has emphasised the need for a sufficient proportion of EU development funding to be channelled towards the Least-Developed Countries (LDCs) irrespective of the precise legal form of the EU's external instruments.[40]

3.6 **We thank the Minister for his helpful update, in particular the clarification of what the UK would expect in terms of influence over the implementation of NDICI funding if the UK were to make a financial contribution. We will use these as a benchmark as and when formal negotiations take place for the framework for the UK's post-Brexit partnership with the EU on foreign and security policy in due course.**

3.7 **Because of the uncertainties engendered by the process of the UK's exit from the EU, the exact (financial) implications for UK taxpayers of the NDICI Instrument, and the EU's next Multiannual Financial Framework from January 2021 more generally, remain ambiguous.**

3.8 **In principle, the UK will cease to be a Member State on 29 March 2019 and leave the EU fully after a subsequent transitional period. This is due to end on 31 December 2020 under the draft Withdrawal Agreement. During the transition, the UK would remain a budgetary contributor as if it were still an EU Member State (albeit with limited representation in the EU institutions and no voting rights over EU policy or funding decisions). However, on 17 October 2018, the Prime Minister told her counterparts at the European Council summit that the UK would be open to considering "an option" in the Withdrawal Agreement to "extend the [transition] period for a matter of months". That would mean the UK were still in the transitional arrangement when the next Multiannual Financial Framework, and the new NDIC Instrument, become operational. In that case, the UK might have no choice but to contribute to the Instrument until the transitional period ended.**

37 See the Committee's Report of 12 September 2018.

38 Based on existing EU approach to calculating the contribution of 'third countries' for participation in its programmes, we have putatively estimated the potential UK contribution to the NDICI over the 2021–2027 period could amount to €2 billion (see "our Report of 12 September 2018 for more information).

39 See the Minister's letter of 1 October 2018.

40 Under the Commission proposal, 36%—€32 billion—of the NDICI's budget would be earmarked for Sub-Saharan Africa. However, it is not ring-fenced in any binding way: due to the consolidation of various funding programmes into one Instrument, it would be easier for resources to be changes between different geographic or thematic priorities.

3.9 **After the end of any transitional period, the UK could voluntarily choose to seek participation in the EU's external action instruments like the NDICI. It is unclear, however, how the UK's demands for levers of influence would be met in practice and set down in a legal agreement with the EU. We remain concerned that, as a 'third country', the UK will find it more difficult to influence the way in which any development assistance channelled via the EU would be spent and managed. However, conversely, it would be easier for the Government to cease any such financial contributions if UK demands were not being met. (As a Member State, and during the transition, the UK does not have the option to withhold its budgetary contributions.) More generally, the impact of the UK's exit from the EU for the effectiveness of both UK and EU development policy will only become clear over time, but it is likely to be adversely affected unless there is mechanism for continuous cooperation, whether informally or via a legal agreement to participate in the relevant EU instruments.**

3.10 **We note in this respect that the negotiations on the UK's orderly withdrawal from the EU have become severely strained, in particular over the issue of the 'backstop' to keep the border with Ireland free of customs and regulatory infrastructure. The prospect of a UK exit from the Union without a Withdrawal Agreement therefore remains realistic.**

3.11 **As we recently set out, the repercussions of a "no deal" Brexit would be wide-ranging and extremely serious. While not an immediate priority, it would also disrupt the establishment of a new UK-EU foreign policy partnership and, in the interim, even day-to-day cooperation on development policy. In particular, the political acrimony following a breakdown in the Article 50 negotiations would abruptly end the Government's ability to influence the legislative deliberations on the NDICI proposal, and therefore reduce the odds that beneficial "third country" provisions are inserted into the final Regulation. In any event, until the UK had settled its outstanding financial commitments vis-à-vis the EU's 2014–2020 Multiannual Financial Framework (which the Government has accepted exist), it is unlikely the remaining Member States or the European Parliament would countenance an agreement with the UK for participation in any future EU programmes, including the NDIC Instrument. In summary, many significant political hurdles to post-Brexit UK participation in the EU's development assistance programmes remain.**

3.12 **As we have noted previously, the implications of the UK's withdrawal are likely to be particularly significant for developing countries in the Commonwealth and among the British Overseas Territories.[41] These will lose the UK's voice of support at the EU's negotiating table when future EU development assistance under the NDICI is allocated, but it remains unclear what—if anything—the Government proposes to do mitigate any lost EU funding for these countries over the short- and medium-term. In his latest letter, the Minister only refers to the Government's ambiguous objective of "seeking specific arrangements for the [British] Overseas Territories on areas of common interest with EU Member States".**

3.13 **In light of the above, and in particular the possible extension of the post-Brexit transitional period, we will continue to monitor the legislative negotiations within the Council and the European Parliament on the NDIC Instrument closely. We also draw**

41 Six British Overseas Territories are currently eligible for financial support from the European Development Fund. They will become in eligible on 29 March 2019, or at the end of any subsequent transitional period.

the Minister's latest letter to the attention of the Foreign Affairs and International Development Committees, and retain the proposal under scrutiny in anticipation of further updates from the Government in the coming months.

Full details of the documents:

Proposal for a Regulation establishing the Neighbourhood, Development and International Cooperation Instrument: (39903), 10148/18 + ADDs 1–2, COM(18) 460.

Background

EU development assistance

3.14 The European Union has a long history of providing financial support for lower-income countries, both in its immediate "Neighbourhood"—Eastern Europe, the Near East and North Africa—and further afield, in particular developing countries in Africa, the Caribbean and the Pacific (the ACP states) with former colonial ties to EU Member States. This support is currently channelled via a variety of funding instruments, the cost of which is ultimately borne by the EU's Member States. These 'external action' programmes principally provide funding for economic development, as well as supporting political and governance reforms.

3.15 The EU's next long-term budgetary cycle, the Multiannual Financial Framework (MFF), begins in 2021 and will run until the end of 2027. The EU's existing funding instruments for external support and development assistance will therefore expire at the end of 2020, meaning the Member States—and the European Parliament—have to agree on a new generation of funding instruments in this area.

The 2018 NDICI proposal

3.16 In May 2018, the European Commission proposed a Regulation to consolidate many of the existing funding programmes for development assistance into a single legal and financial framework from 2021 onwards: the **Neighbourhood, Development & International Cooperation Instrument** (**NDICI**). It would replace, for example, the European Development Fund, the Development Cooperation Instrument and the European Neighbourhood Instrument. Its proposed budget of €89.2 billion (£78.5 billion) over the 2021–2027 period would mark a 10 per cent real-terms increase in EU funding for development assistance compared to the current long-term budget, which runs from 2014 until the end of 2020.

3.17 One of the most significant changes the Commission proposal would make is to the set-up of the European Development Fund. This is the assistance facility for countries with former colonial ties to current EU Member States in the Caribbean, Africa and the Pacific, including many Commonwealth countries, under the 2000 Cotonou Agreement. The Commission has recommended that the EDF should be funded directly by the EU budget, rather than via a separate 'off-budget' mechanism for the first time.[42] This would

42 The European Development Fund is 'off budget' because it has historically been funded by Member State contributions directly. Although managed by the European Commission, those contributions are not—in a legal or accounting sense—part of the EU budget. This ringfences money available for the ACP states from the EU's development assistance for other countries, and reduces the budgetary oversight of the European Parliament.

increase the oversight of the European Parliament over how the funding is spent, and end the existing separation of EU development funding for the Member States' former colonies on the one hand and for all other developing countries on the other.

3.18 The overall implications of the NDICI proposal for the UK are currently unclear, given its decision to leave the EU. As a Member State, the UK has a vote on the annual budgets for the EU's development funding, and over the long-term and annual work programmes that restrict how the European Commission can spend that money. However, given the UK's decision to leave the EU, it will by default not be a participant in, or contributor to, the NDICI.

3.19 Nevertheless, the Government has been explicit in recent months that, ideally, the UK would like to continue working closely with the EU on development cooperation after Brexit. It has said this could involve a financial contribution to the relevant EU programmes, like the NDICI, in return for the UK being "able to shape [them] and to have a say in [their] performance". Despite an explicit UK request for "mechanisms that go beyond existing arrangements for third parties"[43] in the draft legal framework for the NDIC Instrument, the Commission proposal contained no overarching arrangement for non-EU countries to be comprehensively involved in a capacity as donor.

3.20 The NDICI Regulation is still subject to amendments by the European Parliament and the Member States before its formal adoption. However, even if they insert a 'third country' mechanism to allow for closer involvement by the UK, it is unclear by what mechanism the Government proposes to keep oversight over how its contribution—and funding from the Instrument more generally—would be spent. The Secretary of State (Penny Mordaunt) has stated that the UK would demand for a "suitable level of oversight" in return for any payments, including the ability to "shape programmes".[44]

3.21 The European Scrutiny Committee set out the substance of the NDICI proposal, and its assessment of the implications for the UK, in some detail in its Report of 12 September 2018. Given the uncertainty about the UK's future role in the NDIC Instrument and the EU's development programmes more generally, the Committee decided to keep the proposed Regulation under scrutiny. Given the substance of the proposal and the Government's ambitions for post-Brexit cooperation with the EU on development policy, we asked the Minister to provide more clarity about the level of support among Member States for folding the European Development Fund into the new Instrument, and explain the practical implications of the Government's desired ability "to shape" EU development programmes in return for a financial contribution as a 'third country'.

The Minister's letter of 1 October 2018

3.22 The Minister for Europe and the Americas at the Foreign & Commonwealth Office (Sir Alan Duncan) provided further information on the NDICI proposal and the UK's position by letter dated 1 October 2018.

3.23 With respect to the proposed 'budgetisation' of the European Development Fund, the Minister explains that it is "too early" in the budgetary negotiations for 2021–2027 to assess if there is sufficient majority among Member States for the EDF to be folded into

43 Oral evidence by Penny Mordaunt MP to the International Development Committee (17 July 2018), Q4.
44 Oral evidence by Penny Mordaunt MP to the International Development Committee (17 July 2018), Q4.

the NDICI, or to remain outside of the future next Multiannual Financial Framework. He also notes that the UK's position remains that there should be an opportunity for its participation in the Fund, irrespective of its precise legal status under EU law. In the negotiations so far, the Government has also emphasised "the importance of poverty reduction and the [Least Developed Countries], especially in Africa" and requested further information from the Commission about the resource allocation process to ensure a focus on providing assistance to those countries.

3.24 The remainder of the Minister's letter focuses on the Committee's questions in relation to the possibilities for UK involvement in EU development assistance policy via the NDIC Instrument as a 'third country'.

Opportunities for UK participation in the NDIC Instrument after Brexit

3.25 The Minister reiterates that, "as for all discussions on external action instruments under the new Multi-Annual Financial Framework", the Government is using its representation within the relevant Council working parties to "press for expansive provisions on 'third country' participation" (although the legislative deliberations on the final legal text of the NDIC Instrument are expected to last beyond the UK's withdrawal in March 2019).

3.26 As regards the Government's criterion that any financial contribution to the Instrument should come with the ability to "shape" the way the money is used, the Minister explains that "sufficient oversight arrangements" would be needed to enable a UK contribution to the NDICI after Brexit. As per the Minister's letter, the Government 'envisages' that the UK would require:

- Consultation over strategy and funding flows;
- Cooperation in programme approval;
- Agreed mechanisms for disbursement;
- Appropriate involvement in programme evaluations and reporting;
- The ability to manage jointly strategic and programme risks; and
- Eligibility for UK entities to bid for and receive funding from EU instruments to which the UK contributes.

3.27 As a rule, the Minister states, "any UK financial contribution would require an appropriate level of UK participation and oversight, including a say over how UK funds are used, whether that is at the instrument level, programme level or windows". How these levers of influence would be translated into precise legal terms under any future legal agreement setting out the parameters of UK participation—should the final NDICI Regulation allow such 'third country' involvement—remains unclear.

3.28 Finally, with respect to the implications for developing countries with historical or constitutional links to the UK, which have hitherto benefited from the UK's support when EU development assistance is allocated, the Minister states only that " the UK will be seeking specific arrangements for the Overseas Territories on areas of common interest with EU Member States, including their overseas countries and territories". He does not refer to the position of independent Commonwealth countries in this context.

3.29 The Committee considers that the UK retains a significant interest in the final legal text underpinning the NDIC Instrument, particularly as regards the possibility—and potential cost—of UK participation as a "third country". It has therefore retained the proposal under scrutiny in anticipation of further updates from the Minister. The Austrian Presidency of the Council is expected to present a progress report on the negotiations on the NDICI to the Member States in December 2018. The Committee will take stock of developments at that stage and decide in due course whether to report them to the House.

Previous Committee Reports

See (39903), 10148/18 + ADDs 1–2, COM(18) 460: Thirty-eighth Report HC 301–xxxvii (2017–19), chapter 16 (12 September 2018).

4 Money-laundering: powers of the European Banking Authority

Committee's assessment	Politically important
Committee's decision	Not cleared from scrutiny; further information requested; drawn to the attention of the Home Affairs Committee and the Treasury Committees
Document details	(a) Amended proposal for a Regulation of the European Parliament and of the Council amending Regulation 1093/2013 establishing the European Banking Authority and Directive 2015/849 on the prevention of the use of the financial system for the purposes of money-laundering or terrorist financing; (b) Communication from the Commission: Strengthening the Union framework for prudential and anti-money laundering supervision for financial institutions
Legal base	(a) Article 114 TFEU; ordinary legislative procedure; QMV; (b) —
Department	Treasury
Document Numbers	(a) (40057), 12111/18, COM(2018) 646; (b) (40058), 12108/18, COM(2018) 645

Summary and Committee's conclusions

4.1 Following a number of money-laundering scandals involving EU-based banks, including notably the recent revelations about Danske Bank's laundering of Russian money via its Estonian branch—the European Commission in September 2018 proposed to expand the responsibilities of the European Banking Authority (EBA) with respect to the proper implementation of the EU's Anti-Money Laundering Directive (AMLD).

4.2 The legislative proposal, accompanied by a policy paper on its broader approach to limiting the risks of money-laundering in the EU, would give the EBA a greater coordinating role, including by setting "common standards" for combating the risk of money laundering, and also, in certain circumstances, allow it to direct individual banks to take specific actions to ensure the AMLD is complied with.[45] The draft legislation is part of the wider revision of the European System of Financial Supervision (ESFS),[46] tabled

45 From a procedural perspective, the proposal to clarify the powers of the EBA is an amendment to a pending legislative proposal—the review of the European System of Financial Supervision—which dealt with the responsibilities of the EU's financial supervisory authorities more generally. That draft legislation also remains under scrutiny, as we concluded in July 2018 that it could have an impact on the UK both during and after the post-Brexit transitional period.

46 The ESFS was established in the aftermath of the financial crisis and centred on the European Central Bank and three new EU-level 'Supervisory Authorities': the EBA (banking), EIOPA (insurance) and ESMA (markets and securities).

in September 2017, which already foresaw a transfer of regulatory responsibility in the financial sector from the national to the European level. [47] We have set out the substance of the Commission proposal in more detail in 'Background' below.

4.3 The ESFS proposals have been controversial among the Member States, given the implied loss of domestic regulatory power they entail. These latest additions in relation to money laundering are, in the words of the Economic Secretary to the Treasury (John Glen), "likely to add to the contentious nature"[48] of the Council's deliberations on the balance of responsibilities between national and European financial regulators. As such, formal adoption of the proposal to expand the remit of the European Banking Authority is unlikely to occur in the near future.

4.4 **The implications of the proposal to expand the remit of the European Banking Authority for the UK remain unclear. This is partially because the legislative text is still subject to change by the Member States in the Council and by the European Parliament, and partially because of the wider uncertainty about the nature of the UK's economic relationship with the EU after 29 March 2019 (when the two-year EU exit period begun in March last year expires, and the UK becomes a 'third country' vis-à-vis the Union unless the Withdrawal Agreement is ratified).**

4.5 **If the changes proposed by the Commission were to take effect while the UK is still bound by EU law—which it would until the end of the post-Brexit transitional period, currently due to end on 31 December 2020—the European Banking Authority would gain new powers to direct the activities of the Bank of England's Prudential Regulation Authority. However, the UK—having ceased to be a formal Member State on 29 March 2019—would not be permanently represented within the EBA's governance structures, and it would have no voting rights over any measures it wants to adopt to address money-laundering risks (or decisions related to other aspects of its legal mandate, such as prudential supervision).**

4.6 **Without a ratified Withdrawal Agreement (and therefore without a post-Brexit transitional period), there would be an abrupt UK exit from the EU's established structures to tackle money-laundering (and tax evasion). New legal mechanisms, including for the exchange of data and information, would then have to be negotiated afresh in what would likely be an acrimonious political atmosphere, adversely affecting UK-EU cooperation in this area. As the new Regulation would designate the European Banking Authority as the EU's main interlocutor with 'third countries' on issues related to money-laundering, the proposed changes to its mandate would nevertheless remain relevant for the UK even in a 'no deal' scenario. There are also wider considerations about the possible impact of the UK becoming a 'third country' for the purposes of the AMLD on cross-Channel financial flows, which we discussed in our Report of 22 November 2017.[49]**

4.7 **In light of these uncertainties, which we have assessed in more detail in the 'Background' section of this Report, we retain the amended proposal for the responsibilities of the European Banking Authority under scrutiny. We also draw**

47 See for more information on the proposed changes to the ESFS our Report of 21 February 2018. The proposals remain under scrutiny.

48 Explanatory Memorandum submitted by HM Treasury (2 October 2018).

49 See https://publications.parliament.uk/pa/cm201719/cmselect/cmeuleg/301–ii/30121.htm.

these proposed new EU measures to tackle money laundering to the attention of the Home Affairs and Treasury Committees. We are content to clear the Commission's accompanying policy paper from scrutiny.

4.8 **We ask the Minister to keep us informed of further developments in the legislative deliberations within the Council and the Parliament on the European System of Financial Supervision, including this latest proposal.**

Full details of the documents:

(a) Amended proposal for a Regulation of the European Parliament and of the Council amending Regulation 1093/2013 establishing the European Banking Authority and Directive 2015/849 on the prevention of the use of the financial system for the purposes of money-laundering or terrorist financing: (40057), 12111/18, COM(18) 646; (b) Communication from the Commission: Strengthening the Union framework for prudential and anti-money laundering supervision for financial institutions: (40058), 12108/18, COM(18) 645.

Background

4.9 The EU's Anti-Money Laundering Directive[50] (AMLD) requires banks and other businesses handling financial transactions ("obliged entities") to apply due diligence to their customers, and report suspicious activity to the authorities.[51]

4.10 In most EU countries, prudential supervision of banks—monitoring their financial health and stability—and the investigation of money-laundering are the responsibility of different agencies or regulators.[52] Nevertheless, there is a direct link between money-laundering and the prudential health of a financial institution: laundering illicit money flows can affect the reputation and stability of individual banks and, by extension, the financial system as a whole. In May 2018, the Member States and the European Parliament therefore amended the AMLD to improve the exchange of information between anti-money laundering and prudential authorities.[53] However, there is no "mandatory mechanism or detailed guidance" on structural cooperation between the two — especially between different Member States.

4.11 In response to several scandals—including notably the revelations that Danish lender Danske Bank potentially laundered as much as €200 billion of criminal proceeds through its Estonian branch between 2007 and 2015,[54] but also similar occurrences in Latvia and the Netherlands—the European Commission in September 2018 decided further action

50 Directive 2015/849.

51 It also obliges Member States to maintain central registers of the beneficial ownership of both companies and trusts, although there is—at present—no obligation to make the latter accessible to the public.

52 For example, within the Eurozone's Banking Union, prudential supervision of the largest banks is the responsibility of the European Central Bank. However, tackling money-laundering remains a largely national competence of each Member State under the Anti-Money Laundering Directive (AMLD), who must appoint a Financial Intelligence Unit for that purpose (the National Crime Agency in the UK).

53 See Subsection IIIA of the AMLD as amended, relating to "Cooperation between competent authorities supervising credit and financial institutions and other authorities". The amendments to the AMLD adopted in 2018 also make a number of other changes, including more transparency of the beneficial ownership of trusts. See our Report of 31 January 2018 for more information.

54 BBC News, "Danske Bank boss quits over €200bn money-laundering scandal" (19 September 2018).

was necessary.[55] Stating that "gaps remain in the Union's supervisory framework"[56] to prevent money-laundering.[57] It therefore published a policy paper on the steps it wanted the EU to take to further address these risks.

4.12 Its core recommendation is that national anti-money laundering authorities in the EU —called Financial Intelligence Units (FIUs) in the AMLD—and the prudential authorities responsible for ensuring the stability of banks and other financial institutions should work more closely together. Prudential authorities, who operate on the basis of the EU law like the Capital Requirements Directive (CRD), have more powers than FIUs to intervene in the operation of banks and investment firms within their jurisdiction, including—as a last resort—suspending or withdrawing their operating licence. The exchange of information with FIUs can provide these regulators with the input necessary to intervene where money-laundering risks could pose a risk to micro- or macro-prudential stability.

4.13 In aid of this objective, the Commission uses its policy paper to express support for amendments to the Capital Requirements Directive[58] recently put forward by the European Parliament, which seek to address confidentiality requirements that in practice prevent prudential regulators from cooperating with other enforcement authorities.[59] The Committee will assess those proposed changes separately as part of its on-going scrutiny work on the Risk Reduction Measures package of banking reform proposals in due course.[60]

4.14 The Commission has also produced a new legislative proposal to amend the Regulation that established the European Banking Authority (EBA).[61] The objective of the proposal is to expand the remit of the Authority's activities, explicitly incorporating "matters related to combating money-laundering and terrorist financing across the financial sector" into its legal mandate, as set out in more detail below.

Expanding the EBA's powers in relation to money laundering

4.15 The proposed changes to the EBA's remit are not a stand-alone document: they take the form of an amended proposal for a Regulation, first presented in September 2017, to substantially amend the EU's system of financial supervision (ESFS) more broadly. The Committee assessed that proposal in its Reports of 13 December 2017 and 21 February 2018, and retains it under scrutiny (given the potential implications of the proposals for

55 The same sentiment was expressed by France and Germany in their Joint Declaration of 19 June 2018, by the European Parliament, and by the President of the Eurogroup, Mário Centeno.

56 Commission Communication COM(2018) 645, p. 2.

57 Other recent money laundering scandals involving EU banks took place in Latvia and the Netherlands.

58 Directive 2013/36/EU.

59 The relevant amendments are contained in European Parliament Report A8 2018/243, in relation to a new article 4a of Article 117 ("Competent authorities [and] financial intelligence units […] supervising obliged entities listed in [the AMLD], shall cooperate closely with each other within their respective competences and shall provide one another with information relevant for this under […]") and a change to Article 56 on exchange of information ("[The Capital Requirements Directive] shall not preclude the exchange of information between competent authorities within a Member State, between competent authorities in different Member States or between competent authorities and the [competent authorities referred to in Article 48 of the Directive (EU) 2015/849], in the discharge of their supervisory functions".

60 The Risk Reduction Measures (RRM) are a package of proposed reforms to the EU's legislation on banking supervision and, in the cause of bank failure, resolution. We last considered the proposals on 16 May 2018 and retain them under scrutiny in anticipation of further developments in the legislative process.

61 Regulation 1093/2013 establishing the European Banking Authority.

the UK both during and after the post-Brexit transitional period). The remainder of this chapter is focussed only on the latest Commission proposal relating to the EBA's powers in the area of money-laundering.[62]

4.16 The aim of the Commission proposal is to enable the EBA to take action to ensure national banking regulators properly apply the AMLD as part of their supervisory work. The specific details of the proposed Regulation are as follows:

- The EBA would be empowered to set "common standards"[63] for combating money laundering, collect information relating to steps taken by both "financial market operators" and national regulators within the EU to tackle money laundering, and undertake risk assessments in Member States about the strategies and resources being deployed. Ultimately, the Authority would act as a centralised "data hub", including confidential information, which national regulators could use to address money-laundering risks;

- The Authority would also gain the power to request a national regulator "consider" taking action against a specific "financial sector operator"[64] to ensure compliance with the Anti-Money Laundering Directive.[65] If the EBA considers any follow-up action did not 'comply' with the request, the proposal would enable the Authority to initiate a 'breach of Union law' procedure,[66] which could ultimately[67] result in a binding decision requiring either a national regulator or a specific financial market operator to **"**take all necessary action to comply with its obligations under Union law, including the cessation of any conduct**";**

- The initiation of such a "breach of Union law" procedure against a national regulator would ultimately have to be made by the EBA's Board of Supervisors. Under the current legal framework, it is only the EU's national regulators themselves who are voting members of the Board and as a result—the Commission argues—the procedure has never been invoked. Under the parallel review of the European System of Financial Supervision,[68] the Commission has therefore proposed to transfer some of the powers of the EBA's Board of Supervisors— including in relation to 'breach of Union law' procedures to a new four-person Executive Board composed of full-time independent members;[69]

62 The Member States and the European Parliament are also still deliberating the wider ESFS proposals, but there is no firm timetable for their adoption given the contentiousness of what is being proposed.

63 The Committee is still clarifying what the (legal) nature of these "common standards" would be.

64 The Commission proposal defines 'financial sector operators' as "obliged entities" under the Anti-Money Laundering Directive which are also either a 'financial institution' as defined in the EBA or EIOPA Regulations, or as a 'financial market participant' under the ESMA Regulation.

65 The new article 9b of the EBA Regulation would empower the Authority to "request a [national] competent authority [...] to investigate possible breaches of Union law" relating to money-laundering, and if considered necessary ask that authority to "consider adopting an individual decision addressed to that financial sector operator requiring it to undertake all necessary action to comply" with its legal obligations.

66 Currently, the EBA can only use the "breach of Union law" procedure for alleged breaches of EU regulations in the field of financial services (like the Capital Requirements Regulation), not the Anti-Money Laundering Directive.

67 Such binding decisions under a 'breach of Union law' procedure must be preceded by several steps, including a formal Commission Opinion a) concluding that a breach of the AMLD had occurred and b) stipulating the necessary measures to be taken to ensure compliance.

68 See 'Background' for more information on the review of the European System of Financial Supervision.

69 The same would also apply within EIOPA and ESMA.

- The proposal would establish a new Anti-Money Laundering Committee within the EBA for cooperation with and among the EU's national financial regulators;[70] and
- Finally, the Commission foresees a role for the European Banking Authority in leading the EU's cooperation with 'third country' anti-money laundering supervisors (including, after Brexit, the UK's National Crime Agency).

4.17 The amended legislative proposal was not accompanied by an Impact Assessment, presumably because it was produced at speed in response to recent developments and with a view to giving it time for consideration before the 2019 European elections. It will now be considered by the Member States in the Council's working party on financial services, and by the Economic & Monetary Affairs Committee of the European Parliament.

4.18 The Commission has also asked the EBA to issue guidance on use of information on money laundering risks by the European Central Bank and national prudential regulators, to "specify how prudential supervisors should integrate anti-money laundering aspects" into their work. The Authority will also map the distribution of prudential and anti-money laundering supervision in the different Member States to help national authorities identify the relevant counterparts in other EU countries.[71]

Implications of the proposal for the UK

4.19 The Economic Secretary to the Treasury submitted an Explanatory Memorandum on the EBA proposal on 2 October 2018, and a separate—but largely identical—Memorandum on the Commission's related policy paper approximately a week later.[72]

4.20 The Government's Memoranda note that the proposed expansion of the EBA's responsibilities would "represent a significant shift in responsibility and power for supervision within the financial services sector away" from national regulators to the European level. Placing the latest proposal in the context of the EU's wider financial supervision review—through which the Commission had already suggested a significant transfer of power to the European Supervisory Authorities—the Minister adds that the proposed "increased mandate of the EBA" was "likely to add to the contentious nature" of the Council's deliberations in this area.

4.21 The exact implications of the proposed extension of the EBA's remit for the UK are unclear. This is partially because the legal text of the Commission proposal is likely to be altered significantly by both the Member States and the European Parliament during the legislative process, and—in the context of Brexit—because of the continued uncertainty about the future of the UK's economic and regulatory relationship with the EU after March 2019. It is in any event unclear what would be the practical impact of the EBA's new powers to instruct national prudential authorities, given that the "breach of Union law" procedure has never yet been used. Our ability to take an informed position in this respect

70 The other Supervisory Authorities (ESMA and EIOPA), as well as the European Commission, the European Central Bank and the European Systemic Risk Board would be represented on the Committee as observers.
71 Commission Communication COM(2018) 645, p. 10–11.
72 Although this second Explanatory Memorandum was dated 1 October, it was not received by the Committee until 12 October 2018.

is hampered by the fact that the European Commission did not prepare a formal Impact Assessment, and the analysis provided by the Government's Explanatory Memoranda is cursory.

4.22 The substance of the proposal notwithstanding, there is also a wider issue of the Regulation's (potential) applicability to the UK. If the amendments to the EBA Regulation were to take effect during the proposed post-Brexit transitional period, currently scheduled to last until the end of 2020,[73] the Authority's new powers would apply here. In such a scenario, the EBA would gain new powers to direct the activities of the Bank of England's Prudential Regulation Authority in cases of suspected money laundering, even though the UK would not be represented within the EBA's governing structures or have voting rights over potential "breach of Union law" procedures.

4.23 However, the timing of the adoption of the proposal, and consequently its date of application, remains uncertain: as noted, it forms part of the wider review of the European System of Financial Supervision, which has proved to be contentious because it would lead to a significant shift of regulatory responsibilities from the Member States to the EU. Rapid adoption is therefore considered highly unlikely, meaning the new Regulation is likely to take effect in 2021 or later. The likelihood that the new EBA powers might apply to the UK would increase if the post-Brexit transitional period were extended beyond December 2020 for whatever reason.[74]

4.24 Once the UK is outside the Single Market, the EBA Regulation would no longer have any direct effect domestically. However, under the Commission proposals the EBA would still be a key interlocutor for EU cooperation with the UK—and other third countries—on matters of money laundering. The breadth and depth of UK cooperation with the EBA and individual Member States on such matters will need to be established as part of any future negotiations on the detail of a new economic and security partnership.

4.25 In light of the above, we have retained the proposed EBA Regulation under scrutiny in anticipation of further information from the Minister on developments in the legislative process.

Previous Committee Reports

None. For our last Report on the current Anti-Money Laundering Directive, see our Twelfth Report HC 301–xii (2017–19), chapter 14 (31 January 2018).

73 Under the draft Withdrawal Agreement, the UK would stay in the Single Market and the Customs Union until 31 December 2020.

74 The Government itself has previously stated the transition might have to last until mid-2021, and in October 2018 the Guardian reported that the UK and the EU were discussing a potential one-year extension mechanism (i.e. until 31 December 2021).

5 Participation of Iceland, Norway, Switzerland and Liechtenstein in the EU's justice and home affairs IT agency, "eu-LISA"

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, the Justice Committee and the Exiting the European Union Committee
Document details	(a) Proposal for a Council Decision on the signing on behalf of the European Union of the Arrangement with Norway, Iceland, Switzerland and Liechtenstein on participation by those States in the European Agency for the operational management of large-scale IT systems in the area of freedom, security and justice (b) Proposal for a Council Decision on the conclusion of the Arrangement with Norway, Iceland, Switzerland and Liechtenstein on participation by those States in the European Agency for the operational management of large-scale IT systems in the area of freedom, security and justice
Legal base	(a) Articles 74, 77(2)(a) and (b), 78(2)(e), 79(2)(c), 82(1)(d), 85(1), 87(2)(a), 88(2) and 218(5) TFEU, QMV (b) Articles 74, 77(2)(a) and (b), 78(2)(e), 79(2)(c), 82(1)(d), 85(1), 87(2)(a), 88(2) and 218(6)(a)(v), EP consent, QMV
Department	Home Office
Document Numbers	(a) (40044), 11805/18 + ADD 1, COM(18) 607; (b) (40045), 11804/18 + ADD 1, COM(18) 606

Summary and Committee's conclusions

5.1 The proposed Council Decisions would authorise the EU to sign and conclude an "Arrangement" with Norway, Iceland, Switzerland and Liechtenstein setting out the terms of their participation in "eu-LISA" — the EU Agency responsible for the operational management of EU asylum, migration and law enforcement information systems. These four countries have already concluded agreements with the EU associating them with the Schengen rule book and are referred to collectively as "Schengen associated countries". They have also concluded agreements associating them with the application of the EU's "Dublin rules" and Eurodac database which establish a mechanism for determining the country responsible for examining an application for international protection. The 2011

Regulation setting up eu-LISA expressly provides for countries associated with Schengen and Eurodac-related measures to participate in the Agency based on a detailed set of rules which include provisions on financial contributions, staffing and voting rights.[75]

5.2 Under the terms of the Arrangement, the four Schengen associated countries would participate fully in the activities of eu-LISA, be represented on eu-LISA's Management Board and Advisory Groups and have limited voting rights on certain decisions concerning the EU information systems in which they participate. They would be required to make an annual financial contribution to the Agency (based on an agreed funding formula) and to recognise the jurisdiction of the EU Court of Justice on the basis set out in eu-LISA's founding Regulation. The Arrangement is contingent on the Schengen associated countries' continued participation in the Schengen rule book, Dublin rules and Eurodac database. It includes dispute settlement provisions which may lead to the Arrangement being terminated if a Mixed Committee meeting at Ministerial level is unable to resolve the dispute.

5.3 Even though the proposed Council Decisions cite Title V (justice and home affairs) legal bases and concern EU information systems which are subject to the UK's Title V opt-in and Schengen opt-out Protocols, the Commission does not consider that these Protocols apply, meaning that the UK has no choice but to participate in the adoption of the Decisions and will be bound by the Arrangement. This reflects the Commission's view that, as the UK participates fully in eu-LISA's founding Regulation, it is under an obligation to give effect to Article 37 of that Regulation which provides for the Schengen associated countries to participate in eu-LISA.

5.4 In his Explanatory Memorandum of 3 October 2018, the Minister for Policing and the Fire Service (Nick Hurd) supports the terms of participation set out in the Arrangement and the formula to be used to calculate each Schengen associated country's financial contribution.[76] He accepts that the UK's participation in eu-LISA's founding Regulation "implicitly acts as consent" to participate in and be bound by the proposed Council Decisions and says that the UK's Title V opt-in Protocol "is not engaged".

5.5 The Minister notes that negotiations are underway on a proposed Regulation which would repeal and replace eu-LISA's founding Regulation, extending the Agency's mandate to oversee new EU information systems and authorising it to undertake the necessary preparatory work to make the EU's justice and home affairs information systems interoperable.[77] He says it is "likely" that the participation of the Schengen associated countries in eu-LISA will remain effective under the new Regulation (if adopted).[78]

75 See Article 37 of Regulation (EU) No 1077/2011 establishing eu-LISA which provides: "Under the relevant provisions of their association agreements, arrangements shall be made in order to specify, inter alia, the nature and extent of, and the detailed rules for, the participation by countries associated with the implementation, application and development of the Schengen acquis and Eurodac-related measures in the work of the Agency, including provisions on financial contributions, staff and voting rights."

76 As the formula for calculating the annual contribution is mainly based on each participating Schengen associated country's GDP as a proportion of the GDP of all participating countries, it may have the effect of reducing the UK's overall contribution to eu-LISA.

77 See our Thirty-second Report agreed on 20 June 2018, our Twenty-first Report agreed on 21 March 2018, our Eleventh Report agreed on 24 January 2018, our Seventh Report agreed on 19 December 2017 and our First Report agreed on 13 November 2017.

78 Article 38 of the proposed Regulation provides for participation in eu-LISA to be open to countries associated with the Schengen rule book and Eurodac-related measures on the same basis as Article 37 of the current (2011) Regulation establishing eu-LISA.

5.6 Shortly after submitting his Explanatory Memorandum, Home Office officials informed us that the Justice and Home Affairs Council on 11/12 October was expected to adopt the proposed Council Decision authorising the EU to sign the Arrangement.

Our Conclusions

The UK's position at the Justice and Home Affairs Council

5.7 **We understand that the October Justice and Home Affairs Council endorsed the terms of the Arrangement and adopted the proposed Council Decision authorising the EU to sign it. We ask the Minister to explain how the UK voted.**

The application of the UK's Title V opt-in Protocol

5.8 **We accept that there are strong grounds for extending participation in eu-LISA to Schengen associated countries. We are nonetheless concerned that the position taken by the Government on the non-application of the UK's Title V (justice and home affairs) opt-in Protocol represents a significant departure from existing policy and established precedent.**

5.9 **We draw the Minister's attention to a letter dated 3 November 2011 from the then Home Secretary (Theresa May) in which she set out the Government's policy on the interpretation and application of the Title V opt-in Protocol:**

> **We have […] reviewed the UK position on the issue of exclusive external competence and have decided to depart from the policy we inherited from the previous Government. We consider that the opt-in does apply to all measures containing JHA obligations, even where the UK has exclusive external competence in relation to those obligations based on the adoption of internal JHA rules that bind the UK. *This means that if an internal EU rule, to which the UK previously opted in, was subsequently extended to a third country we would consider that the opt-in applies to the extension of that measure and would reserve the right to decide whether or not to participate in the new agreement, even if the EU was exercising exclusive external competence.* [Our emphasis]**

5.10 **We also draw his attention to similar Council Decisions adopted in 2014 concerning the participation of the Schengen associated countries in the European Asylum Support Office.[79] On that occasion, the Government was unable to secure a recital reflecting its position that the UK's Title V opt-in Protocol applied, but said that it would "make our position clear by sending a letter to the Presidency indicating that we were opting in and putting our opt-in position on record by means of a minute statement".[80] Our predecessors endorsed the Government's approach, observing that the Government had been vigilant in asserting its opt-in rights where it considered there to be "JHA content", even in the absence of a Title V legal base, and so should be equally vigilant when Title V legal bases were cited.**

79 See our predecessors' Thirtieth Report agreed on 15 January 2014 and Thirty-fourth Report agreed on 5 February 2014.

80 See the letter dated 30 January 2014 from the then Immigration Minister (Mark Harper) to the Chair of the European Scrutiny Committee.

5.11 **We ask the Minister to explain why he has departed from policy and precedent by accepting the Commission's position that the UK is automatically bound by the proposed Council Decisions and is not entitled to opt out under the terms of the Schengen opt-out Protocol or to choose not to opt in under the Title V opt-in Protocol.**

The UK's relationship with eu-LISA post-exit

5.12 **The proposed Council Decisions are intended to give effect to Article 37 of the 2011 eu-LISA Regulation which provides for the participation of the Schengen associated countries in the activities of the Agency. We ask the Minister:**

- **whether this Article (or its equivalent — Article 38 — in the proposed successor Regulation) would provide an appropriate legal base for the UK to participate in eu-LISA once it has left the EU, given that it only applies to third countries associated with the Schengen rule book and Eurodac-related measures; and**
- **whether the terms of the Arrangement with the four Schengen associated countries (including the funding formula, voting rights and jurisdiction of the EU's Court of Justice) would provide a suitable precedent for the UK as a third country.**

5.13 **Pending the Minister's response, the proposed Council Decisions remain under scrutiny. We draw this chapter to the attention of the Home Affairs Committee, Justice Committee and the Exiting the European Union Committee.**

Full details of the documents:

(a) Proposal for a Council Decision on the signing on behalf of the European Union of the Arrangement with Norway, Iceland, Switzerland and Liechtenstein on participation by those States in the European Agency for the operational management of large-scale IT systems in the area of freedom, security and justice: (40044), 11805/18 + ADD 1, COM(18) 607.

(b) Proposal for a Council Decision on the conclusion of the Arrangement with Norway, Iceland, Switzerland and Liechtenstein on participation by those States in the European Agency for the operational management of large-scale IT systems in the area of freedom, security and justice: (40045), 11804/18 + ADD 1, COM(18) 606.

Previous Committee Reports

None.

6 Preventing the dissemination of terrorist propaganda online

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, the Justice Committee, the Digital, Culture, Media and Sport Committee and the Joint Committee on Human Rights
Document details	Proposal for a Regulation on preventing the dissemination of terrorist content online
Legal base	Article 114 TFEU, ordinary legislative procedure, QMV
Department	Home Office
Document Number	(40069), 12129/18 + ADDs 1–3, COM(18) 640

Summary and Committee's conclusions

6.1 The global reach of the internet and its penetration into all aspects of daily life make it a potent tool for terrorist propaganda and recruitment. One of the core tasks of the EU Internet Referral Unit (based in Europol's European Counter-Terrorism Centre) is to strengthen cooperation between the internet industry and the law enforcement community in identifying and removing online terrorist content. The Unit itself has no enforcement powers — whilst it can "flag" and refer terrorist content to the host platform, the decision to remove the offending material is taken by the hosting company in accordance with its terms and conditions. Since becoming operational in July 2015 until the end of 2017, the Internet Referral Unit has made 44,807 referrals across 170 online platforms and achieved a 92% success rate for removal.[81] Despite this progress, the European Commission considers that voluntary referrals alone are insufficient to ensure that terrorist content is detected and swiftly removed before it can be disseminated across other online platforms. At their June Summit meeting, EU leaders welcomed the Commission's plans to put forward a new law.[82] In his State of the Union speech in September 2018, Commission President Jean-Claude Juncker announced that the EU would be proposing "new rules to get terrorist content off the web within one hour — the critical window in which the greatest damage is done".[83]

81 See the EU Internet Referral Unit Transparency Report 2017.

82 The Conclusions agreed by EU Leaders on 28 June 2018 "welcome the intention of the Commission to present a legislative proposal to improve the detection and removal of content that incites hatred and to commit terrorist acts".

83 For an overview of the Commission's proposal, see the European Commission's fact sheet published on 12 September 2018, A Europe that protects: Countering terrorist content online.

6.2 The Commission's proposal for a Regulation would establish a harmonised set of rules to prevent the dissemination of terrorist content on internet platforms hosted by service providers ("hosting service providers") who offer their services in the EU, even if their headquarters are outside the EU.[84] The main elements of the proposal are:

- a clear definition of "terrorist content" encompassing material that incites, advocates or glorifies the commission of terrorist offences, provides instruction on how to commit a terrorist offence, or promotes the activities of a terrorist group — according to the Commission, such content could be in text form, images, sound recordings and videos but should not encompass "the expression of radical, polemic or controversial views in public debate on sensitive political questions";[85]

- a new "duty of care" on hosting service providers to prevent the dissemination of terrorist content (including specific provisions in their terms and conditions) and to protect users — this may necessitate additional "proactive measures" (such as the use of automated tools to identify suspicious material) which are proportionate to the risk of exposure to terrorist content;[86]

- a requirement for hosting service providers to notify national law enforcement authorities (and/or Europol) if they become aware of any evidence of terrorist offences;[87] and

- a power for national authorities to issue a legally binding "removal order" requiring the hosting service provider to remove terrorist content or disable access to it *within one hour* — the Commission cites research indicating that a third of all links to Daesh propaganda are disseminated within the first hour of release, and the majority within two hours.[88]

6.3 The new power to issue a removal order would operate alongside existing voluntary referral mechanisms, but with a clear obligation on hosting service providers to put in place the necessary operational and technical measures to ensure that referrals are dealt with expeditiously.[89] They would also be required to preserve any terrorist content and related data removed from their platform for at least six months to allow for the completion of any complaint and review procedures and in case the information is needed for a criminal investigation or prosecution.[90] The proposed Regulation also seeks to strengthen cooperation between national authorities and with Europol to avoid duplication, enhance coordination and prevent any interference with ongoing investigations. It envisages that

84 This includes service providers who are not established in the EU but have a substantial connection with one or more Member States because, for example, their activities are targeted towards those countries or they have a significant number of users — Article 2(3).

85 See Article 2(5) and recital (9) of the proposed Regulation and the Commission's fact sheet on taking action to get terrorist content off the web, issued on 12 September 2018. The definition draws on the definition of terrorist offences in Directive (EU) 2017/541 on combating terrorism.

86 Article 3.

87 Article 13(4).

88 See Article 4 and Annex 9, p.141 of the Commission's Impact Assessment accompanying the proposed Regulation (ADD 2). A Member State may designate an administrative, law enforcement or judicial body as the authority responsible for issuing removal orders — see recital (13) of the proposed Regulation.

89 Article 5.

90 Article 7. Related data can include subscriber data (to identify the content provider) and access data (such as log-in and log-off times, IP address, etc) — see recital (20) of the proposed Regulation.

Member States and hosting service providers would be able to use tools and platforms developed by Europol to communicate with each other, channel removal orders and referrals and provide feedback.[91]

6.4 The proposed Regulation includes a range of safeguards in recognition of "the fundamental importance of freedom of expression and information in an open and democratic society".[92] The content provider or hosting platform would be entitled to request a detailed statement of the reasons justifying the issuing of a removal order and to appeal against it.[93] In addition, hosting service providers would be required to:

- include in their terms and conditions details of their policies on preventing the dissemination of terrorist content and publish annual transparency reports on how their policies have been implemented;[94]
- put in place human oversight and verification mechanisms where automated tools are used to detect terrorist content;[95]
- inform content providers if their material has been removed (subject to a time-limited public security exception);[96] and
- establish an effective and accessible complaints mechanism enabling content providers to challenge the removal of their material.[97]

6.5 To ensure effective implementation, hosting service providers must establish a point of contact (available around the clock) to receive and process removal orders and referrals and, if not established in the EU, designate a legal representative within the EU responsible for ensuring compliance with the requirements of the proposed Regulation.[98] Member States must have "the necessary capability and sufficient resources" to fulfil the following functions:

- issue (mandatory) removal orders;
- refer suspected terrorist content to hosting service providers for further assessment;
- oversee the implementation of "proactive measure" taken by hosting service providers to prevent the dissemination of terrorist content and, where necessary and proportionate, require additional measures to be taken;[99] and
- ensure that the penalties envisaged in the proposed Regulation are applied — whilst these are to be determined by Member States, a "systematic failure" to comply with a removal order would be punishable by a fine of up to 4% of the hosting company's global turnover in the previous business year.[100]

91 Article 13.
92 See Articles 3(1) and 6(4).
93 Article 4(4) and (9).
94 Article 8.
95 Article 9.
96 Article 11.
97 Article 10.
98 Articles 15 and 16.
99 Article 6.
100 Articles 17 and 18.

6.6 The proposed Regulation supplements a non-binding Recommendation on measures to tackle illegal online content adopted by the European Commission in March 2018. The Commission considers that legally binding EU rules dealing specifically with online terrorist content are necessary to address the scale of the threat to public security, ensure a more effective response, protect fundamental rights and ensure "a level playing field" for all hosting service providers operating within the EU's Digital Single Market. The proposal cites an internal market legal base — Article 114 of the Treaty on the Functioning of the European Union (TFEU) — as harmonised rules will provide "clarity and greater legal certainty", strengthen trust in the online environment and prevent the emergence of different regulatory approaches across the EU which would impede the functioning of the internal market, "creating unequal conditions for companies as well as security loopholes".[101] The Commission is keen to secure the adoption of the proposed Regulation before the next European Parliament elections in May 2019 (meaning that it would have to approved by March 2019 at the latest). The Commission envisages that the Regulation (a directly applicable measure) would take effect six months after its formal adoption and entry into force.

6.7 In his Explanatory Memorandum of 10 October (see part one and part two), the Minister for Security and Economic Crime (Ben Wallace) welcomes the prospect of EU regulatory action to tackle online terrorist content. Whilst acknowledging the value of voluntary cooperation with service providers, he considers that tech companies "have not gone far enough or fast enough" and that the proposed Regulation will "lay the groundwork and support our own intention to legislate on illegal online content", following the publication later this year of a White Paper covering "the full range of online harms". He shares the Commission's view that a fragmented framework of national rules would be burdensome for companies operating within the EU's digital single market and that Article 114 TFEU, rather than EU Treaty provisions on justice and home affairs matters, is the appropriate legal base as the proposed Regulation does not impose any obligations on judicial or law enforcement bodies.

6.8 The Minister considers that the UK is "well-configured" to implement the proposed Regulation as the UK's Counter-Terrorism Internet Referral Unit (CTIRU) already refers terrorist content to hosting service providers and the Terrorism Act 2006 includes provision for referrals and removal orders. Whilst these are valuable tools, the processes involved in detecting and alerting tech companies to terrorist content are nonetheless too slow:

> Terrorist content may already have been live on platforms for many hours or days before human moderators come across them, by which time the content will likely have been further disseminated or downloaded by supporters. While we welcome the proposal's one-hour timeframe set for the removal of content by an HSP [hosting service provider] and the focus on quick removal, it will likely have taken a competent authority more than one hour to pull this request together. Furthermore, as a legal order, judicial sign off may also be needed, adding to the time taken to issue a removal order.

101 See p.5 of the Commission's explanatory memorandum accompanying the proposed Regulation and recital (1) of the proposed Regulation.

6.9 Moreover, the bulk of terrorist content is detected through tech companies' own technology or internal reviewers rather than through user reports or referrals, underscoring the need for "automated tools and proactive action" by the companies themselves to counter the speed at which terrorist content is disseminated. The Minister therefore expresses the Government's "full support" for the provisions in the proposed Regulation requiring hosting service providers to take proactive measures to prevent the dissemination of terrorist content. For these provisions to be effective, he recognises that there is a need to develop the capacity of smaller tech companies to use automated detection tools and to share guidance on proactive measures across Member States so that they can be implemented in a consistent manner, whilst ensuring they are "proportionate" to the economic capacity of each service provider and the degree of risk that their platform may be used to host terrorist content.

6.10 The Minister welcomes the inclusion of a specific recital in the proposed Regulation clarifying that an obligation placed on hosting service providers to take specific and targeted proactive measures to detect terrorist content would not conflict with the EU's E-Commerce Directive which prevents Member States from imposing on service providers a general obligation to "monitor the information which they transmit or store" or "actively to seek facts or circumstances indicating illegal activity".[102] Whilst the Government would have preferred to go further in fleshing out the proactive measures to be taken by hosting service providers, the Minister recognises that "the Commission has had to act within the limiting parameters of the E-Commerce Directive". He considers that the approach taken by the Commission in seeking to balance public security and fundamental rights (notably, freedom of expression and freedom to conduct a business) establishes "a helpful precedent as we look to develop measures for our domestic legislation on online harms".

6.11 The Minister expresses concern that the provisions on penalties leave too much discretion to Member States, creating a risk that they could choose to set a low bar to attract investment by tech companies. He anticipates that the Commission will be invited to produce guidance "to harmonise penalties across Member States". He also expects the Commission to look again at a provision authorising the Member State issuing a removal order to impose financial penalties, even if the hosting service provider is established in another Member State.[103]

6.12 Whilst recognising that the proposed Regulation would "potentially interfere with a number of fundamental rights", the Minister says it includes "robust safeguards" which ensure that any interference is "limited to what is necessary to protect the public" and that "the requirements of proportionality are interwoven" in all the provisions. He is sanguine about the possibility that the UK may be required to implement the Regulation if it takes effect during a post-exit transition/implementation period, observing:

> To date, the issue of how we tackle terrorist content online has been a somewhat politically neutral issue within the Brexit landscape, as both sides agree more needs to be done, and we have worked collaboratively with our European partners, both bilaterally (particularly with France and Germany) and through the EU Internet Forum. The UK is the global lead

102 See Article 15 of Directive 2000/31/EC on certain legal aspects of information society services, in particular electronic commerce, in the Internal Market (Directive on electronic commerce) and recital (19) of the proposed Regulation.

103 See Article 15(3) of the proposed Regulation.

> on this issue and EU partners value our expertise and views on how to address terrorist content online. We intend to continue to work closely with our EU partners to tackle these issues whilst we remain a Member State and in the future.

6.13 The Minister notes the Commission's intention to secure a general approach in the Council by December 2018 and to conclude trilogue negotiations with the European Parliament no later than March 2019.

Our Conclusions

6.14 **We thank the Minister for his thorough and informative Explanatory Memorandum. Although the proposed Regulation concerns the regulation of online terrorist content, the Government accepts that its principal purpose is to ensure the proper functioning of the EU's digital single market and that Article 114 TFEU (on the internal market) is the correct legal base. This means that the UK will be bound to implement the proposal if it is adopted and takes effect before the UK's exit from the EU (on 29 March 2019) or during a post-exit transition period ending on 31 December 2020. We ask the Minister:**

- **how much support there is for the proposed Regulation amongst Member States and how likely it is to be adopted before the UK leaves the EU, so that the UK would have a vote on the final text agreed;**
- **whether the Government intends to seek changes to the proposal during negotiations;**
- **whether it will be necessary to amend domestic law to implement the proposed Regulation; and**
- **if so, whether any amendments required could be included in the Counter Terrorism and Border Security Bill or would require separate legislation.**[104]

6.15 **The Minister indicates that the Commission may be invited to issue "guidance in order to harmonise penalties across Member States". We ask the Minister:**

- **how great a risk there is that Member States may wish to undercut one another to attract higher levels of investment by hosting service providers;**
- **whether the Commission guidance would be non-binding and, if so, how effective it would be;**
- **whether the Government would support the inclusion of more specific penalties within the Regulation itself; and**
- **if so, whether this would be consistent with the use of an Article 114 TFEU legal base or require the addition of a Title V (justice and home affairs) legal base, bringing into the play the UK's Title V opt-in Protocol.**

104 Under section 3 of the Terrorism Act 2006, terrorist content notified to a hosting service provider must be removed within two working days — substantially longer than the one hour envisaged in the proposed Regulation.

6.16 **We also ask the Minister whether the proposed Regulation should indicate what degree of non-compliance might be considered "systematic" (attracting a fine of up to 4% of the hosting service provider's global turnover in the previous business year) and how concerned he is that such an open-textured and ill-defined provision may induce excessive caution on the part of hosting service providers and have a chilling effect on freedom of expression.**

6.17 **One of the Commission's objectives in putting forward the proposed Regulation is to establish "a clear and harmonised legal framework to prevent the misuse of hosting services for the dissemination of terrorist content online".[105] We ask the Minister whether the proposal (including its recitals) provides sufficient clarity and legal certainty regarding the obligations applicable to the providers of information society services under this and other EU laws. We have in mind the difficulty in reconciling the proactive measures permitted under the proposed Regulation (aimed at preventing the dissemination of online terrorist content) and the obligation under the E-Commerce Directive to protect freedom of expression by precluding any general monitoring obligation.**

6.18 **Finally, we ask the Minister to clarify the circumstances in which it would be appropriate to make a referral rather than issue a removal order under the proposed Regulation, given that for referrals there is no set time limit within which hosting service providers would be required to remove the offending content or disable access to it.**

6.19 **Pending further information, the proposed Regulation remains under scrutiny. We draw this chapter to the attention of the Home Affairs Committee, the Justice Committee, the Digital, Culture, Media and Sport Committee and the Joint Committee on Human Rights.**

Full details of the documents:

Proposal for a Regulation on preventing the dissemination of terrorist content online: (40069), 12129/18 + ADDS 1–3, COM(18) 640.

Background

6.20 The Minister's Explanatory Memorandum sets out the context which has informed the Commission's approach to the regulation of online terrorist content:

> In 2017, there were a total of 205 foiled, failed and completed terrorist attacks in the EU, which killed over 68 and injured many more. The continued high level of terrorist threat in the EU is accompanied by continued concern about the role of the internet in aiding terrorist organisations to facilitate and direct such terrorist activity, but also to radicalise, inspire and recruit, particularly through the dissemination of propaganda. Such illegal terrorist content is shared online in particular through online services that allow the upload of third party content, also known (in this particular context) as hosting service providers (HSPs). This Regulation focuses on the availability and spread of terrorist content on such hosting services.

105 See p.2 of the Commission's explanatory memorandum accompanying the proposed Regulation.

> To date, governments, with the UK leading the way, have worked directly with tech companies on a collaborative, voluntary basis, to address the misuse of their platforms by terrorists to disseminate propaganda, recruit, radicalise and inspire individuals, and plan attacks. We have also engaged with the Global Internet Forum to Counter Terrorism (GIFCT), an industry-led group set up by Google, Facebook, Twitter and Microsoft, as well as through the EU Internet Forum on terrorist content online (launched in December 2015). By sharing our unique understanding of the threat and analysis of how groups such as Daesh use HSPs, the UK has been able to push some of the largest tech companies to do more to tackle this issue. This voluntary approach has yielded results. For example, Facebook announced that it had taken action on 1.9 million pieces of Daesh and al-Qaeda content in Q1 of 2018 — about twice as much from the previous quarter. Twitter also announced in April that, between July and December 2017, 274,460 accounts were suspended for violations related to promotion of terrorism, with 74% of those accounts suspended before their first tweet.
>
> Despite this progress by some of the largest HSPs (Facebook. Google/ YouTube and Twitter), the availability of terrorist content online remains a cause for concern, both in the UK and in the EU. Europol reports that over 150 platforms were identified as hosting terrorist content. A significant number of these companies are established outside of Europe but offer their services within the EU. With terrorist content still accessible on the open Internet and as content continues to diversify and spread on to a wide range of smaller platforms, the EU sees the need to address the issue as an urgent imperative. Voluntary collaboration with some of the major HSPs has only taken us so far, and to fully tackle terrorist content online, regulatory action is necessary.

6.21 The Minister provides details of the outcome of the Commission's consultation on tackling illegal content online. Whilst hosting service providers supported the continuation of a voluntary approach, they recognised "the potential negative effects of emerging legal fragmentation in the Union" and accepted that, if there had to be legislation, it should take the form of "a targeted intervention on specific issues of particular public value (e.g. a focus on terrorist content compared to all online harms)". Many Member States considered that there was a need for binding EU legislation on terrorist content. Stakeholders nonetheless underlined the need to safeguard fundamental rights, particularly freedom of speech.

6.22 The UK response to the consultation:

> […] reflected a previously expressed view that prioritising the use of proactive measures by HSPs to tackle terrorist content online, specifically automated removals, is the best way to make a meaningful impact on the problem. As such, we suggested that any EU action should: not rely solely on referral or 'notice and takedown' measures but put a requirement on the companies to specifically monitor their platforms for terrorist content; reinforce the importance of speed of removal; and ensure that companies take action within an hour of upload or ultimately prevent the content from being uploaded in the first place.

6.23 The Minister recognises that the proposed Regulation will have the greatest impact on small, medium and micro companies that "do not already have the relevant processes in place to address dissemination of terrorist content" (for example, content moderation, filtering technologies) or to fulfil new transparency reporting requirements. There is a risk that the proposal could "reinforce the relative market power of the very large companies which have already internalised costs for the associated processes, or which have preferential arrangements between them to share specific technologies, if these technologies are not available to all market participants". The Government is "actively lobbying the largest tech companies to share tools and expertise with smaller HSPs".

6.24 There is a further risk that the resources needed to comply with the proposed Regulation could have a negative impact on innovation. This has to be set against the potential to "incentivise further technology development on tools for automatic content detection, filtering and moderation technologies" and the prospect that a higher level of trust in the hosting service providers may lead to "greater uptake of digital services", greater investment and increased advertisement revenues.

6.25 The proposed Regulation would increase costs for Member States which lack the capability to detect and notify illegal online content swiftly. However, the costs for the UK are expected to be "minimal" as it already has an effective body (the Metropolitan Police's Counter Terrorism Internet Referral Unit) and the necessary infrastructure to implement the proposal.

Previous Committee Reports

None.

7 European Defence Fund 2021–27

Committee's assessment	Politically important
Committee's decision	Not cleared from scrutiny; further information requested; drawn to the attention of the Business, Energy and Industrial Strategy and Defence Committees
Document details	Proposal for a Regulation establishing the European Defence Fund 2021–2027
Legal base	Articles 173(3), 182(4), 183 and 188 TFEU; ordinary legislative procedure; QMV
Department	Ministry of Defence
Document Number	(39894), 10084/18 + ADDs 1–2, COM(18) 476

Summary and Committee conclusions

Summary

7.1 The EU's Member States and the European Parliament are currently considering a Regulation establishing a European Defence Fund for the 2021–2027 period. With a budget of €13 billion, it would finance research into, and development of, new military technologies for acquisition by the armed forces of EU Member States. The Minister for Defence Procurement (Andrew Stuart) wrote to us on 10 October 2018 with an update on the legislative deliberations, explaining that the Member States are due to adopt their position on the proposal on 20 November with a view to its formal adoption in spring 2019.

7.2 The Minister also reiterated that the UK is seeking some form of participation in the European Defence Fund after Brexit, but added that the exact legal parameters—and, consequently any (potential) UK financial or material contribution to the Fund—remain unclear given that the EDF Regulation is still subject to change. The Committee has asked to be kept informed of further developments in the legislative process and will assess the potential political and financial implications of the Fund for the UK accordingly.

Background

7.3 Since 2017, the EU has been setting aside part of its budget for investment in research and development of military technology, such as encrypted software and drone technology,

as part of a wider effort to make the Union a more cohesive actor in military affairs.[106] This 'European Defence Fund' is due to be fully operational from 1 January 2021, under the EU's next Multiannual Financial Framework.[107]

7.4 The European Commission presented a formal Regulation to establish the Defence Fund in June 2018, recommending a budget of €13 billion (£11.6 billion) for the period from 2021 until 2027 for investment in the "competitiveness, efficiency and innovation capacity of the European defence industry". Financial assistance would normally take the form of grants, although it could also take the form of a public procurement exercise (after which the resulting results would be owned by the European Union).

7.5 Despite the UK's exit from the EU, the Government has supported the establishment of the Defence Fund, citing the benefits to Europe's defensive capabilities, and the Ministry of Defence is actively seeking ways for the British defence industry to be eligible for funding despite the UK's impending exit from the EU and its new status as a 'third country'.[108] However, UK participation in the Fund would be complicated, as it is due to have left the European Union by the time it becomes operational. As such, it would not have automatic right that EU Member States do to be involved in the Fund. Even during the post-Brexit transitional period, when the UK will be a 'third country' while still making budgetary contributions and accepting the supremacy of EU law, the UK's status under the Fund's precursor—the Defence Industrial Development Programme (EDIDP)—is not guaranteed.[109]

7.6 That is not to say that UK participation in the European Defence Fund as a 'third country' is not possible. If the post-Brexit transitional period were to be extended beyond its current proposed end date of 31 December 2020, the UK defence industry might be eligible for participation in the Fund—subject to certain restrictions, which we have elaborated previously—so long as the UK also remained a contributor to the EU budget for the duration of that extension.[110] Once the UK exits the transitional arrangement, there are two theoretical options for its involvement in the Fund.

7.7 Firstly, the Commission proposal contains an explicit provision permitting non-EU countries to seek 'association' with the Fund: in return for a financial contribution, and subject to the EU's agreement, their defence industry would be eligible for funding on the same terms as those of EU Member States. 'Association' does not provide voting rights

106 For example, as part of the 'European Defence Union', Member States have launched Permanent Structured Cooperation on defence and established a centralised Military Planning & Conduct Capability unit for the EU's advisory military missions. The European Commission is also proposing to use the EU's post-2020 Connecting Europe Facility to invest in dual-use infrastructure that can be used by armed forces to move troops and equipment around Europe more efficiently, and has proposed the establishment of a 'European Peace Facility' (considered in a separate Chapter of this Report).

107 The Fund is currently effectively in a pilot phase: a small-scale defence research programme was launched in 2017, and a two-year industrial development fund for the defence industry— the EDIDP—is due to become operational in early 2019. Both strands are linked to the EU's current budgetary cycle, and will therefore end in December 2020.

108 See for example the Ministry of Defence's first Explanatory Memorandum on the European Defence Fund (July 2017). A May 2018 policy paper also confirmed that the Government wanted to discuss "models for participation of the UK, and UK entities" in the European Defence Fund after Brexit.

109 UK participation during the transitional period can be restricted unilaterally by the EU if a project funded under the EDIDP or the defence research programme lasted beyond the end of the transitional period. We have expressed concern about this aspect of the Withdrawal Agreement in more detail in our recent Reports on the European Defence Industrial Development Programme, most recently on 11 July 2018.

110 For more information on the potential restrictions on UK eligibility for EDF projects during an extended transition, please refer to our Report of 20 June 2018 on the EDIDP

over the work programme and individual funding decisions, which would be taken by EU Member States only. However, the Commission has proposed to restrict the ability to seek 'association' only to the three EFTA-EEA countries (Norway, Iceland and Liechtenstein).[111] The UK, considering the Government's policy on the future UK-EU relationship, would therefore not qualify. Limiting the scope of the 'association' process is not, it appears, being challenged by the remaining Member States (see paragraph 7.11 below).

7.8 Secondly, for 'third countries' that *cannot* seek association under the Commission proposal, eligibility for EDF funding would exist but in a limited form: only EU-based subsidiaries of parent undertakings controlled from that third country would be eligible. Furthermore, these subsidiaries would only be able to access funding "if this is necessary for achieving the objectives of the [project] and provided that […] participation will not put at risk the security interests of the Union and its Member States". They would also need to guarantee that any classified information that forms part of the EDF project is not shared with any entity outside the EU or an 'associated country'.[112] In addition, under the Commission proposal, "infrastructure, facilities assets, and resources" located outside of the EU could only be used for EDF projects in a narrowly-prescribed range of circumstances,[113] and ex-post use of technology developed with EDF funding by a non-EU country like the UK could be restricted.[114]

7.9 In August 2018, the Minister for Defence Procurement (Andrew Stuart) confirmed that the Government was working to persuade the European Parliament and the other Member States to make it easier for 'third countries' like the UK to be involved in EDF-funded projects.[115] We also set out the substance of the Commission proposal in some detail in our Report of 12 September 2018, in which we raised concerns about the UK's potential participation in the Fund and the fact that the EU would own any results of procurement exercises financed from it.

The Minister's letter of 10 October 2018

7.10 On 10 October, the Minister wrote to the Committee with further information on the position taken by the Member States on the Commission proposal for the EDF. He noted that the Council's starting point is to copy for the most part the legal text underpinning

111 In practice this would have limited non-EU participation to Norway.

112 This partial derogation to the eligibility criteria—based in the EU, but controlled from elsewhere—is not available to subcontractors: to be eligible for funding, they must be based in, and controlled from, the EU or an associated country. There appears to be some very limited leeway for UK-based or controlled companies to act as sub-contractors vis-à-vis a beneficiary from the European Defence Fund, provided the costs of their contribution are not paid for by the Fund and they do not have access to classified information related to the project.

113 Use of non-EU facilities would have to be "necessary for achieving the objectives of an action", a new test that does not apply under the current EDIDP Regulation for use of beneficiaries' resources or infrastructure located outside the EU; the non-EU 'infrastructure, facilities, assets and resources' must be owned by the beneficiary of EDF funding, or their subcontractor, either of which must by definition be based in the EU or an associated country; and the costs of using any non-EU assets cannot be defrayed against the grant from the European Defence Fund.

114 Under article 25 of the draft Regulation, the Commission has to be notified of "any transfer of ownership or grant of a licence to non-associated third countries". If the transfer or licence contravened the "defence and security interests of the Union and its Member States", this would "necessitate reimbursement of the funding provided under the Fund".

115 The Ministry of Defence acknowledged the limitations of the 'association' mechanism in a letter to the House of Lords dated 1 August 2018. The proposal to establish the European Defence Fund is subject to the ordinary legislative procedure, and as such the European Parliament and the Member States in the Council must jointly agree on its legal text.

the 2019–20 European Defence Industrial Development Programme (the pilot phase for the Fund), and focussing discussions on the new elements such as financial instruments—use of the Fund's resources to guarantee risky private investment in defence projects[116]—and funding priorities (like disruptive military technologies).

UK participation in the European Defence Fund after Brexit

7.11 The Minister also provided an update on the possibility for the UK to be involved in the Fund—and for its industry to receive funding from it—as a 'third country'. He explained that the other Member States are seeking to remove some of the additional restrictions the Commission had put in place for 'third country' involvement and facilitate such cooperation within the Fund, for example with the UK. On this basis, the Austrian Presidency of the Council circulated proposed revision to the draft legal text in early October, which, the Minister says, "is now broadly acceptable to the UK".[117]

7.12 We understand that full 'association' with the Defence Fund, even under this revised text, would be an option only for the EFTA-EEA countries and therefore not for the UK.[118] British defence industry would therefore be subject to the restrictions and limitations on participation we described in paragraph 0.x above and in more detail in our Report of 12 September 2018. Notably, any such participation would have to be self-funded (as UK entities would be ineligible for EDF funding) and take place on a case-by-case basis.

7.13 Since we received the Minister's letter, the Prime Minister has said the UK is considering an extension of the post-Brexit transitional period into 2021.[119] During that transition, which under the current draft of the Withdrawal Agreement is due to last until 31 December 2020, the UK is required to make budgetary contributions as if it were still an EU Member State (albeit with limited representation in the EU institutions and no voting rights over EU policy or funding decisions). Any such extension would mean the UK were still in the transitional arrangement when the next Multiannual Financial Framework, and the new European Defence Fund, become operational. In that case, the UK might have no choice but to contribute to the Instrument until the transitional period ended, but with little influence over how its money was spent.

EU ownership of defence procurement exercises

7.14 In our last Report on the European Defence Fund, the Committee raised concerns about two provisions of the proposed EDF Regulation that would make the EU the owner of any procurement exercises—whether for defence research (article 22.2 of the Regulation) or development of military technology (article 25.4)—financed by the Defence Fund.

7.15 The Minister acknowledged in his letter that this"inevitably gives rise to concerns over the EU ownership of defence capabilities", but added that under the legal base for

116 See for more information on the use of financial instruments to mobilise private investment our recent Report on the InvestEU proposal.

117 The Presidency text is classified as LIMITE and therefore not publicly accessible at this stage.

118 The Minister notes the UK is also pushing for a provision allowing for the participation of international organisations (such as the Joint Research Centre) with the same rights and obligations as a legal entity established in an EU Member State or associated country.

119 https://www.bbc.co.uk/news/uk-politics-45897253.

the Regulation,[120] the Commission would be "unable to procure military equipment". He added that EDF funding is "generally expected" to take the form of grants rather than procurement, and that the European Commission had assured the Member States that "it would use public procurement in limited circumstances such as to procure studies, either for Commission policy making or of general value and to procure their secure IT system for managing the [Fund]".

Legislative timetable for adoption of the EDF Regulation

7.16 As regards the legislative timetable, the Minister explains the Austrian Presidency is hoping to secure a partial general approach on the Regulation at the meeting of EU Defence Ministers on 20 November 2018.[121] This would establish the Member States' common position on the European Defence Fund for negotiations with the European Parliament on the final legal text, with the exception of the Fund's budget (which will be decided as part of the wider negotiations on the EU's spending priorities under the next Multiannual Financial Framework).

7.17 The European Parliament is expected to finalise its position around the same time,[122] with the aim of agreement on the European Defence Fund Regulation between the Parliament and the Member States before the 2019 European elections.

Our assessment

7.18 **We thank the Minister for his timely update on the negotiations for the post-2020 European Defence Fund. The Government has strongly hinted that it wants to maximise opportunities for UK involvement in the new European Defence Fund after post-Brexit the transitional period as a 'third country'. The legal text underpinning the Fund, even taking into account the amendments proposed by the Member States, would severely restrict the scope of participation by the British defence industry in projects funded by the EDFIt appears that the remaining Member States support the Commission proposal that full 'association' with the Fund—making a non-EU country's defence industry generally eligible for EDF funding in return for an annual financial contribution from its Government—will be available only to the EFTA-EEA countries. Organisations from non-associated countries could be involved in EDF projects via EU-based subsidiaries, or on a very limited scale from a base in their home country.**

7.19 **While the current draft of the EDF legal text would therefore restrict the opportunities for UK participation after Brexit, it also assuages concerns we have voiced before about the potential downsides were the UK to seek 'association' with the European Defence Fund. In particular, as a non-associated 'third country', UK defence industry would participate in EDF projects only a case-by-case basis at its own**

120 The legal base for the proposed EDF Regulation is Articles 173(3), 182(4), 183 and 188 TFEU, and as such it will be financed from the general EU budget. Under Article 41(2) TEU, the general EU budget cannot be used for "operations having military or defence implications".

121 The Council meeting on 20 November 2018 would be preceded by a final Working Party meeting on 7 November, followed by diplomatic sign-off at the meeting of COREPER on 14 November.

122 The Industry, Research & Energy (ITRE) Committee has scheduled a vote on the Regulation for 21 November 2018.

volition, removing the need for an annual financial contribution from the UK taxpayer to the Fund—a requirement of association—with only limited influence over the way that money would be spent, or how any resulting technology could be used.

7.20 **We also note the remaining Member States are seeking to remove some of the restrictions proposed by the Commission on participation by non-associated 'third countries'. These changes may relate to the granting of licences for the use of EDF-funded military technology by 'third countries', which would make it easier for the UK to benefit from the Fund's successes (especially where EU-based subsidiaries of UK organisations were involved in the original EDF project).[123] However, we have not been able to assess the substance of the Council's efforts to facilitate third country involvement in the Fund, as we have not been able to view the latest Presidency legal text in which they are set out. Clearly, the more restrictive the intellectual property provisions of the Regulation in relation to transfers, or licences for use, of EDF-funded technology by 'third countries', the less value there would be for the UK to contribute to such projects.**

7.21 **In any event, the possibility of UK involvement in the European Defence Fund in any guise after the end of any extended transitional period will also depend on the overall political context: if the negotiations on the Withdrawal Agreement were to collapse, resulting in a disorderly UK exit from the EU, it is unlikely there would be a possibility of UK participation in any EU funding programmes until the outstanding issues related to UK withdrawal—not least its financial obligations vis-à-vis the EU budget accrued during its membership—were resolved.**

7.22 **Finally, the possibility that the post-Brexit transitional period could be extended — a suggestion made explicitly by the Prime Minister at the European Council summit on 17 October 2018 — could require the UK to remain a financial contributor to the European Defence Fund for the duration of the transition after 1 January 2021. In that eventuality, the same controversial restrictions on UK eligibility for participation in 'sensitive' projects — to which we objected in our scrutiny of the EDF's precursor programme, the EDIDP — could apply, despite the Fund being part-financed by UK taxpayers.[124]**

7.23 **Given the Government's desire to secure some form of UK participation in the Defence Fund after Brexit, and the consequent uncertainty about the legal and financial conditions for such involvement, we again retain the proposal under scrutiny. The Committee will in particular keep the legal provisions relating to 'third country' participation in the Fund under review, and assess the Government's position**

123 In its proposal for the EDF Regulation, the Commission proposed to revive a restriction, mooted but ultimately not included in the EDIDP precursor programme, that even the granting of a licence to a 'third country'—like the UK— to use defensive technology developed with EU funding could be subject to "all funding….. be[ing] reimbursed" if the licence contravene[s] the defence and security interests of the Union and its Member States. This could limit the extent to which technology developed with support from the EDF could be licensed to the UK defence industry, even if British companies had been involved in the original project via an EU-based subsidiary.

124 Under Article 127 of the draft Withdrawal Agreement, the EU during the transitional period can unilaterally exclude the UK from participating in EU-funded projects which are considered too 'sensitive' for involvement by a non-Member State. That provision can be invoked against the UK in relation to any projects funded from the European Defence Industrial Development Programme (EDIDP), and therefore by extension also to the European Defence Fund if the transitional arrangement is still active when the Fund goes 'live' in January 2021. We have described the implications of Article 127 in more detail in a series of Reports on the EDIDP in spring and summer 2018.

on post-Brexit participation accordingly. We will also reassess the potential financial and political implications of the EDF proposal for the UK if the draft Withdrawal Agreement is amended to include a mechanism for extension of the transitional period.

7.24 **The Minister notes the Presidency of the Council hopes to secure a partial general approach—an agreement among the Member States on all aspects of the Regulation establishing the European Defence Fund with the exception of its budget—at the meeting of EU Defence Ministers on 20 November 2018. We ask him to provide a further update, accompanied by the draft legal text, in good time before that meeting so that we can consider the granting of a scrutiny waiver. We will report the substance of any partial general approach to the House in due course.**

7.25 **We draw these developments to the attention of the Defence and Business, Energy & Industrial Strategy Committees.**

Full details of the documents:

Proposal for a Regulation establishing the European Defence Fund: (39894), 10084/18 + ADDs 1–2, COM(18) 476.

Previous Committee Reports

See (39894), 10084/18: Thirty-eighth Report HC 301–xxxvii (2017–19), chapter 26 (12 September 2018).

The Committee also considered the predecessor, the European Defence Industrial Development Programme, on five occasions. See: (38831), 10589/17: First Report HC 301–i (2017–19), chapter 30 (13 November 2017); Twelfth Report HC 301–xii (2017–19), chapter 10 (31 January 2018); Twenty-seventh Report HC 301–xxvi (2017–19), chapter 7 (9 May 2018); Thirty-second Report HC 301–xxxi (2017–19), chapter 8 (20 June 2018); and Thirty-fifth Report HC 301–xxxiv (2017–19), chapter 14 (11 July 2018).

8 EU Clean Energy legislation

Committee's assessment	Politically important
Committee's decision	Cleared from scrutiny (decision reported on 05/09/2018); drawn to the attention of the Business, Energy and Industrial Strategy Committee
Document details	(a) Proposal for a Directive amending Directive 2012/27/EU; (b) Proposal for a Directive on the promotion of the use of energy from renewable sources (recast); (c) Proposal for a Regulation on the Governance of the Energy Union, amending Directive 94/22/EC, Directive 98/70/EC, Directive 2009/31/EC, Regulation (EC) No 663/2009, Regulation (EC) No 715/2009, Directive 2009/73/EC, Council Directive 2009/119/EC, Directive 2010/31/EU, Directive 2012/27/EU, Directive 2013/30/EU and Council Directive (EU) 2015/652 and repealing Regulation (EU) No 525/2013
Legal base	(a) Article 194(2) TFEU, ordinary legislative procedure, QMV; (b) Article 194(2) TFEU, ordinary legislative procedure, QMV; (c) Articles 192(1) and 194(2) TFEU, ordinary legislative procedure, QMV
Department	Business, Energy and Industrial Strategy
Document Numbers	(a) (38340), 15091/16 + ADDs 1–13, COM(16) 761; (b) (38345), 15120/16 + ADDs 1–9, COM(16) 767; (c) (38352), 15090/16 + ADDs 1–5, COM(16) 759

Summary and Committee's conclusions

8.1 The Commission proposed its "Clean Energy for all Europeans" package[125] of legislation at the end of November 2016, aiming to "keep the European Union competitive as the clean energy transition is changing the global energy markets". We considered the outcome of negotiations on the proposals relating to energy efficiency, renewable energy and governance at our meeting of 5 September 2018.[126]

8.2 In her response[127] to our queries, the Minister of State for Energy and Clean Growth (Claire Perry) makes the following points:

- the transposition deadline for most of the Energy Efficiency Directive would be June 2020, thus falling within the proposed post-Brexit implementation period ending on 31 December 2020 and therefore requiring the UK to transpose the Directive;

125 "Commission proposes new rules for consumer centred clean energy transition", European Commission, 30 November 2016.

126 Thirty-seventh Report HC 301–xxxvi (2017–19), chapter 22 (5 September 2018).

127 Letter from Claire Perry to Sir William Cash, dated 11 October 2018.

- the Governance Regulation would apply upon entry into force (early 2019 at the latest), with the exception of a small number of provisions applicable from 1 January 2021, so most of it would need to be to applied by the UK under the terms of the implementation period;
- replying to the Committee's observation that the delineation between energy policy on the one hand and environmental and climate change rules on the other may not be as simple as portrayed by the Government in its White Paper on the future EU-UK relationship (which acknowledged the potential need for a common energy rulebook, but not extending to environmental and climate change rules), the Minister observes that the Clean Energy legislation does indeed have multiple objectives; and
- the UK's continued implementation of the nationally-binding energy savings target will be subject to the wider EU exit negotiations on the future EU-UK energy partnership.

8.3 **While we cleared the proposals from scrutiny at our meeting of 5 September, we report to the House the Government's response as we consider the Brexit-related elements to be of political importance. The Minister's recognition that delineation between EU energy, environmental and climate change policies is not as neat as presented in the White Paper on the future relationship between the EU and UK is of particular importance. It suggests that the Government either has not reflected in any depth on the conditions that it might demand in return for applying EU energy legislation, or it has reflected and does not have a clear position. We consider that it is likely to be futile at this stage to request any further detail from the Government but we flag our awareness of this gap in the Government's position and we will monitor discussions closely as we scrutinise the remaining elements of the Clean Energy Package.**

8.4 **The documents have already been cleared from scrutiny. We draw this chapter to the attention of the Business, Energy and Industrial Strategy Committee. We require no further correspondence on these proposals.**

Full details of the documents:

(a) Proposal for a Directive amending Directive 2012/27/EU: (38340), 15091/16 + ADDs 1–13, COM(16) 761;

(b) Proposal for a Directive on the promotion of the use of energy from renewable sources (recast): (38345), 15120/16 + ADDs 1–9, COM(16) 767;

(c) Proposal for a Regulation on the Governance of the Energy Union, amending Directive 94/22/EC, Directive 98/70/EC, Directive 2009/31/EC, Regulation (EC) No 663/2009, Regulation (EC) No 715/2009, Directive 2009/73/EC, Council Directive 2009/119/EC, Directive 2010/31/EU, Directive 2012/27/EU, Directive 2013/30/EU and Council Directive (EU) 2015/652 and repealing Regulation (EU) No 525/2013: (38352), 15090/16 + ADDs 1–5, COM(16) 759.

Previous Committee Reports

Thirty-seventh Report HC 301–xxxvi (2017–19), chapter 22 (5 September 2018); Thirtieth Report HC 301–xxix (2017–19), chapter 3, chapter 4 and chapter 6 (6 June 2018); Fifth Report HC 301–v (2017–19), chapter 2, chapter 3 and chapter 5 (13 December 2017); Fortieth Report HC 71–xxxvii (2016–17), chapter 4, chapter 5 and chapter 7 (25 April 2017); Twenty-ninth Report HC 71–xxvii (2016–17), chapter 2, chapter 3 and chapter 5 (25 January 2017).

9 European Electronic Communications Code

Committee's assessment	Politically important
Committee's decision	Cleared from scrutiny; drawn to the attention of the Digital, Culture, Media and Sport Select Committee and the Select Committee for Exiting the European Union
Document details	(a) Proposal for a Directive on establishing the European Electronic Communications Code (Recast); (b) Proposal for a Regulation establishing the Body of European Regulators for Electronic Communications
Legal base	(a) (b) Article 114 TFEU; ordinary legislative procedure; QMV
Department	Digital, Culture, Media and Sport
Document Numbers	(a) (38106), 12252/16 + ADDs 1–3, COM(16) 590; (b) (38107), 12257/16 + ADDs 1–4, COM(16) 591

Summary and Committee's conclusions

9.1 Trilogue negotiations have concluded with a provisional political agreement on two legislative proposals which would amend the existing EU regulatory framework for telecommunications and consolidate it in a single document referred to as the European Electronic Communications Code.

9.2 The Minister for Digital and the Creative Industries at the Department for Digital, Culture, Media and Sport (Margot James) wrote to the Committee on 16 July 2018 to provide the Committee with an update. [128]

9.3 The Minister informs the Committee that the principal change made in trilogues was the introduction of regulated price caps for intra-EU telephone calls. The EU has effectively committed to apply a similar regulatory regime to that which currently applies to mobile roaming charges to all intra-EU (international) calls. The Minister reported that the Council did not support the European Parliament's proposal to completely abolish surcharges for international calls within the EU, preferring "a more balanced version with low call and text charges" (16p/min and 5p/text). This is not a concern for the Government, which had previously informed the Committee that it recognised "that intra-EU calls can currently be expensive and do not accurately reflect the price of their provision, so consumers in the EEA, including the UK, might benefit from such a proposal".

9.4 In exchange for supporting this European Parliament initiative, the Minister reports that the Council's negotiators were able to extract significant concessions on a range of other issues on which the negotiators agreed. As a result, the provisional agreement "meets all of the Government's key negotiating lines".

128 Letter from the Minister of State at the Department for Digital, Culture, Media and Sport (Margot James) to the Chair of the European Scrutiny Committee (16 July 2018).

9.5 The Minister also provides an overview of the key provisions of the agreement:

- Universal service obligation (USO): Despite European Commission and European Parliament proposals to require Member States to fund USOs through the public purse only, the agreement preserves the existing provisions, which are consistent with the UK's domestic USO policy, which will be funded through an industry levy;

- Reverse-112: The text requires Member States to introduce a public warning system via the regular public communications network or via an app, which will allow EU citizens to be warned about potential hazards (man-made or natural) via their phones, so danger zones are more quickly evacuated or more effectively avoided, thereby reducing the chances of casualties. This system will have to be alerted within three and a half years. The UK is already looking to develop a national public alert system consistent with the provisions of the EECC;

- Retail price regulation: The UK successfully secured the reintroduction of regulatory controls on retail services—which the Commission had originally proposed to delete—effectively allowing Ofcom to maintain their existing power to directly intervene in retail markets, and to set prices when all other remedies have failed; and

- Body of European Regulators of Electronic Communications (BEREC): BEREC will not become an agency of the European Union or be able to make legally binding decisions which affect the Member States.

9.6 The Committee was concerned that the Minister's letter on other aspects of the provisional agreement was insufficiently detailed and wrote to the Minister on 12 September requesting a more detailed response.[129] The Minister responded to the Committee's request with a further letter on 9 October 2018.[130]

9.7 In her response, the Minister notes that the EECC provisions on end-user rights match current UK protections, meaning that levels of consumer protection in the UK will not be affected. The Minister adds that some of the provisions subject to full harmonisation provide flexibility for Member States to go beyond the provisions in order to provide higher levels of consumer protection, and that as full harmonisation of end-user rights is limited to matters explicitly covered in the EECC, Member States can continue to make national provisions relating to other consumer protections.

9.8 On regulation of over the top services (OTTs), the EECC has taken a 'service blind' approach to the regulation of over-the-top services. That means that there specific categories which determine which aspects of the EECC will apply to an OTT — the key being whether it is 'number-based' or 'number-independent'. If a service connects to the national numbering plan (i.e. an end-user is assigned a direct number as part of the service), it is number based. This was done to give the EECC fluidity, and to ensure that

129 This letter will be made available in due course on the following page of DEXEU's web-site: https://goo.gl/Mpes5e.

130 Letter from the Minister of State at DCMS (Margot James) to the Chair of the European Scrutiny Committee (9 October 2018).

the relevant provisions apply to the right service types. For instance, porting of numbers/switching and contract duration would not be relevant to number-independent services, but would be for number-based OTTs.

9.9 On this issue, the Minister states that "number-independent interpersonal communications services" (NIICS) are only in scope of the end-user rights, network security and interoperability provisions of the Code. The Minister reports that NIICS will only be subject to the same regulation as traditional telecoms services (e.g. mobile and landline calling and SMS) where they display the same relevant characteristics. Thus, if an NIICS provides consumers with a contract or offers minimum quality of service, the provisions that set out minimum standards of contract information or quality of service will apply. The network security provisions provide Ofcom with sufficient flexibility to decide on the extent to which NIICS should report on network security breaches, and Ofcom will only be able to impose obligations of interoperability on NIICS that meet a threshold of coverage and user uptake where end-to-end connectivity between end-users is endangered due to a lack of interoperability. The Minister indicates that the approach taken to NIICS is a "proportionate compromise".

9.10 On network access regulation the Minister states that the foundations of the system continue to be based on competition law centred on the concept of significant market power (SMP), and that, in this regard, there has been no significant change from the original proposal and the current Access Directive (2002/19/EC). The Minister states that the current suite of regulatory tools available to Ofcom to impose on operators with SMP remains intact, but with greater emphasis on requiring regulators to remove regulation that is no longer necessary and on encouraging investment in very high capacity networks through infrastructure competition. The Minister states that this approach "corresponds to UK policy objectives".

9.11 Regarding the regulatory incentive provision specific for co-investment in very high capacity networks, according to the Minister the provision now contains sufficient discretion for Ofcom to ensure that they are not forced to remove regulation from the dominant operator where this would be detrimental to competitive markets and consumers. If a proposed co-investment satisfies strict criteria, Ofcom will not be able to impose any additional obligations on the new fibre deployment; however, Ofcom will still be able to "maintain or adapt remedies… in order to address significant competition problems" if those problems cannot be addressed any other way.

9.12 On spectrum management—one of those aspects of the original proposal about which the Government was most concerned—the Minister confirms that majority of the new powers for the Commission to introduce implementing acts to restrict Member State flexibility over spectrum management have been removed and that only one new power remains in the final text, which allows the Commission to address cross border interference which may only be used following a request from a directly affected Member State. The Minister indicates that "we are satisfied that the Member State trigger sufficiently mitigates the risk of unnecessary encroachment on Member State competence".

9.13 In her letter of 16 July,[131] the Minister stated that the legal text was being finalised and that the Code was expected to be adopted and to enter the Official Journal in Autumn

131 Letter from the Minister of State at the Department for Digital, Culture, Media and Sport (Margot James) to the Chair of the European Scrutiny Committee (16 July 2018).

2018. The implementation deadline will be Autumn 2020, meaning that the UK will have to transpose the provisions into UK law during the transition period provided for in the draft Withdrawal Agreement (assuming it is concluded).

9.14 The Minister has also responded to a number of questions about EU exit in its last report on the Code.[132]

9.15 Asked how the level of access in telecommunications markets differs from that provided by the WTO General Agreement on Trade in Services (GATS) as compared to within the EU, the Minister stated that "The rules provided by the WTO should afford a similar level of EU market access for UK telecoms operators, but without requiring full alignment with EU telecoms law". The Minister cites Paragraph 5(a) of the GATS telecoms annex, which states that each Member shall ensure that any service supplier of any other Member is accorded access to and use of public telecoms networks and services, on reasonable and non-discriminatory terms, and notes that the current EU Framework is based on the same principles as GATS, which seeks to ensure liberalised access by any company that offers telecommunications services within any member (for example providing access to an incumbent's infrastructure).

9.16 Asked to what extent retaining current levels of access to the EU public-sector procurement market is important to BT and other telecoms companies, the Minister acknowledged that "public procurement contracts are important for global telecoms companies, and EU contracts generate annual revenue for UK telecoms companies" and that "It is therefore important for UK telecoms companies to retain the ability to compete and win future bids on a non-discriminatory basis."

9.17 On mobile roaming charges, which the Committee has reported on previously,[133] the Minister stated that "Two operators (Vodafone and Three) have committed publicly to continue surcharge-free roaming in the EU on UK exit", but also acknowledged that "roaming arrangements are inherently cross-border in nature, and are therefore subject to the sensitivities of the UK's negotiating position". The Guidance subsequently issued by the Government on mobile roaming in the event of a No Deal scenario[134] confirms that the Government cannot prevent EU operators from increasing wholesale roaming charges applied to UK operators, and acknowledges that "surcharge-free roaming when you travel to the EU could no longer be guaranteed". The Government's guidance states that it would retain various EU provisions related to roaming in domestic law post-exit, but it is clear that the Government does not intend to retain the ban on retail roaming charges in domestic law: "the availability and pricing of mobile roaming in the EU would be a commercial question for the mobile operators".

9.18 The Government also indicates in its No Deal notice that it intends to legislate to limit the total amount of mobile roaming surcharges to a maximum of £45 per monthly billing period "as at present" and to ensure that consumers receive alerts at 80% and 100% usage of any surcharge-free roaming data allowance their operators choose to offer them. It is important to note that the £45 limit monthly mobile roaming surcharge limit to

132 First Report HC 301–i (2017–19), chapter 11 (13 November 2017).
133 Fortieth Report HC 71–xxxvii (2016—17), chapter 22 (25 April 2017).
134 HM Government, Guidance: Mobile roaming if there's no Brexit deal (13 September 2018).

which the Government refers relates very specifically to mobile roaming surcharges which may be levied for a limited set of reasons, such as when a consumer's usage is defined as "anomalous" or "abusive" by the fair use policy. [135]

9.19 Asked whether EU telecoms rules would continue to function if retained or transposed into domestic law post-exit, the Minister stated that the EU regulatory framework for telecommunications is administered at national level and primarily consists of EU directives which are already implemented into UK law, that the EU framework also includes certain directly-applicable EU Regulations and Commission Decisions which the EU (Withdrawal) Act will convert into UK law, and, with the exception of the roaming rules, there are no functions which are directly carried out in the UK by an EU agency and few reciprocal arrangements between the UK and other EU member states. On this basis, the Minister concludes that "UK telecommunications law will therefore largely continue to function after EU-exit", and that any deficiencies which might arise from EU exit would be corrected through statutory instruments under the EU Withdrawal Act.

9.20 **We have taken note of the Minister's detailed summary of the technical agreement which has been reached following trilogue negotiations on the proposal for a Directive establishing the European Electronic Communication Code and the proposal for a Regulation establishing the BEREC, both of which are expected to be adopted by the Council of Ministers during the final months of the Austrian Presidency.**

9.21 **Whereas the Commission's original proposal sought to radically incentivise investment in next generation infrastructure, the Member States have considerably watered down the deregulatory provisions in the proposal and the revised Code to a large extent consolidates and retains the status quo.**

9.22 **The clearest benefit brought about by the proposed revision is the late-stage addition by the European Parliament of a proposal to introduce regulated price caps for international calls within the EU, which Council negotiators accepted in exchange for the rejection of a wide range of other proposed changes to which the Member States objected. The Government supports this reform on the basis that, much like roaming charges before them, "intra-EU calls can currently be expensive and do not accurately reflect the price of their provision, so consumers in the EEA, including the UK, might benefit from such a proposal**".

9.23 **The Minister states that the provisional agreement "meets all of the government's key negotiating lines". Elements of the original proposals to which the Government objected, including the expansion of the Commission's powers in relation to spectrum management, the removal of the industry funding option for the Universal Services Obligation, and the transformation of BEREC into an EU agency with significantly enhanced powers, have been removed. Furthermore, the regulatory approaches taken to network access, communications platforms, and end user rights are proportionate and afford Member States' national regulatory authorities greater discretion than in the Commission's original text.**

135 See House of Commons Library, The abolition of mobile roaming charges and Brexit, particularly sections 2.2. and Appendix 1, for further information.

9.24 **On this basis, the Minister seeks clearance of both documents, so that the Government can vote for them when they are adopted in the coming months—potentially at Transport, Telecommunications and Energy Council on 3 December 2018.**

9.25 **On EU exit, we note the Minister's assessment that the EU regulatory framework for telecommunications is administered at national level and primarily consists of EU directives which are already implemented into UK law, and that, with the exception of the roaming rules, there are no functions which are directly carried out in the UK by an EU agency and few reciprocal arrangements between the UK and other EU member states, and that "UK telecommunications law will therefore largely continue to function after EU-exit".**

9.26 **The Minister also states that, in terms of market access, the WTO General Agreement on Trade in Services (GATS) should afford "a similar level of EU market access for UK telecoms operators, but without requiring full alignment with EU telecoms law". However, we note that the Government's sectoral analysis of the implications of EU exit for telecommunications[136] notes that telecoms chapters of EU trade agreements go beyond GATS to deliver further incremental liberalisation, with the EU-Canada Comprehensive Economic and Trade Agreement (CETA) improving access to the EU market in a number of respects (regulatory transparency; safeguarding against anti-competitive practices; requirement for suppliers to have access to domestic dispute resolution procedures), and states that the EU's Association Agreements grant EU investors the same regulatory environment in the associated country as in the EU. We also note that the EU's GATS schedule of commitments on market access in telecommunications[137] specifies a number of limitations from MFN rules for certain EU Member States, including Finland, Portugal, Greece, Ireland and France.**

9.27 **More specific EU exit implications for UK telecommunications businesses and consumers include the following:**

- **The return of mobile roaming charges: Outside the EU, the roaming regulations—which have effectively abolished voice, SMS and data roaming charges for UK citizens when travelling within the EU will cease to apply, meaning that EU operators will be free to increase the wholesale roaming charges they charge UK operators, and UK operators will be free to start to charge UK consumers for using roaming services.[138] The EU's "Roam like at Home" regime will come to an end for UK consumers. As the Government does not seek participation in the Digital Single Market as part of the future economic partnership, this situation will arise in the event of both a negotiated and a non-negotiated exit.**

  The Government's No Deal guidance on mobile roaming charges[139] implies that it has made a policy decision not to legislate to prevent UK operators from imposing roaming surcharges on consumers, stating that "the availability

136 Department for Exiting the European Union, Sectoral Report—Telecommunications (21 December 2017).
137 WTO GATS/SC/31/Suppl.3, European Communities and Their Member States, Schedule of Specific Commitments, Supplement 3 (11 April 1997).
138 For background see: House of Commons Library, The abolition of mobile roaming charges and Brexit (6 July 2017).
139 HM Government, Guidance: Mobile roaming if there's no Brexit deal (13 September 2018).

and pricing of mobile roaming in the EU would be a commercial question for the mobile operators" and that "surcharge-free mobile roaming in the EU may not continue to be standard across every mobile phone package from that point". We infer that the Government's reluctance to transpose the EU ban on retail roaming charges (roaming charges applied to consumers) into domestic law is because it cannot use domestic law to retain the EU price caps on the wholesale roaming charges that EU operators can charge UK businesses for using their networks to provide roaming services due to the cross-border nature of the wholesale roaming market. Given that the EU price caps on wholesale roaming charges were specifically intended to make the abolition of roaming charges financially sustainable for operators, imposing a blanket ban on retail roaming charges in the absence of effective caps on wholesale prices would potentially be disruptive for some operators and have competition-distorting effects, with MVNOs and operators which are not part of a large European group and MVNOs being worst hit.

Although the Government's technical notice states that some mobile operators have already said that they have "no current plans" to change their approach to mobile roaming after the UK leaves the EU, this may not be sustainable in the long term if EU networks increase the wholesale roaming charges they apply to UK networks (and there may be an incentive for them to do so, as more UK consumers holiday in the EU27 than vice-versa, and UK consumers are more inclined to use large amounts of roaming data when abroad than their European counterparts). If this comes to pass, higher operating costs will either have to be absorbed by mobile operators or passed on to consumers in one form or another (for example, higher wholesale roaming charges could be passed on to consumers through higher overall prices, rather than through the reintroduction of roaming charges).

We therefore consider that, post-exit, consumers should consider the roaming policies of their mobile operators extremely carefully before signing new contracts or using roaming services, as (i) there will be potential for roaming charges much higher than those which preceded the EU's latest regulatory intervention to be applied, and (ii) there may be a return of confusing "roam like at home" commercial offerings where the cost of roaming is effectively priced in to a more expensive product, in contrast to the EU's "Roam like at Home" regime under which it is a legal requirement for all contracts to allow consumers to use their domestic mobile allowances throughout the EU without incurring surcharges.

- **Higher prices for international UK-EU calls: The intra-EU price caps which the EU has agreed to introduce for international calls (as distinct from the existing caps on roaming charges) will only apply to UK operators and consumers for as long as EU law applies directly to the UK (i.e. during the implementation period). In addition, the EU's regulatory framework which relates to wholesale voice termination rates (the charges paid between operators to deliver the calls to their customers) will no longer apply to calls between the EU and the United Kingdom. Given that most EU Member States**

apply higher termination rates to non-EU providers,[140] UK operators may incur higher wholesale costs for international calls, and pass these on to consumers.

- **Restricted access to the EU broadcasting market: Outside the EU, given the Government's stated desire not to participate in the Digital Single Market and the EU's exclusion of broadcasting from Free Trade Agreements, it is clear that UK-based international broadcasters will no longer be able to broadcast directly to the EU27 on the basis of the country-of-origin principle unless they relocate a proportion of their operation to the EU27, in line with the requirements of the Audio Visual Media and Services Directive (EU) 2010/13. This is a significant challenge for the sector, given the UK's current status as the destination of choice for international broadcasters in Europe.**

9.28 **We also note that two non-sectorial areas of policy of particular importance to UK telecommunications businesses which provide fixed services in EU Member States are:**

- **Procurement: The Minister acknowledges that "public procurement contracts are important for global telecoms companies, and EU contracts generate annual revenue for UK telecoms companies" and that "it is therefore important for UK telecoms companies to retain the ability to compete and win future bids on a non-discriminatory basis".**

- **Movement of natural persons: The provision of fixed telecommunications services in other countries requires the presence of skilled staff to install equipment and to provide ongoing service support. While the Government intends to leave the EU's regime for the free movement of persons, it will be important that UK businesses retain the ability to efficiently move employees throughout their European operations.**

9.29 **We now clear these documents from scrutiny.**

Full details of the documents:

(a) Proposal for a Directive on establishing the European Electronic Communications Code (Recast): (38106), 12252/16 + ADDs 1–3, COM(16) 590; (b) Proposal for a Regulation establishing the Body of European Regulators for Electronic Communications: (38107), 12257/16 + ADDs 1–4, COM(16) 591.

Previous Committee Reports

First Report HC 301–i (2017–19) chapter 11 (13 November 2017); Fortieth Report HC 71–xxxvii (2016–17), chapter 11 (25 April 2017); Twenty-second Report HC 71–xx (2016–17), chapter 2 (7 December 2016).

140 Clifford Chance, Brexit impact on the telecoms industry (27 April 2017).

10 Commission Report on progress made in preparing for the European Union Agency for Railways

Committee's assessment	Politically important
Committee's decision	(a) Cleared from scrutiny; further information requested (b) Cleared from scrutiny
Document details	(a) Report from the Commission on the progress made in preparing for the European Union Agency for Railways enhanced role under Directive (EU) 2016/797 on the interoperability of the rail system within the European Union (b) Recommendation for a Council Decision authorising the Commission to open negotiations with the Swiss Confederation to amend the Agreement between the European Community and the Swiss Confederation on the Carriage of Goods and Passengers by Rail and Road with a view to enabling the participation of the Swiss Confederation in the European Union Agency for Railways
Legal base	-
Department	Transport
Document Number	(a) (40078), 12246/18 + ADD 1, COM(18) 623; (b) (39249), 14507/17 + ADD 1, COM(17) 664

Summary and Committee's conclusions

10.1 The report under consideration outlines progress made in preparing for the EU Agency for Railway's strengthened role as per Article 53(1) of the Interoperability Directive. The Interoperability Directive is one of three legal acts comprising the 'technical pillar' of the 'Fourth Railway Package'.[141] As of 16 June 2019 (barring the possibility of time-limited extensions), the EU Agency for Railways (the EU Railways Agency) will become the EU authority responsible for issuing authorisations for placing railway vehicles on the market and for issuing single safety certificates for railway undertakings.[142] This is an extension of the Agency's current role in providing Member States with advice and technical assistance.

10.2 By way of background, the Fourth Railway Package is a set of six legislative acts designed to complete the single market for rail services (also known as the 'Single European Railway Area'). The overarching goal of the Fourth Railway Package is to revitalise the rail sector and make it more competitive *vis-à-vis* other modes of transport. The technical pillar of the package is complemented by the 'market pillar'. The market

141 The other are the 'Agency' Regulation (on the enhanced role of the EU Railways Agency) and the 'Safety' Directive.

142 The Agency will also be responsible for the implementation of the European Railway Traffic Management System (ERTMS) (including the approval of ERTMS trackside projects).

pillar—due to enter into force on 1 January 2019—will complete the process of the gradual market opening of Europe's railways started with the First Railway Package. The market pillar will:

- Establish the general right of every railway undertaking established in one Member State to operate passenger services in another Member State;
- Set rules aimed at improving the impartiality of the governance of railway infrastructure and the prevention of commercial discrimination; and
- Introduce the principle of mandatory tendering for public service contracts.

10.3 In concert with the market pillar, the technical pillar is designed to boost the competitiveness of the railway sector by significantly reducing costs and administrative burden for railway undertakings wishing to operate across Europe. As alluded to above, the technical pillar will:

- Charge the EU Railways Agency with issuing vehicle authorisations and safety certificates;
- Create a 'one-stop-shop' for authorisation and safety certificate applications;
- Ensure ERTMS equipment is interoperable; and
- Reduce the large number of remaining national rules (including on rail subs-system interoperability).

10.4 The Commission's Report focusses on progress made in preparing for the EU Railways Agency's enhanced role, specifically, the transposition of relevant law by Member States, the development of delegated and implementing acts, the 'cleaning-up' of national rules, the development of the Agency's preparedness, and progress made on cooperation agreements between the Agency and National Safety Agencies.

10.5 Of these areas of focus, the state of play with regards to the development of delegated and implementing acts is worthy of specific mention. The technical pillar requires the Commission to adopt considerable numbers of delegated and implementing acts in pursuit of fleshing-out the legislative framework set by the Fourth Railway Package. Revisions to existing 'Technical Specifications for Interoperability' (TSIs) are foreseen, alongside decisions on setting out the specifications for a European vehicle register and register of infrastructure.

10.6 Technical Specifications for Interoperability are common, harmonised, standards defining how rail components must be built and compliance assessed and verified to ensure rail system interoperability (in this case, that of the Single European Railway Area). They set specific requirements relating to, for example, either 'structural' sub-systems such as infrastructure, rolling stock, energy and control/command and signalling or 'functional' sub-systems such as maintenance, traffic operation and management, and telematic applications for passengers and freight services.

10.7 Technical Specifications are developed by the EU Railways Agency in collaboration with Member States and industry experts. Currently, in the UK, the Office of Rail and Road (ORR) is responsible for issuing technical authorisations in order for rolling stock

and infrastructure to be placed on the market. The authorisation process also covers certain interoperability constituents (held in TSIs). As of the entry into force of the Fourth Railway Package, vehicles—and covered sub-system elements—intended for cross-border use will have to be authorised by the EU Railways Agency. For vehicles intended for use on networks limited to one Member State, undertakings will be able to seek authorisations from either the EU Agency or a relevant national authority.

10.8 A similar system is to be instituted for the issuance of safety certificates. Access to railway infrastructure is granted only to railway undertakings that hold a valid single safety certificate. In the case of rail operations in more than one Member State, the EU Railways Agency will be the competent issuing authority. For operations restricted to one Member State, undertakings may apply either the EU Railways Agency or the relevant national safety authority.

10.9 The issuance of authorisations and safety certificates is the subject of a recent Commission 'notice to stakeholders' on 'the withdrawal of the United Kingdom and EU rules in the field of rail transport'. The notice advises stakeholders that after the UK's withdrawal from the EU, authorisations relating to interoperability constituents and vehicles, vehicle types and sub-systems, will be valid until their expiration, however, after this date, renewal —or new approval—will have to be sought through designated bodies in the EU27 (or, where applicable under the new regime, the EU Railways Agency). As for safety certificates, upon UK withdrawal, all UK-issued certificates will become invalid and, as such, undertakings wishing to continue operations will have to seek new certification from a relevant agency in the EU27 (or again, where covered by the new regime, the EU Railways Agency).

10.10 The establishing Regulation of the EU Railways Agency provides for 'participation by third countries in the work of the Agency' (Article 75). Such participation is to be undertaken on the basis of an agreement. Under the Regulation, third countries are not to be granted the right to vote on matters heard before the Agency's Management Board, however, participation in working groups—such as those relating to the setting of TSIs and the authorisation process—is foreseen. In chapter 4 of our Ninth Report of Session 2017–19, we considered Swiss participation in the EU Railways Agency.

10.11 In an article published on 5 October 2018, the Railway Gazette cited the Rail Safety & Standards Board (RSSB) as suggesting that it wanted UK technical standards on interoperability and common safety standards to be closely aligned with those of the EU after withdrawal.[143] Furthermore, the RSSB is quoted as saying that it anticipates a 'pragmatic' solution will be proposed for recognising certification in the EU, in particular, where UK and EU standards remain aligned.[144]

10.12 On the remainder of the report, the Commission details the steps it is taking in preparation for the transition of the EU Railways Agency from a purely advisory body to a revenue-generating authorising/certifying agency. This task is said to be complicated by uncertainty surrounding the number of Member States that will transpose the Fourth Railway Package by the 16 June 2019 deadline or, as provided for by the Agency Regulation, request a 12-month extension of the transposition period.

143 Railway Gazette, "UK to retain EU rail standards following Brexit" (5 October 2018) pp 1.
144 ibid.

10.13 In her Explanatory Memorandum of 1 October 2018, Parliamentary Under Secretary of State at the Department of Transport, Baroness Sugg, welcomes the Commission's report as "providing a helpful update on the EU Railways Agency's [preparations] for assuming its expanded responsibilities".

10.14 The Minister states that the UK's plans for transposition of the Interoperability Directive are based upon "meeting a deadline of 16 June 2020 in the event of an Implementation Period". Furthermore, the Minster also proffers that the ORR have been engaging with the EU Railways Agency on a cooperation agreement and that the "Government expects that this should be in place in readiness for transposition".

10.15 **We thank the Minster for her Explanatory Memorandum and—as the Commission's report does not raise any question of significant legal or political importance—clear it from scrutiny. This having been said, we request further information on a number of issues related to the Government's plans for cooperation with the EU Railways Agency after the UK's withdrawal from the EU. We request this information by the end of November 2018.**

10.16 **We note our Report of 16 January 2018, in particular, chapter 4 on Swiss participation in the EU Railways Agency[145] and our questions concerning the Government's plans for UK participation in the Agency after EU exit, in which the Minister indicated that there were diverse views among stakeholders both with regard to continuing to apply EU rules for standards and safety for rail, "with some suggesting that there are benefits to be gained from continuing to apply EU rules for standards and safety for rail, while others have highlighted the need for future flexibility", while the views on the UK's participation in the EU Railways Agency were "equally varied".[146] As the Council Decision recommending Swiss participation in the Agency has now been taken, we now clear this document from scrutiny.**

10.17 **In light of the Minister's statement that the ORR is in discussions with the EU Railways Agency on a potential cooperation agreement, we seek information on:**

- **Whether such an agreement would cover Technical Specifications for Interoperability and, if it would, whether the ORR would have a role in influencing their form;**
- **Whether the validity of UK-issued safety certificates after withdrawal has been discussed and, more specifically, whether the Government has—or seeks to— reach an arrangement whereby UK authorities will be able to issue safety certificates after EU exit; and**
- **Whether the ability for UK authorities to issue vehicle, vehicle type and sub-system authorisations has been discussed and, if so, the content of these discussions.**

10.18 **In her Explanatory Memorandum, the Minister states that the Government intends on meeting "a deadline of 16 June 2020 [for the Interoperability Directive] in the event of an Implementation Period". We would like to clarify that for the purposes**

145 Ninth Report HC 301–ix (2017—19), chapter 4 (10 January 2018).

146 Letter from the Secretary of State at the Department for Transport (Chris Grayling MP) to the Chair of the European Scrutiny Committee (22 February 2018).

of Article 57 of the Interoperability Directive this 'deadline'—of 16 June 2020—is to be issued at the discretion of the Commission and that Member States must inform the Commission by 16 December 2018 of their intention to seek such an extension. As such, we request clarification as to whether the Government has sought—or is planning to seek—an extension.

Full details of the documents:

Report from the Commission on the progress made in preparing for the European Union Agency for Railways enhanced role under Directive (EU) 2016/797 on the interoperability of the rail system within the European Union: (40078), 12246/18 COM(2018) 62; Recommendation for a Council Decision authorising the Commission to open negotiations with the Swiss Confederation to amend the Agreement between the European Community and the Swiss Confederation on the Carriage of Goods and Passengers by Rail and Road with a view to enabling the participation of the Swiss Confederation in the European Union Agency for Railways: (39249), 14507/17, COM(17) 664.

Previous Committee Reports

Ninth Report HC 301–ix (2017—19), chapter 4 (10 January 2018).

11 EU sanctions regime for chemical attacks

Committee's assessment	Politically important
Committee's decision	Cleared from scrutiny; drawn to the attention of the Defence, Foreign Affairs and International Development Committees
Document details	(a) Council Decision concerning restrictive measures against the proliferation and use of chemical weapons; (b) Council Regulation concerning restrictive measures against the proliferation and use of chemical weapons
Legal base	(a) Article 29 TEU; unanimity; (b) Article 215 TFEU; QMV
Department	Foreign and Commonwealth Office
Document Number	(a) (40097), 11936/18; (b) (40098), 11938/18

Summary and Committee's conclusions

11.1 On 28 June 2018, the European Council—the meeting of the EU's Heads of State and Government—called for "a new EU regime of restrictive measures to address the use and proliferation of chemical weapons" to be adopted "as soon as possible". Its request came in response to a number of recent chemical attacks, including the assassination of North Korea's Kim Jong-nam in Malaysia in February 2017; repeated use of chemical weapons in Syria, most recently in the city of Douma in April 2018; and, of course, the Russian Novichok nerve agent attack in Salisbury in March this year. The UK has been reported as one of the driving forces behind the European Council's call for action.[147]

11.2 In response to the European Council's conclusions, the European External Action Service (EEAS)—responsible for formally proposing EU foreign policy measures for consideration by the Member States in the Council—circulated the finalised draft legal acts to establish a new EU-wide sanctions framework on 25 September 2018.[148] These would, once invoked against specific people or entities, require EU Member States to impose "asset freezes and travel bans […] to those involved in or responsible for the use and proliferation of chemical weapons". The new framework would complement the existing EU sanctions under the Common Foreign & Security Policy (CFSP) that already apply against countries including Russia, Syria and North Korea, but allow people to be sanctioned regardless of their nationality (the sole criterion being that those listed must be involved in some manner in the use of chemical weapons).[149]

147 Reuters, "EU to agree new sanctions regime for chemical attacks" (24 September 2018).

148 The documents remain classified as LIMITE until their publication in the Official Journal and are therefore not publicly accessible at the time of consideration by the Committee.

149 The legal acts are aimed at natural and legal persons "who are responsible for, provide financial, technical or material support for or are otherwise involved in: manufacturing, acquiring, possessing, developing, transporting, stockpiling or transferring chemical weapons; using chemical weapons; [or] engaging in any preparations for the use of chemical weapons".

11.3 The new framework does not currently list any specific persons or entities:[150] article 4 of the draft Council Decision provides that the Member States "acting by unanimity" upon a proposal from a Member State or from the [EU] High Representative [Federica Mogherini], shall establish and amend the list. Any proposals to make such changes would be subject to parliamentary scrutiny via this Committee in the usual way. Those listed will be able to challenge the sanctions applied to them before the General Court of the European Union.

11.4 The new legal framework will remain in force for 12 months, until October 2019, after which it would need to be extended by a further unanimous Decision of the remaining Member States (the UK being due to withdraw as a Member State in March 2019). If it is not extended, any sanctions applied under it would expire automatically.

11.5 The Minister for Europe (Sir Alan Duncan) submitted the EEAS proposals and an Explanatory Memorandum[151] for scrutiny on 11 October 2018, ahead of their scheduled formal adoption by EU Foreign Affairs Ministers in Luxembourg on 15 October.[152] In the Memorandum, he expresses the UK's strong support for the EEAS proposal as an "important signal of the UK's and its EU partners' continued commitment to upholding global norms, supporting the existing international architecture (particularly the effective implementation of the Chemical Weapons Convention), and deterring the use and proliferation of chemical weapons".

11.6 The Minister also states that it is the UK's intention to "continue to press" for all the measures agreed so far to be fully implemented, presumably referring to the inclusion of specific people—for example the perpetrators of the Salisbury attack — in the list of subjects of the new sanctions regime. We understand it is not yet known when the first listings are likely to take place. The Government is also pushing the EU to implement similar horizontal sanctions frameworks to target the perpetrators of human rights abuses and cyber-attacks.

Our assessment

11.7 **The Foreign Affairs Council adopted the legal acts establishing the new EU sanctions framework targeting perpetrators of chemical attacks on 15 October 2018. The Government overrode the scrutiny reserve to propose their adoption, given the short amount of time available between the proposal's formal circulation and adoption by the Council. In light of the UK's interest in pursuing coordinated European action, following the Novichok attack that occurred on UK soil, we understand the Government's reasons for voting in support of the new sanctions framework in spite of the scrutiny reserve.**

11.8 **In the absence of any initial listing of specific persons or entities, it is difficult to judge the likely effectiveness of the new regime. It appears to have been established**

150 This is a common practice with the imposition for EU sanctions: often the legal framework setting out the criteria for, and consequences of, being listed are adopted, and those actually subject to the sanctions are added by the Member States at a later stage. See for example our recent Report on the EU's sanctions vis-à-vis certain Venezuelan officials.

151 Explanatory Memorandum submitted by the Foreign & Commonwealth Office (4 October 2018). Not yet available online.

152 Although the Committee was made aware of the proposal on 4 October 2018, the Explanatory Memorandum was not submitted until 11 October.

to avoid the appearance of directly attacking foreign governments—in particularly Russia—by applying the new regime to those seen as responsible for specific actions (use of chemical weapons) irrespective of their nationality, political affiliation or the location of their transgressions. However, as the effect of listing persons or entities is the same as if they had been listed under a country-specific regime, and the Member States must still unanimously agree to the inclusion of new people and organisations as subject of the sanctions,[153] the listing process is likely to remain politically charged.[154]

11.9 **There is, of course, also a wider Brexit context. When the UK leaves the EU on 29 March next year, it will also cease to be bound by the Common Foreign & Security Policy of which this new sanctions regime forms part. Naturally, the Government will also lose its current veto over most new EU foreign policy measures and its current (significant) degree of influence over the general direction of the CFSP.**

11.10 **While both the UK and the EU have expressed a desire for a close security partnership after Brexit, the legal and institutional practicalities of that new relationship are yet to be established. The EU would benefit from a close relationship with the UK in the field of foreign policy, especially in the field of sanctions: as the House of Lords EU Committee noted in December last year, the UK "currently plays a leading role in developing EU sanctions policy, is most active in proposing individuals and entities to be listed, and is home to the largest international financial centre of the bloc"[155] (making asset freezes more effective when they include London). However, the UK cannot expect to be involved in the EU's decision-making structures for the CFSP in the same way as Member States. In the event of a 'no deal' Brexit, day-to-day foreign policy cooperation—coordinated, for example, via the weekly meeting of the EU's Political & Security Committee—would be severely disrupted in March 2019.**

11.11 **The UK will be able to impose sanctions unilaterally more easily once outside the Common Foreign & Security Policy: the Sanctions and Anti-Money Laundering Act 2018[156] gives the Government the necessary powers to implement an independent sanctions policy from EU 'exit day'.[157] However, the UK's undoubted capacities in this field notwithstanding, it is likely to find it more difficult to coordinate concerted EU-wide restrictive measures once outside of the Union's political structures. If the UK imposes foreign policy sanctions that the EU-27 do not, this is likely to reduce their overall effectiveness. The House of Lords' European Union Committee concluded in December 2017 that "while informal engagement with the EU on sanctions […] can be very valuable, it is no substitute for the influence that can be exercised through formal inclusion in EU meetings".[158]**

153 The European Commission recently suggested the European Council should take a decision under a so-called "passerelle" clause in the Treaty to allow EU sanctions regimes to be adopted and amended by Qualified Majority. We are awaiting an Explanatory Memorandum from the Foreign Office on this Commission document, and plan to make a Report to the House in due course.

154 For example, it was reported in September 2018 that the new Italian Government had blocked the addition of a new name to the EU's sanctions regime targeting those responsible for Russia's annexation of Crimea in Ukraine.

155 House of Lords External Affairs EU Sub-Committee, "Brexit: sanctions policy" (12 December 2017).

156 http://www.legislation.gov.uk/ukpga/2018/13/contents/enacted.

157 'Exit day' is either 29 March 2019 or the end of any subsequent post-Brexit transitional period, should the Withdrawal Agreement be ratified.

158 House of Lords EU Committee, "Brexit: sanctions policy" (December 2017).

11.12 **The Committee will continue to monitor the discussions on the UK's future relationship with the EU closely, including any new institutional architecture and the implications for the autonomy of UK foreign policy after Brexit. It will also consider any formal proposals for listings under the new chemical attacks sanctions framework, or for parallel sanctions regimes for human rights abuses or cyber-attacks, in due course.**

11.13 **We draw these developments to the attention of the Defence, Foreign Affairs and International Development Committees.**

Full details of the documents:

(a) Council Decision concerning restrictive measures against the proliferation and use of chemical weapons: (40097), 11936/18; (b) Council Regulation concerning restrictive measures against the proliferation and use of chemical weapons: (40098), 11938/18.

Previous Committee Reports

None, this is a new sanctions framework.

Documents not raising questions of sufficient legal or political importance to warrant a substantive report to the House

Department for Business, Energy and Industrial Strategy

Other

(36687) 6594/15 + ADD 1 COM(15) 80	Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee, the Committee of the Regions and the European Investment Bank: A Framework Strategy for a Resilient Energy Union with a Forward-Looking Climate Change Policy.
(36688) 6595/15 + ADD 1 COM(15) 82	Communication from the Commission to the European Parliament and the Council on achieving the 10% electricity interconnection target — Making Europe's electricity grid fit for 2020.
(39940) 10582/18 +ADD 1 COM(18) 482	Report from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions Report on Competition Policy 2017.

Department for Digital, Culture, Media and Sport

(40065) 11911/18 COM(18) 612	Report from the Commission on the evaluation of Europeana and the way forward

Department for Environment, Food and Rural Affairs

(40083) 12306/18 +ADD 1 COM(18) 627	Report from the Commission to the European Parliament and the Council On the overall operation of official controls performed in Member States (2014–2016) to ensure the verification of compliance with food and feed law, animal health and welfare rules.

(40092)
12500/18
+ADD 1–15
COM(18) 656

Report from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions on the implementation of EU waste legislation, including the early warning report for Member States at risk of missing the 2020 preparation for reuse/ recycling target on municipal waste.

Department for International Development

(39980)
10988/18
+ ADD 1
COM(18) 496

Report from the Commission to the European Parliament and he Council on the Interim Evaluation of the EU Aid Volunteers initiative for the period mid-2014 to mid-2017.

(40076)
12190/18
+ ADD 1
COM(18) 641

Communication from the Commission A Europe that protects: an initiative to extend the competences of the European Public Prosecutor's Office to cross-border terrorist crimes A contribution from the European Commission to the Leader's meeting in Salzburg on 19–20 September 2018.

Department for International Trade

(39707)
8684/18
COM(18) 262

Annual Review by the Commission of Member States' Annual Activity Reports on Export Credits in the sense of Regulation (EU) No 1233/2011.

(39729)
9116/18
COM(18) 305

Annual Review by the Commission of Member States' Annual Activity Reports on Export Credits in the sense of Regulation (EU) No 1233/2011.

(40009)
11512/18
+ ADD 1
COM(18) 561

Report from the Commission to the European Parliament and the Council 36th Annual Report from the Commission to the Council and the European Parliament on the EU's Anti-Dumping, AntiSubsidy and Safeguard activities (2017).

Department for Transport

(40099)
12727/18
+ ADD 1
COM(18) 664

Proposal for a Council Decision on the position to be taken on behalf of the European Union in the Group of Experts on the European Agreement concerning the work of crews of vehicles engaged in international road transport of the United Nations Economic Commission for Europe.

Foreign and Commonwealth Office

(40017)	Council Decision amending Decision 2010/573/CFSP concerning restrictive measures against the leadership of the Transnistrian region of the Republic of Moldova
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(40105)	Proposal of the High Representative of the Union for Foreign Affairs and Security Policy to the Council for a Council Decision amending and extending Decision 2010/96/CFSP on a European Union military mission to contribute to the training of Somali security forces.
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HM Treasury

(40046)	Report from the Commission to the European Parliament and the Council: 29th Annual Report on the Protection of the European Union's financial interests—Fight against fraud—2017.
117/18	
+ADD 1–7	
COM(18) 553	

Home Office

(40050)	Proposal for a Council Decision on the conclusion of the status agreement between the European Union and the former Yugoslav Republic of Macedonia on actions carried out by the European Border and Coast Guard Agency in the former Yugoslav Republic of Macedonia.
11913/18	
+ ADD 1	
COM(18) 611	
(40051)	Proposal for a Council Decision on the conclusion of the status agreement between the European Union and the former Yugoslav Republic of Macedonia on actions carried out by the European Border and Coast Guard Agency in the former Yugoslav Republic of Macedonia.
11909/18	
+ ADD 1	
COM(18) 610	
(40081)	Proposal for a Council Decision on the position to be taken on behalf of the European Union in the United Nations Economic Commission for Europe Working Party on customs questions affecting transport and in the Inland Transport Committee in connection with the envisaged adoption of a new Convention on the facilitation of border crossing procedures for passengers, luggage and load-luggage carried in international traffic by rail.
11877/18	
COM(18) 605	

Formal Minutes

Wednesday 24 October 2018

Members present:

Sir William Cash, in the Chair

Martyn Day	Mr David Jones
Richard Drax	Andrew Lewer
Marcus Fysh	Michael Tomlinson
Kelvin Hopkins	

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 12 read and agreed to.

Summary agreed to.

Resolved, That the Report be the Forty-first Report of the Committee to the House.

Ordered, That the Chair make the Report to the House.

[Adjourned till Wednesday 31 October at 1.45pm

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)

Geraint Davies MP (*Labour/Cooperative, Swansea West*)

Martyn Day MP (*Scottish National Party, Linlithgow and East Falkirk*)

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*)