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Documents considered by the Committee on 25 April 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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Contents

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:

Emergency oil stocks

- Arrangements for emergency oil stocks post-Brexit.

Pet travel scheme

- Pet travel post-Brexit.

EU chemical policy review

- Associate membership of the European Chemicals Agency.

EU plastics strategy

- EU plastics policy.

State of paediatrics medicines in the EU

- Paediatric medicines development.

Adoption of detailed EU fishing rules

- Development arrangements for involvement of the UK in the preparation of detailed EU fisheries rules during the implementation period.

Animal welfare standards and international competitiveness

- International competitiveness and high animal welfare standards post-Brexit.

State of paediatric medicine in the EU competitiveness

- Paediatric medicines development.

Crowdfunding Regulation

- A new EU proposal to regulate crowdfunding would allow crowdfunding and P2P platforms to avoid national regulation by applying for a licence to operate across the European Union from the European Securities & Markets Authority (ESMA). As the UK is home to 80 per cent of the EU's crowdfunding market, it could have a disproportionate impact here if the new legislation had to be implemented into British law during the post-Brexit transitional period or under the terms of any new UK-EU free trade agreement.

Covered Bonds

- A new EU regulatory framework for covered bonds, a special type of asset-backed security, seeks to harmonise rules for issuance of such bonds as a way of creating a larger market and deepening the EU's capital markets. The UK may have to apply the new legislation for its £100 billion covered bond market if the new rules become applicable during the post-Brexit transitional period.

Summary

Emergency oil stocks

A ministerial response to various issues raised by Committee regarding the impact of Brexit on the UK's emergency oil stocks states that the EU oil stocking Directive adds value to the international framework, but notes that future options for engagement with EU policy in this area are subject to negotiations on the economic partnership agreement between the EU and the UK. The Committee releases the document from scrutiny, while signalling our continued interest in the issues raised.

Cleared; drawn to the attention of the Business, Energy and Industrial Strategy and the Exiting the EU Committees.

Pet travel scheme—tackling puppy smuggling

The Commission's Report proposes no change to the EU pet travel scheme Regulations, but does call for better enforcement of the derogation limiting the number of pets that may travel during a single trip. The Government is disappointed that the Commission has not chosen to act to address the illegal puppy trade. In response, the Government will continue to press for change and will give consideration to options for the UK's pet travel policy post-Brexit. Noting that the Environment, Food and Rural Affairs Committee recommended in its report on "Animal welfare in England: domestic pets" in November 2016 that the issue should be included within the Brexit negotiations, we raise the same questions in our report. The Committee also seeks information on the practicalities of a change of approach post-Brexit.

Not cleared; further information requested; drawn to the attention of the Environment, Food and Rural Affairs Committee.

EU chemicals policy review

The Commission concludes that the REACH (Registration, Evaluation, Authorisation and Restriction of Chemicals) Regulation is effective but there are opportunities for further improvement, simplification and burden reduction. The Committee expresses surprise that the Government did not reference the Prime Minister's intention to seek associate membership of the European Chemicals Agency (ECHA) post-Brexit and asks whether: it is safe to assume that the UK would apply relevant EU legislation if it was successful in negotiating associate membership; and, if so, whether that would extend beyond REACH to include the other Regulations covered by the ECHA (i.e. Biocidal Products Regulation, the Classification, Labelling and Packaging Regulation and the Prior Informed Consent Regulation).

Not cleared; further information requested; drawn to the attention of the Environmental Audit Committee.

EU Plastics strategy

In her original EM on this document, the Minister did not acknowledge potential ongoing implications for the UK of EU plastics policy. In reality, the Committee observes, it seems from the Minister's latest letter that the UK has been engaging closely and intends to continue doing so.

Cleared from scrutiny; drawn to the attention of the Environmental Audit Committee and the Environment, Food and Rural Affairs Committee.

State of Paediatric Medicines in the EU

Following a request by the Committee, the Government has committed to a discrete piece of analysis on paediatric medicines development in the UK in the specific context of the UK's withdrawal from the EU. The Committee welcomes the Minister's commitment and emphasises the desirability of including clinical trials within the Government's analysis. Continued cooperation on clinical trials, including the ability to share and access data through mechanisms such as the European clinical trial database (EudraCT), is crucial to the ability of UK paediatricians to engage in research on rare congenital diseases in particular. The Committee also notes the relevance of the Prime Minister's recent commitment to seeking associate membership of the European Medicines Agency post-Brexit.

Cleared; drawn to the attention of the Health and Social Care Committee.

Crowdfunding Regulation

The European Commission has proposed a dedicated regulatory regime for crowdfunding for the first time, which would allow platforms to apply for a pan-EU 'passport' to operate in any Member State based on a centralised licensing process by the European Securities & Markets Authority (ESMA). For example, a Spanish-based peer-to-peer lending platform that obtains a crowdfunding licence from ESMA would be able to provide its services to UK-based investors without the ability for the Financial Conduct Authority to prevent it from operating if there were concerns about investor protection.

The Committee shares the Government's concerns that the proposal could undermine the safety net provided by domestic regulatory regimes in individual Member States by allowing platforms to by-pass national supervisory processes. It has therefore retained the proposal under scrutiny. We have also asked the Government, again, for more information about the details of its proposed UK-EU financial services agreement, and whether it might in practice lead to the UK following EU financial services law to maintain preferential market access after it leaves the Single Market.

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

Covered Bonds

In March 2018 the European Commission proposed a new EU-level regulatory framework for covered bonds, a type of debt obligation issued by banks that offers bondholders extra security in case the issuer goes insolvent. Covered bonds are seen as very safe investments, because they are secured against a ring-fenced pool of high-quality, low-risk assets (typically residential mortgages), which holders can access directly as preferred creditors if the issuer of the bond cannot make their contractual payments. The UK market is estimated to amount to €121 billion (£100 billion) of outstanding covered bonds.

To increase their uptake in- and outside of the Single Market under a harmonised regulatory framework, the European Commission has now proposed a Directive for the issuance of all covered bonds. It has also proposed new rules on prudential reliefs for banks that purchase such bonds issued within the EU, allowing them to hold less regulatory capital because these investments are seen as very safe.

The Committee has taken note of the proposal, and summarised the implications for the UK financial services industry after it leaves the Single Market. In particular, UK-issued covered bonds would not trigger the same prudential reliefs because they would be considered 'third country' products. The Directive proposed does not contain an 'equivalence' regime, but the Committee will keep this under review as the negotiations progress. We have also asked the Government to publish a more detailed proposal for its desired UK-EU financial services agreement after Brexit, which would be based on cross-border market access and regulatory cooperation but without the need for the UK to directly apply EU law.

Not cleared from scrutiny; drawn to the attention of the Treasury Committee.

European Labour Authority

A new proposal for a European Labour Authority (ELA) is due to become operational in 2019. We conclude that the role of the Authority as proposed would largely be of a coordinating and supporting nature, by issuing guidance on employment rights and resolving disputes between Member States on free movement of labour within the Single Market.

Although the ELA would not have any enforcement powers against Member States or businesses, the Committee has retained the proposal under scrutiny in case the European

Parliament seeks to expand the powers of the new Authority. The Government has said the ELA and the relevant UK authorities are likely to have to cooperate during the post-Brexit transitional period, and possibly beyond.

Not cleared from scrutiny; further information requested.

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: Emergency oil stocks [Staff Working Document (C)]; EU chemicals policy review [Commission Communication (NC)]

Exiting the European Union Committee: Emergency oil stocks [Staff Working Document (C)]

Environment, Food and Rural Affairs Committee: EU Pet Travel Scheme [Commission Report (NC)]; EU Plastics strategy [Commission Communication (C)]

Environmental Audit Committee: EU chemicals policy review [Commission Communication (NC)]; EU Plastics strategy [Commission Communication (C)]

Health and Social Care Committee: State of Paediatrics Medicines in the EU [Commission Report (C)]

Home Affairs Committee: EU approval of the Global Compact on Migration [Proposed Decisions (NC)]

International Development Committee: EU approval of the Global Compact on Migration [Proposed Decisions (NC)]

Political and Constitutional Affairs Committee: The EU Civil Protection Mechanism: strengthening EU disaster management [Proposed Decision (NC)]

Treasury Committee: Regulation of covered bonds [Proposed Directive (NC), Proposed Regulation (NC)]; Crowdfunding and P2P lending: new EU regulatory framework [Proposed Regulation (NC), Proposed Directive (C)]

1 European Labour Authority

Committee's assessment	Politically important
Committee's decision	Not cleared from scrutiny; further information requested
Document details	Proposal for a Regulation establishing a European Labour Authority
Legal base	Articles 46, 48, 53(1), 62 and 91(1) TFEU; ordinary legislative procedure; QMV
Department	Business, Energy and Industrial Strategy
Document Number	(39563), 7203/18 + ADDs 1–3, COM(18) 131

Summary and Committee's conclusions

1.1 Against a backdrop of increased levels of worker mobility within the EU, the European Commission has taken note of concerns about the potential negative impact of free movement of workers where existing EU rules to avoid 'social dumping'—for example in relation to tackling undeclared work, posted workers and coordination of unemployment benefits—are not adequately enforced. As part of the new 'European Pillar of Social Rights',[1] the European Commission has now proposed the creation of a new European Labour Authority (ELA) that would reinforce "effective cooperation between national authorities and for concerted administrative action to manage the increasingly European labour market".

1.2 Despite its name, the Authority would have no regulatory or enforcement powers (either vis-à-vis Member State governments or individual businesses). Instead, it would play a supporting and coordinating role by:

- facilitating access for individuals and employers to information on their rights and obligations as well as to relevant national services;
- supporting cooperation between EU countries in the cross-border enforcement of EU employment and social legislation affecting the free movement of labour, including facilitating joint inspections of business sites. As part of this, the ELA would subsume various existing technical advisory bodies that already exist at EU-level to promote fair labour mobility; and
- providing mediation and facilitating solutions in cases of cross-border disputes between national authorities or labour market disruptions, in particular the system for conciliation between Member States where there is a dispute about which country is responsible for payment of a benefit to an EU citizen which has exercised their freedom of movement.

1 See our Report of 29 November 2017 for more information on the Pillar of Social Rights and the Government's position on it.

1.3 The ELA would have running costs estimated to run to 52 million euros (£45 million)[2] annually once fully operational,[3] with 140 staff split almost evenly between fulltime officials and experts seconded by Member States.

1.4 The Minister of State for Small Business, Consumers and Corporate Responsibility (Andrew Griffiths) submitted an Explanatory Memorandum on the proposal to establish the ELA on 5 April 2018.[4] The Memorandum outlines the Government's view that—despite Brexit—the UK is likely to have a working relationship with the ELA as foreseen for the remaining Member States during the post-Brexit transitional period, when EU law will continue to apply. It adds that Regulation as drafted "does not impose new obligations on Member States, individuals or employers nor does it impinge on national decision making, legislation, enforcement activities which remain in the competence of Member States". It will, however, place a few "minor obligations" on the Government, for example if an enforcement authority[5] declines to participate in a joint inspection with authorities from other Member States (in which case it must provide the ELA with written reasons for its refusal). During the transitional period, the UK will not have any institutional representation at EU-level, meaning in this instance the Government will not have a seat or vote on the Management Board of the Authority, which will set its budget and appoint its Executive Director.

1.5 After the UK's exit from the Single Market, the Minister adds, "our role and relationship [with the Authority] in the long term will depend on the arrangements agreed with the UK and the EU for the future economic partnership". A regulatory checklist prepared by his Department on the proposal also identified a number of benefits from continued UK participation in the Authority's work after Brexit, including access to analytical work on "patterns of mobility", mutual learning opportunities, use of conciliation facilities in the case of disputes, and technical support.[6] He notes that this would require a financial contribution by the Government, which presents an "opportunity-cost to the UK contributing to the ELA budget, in terms of greater participation and opportunity to influence".

1.6 **We thank the Minister for his Explanatory Memorandum, and note that the European Labour Authority as proposed would not impact on the substance or enforcement of employment legislation in the UK. As the ELA is due to become operational in 2019, we agree that the new body is likely to have a role working with the relevant UK authorities while we remain in the Single Market, albeit without any formal say over its functioning via the Council or the Authority's own Management Board, with any subsequent relationship between the Government and the Authority dependent on "the arrangements agreed with the UK and the EU for the future economic partnership".**

2 €1 = £0.88415 or £1 = €1.13103 as at 28 February.

3 The total 'start-up' costs under the remainder of the 2014–2020 Multiannual Financial Framework are expected to be approximately 33 million euros (£28 million). These would be met partially through redeployment from existing activities currently implemented under the EU Programme for Employment and Social Innovation (EaSI).

4 Explanatory Memorandum submitted by the Department for Business, Energy & Industrial Strategy (5 April 2018).

5 In the UK, this would be the National Minimum Wage enforcement team at HM Revenue and Customs; the Employment Agency Standards Inspectorate (EAS) in England, Scotland and Wales and the Employment Inspectorate (EIA) in Northern Ireland; and the Gangmasters and Labour Abuse Authority.

6 Regulatory checklist submitted by the Department for Business, Energy & Industrial Strategy (5 April 2018).

1.7 **We note the potential benefits of continued cooperation with the Authority after Brexit identified by the Minister. We also consider that the proposal to establish the European Labour Authority is politically important for two reasons:**

- **the draft Withdrawal Agreement on the UK's exit from the EU would preserve the social security rights for UK and EU nationals who have exercised their freedom of movement before the UK leaves the Single Market for their lifetime. As such, the Committee is of the view that the Government will retain an interest in the work of the Administrative Commission on Social Security, and therefore in any social security-related work by the European Labour Authority despite Brexit; and**
- **secondly, there is no clarity about the nature of any long-term post-Brexit working relationship between the relevant UK authorities and the ELA despite the benefits of cooperation with EU countries on labour mobility issues via the Authority as identified by the Minister.**

1.8 **With respect to the latter point, we note that the Commission proposal would restrict formal cooperation agreements between the Authority and non-EU Member States to "countries to which the relevant Union law on labour mobility and social security coordination applies". As we have discussed extensively in a recent series of Reports on proposed amendments to the Social Security Coordination Regulation,[7] the Government's long-term intentions with respect to EU-UK labour mobility and the coordination of social security with the EU after the UK's exit from the Single Market—which includes matters such as provision of healthcare to UK pensioners in France and Spain—is not clear.**

1.9 **Overall, it is therefore likely that any continued participation by the Government with the European Labour Authority after the exit from the Single Market, to obtain the benefits listed by the Minister, is likely to be a function of the broader negotiations on labour mobility and social security coordination, rather than a priority in its own right. We note again in this respect that the Social Security Coordination Regulation has only been extended to non-EU countries which accept full freedom of movement rights for their own citizens to the EU and vice versa (Norway, Switzerland, Iceland and Liechtenstein).**

1.10 **Therefore, while the ELA proposal itself would have relatively little impact on the UK, we consider it politically important in the context of the uncertainty about the UK's future relationship with the Single Market and the free movement of workers. Accordingly, we retain the proposed Regulation under scrutiny and ask the Minister to keep us updated on progress in the legislative negotiations within the Council and the European Parliament.**

Full details of the documents

Proposal for a Regulation establishing a European Labour Authority: (39563), 7203/18 + ADDs 1–3, COM(18) 131.

7 See for example our latest Report on social security coordination of 10 January 2018.

Background

1.11 In November 2017, the EU institutions—with the UK Government's support—adopted the 'European Pillar of Social Rights'.[8] It summarises employment and social rights already available to workers by virtue of EU law, and also sets a wider range of social policy objectives for the coming years (some of which involve new EU Directives, such as the recent European Commission proposals on parental and carers' leave[9] and the rights of workers with non-standard employment contracts).[10]

1.12 The social implications of free movement of labour within the Single Market have been another area of particular political attention. Cross-border labour mobility within the EU has increased significantly in recent years: in 2017, 17 million citizens lived or worked in a Member State other than that of their nationality, almost double compared to a decade ago. Postings of workers, where they retain contractually employed in one Member State but carry out their work in another, have increased by nearly 70 per cent since 2010 and reached 2.3 million in 2016 (although the number of posted workers in the UK, estimated at just over 50,000 in 2015, is almost negligible compared to the working population).[11] The EU already has an extensive body of legislation to ensure that social and employment rights in one Member State are not undercut by businesses using workers from another Member State, such as the Posted Workers Directive,[12] the Social Security Coordination Regulation[13] and the Free Movement Directive.[14]

1.13 However, the Commission has expressed concerns that these rules are not always effectively enforced. In particular, it believes mobile workers are more vulnerable to being denied their employment rights, and the complexity of EU rules can mean businesses operate "in an uncertain or unclear business environment and unequal playing field". The Commission identified the following challenges in enforcing effective labour market mobility rules:

- inadequate EU-level support and guidance for workers, jobseekers and businesses seeking to make use of the free movement of labour;
- insufficient access to and sharing of information between national authorities, including a lack of capacity to organise cross-border cooperation, investigations and enforcement of employment law; and
- a lack of a dedicated cross-border mediation mechanism between Member States in case of a dispute over the application of employment and social law in cases involving the cross-border labour mobility.

8 See our Report of 29 November 2017 on the Pillar of Social Rights and the Government's position on it.
9 See our Report of 31 January 2018 for more information on the proposed Parental and Carers' Leave Directive.
10 The Committee discussed the substance of the draft Employment Rights Directive in more detail in our Report of 31 January 2018.
11 See our Report of 22 November 2017 on amendments to the Posted Workers Directive.
12 These Posted Workers Directive requires a minimum set of host country employment rules to apply to posted workers (who are still employed by the sending company and therefore in principle subject to the law of their home Member State). A proposal to amend the Directive has been provisionally agreed (see our Report of 22 November 2017).
13 Regulation 883/2004. See also our Report of 18 January 2018 for more information on the coordination on social security within the EU.
14 Directive 2004/31/EC on free movement.

1.14 There is thus, in the Commission's view, a need for "effective cooperation between national authorities and for concerted administrative action to manage the increasingly European labour market". Against this backdrop, European Commission President Jean-Claude Juncker announced in September 2017 that the Commission was preparing the legal basis for a new 'European Labour Authority' to ensure that EU rules on labour mobility are enforced in a "fair, simple, and effective way" as required by the European Pillar of Social Rights.[15]

The Commission proposal

1.15 The Commission published its legislative proposal for the establishment of the European Labour Authority (ELA) in March 2018. The Authority will have no independent investigative or enforcement powers vis-à-vis businesses, or be able to direct Member State Governments to take or refrain from specific actions. Instead, it would play a supporting and coordinating role by:

- facilitating access for individuals and employers to information on their rights and obligations as well as to relevant national services;
- supporting cooperation between EU countries in the cross-border enforcement of EU employment and social legislation affecting the free movement of labour, including facilitating joint inspections of business sites; and
- providing mediation and facilitating solutions in cases of cross-border disputes between national authorities or labour market disruptions, including through the sharing of (anonymised) social security data.

1.16 In addition, the Authority will replace the various existing technical advisory bodies that already exist at EU-level to promote fair labour mobility, including the European Coordination Office of EURES,[16] the Technical Committee on the Free Movement of Workers,[17] the European Platform on tackling undeclared work[18] and the Committee of Experts on Posting of Workers.[19]

1.17 The ELA would have running costs estimated to run to 52 million (£45 million) annually once fully operational,[20] with 140 staff split almost evenly between fulltime officials and experts seconded by Member States. It would be overseen by a Management Board, on which the Member States and the European Commission will be represented.

15 Jean-Claude Juncker, "State of the Union" speech (13 September 2017).

16 EURES (the European Employment Services) provides information on labour mobility to workers, jobseekers and businesses in the European Economic Area and Switzerland. It includes job placement schemes run by national governments, like the Department for Work and Pensions' 'Universal Jobmatch' scheme.

17 The Technical Committee, which is composed of six members for each Member State, assists the European Commission in the examination of the application of EU law on free movement of workers.

18 The European Platform tackling undeclared work aims to enhance cooperation between EU countries in fighting undeclared work (UDW).

19 The Posted Workers Committee consists of EU-level trade unions and employers' organisations, as well as Government representatives of the Member States of the EEA. It provides support to Member States in "identifying and exchanging experience and good practice, promote the exchange of relevant information, examine any questions and difficulties which might arise in the practical application of the posting of workers legislation, as well as its enforcement in practice".

20 The total 'start-up' costs under the remainder of the 2014–2020 Multiannual Financial Framework are expected to be approximately 33 million (£x). These would be met partially through redeployment from existing activities currently implemented under the EU Programme for Employment and Social Innovation (EaSI).

Among other things, the Board will establish the Authority's annual budget and appoint its Executive Director. The seat of the Authority is yet to be decided by common accord between the EU's national governments. It may be allocated to one of the newer EU Member States, following the decision to relocate both the European Banking Authority and the European Medicines Agency from London to France and the Netherlands respectively after the UK's exit from the EU.

Support for social security coordination

1.18 In addition to performing the tasks described above, the ELA would also take over certain functions of the Administrative Commission for the Coordination of Social Security Systems. Under Regulation 883/2004, EU Member States coordinate among themselves who is responsible for the payment of social security benefits for people, including workers, who move within the EU. Such citizens are, in principle, entitled to use the local benefits system on the same basis as nationals of their host Member State, including unemployment benefit, state pensions, and access to long-term healthcare. The Committee has published a number of Reports in the past year on proposed amendments to the Regulation, which would affect access to the UK benefits system for EU nationals and vice versa.

1.19 The Administrative Commission brings together Member State representatives to discuss the interpretation of the Regulation, fulfil certain technical regulatory tasks, and resolve any disputes. The European Labour Authority would take over the operational, non-regulatory functions of the Commission,[21] namely:

- the Technical Commission on Data Processing, which works on the common architecture rules for the exchange of personal data on social security;
- the Audit Board, which verifies the annual costs incurred by Member States, for example those related to refunding the costs of any healthcare provided to their residents received during a temporary stay in another Member State (the European Health Insurance Card scheme); and
- the Conciliation Commission, which aims to resolve disputes between Member States about the application of the social security coordination rules.

1.20 As the draft Withdrawal Agreement on the UK's exit from the EU would preserve these rights for UK and EU nationals who have exercised their freedom of movement before the UK leaves the Single Market for their lifetime, meaning the Government will retain an interest in the work of the Commission and any social security-related work by the ELA despite Brexit.

Implications of Brexit

1.21 The plan is for the European Labour Authority to become operational during 2019, depending on agreement on its establishment by the European Parliament and a qualified majority of EU Member States. As such, it is expected to work with the relevant UK public authorities during the post-Brexit transitional period (see below). After the UK leaves the

21 Regulation 883/2004 confers a number of regulatory tasks on the Administrative Commission, for example drawing up the most up-to-date list of long-term care benefits, in cash and in kind, available in all EU Member States to which the social security coordination rules apply to avoid overlap of the provision of benefits.

Single Market, the nature of any working relationship with the ELA would depend on negotiations with the EU about the wider economic partnership and in particular any continued free movement of labour between the UK and the European Economic Area. The Commission proposal restricts formal cooperation agreements between the ELA and non-EU Member States to "countries to which the relevant Union law on labour mobility and social security coordination applies".

1.22 As we have discussed extensively in a recent series of Reports on proposed amendments to the Social Security Coordination Regulation,[22] the Government's long-term intentions with respect to EU-UK labour mobility and the coordination of social security with the EU after the UK's exit from the Single Market—which includes matters such as provision of healthcare to UK pensioners in France and Spain—is not clear. Any continued engagement with the European Labour Authority is likely to be a function of those broader negotiations, rather than a priority in its own right. We note in this respect that the Social Security Coordination Regulation has only been extended to non-EU countries which accept full freedom of movement rights for their own citizens to the EU and vice versa (Norway, Switzerland, Iceland and Liechtenstein).

The Government's view

1.23 The Minister of State for Small Business, Consumers and Corporate Responsibility (Andrew Griffiths) submitted an Explanatory Memorandum on the proposal to establish the ELA on 5 April 2018.[23] The Memorandum outlines the Government's view that "it is important that the ELA respects Member State competence", and that the Authority should "respect the competence of national labour enforcement agencies and complement their work, particularly on cross border mobility, employment and social security matters", adding that the Regulation as drafted "does not impose new obligations on Member States, individuals or employers nor does it impinge on national decision making, legislation, enforcement activities which remain in the competence of Member States".

1.24 The Minister explains that, given the nature of the proposal, the Regulation "will not have any impact on UK law" except to place a few "minor obligations" on the Government, for example if an enforcement authority declines to participate in a joint inspection with authorities from other Member States (in which case it must provide the ELA with written reasons for its refusal). The Government does express a concern over the security risks of sharing of social security data by the ELA in the case of cross-border disputes over which Member State is responsible for the payment of benefits to a specific worker.

1.25 As the ELA is due to become operational in 2019, the Minister notes that the ELA is likely to have a role working with these public authorities while the UK remains in the Single Market, which is expected to be the case until at least the end of 2020 under the terms of the post-Brexit transitional arrangement. During this period, the ELA would cooperate with the various agencies that undertake enforcement of specific pieces of UK employment legislation, including:

- the **National Minimum Wage enforcement team** at HM Revenue and Customs;

22 See for example our latest Report on social security coordination of 10 January 2018.

23 Explanatory Memorandum submitted by the Department for Business, Energy & Industrial Strategy (5 April 2018).

- the **Employment Agency Standards Inspectorate** (EAS) in England, Scotland and Wales and the **Employment Inspectorate** (EIA) in Northern Ireland, which seeks to enforce compliance by employment agencies and employment businesses with their statutory obligations;[24] and
- the **Gangmasters and Labour Abuse Authority** (GLAA), which licences labour providers in the agricultural, shellfish and fresh food processing and packaging sectors. It can also investigate serious labour market offences using police powers across any sector of the labour market in England and Wales.

1.26 The Minister concludes that there are "possibly some costs to the UK government and enforcement agencies through increased administrative work in participating with the ELA, and possibly some costs in ELA related cross border joint inspections". However, he says these "are likely to be low" as the UK, while still in the Single Market, "could determine whether the benefits from participation outweigh the costs and how much to engage with the ELA".

1.27 After the UK's exit from the Single Market, he states, "our role and relationship [with the Authority] in the long term will depend on the arrangements agreed with the UK and the EU for the future economic partnership". A regulatory checklist prepared by his Department on the proposal also identified a number of benefits from continued UK participation in the Authority's work after Brexit, including access to analytical work on "patterns of mobility", mutual learning opportunities, use of conciliation facilities in the case of disputes, and technical support.[25] He notes that this would require a financial contribution by the Government, which would present an "opportunity-cost to the UK contributing to the ELA budget, in terms of greater participation and opportunity to influence".

Previous Committee Reports

None, this is a new proposal.

24 These obligations are contained in the Employment Agencies Act 1973 and its supporting regulations, as well as the Employment (Miscellaneous Provisions) (Northern Ireland) Order 1981 and the Conduct of Employment Agencies and Employment Business Regulations (Northern Ireland) 2005.

25 Regulatory checklist submitted by the Department for Business, Energy & Industrial Strategy (5 April 2018).

2 The EU Civil Protection Mechanism: strengthening EU disaster management

Committee's assessment	Legally and politically important
Committee's decision	Not cleared from scrutiny; further information requested; drawn to the attention of the Public Administration and Constitutional Affairs Committee
Document details	Proposed Decision amending Decision No 1313/2013/EU on a Union Civil Protection Mechanism
Legal base	Article 196 TFEU, ordinary legislative procedure, QMV
Department	Cabinet Office
Document Number	(39265), 14884/17, COM(17) 772

Summary and Committee's conclusions

2.1 The EU Civil Protection Mechanism enables Member States to coordinate their response to natural and man-made disasters within and beyond the EU. It was overhauled in 2013 to strengthen the focus on disaster prevention and risk management and enhance the collective operational capacity of the EU and Member States to plan for and respond to disasters. The Emergency Response Coordination Centre is the operational hub of the Mechanism. It is supported by a voluntary pool of resources committed in advance by Member States to respond to emergencies (the European Emergency Response Capacity).

2.2 The EU Civil Protection Mechanism is funded until the end of 2020. A new funding instrument will be needed to continue the Mechanism beyond 2020. The Commission considers that changes need to be made before then to increase the focus on prevention and disaster risk management as well as the assets available to the Mechanism so that it can respond at times when Member States' own capacities are stretched to their limits. It says that the EU Civil Protection Mechanism as it currently operates cannot meet the demands placed on it—in 2017 alone, it was unable to respond to 7 (out of 17) requests for assistance to fight forest fires.

2.3 The proposed Decision would make "targeted changes" to the EU Civil Protection Mechanism which are intended to address capacity gaps and ensure that the Mechanism is equipped to respond to a range of emergency situations. The Commission proposes a dual system based on "two complementary pillars":

- a European Civil Protection Pool which would operate in a similar way to the existing voluntary pool, but with additional incentives for Member States to "pre-commit" their own disaster response capacities so that these assets are more readily available in an emergency; and

- a new dedicated reserve of EU-acquired and funded response capacities—*rescEU*—which would provide "a last resort capacity" that can be mobilised immediately and (unlike assets provided by Member States) would be under the Commission's operational control.

2.4 As well as strengthening the capacities available to the EU Civil Protection Mechanism, the Commission envisages a more proactive role for itself in overseeing the risk assessments and disaster risk management plans developed by Member States to ensure that effective prevention measures are in place across the EU and that *rescEU* is not used as a substitute for national disaster response capacities. Other changes proposed include establishing a Civil Protection Knowledge Network to share best practice, strengthening coherence with other EU policies and funding instruments, and streamlining administrative procedures so that assistance can be deployed more rapidly.

2.5 The Government expressed concern that the changes proposed by the Commission had pre-empted negotiations (expected to begin this year) on a new legislative instrument to take effect from the beginning of 2021 and were not accompanied by an Impact Assessment, making it "difficult to assess the validity of some of the Commission's assertions". Whilst welcoming the Commission's focus on enhancing prevention and preparedness-planning and supporting Member States in building their disaster response capabilities, the Government said there was "no evidence […] to support the conclusion that the Commission's ownership of assets would significantly reduce deaths, damage and economic losses from natural disasters".[26] The Government recognised that civil protection was likely to be "an important area for future cooperation between the UK and the EU" post-exit and that the outcome of negotiations on the changes proposed by the Commission would affect the structures within which that cooperation would take place.

2.6 We asked the Government for further information on the extent of the EU's competence to act in the field of civil protection (the relevant powers are contained in Article 196 of the Treaty on the Functioning of European Union—TFEU), as well as the need for and "added value" of a dedicated reserve of EU response capacities (*rescEU*), and the broader policy and Brexit implications of the changes envisaged to the EU Civil Protection Mechanism.

2.7 Whilst reiterating the Government's support for the Commission's commitment to improve the operation of the EU Civil Protection Mechanism, the Minister for Implementation at the Cabinet Office (Oliver Dowden) expands on the areas of concern. In summary:

- the Government does not consider that Article 196 TFEU gives the Commission the power to make decisions on the deployment of assets and exercise command and control of assets on the ground;
- whilst there may be a shortage of capability to deal with forest fires, the lack of an Impact Assessment means that the Government "cannot take a view on whether there is a shortfall in capacity at the European level in all of the areas identified" or whether the solution proposed by the Commission is the most cost-effective means of addressing any shortfall;

26 See paras 16 and 19 of the Explanatory Memorandum provided by the then Minister for Government Resilience and Efficiency (Caroline Nokes).

- the Government's view remains that national governments are primarily responsible for planning to ensure that all natural and man-made risks are managed appropriately—action at EU level should not undermine or be a substitute for Member States' own investment in core civil protection capabilities;
- assets should not be directly owned or operated by the Commission;
- any assistance provided to the European Civil Protection Pool "must be in the spirit of voluntary cooperation" and there should be "no compulsion" to provide assistance or more onerous conditions placed on the withdrawal of assets from the Pool;
- there should be flexibility to co-finance assets provided by Member States which do not form part of the European Civil Protection Pool; and
- the Government sees "clear benefits" in cooperating with the EU on civil protection post-exit, but its position may be affected by any changes made to the current EU Civil Protection Mechanism.

2.8 The Minister says that "many Member States have expressed similar views to the UK" on *rescEU* and the European Civil Protection Pool. The Council will shortly begin to negotiate changes to the proposed Decision. The European Parliament is expected to vote on its negotiating position in May. The Commission is keen to complete negotiations "as soon as possible and preferably before the end of 2018".

2.9 **We thank the Minister for his helpful and informative response. On the question of the EU's competence to act under Article 196 TFEU on civil protection, the Minister draws a distinction between setting up *rescEU* (which would, in his view, be in line with Article 196 TFEU) and giving the Commission the power to make decisions on the deployment of *rescEU* assets and exercise command and control over them (which would not). We question whether this distinction is sustainable. If the EU has the power to establish its own autonomous disaster response capability, it would seem to follow that it must also be able to decide when and how to deploy it. We ask the Minister to explain how decisions on the deployment of *rescEU* assets should be taken and who should exercise command and control over them, given that the assets would not be the property of individual Member States.**

2.10 **We note that at least some of the Government's concerns are shared by other Member States. We ask the Minister to provide progress reports on negotiations within the Council which explain how these concerns are being addressed and to update us before the Presidency seeks a mandate to begin negotiations with the European Parliament. We also ask him to set out the Government's position on the changes sought by the European Parliament once it has finalised its negotiating mandate in May. Pending further information, the proposed Decision remains under scrutiny. We draw this chapter to the attention of the Public Administration and Constitutional Affairs Committee.**

Full details of the documents

Proposed Decision amending Decision No 1313/2013/EU on a Union Civil Protection Mechanism: (39265), 14884/17, COM(17) 772.

Background

2.11 Our earlier Report listed at the end of this chapter provides a detailed overview of the Commission proposals and the Government's position.

The Minister's letter of 17 April 2018

2.12 We sought further information on:

- the EU's competence to act under Article 196 TFEU;
- whether the setting up of *rescEU* complies with the subsidiarity principle;
- the European Civil Protection Pool; and
- the wider Brexit implications of the proposed changes to the EU Civil Protection Mechanism ("UCPM").

Competence to act

2.13 We asked the Government to clarify its position on the limits of the EU's competence under Article 196 TFEU and to explain whether this Article gave sufficient powers to the EU to establish *rescEU*. The Minister responds:

> "*RescEU* is in line with Article 196 TFEU to the extent that it is used where existing capacities at the national level are not sufficient. In such instances, *rescEU* may be considered as a supporting and complementing measure. However, the Government is of the view that to the extent that the proposals regarding *rescEU* would give the Commission the power to make decisions on deployment of assets and maintain command and control over assets on the ground, the current proposal exceeds the limits of the EU's competence under Article 196 TFEU. The UK is also of the view that developing assets at the EU level has the potential to undermine the effectiveness of prevention, preparedness and response activities at the national level."

Subsidiarity—the setting up of rescEU

2.14 We shared the Government's concern that the Commission had failed to produce an Impact Assessment, but questioned whether it was fair to conclude that there was "no evidence" that *rescEU* would make some contribution to reducing loss of life and environmental and economic damage, even if the scale of the contribution might be open to question.[27] We asked:

- whether the Government accepted that there was a shortfall in the capacities available at a European level to respond to natural disasters, such as forest fires;
- where responsibility lay for any shortfall;
- whether there were more cost-effective means to address any shortfall; and
- whether the Government saw any added value in *rescEU* as a dedicated "last resort" reserve of EU assets available for immediate deployment.

27 The Commission does not claim that *rescEU* would result in a "significant" reduction, rather that it would bring "clear added value" and "benefits in terms of reducing the loss of human life, environmental, economic and material damage"—see p.3 of the Commission's explanatory memorandum accompanying the proposed Decision.

2.15 The Minister responds:

> "The Commission's proposal for *rescEU* is currently composed of aerial forest firefighting planes, high capacity pumping modules, urban search and rescue, and field hospitals and emergency medical teams. The Commission has cited long-standing logistical and operational experience, high political interest and several assessments of UCPM including the Court of Auditors special report on the UCPM and the UCPM Interim Evaluation as the basis for identifying these assets.
>
> "Without an Impact Assessment, the Government cannot take a view on whether there is a shortfall in capacity at the European level in all of the areas identified, or that the proposed solution is the most cost-effective means of addressing any shortfall. For example, the UN's International Search and Rescue Advisory Group recognise at least 27 internationally accredited Search and Rescue teams are available across Europe. The recent UCPM performance reports concluded that the UCPM works well, with the role of the Commission limited to supporting and coordinating the activity of Participating States.
>
> "However, the Government does recognise that there may be a shortage of capability to deal with forest fires. The Government's view remains that national governments are primarily responsible for planning to ensure that all natural and man-made risks are managed appropriately. This includes risk prevention/mitigation, preparedness (including training and exercising of responding organisations), response (including capabilities required to manage a reasonable worst-case scenario) and recovery.
>
> "The UK will encourage and work with the Commission and other Member States to examine alternative and cost-effective ways to address any shortfall in capacities identified at the European level. This might include reviewing Article 12 of the existing Decision 1313/2013/EU[28] for addressing response capacity gaps, and encouraging greater collaboration between European countries facing similar risks in developing shared response capacities (we note, for instance, that Estonia, Latvia and Lithuania have developed a shared high-capacity pumping capacity for dealing with flooding events). The Government position is that activity by the European Commission should not undermine, or be a substitute for, States' own investment in core civil protection capabilities. Assets should not, therefore, be directly owned or operated by the Commission."

2.16 We noted the Commission's position that *rescEU* should "not be a substitute for efforts at national, regional and local level" and that it should only operate as "a last resort capacity" in response to disasters "that are exceptional in scope or nature" and at times when "national capacities are insufficient or overwhelmed".[29] We suggested that other changes proposed by the Commission (which the Government supported) appeared to reinforce its position that *rescEU* should not reduce capacity at national level—for example, greater

28 Article 12(3) of Decision1313/2013/EU provides: "The Commission shall encourage Member States to address, either individually or through a consortium of Member States cooperating together on common risks, any strategic capacity gaps that have been identified."

29 See pp.5 and 10 of the Commission Communication (Council document 14883/17) accompanying the proposed Decision.

oversight and monitoring of risk assessments and disaster risk management planning at national and sub-national level, more incentives for Member States to contribute assets to the voluntary European Civil Protection Pool, and the introduction of an element of conditionality in future EU funding for disaster prevention measures at national level. We asked whether the Government's concerns could be allayed by amendments to the text of the proposed Decision which, for example, would make clear that *rescEU* would only operate as a "last resort capacity" or give the Council rather than the Commission the power to decide on the future composition of *rescEU*.

2.17 The Minister says that textual amendments of this nature "would not appear to reduce the risk outlined above—particularly the potential undermining of national responsibilities for safety and security". He adds:

> "On the issue of capacity goals, greater Council control would strengthen the proposal, but would not be determinative on our overall position, due to the wider weaknesses that have been identified."

The European Civil Protection Pool

2.18 We noted that assets made available to the European Civil Protection Pool would "remain available for national purposes at all times" and, once deployed, would "remain under the command and control of the Member States making them available".[30] The requirement to "consult" the Commission would only arise if a Member State intended to withdraw assets after their deployment, during the lifetime of an operation. We suggested that this was not unreasonable, given the Commission's coordinating role, provided it had no power to resist the withdrawal of assets.

2.19 The Minister makes clear that any assistance provided to the European Civil Protection Pool ("ECPP") "must be in the spirit of voluntary cooperation" and that there should be "no compulsion to provide assistance requested by other countries, or the Commission". He continues:

> "The Government's principal concern in relation to changes from the previous Voluntary Pool is in the proposed amendments to Article 11, Clause 7—in particular, the replacement of 'domestic emergencies, force majeure or, in exceptional cases, serious reasons' with 'an exceptional situation substantially affecting the discharge of national tasks' as the reasons why a Participating State can refuse a request to deploy an ECPP asset. The Commission has cited alignment with wording for FRONTEX legislation as a reason for this change, but this also appears to have the effect of strengthening the Commission's control over ECPP assets, and setting an exceptionally high bar for refusal on the part of the Participating State (although there does not appear to be any legal ramification for refusal). We are seeking clarification from the Commission as to why, other than bureaucratic simplicity, this change is being sought."

2.20 Under the Commission's proposal, the EU would only subsidise (co-finance) assets that are part of the European Civil Protection Pool, not those which are outside the Pool and made available on an ad hoc basis—a change which the Commission describes as "a

30 See Article 11(6) of Decision No 1313/2013/EU on a Union Civil Protection Mechanism and the amended Article 11(8) in the proposal.

significant shift compared to the situation today".[31] We asked the Government to explain how this would affect the UK and how much funding for its own disaster response capacities the UK might stand to lose.

2.21 The Minister responds:

> "The principal means by which the UK currently benefits from the Mechanism is via co-financing of transport for assets outside of the Voluntary Pool, in response to an international emergency. The UK would no longer benefit from this incentive under the Commission's new proposal to remove financial incentives for transporting assistance for countries deploying outside of the Pool framework. DFID [the Department for International Development] is the main government department to benefit from transport assistance and does not currently have any assets committed in the Pool. Between 2013 and 2017, DFID undertook 226 movements of people and equipment via the UCPM. The UK provided more than 5,000 tonnes of assistance items, worth nearly €50m, and sent more [than] 1200 experts to assist in disaster response on the ground. DFID received around €15m funding from the Commission to co-finance the transport of assistance during this period.
>
> "Member States should not be penalised for providing assistance in different forms. Recent emergencies have shown the uniqueness of every situation, and the requirement for items that have not previously been identified as a need. For example, in response to a specific need during the 2016 Haiti hurricane response, DFID sent a quantity of timber for rebuilding damaged homes. Under the current proposals, such assistance would not qualify for co-financing. Given the unpredictability of requirements in emergencies, flexibility needs to be retained to co-finance unforeseen assistance. The UK and other Member States including Germany, the Netherlands, Denmark, Austria and Sweden share this view."

Brexit implications

2.22 We noted that the EU Civil Protection Mechanism was open to participation by non-EU members of the European Economic Area "and other European countries when agreements and procedures so provide". Six non-EU countries currently participate in the EU Civil Protection Mechanism.[32] We sought a general indication of the terms on which they are able to participate and the extent to which these would provide a suitable model for the UK, given that the Government has highlighted civil protection as an important area for future cooperation between the UK and the EU post-exit.

2.23 The Minister confirms that participation in the EU Civil Protection Mechanism is not limited to Member States:

> "Other non-EU countries negotiate a treaty and payment to participate in the CPM. The UK would have to negotiate its agreement for post-Exit participation in the UCPM."

31 See p.5 of the Commission Communication (Council document 14883/17) accompanying the proposed Decision.
32 The former Yugoslav Republic of Macedonia, Iceland, Montenegro, Norway, Serbia and Turkey.

2.24 Turning to UK cooperation with the EU in this field post-exit, the Minister draws attention to the Government's future partnership paper on Security, Law Enforcement and Criminal Justice published in September 2017 which states:

> "There are are clear benefits for both the UK and the EU in coordinating efforts to protect citizens by making best use of resources and ensuring that complementary action is taken in areas with common objectives, such as… civil protection."

2.25 This position is also reflected in the Government's future partnership paper on Foreign Policy, Defence and Development. The Minister adds, however, that this position was based on "civil protection arrangements—including the UCPM—as they stood at the time, which include the ability for non-EU countries to participate in the Mechanism through an existing treaty-based route defined in the UCPM legislation". He continues:

> "If the current set of proposals change the Mechanism, it would be necessary to reflect whether those changes affect the Government's policy position."

2.26 The Minister makes clear that the UK's future relationship with the EU "remains a live and developing issue".

Progress of negotiations

2.27 The Minister tells us that negotiations within the Council are in their initial stages and that "many Member States have expressed similar views to the UK" on *rescEU* and the European Civil Protection Pool. He continues:

> "Following receipt of additional information on the proposals from the Commission, the Council will shortly progress to negotiating text changes to the proposed legislation. The Government agreed its negotiation mandate on 9 March and officials will continue to work with the Commission and other Member States in line with this mandate. The Commission has expressed an intention to complete the negotiation process as soon as possible and preferably before the end of 2018.
>
> "The proposals for legislative change are subject to the co-decision procedure in the European Parliament (ENVI committee). The European Parliament rapporteur provided a draft report on the proposals on 20 March. A vote in the European Parliament is due to take place on 16–17 May 2018 to agree the Parliament's position on the current set of proposals. MEPs are broadly supportive of the Commission's proposals to improve the UCPM. However, MEPs have expressed scepticism over the Commission's proposal to own specific civil protection assets such as field hospitals. MEPs have also shared concerns about the potential impact of the proposals on State sovereignty when dealing with natural disasters within their own borders—a concern echoed by the UK and other Member States."

Previous Committee Reports

Eleventh Report HC 301–xi (2017–19), chapter 2 (24 January 2018).

3 EU Pet Travel Scheme

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
Document details	Commission Report on the implementation of Article 5 of Regulation (EU) No 576/2013 on the non-commercial movement of pet animals
Legal base	—
Department	Environment, Food and Rural Affairs
Document Number	(39533), 6869/18, COM(18) 88

Summary and Committee's conclusions

3.1 The EU Pet Travel Scheme (PETS) governs the non-commercial movement of pet animals.[33] As a rule, a maximum of five pet dogs, cats or ferrets may accompany their owner/authorised person during a single trip. While a derogation from the five-pet rule is permitted for the purposes of competitions, exhibitions or sporting events or training for such events, the Government is concerned that this facilitates fraudulent commercial trade.

3.2 The Commission's Report assesses the effectiveness of the derogation. Only the UK and one other Member State reported concerns that the derogation facilitates fraudulent commercial trade. Those Member States suggested further restrictions or revocation of the derogation. The Commission does not propose any changes, but encourages Member States to act to ensure proper implementation and enforcement of the legislation to counter fraudulent practices.

3.3 The Parliamentary Under-Secretary of State for Rural Affairs and Biosecurity (Lord Gardiner of Kimble) expresses disappointment that the Commission has not chosen to act to address the illegal puppy trade. The Government will continue to press for change and to seek opportunities to provide robust enforcement in relation to health, welfare and consumer protection for pet travel. This will include consideration of the UK's pet travel policy post-Brexit.

3.4 In its Report, "Animal welfare in England: domestic pets" in November 2016,[34] the Environment, Food and Rural Affairs Committee reported on the illegal puppy trade enabled by the PETS. It recommended that: this issue should be included within the Brexit negotiations; the age at which dogs can enter the United Kingdom under PETS should be increased to six months; and the Government should increase spot checks at entry points into the UK. Responding,[35] the Government explained that the Animal and Plant Health

33 Regulation (EU) No 576/2013 on the non-commercial movement of pet animals.

34 Environment, Food and Rural Affairs Committee, Third Report of Session 2016–17, Animal welfare in England: domestic pets, HC 117.

35 Environment, Food and Rural Affairs Committee, Fourth Special Report of Session 2016–17, Animal welfare in England: domestic pets: Government Response to the Committee's Third Report, HC 1003.

Agency (APHA) completed checks on 5,663 animals travelling into Great Britain in 2015. Of those, 73 animals were found to be non-compliant with PETS. The Government was seeking to gain a better understanding of pet movements under PETS.

3.5 **We note that the UK has advocated restrictions or revocation of the five-pet derogation, but that there has been insufficient support at EU-level for change. Following the Environment, Food and Rural Affairs Committee Report highlighting concerns that the Pet Travel Scheme was facilitating puppy smuggling, it is disappointing that the Government has been unable to build a coalition of support at EU level. We would welcome information from the Government on the practicalities of a change of approach post-Brexit and what work the Government is undertaking to assess options for future policy. It would also be helpful to know whether this issue is likely to feature in negotiations on the future relationship between the UK and the EU.**

3.6 **We retain the document under scrutiny and draw it to the attention of the Environment, Food and Rural Affairs Committee given that Committee's previous work in this area.**

Full details of the documents

Commission Report on the implementation of Article 5 of Regulation (EU) No 576/2013 on the non-commercial movement of pet animals: (39533), 6869/18, COM(18) 88.

Explanatory Memorandum of 20 March 2018[36]

3.7 The Minister expresses the Government's view in the following terms:

> "We are disappointed that the Commission has not chosen to take action to address the illegal puppy trade. We will continue to press for change, including raising the issue at future Chief Veterinary Officer (CVO) meetings in Brussels. We will continue to seek opportunities to provide robust enforcement in relation to health, welfare and consumer protection for pet travel, including consideration of the UK's pet travel policy after we have left the EU."

Previous Committee Reports

None.

36 Explanatory Memorandum from Lord Gardiner of Kimble dated 20 March 2018.

4 EU chemicals policy review

Committee's assessment	Politically important
Committee's decision	Not cleared from scrutiny; further information requested; drawn to the attention of the Environmental Audit and the Business, Energy and Industrial Strategy Committees
Document details	Commission Communication—Commission General Report on the operation of REACH and review of certain elements: Conclusions and Actions
Legal base	—
Department	Environment, Food and Rural Affairs
Document Number	(39540), 6916/18 + ADDs 1–7, COM(18) 116

Summary and Committee's conclusions

4.1 The core of EU chemicals policy is the "REACH" (Registration, Evaluation, Authorisation and Restriction of Chemicals) Regulation.[37] This was adopted in 2006 to improve the protection of human health and the environment from the risks that can be posed by chemicals. It included the establishment of the European Chemicals Agency (ECHA), of which the Prime Minister has said the UK intends to seek associate membership post-Brexit.[38]

4.2 The Commission's document is the second five-yearly review of the Regulation. It concludes that REACH is effective but there are opportunities for further improvement, simplification and burden reduction. A number of proposed actions are identified, as set out below. These are of a non-legislative nature as it was concluded that the legal requirements remain fit for purpose.

4.3 The Parliamentary Under Secretary of State for the Environment (Dr Thérèse Coffey) does not refer to the Prime Minister's commitment to seek associate membership of the ECHA, but she does confirm that UK manufacturers and distributors exporting chemicals to the EU will have an interest in any changes to the implementation approach in REACH. She also confirms that UK officials will be seeking to influence follow-up actions and activities, with a particular focus on embedding better regulation approaches via simplification measures.

4.4 The Minister states that UK officials remain engaged in EU decision-making forums "and are working hard" to maintain relationships and policy outcomes that ensure protection for human health and the environment, and maintain the UK's reputation for excellence in scientific analysis and evidence-based regulatory policy-making.

4.5 **We welcome the continued engagement of UK officials in EU decision-making forums, working hard to maintain relationships and policy outcomes even as the UK negotiates its withdrawal from the EU.**

37 Regulation (EC) No 1907/2006 concerning the Registration, Evaluation, Authorisation and Restriction of Chemicals (REACH).

38 Mansion House speech, 2 March 2018.

4.6 **We are surprised, however, that the Minister does not reference the Prime Minister's intention to seek associate membership of the European Chemicals Agency post-Brexit. While the outcome of negotiations is unknown, we believe that the Prime Minister's objective is an important consideration in the UK's approach to the various actions proposed.**

4.7 **The Prime Minister was asked at the House of Commons Liaison Committee meeting on 27 March 2018 what associate membership of ECHA would look like in practice. In response, she referred to Switzerland's membership of the European Aviation Safety Authority (EASA) and also said that the objective of ECHA associate membership would be to ensure that there would be only one set of approvals for access to UK and EU markets. She was otherwise imprecise in terms of the UK's vision for associate membership of ECHA.**

4.8 **Following the example of Swiss participation in EASA, however, and the logic of requiring only one set of approvals, it would seem reasonable to assume that the UK would apply relevant legislation, in the same way as the Swiss implement EU aviation safety legislation.[39] We ask whether this is a reasonable assumption and whether the Government envisages that any such application would extend to the other Regulations covered by ECHA—i.e. Biocidal Products Regulation, the Classification, Labelling and Packaging (CLP) Regulation and the Prior Informed Consent Regulation.**

4.9 **We note that one of the areas covered in the Commission's report is that of the future role and funding of ECHA, given that ECHA's income from fees post-2020 will reduce substantially because the number of registrations will drop significantly. In the light of the commitment to seeking associate membership of ECHA, we would welcome the Minister's view on the Commission's assessment of the future role and funding of ECHA and how the issues identified might be addressed.**

4.10 **We retain the document under scrutiny and draw it to the attention of the Business, Energy and Industrial Strategy Committee in the light of its work on the implications of Brexit for the pharmaceuticals sector and to the attention of the Environmental Audit Committee given its interest in the future of chemicals regulation.**

Full details of the documents

Commission Communication—Commission General Report on the operation of REACH and review of certain elements: Conclusions and Actions: (39540), 6916/18 + ADDs 1–7, COM(18) 116.

Background

4.11 REACH puts obligations on industry to collect chemical safety information, to use this information to develop and apply appropriate risk management measures, to communicate these measures to users of chemicals and, finally, to document this in registration dossiers submitted to the European Chemicals Agency (ECHA).

39 Article 66 of the EASA Regulation (Regulation No 216/2008 on common rules in the field of civil aviation and establishing a European Aviation Safety Agency) provides for participation of European third countries in EASA on condition that they apply Community law in the field covered by the Agency, including implementing rules.

4.12 ECHA or Member States evaluate if the safety information is sufficient and, if not, require additional information. REACH also establishes two distinct EU risk management approaches: a) Restrictions enable the EU to impose conditions on the manufacturing, placing on the market or use of substances; b) Authorisation is designed to ensure that substances of very high concern (SVHCs) are used safely while promoting substitution by suitable alternatives.

Achievement of REACH Objectives

4.13 REACH first came into force in June 2007, and today it is fully operational and delivering results towards achieving its objectives. REACH has influenced legislation in third countries (such as South Korea and China), highlighting the potential for it to serve as a global model for chemicals legislation. The cost of REACH to businesses and regulators is estimated at £2–2.3 billion. However, the estimated benefit to human health and the environment is £88 billion over 25–30 years. A number of improvements are suggested (see below).

Industry responsibility

4.14 Industry (manufacturers and exporters) have generally completed their registration dossiers on time for existing substances, and measures to support SMEs to meet their registration obligations have been effective. More work, however, needs to be done in filling important data gaps and companies therefore need to be incentivised to update their registration dossiers. Compliance with EU information requirements by registrants was considered insufficient due to the use of alternative methods to animal testing and inconsistencies in hazard assessment between registrants and regulatory authorities. Information passed through the supply chain has increased, though this could be achieved more efficiently, further reducing costs and especially benefitting SMEs. REACH has, however, stimulated the development of alternative substances, to be used as substitutes for more hazardous chemicals, compared to previous legislation.

Action by Member States and the Commission

4.15 The review highlighted insufficient resources in Member States to participate in risk assessment and regulatory proposals. Despite improvements, further work is needed to reinforce national enforcement activities. Discrepancies were established between REACH and other EU legislation that the Commission needs to address. In addition, the ongoing regulatory gap relating to information needs for nanomaterials is currently being addressed by proposed amendments to the REACH Annexes.

European Chemicals Agency (ECHA)

4.16 ECHA has been instrumental in the implementation of REACH and has built up significant competence in chemicals management by enabling stakeholders to easily access the world's largest database on chemicals. It has also established scientific cooperation with a number of EU and non–EU agencies. However, ECHA's income from fees post-2020 will reduce substantially because the number of registrations will drop significantly. The Commission has committed to assessing how ECHA's independence and expertise can be maintained.

Proposed actions

4.17 The Commission proposes sixteen actions, to be undertaken by the Commission, ECHA, Member States and industry:

- encourage the updating of registration dossiers;
- improve evaluation procedures;
- improve the workability and quality of extended Safety Data Sheets;
- track substances of concern in the supply chain;
- promote substitution of "substances of very high concern" (SVHCs);
- simplification of the authorisation process;
- make socio-economic information available early in the process of considering possible regulatory measures;
- improve the procedure for identifying, and derogating from, restrictions;
- further enhance Member State involvement in the restriction procedure;
- frame the application of the precautionary principle (when scientific data do not permit a complete evaluation of risk);
- assess the interplay between authorisation and restriction;
- assess the interplay between REACH and health and safety legislation;
- enhance enforcement;
- support compliance by small and medium-sized enterprises;
- assess funding and tasks of the ECHA; and
- review the registration requirements for low tonnage substances and polymers.

The Minister's Explanatory Memorandum of 29 March 2018

4.18 The Minister explains that the Commission is now opening discussion with stakeholders on implementation of its proposed actions. The UK will, she says, be seeking to influence follow-up actions and activities. The Minister adds:

> "UK officials remain engaged in EU decision making forums, and are working hard to maintain relationships and policy outcomes that ensure protection for human health and the environment, and maintain the UK's reputation for excellence in scientific analysis and evidence based regulatory policy making."

4.19 Concerning the content of the review, there are certain aspects that the UK particularly welcomes, such as the importance of closing the regulatory gap in REACH for nanomaterials. More broadly, says the Minister, the UK will use the review to further

embed better regulation approaches via simplification measures, reducing costs for business and SMEs in particular. Specific proposals which could be fruitful in furthering a better regulation approach might include (but not be limited to):

- enforcement—this would be a UK priority to avoid REACH non-compliant and counterfeit goods undermining UK industry standards;
- measures linked to improving dossier quality, including simplification and clearer guidance on testing requirements—to help avoid double and follow up testing, which imposes unnecessary costs and the use of vertebrate animals in tests; and
- initiatives to drive substitution of hazardous chemicals.

4.20 The Minister notes that the review highlighted issues around insufficient resources in Member States for scientific evaluation, which reduces the overall EU activities in assessing and regulating substances. The UK, says the Minister, has been a leader in this area, and has put forward a number of regulatory dossiers.

4.21 On the UK's withdrawal from the EU, the Minister writes:

> "In light of the UK's departure from the EU, UK manufacturers and distributors exporting chemicals to the EU will have an interest in any changes to the implementation approach in REACH. Those operating in the UK will also have an interest, as REACH will be brought into UK law under the Withdrawal Bill as retained EU law, although the changes proposed in the review are non-legislative."

Previous Committee Reports

None.

5 Regulation of covered bonds

Committee's assessment	Politically important
Committee's decision	Not cleared from scrutiny; further information requested; drawn to the attention of the Treasury Committee
Document details	(a) Proposal for a Directive on the issue of covered bonds and covered bond public supervision and amending Directive 2009/65/EC and Directive 2014/59/EU; (b) Proposal for a Regulation amending Regulation (EU) No 575/2013 as regards exposures in the form of covered bonds
Legal base	Article 114 TFEU; ordinary legislative procedure; QMV
Department	Treasury
Document Number	(a) (39544), 7064/18 + ADDs 1–2, COM(18) 94; (b) (39555), 7066/18 + ADDs 1–2, COM(18) 93

Summary and Committee's conclusions

5.1 In March 2018 the European Commission proposed a new EU-level regulatory framework for covered bonds, a type of debt obligation issued by banks that offers bondholders extra security in case the issuer goes insolvent. Covered bonds are seen as very safe investments, because they are secured against a ring-fenced pool of high-quality, low-risk assets (typically residential mortgages), which holders can access directly as preferred creditors if the issuer of the bond cannot make their contractual payments.[40] Germany and Denmark are the largest markets for this type of debt instrument globally, with outstanding volumes totalling approximately €383 billion (£333 billion)[41] each. The UK market is estimated to amount to €121 billion (£100 billion) of outstanding covered bonds.

5.2 The low-risk nature of these bonds allows the issuing bank to offer a low interest rate, making them a relatively cheap way of raising capital that can then be used to finance business and consumer loans. For the same reason, EU financial services legislation contains certain regulatory and prudential reliefs for EU-based financial institutions, such as investment funds, banks and insurers, which purchase covered bonds issued by EU banks (see "Background" below). However, the EU has not to date substantively regulated matters relating to the *issuance* of covered bonds, such as prudential, governance or transparency requirements.

5.3 To address divergent national regulatory practices with respect to the technical aspects of the covered bond market, and increase their uptake in- and outside of the Single Market under a harmonised regulatory framework, the European Commission has now proposed a Directive with minimum harmonising standards for the issuance of all covered bonds within the European Union, and products that are compliant can carry the

40 If there are insufficient assets in the asset pool to meet obligations to covered bond-holders where the issuer has defaulted, they become unsecured creditors of the failed issuer for the residual amount.

41 €1 = £0.88415 or £1 = €1.13103 as at 28 February.

label 'European Covered Bond' (ECB). Purchase of an ECB by an EEA-based[42] investment fund, bank or insurer would trigger the application of the existing regulatory or prudential reliefs (the latter of which will be subject to tighter requirements under a parallel proposal to amend the Capital Requirements Regulation) in a way that the purchase of a covered bond issued outside the Single Market would not. We have described the substance of the proposed regulatory framework in more detail in paragraphs 5.25 to 5.27 below.

5.4 The Commission proposal does not contain an 'equivalence' provision which would allow the EU to recognise the regulatory framework for covered bonds of a "third country" (like the UK after it leaves the Single Market) as equivalent, which would mean bonds issued in that country would trigger the same prudential and regulatory reliefs as EU-issued covered bonds. Instead, EU banks investing in covered bonds issued outside the European Economic Area (EEA) would remain entitled to an existing, more limited prudential relief with respect to their liquidity buffer.[43] The new Directive would, however, require the Commission to assess within three years of the new framework becoming operational "whether a general equivalence regime for third-country covered bond issuers and investors is necessary or appropriate".[44] The proposal would also allow individual EU countries to prohibit banks from including non-EU assets in their cover pool.[45]

5.5 The Economic Secretary to the Treasury (John Glen) submitted an Explanatory Memorandum with the Government's views on the proposal in April 2018.[46] The Government is broadly supportive of the proposed legislation, but will seek to use the UK's part in the legislative process before Brexit in March 2019 to "ensure that [the] proposals will enhance comparability, transparency and market stability by helping investors better understand the profile and risks of a programme as they undertake their due diligence". The Minister also "notes" the Commission's intention to assess the need for a third country 'equivalence' regime to recognise non-EU covered bonds as meeting EU criteria for prudential reliefs at some stage in the future, but makes no further comment on the matter.

5.6 **The UK market for covered bonds forms only a small part of its capital markets, but with £100 billion outstanding it is nonetheless significant. We note that the Minister has not raised any substantive concerns about the impact the new EU regulatory framework for such bonds may have on the existing UK regulatory approach. It is unclear whether this is because the proposals would not materially alter the current framework, or because the legislation is not expected to have an impact on the UK due to its withdrawal from the European Union. We note in this regard that the Government has sought a post-Brexit transitional arrangement during which EU law would continue to apply, which may include the new Covered Bonds Directive should it take effect during this period.**

42 The Covered Bonds Directive, after its adoption, is likely to be incorporated into the EEA Agreement and thus apply in Norway, Iceland and Liechtenstein as well.

43 See Commission Delegated Regulation (EU) 2015/61 (the Liquidity Coverage Requirement Regulation).

44 The creation of an equivalence regime, if not included in this proposed Directive by the European Parliament and the Member States in the Council, would require a new legislative proposal in due course.

45 If a Member State does allow inclusion of loans to non-EU entities in the cover pool, their national regulator would have to "[verify] whether the assets located outside of the Union meet all the [quality] requirements [that apply to the other assets held in the pool] and that the realisation of such assets is legally enforceable in a way similar to assets located within the Union".

46 Explanatory Memorandum submitted by HM Treasury (11 April 2018).

5.7 **Broadly speaking, the impact of the new legislation in the context of the UK's EU exit, based on the current state of the Article 50 negotiations, can be summarised as follows:**

- **if the Covered Bonds Directive takes effect while the UK is still in the Single Market (which it will be until at least the end of 2020 if the transitional agreement provisionally agreed between the Government and the EU is ratified before March 2019), the Treasury and the Financial Conduct Authority will have to apply the new legislation;**
- **as a result of the continued Single Market membership, covered bonds issued by British banks would trigger the same prudential and regulatory reliefs as for those issued by the remaining EU banks. This would be the case until the UK leaves the Single Market. Similarly, there would be no restrictions on the ability of issuing banks to include UK-based assets in their cover pool;**
- **after the UK leaves the Single Market, and barring any agreement with the EU that may require continued regulatory alignment in the area of financial services, the Government would be free to modify the domestic regulatory framework for covered bonds as it sees fit. However, such bonds issued by British banks would no longer entitle EU-based banks to prudential and regulatory reliefs, reducing their competitiveness within the Single Market. It is not clear if the reliefs would remain available to EU-based banks in respect of bonds issued before the UK leaves the Single Market;**
- **after the UK leaves the Single Market, whether UK assets can be included in issuing banks' cover pools for covered bonds will depend on the national legislation of the EU country where the bank is based. In any event, inclusion of such assets will be subject to additional compliance requirements to ensure they meet the Directive's asset eligibility requirements and can be converted into cash "in a way similar to assets located within the Union" and which "is legally enforceable in a way similar to assets located within the Union";[47] and**
- **however, if the Treasury were to seek 'equivalence' between the EU's and the UK's covered bonds regime (should this become possible under the Covered Bonds Directive), its practical room to make amendments to domestic UK regulations on covered bonds would likely be constrained, unless it was willing to see the equivalence decision revoked by the European Commission.**

5.8 **The situation as described above may change as a result of the negotiations between the Government and the EU on a new trade agreement on financial services, where the UK is seeking a horizontal presumption of mutual recognition of regulatory standards combined with a mechanism to assess continued alignment of regulatory outcomes on an on-going basis.[48] There has been no substantive indication from the European Commission or the remaining Member States that they would contemplate such a radical departure from the existing case-by-case 'equivalence' approach to preferential**

47 See Article 7 of the Proposed Directive.

48 See for more information the speech by the Chancellor of the Exchequer, "Chancellor's HSBC speech: financial services" (7 March 2018).

treatment of non-EEA financial services providers within the Single Market.[49] It would fundamentally alter the regulatory 'perimeter' that separates those states subject to Single Market legislation from those states that are not, and likely create friction with the EU's other trading partners that either commit to applying EU law to secure market access (such as Norway, Iceland, Ukraine) or rely on the 'equivalence' process (for example Canada, the US, and Japan).

5.9 **In any event, it does not appear—in the case of Covered Bonds or any other sector of the financial services industry—that the Government's preferred outcome would fundamentally alter the trade-off between continued preferential treatment of UK financial services and products within the Single Market, and constraints on regulatory autonomy after Brexit (unless it calculates that the EU-27 will in the end be willing to take a very flexible approach to regulatory alignment—and therefore give the Treasury greater leeway to legislate differently from the EU—to preserve their businesses' access to the UK's capital markets despite the potential impact on the regulatory cohesion of the Single Market). Time will tell whether the EU's position on the Government's offer will shift, and the European Scrutiny Committee will keep developments in the negotiations under close review to ensure that any commitments made by the Government for post-Brexit regulatory alignment with the EU are subject to on-going parliamentary oversight.**

5.10 **Given the continued uncertainty about the future of regulatory cooperation and alignment with the EU on financial services after the UK leaves the Single Market, we retain the proposed Directive and Regulation under scrutiny and ask the Minister to keep us informed of developments in the legislative process (particularly with respect to the inclusion of an 'equivalence' regime by either the Council or the European Parliament). We also ask for his next update to us to include information, if available, on the volume of UK-issued covered bonds held by investors elsewhere in the EU. We draw the proposals to the attention of the Treasury Committee.**

Full details of the documents

Proposal for a Directive on the issue of covered bonds and covered bond public supervision and amending Directive 2009/65/EC and Directive 2014/59/EU: (39544), 7064/18 + ADDs 1–2, COM(18) 94. Proposal for a Regulation amending Regulation (EU) No 575/2013 as regards exposures in the form of covered bonds: (39555), 7066/18 + ADDs 1–2, COM(18) 93.

Background

5.11 Covered bonds are debt obligations issued by credit institutions and secured on the back of a ring-fenced pool of assets (the "cover pool" or "cover assets") which bondholders have direct recourse to as preferred creditors. This is called "double-recourse protection"

49 The General Affairs Council of 20 March 2018 discussed the use of reviewed and improved equivalence frameworks to form the basis for any EU-UK agreement on financial services. Similarly, the European Council of 23 March 2018 said the UK-EU trade agreement should "address (…) trade in services, with the aim of allowing market access to provide services under host state rules, including as regards right of establishment for providers, to an extent consistent with the fact that the UK will become a third country and the Union and the UK will no longer share a common regulatory, supervisory, enforcement and judiciary framework".

for bondholders: if the issuer fails, the bondholder has a direct and preferential claim against certain earmarked assets and an ordinary claim against the issuer's remaining assets:

- under normal circumstances, covered bonds are an obligation of the issuer, so investors can expect that the issuer will make interest and principal payments on the agreed dates;
- if the issuer of the covered bond defaults on its obligations to covered bond holders or becomes insolvent, the asset pool is used to continue making payments to bondholders on the agreed dates; and
- if there are insufficient assets in the asset pool to meet obligations to covered bond-holders where the issuer has defaulted, they become unsecured creditors of the failed issuer for the residual amount.

5.12 Furthermore, the cover pool is usually made up of high-quality, low-risk assets (for example residential mortgage loans and public sector debt). The covered bond pool is also dynamic (unless the issuer defaults): the issuing entity is under an obligation to ensure that the value of the assets in the cover pool at least matches at all times the value of the covered bonds and to replace assets that become non-performing, or otherwise do not meet the relevant eligibility criteria. As such, covered bonds are seen as a safe investment compared to unsecured bonds.

5.13 These core features reduce the risk of investments in covered bonds, which allows banks to issue them more cheaply because their reliability means a lower rate of return is possible. This, in turn, means they have more capital available to provide loans to businesses, consumers and the public sector. The lower risk associated with covered bond has also led to certain regulatory reliefs for financial firms which invest in them under EU law:

- under the Capital Requirements Regulation, banks can hold less regulatory capital against these products;[50]
- UCITS investment funds can hold up to 25 per cent of their assets in the form of covered bonds issued by one issuer, compared to 5 per cent for other assets; and
- under the Solvency II Directive, larger insurance firms can invest freely in regulated covered bonds, subject to their risk appetite and the constraints of their capital requirements and the 'Prudent Person Principle'.[51] However, with respect to smaller insurance firms, UK law allows them to take credit for up to 40 per cent of the value of their assets held in such bonds issued by a single counterparty, but only 5 per cent in unregulated covered bonds.

5.14 The UK covered bond market was established in July 2003 under UK general law. In March 2008 the Treasury introduced dedicated covered bond legislation (Regulated

50 Article 129 of the Capital Requirements Regulation.

51 The Prudent Person Principle, a legal principle under the Solvency ii Directive, requires asset managers to only make investment decisions for their customers that a "prudent person" would make.

Covered Bond Regulations 2008) for the UK market,[52] where assets backing the bond are transferred to a separate legal entity (a 'Special Purpose Vehicle' or SPV) and form collateral for the bonds.[53] The total volume of covered bonds outstanding in the EU at the end of 2014 was €2.5 trillion (£2.2 trillion). Within the EU, Germany and Denmark are the largest markets with outstanding volumes of €384 billion and €383 billion respectively. The UK's market is estimated at €121 billion (£100 billion), with fifteen issuers (compared to 79 in Germany). France, Spain, Sweden and Italy are also major issuing country. As of 2015, there were 317 active covered bond issuers globally, of which 261 in the EU.

EU regulation of covered bonds

5.15 At present, covered bonds are only partially regulated at EU-level. As noted, they confer certain prudential and regulatory benefits on banks and investment funds who purchase them in light of their lower financial risk. However, EU law does not comprehensively define the term 'covered bond' for general purposes or substantively address prudential or conduct requirements for their issuance.[54] As a result, covered bond markets in the EU remain largely fragmented along national lines and their volumes varies greatly between individual Member States.

5.16 According to the Commission, this fragmentation "constrains standardisation in underwriting and disclosure practices and creates obstacles to deep, liquid and accessible markets, in particular across borders". In its 2013 Green Paper on the "long-term financing of the European economy", the Commission also asked for stakeholder views on the "pros and cons of developing a more harmonised framework for covered bonds" in the EU to stimulate their issuance by banks and uptake by investors.[55] It also saw an opportunity to create a regulatory regime easily recognised outside of the EU, in the same manner as the 'UCITS' label for investment funds, which would make EU-issued covered bonds more a attractive investment prospect for non-EU investors.

5.17 In 2012 the European Systemic Risk Board, which monitors the build-up of macro-economic risks in the EU, also called on the European Banking Authority (EBA) to identify and monitor best practices in the covered bond market "so as to ensure robust and consistent frameworks Union", with a view to ensuring that the prudential reliefs banks enjoy when investing in covered bonds remained justified.[56] Moreover, in its 2015 Capital Markets Union Action Plan, the European Commission also undertook to "assess

52 The 2008 UK regulations transposed Article 22(4) of the 1985 UCITS Directive as amended, which provided: "Member States may raise the 5 % limit laid down in the first sentence of paragraph 1 to a maximum of 25 % in the case of certain bonds when these are issued by a credit institution which has its registered office in a Member State and is subject by law to special public supervision designed to protect bond-holders. In particular, sums deriving from the issue of these bonds must be invested in conformity with the law in assets which, during the whole period of validity of the bonds, are capable of covering claims attaching to the bonds and which, in the event of failure of the issuer, would be used on a priority basis for the reimbursement of the principal and payment of the accrued interest."

53 See https://www.fca.org.uk/firms/regulated-covered-bonds.

54 EU law refers substantively to covered bonds only in the UCITS Directive, with the sole purpose of demarcating for which types of bonds UCITS investment funds can exceed normal limits on investment in securities issued by a single body (see article 52(4) of the current UCITS Directive). The related regulatory reliefs for banks and insurers refer back to the definition contained in the UCITS Directive.

55 See Commission document COM(2013) 150, "Green Paper: long-term financing of the European economy" (25 March 2013).

56 ESRB Recommendation of 20 December 2012 on the funding of credit institutions (ESRB/2012/2).

whether and how to build a pan-European covered bond framework, building on national regimes that work well" to overcome "obstacles to market depth, liquidity and investor access, in particular on a cross-border basis".

5.18 A public consultation, however, revealed concerns about an overly prescriptive approach at European level:

> "Harmonisation based on a 'one size fits all' approach could impair well-functioning markets and reduce flexibility and the range of products on offer, they also expressed cautious support for targeted EU action, provided that harmonisation is principles-based, builds on existing frameworks and takes account of the specificities of national markets".[57]

5.19 The EBA published its final report on covered bonds in December 2016.[58] It recommended that the European Commission should produce a legal proposal to set 'harmonised minimum quality standards of regulated covered bonds', as well as amendments to banks' ability to claim prudential relief for holding covered bonds under the Capital Requirements Regulation.

5.20 In June 2017, the Commission confirmed that it had decided to prepare a legislative proposal for an EU-level regulatory framework for covered bonds.[59] It also published an outline of the options it had identified for a legislative approach.[60] These included a non-regulatory option; minimum harmonisation requiring modification of existing national regimes; full harmonisation to replace existing national regimes; and a '29th regime', a regulatory framework for a specific covered bond product that would operate in parallel to national regulations. A majority of Member States expressed support for an EU-wide framework based on the EBA's 2016 report (see above), as long as the resulting legislation was "principles-based".[61] The Commission therefore ultimately opted for the 'minimum harmonising' approach, having concluded that maximum harmonisation would unnecessarily disrupt existing, well-functioning national markets (and likely struggle to gain majority approval within the Council).[62]

5.21 In addition to its proposals on covered bonds, the Commission is also in the early stages of preparing additional legislation for a "European Secured Note" (ENS). This would be a debt instrument with the same dual-recourse structure for investors as covered bonds, but with a cover pool consisting of "non-traditional" (i.e. more risky) non-mortgage assets, namely loans to small businesses and infrastructure bank loans. The Commission considers a separate regulatory framework necessary to "protect the strong reputation covered bonds earned in the last decades in European financial markets" from being 'tainted' with the higher risk profile of similar instruments that use lower-quality

57 The outcome of the public consultation is summarised in the Commission's Explanatory Memorandum accompanying its covered bond proposals.
58 See EBA Opinion 2016/23 (20 December 2016).
59 See https://ec.europa.eu/info/sites/info/files/communication-cmu-mid-term-review-june2017_en.pdf.
60 See https://ec.europa.eu/info/law/better-regulation/initiatives/ares-2017–2899641_en.
61 See the Commission proposal for a Directive (COM(2018) 94).
62 Similarly, the Commission concluded that a non-regulatory approach was unlikely to have an effect; and that a '29th regime' for an EU covered bond product would suffer from low uptake. It has proposed parallel product regimes in this way for the pan-European personal pension product (PEPP) and the new Crowdfunding Regulation.

collateral.[63] A dedicated legislative proposal is not expected before the European elections in May 2019, as the Commission has said it will launch a consultation exercise by the end of 2018.

The Commission proposal on covered bonds

5.22 The Commission presented its draft legislation on covered bonds in March 2018, alongside a number of other proposals as part of its Capital Markets Union Action Plan.[64] They are based largely on the recommendations made by the European Banking Authority in 2016.

5.23 As noted, the purpose of the proposals is to encourage the issuance and purchase of covered bonds across the Union, particularly in Member States where no market for them currently exists, and to attract more foreign (i.e. non-EU) investment by offering a standardised European regulatory framework (in the same way that the UCITS Directive does for collective investment funds). This would contribute to increased cross-border flows of capital and investment within the Single Market, and allow issuing banks to fund more loans in support of the wider economy in a "safe and efficient" way.

5.24 The covered bond proposals consist of a Directive, which contains the "core elements" of the new EU-wide minimum standards for covered bonds (to be supervised by Member States' national financial regulators), and a Regulation to amend the existing capital requirements framework to make the prudential relief banks enjoy when investing in covered bonds more restrictive. Issuers which comply with the new framework will be entitled to use the label 'European covered bonds' when marketing their product, in addition to any country-specific designation in use domestically in their home Member State.[65]

5.25 The Economic Secretary to the Treasury (John Glen) submitted an Explanatory Memorandum on the proposals on 11 April 2018.[66] In the section below, we have described the substance of the proposed legislation and the Government's views on the different elements thereof.

Minimum requirements for covered bonds

5.26 The Directive would create minimum standards for any covered bond—which it defines as "debt obligations issued by credit institutions and secured against a ring-fenced pool of assets to which bondholders have direct recourse as preferred creditors"[67]—issued in the European Union. Broadly speaking, these standards would be as described below.

- Given current practice, and the fact that these instruments exist to provide funding for bank loans, the legislation would only allow banks to issue covered

63 According to the Commission, the Member States support this dual approach "subject to clear differentiation of ESNs from covered bonds and further analysis". The European Parliament called for an ENS framework in July 2017.

64 In parallel to the Covered Bonds proposal the Commission also tabled new legislation on crowdfunding, non-performing loans and assignment of claims. We are considering those separately in the near future.

65 Such as German *Pfandbriefe*.

66 Explanatory Memorandum submitted by HM Treasury (11 April 2018).

67 This definition would replace the one currently contained in the UCITS Directive, and the references to it in the Capital Requirements Regulation and the Solvency II Directive.

bonds.[68] The 'European Covered Bond' label, and associated regulatory and prudential reliefs, would be reserved only for instruments issued by EU-based banks (see paragraph 5.31 below for the position of non-EU issuers);

- The Directive lays down statutory minimum requirements with respect to the dual-recourse mechanism that characterises covered bonds, including 'bankruptcy remoteness': if the issuer goes insolvent, the maturity of its covered bonds cannot automatically be shortened. Instead, the secured creditors would be repaid in line with the pre-existing contractual schedule, even in the event of a default;

- The cover pool against which the bonds are secured would be subject to a number of requirements, including one to ensure that only high-quality, low-risk assets are used as collateral; and

- The pool must be more than sufficient to cover all bond liabilities at all times, and be structured in such a way as to guarantee investors' access.[69] The Directive also contains requirements for a cover pool-specific liquidity buffer, and for any 'innovative' structures deployed by the issuer to guard against market risk and the possible erosion of the value of the cover pool.

5.27 In his Explanatory Memorandum, the Minister expresses the Government's support for "additional consistency in the regulatory treatment of covered bonds" given the "existing diversity of legal, regulatory and supervisory covered bond frameworks across the EU". He adds that the Government "will seek to ensure that proposals will enhance comparability, transparency and market stability by helping investors better understand the profile and risks of a programme as they undertake their due diligence".

Relationship with the bank resolution framework

5.28 The low-risk nature of covered bonds is derived from the extra security its holders enjoy even if the issuing bank goes insolvent and defaults on debt payments. However, the proposed legislation would not change national insolvency regimes or the treatment of covered bonds in cases the issuing bank goes insolvent. In particular, the proposal does not alter the 2014 Bank Recovery & Resolution Directive, which excludes the asset pool for covered bonds from being 'bailed in' (i.e. sold) to recapitalise the issuing bank (except for any collateral in excess of what is needed to cover the bond payments).[70] Similarly, derivative contracts included in the cover pool also serve as collateral and cannot be terminated upon the issuer's insolvency or resolution. This seeks to ensure that the cover pool "remains unaffected and adequately funded".

68 The Directive would also allow multiple banks to pool cover assets under certain conditions. This is intended to encourage issuance by smaller banks and give them access to the covered bonds market if they would be unable to accrue sufficient collateral by themselves.

69 For example, in the UK, the cover pool is maintained by a special purpose vehicle (SPV) that is legally separate from the issuing bank.

70 See article 44(2) of the Bank Recovery & Resolution Directive.

Prudential relief for banks

5.29 With respect to the prudential relief for banks that invest in covered bonds, the proposal to amend the Capital Requirements Regulation would introduce new requirements on minimum over-collateralisation and substitution assets:

- to enhance the quality of the covered bonds that receive the favourable capital treatment under CRR, those bonds should be subject to a requirement of a minimum level of over-collateralisation (i.e. the collateral against which they are secured should exceed the value of the outstanding bonds). However, the Regulation would not allow the inclusion of residential or commercial mortgage-backed securities as eligible assets as it this would add "unnecessary complexity to the covered bond programme";

- banks would be subject to loan-to-value (LTV) limits to ensure the credit quality for covered bonds, with respect to the portion contributing to the coverage of liabilities attached to the covered bond; and

- to ensure the prudential treatment of covered bonds issued before the application of the new regulatory framework is not disrupted, they will remain exempted from the requirements on eligible assets, over-collateralisation and substitution assets and remain eligible for the preferential treatment set out in the current Capital Requirements Regulation.

5.30 The Minister's Explanatory Memorandum states that the Government welcomes the "strengthening of the eligibility criteria for qualifying covered bonds to receive preferential treatment", and that it will seek to ensure the new legislation "promotes financial stability, but also provides the necessary incentives to appropriately support covered bonds markets". He also supports the Commission's proposed 'grandfathering' provisions, which will prevent unintended consequences for existing covered bonds from a change in the regulatory regime.

Non-EU covered bonds and non-EU cover assets

5.31 In the context of the UK's withdrawal from the EU, the interaction of the proposed regulatory framework with non-EU covered bond regimes is also pertinent. Under current EU capital requirements rules, banks within the Single Market investing in covered bonds issued outside the European Economic Area (EEA) can in some cases benefit from preferential treatment when determining part of their liquidity buffer.[71] However, this falls short of the full prudential relief available when they invest in EEA-issued covered bonds.

5.32 The new Covered Bonds Directive would apply to EU-based banks only. While the legislation is likely to be extended to Norway, Iceland and Liechtenstein in due course as part of their obligations to adopt the Single Market *acquis* under the EEA Agreement, there is no "equivalence" regime contained in the proposal. As such, the 'European Covered Bond' label, and more importantly the associated regulatory reliefs for financial firms that purchase such bonds, would not apply to non-EEA covered bonds.

71 See Commission Delegated Regulation (EU) 2015/61 (the Liquidity Coverage Requirement Regulation).

5.33 However, the new Directive *would* require the Commission to assess within three years of the new framework becoming operational "whether a general equivalence regime for third-country covered bond issuers and investors is necessary or appropriate". Where equivalence was granted, covered bonds from an 'equivalent' third country would trigger the same prudential and regulatory reliefs as EU bonds. The creation of an equivalence regime, if not included in this proposed Directive by the European Parliament and the Member States in the Council, would require a new legislative proposal in due course.

5.34 The other element of the Covered Bonds Directive that is relevant in the Brexit context is the definition of 'eligible assets' banks could use for the dual recourse mechanism. The proposed legislation would allow banks to include assets in their cover pool for covered bonds that are located outside of the EU, for example loans issued in the UK after it leaves the Single Market. However, individual EU countries would be entitled to prohibit use of non-EU assets at their own discretion. If a Member State does allow it, their national regulator would have to "[verify] whether the assets located outside of the Union meet all the [quality] requirements [that apply to the other assets held in the pool] and that the realisation of such assets[72] is legally enforceable in a way similar to assets located within the Union".[73]

5.35 In sum, for the UK the Directive will have different implications depending on its status in or outside of the Single Market:

- if the Covered Bonds Directive takes effect while the UK is still in the Single Market (which it will be until at least the end of 2020 if the transitional agreement provisionally agreed between the Government and the EU is ratified before March 2019), the Treasury and the Financial Conduct Authority will have to apply the new legislation;
- as a result of the continued Single Market membership, covered bonds issued by British banks would trigger the same prudential and regulatory reliefs of EU banks as those issued in the remaining Member States until the UK leaves the Single Market. Similarly, there would be no restrictions on the ability of issuing banks to include UK-based assets in their cover pool;
- after the UK leaves the Single Market, and barring any agreement with the EU that may require continued regulatory alignment in the area of financial services, the Government would be free to modify the domestic regulatory framework for covered bonds as it sees fit. However, such bonds issued by British banks would no longer entitle EU-based banks to prudential reliefs, reducing their competitiveness within the Single Market. It is not clear if the reliefs would remain available to EU-based banks in respect of bonds issued before the UK leaves the Single Market;
- after the UK leaves the Single Market, whether UK assets can be included in issuing banks' cover pools for covered bonds will depend on the national

72 I.e. the conversion of the assets into cash to pay the holders of a covered bond if the issuing bank is unable to make their contractual debt payments.

73 See article 7 of the proposed Directive: "Member States may allow credit institutions issuing covered bonds to include assets located outside of the Union in the cover pool. (…) Where Member States allow for [their] inclusion (…), they shall ensure investor protection by verifying whether the assets located outside of the Union meet all the requirements set out in Article 6 and that the realisation of such assets is legally enforceable in a way similar to assets located within the Union".

legislation of the EU country where the bank is based. In any event, inclusion of such assets will be subject to additional compliance requirements to ensure they meet the Directive's asset eligibility requirements and can be converted into cash "in a way similar to assets located within the Union";

- however, if the Treasury were to seek 'equivalence' between the EU's and the UK's covered bonds regime (should this become possible under the Covered Bonds Directive), its practical room to make amendments to domestic UK regulations on covered bonds would likely be constrained, unless it was willing to see the equivalence decision revoked by the European Commission.

5.36 In his Explanatory Memorandum the Minister only "notes the Commission's openness to develop a third country equivalence framework in the future", but does not indicate whether the Government will push for the inclusion of an equivalence regime at this stage. He does not indicate how the Government's recent high-level proposal for a new trade agreement on financial services with the EU, based on bilateral market access and mutual recognition of regulatory standards without legislative harmonisation,[74] could impact on the UK's regulation of covered bonds. The Committee will continue to monitor developments in the trade negotiations with the EU closely to ensure that any commitments the Government may enter into for continued *de facto* application of EU legislation are identified as they arise and any such requirements for alignment made subject to parliamentary scrutiny.

Previous Committee Reports

None. These are new proposals.

74 See for more information the speech by the Chancellor of the Exchequer, "Chancellor's HSBC speech: financial services" (7 March 2018).

6 Crowdfunding and P2P lending: new EU regulatory framework

Committee's assessment	Politically important
Committee's decision	(a) Not cleared from scrutiny; further information requested; drawn to the attention of the Treasury Committee; (b) Cleared from scrutiny
Document details	(a) Proposal for a Regulation on European Crowdfunding Service Providers (ECSP) for Business; (b) Proposal for a Directive amending Directive 2014/65/EU on markets in financial instruments with respect to crowdfunding
Legal base	Article 114 TFEU; ordinary legislative procedure; QMV
Department	Treasury
Document Numbers	(a) (39550), 7049/18 + ADDs 1–3, COM(18) 113; (b) (39551), 7048/18 + ADDs 1–2, COM(18) 99

Summary and Committee's conclusions

6.1 Crowdfunding is a relatively new form of financing, where an online platform or intermediary connects investors—often individual savers—with counterparts looking for funding. The most common forms are peer-to-peer (P2P) lending, where businesses or consumers are provided with a loan and the investors receive debt repayments, and investment-based crowdfunding, where investors bet on a business generating a cash flow in the future by buying investments such as shares or debt securities. British platforms are by far the most prolific European crowdfunding 'hubs': of the €4.2 billion (£3.6 billion)[75] raised through crowdfunding in the EU in 2015, 80 per cent was raised in the UK.

6.2 In March 2018 the European Commission proposed a new Regulation to create an EU-level regulatory framework for investment- and loan-based crowdfunding platforms that provide funding for businesses, referred to as the "European Crowdfunding Service Provider" (ECSP) label.[76] The proposal is part of both the EU's Capital Markets Union work programme and the Commission's recent Fintech Action Plan.[77]

6.3 The objective of the Regulation is to allow crowdfunding platforms to solicit investments from investors across the EU after being authorised to do so centrally by the European Securities & Markets Authority (ESMA). This, the Commission argues, would enable them to maximise economies of scale by expanding across national borders and increasing their ability to provide capital to European businesses.[78] Authorisation as an

75 €1 = £0.88415 or £1 = €1.13103 as at 28 February.

76 See Commission document COM(18) 133.

77 The Committee will consider the European Commission's Fintech Action Plan and its latest progress report on the Capital Markets Union separately in the near future, when it has received the Explanatory Memoranda from the Treasury setting out the Government's views and position.

78 The ECSP regime would not apply to crowdfunding platforms which lend money to consumers, as such activity is regulated separately by the Consumer Credit Directive.

ECSP by ESMA would be conditional on the platform meeting a number of organisational, governance and conduct requirements, but no specific capital buffers or other prudential requirements.

6.4 However, platforms could *only* apply for the ECSP label if they do not already hold authorisation to provide crowdfunding services under national law (to avoid interfering in functioning domestic regulatory frameworks), or provide wider investment services under the Markets in Financial Instruments Directive (to avoid firms avoiding the stricter requirements of that Directive, which covers many more investment services than facilitating crowdfunding).[79] The ECSP authorisation would also not cover peer-to-peer lending to consumers, which are already covered by specific legislation governing consumer credit,[80] or any crowdfunding projects seeking to raise more than €1 million (£880,000), which is the point at which EU law requires a formal prospectus to be issued to prospective investors.[81]

6.5 We have set out the substance of the proposal, and the restrictions on platforms that seek ECSP authorisation, in more detail in "Background" below.

6.6 The implications of the proposal for the UK, in the context of Brexit, remain unclear. Under the terms of the proposed Regulation, the ESCP 'passport' would only be available to companies based in the EU. Although the Commission notes in the accompanying Impact Assessment that the withdrawal of the UK—as the EU's largest hub for crowdfunding—"raises questions about the need for a (…) framework to assess the equivalence of a third country regime",[82] the draft legislation itself contains no provisions on equivalence mechanism to extend the passport to non-EU crowdfunding platforms.[83] However, the proposal would permit EU-based platforms to delegate part of their operations to a third party outside the Union, provided it does "not impair materially" the crowdfunding service provider's compliance with its obligations as an ESCP.

6.7 The Government supports efforts to increase the reach of crowdfunding platforms across the EU, but has expressed concerns about the substance of the Commission proposal. The Economic Secretary to the Treasury (John Glen) submitted an Explanatory Memorandum[84] on 27 March 2018, in which he lists a number of areas where the Government will seek changes to the legal text. These include the need to differentiate between investment- and loan-based crowdfunding, given their different business models; ensuring companies cannot use the ECSP regime to escape stricter domestic regulation when offering crowdfunding services; a larger role for domestic regulators in supervising the new regime; and the inclusion of proportionate prudential requirements for crowdfunding platforms as a pre-condition for their authorisation as an ECSP.[85] With

79 To ensure authorization under the ECSP Regulation and MiFID II are mutually exclusive, the proposed Regulation is accompanied by a draft Directive making consequential amendments to MiFID II.

80 In particular, the Consumer Credit Directive and the Mortgage Credit Directive.

81 See Regulation 2017/1129.

82 See Commission Impact Assessment (SWD(2018) 562), p.37.

83 'Equivalence' in EU financial services legislation allows the European Commission, with the support of a qualified majority of Member States, to recognise the regulatory regime of a non-EU country in a specific area of financial services as 'equivalent'. Such decisions are made at the EU's sole discretion and can be unilaterally revoked with a month's notice. The effect of 'equivalence' differs for each sector; for example, it can grant preferential market access or trigger prudential reliefs for EU-based financial services providers that deal with providers in the 'equivalent' country.

84 Explanatory Memorandum submitted by HM Treasury (27 March 2018).

85 We have described the Government's concerns in more detail in "Background" below.

respect to the consequences of the proposal in the context of the UK's EU exit, the Minister says that "the applicability of the proposed Regulation [after Brexit] will depend on the future relationship between the UK and the EU, which is subject to negotiations".

6.8 **Given that the UK is home to 80 per cent of all crowdfunding activity in the EU, the proposal is clearly of political importance. The Minister's Explanatory Memorandum sets out a number of substantial concerns about the content of the Commission proposal, with which we concur. Careful drafting will be necessary to ensure that the European crowdfunding regime cannot be used to circumvent domestic regulation aimed at protecting investors, which in itself will require a greater role for national authorities in supervising platforms with ECSP authorisation.**

6.9 **Irrespective of the proposal's substance, we cannot yet say whether the new Regulation will apply in the UK. This is due to both the uncertainty about the timetable for adoption of the legislation, and the Government's continued ambiguity about the length of the post-Brexit transitional period (during which the UK will stay in the Single Market, and bound by all EU law).[86] As a result, we do not know whether, and if so for how long, the UK and its crowdfunding industry might be covered by the new ECSP regime. Although it is unlikely the Regulation will take effect before early 2020, there is a distinct possibility that the ECSP regime will be binding on the UK during the transitional/implementation period.**

6.10 **Moreover, the Government is pushing for an ambitious agreement to replace the current Single Market 'passporting' arrangements for various parts of the financial services industry. It is not yet known what provisions such an agreement could contain on continued regulatory alignment between the UK and the EU. The Government is pressing for mutual recognition of regulatory standards without legal harmonisation, whereas the EU has so far refused to countenance preferential market access for the UK other than through its established 'equivalence' regimes (which is not included in the Commission proposal for the Crowdfunding Regulation, although it could be introduced by the European Parliament or the Member States as part of the legislative process).[87]**

6.11 **While both approaches have in common that neither side would be *required* to adopt the regulatory standards of the other party, the practical impact on cross-border flows of financial services would be very different. The UK is seeking a regime which operates on the basis of a general presumption of preferential market access unless there is a determination to the contrary (because of divergent regulatory outcomes); the remaining Member States envisage a regime where there is no general presumption of preferential market access for financial services. In the latter case preferential market access would be accorded only on a case-by-case basis and at the EU's own discretion (and subject to unilateral revocation) under existing 'equivalence' regimes. In this case, reliance on such an arrangement—especially in areas where UK financial services providers have a large EU client base and therefore an economic interest in**

86 Although the other Member States have proposed the transitional arrangement should end on 31 December 2020, the Government's position is that "the Period's duration should be determined simply by how long it will take to prepare and implement the new processes and new systems that will underpin the future partnership".

87 See "x" above on the possibility of an equivalence regime for third countries under the Regulation.

maintaining equivalence indefinitely—may lead to the Government having to keep in step with developments in EU regulation after Brexit, without a formal say over its substance.[88]

6.12 **Given the political and legal consequences of the final outcome of the Government's negotiations with the EU in this area, over the coming months we will continue to monitor to what extent the UK may either, as a legal requirement or voluntary, continue aligning itself with EU financial services legislation so as to secure continued market access (including for its crowdfunding providers under the proposed ECSP Regulation).**

6.13 **With respect to the Crowdfunding Regulation specifically, we ask the Minister to keep us informed of developments in the legislative process. We will consider in more detail its implications when the Minister is able to provide us with further information on the legislative process. We also ask the Minister to clarify whether the Government intends to push for the inclusion of an equivalence regime under the Regulation, so that the UK—if necessary—could apply to stay part of the ESCP regime after it leaves the Single Market (if such market access cannot be secured through a bilateral trade agreement).**

6.14 **In the meantime, we retain the proposed Regulation under scrutiny and draw it to the attention of the Treasury Committee. We are content to clear the Directive amending MiFID II from scrutiny as it is consequential on the main Regulation and not independently politically important.**

Full details of the documents

(a) Proposal for a Regulation on European Crowdfunding Service Providers (ECSP) for Business: (39550), 7049/18 + ADDs 1–3, COM(18) 113; (b) Proposal for a Directive amending Directive 2014/65/EU on markets in financial instruments: (39551), 7048/18 + ADDs 1–2, COM(18) 99.

Background

6.15 Crowdfunding is a relatively new form of financing, where an online platform or intermediary connects investors—often individual savers—with small businesses and consumers looking for funding. The two main forms are investment-based crowdfunding, where investors buy shares or debt in a firm; and peer-to-peer (P2P) lending, where investors loan money directly to a firm or consumer.[89]

6.16 In recent years, crowdfunding has emerged as a significant non-bank source of capital for companies and consumers in the EU. Across the Union there are now more than 500 crowdfunding platforms, but activity is heavily concentrated in the UK: it accounts

88 The Committee remains to be persuaded that the other Member States are likely to accept the UK's proposal for mutual recognition (given their interest in having regulatory oversight over the financial infrastructure and systems that underpin their economy, even if it comes at a higher cost to businesses), or that this new arrangement—given its unprecedented nature and far-reaching regulatory and economic consequences—could be negotiated and take effect by January 2021, when the UK is scheduled to leave the Single Market and lose its current market access rights.

89 There are also other varieties, including the trading of invoices, as well as reward- and donation-based crowdfunding.

for approximately 80 per cent of the entire EU crowdfunding market. In 2016, peer-to-peer business lending (including property loans) amounted to €3.5 billion (£3.1 billion), making it the largest market segment by volume. P2P consumer credit totalled just under €2 billion (£1.7 billion), while investment-based crowdfunding attracted investments worth approximately €750 million (£654 million).

6.17 While opening up new channels of funding for the economy, crowdfunding also poses a number of risks to investors. Investments are often illiquid and high-risk, as there may not be a secondary market and the funding recipients are usually new companies with a high failure rate. Where the platform solicits investment from individual savers, there is also an information asymmetry that makes it difficult for investors to assess the risk they are taking with their money. Investor compensation schemes do not typically cover investments made through crowdfunding platforms, and in any event would not compensate for losses due to investment risk. Additionally, investors could lose out if the platform holds their assets but becomes insolvent. The crowdfunding sector's financial stability risks are currently considered low, given the overall size of the market.

Existing EU and UK legislation that applies to crowdfunding

6.18 Currently, there is no European legal framework which deals specifically for lending-based crowdfunding where the loan is provided to a business (as commercial lending is not regulated by the EU), while lending to consumers is regulated by the Consumer Credit Directive. The UK's Financial Conduct Authority (FCA) launched a bespoke regulatory framework for peer-to-peer lending platforms in April 2014.[90]

6.19 For investment-based crowdfunding, a number of Member States use the framework created by existing EU legal frameworks, including primarily MiFID, but also the Payment Services Directive or the Alternative Investment Fund Managers Directive). Approximately 40 per cent of investment-based platform operators in the EU already hold a MiFID licence (either directly or via a parent firm). The UK does not have a bespoke regime for investment-based crowdfunding, but has implicitly regulated the underlying activities under MiFID II, with the regulator deciding which specific permissions are needed based on the an individual platform's operations.

A new European regulatory approach to crowdfunding

6.20 The Commission in March 2013 published a Green Paper on the "long-term financing of the European economy".[91] This indicated the possibility of further measures aimed at "developing or promoting other 'non-traditional' sources of finance", including "internet-based sources of funding like crowdfunding". In response, the EU's Heads of State and Government in June 2013 called on the Commission to "develop alternative sources of financing in close cooperation with Member States".[92]

6.21 The EU market for this new type of financing remains underdeveloped compared to other major economies.[93] In October 2013, the European Commission launched

90 See FCA Policy Statement PS14/4, "The FCA's regulatory approach to crowdfunding over the internet, and the promotion of non-readily realisable securities by other media" (March 2014).

91 Commission document COM(2013) 150, "Green Paper: Long-term financing of the European economy".

92 European Council conclusions of 27–28 June 2013.

93 See Commission Impact Assessment SWD(2018) 56, p. 18.

a dedicated consultation on the "potential added value of EU action" in the area of crowdfunding.[94] This was followed in March 2014 by a policy paper[95] which mentioned the potential of an 'EU quality label' for crowdfunding platforms, an initiative for which the then-Coalition Government told our predecessors at the time that a case "[had] not been made" given the embryonic state of the sector.[96] That year also saw the establishment of the 'European Crowdfunding Stakeholder Forum' to discuss matters of interest to the industry and regulators at EU-level.[97] It has not met since February 2016.

6.22 The European Securities & Markets Authority (ESMA) issued advice on investment-based crowdfunding in December 2014.[98] It concluded that many platforms were deliberately structuring their business models to avoid regulatory requirements under MiFID II, leading to "significant risks to investors" not addressed at EU level. It also argued that the lack of a standardised European regulation hampered crowdfunding platforms from offering their services across borders within the Single Market, raising compliance and operational costs and restricting opportunities for expansion.

6.23 In September 2015 the European Commission published an Action Plan for a European "Capital Markets Union" (CMU).[99] The threefold objective of the CMU was to provide new sources of funding for EU businesses, help increase opportunities for yield for savers, and make the economy more resilient by making Europe's economy less reliant on bank lending. The Action Plan set out a number of policy measures to achieve these ambitions, including an undertaking to assess the need for further policy measures in the area of crowdfunding, with a view to developing the "best means to enable the development of this new funding channel across the [EU]".

6.24 In May 2016 the European Commission published a second, more detailed policy paper on crowdfunding.[100] It concluded that this form of alternative finance could make a "significant contribution" to the CMU objective mobilising new sources of capital for European businesses, and that it would further consider its policy approach to crowdfunding "as part of our broader approach to FinTech and the digitalisation of financial services". However, it concluded that, "given the predominantly local nature of crowdfunding" and the need for the sector to have "space to innovate and develop", there was "no strong case for EU level policy intervention at this juncture".

6.25 In November 2016 the Commission tendered for a study on "assessment of the potential for development of cross-border crowdfunding business, and how existing EU legislation applies and interacts with existing and upcoming national regulatory

94 Commission consultation "Crowdfunding in the EU—Exploring the added value of potential EU action" (3 October 2013).

95 Commission document COM(2014) 172, "Unleashing the potential of Crowdfunding in the European Union".

96 Explanatory Memorandum submitted by HM Treasury (April 2014).

97 At present, both NESTA and Peer-to-Peer Finance Association (P2PFA) are UK members of the Forum. It appears likely they will forfeit their places when the UK ceases to be a Member State as members must be "organisations established in a Member State of the European Union".

98 https://www.esma.europa.eu/sites/default/files/library/2015/11/2014–1378_opinion_on_investment-based_crowdfunding.pdf.

99 See Commission document COM(2015) 468. For more information on the CMU, see the previous Committee's Report of 21 July 2015. In parallel, the Commission also pursued further regulatory measures to stabilise the European banking sector (the so-called 'Risk Reduction Measures') and improve its capacity to lend by improving the transparency of the securitisation of debt instruments, and creating a new EU legislative framework for a special type of security called a 'covered bond'. The proposal for the latter was tabled in March 2018, which we consider in a separate chapter in this Report.

100 See SWD(2016) 154, "Crowdfunding in the EU Capital Markets Union".

frameworks in cross-border situations". As part of the mid-term review of its 2015–2019 Capital Markets Union Action Plan, the Commission launched a consultation in March 2017 on ways in which the EU should approach 'fintech', including crowdfunding.[101] This asked stakeholders, among other things, how the EU could "support further development of […] non-bank financing, i.e. peer-to-peer/marketplace lending [and] crowdfunding". The Commission said the responses to this consultation showed broad support for regulatory intervention at EU-level to:

- address the market fragmentation and potential for regulatory arbitrage within the Single Market for crowdfunding and P2P platforms that have resulted from divergent national regimes;
- ensure platforms that want to connect investors and businesses across the EU compete on a regulatory level playing field to increase competition, which in turn would lead to more choice for savers and improved funding options for businesses;
- put in place EU-level disclosure requirements to ensure savers understand the risks associated with their investments through platforms; and
- prevent financial integrity risks by imposing regulatory requirements with respect to the governance of crowdfunding platforms.

6.26 By October 2017 the Commission had therefore decided to press ahead with a legislative proposal on an EU-level framework for crowdfunding and P2P platforms.[102] That month, it stated such a framework would enable platforms to become a more important source of market-based financing by allowing them to seize opportunities for economies of scale offered by the Single Market as a whole. The Commission argues the case for EU-level intervention changed because, since May 2016, it had "gathered additional evidence on the demand for cross-border activity and on the barriers in the Single Market through stakeholder consultations and external studies". It also concluded that the concentration of the European crowdfunding sector in a few Member States only had "underlined the need to make this funding method available more widely, notably for the benefit of fund seekers and investors in smaller Member States". It identified three possible policy options, each of which required some level of regulatory harmonisation:

- establishing minimum regulatory standards are combined with self-regulatory efforts by the industry;
- bringing crowdfunding within the existing EU single rulebook, under different regimes for investment and lending-based crowdfunding activities (MiFID II for the former, and a new regime for credit intermediation for commercial lending for the latter); or
- creating a voluntary EU-wide regulatory regime for crowdfunding and P2P lending which would operate separately from national regimes (but under which platforms could choose to operate under their domestic regulatory regime or the new EU-level regime, but not both simultaneously).

101 European Commission consultation, "FinTech: a more competitive and innovative European financial sector" (23 March 2017).

102 http://ec.europa.eu/info/law/better-regulation/initiatives/ares-2017–5288649_en.

6.27 In November 2017 the European Commission presented the policy options it had identified to the Member States. Most of them "supported a regulatory approach at the EU-level" for crowdfunding, although two Member States—including the UK—"were sceptical about the usefulness of EU legislation in this field."[103] The UK Government's principal objection to the initiative was that

> "Member States have been best placed to determine how to balance the need for regulation to protect consumers, without being overly restrictive and preventing viable companies from accessing funds and firms from innovating; as markets are currently domestically focused, a bottom-up approach has seemed most logical."

6.28 The Treasury also raised a number of specific concerns with the Commission, namely:

- a regulatory distinction should be made between investment-based crowdfunding and peer-to-peer lending, given the differences in their respective business models and activities;
- more clarity was needed on how any proposed framework would interact with existing EU legislation affecting crowdfunding, especially investment-based crowdfunding under MiFID II; and
- the Commission should clarify "what services a cross-border framework could provide beyond what is already provided for in EU law" with respect to investment-based crowdfunding, as the Government took the view that Article 34 of MiFID II already permitted crowd-funders to provide "relevant services" cross-border into another Member State.

The Commission proposal

6.29 The Treasury's concerns notwithstanding, the European Commission presented a proposal to establish a voluntary pan-EU regulatory regime for crowdfunding service providers in March 2018. It was part of a larger 'Action Plan' on fintech, which announced a number of "targeted initiatives for the EU to embrace digitalisation of the financial sector".[104]

6.30 The policy option chosen by the Commission (see paragraph 6.24 above) is a stand-alone voluntary European crowdfunding regime. This would enable platforms to apply for the status of "European Crowdfunding Service Provider" (ECSP), which would allow a firm to provide both crowdfunding and peer-to-peer lending in their home EU country, and on a cross-border basis in any other Member State (the so-called 'passport'). It would exist in parallel to existing national regulatory regimes, but a firm could only be authorised to perform crowdfunding services under either domestic law[105] *or* the new ECSP Regulation. A licence from a national regulator, with the attendant regulatory requirements as prescribed by domestic law, would therefore preclude a platform from seeking authorisation to use the ECSP 'passport'.

103 http://ec.europa.eu/transparency/regexpert/index.cfm?do=groupDetail.groupMeetingDoc&docid=9267.

104 See Commission document COM(2018) 109.

105 Many Member States regulate crowdfunding under their national transposition of existing EU, such as MiFID II, the Payment Services Directives or the AIFMD.

6.31 The Commission dismissed the option of a more prescriptive regulatory approach that would have brought crowdfunding within the EU's harmonised rulebook for financial services, because this was "not as cost effective […] while achieving similar results in terms of integrity and transparency" as its chosen approach, especially as it would have required the EU to regulate credit intermediation for business customers for the first time.

Details of the Commission proposal

6.32 As noted, the Regulation is not a harmonising proposal, in the sense that it would not replace national rules on crowdfunding where they exist in the Member States.[106]

Parallel EU and domestic crowdfunding regimes

6.33 Under the terms of the proposal, a crowdfunding service provider could choose to either provide or continue providing services on domestic basis under applicable national law (including where a Member State chooses to apply MiFID II to crowdfunding activities), *or* seek authorisation to provide crowdfunding services as an ECSP under the proposed Regulation across the EU (including in its home Member State).

6.34 To ensure firms have to select either their domestic regulatory regime or the new EU passport, the proposal stipulates that authorisation under the Regulation cannot be granted to crowdfunding or P2P platforms which:

- provide investment services using national authorisation under the second Markets in Financial Instruments Directive (Directive 2014/65/EU); or
- provide crowdfunding services under a regulatory authorisation granted for that purpose by the national law of a Member State.

6.35 The legal consequence is that the new EU-level framework would be available only to firms that exclusively provide crowdfunding services, and prevent platforms from being covered by overlapping national and EU regulations concurrently. The Commission has proposed consequential amendments to the second Markets in Financial Instruments Directive (MiFID II) that would explicitly exclude any crowdfunding platforms subject to the new EU-level regulatory regime from the scope of that Directive.

Crowdfunding services covered by the ECSP regime

6.36 The proposal only applies to those crowdfunding services entailing a financial return for investors, i.e. equity and debt crowdfunding, where the investors purchase a stake in the success of a company or issue it with a loan agreement, respectively. The ECSP authorisation would therefore not cover donation- and rewards-based crowdfunding. The Commission has proposed a legal definition of crowdfunding services as "the facilitation and granting of loans" and "the placing without firm commitment of transferable securities and the reception and transmission of client orders". These definitions are purposefully restrictive, in a bid to mitigate the risk of regulatory arbitrage for more complex financial services—such as portfolio management and investment advice—which platforms

106 However, as a Regulation, it would—once adopted—not provide individual EU countries with any leeway in setting additional conditions before platforms with authorisation under the legislation, even if established in another Member State, could provide services within their territory.

sometimes add on top of these services.[107] In this way, providers could not escape more onerous regulation for these services under MiFID II by applying for authorisation as an ECSP.

6.37 However, within those parameters the Regulation would still not apply to peer-to-peer lending where the recipient of the funding is a consumer, as the provision of consumer credit is regulated separately.[108] Similarly, it would not apply to crowdfunding offers for which a platform wants to raise more than €1 million (£880,000), the threshold above which it is required for the business to issue a formal prospectus to investors under EU law.[109]

The role of the European Securities & Markets Authority

6.38 In order to benefit from the ECSP 'passport' created by the Regulation, a platform would have to apply for authorisation from the European Securities & Markets Authority (ESMA).

6.39 ESMA could only grant a licence if the applicant meets a number of substantive governance, organisational and conduct requirements, including avoidance of conflicts of interest, safekeeping of customers' assets, and dispute resolution. However, the Commission has not proposed that ECSPs should hold any regulatory capital of their own, given that the platforms operate "services that do not warrant prudential treatment for minimal operational and continuity risk" and do not pose a risk to financial stability, given the relatively small volume compared to capital markets as a whole. Payments for crowdfunding transactions must take place via entities that are authorised under the Payment Service Directive (PSD) and, therefore, subject to the 4th Anti-Money Laundering Directive (AMLD), whether the payment is provided by the platform itself or by a third party.[110]

6.40 EMSA would maintain a public register of all successful applications, whose authorisation would entitle them to carry out crowdfunding activities in any EU Member State without needing to seek permission from domestic regulators or establish a physical presence anywhere but their host Member State.

Investor protection

6.41 While marketing of crowdfunding services under the ECSP label would remain subject to the national legislation of each Member State in which it is carried out, the Regulation would at a minimum require platforms to undertake an "initial assessment of appropriateness of a potential client", offer investors the possibility of "[simulating] their

107 The draft Regulation also limits the scope of the new framework to crowdfunding platforms operating a primary market for investments. Should investors wish to sell their investments via a secondary market, the platform is limited to providing a "bulletin board" which facilitates contact between investors but does not itself provide a platform for the execution of trades.

108 'Consumer' would be defined as in article 3 of the Consumer Credit Directive (Directive 2008/48/EC): "A natural person who (…) is acting for purposes which are outside his trade, business or profession".

109 See the Prospectus Directive (Directive 2003/71/EC), which will be replaced by the Prospectus Regulation (Regulation 2017/1129) as of 21 July 2019.

110 In the longer term, the Commission will assess the necessity and proportionality of subjecting crowdfunding service providers to obligations for compliance with the national provisions implementing Directive (EU) 2015/849 in respect of money laundering or terrorism financing and adding such crowdfunding service providers to the list of obliged entities for the purposes of Directive (EU) 2015/849.

ability to bear losses". Crowdfunding providers would also have to issue a Key Investment Information Sheet to investors, with details of the investment offer for either equity- or loan-based crowdfunding campaigns for which they are seeking contributions.[111]

Recognition of non-EU crowdfunding regimes

6.42 The European Commission has noted that Brexit could require an 'equivalence' mechanism to allow British crowdfunding intermediaries to continue servicing EU-based customers, because so much crowdfunding activity in Europe is carried out through UK-based platforms:[112]

> "Without a functioning third country regime, the departure of the UK from the EU poses the risk of leaving the EU with even lower scale to deal with the cross-border provision of early stage financing for businesses across Europe. It also raises questions about the need for a more uniform approach to provide a framework to assess the equivalence of a third country regime."

6.43 However, the Regulation as proposed by the Commission does *not* make provision for the extension of the 'passport' to non-EU crowdfunding platforms, or otherwise cover non-EU intermediaries.[113] As such, British platforms would not be able to apply after the UK leaves the Single Market (whether in March 2019 or at the end of any subsequent transitional period under the Withdrawal Agreement), and any that might have successfully applied for it by then will automatically lose their passport when EU law ceases to apply to the UK. The proposal does permit EU-based platforms to delegate part of their operations to a third party outside the Union, provided it does "not impair materially the quality of the crowdfunding service providers' internal control and the ability of ESMA to monitor the crowdfunding service provider's compliance with all obligations laid down in this Regulation".

The Government's view

6.44 In its initial comments on the Commission's broad approach to regulation of crowdfunding, circulated in November 2017 (see paragraph 6.26 above), the Treasury warned that an 'opt-in' regulatory regime, where holding a EU licence would allow platforms to avoid having to hold a domestic licence, could lead to problems if the EU-level framework was "perceived as less strict than national regimes", as this could incentivise companies to apply for an EU licence to avoid existing national regulations.

6.45 Following formal publication of the legislative proposal, the Economic Secretary to the Treasury (John Glen) submitted an Explanatory Memorandum on the proposal on 27 March 2018.[114] In it, he noted that the Government believes that "increased cross-border activity is one possible way that crowdfunding platforms could continue to grow and

111 file:///Users/fnoppert/Downloads/PART-2018–141058V1%20(6).pdf

112 See Commission Impact Assessment (SWD(2018) 562), p. 36.

113 Article 4 of the proposed Regulation states that only crowdfunding platforms "provided by legal persons that have an effective and stable establishment in a Member State of the Union" can apply for the new 'passport'. As a Single Market measure, the legislation is expected to be extended to Norway, Iceland and Liechtenstein in due course as well.

114 Explanatory Memorandum submitted by HM Treasury (27 March 2018).

support small businesses", but—as home to the EU's largest crowdfunding industry—it also has a "number of concerns" with the proposal. These largely reflect the concerns the Treasury already expressed to the Commission in its feedback in November 2017.

6.46 In summary, the Government will seek the other Member States' support for amendments as follows:

- the difference between investment- and lending-based crowdfunding should be recognised by giving them separate regulatory regimes, which the proposed Regulation does not currently do. The Minister says that this fails to acknowledge the "complexity of some business models, especially those of P2P lending platforms";
- the legal definition of 'crowdfunding' needs to be changed so it does not either "exclude platforms with a more complex model from benefitting from the ECP" or, conversely, "allow more complex firms to operate in a 'lighter touch' regulatory regime, without some of the safeguards that the UK has in place";
- there should be no role (or a much more limited one) for the European Securities & Markets Authority in supervising the new EU-level regulatory regime. The Government wants national competent authorities to be primarily responsible for supervision of crowdfunding platforms (whether regulated under domestic or EU law), given that the UK has a "well-established and internationally respected regimes for investment-based crowdfunding and P2P lending". The UK has particular concerns about giving ESMA a supervisory role even for crowdfunding platforms that apply for the European label but only operate in one Member State;
- with respect to the proposed disclosure requirements for ECSPs and their investors, the Government believes a UK-style "principles-based" approach would be "more appropriate". The Minister says it would ensure transparency "without being overly prescriptive", calling the Commission proposal potentially burdensome for platforms, borrowers and investors; and
- in one respect the Government believes the proposal does not go far enough: the Commission has not proposed any prudential requirements, whereas the UK believes that sustainable growth in the sector requires "appropriate levels of regulatory capital" without posing an unnecessary market entry barrier. In the UK, P2P platforms need to hold capital of at least £50,000.

6.47 The Government has also expressed concern about the proposed limit of €1 million (£885,000) for fundraisers that are carried out under the ECSP label. It says this limit would mean that the large majority of platforms currently operating in the UK would be dual-regulated if they sought to apply for authorisation under the new EU-wide framework, as any crowdfunding campaigns seeking investment above that threshold would fall outside the scope of the EU-wide regime and remain regulated by the FCA.[115] It is not clear whether it will press for this limit to be raised, or removed altogether.

115 According to the Commission, the average deal size for investment-based crowdfunding platforms "is well over €600,000" (£524,000).

6.48 With respect to the consequences of the proposal in the context of Brexit, the Minister says that there "are no direct EU-exit implications", because once the UK has left the EU (or, more pertinently, the Single Market at the end of the post-Brexit transitional period), "the applicability of the proposed Regulation will depend on the future relationship between the UK and the EU, which is subject to negotiations". He also refers to the Commission's Impact Assessment, which states that after the UK leaves the EU, 'third country' rules may be required to ensure that crowdfunding services are not interrupted.

Previous Committee Reports

None. This is a new proposal for legislation.

7 EU approval of the Global Compact on Migration

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 and the International Development Committees
Document details	(a) Proposal for a Council Decision authorising the Commission to approve, on behalf of the Union, the Global Compact for Safe, Orderly and Regular Migration in the field of development cooperation; (b) Proposal for a Council Decision authorising the Commission to approve, on behalf of the Union, the Global Compact for Safe, Orderly and Regular Migration in the area of immigration policy
Legal base	(a) Article 16 TEU and Article 209 TFEU, QMV; (b) Article 16 TEU and Article 79 TFEU, QMV
Department	Home Office
Document Numbers	(a) (39583), 7400/18 + ADD 1, COM(18) 167; (b) (39584), 7391/18 + ADD 1, COM(18) 168

Summary and Committee's conclusions

7.1 The United Nations Refugee Agency reports that by the end of 2016, 65.6 million individuals were forcibly displaced worldwide as a result of persecution, conflict, violence or human rights violations, 22.5 million were refugees, the highest level ever recorded. The vast majority (84%) are hosted by developing regions.[116] In September 2016 the United Nations General Assembly adopted the New York Declaration for Refugees and Migrants which recognises that large-scale movements of refugees and migrants are a "global phenomena that call for global approaches and global solutions". The Declaration sets out a process for international negotiations which will culminate in the adoption of a Global Compact for Safe, Orderly and Regular Migration ("the Global Compact on Migration") in December 2018 establishing "a framework for comprehensive international cooperation on migrants and human mobility".[117]

7.2 A first draft of the Global Compact was published in February followed by a revised draft ("zero draft plus") in March and intergovernmental negotiations are underway to agree the final text.[118] The European Commission considers that active engagement and a "unified EU approach" during the preparatory stages have resulted in a draft text which largely reflects EU policy on migration. It has proposed two Council Decisions which

116 See UNHCR Global Trends Forced Displacement in 2016.
117 See the text of the New York Declaration for Refugees and Migrants agreed on 19 September 2016.
118 The latest version of the text—"zero draft plus"—is attached to the proposed Council Decisions (see ADD 1).

would give it the authority to approve the Global Compact on behalf of the EU at the intergovernmental conference in December. The first—document (a)—would cover the development policy elements of the Global Compact and the second—document (b)—the immigration policy elements. Two Decisions are needed as the UK's Title V (justice and home affairs) opt-in applies to document (b) dealing with immigration, meaning that the UK is not bound to participate in the second Council Decision unless it chooses to opt in but will be bound by the first Decision if it is adopted.

7.3 The European Commission considers that the Council can give the authorisation it seeks to approve the Global Compact on Migration under the powers conferred by Article 16 of the Treaty on European Union (TEU) which provide that the Council shall exercise "policy-making and coordinating functions". It says it is seeking authorisation so far in advance of the intergovernmental conference in December because it believes that the EU's influence can be exercised most decisively during the early stages of negotiation on a final text. It undertakes to cooperate closely with Member States and revert to the Council if the final text of the Global Compact on Migration diverges substantially from the latest draft text (which is attached to both of the proposed Council Decisions).

7.4 The Immigration Minister (Caroline Nokes) says that the UK has worked constructively with the European Commission and EU Member States to shape the early drafts of the Global Compact on Migration and that their positions are closely aligned. Even if the Government decides not to opt into the proposed Council Decision concerning the immigration aspects of the Global Compact—document (b)—the UK will still be bound by the proposed development cooperation Decision—document (a)—and so will be able to attend and influence EU coordination meetings within the United Nations and negotiate as part of the EU block.[119] She sets out the factors that will inform the Government's opt-in decision but indicates that a decision not to opt into document (b) is unlikely to have a negative political impact.

7.5 The Minister explains that there is some uncertainty as to the procedures that the Commission should follow to obtain the Council's authorisation to approve the Global Compact on Migration and some doubt whether the proposed Council Decisions will be put to the vote. The Commission has cited Article 16 TEU as the procedural legal base for both proposals. This is because the Commission considers that the usual procedures for negotiating, signing and concluding international agreements or establishing the EU's position in an international body (set out in Article 218 TFEU) do not apply as the Global Compact will not create any legal obligations under domestic or international law.[120] The Commission relies on Court of Justice case law to support its position.[121] The Minister says "this is the first time the Commission has taken this approach in using Article 16 TEU" and that the Government "is considering its position on whether we agree with this approach".[122]

7.6 **The Minister tells us that "there is no date for a vote on the Council Decisions and they might not be voted on". Yet, despite this apparent lack of urgency, she questions "whether the UK will have the time to take a decision to opt in".[123] Under the UK's**

119 The EU has observer status within the United Nations General Assembly and can present common positions agreed on behalf of the EU and EU Member States.

120 See p.3 of the Commission's explanatory memorandum accompanying both proposed Council Decisions.

121 See *Council v. Commission*, Case C-660/13.

122 See para 7 (i) of the Minister's Explanatory Memorandum.

123 See paras 12 and 19 of the Minister's Explanatory Memorandum.

Title V (justice and home affairs) opt-in Protocol, the UK has three months in which to decide whether to opt into the proposed Council Decision concerning the immigration aspects of the Global Compact on Migration—document (b). We ask the Minister to:

- **inform us of the date on which the three-month opt-in deadline will expire;**
- **provide a clear justification for any decision to curtail this period; and**
- **explain on what basis the European Commission "has already assumed" that the UK will not opt in.**[124]

7.7 **We would welcome the Minister's view on the case law relied on by the Commission to support its choice of Article 16 TEU as the procedural legal base for the proposed Council Decisions. We ask her to:**

- **clarify the Government's position on the use of Article 16 TEU to obtain the Council's authorisation to approve a non-binding agreement;**
- **explain how far in advance that authorisation should be sought, given the possibility that the content of the Global Compact on Migration may change during negotiations;**[125] **and**
- **indicate what options (other than Article 16 TEU) are available to give the authorisation the Commission seeks.**

7.8 **The Minister's Explanatory Memorandum does not include an assessment of the application of the subsidiarity principle—an important omission given that development cooperation and migration are areas of shared competence in which the EU and Member States are entitled to act. Nor is there any indication that the Commission has produced its own competence assessment to demonstrate the basis on which the EU has competence for policy areas covered in the Global Compact on Migration. We ask the Minister to explain:**

- **whether there are elements of the Global Compact on Migration for which the EU has acquired exclusive competence, meaning that the EU alone must act;**
- **whether all elements of the Global Compact are matters of shared competence; and**
- **if competence is shared, what need or justification there is for separate EU approval of the Global Compact.**

7.9 **Pending further information, the proposed Council Decisions remain under scrutiny. We draw this chapter to the attention of the Home Affairs Committee and the International Development Committee.**

124 See para 14 of the Minister's Explanatory Memorandum.

125 See para 43 of the Court's ruling in *Council v. Commission*, Case C-660/13.

Full details of the documents

(a) Proposal for a Council Decision authorising the Commission to approve, on behalf of the Union, the Global Compact for Safe, Orderly and Regular Migration in the field of development cooperation: (39583), 7400/18 + ADD 1, COM(18) 167. (b) Proposal for a Council Decision authorising the Commission to approve, on behalf of the Union, the Global Compact for Safe, Orderly and Regular Migration in the area of immigration policy: (39584), 7391/18 + ADD 1, COM(18) 168.

Background

7.10 The Global Compact on Migration is intended to address all aspects of international migration, including its humanitarian, developmental, human rights-related and other dimensions. According to the International Organisation for Migration it will:

- make an important contribution to global governance and enhance coordination on international migration;
- present a framework for comprehensive international cooperation on migrants and human mobility;
- set out a range of actionable commitments, means of implementation and a framework for follow-up and review among Member States regarding international migration in all its dimensions;
- be guided by the 2030 Agenda for Sustainable Development and the Addis Ababa Action Agenda; and
- be informed by the Declaration of the 2013 High-Level Dialogue on International Migration and Development.[126]

The proposed Council Decisions

7.11 The first proposed Council Decision—document (a)—would authorise the Commission to approve the development cooperation elements of the Global Compact on Migration. Migration is one of the cross-cutting themes included in the European Consensus on Development, a framework agreed by the EU institutions and Member States in 2017 to guide their cooperation with developing countries and implement the United Nations' 2030 Agenda for Sustainable Development. The European Consensus on Development states that the EU and Member States "actively support […] the elaboration of the UN Global Compacts on Migration and Refugees, as called for by the 2016 New York Declaration for Refugees and Migrants".[127] In addition to Article 16 TEU, the proposed Council Decision cites Article 209 TFEU on development cooperation as the legal base for the EU to act.

7.12 The second proposed Council Decision—document (b)—would authorise the Commission to approve the immigration policy elements of the Global Compact on Migration. It includes a recital stating that the UK's Title V (justice and home affairs) opt-

126 See the website of the International Organisation for Migration for further details.
127 See the European Consensus on Development.

in applies and that the UK has decided *not* to opt in. The proposal cites Article 79 TFEU concerning the development of a common immigration policy and Article 16 TEU as the legal base for the EU to act.

7.13 In its explanatory memorandum accompanying the proposed Council Decisions, the Commission states that the Global Compact on Migration "does not, nor does it intend to, create any legal obligations under domestic or international law". It says that it has "exceptionally" put forward proposals to obtain the Council's advance authorisation to approve the Global Compact on behalf of the EU so that the EU (through the Commission) can be active and influential "at a stage where the policy making function is exercised in substance" and ensure that the final text agreed is consistent with EU laws and policies.[128]

The Minister's Explanatory Memorandum of 11 April 2018

7.14 The Minister confirms that the Global Compact on Migration will be "a non-binding agreement".[129] She says the UK has engaged constructively with the European Commission and EU Member States during the initial consultation phase and the early rounds of negotiations and "our views have been largely aligned", with particular emphasis placed on "the need for state sovereignty on migration policies", border management and the return of individuals that have no right to remain, and "the need for a clear distinction between refugees and economic migrants".[130]

7.15 The Minister notes that the UK's Title V (justice and home affairs) opt-in applies to the proposed Council Decision dealing with the immigration policy—document (b). She sets out the factors which will inform the Government's opt-in decision:

- whether the UK will have time to take a decision to opt in;
- the extent to which opting in will give greater weight to the UK's position and its ability to influence the Global Compact on Migration;
- how closely the EU's position is aligned with the UK's and whether the UK's view will be taken into account in agreeing the Global Compact on Migration if the UK is bound by the EU position;
- the implications of not opting in for the UK's broader relationship with the EU and its institutions, and with other Member States bilaterally—in particular the ability to take an identifiable UK position both with the EU and the UN to secure co-operation and support from other Member States on immigration and wider areas of Justice and Home affairs; and
- the result of the referendum on the UK's membership of the EU and the impact on negotiations on the UK's exit from the EU.[131]

7.16 The Minister adds:

> "Even if we do not opt in, the UK will continue to attend and influence the EU coordination meetings in the UN as we will be bound by the

128 See p.3 of the Commission's explanatory memorandum accompanying both proposed Council Decisions.
129 See para 3 of the Minister's Explanatory Memorandum.
130 See paras 4 and 13 of the Minister's Explanatory Memorandum.
131 See para 12 of the Minister's Explanatory Memorandum.

development co-operation Council Decision. This will allow the UK to negotiate as part of the European Union block, but will also enable the UK to voice its views on migration matters. Consequently, the UK will be able to advocate removing any unhelpful suggestions from the EU's and the UN's text in relation to migration matters, which can be particularly helpful on areas where there is divergence.

"The European Commission has already assumed that the United Kingdom, together with the Republic of Ireland and the Kingdom of Denmark will be bound by the Council Decision on development cooperation, but will not opt in to the Council Decision on migration policy. Therefore, we do not expect a negative political impact from a decision to not opt in to the Council Decision."[132]

7.17 The Minister indicates that questions remain over the process proposed by the Commission to secure authorisation from the Council to approve the Global Compact on Migration and that the Government has yet to reach a view on the use of Article 16 TEU for this purpose. She says that the proposed Council Decisions may not be put to the vote. Whatever the outcome, the UK will remain free to sign the Global Compact on Migration in its national capacity as the EU only has observer status within the United Nations.

Previous Committee Reports

None on these documents.

132 See paras 13–14 of the Minister's Explanatory Memorandum.

8 Emergency oil stocks

Committee's assessment	Politically important
Committee's decision	Cleared from scrutiny; drawn to the attention of the Exiting the EU and the Business, Energy and Industrial Strategy Committees
Document details	Commission Staff Working Document—mid-term evaluation of Council Directive 2009/119/EC imposing an obligation on Member States to maintain minimum stocks of crude oil and/or petroleum products
Legal base	—
Department	Business, Energy and Industrial Strategy
Document Number	(39302), 15130/17, SWD(17) 438

Summary and Committee's conclusions

8.1 In case of supply disruptions, EU Member States are obliged to maintain minimum stocks of crude oil and/or petroleum products, some of which may be held in other Member States. The UK currently holds around five million tonnes in other EU Member States (40% of its obligation) and holds around 500,000 tonnes belonging to other EU Member States. This EU obligation is in addition to similar obligations applied by the International Energy Agency (IEA),

8.2 The Commission's document assessed implementation of the EU Directive following amendment in 2009. In our report of 21 February 2018, the Committee raised a number of questions (see below), to which the Minister for Climate Change and Industry (Claire Perry) has now responded.

8.3 In summary, the Minister considers that the EU Directive adds value to the IEA system, but notes that future options for engagement with EU policy in this area are subject to negotiations on the future economic partnership agreement between the EU and the UK.

8.4 **The Minister has responded to our various questions, but is clearly unable to provide any clear indication of future EU-UK arrangements in this area. While that is understandable given the stage of negotiations, we signal our continued interest in this matter. As we consider that it is likely to be of interest too to the Exiting the EU Committee and the Business, Energy and Industrial Strategy Committee, we draw this chapter to their attention.**

8.5 **We clear the document from scrutiny and require no further information.**

Full details of the documents

Commission Staff Working Document—mid-term evaluation of Council Directive 2009/119/EC imposing an obligation on Member States to maintain minimum stocks of crude oil and/or petroleum products: (39302), 15130/17, SWD(17) 438.

Background

8.6 Council Directive 2009/119 imposes an obligation on Member States to maintain minimum emergency stocks of crude oil and/or petroleum products. The Commission's review of the Directive over the period 2009–16 found it to be effective and relevant. A number of suggestions were made for changes to the annexes so as to improve the Directive's efficiency. Further details were set out in our report of 21 February.

8.7 In the Government's original EM, the Minister for Energy and Industry (Richard Harrington) said that none of the proposed changes was likely to be substantial. The suggestion regarding cross-border stocks was potentially the most significant. The result might be a light touch register to improve the reporting of cross border stocks. He concluded that any changes were largely technical and would not fundamentally impact on the UK's ability to meet its international oil stocking obligations in the future.

8.8 In our Report of 21 February, we noted that the Directive allows for some stocks to be held in other Member States and, as such, the UK both holds stocks for other Member States and has stocks elsewhere. Given this reciprocity, we considered that the UK's exit from the EU is relevant to future oil stocking arrangements. We welcomed responses to the following queries:

- how important the Government considers the EU Directive to be as a way of safeguarding the security of UK supply of crude oil and/or petroleum products;
- whether the Government agrees with the assessment that the EU Directive adds value to the IEA system, due not least to the Directive's requirement that a proportion of the stocks should be in the form of finished products;
- whether or not the UK will therefore seek, post-Brexit, to continue its cooperation with the EU (as well as the IEA) in this area;
- how the UK would do so as the Directive includes no third country provision;
- whether the UK would like to continue to participate in the EU's Coordination Group for oil and petroleum products, and what the implications of non-participation would be (noting the Department's confirmation that it has inputted throughout the review process by virtue of the UK's attendance at meetings of this Group);
- whether responsibility for oil stocks held in the UK and EU-27 respectively, but belonging to the other, has been discussed within the exit negotiations;
- whether resolution of the matter is likely to form part of the Withdrawal Agreement or is seen as part of the agreement on the future relationship between the EU and UK; and
- what the approximate additional cost would be of storing all UK stocks in the UK, rather than making use of excess capacity elsewhere.

The Minister's letter of 29 March 2018

8.9 The Minister for Climate Change and Industry (Claire Perry) considers that the UK's oil supply chain continues to deliver security of supply and in the short-medium term is expected to continue to function well, with sufficient capacity to meet demand, as well as respond to supply shocks. She says that the UK is well placed in global oil markets (crude and product), trading extensively in all oil types and with significant import/export infrastructure on coastal locations able to source fuels from around the globe.

8.10 Regarding the role of emergency oil stocks, she comments that these form an important contribution to UK energy security in extreme scenarios as part of coordinated actions with the International Energy Agency (IEA) and EU member states. The UK Government, she says, takes the requirement to adhere to international obligations seriously. She observes that, as a member of both the IEA and the EU, the UK has (complementary) obligations under both the IEA's International Energy Programme (IEP) and under Council Directive 2009/112/EC. Oil stockholdings are most effective as part of coordinated international action so there is value, says the Minister, in bringing additional countries under the system, as the IEA and EU have done.

8.11 Regarding the added value of the EU Directive, the Minister considers that the Directive adds value to the IEA system, through low barriers to cross-border stockholding and through a finished products requirement. Holding finished products has greater resilience benefits, she says, than just holding crude oil.

8.12 Regarding future UK-EU cooperation in this area, the Minister comments:

> "Our exact future relationship, including the scope of the Implementation Period, remains subject to negotiations with our EU partners. The UK expects to meet its international oil stocking obligations in line with current policy. Our policy remains to meet those obligations as flexibly as possible and we are considering all options for post Exit arrangements."

8.13 The Minister goes on to note that oil stocking under the EU Directive is to be considered under the future economic partnership agreement between the EU and UK and these discussions have not yet taken place. As for continued participation in the EU's Coordination Group for oil and petroleum products, this also remains subject to negotiations.

8.14 In response to the Committee's question about the approximate additional cost of storing all UK stocks in the UK, rather than making use of excess capacity elsewhere, the Minister says:

> "Under the EU Directive emergency oil stocks can be held anywhere within the EU, and under the IEA's International Energy Programme there are no restrictions on location of stockholdings. Over one-third of the UK's obligation is currently stored in other EU Member States (majority in the Netherlands) making use of excess capacity elsewhere.
>
> "Given we are currently obligated to hold a lower level of stocks under the IEA, we have the capacity to hold stocks to meet the IEA obligation domestically if required (no additional cost). The IEA requires the UK to

hold 90 days of net imports, whereas the EU Directive requires the UK to hold the higher of 61 days of inland consumption or 90 days of net imports (we are currently on the former). The Directive currently requires [at least] 12 million tonnes of oil equivalent (mtoe) to be held, the IEA [at least] 6mtoe; the difference is mainly due to North Sea production reducing our net imports although over time the two obligations will be the same."

Previous Committee Reports

Fourteenth Report HC 301–xiv (2017–19), chapter 1 (21 February 2018).

9 Review of Article 185 initiatives

Committee's assessment	Politically important
Committee's decision	Cleared from scrutiny
Document details	(a) Commission Staff Working Document: Long-term sustainability of Research lnfrastructures; (b) Commission Staff Working Document: Executive summary of Evaluation of the participation of the EU in research and development programmes undertaken by several Member States based on Article 185 of the TFEU; (c) Commission Staff Working Document: Evaluation of the Participation of the EU in research and development programmes undertaken by several Member States based on Article 185 of the TFEU
Legal base	—
Department	Business, Energy and Industrial Strategy
Document Numbers	(a) (39091), 12619/17, SWD (2017) 323 final; (b) (39092), 12988/17, SWD (2017) 340 final; (c) (39093), 12990/17, SWD (2017) 341 final

Summary and Committee's conclusions

9.1 The European Commission has produced an evaluation[133] of the EU's participation in Article 185 initiatives—Public-Public Partnerships through which the EU can contribute financially to multiannual research programmes proposed by EU Member States or countries associated to the Framework Programme. This evaluation is intended to feed in to the interim evaluation of Horizon 2020, which the Committee has scrutinised separately.[134]

9.2 Although the evaluation finds that Article 185 initiatives are coherent with the Horizon 2020 objectives and actions, and their governance structures efficient, concerns are expressed about their sustainability: the initiatives are time-limited and intend to make their activities more self-sustaining. In consequence, most of the initiatives evaluated identify possible alternatives to Article 185 to provide greater sustainability. A desire to simplify the complex R&I landscape at national and EU level is also expressed, and noted in the separate evaluation of Horizon 2020.

9.3 In the Government's Explanatory Memorandum,[135] the then Minister of State for Universities and Science at the Department of Business, Energy and Industrial Strategy (Jo Johnson) stated that the UK Government welcomed "the finding on the positive contribution of Article 185 initiatives to the wider EU policy objective of international cooperation".

133 Commission Staff Working Document: Evaluation of the Participation of the EU in research and development programmes undertaken by several Member States based on Article 185 of the TFEU SWD (2017) 341 final.

134 Sixteenth Report HC 301–xvi (2017–19) chapter 10 (28 February 2018).

135 Explanatory Memorandum from the Minister, BEIS, to the Chair of the European Scrutiny Committee (23 October 2017).

9.4 As no assessment of the Brexit implications for future UK participation in Article 185 initiatives specifically was provided, further clarification has been sought from department officials. They reiterated the Government's desire to explore all possible options with the EU to build an ambitious science and innovation agreement, and that this included future participation in Article 185 projects. The Department also clarified that, subject to the withdrawal agreement, the UK would continue to benefit from EU research funding, including funding for Article 185 projects, until the end of the current budget plan in 2020, and for as long afterwards as individual projects continue.

9.5 The Government's Explanatory Memorandum concerning this evaluation also considered a second document regarding research infrastructures (RI) in the EU, which recommended that a number of action points be included within a plan to ensure the long-term sustainability of these infrastructures.[136] The Government also supported the findings of this report.

9.6 **We take note of the Commission's evaluation report of the Article 185 multiannual research programme initiatives, and the Government's support for these findings.**

9.7 **Regarding the implications of the UK's withdrawal from the European Union for future participation in these initiatives, we note that, although countries associated to Horizon 2020 can take part in Article 185 initiatives, provisions do not exist in EU law that specifically permit the participation of third countries; however, the EU has introduced measures to allow third country participation in some cases, subject to the conclusion of international agreements with the relevant countries and a Council Decisions which permits third country participation in a specific project and applies derogations to the rules of third country participation. For example, Morocco, Egypt and Lebanon will participate in the Partnership for Research and Innovation in the Mediterranean Area (PRIMA) initiative.**

9.8 **Although Article 185 initiatives are clearly of value, we note that they represent one of many EU research funding instruments, and account for only €1.7bn of €80bn of total Horizon 2020 funding during the current period, that only five such projects currently exist, and that a number of these have a highly regional focus (e.g. the initiatives on the Baltic Sea and the Mediterranean Area). The key aspect of the UK's future relationship with the EU in scientific research will clearly be its relationship with future Framework Programmes.**

9.9 **We also note the Government's support for the Commission's recommendations regarding a future plan to ensure the long-term sustainability of research infrastructures.**

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

Full details of the documents

(a) Commission Staff Working Document: Long-term sustainability of Research Infrastructures: (39091), 12619/17, SWD (2017) 323 final; (b) Commission Staff Working Document: Executive summary of Evaluation of the participation of the EU in research and development programmes undertaken by several Member States based on Article

136 Commission Staff Working Document: Long-term sustainability of Research Infrastructures SWD (2017) 323 final.

185 of the TFEU: (39092), 12988/17, SWD (2017) 340 final; (c) Commission Staff Working Document: Evaluation of the Participation of the EU in research and development programmes undertaken by several Member States based on Article 185 of the TFEU: (39093), 12990/17, SWD (2017) 341 final.

Background

9.11 Article 185 initiatives are multi-annual R&I funding programmes funded jointly by EU Member States, associated states, third countries and the EU's framework programmes for funding of R&I under the Horizon 2020 regulation. They enable the EU to contribute financially to multiannual research programmes proposed by EU Member States or countries associated to the Framework Programme. They are part of a larger family of so-called Public-Public Partnerships (P2Ps).[137]

9.12 The criteria applicable to Article 185 projects are set out in Article 26 of the Horizon 2020 regulation.[138] It states that EU participation in such projects should be "justified by the scope of the objectives pursued and the scale of the resources required" and only "proposed in cases where there is a need for a dedicated implementation structure and where there is a high level of commitment of the participating countries to integration at scientific, management and financial levels". Article 26 also details five criteria for the identification of such initiatives, which include: a clear definition and relevance to Horizon 2020 and EU policy objectives; indicative financial commitments of the participating countries; added value at Union level; critical mass; and the appropriateness of Article 185 TFEU for achieving the objectives.

9.13 At present, there are five Article 185 initiatives, of which the UK participates in four:

- Active and Assisted Living (AAL2) involves innovative ICT-based solutions for active and healthy ageing;
- Second European and Developing Countries Clinical Trials Partnership Programme (EDCTP2) involves accelerating the development of new or improved treatments for poverty-related diseases in sub-Saharan Africa;
- European Metrology Research Programme (EMRP) and European Metrology Programme for Innovation and Research (EMPIR) involves to advancing metrology solutions for industrial competitiveness and societal challenges;
- Eurostars2 involves transnational collaboration of SMEs performing R&D; and
- the Joint Baltic Sea Research and Development Programme (BONUS) is aligned with the European Strategy for Marine and Maritime Research, which seeks to respond to the key challenges facing the Baltic Sea Region.

9.14 By the end of Horizon 2020, public funding for Article 185 initiatives will have amounted to almost €4 billion (€2.2 billion from Member States and €1.7 billion from the Union).

137 https://www.era-learn.eu/public-to-public-partnerships

138 Article 26 of Regulation 1291/2013 of the European Parliament and of the Council of 11 December 2013 establishing Horizon 2020—the Framework Programme for Research and Innovation (2014–2020).

9.15 The Government has been clear that it wants to remain involved in the successor programme to Horizon 2020 from 2021 onwards. In its September 2017 "future partnership paper" on cooperation with the EU on science and research,[139] the Department for Exiting the EU said it would seek to "agree a far-reaching science and innovation agreement with the EU" after Brexit. The paper notes that this would be in the interest of both sides, especially in the field of medicine and health, but the Government wants to discuss continued UK involvement across the spectrum of EU research policy (i.e. the Framework Programme, as well as the EU's separate research programmes for the defence, space and nuclear industries).

9.16 In the Committee's recently published report on Horizon 2020, we concluded that the UK's continued involvement in the successor to Horizon 2020 should not be taken as a given, and asked the Government to confirm that it would seek for the UK to become "associated" with the next Framework Programme, or, if not, which other "options for participating" the Government was exploring.

The reports

(i) Evaluation of EU participation in Article 185 initiatives

9.17 The Article 185 evaluation[140] reports on the performance of Article 185 initiatives to date, identifying their strengths and challenges as part of the overall interim evaluation of Horizon 2020, which the Committee has scrutinised separately.[141]

9.18 In the Commission's report, it identified the following strengths of Article 185 initiatives:

- their long-term financial perspective provides an incentive for stable programming, contributing to more effective and efficient R&I programme coordination and cooperation across Europe. Consequently, Article 185 initiatives are of special relevance for achieving the European Research Area (ERA);
- they are coherent with the Horizon 2020 objectives and actions. The Article 185 initiatives display a high coherence with wider EU policies beyond Horizon 2020, including international cooperation; and
- the governance structures of the Article 185 initiatives are efficient.

9.19 The report also identifies some challenges with the use of Article 185 initiatives:

- the evaluations of the individual initiatives express concerns about their sustainability—as these initiatives are designed to eventually become more self-sustaining—and identify potential alternatives to the use of Article 185 to ensure the desired sustainability of the respective programmes which might allow for more flexibility and administrative simplification.

139 DExEU, "Collaboration on science and innovation: a future partnership paper" (September 2017).
140 Commission Staff Working Document: Evaluation of the Participation of the EU in research and development programmes undertaken by several Member States based on Article 185 of the TFEU SWD (2017) 341 final.
141 Sixteenth Report HC 301–xvi (2017–19) chapter 10 (28 February 2018).

- given the complexity of the R&I landscape at national and EU level, including a large number of programmes jointly funded by Members States and the EU, it is not always clear how Article 185 initiatives are positioned in this context. This has led to the proliferation of Public-Public Partnerships (e.g. Article 185, ERA-NETs, Joint Programming Initiatives), Public-Private Partnerships (e.g. Article 187 initiatives, contractual Public Private Partnerships) and broader governance and stakeholder platforms (European Innovation Platforms, European Technology Platforms and other related initiatives such as the European Institute of Technology and its KICS, FET Flagships); and

- concerns are expressed that due to the variable geometry approach, Member States can "cherry-pick" in terms of participation, and the participation of less R&D-intensive countries is not sufficient.

9.20 In terms of next steps, the Commission proposes to develop a plan to address the challenges identified through the evaluation of Article 185 initiatives. The evaluation has contributed to the overall interim evaluation of Horizon 2020, which will help to focus the European Commission's thinking about the final years of the programme.

(ii) Research infrastructures

9.21 The Commission has published a staff working document[142] on the long-term sustainability of research infrastructures (RI)—facilities, resources and services used by research communities to enable discovery, develop technology, and foster innovation in their fields. They include major scientific equipment, knowledge-based resources such as collections, archives or scientific data, e-infrastructures such as data, computing systems and communication networks, and any other infrastructure of a unique nature essential to research and innovation. The Government explains that such infrastructures may be 'single-sited', 'virtual' or 'distributed'. The Government's Explanatory Memorandum, summarised below, states that the UK has many research infrastructures that it leads, runs or is involved in, and that most of these are overseen by the UK Research Councils.

9.22 The sustainability of research infrastructures was identified as a key priority at the EU Informal Competitiveness Council in July 2014, at which it was recognised that RI are critical for the EU to remain competitive in the global knowledge-based economy, but that putting in place and maintaining a European landscape of excellent RI has significant budgetary implications at national and European level, raising questions about their long-term sustainability.

9.23 Following several rounds of consultation, into which the UK Research Councils provided input, the Commission has produced a report which recommends that a plan be developed to ensure the long-term sustainability of research infrastructures which should include the following action points:

- Scientific excellence: Promote the funding of access to research infrastructures based on research excellence and implement independent international peer review; more rigorous evaluation of RI by creating a set of Key Performance Indicators;

142 Commission Staff Working Document: Long-term sustainability of Research Infrastructures SWD (2017) 323 final.

- Skilled staff and users: Encourage staff and users to work at research infrastructures throughout Europe, raise awareness of research infrastructures services and simplify access to broaden the range of potential users, and increase harmonisation of the research infrastructures job market;
- Unlocking innovation: Increase research infrastructure's engagement with industry;
- Data: Encourage research infrastructures to take responsibility for data management ensuring openness and accessibility;
- Governance and funding: Encourage the alignment of European and National research infrastructure roadmaps. Support funding through: the private sector, European Structural and Investment Funds, EU financial instruments, and national budgets; and
- Global promotion: Increase visibility and leadership in international research infrastructure fora.

9.24 The Commission states that the consultation will lead to an action plan that will contribute to planning discussions on research funding programmes and European Structural and Investment Funds.

The Government's view

9.25 On 24 October 2017 the then Minister of State for Universities and Science at the Department of Business, Energy and Industrial Strategy (Jo Johnson) submitted an Explanatory Memorandum to Parliament[143] in which he stated that the UK Government noted the findings of the Article 185 evaluation and welcomed "the finding on the positive contribution of Article 185 initiatives to the wider EU policy objective of international cooperation".

9.26 As the Government's Explanatory Memorandum did not provide any information about the implications of Brexit for UK involvement in these initiatives, further clarification was sought from officials at BEIS. In response, they stated that:

- the Government's position paper states that it wishes to discuss all possible options with the EU in order to build an ambitious science and innovation agreement, which includes discussing possible options for participating in things like Article 185 projects;
- the financial settlement agreed between the UK and the EU in December means that, subject to the withdrawal agreement, the UK will continue to benefit from EU programmes, including funding for Article 185 projects, until the end of the current budget plan in 2020, and for as long afterwards as individual projects continue. UK based individuals and organisations will remain eligible to bid for funding, participate in and lead consortia including for calls in 2019 and 2020. Projects approved during this period will be able to continue with an uninterrupted flow of EU funding; and
- entities from third countries participate in Article 185 projects and there are established mechanisms for doing so.

143 Explanatory Memorandum from the Minister, BEIS, to the Chair of the European Scrutiny Committee (23 October 2017).

9.27 Contrary to this last point, it appears that there is not a formal established mechanism for third countries that are not associated to the Framework Programme to participate in Article 185 initiatives. A European Parliament briefing on the PRIMA initiative[144] states that Article 185 TFEU does not include a reference to the participation of third countries, and that specific measures are therefore needed to enable third country participation in the initiative, which would involve:

- the conclusion of international agreements between the EU and participating states with third country status under Horizon 2020; and
- adoption of a Council decision with the consent of Parliament in accordance with Articles 186 and 218(5) TFEU, which would also establish derogations to the rules of participation applying to the Horizon 2020 programme.

9.28 Regarding the document on the long-term sustainability of research infrastructures, the Minister states that it recognises the work of the Commission, ESFRI and the scientific community in producing a clear working document that outlines the key issues facing the long-term sustainability of research infrastructures. The Minister states that the Government will work with partners to produce an action plan that will address these issues.

Previous Committee Reports

Sixteenth Report HC 301–xvi (2017–19) chapter 10 (28 February 2018).

144 European Parliament, Briefing: Legislation in progress: Partnership for Research and Innovation in the Mediterranean Area (PRIMA) pp3–4.

10 Access to published works for the visually impaired

Committee's assessment	Legally and politically important
Committee's decision	Cleared from scrutiny; further information requested
Document details	(a) Regulation 2017/1563 on the cross-border exchange between the Union and third countries of accessible format copies of certain works and other subject matter protected by copyright and related rights for the benefit of persons who are blind, visually impaired or otherwise print-disabled; (b) Directive 2017/1564 on certain permitted uses of works and other subject-matter protected by copyright and related rights for the benefit of persons who are blind, visually impaired or otherwise print disabled and amending Directive 2001/29 on the harmonisation of certain aspects of copyright and related rights in the information society
Legal base	(a) and (b) Article 114 TFEU, ordinary legislative procedure, QMV
Department	Business, Energy and Industrial Strategy
Document Numbers	(a) (38079), 12264/16; (b) (38080), 12270/16, COM(16) 596

Summary and Committee's conclusions

10.1 These documents bring EU law into line with the Marrakesh Treaty.

10.2 As set out in detail in our first Report on this subject, the Marrakesh Treaty was negotiated by Members of the UN's World Intellectual Property Organisation (WIPO), and aims to improve access to copyright works for people who are visually impaired or have print disabilities. The Treaty achieves this through the international harmonisation of copyright exceptions (acts that do not need the permission of the copyright owner) allowing for the creation of accessible format versions of copyright works (for example, Braille versions) for the benefit of visually impaired or otherwise print disabled people, under certain conditions, without infringing copyright. The Treaty also provides, in certain circumstances, for the import and export of accessible copies between contracting parties. The Treaty has been concluded (ratified) by the EU. The decision authorising the EU to conclude the Treaty (which was cleared by the Committee) was the subject of a separate report by the Committee.[145]

10.3 Two EU instruments give effect to the Treaty within the EU: a Regulation and a Directive. The Regulation, document (a), allows the import and export of accessible format copies between the EU and third Countries party to the Marrakesh Treaty. The Directive, document (b), harmonises the exceptions to copyright found in EU law. These changes make EU law compatible with the Marrakesh Treaty and thus have enabled the EU to conclude the Treaty.

145 Thirteenth Report 301–xiii (2018–19) chapter 4 (7 February 2018).

10.4 Before the Committee was established after the Election, the Minister wrote to state[146] that the Government had over ridden the scrutiny reserve on both the Regulation and Directive by voting in Council on 17 July 2017 in favour of the Proposals. The reason given being "the importance of the Marrakesh Treaty on both a humanitarian and diplomatic level".[147]

10.5 The Regulation has been applicable since 12 October. Member States are under an obligation to transpose the Directive by 11 October 2018.

10.6 **We thank the Minister for the helpful updates and his and his predecessor's explanations of the reasons for overriding the scrutiny reservation. The Committee notes:**

a) **the Government's intention to implement the Directive by the transposition deadline of 18 October 2018;**

b) **the text of the Directive as adopted does not permit a 'commercial availability' limitation in relation to the creation, under an exception to copyright, of accessible format copies for the visually impaired;**

c) **the Government's intention to consult prior to implementation of the Directive on the impact of removing the 'commercial availability' limitation in domestic law;**

d) **the Government's intention to consult on the scope and options to safeguard commercial markets (in the absence of a 'commercial availability' limitation in domestic law'), for example, by means of a scheme to compensate for any harm removal of the current limitation in domestic law may cause to rights holders; and**

e) **the Government's desire to "ensure the benefits of the Treaty, including the cross-border exchange of accessible format copies, continues during this [the transitional/implementation] period"[148].**

10.7 **The Committee clears these documents but asks the Minister the following:**

a) **in the light of the recent clarification by the EU of the position as it currently stands regarding application of the Directive and Regulation to the UK on exit[149] (which, in particular, states that the UK will not benefit from the exchange of assessible format copies with third countries in the absence of the UK becoming a party to the Marrakesh Treaty), what steps the UK intends to take to "ensure the benefits of the Treaty are maintained in the UK",[150] in particular as regards exchange of assessible format copies with third countries; and**

b) **whether it is the Government's intention to seek EU permission to ratify and bring the Treaty into force on UK exit.**

146 By letter of 7 August 2017.

147 Letter from Jo Johnson MP to Sir William Cash of 28 November 2017.

148 Letter of 19 March 2018 to Sir William Cash from Sam Gyimah MP.

149 Commission notice to Stakeholders of 28 March 2018 "Withdrawal of the United Kingdom and EU rules in the field of copyright".

150 Letter of 19 March 2018 to Sir William Cash from Sam Gyimah MP.

c) **We also ask to be kept informed of the results of the proposed consultation and the Government's assessment of the impact of the removal of the limitation on 'commercial availability'[151] in domestic law; in particular, if it is decided to create a compensation scheme in domestic law for the benefit of rightsholders, how it is intended that scheme will be funded.**

Full details of the documents

(a) Regulation 2017/1563 on the cross-border exchange between the Union and third countries of accessible format copies of certain works and other subject matter protected by copyright and related rights for the benefit of persons who are blind, visually impaired or otherwise print-disabled: (38079), 12264/16, COM(16) 595; (b) Directive 2017/1564 on certain permitted uses of works and other subject-matter protected by copyright and related rights for the benefit of persons who are blind, visually impaired or otherwise print disabled and amending Directive 2001/29 on the harmonisation of certain aspects of copyright and related rights in the information society: (38080), 12270/16, COM(16) 596.

Background

10.8 As set out in more detail in our first Report on this subject, the Marrakesh Treaty of 26 March 2014 seeks to achieve its objectives through the international harmonisation of copyright exceptions (i.e. acts that do not need the permission of the copyright owner) for the benefit of those who are visually impaired or otherwise print-disabled to enable accessible versions of copyright works (for example, Braille versions of books) to be produced under certain conditions without infringing copyright. The Marrakesh Treaty also provides for the import and export of accessible copies subject to certain conditions.

10.9 The Regulation and Directive implementing the Marrakesh Treaty were adopted on 13 September 2017 and the decision to conclude the Treaty was adopted by the Council on 15 February 2018. The UK voted in favour of the Proposals overriding the scrutiny reserve in the Committee's absence. The then Minister explained the reasons for the override in his letters of 30 October and 28 November 2018:

> "On 17 July 2017, due to the Committee's absence, the Committee had not responded to my request of 3 July 2017 to lift its scrutiny reserve. As discussed above, given the importance of the Marrakesh Treaty on both a humanitarian and diplomatic level, I took the decision to override the Scrutiny Reserve Resolution and vote in favour. To have abstained or voted against could have called into question the Government's commitment to the aims of the Treaty, and suggested that it had outstanding objections to the substance of the implementing legislation, which it did not."

10.10 The Minister wrote to the Committee on 3 July and 7 August to update the Committee on the progress of negotiations. In his letter of 7 August, the Minister set out the Government's position:

> "During the course of negotiations, groups representing visually impaired people argued that commercial availability restrictions would place

151 See paragraph 43 of EM 12264/16 which refers to the potentially negative impact of this on authors and commercial publishers of accessible format copies.

unreasonable burdens on organisations which make accessible format copies, and that there was little evidence that such restrictions were needed to protect commercial markets. Reflecting this view, the agreed texts do not provide flexibility for Member States to maintain commercial availability clauses in their national exceptions. They do, however, provide other market safeguards, including:

"a. the option for Member States to provide schemes to compensate for any harm the exception may cause for rights holders;

"b. the requirement that domestic exceptions of Member States apply only in certain special cases which do not conflict with the normal exploitation of the work, and do not unreasonably prejudice the legitimate interest of the right holder;

"c. an obligation on the European Commission to assess any negative impact the proposals have on commercial markets, 6 years after the date of entry into force.

"On implementing the Directive and Regulation, we will consult on the impact of removing the commercial availability provision in UK law, and on the scope and options to safeguard commercial markets.

"'*Compensation schemes*'

"The compromise texts for the draft Regulation and Directive do not provide full flexibility for Member States, but allow Member States to provide certain market safeguards. One of these safeguards is the option for Member States to provide schemes to compensate rightsholders for any harm the exception may cause to them. The UK does not currently take this approach in its disability exception, as it considers rightholders' interests to be sufficiently protected via a number of safeguards, including a commercial availability clause. The UK's future approach to compensation schemes will depend on the outcome of the consultation, including potential impacts from the removal of the commercial availability clause.

"'*Implementation*'

"We intend to implement on the transposition deadline set by the Directive, which is expected to be before the UK exits the EU."

Previous Committee Reports

Seventeenth Report HC 71–xv (2016–17) chapter 4 (2 November 2016).

11 EU Plastics Strategy

Committee's assessment	Politically important
Committee's decision	Cleared from scrutiny; drawn to the attention of the Environmental Audit Committee and the Environment, Food and Rural Affairs Committee
Document details	Commission Communication: A European Strategy for Plastics in a Circular Economy
Legal base	—
Department	Environment, Food and Rural Affairs
Document Number	(39438), 5477/18 + ADDs 1–2, COM(18) 28

Summary and Committee's conclusions

11.1 To tackle challenges associated with plastic production and consumption, along with low reuse and recycling of plastic, the Commission proposed a plastics strategy with the aim of addressing three aspects in particular: high dependence on virgin fossil feedstock; the low rate of recycling and reuse of plastics; and the significant leakage of plastics into the environment.

11.2 The Committee first considered this document at our meeting of 7 March, raising several concerns including the need for the Government to re-visit its assessment of the Brexit implications. The detail of the response from the Parliamentary Under-Secretary of State for the Environment (Dr Thérèse Coffey) is set out below. In summary, she says:

- the UK engaged in the development of the plastics strategy pre-publication;
- some of the initiatives, such as Extended Producer Responsibility (EPR) schemes, will have direct implications for UK policies post-Brexit, but the detail of the Commission's plans remains unclear;
- the Government will continue to engage with the Commission as it develops its plans; and
- acknowledging that there are synergies between the UK's proposed approach and that of the EU, the UK will want to continue cooperation on tackling the environmental impacts of plastics.

11.3 **The Minister's explanation of the ongoing engagement between the UK and the EU on these matters, even as the UK prepares to leave the EU, is helpful. We have no outstanding questions and are now content to clear this document from scrutiny. We draw the chapter to the attention of the Environmental Audit Committee and the Environment, Food and Rural Affairs Committee.**

Full details of the documents

Commission Communication: A European Strategy for Plastics in a Circular Economy: (39438), 5477/18 + ADDs 1–2, COM(18) 28.

Background

11.4 Further details of, and background to, the strategy were set out in our Report of 7 March 2018.[152]

11.5 In her original EM,[153] the Minister provided no detailed analysis nor specific comment on any of the suggestions. She considered the commitments to be helpful and that they appeared to be broadly consistent with UK ambitions, including the UK objective of zero avoidable plastics waste by 2042. The detail of the proposals needed development, she said, and so it was too early to know exactly how they would fit with the UK's plans. Moving forward, she said, the Government would continue to work with the Commission to support the delivery of the strategy and the development of the UK's own Resources and Waste Strategy later in 2018. The Minister insisted that there were no specific issues relating to the UK's departure from the EU arising from the strategy.

11.6 In our report of 7 March 2018, we disputed the Minister's contention, considering that there are wide-ranging implications for the design of policy in the UK post-Brexit, assuming that at least some of the ideas come to fruition and assuming that some sort of co-operative and trading relationship is maintained between the UK and the EU. We therefore invited the Minister to re-visit her assessment of the Brexit implications, setting out a headline analysis of the potential implications for the UK post-Brexit. We also asked for information on:

- the UK's focus in its contributions towards the preparation of the strategy;
- any interventions made by the UK when the matter was discussed at the informal Environment Council meeting in April 2017;
- the areas on which the UK would focus during the UK's remaining time as an EU Member State;
- whether any of the measures recommended to national authorities and industry find favour with the Government; and
- whether the Government would be consulting UK on stakeholders on the Commission's strategy with a view to considering what might be incorporated into the UK's own waste and resources strategy later this year.

The Minister's letter of 9 April 2018[154]

11.7 The Minister notes that the UK has welcomed the EU's ambitions and, in particular, the emphasis placed on tackling the environmental impacts associated with plastics production, use and disposal. She agrees that the plastics strategy is broadly consistent

152 Seventeenth Report HC 301–xvii (2017–19), chapter 1 (7 March 2018).
153 Explanatory Memorandum dated 31 January 2018.
154 Letter from Dr Thérèse Coffey to Sir William Cash dated 9 April 2018.

with the UK's own ambitions in this area, as set out in England's 25 Year Environment Plan and as reflected in the high priority devoted in Scotland, Wales and Northern Ireland to tackling plastic waste and developing their own ambitious targets for the circular economy and waste.

11.8 Regarding the UK's focus in influencing the development of the plastics strategy, the Minister notes that the Commission published a roadmap in January 2017 and Defra representatives attended expert working group meetings in 2017 where it was discussed. At the informal Environment Minister's meeting in April 2017, at which the UK was represented by officials given the general election, the UK intervention at this meeting highlighted the impact of the five pence plastic bag charge, the proposals on microbeads and the need for evidence on other sources of microplastics to help inform future actions to protect the marine environment.

11.9 In its contributions, the Government:

- called for effective links to be made between the plastics strategy and wider proposals in the Circular Economy Package relating to product design standards and producer responsibility in order to create a fully integrated set of proposals that would maximise the impact of the strategy and promote action across the whole value chain;
- highlighted the need to be mindful of potential costs to businesses and negative impacts on innovation of overly restrictive proposals and that, as far as possible, actions should be outcome-focused;
- supported the proposed focus on increasing demand for secondary materials and enabling more efficient recovery through better product design and underscored the need for sound evidence and a robust impact assessment to underpin decision making; and
- acknowledged the global nature of marine litter and that, accordingly, any action at national or EU level needed to be supported by global initiatives and partnerships.

11.10 Concerning future focus and action, the Minister draws attention to England's 25 Year Environment Plan, which identifies the ambition to eradicate all avoidable plastic waste by 2024. It includes a list of actions to be taken at the production, consumption, end-of-use and end-of-life stages of the lifecycle to support this goal. The Plan also references collaborative industry action and examples of how the UK is demonstrating international leadership in this area. Since publication of the Plan, the Government has also launched a call for evidence on how the tax system or charges could reduce single-use plastic waste.

11.11 Concerning the list of measures recommended to national authorities and industry, the Government is supportive of all measures that align with the actions set out in the 25 Year Environment Plan. The detail of individual proposals will need to be considered, however, before the Government can set out its position on them. It will also be important to ensure that local circumstances and implications for businesses and consumers are taken into account.

11.12 The Minister goes on to remind the Committee of the provisions of the EU Withdrawal Bill, clarifying that retained EU law will not include EU Directives but will include Statutory instruments made under s.2(2) ECA and which transpose those Directives. She also reminds the Committee that the UK is leaving the EU and will cease to be a member of its institutions. The Government, she says, is negotiating the terms of how the UK will operate during the proposed implementation period.

11.13 The Minister acknowledges that some of the initiatives, such as the review of Extended Producer Responsibility (EPR) schemes, will have direct implications for UK policies post-Brexit. She adds:

> "What is unclear is how specifically the strategy will impact on those proposals moving forward. We will continue to monitor developments at the EU level in order to consider how these might impact on UK businesses and trade and on our own policy ambitions as and when these details emerge. Matters relating to transposition are still subject to discussion."

11.14 In terms of future engagement in EU policy, the Minister welcomes the Commission's parallel work proposing possible options to address the interface between chemical, product and waste legislation. She explains:

> "The lack of coherent policy integration on these issues creates a barrier for circular business models, eco-innovation and the effective management of hazardous chemicals (substances of very high concern, such as persistent, bio-accumulative and toxic substances), leading to impacts on human health and the environment. We will continue to engage in discussions on options for overcoming the key challenges identified by the Commission and will ensure that the implementation challenges for manufacturers and industry are considered in these discussions so that practical solutions can be identified to protect human health and wildlife."

11.15 The Minister goes on to acknowledge that there are synergies between the UK's proposed approach to tackling the environmental impacts of plastics and the proposals outlined in the plastics strategy. The UK is looking to develop a deep and special relationship with the EU and will want to continue to cooperate with the EU on this important issue as well as meeting wider international commitments in this area, through fora such as the UN and the G7 Resource Efficiency Alliance.

11.16 The Minister concludes with reference to stakeholder engagement:

> "We have no plans for a formal consultation on the Commission's strategy. However, it includes proposals which are also among those we have been considering as part of the process to develop our new resources and waste strategy. We will be holding a number of stakeholder workshops to test policy ideas and gather feedback and will consult with other Government departments, the devolved administrations and other interested parties as necessary as specific actions are taken forward."

Previous Committee Reports

Seventeenth Report HC 301–xvii (2017–19), chapter 1 (7 March 2018).

12 State of Paediatrics Medicines in the EU

Committee's assessment	Politically important
Committee's decision	Cleared from scrutiny; drawn to the attention of the Health Committee
Document details	Report from the Commission: State of Paediatric Medicines in the EU—10 years of the EU Paediatric Regulation
Legal base	—
Department	Health and Social Care
Document Number	(39173), 13779/17, COM(17) 626

Summary and Committee's conclusions

12.1 In its assessment of the impact of the EU's Paediatric Medicines Regulation,[155] the European Commission concluded that the Regulation had boosted the development of paediatric medicines, but that these positive developments were not spread evenly across all therapeutic areas. They were often linked to research priorities in adults rather than children and there had also been issues about the availability of licensed medicines and long deferrals of clinical trials.

12.2 The Parliamentary Under-Secretary of State for Health (Lord O'Shaughnessy) has responded to queries raised by the Committee in our Report of 10 January 2018. In particular, the Minister makes a commitment to undertake a discrete piece of analysis, considering: the impact of the Regulation in the UK specifically; the possible implications of EU exit on paediatric medicines development; and the future of paediatric medicines development for the UK. He says that this work should be concluded by the end of 2018, but warns that the Government would not be able to publish anything that would prejudice the UK's negotiating position.

12.3 Writing before the Prime Minister's Mansion House speech—in which she expressed an intention to seek associate membership of the European Medicines Agency—the Minister explains current arrangements for cooperation between the EU and third countries in this area and emphasises the UK's desire for continued close cooperation.

12.4 **We welcome the Minister's commitment to a discrete piece of analysis on paediatric medicines development in the UK in the specific context of the UK's withdrawal from the EU. We recognise the potential sensitivity of this material as the UK negotiates its exit from the EU, but we would caution against an assumption that none of the assessment could be published.**

12.5 **We emphasise the desirability of including clinical trials within the Government's analysis. Continued cooperation on clinical trials, including the ability to share**

155 Regulation (EC) No 1901/2006 of 12 December 2006 on medicinal products for paediatric use.

and access data through mechanisms such as the European clinical trial database (EudraCT), is crucial to the ability of UK paediatricians to engage in research on rare congenital diseases in particular.

12.6 **Since the Minister wrote, the Prime Minister has expressed the Government's intention to seek associate membership of the European Medicines Agency (EMA). We note that EU legislation on the EMA currently makes no such provision and would therefore need to be amended. Equally, however, the European Council guidelines on the negotiation of the future relationship between the EU and the UK appear not to preclude some form of UK non-voting participation in EU agencies in the future. The Health Committee is taking these issues forward with the Department.**

12.7 **We will monitor with interest the Department's work on paediatric medicines development and evolving discussions on future engagement between the EU and the UK. We clear this document from scrutiny and draw this chapter to the attention of the Health Committee.**

Full details of the documents

Report from the Commission: State of Paediatric Medicines in the EU—10 years of the EU Paediatric Regulation: (39173), 13779/17, COM(17) 626.

Background

12.8 The Paediatrics Regulation sets up a system of obligations, rewards and incentives, and puts in place measures to ensure that medicines are regularly researched, developed and authorised to meet children's therapeutic needs. The Regulation obliges companies to agree at an early stage of development a paediatric investigation plan (PIP) with the European Medicines Agency (EMA). In its report, the Commission suggested that further scrutiny was required of why major therapeutic advances had failed to materialise in diseases that are rare and/or unique to children and which, in many cases, were equally supported by the orphan legislation.[156] Full details on the background to, and content of, the Commission's report were set out in our Report of 10 January 2018.

12.9 In his original EM, the Minister was unable to confirm the extent to which the Government agreed—or disagreed—with the report. This was largely because the report's conclusions were based on an EU-wide sample and further work would be needed to confirm whether the conclusions applied to the UK. The Minister nevertheless confirmed that, while the UK was still represented at the EMA Paediatric Committee, the UK would work with other regulators and stakeholders to undertake the activities proposed in the report. The degree to which the UK would collaborate with the EU on paediatric medicines post-Brexit was still to be confirmed.

156 Regulation (EC) No 141/2000 of 16 December 1999 on orphan medicinal products. Orphan medicinal products are intended for the diagnosis, prevention or treatment of life-threatening or very serious conditions that affect no more than 5 in 10,000 people in the European Union. Due to the small usage, the pharmaceutical industry has little financial interest in their development.

12.10 When the Committee first considered the document, at our meeting of 10 January 2018, we asked the Minister to:

- commit to the immediate launch of a UK-specific analysis to be completed well in advance of the UK's withdrawal from the EU;
- explain how third countries currently engage with the EU on the development of paediatric medicines and confirm whether or not that level of engagement would be satisfactory post-Brexit or if the UK would be seeking closer engagement; and
- explain the impact of the UK diverging from EU rules in the areas of both paediatric and orphan medicines.

The Minister's letter of 6 February 2018[157]

12.11 The Minister makes a commitment that the Medicines and Healthcare products Regulatory Agency (MHRA) will undertake a discrete piece of analysis on paediatric medicine development in the UK with support from the DHSC. The analysis will consider:

- the impact of the EU Paediatric Regulation, ten years after its introduction, considering to what extent the experience of the UK matches that of the EU more widely;
- the possible implications of EU exit on paediatric medicines development; and
- the future of paediatric medicines development for the UK.

12.12 The Minister explains that the analysis will be completed by the end of 2018 so that outcomes can be fed into wider EU exit work. He expresses confidence that the Committee will understand that such analysis will be sensitive during this time of negotiations with the EU, and will appreciate that the Government has a duty not to publish anything that could risk exposing its negotiating position. However, he assures the Committee that undertaking this work will ensure future decisions on paediatric medicines regulation in the UK are backed by a solid foundation of evidence.

12.13 The Minister re-iterates the UK's position on medicines regulation post-Brexit in the following terms:

> "we wish to retain a close working partnership with the EU. Our overall aim is to ensure that patients in the UK and the EU continue to access the best and most innovative medicines, and are assured that their safety is protected through ongoing cooperation and the strongest regulatory framework for all medicines, including paediatric medicines in every respect."

12.14 Regarding current third country engagement with the EU on the development of paediatric medicines, the Minister explains that the European Medicines Agency (EMA) and medicines regulators in third countries cooperate in a number of ways on regulatory approaches to development of paediatric medicines. He notes that, while there are different legal requirements in relation to medicines between the EU and third

157 Letter dated 6 February 2018 from the Lord O'Shaughnessy to Sir William Cash MP.

countries, there is a great deal of voluntary collaboration between regulators around the world. This collaboration includes the MHRA and EMA, and aims to promote effective and streamlined approaches to paediatric drug development internationally.

12.15 The EMA, he says, holds regular meetings with other non-EU regulators to discuss global development plans for paediatric medical products (such as internationally coordinated paediatric trials) and to exchange information on specific products and other topics related to development of drugs for children. The intention is to avoid the unnecessary duplication of paediatric clinical trials and to maximise the exchange of information on safety and efficacy of paediatric medicines. The EMA has also arranged joint workshops with international partners on the development of specific paediatric regulatory guidelines to foster common approaches.

12.16 The Minister goes on to reference the European Network of Paediatric Research at the European Medicines Agency (Enpr-EMA), which is a network of research networks, investigators and centres with recognised expertise in performing clinical studies in children. Enpr-EMA's main objective is to facilitate studies in order to increase availability of medicinal products authorised for use in children. Participation is not limited to networks from EU countries and Enpr-EMA works with international partners specialising in the regulation of medicines for children including the World Health Organisation (WHO) through the EMA's membership of the Paediatric Medicines Regulators' Network (PmRN) and with the US Food and Drug Administration (FDA) through the EMA's existing interaction on paediatric therapeutics.

12.17 In terms of prospects for future collaboration between the EU and the UK, the Minister concludes:

> "This range of international collaboration activities illustrate well that the regulation of medicines and the sharing of best practice already happens globally, not just within the EU. The UK already collaborates with countries both within and outwith the EU on a range of regulatory issues, and intends to do so once we leave the EU, including on paediatric medicines. It shall continue to be in the best interest of both the UK and EU to collaborate and support the development of better medicines for young patients whether they are in the UK or in the EU as illustrated in the Commission's 10-year report. The Paediatric Regulation has been achieving its aims of increasing the number of well-evidenced medicines for children with age-appropriate formulations in the EU, but more can be done to reach its full potential."

12.18 The Minister emphasises that the UK is fully committed to continuing and evolving the close working relationship with its European partners. Its aim is to ensure that patients in the UK and across the EU continue to be able to access the best and most innovative medicines and be assured that their safety is protected through the strongest regulatory framework and sharing of data. The Minister believes that the health needs of children will be best served by a continued close relationship between the UK and EU and its associated paediatric networks.

12.19 Finally, the Minister emphasises that there is no immediate prospect of any change to the UK's regulatory relationship with the EU in the light of the planned post-Brexit implementation period and the conversion of EU law into UK law. Longer term,

he says, the UK will be pragmatic in establishing UK regulatory requirements, bearing in mind the needs of patients and industry, and giving sufficient time to consult on, and implement, any new requirements.

Previous Committee Reports

Ninth Report HC 301–ix (2017–19), chapter 5 (10 January 2018).

13 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

(39541) 6953/18 + ADDs 1–2 COM(18) 86	Report from the Commission to the Council and the European Parliament On the implementation of the European Energy Programme for Recovery and the European Energy Efficiency Fund.
(39581) 7065/18 SWD(18) 49	Commission Staff Working Document on the mid-term review of the Atlantic action plan.

Department for Communities and Local Government

(39557) 6312/18 + ADD 1	Commission Delegated Decision (EU) …/… of 19.2.2018 on the applicable systems to assess and verify constancy of performance of metal faced sandwich panels for structural use pursuant to Regulation (EU) No 305/2011 of the European Parliament and of the Council.

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Department for Environment, Food and Rural Affairs

(39534) 6866/18 COM(18) 87	Report from the Commission to the European Parliament and the Council on the possibility of introducing certain requirements regarding the protection of fish at the time of killing.
(39543) 6772/18 + ADDs 1–8 COM(18) 115	Proposal for a Regulation of the European parliament and of the Council establishing a multi-annual plan for the fisheries exploiting demersal stocks in the western Mediterranean Sea.
(39566) 5365/18 + ADD 1	Commission Regulation (EU) …/… of XXX amending Annex II to Regulation (EC) No 1107/2009 by setting out scientific criteria for the determination of endocrine disrupting properties.

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(39593) 7454/18 COM(18) 143	Proposal for a Regulation of the European Parliament and of the Council amending Regulation (EU) No 1343/2011 on certain provisions for fishing in the GFCM (General Fisheries Commission for the Mediterranean) Agreement area.

Department for International Trade

(39385) 15932/17 COM(17) 737	Report From the Commission to the Council and the European Parliament in accordance with Article 21(3) of Regulation (EU) No 258/2012 of the European Parliament and of the Council of 14 March 2012 implementing Article 10 of the United Nations' Protocol against the illicit manufacturing of and trafficking in firearms, their parts and components and ammunition, supplementing the United Nations Convention against Transnational Organised Crime (UN Firearms Protocol), and establishing export authorisation, and import and transit measures for firearms, their parts and components and ammunition.

Foreign and Commonwealth Office

(39627) — —	Council Decision (CFSP) 2018/XXX of [ ] amending Decision 2013/184/CFSP concerning restrictive measures against Myanmar/Burma
(39628) — —	Council Regulation amending Regulation (EU) No 401/2013 of 2 May 2013 concerning restrictive measures in respect of Myanmar/Burma

HM Treasury

(39597) 7543/18 COM(18) 156	Proposal for a Decision of the European Parliament and of the Council on the mobilisation of the European Globalisation Adjustment Fund following an application from Belgium—EGF/2017/010 BE/Caterpillar.

Department for Transport

(39546) 7050/18 COM(18) 122	Proposal for a Council Decision on the position to be taken on behalf of the European Union during the 99th session of the International Maritime Organization's Maritime Safety Committee on the adoption of amendments to SOLAS regulations II-1/1 and II-1/8–1, the approval of relevant guidelines on computerised stability support for the master in case of flooding for existing passenger ships and on the adoption of amendments to the International Code for Application of Fire Test Procedures, 2010.

(39547) 7042/18 + ADD 1 COM(18) 111	Proposal for a Council Decision on the position to be taken on behalf of the European Union at the 55th session of the Organisation for International Carriage by Rail Committee of Experts for the Carriage of Dangerous Goods as regards certain amendments to Appendix C to the Convention concerning International Carriage by Rail as applicable from 1 January 2019.

Formal minutes

Wednesday 25 April 2018

Members present:

Sir William Cash, in the Chair

Douglas Chapman	Kelvin Hopkins
Steve Double	Kate Hoey
Marcus Fysh	Darren Jones
Kate Green	David Jones

2. Scrutiny report

Draft Report, proposed by the Chair, brought up and read.

Ordered, That the draft Report be read a second time, paragraph by paragraph.

Paragraphs 1.1 to 12.19 read and agreed to.

Summary agreed to.

Resolved, That the Report be the Twenty-fifth Report of the Committee to the House.

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

[Adjourned till Wednesday 2 May 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)

Douglas Chapman MP (*Scottish National Party, Dunfermline and West Fife*)

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

Steve Double MP (*Conservative, St Austell and Newquay*)

Richard Drax MP (*Conservative, South Dorset*)

Mr Marcus Fysh MP (*Conservative, Yeovil*)

Kate Green MP (*Labour, Stretford and Urmston*)

Kate Hoey MP (*Labour, Vauxhall*)

Kelvin Hopkins MP (*Independent, Luton North*)

Darren Jones MP (*Labour, Bristol North West*)

Mr David Jones MP (*Conservative, Clwyd West*)

Stephen Kinnock MP (*Labour, Aberavon*)

Andrew Lewer MP (*Conservative, Northampton South*)

Michael Tomlinson MP (*Conservative, Mid Dorset and North Poole*)

David Warburton MP (*Conservative, Somerton and Frome*)

Dr Philippa Whitford MP (*Scottish National Party, Central Ayrshire*)