Welsh Government reflections on UK Government's response to the House of Lords EU Committee mini-inquiry into UK-EU negotiations on State aid and the Level Playing Field

Following the submission of the UK Government's response to the House of Lords EU Committee mini-inquiry into UK-EU negotiations on State aid and the Level Playing Field, the Welsh Government was asked to provide its reflections on its contents. These have been structured around the original questions to which the Welsh Government was invited to provide comment.

1) Has the UK Government consulted with you, as a devolved administration, in developing the UK's negotiating position on the level playing field? (N.B. We are particularly interested in the Government's engagement with you on the UK's future state aid or subsidy control regime, including progress (if any) towards the conclusion of a common framework on state aid.)

In their letter of response to the Committee, the UK Government claims that it has discussed with officials from the Devolved Administrations possible objectives for a domestic subsidy control regime. This is not the experience of the Welsh Government, as in the few discussions that have taken place UK Government officials have merely provided high-level statements of their intention to diverge from EU rules, with no opportunity for the Welsh Government to engage on detail.

The UK Government letter also states that it has committed to further discussions as the policy develops. We agree with the letter that *"it is in all our interests to ensure that the regime works for the whole of the UK and enables the UK's internal market to function properly'* but doing so will require a step change in the engagement with ourselves and the other Devolved Administrations. The Welsh Government has consistently called for development of a future subsidies regime to be undertaken on a quadrilateral basis but the UK Government have consistently failed to provide the level of granularity required for Devolved Administrations to provide a meaningful contribution.

The UK Government states that it is developing a new domestic policy in tandem with the EU negotiations on open and fair competition, working at pace to develop this policy with the intention of sharing more detail on domestic subsidy control with key stakeholders in due course. The Welsh Government has been given no opportunity to engage with this process and this is unacceptable.

Whilst the UK Government *"notes"* the Scottish and Welsh positions on competence, and states that the *"Cabinet Office is leading work across Whitehall to ensure that Devolved Administrations are engaged in key stages of the EU negotiations, with the opportunity to scrutinise the process"*, this has not been the experience of the Welsh Government. As Welsh Ministers have repeatedly made clear, the level of engagement in respect of the negotiations with the EU has been wholly unsatisfactory and does not reflect the commitments made in the terms of reference of the Joint Ministerial Committee (EU Negotiations).

2) What is your assessment of the European Commission's position that EU state aid rules should continue to apply to the UK after the end of the transition period?

In our response, the Welsh Government made clear that we do not advocate retaining alignment with EU State aid rules as an end in itself but believe it would be a price worth paying, if the alternative is a radically worse trade deal. It appears to us that such alignment may well be necessary to avoid the imposition of tariff and non-tariff barriers to trade between the UK and the EU market.

The UK Government's response to the Committee simply repeated its commitment to develop a separate and independent policy on subsidies with no alignment to EU rules. The UK Government further stated that they are continuing to develop a domestic policy alongside the EU negotiations and are working at pace to develop this policy with the intention of sharing more detail on domestic subsidy control with key stakeholders in due course.

The Welsh Government is alarmed at this confirmation that the UK Government are currently developing a future UK subsidies regime without input from DAs. This suggests that we will be faced by a *fait accompli* despite the contested issue of whether state aid is reserved or devolved and the major effects that a future UK subsidies regime will have upon other areas of devolved policy. . A coherent approach to the Assisted Areas map across the UK – which has always since devolution been agreed between the four governments – is essential to ensuring that the subsidies regime is implemented in a way which acts as a counter-weight to market forces which act to attract investment to areas which are already most economically successful.

The UK Government confirmed in its letter that it is seeking a *"progressive and comprehensive FTA similar to those the EU has struck with other countries such as Canada and Japan"*, rather than membership of the Single Market or Customs Union. Accordingly, level playing field commitments found in Accession Agreements akin to the one currently in place with Ukraine are currently ruled out as inappropriate to the (limited) scale of access that the UK is seeking. However, no mention is made of the European Economic Area Agreement, which would appear to be a helpful precedent given that the proximity and current inter-dependence of the UK and EU markets means the analogies with geographically distant markets such as Canada and Japan is not a good one.

Moreover, the letter fails to acknowledge the severe consequences that a basic FTA will have in terms of the UK economy, nor is any evidence presented to support the UK Government's claim that the advantages of a more light-touch subsidies regime will offset this throttling of the UK's access to its largest market and most important trading partner. This was a key question we asked that the UK Government address in our original submission.

3) The Prime Minister's speech of 3 February 2020 suggests that, while the UK will maintain a subsidy control system after the end of the transition period, this will not necessarily be based on EU state aid rules.

- What elements should the UK Government take into consideration in designing a new domestic system, especially as far as regional aid and the planned UK Shared Prosperity Fund are concerned?
- What implications, if any, does the uncertainty over the shape of a UK future state aid or subsidy control regime have for you, as aid grantor, and recipients in your nation?

In its response to the EU committee mini-enquiry, the UK Government states that it *"will continue working closely as one United Kingdom to understand the changing needs of local and regional economies and our response to that, including the role that the UK Shared Prosperity Fund can play."* Whilst the Welsh Government welcomes the UK Government's continuing commitment to a funding mechanism to replace European Structural Investment Funds, we are concerned that no commitment is made to retain and support the existing 'Assisted Area' system to enable authorities to target their activities at areas of most need. 'Assisted Area' status for regions in Wales has enabled the Welsh Government and Local Authorities to provide targeted support in order to offset Wales' structural disadvantages and facilitate economic development. The response does acknowledge that Devolved Administrations are responsible for their own spending decisions on subsidies, but does not commit to ensuring that this will include resources from the Shared Prosperity fund. We are also concerned that no detail has been provided with regard to the level of Agricultural Support to be provided, despite assurances provided in the 2019 Conservative manifesto that a Conservative government would "guarantee the current annual budget to farmers in every year of the next Parliament"

Whereas the Government during the term of office of Mrs May had signalled its intention to ask the Competitions and Markets Authority to act as a future UK State aid regulator, the UK Government in its letter states that its position on subsidies for the trade agreement negotiations with the EU does not necessarily require a domestic regulator *"as demonstrated by other countries, like Canada, that do not maintain a domestic subsidy control regulator to fulfil their trade agreement obligations with the EU"*. This is the first time that the UK Government has formally suggested that there may be no subsidies regulator in the UK post-Transition and we are extremely concerned at this announcement. Having a strong and impartial regulator, with sufficient policing powers to enable it to facilitate a robust UK subsidies regime, is vital to protect the UK's internal market and instil confidence in trading partners that UK authorities will not seek to undercut their businesses.

4) If the Protocol on Ireland / Northern Ireland entered into force, EU state aid rules would continue to apply to the UK in respect of measures affecting trade between Northern Ireland and the EU. What implications, if any, might this have for Wales as a devolved nation?

The UK Government's statement in response to this issue, that it will *"take into account the unique circumstances that have been agreed for the island of Ireland as we develop and implement our domestic policy on subsidy control and [we] intend to provide further information on this prior to the end of the Transition Period"* is an insufficient response given the risk to the economies of Northern Ireland, Wales and the rest of the UK. Currently, significant volumes of goods travel in both directions between Wales and Northern Ireland via Dublin; any increase in friction in these flows risks significant damage to the viability of Welsh ports and Welsh prosperity more widely.

It is vital that the UK Government immediately engage with the Devolved Administrations to develop the UK's future subsidy regime on a quadrilateral basis, to allow as much lead-in time as possible to limit the damage that increased friction to the movement of goods will bring to the Welsh economy and Welsh ports.

In addition, the UK Government's response makes no attempt to address the reach of the 'at risk' clause into support granted within Great Britain to companies with a presence in Northern Ireland. This is an issue that could potentially have far-reaching ramifications upon the freedom of Welsh authorities to support businesses and enable Wales' economic development.

We have repeatedly called on the UK Government to establish a joint working group on the Northern Ireland Protocol to support a common understanding of the implications of the Protocol on trade and competition within the UK. At the January meeting of the Joint Ministerial Committee (EU Negotiations) there was agreement to establish this joint working group. Despite continued representations, there remain no details on how and when this working group will be up and running.