



The Rt Hon Michael Gove MP
Chancellor of the Duchy of Lancaster
Cabinet Office
70 Whitehall
London SW1A 2AS

8 May 2020

Dear Michael

I am writing to you to set out some further detail on the Welsh Government's priorities in respect of level playing field issues, as part of the UK/EU future relationship negotiations. Whilst the Welsh Government recognises that certain level playing field policy areas are not devolved, their broad and crosscutting nature means that we have a strong interest in future level playing field regulation.

We have been clear that the Welsh Government would have set a different approach to the negotiations than the one advanced by the UK Government and we believe that in the current circumstances, the negotiations should be paused and the transition period extended. Despite this, we want to remain constructive in the negotiations to seek to ensure that Welsh interests and impacts are taken into account properly in the negotiations. We therefore continue to seek meaningful Ministerial arrangements for ensuring Welsh priorities are reflected in the development and evolution of agreed UK negotiating positions. In the meantime we intend to set out further detail on our negotiating priorities in a series of letters.

In 'The Future UK/EU Relationship: Negotiating Priorities for Wales', which we published in January 2020, we included as a priority the fullest possible access to the EU Single Market. We believe this should be prioritised over what we see as an extreme interpretation of the idea of "taking back control" which will have limited practical benefit yet will impose potentially enormous costs on individual businesses and the wider economy.

To take a specific example: the UK has played a significant role in the development of EU wide policy in areas such as Environmental Permitting (Integrated Pollution Prevention and Control), where the EU adopted the UK regime. Why would we not commit, at a minimum, to non-regression from this approach? The only interpretation of the UK Government's position is that you will be looking to set lower standards across many areas of Environment policy. This is not a policy position that we support. As we set out in further detail below, joint work through the Common Frameworks programme and the UK internal market is essential in this area in order to manage continued policy flexibility and scope for distinctive approaches across the countries of the UK.

Based on reports from the latest round of negotiations, the Level Playing Field remains a big issue and a challenging area of negotiations. It is clear that flexibility will be needed, as without compromise this area could prove to be a key stumbling block.

The European Union has been clear from the outset that access to EU markets will be reduced if the UK does not commit to dynamic alignment with EU level playing field regulation to ensure there is open and fair competition. It is difficult to imagine that an insistence by the UK that it does not need to and will not enter legal commitments to, at a minimum, non-regression will lead to any other outcome than a 'bare bones' Free Trade Agreement.

The latest economic analysis, included in our above paper, demonstrates that under any scenario where tariff or non-tariff barriers to trade with the EU are introduced, the UK economy as a whole will suffer negative impact. The greater the barriers the larger the impact. If the UK is to secure an agreement that meets the needs of the economy, the UK Government must be prepared to move from your initial position.

Environment

As a devolved area, it is vital any UK position is developed on the basis of the views of all four countries in the UK. The Welsh Government has consistently highlighted the importance of continuing to improve on our existing environmental standards if we are to address decarbonisation and biodiversity loss, act to combat the climate emergency and support businesses as we transition to a low carbon, circular economy. It is important that there is no reduction in the Welsh Government's and the Senedd's right to regulate; retaining existing levels of flexibility to set, where appropriate, regulatory standards to address Wales's specific circumstances and which reflect our sustainable development ambitions reflected in our legislative framework. It is also imperative that regulatory policy across the UK is developed collaboratively to build and promote intra-UK supply chains without resulting in competition between, and the economic undermining of, different countries' regulatory preferences. We will expect policy positions taken in England not only to avoid negative impacts on the environment in Wales but also on businesses in Wales. We will further expect at minimum to see continued UK Government commitment to the Common Frameworks programme as the basis for managing future policy divergence within the UK.

The UK Government's approach sets out a process of reciprocal commitments to not weaken or reduce protection afforded by environmental laws. What will be the nature of these commitments and how will these respond to the dynamic nature of regulation in this area? It is vital that input from Devolved Governments is sought on this matter, otherwise the resulting position will not be fit for the whole of the UK.

The environment covers a range of policy areas. For some areas, such as chemicals legislation, spearheaded by REACH (which allows the free movement of substances on the EU market and applies to substances manufactured or imported into the EU), securing alignment with the EU will help ensure that our processes continue to consistently reflect future scientific developments and help avoid any additional expenses for industry of having to meet two potentially different standards. There is no support in this sector for moving away from alignment with the EU system.

We must remember that in some other areas of Environment policy the UK may be considered to be *ahead* of the EU and more closely reflecting wider international developments; an example being the integrated systems-based approach to the management of our natural resources as opposed to the more EU medium-specific approach. However even in instances such as this, we would argue it is in our interests to work closely with the EU as well as other global players to 'level up' standards, rather than risk our competitiveness be undermined by lower standards elsewhere.

The UK Government has consistently stated that it intends to use the FTA process to ensure that the UK remains a world leader in Environmental policy; how will this be achieved? The UK Government needs to provide clarity on this issue to enable businesses to plan for future investment.

State Aid

Effective State aid regulation ensures a level playing field for businesses, allowing us to foster innovation through targeted support for research and innovation, whilst minimising the potential for damaging subsidy wars between regions competing to attract businesses. Post-Transition, a functioning level playing field within the UK will be just as important to Wales' future prosperity as a level playing field with the EU.

The UK Government has expressed a wish for the UK to adopt looser State aid rules in order to make it easier to intervene in failing industries and invest in British businesses. We do not accept that the UK's alignment with the EU's State aid rules has undermined our ability to support UK businesses: on the contrary, it is the non-interventionist policy choices of previous UK Governments that have led to the UK's consistent underspending on compatible State aid in comparison to major EU Member States. The European Commission's State aid Scoreboard for 2018 put the UK's *per capita* expenditure at less than half that of either France or Germany.

The regulation of subsidies is not just an EU requirement. WTO membership requires that we continue to comply with the WTO subsidy rules that underpin the EU rules regarding State aid. Further, the EU has signalled that access to the EU Single Market is dependent upon the UK's maintaining close alignment on State aid regulation; what benefit is there to be gained from having greater opportunity to more intensively support businesses if at the same time the UK government is tempering their access to EU markets?

Within the setting of any domestic policy, and particularly given the Government's stated commitment to 'levelling up', it is vital that the UK Government commits to maintaining the UK's map of 'Assisted Areas', including parts of Wales, that are eligible for a broader range of State interventions at higher aid intensities to offset historic and ongoing structural disadvantages. This will allow Wales and other historically disadvantaged parts of the UK to compete on a more even basis with wealthier regions. Maintenance of the UK's 'Assisted Areas' map will also ensure that future funding from any Shared Prosperity Fund can be targeted at those areas that are most in need, rather than on the basis of political expediency.

The Northern Ireland Protocol, signed by the UK Government, requires that subsidies provided to undertakings with a presence in Northern Ireland remain subject to EU State aid rules if the subsidies affect trade between Northern Ireland and the EU. This risks the UK's internal market being broken into a two-tier system, creating uncertainty both to businesses and to aid awarding bodies. Close alignment with the EU's State aid rules will minimise the potential for disruption within the UK no matter what the outcome of the current EU-UK FTA negotiations.

We believe that the UK Government should not jeopardise the rapid achievement of a FTA by insisting on an independent UK policy on State aid. What additional policy flexibility does the UK Government need from a State aid regime that will not be available under future EU policy? If there are no plans to change then why should the UK not commit to aligning with the EU and gain the benefits of such a commitment?

Post-Transition, it will be important that the UK's subsidies regime is policed by a regulator that is independent of government and fully autonomous, such as the Competition and

Markets Authority (CMA). Any attempt by the UK Government to bring State aid regulation in-house will send negative signals to both overseas trading partners and the Devolved Governments about the willingness of the UK Government to effectively regulate the provision of subsidies.

Governance and accountability for the UK State aid regime should be shared between the four administrations, with political-level decisions on the direction of future regulation being made by a Joint Ministerial Committee (JMC) rather than reserved to the Secretary of State for BEIS. The Inquiry Panel Chair positions for the regulator should include one allocated to the Welsh Government to ensure that a Welsh perspective is included when decisions are made.

Taxation

Given our geographical proximity to the EU and the extent of our trade, any future changes to taxation rates and standards in either party will have effects in both markets. It will therefore be in the mutual interest of both the UK and the EU to continue to cooperate closely on taxation matters post-Brexit.

The UK currently has a good record on taxation within the EU; and we see no reason to object to the EU's published negotiating mandate, which contains no reference to formal ongoing alignment with EU rules, merely non-regression, the upholding of common high standards, and corresponding high standards over time. The risk to the UK's economy from reduced access to the EU Single Market would likely far outweigh any benefits that deregulation and a reduction in taxation would bring.

Labour and Social Protection

Whilst employment law is currently for the most part a reserved matter, we are strongly opposed to any weakening of employment rights – as your Government also says it is.

We also believe it is vital that future UK employment legislation keeps pace with progressive developments at EU level supportive of fair work, a position reflected in the recommendations of the Fair Work Commission's report *Fair Work Wales*. International evidence from the OECD suggests that far from undermining competitiveness, high labour standards and smaller inequalities in the distribution of income and wealth, are associated with economic success¹.

We would expect to see this position reflected in the UK's upcoming Employment Bill. Further, it is crucial that the UK Government provides commitments to, and cooperation on, promoting gender equality in trade, aiming for mainstreaming across FTA chapters.

The UK currently exceeds the EU minimum standards in certain areas of employment law; we would not wish to see these hard-won rights eroded in the search for illusory short-term gains.

I note from the 'The Future Relationship with the EU; The UK's Approach to Negotiations' document, published on 27 February, that you will be seeking "reciprocal commitments not to weaken or reduce the level of protection afforded by labour laws and standards in order to encourage trade or investment". What sort of commitments will the UK Government be seeking to make? If the UK Government is committed to this position of not weakening or reducing protection then what is the rationale for not doing so in the FTA?

¹ <https://www.oecd.org/social/in-it-together-why-less-inequality-benefits-all-9789264235120-en.htm>

Given that the UK is already party to a number of international agreements that include commitments that bind both the current and future governments and parliaments, it would seem inconsistent to refuse to do so in this instance.

Competition Regulation

Given the importance of effective Competition regulation in protecting industry and consumers against unfair and injurious trade practices, and ensuring a level playing field for businesses, it is crucial that the future UK Competition regime is transparent and non-discriminatory, with robust enforcement procedures. This is a point acknowledged by the UK Government in the 'The Future Relationship with the EU; The UK's Approach to Negotiations' paper. This will encourage enterprise and efficiency, create a wider choice for consumers, help reduce prices and improve quality.

The Welsh Government's position on Competition is that the UK should retain full alignment with EU Competition rules in order to ensure maximum access to the EU's Single Market and avoid a 'race to the bottom' which could compromise our environmental and labour standards and distort the UK's own internal market. The UK's negotiations paper seeks for any future UK-EU FTA to commit both parties to maintain effective competition laws, including merger control, anticompetitive agreements and abuse of dominance. However, without a UK commitment to ongoing alignment with EU regulation there is a danger that, as the two regimes develop separately, regulatory drift develops and grows, risking our access to the EU Single Market.

Given that the UK Government has yet to identify a direct policy intention behind this refusal to commit to ongoing alignment beyond a desire for 'flexibility', in what areas does the UK Government envisage wanting to move away from EU regulations in this area? What possible benefit can be gained for the UK by such divergence that could offset any decreased access to the EU Single Market?

Concluding Remarks

Of course, the EU needs to recognise the leading role that the UK has played in developing the EU level playing field, including in establishing and upholding with both European and global partners the standards the EU wants the UK to follow post-Transition. We understand why the UK Government might be nervous that in some areas, such as competition law, an EU without the UK might make different policy choices.

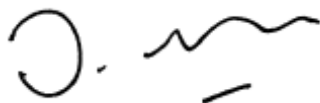
But we also believe the EU is serious – and not unreasonable - in its assertion that it cannot readily give maximum access to its market to an economy on its doorstep that plays by very different rules. We would argue that both in terms of the substance of current level playing field policies and in terms of the likelihood of achieving the right outcome to the negotiations, the UK Government must drop its rigid refusal to contemplate measures that go beyond those typically included in a comprehensive free trade agreement, and its strategy of seeking regulatory divergence, refusing close alignment of rules and rejecting any role for the European courts. Maintaining close and ongoing alignment with the EU on level playing field issues will enable a stronger and more effective relationship to be agreed, recognising that, given the level of economic integration between the UK and the EU, the UK will continue to work in partnership with the EU, and not in competition with it.

The UK Government must urgently justify the rigid position it is taking on these issues with proper economic analysis and evidence so that this information can positively influence negotiations in support of the UK's position.

I hope therefore that both the UK and the EU will recognise that compromise is very much in the interests of both parties, and that you will approach the negotiations on level playing field issues in that spirit.

I am copying this letter to the Secretary of State for Wales, the Cabinet Secretary for Constitution, Europe and External Affairs in the Scottish Government and the First Minister and Deputy First Minister in the Northern Ireland Executive.

Yours sincerely,

A handwritten signature in black ink, consisting of a large, stylized 'J' followed by a series of wavy lines and a short horizontal stroke at the end.

Jeremy Miles AS/MS

Cwnsler Cyffredinol a'r Gweinidog Pontio Ewropeaidd
Counsel General and Minister for European Transition