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Subject: Internal EU27 preparatory discussions on the framework for the future relationship: "Level Playing Field"

Origin: European Commission, Task Force for the Preparation and Conduct of the Negotiations with the United Kingdom under Article 50 TEU

Remarks: These slides are for presentational and information purposes only and were presented to the Council Working Party (Article 50) on 25 January 2018. The contents are without prejudice to discussions on the framework of the future relationship.

In December 2017, the European Council invited the Council (Art. 50) together with the Union negotiator to continue internal preparatory discussions on the scope of the future EU-UK relationship. The slides support those discussions. They are based on the April European Council guidelines which continue to apply in their entirety.

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Internal preparatory discussions on
framework for future relationship

Level Playing Field

An introduction

AD HOC WORKING PARTY ON ARTICLE 50 (*Seminar mode*)
25/01/2018



Outline

1. Introduction

- Default scenario
- Transition
- Future relationship

2. Key elements for the way forward

- Substantive rules
- Enforcement mechanism
- Dispute settlement system

3. EU autonomous measures

Default scenario

- EU acquis on state aid, taxation, environment, labour stops applying
- Fall back on international framework:
 - WTO system for trading in goods (Agreement on subsidies and countervailing measures)
 - Multilateral environmental agreements
 - Conventions and recommendations of the International Labour Organisation
 - OECD Base Erosion and Profit Shifting (BEPS) and transparency standards
- Scope and enforcement

Transition

If a Transition Agreement with the UK is reached (EUCO guidelines 15/12/2017 and negotiating directives)

- UK applies all EU acquis and keeps participating in the Single Market, for a limited period
- EU law continues to apply
- UK no longer part of the EU institutions and bodies

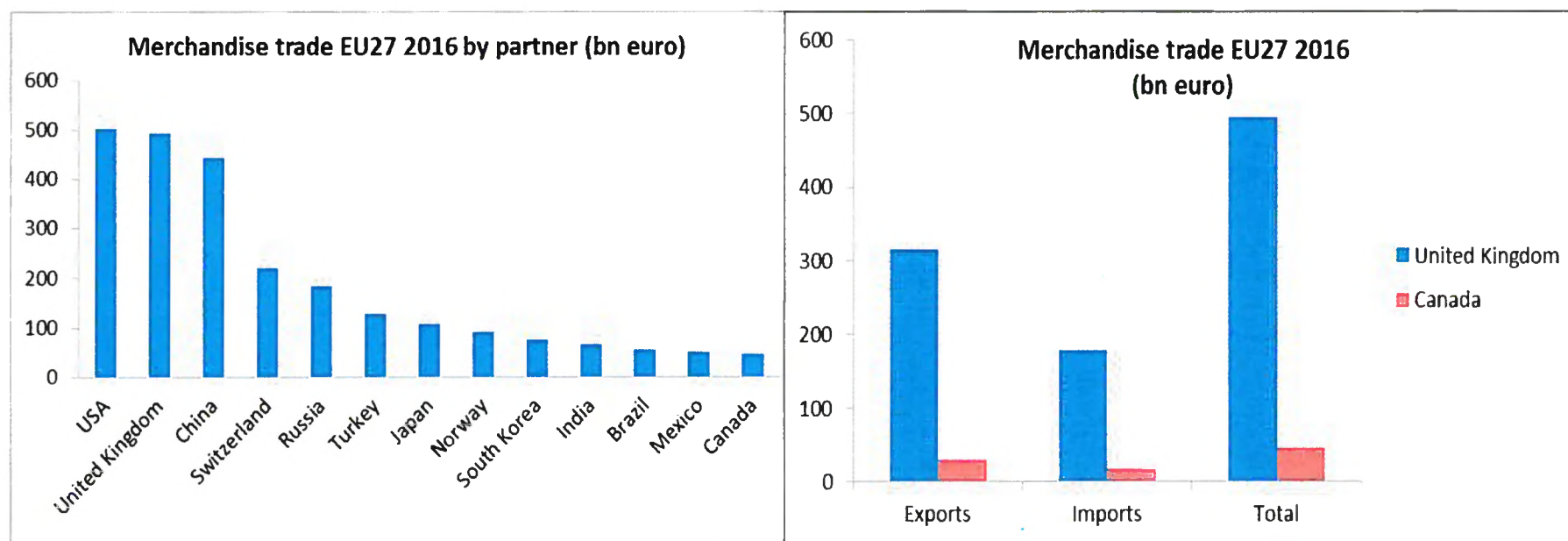
Future relation European Council Guidelines – April 2017 paragraph 20

"Any free trade agreement should be balanced, ambitious and wide-ranging ... A level playing field must be ensured, notably in terms of competition and state aid, and in this regard encompass safeguards against unfair competitive advantages through, inter alia, tax, social, environmental and regulatory measures and practices."

- LPF has to be seen in the context of the future trade relationship
- LPF cuts across different policy areas, in particular competition and state aid, social and environmental standards, taxation, other regulatory measures and practices

LPF - Specificities of the EU/UK relationship

- The depth and breadth of the EU–UK economic integration
- The geographic proximity of the UK to the rest of the EU



Import dependency on EU (% of total supply)			EU import dependency		
UK	US	Canada	UK	US	Canada
7.7%	1.3%	1.7%	1.0%	1.3%	0.1%

→ Need to cater for the specificities of the EU-UK relationship

LPF – key elements for the way forward

- ❑ Set LPF conditions as a **horizontal framework of the future economic relation**
- ❑ Focus on the policy areas that are **most relevant for LPF** and identify in each area the **key components**
- ❑ Find the **right balance** between LPF safeguards and regulatory autonomy
- ❑ Build up an effective system, based on **3 interlinked pillars**:
 1. **Substantive provisions**
 2. **Enforcement mechanism**
 3. **Dispute settlement system**

Substantive provisions

State aid

Taxation

Environment

Labour

General approach: Non-lowering of standards



Provisions of Artt.
106-108 TFEU +
Union instruments



- Tax good governance clause
- Requirements on exchange of information and anti-tax avoidance
- Code of conduct on business taxation



General principles and substantive provisions
anchored in international law and derived
from relevant EU rules
+
Non regression clause



The three components of governance of an international agreement

1. Ongoing management / supervision:

Joint Committee



2. Dispute settlement

Political (Joint Committee)

Judicial (Arbitration)

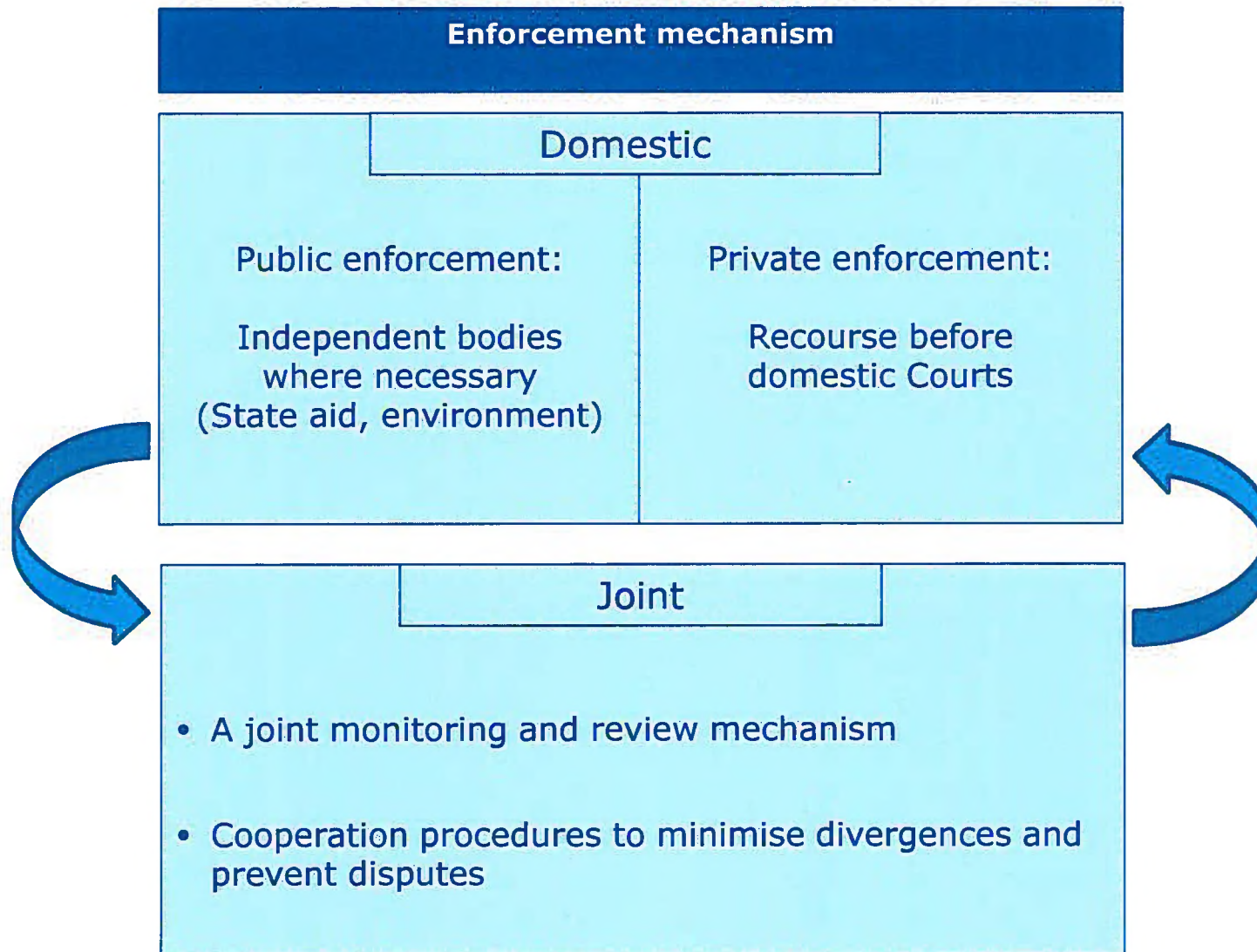


3. Enforcement after dispute settlement

Sanctions



LPF – enforcement mechanism and structures



LPF – dispute settlement system

Key questions for LPF are the **when & how** and the **sanctions** mechanism

When & how:

- Dispute settlement should in principle be available for any violation of the LPF provisions
- Two stages:
 1. A discussion forum, with a timeframe.
 2. A dispute settlement procedure



The possible options for judicial dispute settlement are subject to constraints: concepts derived from EU law can only be interpreted in a binding way by the ECJ.

LPF – Sanctions regime

Available **sanctions**:

- In principle sanctions should be available for any violations of the LPF provisions
- A menu of options available exists
 - suspension of obligations, temporary compensations, financial sanctions, cross retaliation, "guillotine clause", etc.
- Interim measures need to be available in some areas
 - e.g. State aid
- Post-dispute enforcement system depends on the model chosen for the dispute settlement system, which in turn depends on content



EU autonomous measures

- Horizontal, not Brexit-specific matter, even if it has a clear preparedness angle.
- In compliance with the EU international obligations (WTO).
- Few examples:
 - ❑ Taxation: 'black' listing of non-cooperative jurisdictions.
 - ❑ State aid: specific instrument in aviation, but not possible for goods (Agreement on subsidies and countervailing measures).
 - ❑ Sustainable development: WTO exceptions, where necessary for health or environmental reasons.
 - ❑ EU TDI: on-going review

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Level Playing Field State Aid

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Key features of EU State aid control

- ☐ Primary law (TFEU art 107, 108 and 109) complemented by secondary law (Guidelines);
- ☐ Ex ante control: by Member States under 'Block Exemptions' (97%) and by the COM for larger/more distortive measures;
- ☐ Transparency, ex post control, and ex post evaluation of aid.
- ☐ The ECJ reviews COM decisions (existence and compatibility of aid); National courts may decide if aid, but not on compatibility.

Secondary State aid law

- ❑ Significant body of law, including Guidelines and Regulations (e.g. General Block Exemption)
- ❑ Most is adopted by the COM, but also some Council Regulation
- ❑ Clarifies how the Treaty rules on State aid are applied in practice by the COM and how Member States can grant aid without prior COM approval
- ❑ ECJ case law focuses on the notion of aid, the ECJ leaves a margin of discretion on compatibility

Default scenario for State aid

- ❑ The WTO system of subsidy control applies, BUT:
 - ❑ Limited to goods
 - ❑ Damage to trade would have to be demonstrated
 - ❑ Remedies are limited and apply subject to strict conditions – the EU could start an ex officio investigation regarding the subsidised imports and impose import duties, provided i) there is a material injury to the Union industry or threat of material injury and ii) an EU interest to act.

State aid disciplines in existing FTAs

❑ Existing FTA State aid provisions (CETA/KOR/JAP) build on WTO (WTO+):

- Limited substantive provisions focused on transparency of subsidies and consultation in case of breach (e.g. CETA)
- Leave out services completely (e.g. CETA) or only some categories (JAP);
- State aid provisions with limited dispute resolution system in the FTA

Ad-hoc model – Building blocks

- Substantive rules: equivalent to the EU State aid rules, including transparency; Quid a mechanism ensuring convergence in case of changes to those rules over time?
- Enforcement through ex ante control by an independent State aid authority, having the same powers as the COM
- Dispute resolution and remedies. Effective, swift and unilateral remedies, within and outside the EU-UK Agreement, to address aid threatening the level playing field.

Conclusion

- International rules do not adequately address the (potential) distortive effects of subsidies on investment, trade and competition and
 - the close integration of the UK in the EU economy and its value chains,
 - the long-standing and deep trading relations,
 - and the geographical proximity of the UK to the EU
- Means the EU-UK Agreement will have to include robust provisions on State aid to ensure a level playing field with the Member States.

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Level Playing Field Taxation

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Agenda

- Taxation: the acquis communautaire
- Consequences of Brexit
- Risks to the level playing field post-Brexit
- Options for the future
- Proposed approach for a level playing field in taxation
- Monitoring and enforcement
- Summary

Direct Taxation: key elements

- **Corporate Tax Directives:**
 - *Interest & Royalties (Dir. 2003/49/EC); Mergers (Dir. 2009/133/EC) and Parent-Subsidiary (Dir. 2011/96) Directives*
- **Dispute Resolution Directive** (Dir. 2017/1852)
- **Recovery Directive** (Dir. 2010/24/EU)
- **Anti-Tax Avoidance Directive** (Dir. 2016/1164)
- **Directive on Administrative Cooperation** (Dir. 2011/16/EU)
- **Code of Conduct for Business Taxation**
- **EU List of uncooperative tax jurisdictions**

Consequences of Brexit

- UK no longer bound by *acquis communautaire* on taxation.
- EU law-based rights, obligations and benefits cease, for instance:
 - ❖ End of legal requirement for the UK to exchange information with EU Member States on tax matters (and vice-versa);
 - ❖ End of legal obligation for UK to apply anti-tax avoidance provisions;
 - ❖ End of UK's political commitment to the Code of Conduct : no standstill/roll-back of harmful tax regimes
 - ❖ UK loses benefits of the EU Corporate Tax Directives;

Risks for the EU27 – Default scenario

- **Clear risks** - but depends on yet undefined future UK tax policy.
- **UK policy today:** low corporate tax rate (19%) with plans to lower further; tax policies aimed at gaining competitive advantage; large number of offshore entities.
- **Impact of Brexit:** UK likely to use tax to gain competitiveness – very limited legal/political restrictions to prevent this.
US tax reform could increase competitive pressure on UK.
- **Key risk:** Targeted UK tax measures to attract investment and business.

Options for the future

✗ Internal Market

Direct taxation acquis

- *Corporate Tax Directives*
- *Dispute Resolution Directive*
- *Anti-Tax Avoidance Directive*
- *Administrative Cooperation Directive*
- *Tax Recovery Directive*
- *Code of Conduct for Business Taxation*
- *EU list of non-cooperative tax jurisdiction*

Enforcement/ECJ

✓ External relations

- **Type 1:** Some specific agreements on taxation between the EU and San Marino, Liechtenstein, Monaco, Andorra and San Barthelemy.
- **Type 2:** Good governance clause (Canada/Singapore)
- **Type 3:** Non-binding OECD-BEPS standards

Proposed approach for level playing field in taxation

- **Overall philosophy:** principle of **non-lowering of existing standards** that are important for the Level Playing Field.
- Specifically:
 1. Tax good governance clause;
 2. Binding requirements on:
 - ❖ Exchange of information;
 - ❖ Anti-tax avoidance measures;
 - ❖ Public CBCR for credit-institutions and investment firms
 3. Code of Conduct on business taxation (mirroring EU Code);
- EU has its unilateral listing process for uncooperative tax jurisdictions

Monitoring and Enforcement

- Commission monitors application legally binding requirements by the UK. Code of Conduct Group the political commitments.
- **Horizontal dispute settlement** of Agreement for any breach or concerns
- **Dispute resolution** and **sanction regime** aligned to wider procedures of the Agreement

Summary

- EU27 interest to shape negotiating position, taking into account the UK's unique "proximity/market size" mix.
- Target only those tax standards most important for the level playing field.
- Both political and specific legal commitments.
- EU27 continue to have a unilateral tool: EU listing process

Thank you for your attention

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Level Playing Field Environment and Labour

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25/01/2018

Outline

- I. The level playing field & the importance of labour and environment policies
- II. The FTA approach to trade and environment and labour
- III. Developing a tailored approach for the relations with UK

I

The level playing field & the importance of
labour and environment policies

The default - International framework

- UK has signed up to international environmental agreements, a number of ILO conventions and the 1961 Council of Europe European Social Charter
- UK free to denounce
 - pressure on European Convention on Human Rights,
 - departure from London Fisheries Convention
 - departure in 1985 of ILO minimum wage fixing machinery Convention
- Multilateral environmental conventions of limited scope and enforceability

Risks – no level playing field protection

- UK can decide environmental protection
 - Aiming to increase competitiveness
 - Imposing costs on EU citizens and companies
- UK can reduce labour and social protection
 - Aiming to increase competitiveness
 - EU workers' rights put under strain
 - Undermining Europe as an area of high social protection

Some impacts and key facts - Environment

- Industrial Emissions Directive – best available technologies requirement
 - Currently applicable to more than 4,000 UK installations (industry, agriculture, energy), including 114 large combustion plants (e.g. power stations) which have temporary derogations
 - Risk UK prolongs or extends derogations – with clear transboundary and competitiveness costs
- National Emission Ceiling Standards
 - Reduced UK ambition could result in neighbouring states requiring up to 9% more effort to reach their objectives. This is a significant cost.
- Potential 4.7 Billion euro gain for UK industry per annum in reduced direct costs (and even more indirect costs through e.g. reduced environmental taxation) whilst increasing pollution for neighbours.

Level playing field challenges – labour and social protection

- Restructuring of companies
 - UK could opt for reducing information and consultation rights for workers in order to reduce cost and delays for collective dismissals
 - UK could opt for derogating from the maintenance of rights for lowering cost of company transfers
- Export processing zones (EPZ)
 - UK could opt for derogations in EPZs on collective bargaining, working conditions, social security contributions and labour inspection resulting in lower protection
- Reducing levels of occupational safety and health
 - Higher exposure to chemicals and carcinogens resulting in lower production cost
- Reducing rights of collective bargaining in order to lower wages

II

The FTA approach to
trade and environment and labour

FTA Overall approach

- Ensure that trade contributes to sustainable development
- Strengthen the multilateral governance and standards on labour (ILO) and environment (MEAs); no parallel set of bilateral rules on labour and environment
- Avoid a 'race to the bottom' through selectively weakening domestic labour or environment protection (non-regression clause)
- Long-term engagement: incentivize partner countries to work with us and systematic dialogues on sensitive issues

FTA approach to environment and labour

- Effective implementation of Multilateral Environmental Agreements and ILO conventions
- Thematic articles on trade in timber, fisheries, climate change, biodiversity
- Adherence to and implement ILO core labour standards
- Commitments on occupational safety and health (OSH), labour inspection and access to remedies
- Promotion of wider decent work agenda with particular focus on acceptable minimum employment standards for all workers and non-discrimination in respect of working conditions

Non regression clause in FTA (Japan)

- The Parties shall not encourage trade and investment by relaxing or lowering the level of protection provided by their respective domestic environmental or labour laws and regulations. To this effect, the Parties shall not waive or otherwise derogate from such laws and regulations or fail to effectively enforce them through a sustained or recurring course of action or inaction, in a manner affecting trade or investment between the Parties.

III

Developing a tailored approach for the relations
with UK

Key elements for level playing field

- Joint commitment to high level of protection
- Focus on competitiveness in a context of economic complementarity and geographic proximity
- Principles and substantive provisions anchored in EU and international law
- Principle of << non-lowering of standards>> of protection below the pre-Brexit level and non-regression clause
- Upholding standards across whole territory

Key areas – environmental protection

- Industrial emissions
- Air quality
- Water quality – including nitrates and marine
- Waste management
- Nature conservation
- Impact assessments
- Transparency, permitting, controls, public & private enforcement

Key areas - labour rights and social protection

- Fundamental rights at work
- Occupational Health and Safety
- Fair working conditions and employment standards
- Labour inspection and access to remedy
- Information and consultation rights at company level
- Fair wages
- Right to social security

Enforcement

- Respect the logic of reciprocity
- Specific public enforcement structures where appropriate
 - Domestic authorities upholding environmental standards
 - Build on both private and public enforcement in the parties' jurisdictions.
- Need for consistent information and data
 - Access to information, public participation in decision-making
 - Commitment to transparency and monitoring based on EU and international standards
- Dispute settlement / sanctions: horizontal matter for the LPF provisions