The primary purpose of the House of Lords European Union Select Committee is to scrutinise EU law in draft before the Government take a position on it in the EU Council of Ministers. This scrutiny is frequently carried out through correspondence with Ministers. Such correspondence, including Ministerial replies and other materials, is published where appropriate.

This edition includes correspondence from 9 May 2013- 30 November 2013

ECONOMIC AND FINANCIAL AFFAIRS
(SUB-COMMITTEE A)

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ANNUAL REPORT ON INTERNAL AUDITS IN 2012 (13213/13)

Letter from the Chairman to Sajid Javid MP, Financial Secretary, HM Treasury

Thank you for the Explanatory Memorandum, dated 26 September 2013, from your predecessor, Rt. Hon Greg Clark MP, on EM 13213/13: the Annual Report to the Discharge Authority on Internal Audits carried out in 2012. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 15 October 2013.

We note the Commission’s assessment that this report demonstrates steady improvement in the Commission’s internal framework. We also note that paragraph 43 of the EM, on the Government’s assessment of the report, is identical to that contained in EM 144431/12 on the 2011 report. In light of this, we would be grateful for more detail on your views. In particular, in what specific ways do you believe that standards have improved in 2012 in comparison to 2011? What priorities would you identify to ensure that such steady progress is maintained and enhanced in 2013?

The report also makes clear that standards, although improving, remain uneven across DGs. Which in your view are the most significant weaknesses that need to be addressed, both in terms of the Commission as a whole, and in relation to individual DGs? Which DGs would you identify as most at risk? What would you identify as the root causes of inconsistent standards across DGs, and how can such inconsistency be corrected?

We would be grateful for a response to these questions by 12 November 2013. In the meantime we are content to clear the document from scrutiny.

15 October 2013

Letter from Nicky Morgan MP, Economic Secretary to the Treasury, HM Treasury, to the Chairman

Thank you for your letter of 15 October on the Annual Report on Internal Audits.

With regard to ways standards have improved in 2012, the Internal Audit Service (IAS) have achieved this in a number of ways by following a risk based approach. It has continued to focus on financial compliance and IT audits as key areas of risk and an increasing emphasis on performance audits. The IAS works with other parties, including the European Court of Auditors to ensure that, collectively, audit plans cover all entities rated as high risk and which are material for the implementation of the EU budget. To address risks of error in payments the IAS examines control strategies to make sure that these are proportionate to the risks and will be effective in preventing and detecting error with dissuasive administrative penalties and reports on the residual rate of error. Therefore priority is also given to audits to examine whether a coherent control strategy is being implemented for every significant area of expenditure.

The Government draws further assurance from the IAS’s successful delivery of its programme of work (it carried out 100% of priority audits in 2012); the acceptance by Commission management of the recommendations made in audit reports (all of those in the second most significant category of recommendation were accepted, with no high category recommendations); and the strong record of recommendations being implemented, as tested in IAS follow-up audits.

More specifically the IAS has identified good practice and progress in the establishment and maintenance of effective and proportionate control systems. These practices include a well established Annual Activity Report (AAR) process for the Commission itself, which is a key management accountability and assurance tool, supporting the Declarations of Assurance made by Authorising Officers by Delegation; and a well prepared closure process for the 2000-06 programming period in respect of the European Development Funds (DG REGIO) and European Social Funds (DG EMPL).
In terms of maintaining and enhancing progress going forward, the IAS has drawn up a new Strategic Audit Plan covering the period 2013-15. This will continue to follow a risk based approach, with a focus on financial/compliance and IT audits. It will also step up efforts on activities in performance auditing, which was a new area of activity in its 2010-2012 strategic audit plan. This approach should ensure that IAS activities are prioritised appropriately and as a result that control improvements continue.

The IAS should specifically maintain audit work already planned in respect of ensuring that a coherent control strategy is being implemented for every significant area of expenditure, that it addresses areas of inconsistency and unsuccessful co-ordination (such as in cross Directorate audits), that it delivers on agreed improvement action plans and it gives attention to areas which may represent previously unidentified areas of risk or control weakness (including new structures and new programme initiatives).

Moving on to weaknesses and DGs at risk, the IAS highlight a number of areas that require improvement, such as the need for better co-ordination between units to more effectively monitor application of EU law in the Customs area and EC Central Services developing improved frameworks for managing and monitoring staff allocation to ensure effective achievement of staff reduction targets (5% during the period 2013-17).

On specific DGs, the IAS flagged that DG REGIO needs to improve checks on audit authorities’ annual control reports, including inconsistencies in areas such as statistical sampling and the extent and the depth of its own on the spot tests on reported error rates, while DG ESTAT has to make ground on statistical data production to minimise risks of inconsistencies, gaps/overlaps, low quality of data and disruption to business continuity.

Other examples are risk management practices and controls in ECFIN regarding the management of new financial instruments and the need for improvements in programme closure processes, for example, in DG REGIO.

The IAS reports that improvement recommendations have been accepted and improvement actions are already in progress in a number of cases, for example, in DG REGIO and DG ESTAT. It will carry out follow-up audits to check that improvement actions have been implemented effectively.

There are three main reasons for inconsistent standards across DGs: the differing interpretations of guidance, ineffective coordination of cross Directorate activity and inconsistent application of control strategies. These issues can be best addressed by: reinforcing the responsibilities of relevant DGs or Central Services to develop guidance and monitoring tools to test their application; and by assessing progress in these areas within the priorities in the IAS audit plans, as it is already, for example, in an overview report planned to identify any recurrent and Commission-wide issues in the application of EU law.

8 November 2013

Letter from the Chairman to Nicky Morgan MP


We are grateful to you for this thoughtful response to our letter of 16 October 2013. As you know, we have over the past year raised concerns about HM Treasury’s engagement with this Committee, and we are therefore pleased to note the positive way in which your letter engages with the queries that we raised.

19 November 2013

Letter from the Chairman to David Gauke MP, Exchequer Secretary, HM Treasury

You indicated a risk that this proposal might be inconsistent with international work to develop a
global standard in the automatic exchange of information. We understand that negotiations are at an
early stage but can you be more specific about your concerns? Which elements of this proposal might
be inconsistent, and can you give us an example of the problems that might arise? Will the proposal
be practical from an administrative point of view? Can you confirm that exchange of information will
be automatic rather than upon request? If so, what is being done to ensure the optimal exchange of
information, and that an unnecessary administrative burden is not created? On a similar note, what
work is being done to define exactly what aggressive tax planning is?

Bearing in mind the precedent of the EU Savings Directive, can you also clarify how this proposal
would be applied to the UK Crown Dependencies?

We would be grateful for a response by 30 August 2013. We would also appreciate updates as
negotiations progress. In the meantime, we will continue to hold this document under scrutiny.

17 July 2013

Letter from David Gauke MP to the Chairman

Thank you for your letter of 17 July in response to the Explanatory Memorandum submitted to
directive 2011/16/EU with regards to the mandatory automatic exchange of information in the field of
taxation

As you know, the Government strongly believes that tax evasion is a global issue requiring a global
solution. As a result of UK leadership we now have a realistic prospect of achieving a single new
global standard for automatic exchange of tax information which will enable a step change in the fight
against evasion. The development of this new standard is being taken forward by the OECD,
supported by the pilot announced by the UK, France, Germany, Italy and Spain and with the
endorsement of the G8 and G20. EU action can help in promoting rapid adoption of this new
standard globally provided that EU proposals are fully consistent with the standard. Competing
standards would vastly increase compliance costs for business and governments and would stand in
the way of a global solution by providing an easy excuse for some jurisdictions not to move to
automatic exchange.

The European Commission’s new proposal is high level and unclear in a number of respects, and
therefore the exact detail will only emerge as discussions take place. It is therefore difficult at this
time to provide a substantive response to your points.

However, I can confirm that this proposal to amend the Administrative Cooperation Directive relates
to the automatic exchange of tax information. I can also confirm that it does differ from the emerging
global standard, for example, with the inclusion of capital gains rather than gross proceeds. In addition
the information to be exchanged is not properly defined which leads to uncertainty in application, as
opposed to the precision found in the new standard.

In early Brussels meetings on the proposal we have made it clear that we cannot support any
proposal which is not fully consistent with the global standard. A large majority of Member States take
the same view. As you will know this is a dossier that requires unanimity agreement.

Turning to your point about the Crown Dependencies, the Isle of Man, Guernsey and Jersey all
voluntarily abide by the EU Savings Directive. Whether they will wish to do the same under an
amended Administrative Cooperation Directive, if and when agreed, will be a matter for them.
However they have already fully committed to the new standard in automatic exchange of
information so will nevertheless be automatically exchanging the same information.

Please be assured that we will fully engage in discussions with the European Commission, and other
Member States going forward, with the key objective of ensuring that there is a consistent approach
to any action taken at the EU level with ongoing discussions through the OECD, and G20 to develop
a global standard.

22 August 2013

Letter from the Chairman to David Gauke MP

Thank you for your letter, dated 22 August 2013, on EM 10243/13, on automatic exchange of
information in the field of tax. The House of Lords European Union Sub-Committee on Economic and
Financial Affairs considered this document at its meeting on 10 September 2013.
We are grateful for your detailed response to our queries. We understand that there is a long way to go with negotiations and more detail regarding the proposal will emerge over time. As such, we will continue to retain this document under scrutiny and would welcome regular updates as negotiations proceed.

10 September 2013

BANK RECOVERY AND RESOLUTION (11066/12)

Letter from the Rt. Hon. Greg Clark MP, Financial Secretary, HM Treasury, to the Chairman

I last wrote to you on 15th February to provide an update on the European Commission’s proposal for a Bank Recovery and Resolution Directive (RRD).

I am grateful for your Committee’s continued interest in the dossier and am pleased to provide you with a further update, following the May ECOFIN. Indeed, given that the March European Council concluded that agreement on the RRD should be reached before June 2013, this is a particularly pertinent moment to update you. We consider that the Irish Presidency is likely to aim to reach a general approach at the June ECOFIN (21 June).

While achievable, this goal is ambitious as there are a number of outstanding issues where compromises still need to be reached. Given the anticipated timetable, I hope this update will be sufficient to enable your Committee to clear the RRD from scrutiny.

During the negotiations we have established constructive relationships with the Presidency, other Member States and the Commission which have helped to shape the proposals in a way that will enhance the effectiveness of the recovery and resolution framework. I provide more detail on progress that has been made in the main elements of the Directive below.

RECOVERY AND RESOLUTION PLANNING AND PREVENTATIVE POWERS

We have continued to support the inclusion of recovery and resolution planning provisions, as well as the proposed preventative powers. These proposals are likely to be retained.

EARLY INTERVENTION

As detailed in our June 2012 explanatory memorandum, the Government had some reservations about the implications of the Commission’s proposed intra-group financial support provisions and special manager tool. With the caveat that the negotiations are still ongoing, we have considerable support to be able to secure appropriate safeguards so that these tools can operate without prejudice to any ring-fencing regime that Member States might impose to enhance financial stability. We also have considerable support for our position that the special manager tool will not be used on any institution in the UK without the consent of UK authorities.

RESOLUTION TOOLS

As you are aware, in the UK, the Banking Act 2009 already provides the Bank of England with the sale of business and bridge institution tools. In the 2012 Banking Reform White Paper, the Government outlined its preference for introducing the bail-in tool through the RRD. The Government therefore broadly welcomed the Commission’s proposed set of resolution tools.

In particular, we have sought to ensure that the bail-in tool is credible and effective across the EU, since this is an important tool for the resolution of the most systemic banks. The Government takes the view that the EU bail-in tool should provide national authorities with statutory bail-in powers covering a broad scope of liabilities. The broad scope should be supplemented with a Minimum Requirement for Eligible Liabilities (which is similar to the Primary Loss Absorbing Capacity requirement recommended by the Independent Commission on Banking [ICB]). While there are outstanding details relating to the design of the bail-in tool still to be worked through, in particular in relation to the degree of discretion available to resolution authorities when they use the tool, we believe that there is broad support for a credible bail-in tool.
DEPOSITOR PREFERENCE

A key recommendation of the ICB was the implementation of insured depositor preference. The Commission’s initial proposal would have prevented that. However, there seems to be agreement amongst most Member States that insured depositors should benefit from preference in the creditor hierarchy. There is also a debate about whether preference should be expanded to a broader set of depositors.

THE ROLE OF THE EUROPEAN BANKING AUTHORITY (EBA)

We have previously noted that Member States, including the UK, were carefully considering the proposed role for EBA in the RRD. This continues to be the case and the issues remain under discussion.

THE ROLE OF THE EBA AND THE EUROPEAN COMMISSION IN RELATION TO THIRD COUNTRIES

We have also been carefully considering the implications of the proposed roles for EBA and the European Commission in relation to Member States’ ability to establish appropriate cooperation arrangements with third country authorities. At this stage of the negotiation we are hopeful of securing safeguards that will preserve sufficient Member State competence in this area.

RESOLUTION FINANCING

Resolution financing is proving to be a challenging aspect of the negotiation. The issues are complex and we remain sceptical about some aspects of the proposals. However we are working to ensure a sensible outcome that does not create moral hazard.

17 May 2013

Letter from the Chairman to the Rt. Hon. Greg Clark MP

Thank you for your letter, dated 17 May 2013, on EM 11066/12 on the Recovery and Resolution Directive (RRD). The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 4 June 2013.

You have requested that we now consider clearing the document from scrutiny. However, it is clear from your letter that agreement on some of the key elements of the proposal, notably on the bail-in tool, depositor preference, the role of the EBA and resolution financing, remains some way off. On bail-in and depositor preference, whilst you refer to insured depositors, you make no reference to uninsured depositors. Can you confirm reports that Member States are now moving towards favouring large uninsured depositors over bondholders when imposing losses on a failing bank’s creditors? What are the implications of this? Can you confirm that the Chancellor of the Exchequer has warned that this may create perverse incentives? What will be the consequences of providing, as you desire to see, broad discretion to Member States in the operation of bail-in? The need to ensure that a bail-in is handled with the utmost care is apparent in light of recent events in Cyprus. Therefore any flaws in the RRD bail-in provisions could prove catastrophic, creating a danger of bank runs and the collapse of confidence in a Member State’s banking sector, not to mention the wider danger of contagion across the EU. How in your view can the bail-in mechanism be most appropriately designed to overcome these dangers?

We regret that you have been unable to give us more information on the nature of discussions on the role of the EBA, and would be grateful for clarification of the main areas of concern. On resolution financing, you state that this is a challenging aspect of the proposals, and that the Government are sceptical about some aspects. What further information can you give us? Can you confirm reports that the Chancellor believes such a fund to be “totally useless” for countries with large banking sectors, and which would take decades to build up?

Therefore, whilst we recognise the urgency of seeking agreement on this important proposal in order to provide greater certainty for the EU banking sector, the need to ensure quick agreement does not obviate the need to ensure that the legislation is effective. We are heartened to hear that you have formed constructive relationships with the Presidency, other Member States and the Commission during negotiations, and we urge you to do all you can to ensure that the legislation is effective, and that it will not have any inadvertent negative effects.

We are unable to clear this document from scrutiny until you provide us with further information in response to these questions. We would require a response from you by Tuesday 11 June in order to
allow us to consider clearing the document before the 21 June ECOFIN. In the meantime we will continue to hold the document under scrutiny.

4 June 2013

**Letter from the Rt. Hon. Greg Clark MP to the Chairman**

Thank you for your letter of 4 June, on the European Commission’s proposal for a Bank Recovery and Resolution Directive (BRRD). To keep you updated of the latest developments, I would like to inform you that the Irish Presidency still aim to reach a general approach on this file at the 21 June ECOFIN. As you have noted, there are a number of key areas that still warrant further discussion before an agreement can be found. It is likely that such discussions will continue right up until the date of ECOFIN and most likely on the day of Council itself. Given the anticipated timetable, I hope this further update will be sufficient to enable your Committee to grant a waiver or clear the proposal from scrutiny in advance of June ECOFIN.

Your letter raises a number of questions, on the treatment of uninsured depositors, bail-in, role of the European Banking Authority (EBA), and resolution financing. As you may be aware, the Chancellor made interventions on many of these points at the May ECOFIN. I provide more detail on these elements of the Directive below.

**TREATMENT OF UNINSURED DEPOSITORS**

The treatment of uninsured depositors in resolution is a more complicated issue than for insured depositors. On the latter, the Government supports the recommendation of the Independent Commission for Banking (ICB), that there should be preference in the hierarchy for insured depositors. At the May ECOFIN, the Chancellor was clear in his intervention that Member States must stand behind their commitment to insured depositors. Preferring insured deposits makes this task easier for Member States to meet this commitment as it reduces the likelihood that these deposits would need a pay-out by the Deposit Guarantee Scheme (DGS), in the event of a bank failure. From the ECOFIN discussions there seems to be broad agreement amongst most Member States for this approach.

The treatment of uninsured depositors requires further consideration. The key issue is to ensure that the protection for insured depositors is not undermined. There has also been some discussion about either possibly broadening this depositor preference, or creating a secondary preference (behind those insured depositors). If this is the case, we need to ensure that there is a clear definition of what would be within this category, in order to minimise unintended consequences for corporates.

**BAIL-IN**

We still seek to deliver a credible and usable bail-in tool. This will be one of the key resolution tools in ensuring the effective resolution of systemically important bank. Most Member States support this ambition.

Recent events in Cyprus have indeed highlighted the need to consider the design of the tool carefully. The Government considers that the bail-in tool should provide national authorities with statutory bail-in powers covering a broad scope of liabilities. This should be supplemented with a requirement for banks to hold a minimum amount of high-quality loss absorbing debt. This is equivalent to the Primary Loss Absorbing Capacity requirement recommended by the ICB.

The ICB recommended that this minimum requirement should only consist of regulatory capital, and subordinated and senior unsecured debt with greater than one year remaining on its term. If banks are required to hold a sufficient amount of liabilities that are more feasible to bail-in, this will reduce the run risk when the tool is triggered. Since Cyprus, Member States seem to be more open to this design.

**THE ROLE OF THE EUROPEAN BANKING AUTHORITY**

The proposed role of EBA remains under discussion. There is acknowledgement that EBA has a role to play in ensuring that good practice is followed while implementing and undertaking recovery and resolution matters. However, Member States, are keen to ensure that there is an appropriate balance of decision making power between home and host authorities, whilst ensuring that decision making and fiscal responsibility are aligned.
We are also seeking to ensure that the role of the EBA is in line with their powers and responsibilities as defined in the Regulation which establishes them. In particular, that Regulation (No. 1093/2010) states that “decisions taken by the European Supervisory Authorities should not impinge on the fiscal responsibilities of Member States”. We have concerns that some of EBA’s roles as proposed by the Commission would cut across this safeguard – especially in Article 83, on group resolution. We consider that EBA binding mediation would be inappropriate here, as resolution actions have the strong potential to have fiscal consequences for Member States. It is also not realistic in the middle of a crisis to expect Member State authorities to refer decisions that can have profound consequences for their economies to a technical EBA committee. We have support from a number of other Member States on this specific issue.

RESOLUTION FINANCING

As you are aware, resolution financing still remains one of the key issues to be resolved. The Government is still evaluating these proposals, with the objective of ensuring that they do not impose disproportionate burdens on banks, which could be passed on to the wider economy or adversely impact the Government’s fiscal position.

After careful consideration, we remain confident of achieving an outcome that meets these objectives. For example, we are considering whether the UK’s bank levy should be recognised in an appropriate way as part of this package. This would be in line with the June 2010 European Council agreement, which called on Member States to establish systems of levies and taxes as part of a credible resolution framework. The UK has delivered this through the establishment of the bank levy.

Negotiations in this area remain very fluid. You might also have noticed the ECOFIN press release in which the Presidency recognised that some country-specific concerns should be addressed, in particular as regards issues specific to non-euro area Member States.

7 June 2013

Letter from the Chairman to the Rt. Hon. Greg Clark MP

Thank you for your letter, dated 7 June 2013, on EM 11066/12 on the Recovery and Resolution Directive (RRD). The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 18 June 2013.

We are grateful to you for this helpful and prompt response and for the further detail you provide on the current state of negotiations. We note that negotiations remain fluid, and that discussions are likely to continue, even on the day of the ECOFIN meeting itself. The implications of this proposal are serious and it is vital that you and Member State colleagues reach an agreement that will strengthen rather than undermine the stability of the EU banking sector.

We note your update on the treatment of insured and uninsured depositors and on bail-in. In that context, we note the recent Financial Times report that European banks’ issuance of senior debt has fallen to its lowest level in more than a decade amidst concern that investors will take losses as a result of demands for greater protection of taxpayers and depositors. Do you share such concerns about the potential knock-on effect, in terms of the costs of financing banks, of bail-in rules that seek to reduce the liability of taxpayers?

In light of forthcoming discussions at ECOFIN we are now willing to clear the document from scrutiny. However we would be grateful for a swift update on negotiations, by 3 July 2013.

18 June 2013

Letter from the Rt. Hon. Greg Clark MP to the Chairman


Since, your letter, I am pleased to inform you that the Economic and Financial Affairs Council [ECOFIN] has agreed an approach to enter into discussions with the European Parliament and the European Commission. We agreed to the package on the basis of achieving a number of favourable outcomes for the UK. In summary, the approach includes:
TREATMENT OF DEPOSITORS

As per previous ECOFIN discussions, there was broad agreement to protect insured deposits (i.e. those up to £85,000) and to grant them preference over other depositors on insolvency. Further to this, it was agreed that deposits of natural persons and micro, small and medium enterprises would receive second tier preference over other deposits (including deposits of large corporations).

BAIL-IN

As you are aware, throughout the negotiations we have sought to deliver a credible and usable bail-in tool which ensures that shareholders and creditors of a failed bank would, to the extent possible, bear the cost of a bank’s failure, not the taxpayer. We are confident that this has been achieved.

The Council agreed a tool whereby 8% of total liabilities of the failed bank would have to be bailed-in before a resolution authority may draw down on the resolution financing arrangement in its jurisdiction to absorb losses or recapitalise the institution.

This contribution would be capped at 5% of the institution’s liabilities. In line with pre-existing competencies (as part of state aid rules), the Commission will have to be notified, and will have the right to prohibit the use of resolution financing arrangements. If there were losses beyond this 5%, the resolution authority would have to bail-in any remaining non-preferred liabilities, except for eligible deposits, before deploying any further resolution or alternative financing means (including the European Stability Mechanism for Eurozone countries).

During the negotiations, I managed to secure a degree of tightly constrained flexibility for resolution authorities to depart from the creditor hierarchy when a liability is impossible to bail-in (e.g. debt that is governed by the law of a third country) or bail-in would cause a serious risk to financial stability (e.g. would lead to contagion or would disrupt the running of critical functions to the economy). This is a fundamental aspect of ensuring the bail-in tool is usable.

ROLE OF THE EUROPEAN BANKING AUTHORITY (EBA) AND THE COMMISSION

The Council has given EBA powers in relation to resolution, but has ensured that the Directive does not expand the nature of EBA’s role beyond that already agreed under the regulation that established the Authority (No. 1093/2010 as amended).

Member States, in particular those outside the Euro-zone, remain concerned about EBA’s role in mediating disputes between resolution authorities, particularly given that the resolution authority of the Banking Union is still unknown.

To address this concern, the Council agreement, includes a clause to review EBA’s role to take account of future developments in financial services legislation. This would allow a re-consideration of EBA’s role once more information on the Single Resolution Mechanism (SRM) is known and the UK intends to pursue this matter further in the context of the forthcoming SRM proposal.

It was also agreed that EBA will not have a role in mediating disputes regarding which resolution action to take when resolving a bank at the point of its failure.

RESOLUTION FINANCING

As part of the general approach we have managed to ensure that the UK’s bank levy can act as a resolution financing arrangement for the purpose of the BRRD and that the contributions already collected can count towards the target level set out within the Directive. This acknowledged that the UK’s levy has been set up as a response to the June 2010 European Council agreement, which called on Member States to establish systems of levies and taxes as part of a credible resolution framework.

The next phase of the process will be for the Council to enter into discussions with the European Parliament. This will begin shortly under the Lithuanian Presidency.

9 July 2013

Letter from the Chairman to the Rt. Hon. Greg Clark MP

Thank you for your letter, dated 9 July 2013, on EM 11066/12 on the Bank Recovery and Resolution Directive. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 16 July 2013.
We are grateful to you for this update, and are pleased to learn that a General Approach has been agreed. However, we note some concerns about the nature of the deal. Your letter emphasises the flexibility that you have secured in the revised text. However, we note the reported concerns of EU officials that giving countries too much flexibility in bail-in rules would allow large and wealthier Member States to use public money for bailouts while smaller, economically vulnerable Member States would be forced to impose losses on creditors, including depositors. How would you respond to these concerns? Is there any danger that the agreement will result in a two-tier recovery and resolution system, exacerbating the worrying trend towards fragmentation of financial markets that we have witnessed since the financial crisis erupted? Can you guarantee that the mistakes of the Cypriot bank bailout deal will not be repeated, where it was initially proposed that insured deposits below €100,000 would be caught? Given that many bondholders are pension funds, how practical do you believe the bail-in model to be?

You state that the Council agreement includes a clause to review EBA’s role to take into account future developments in financial services legislation. Now that the proposals for a Single Resolution Mechanism proposal has been published, how will this matter be taken forward?

We also note that you did not respond to the question in our letter of 18 June, when we noted reports that European banks’ issuance of senior debt has fallen to its lowest level in more than a decade amidst concern that investors will take losses as a result of demands for greater protection of taxpayers and depositors. We asked if you share such concerns about the potential knock-on effect, in terms of the costs of financing banks, of bail-in rules that seek to reduce the liability of taxpayers. We would be grateful for a response to this question.

We also understand that the new system will become operational in 2018. What risks are created by such a delay, and how can they be mitigated?

We would be grateful for a response to this letter by 30 August 2013.

17 July 2013

Letter from the Rt. Hon. Greg Clark MP to the Chairman

Thank you for your letter of 17 July on the Bank Recovery and Resolution Directive (BRRD). You raised a number of questions regarding the General Approach agreed at the Economic and Financial Affairs Council meeting of 26-27 June, some of which were discussed when I appeared before the Sub-Committee on Tuesday 23 July.

LESSONS LEARNT FROM CYPRUS AND THE TREATMENT OF DEPOSITORS

Recent events in Cyprus highlighted again that EU Member States need a robust framework for bank recovery and resolution. As I set out in my previous letter, dated 9 July, we agreed to the package having achieved a number of favourable outcomes for the UK.

Our consistent aim has been to agree a common set of credible tools, including a useable bail-in tool, to increase the resilience of banks and, where necessary, manage their failure in an orderly way. The General Approach provides a common set of recovery and resolution tools, including a credible bail-in regime. These tools should preserve the continuity of critical functions and avoid damaging financial stability.

Under the General Approach text, deposits covered by the Deposit Guarantee Scheme (the FSCS in the UK) will be permanently excluded from bail-in. Moreover, insured depositors and by extension the DGS will have “super-preference” in the insolvency hierarchy, which will limit the likelihood that the DGS will be called upon to bear losses in the event of a failure of a deposit-taker and so offers further protection to taxpayers. This is in line with the Vickers recommendations.

FLEXIBILITY AND LEVEL PLAYING FIELD OF THE SINGLE MARKET

Your letter asked about the possibility of a two tier recovery and resolution system, whereby some Member States would bail-out, while others bail-in. The agreement seeks to protect the level playing field by outlining clear rules for when resolution financing arrangements, or alternative financing arrangements, can be used which all countries must adhere to.

The European Commission will also continue to have a strong role in protecting the single market through the State-aid framework. For example, you may have seen the European Commission recently published new temporary State-aid guidelines that impose tougher burden sharing provisions. Robust State aid principles, including imposing private sector burden sharing conditions prior to any
disbursement of State aid, will create an environment which will help ensure a level-playing field across the single market.

**SINGLE RESOLUTION MECHANISM (SRM)**

Your letter raises questions regarding the recent European Commission proposal for a Single Resolution Mechanism. I will be sending you an Explanatory Memorandum on this proposal shortly but we note that the role for the European Banking Authority will continue to be considered carefully in the context of the negotiations of both the BRRD and the SRM proposal.

**FUNDING IMPACT ON BANKS**

We have been working to ensure that all banks are subject to normal competitive market forces. They should be able to fail safely, without the need for taxpayer support. This means that creditors must expect to share the burden if capital levels are insufficient to cover losses.

A necessary consequence of reducing the size of any perceived implicit guarantee is that these costs would be imposed on banks. By exposing creditors to these costs, bail-in helps ensure that they do not obtain financial rewards without being appropriately exposed to the corresponding risks.

To manage the potential effects on bank funding costs any transition period needs to be managed so that market participants can appropriately ‘price in’ the risk of the bail-in tool being used. The fact that there is a common framework across the EU should minimise any competitive distortions.

**BAIL-IN IMPLEMENTATION DATE**

The Council General Approach text does not require the introduction of the bail-in tool until four years after the entry into force of the Directive (currently expected to be 2018). However, Member States may introduce the bail-in power earlier, alongside the rest of the proposals (currently expected to be 2015), if they choose. The European Parliament version of the text requires the bail-in provisions to be implemented by 1 July 2016 at the latest, so it is not yet clear what the final implementation date will be.

In addition, it is worth pointing out that the provisions relating to write down of capital instruments (Articles 51-55) will apply from the entry into force of the Directive (currently expected to be 2015). This will ensure that all regulatory capital instruments are fully able to bear losses.

27 July 2013

**BANKING UNION (13682/12, 13683/12)**

**Letter from the Chairman to the Rt. Hon. Greg Clark MP, Financial Secretary, HM Treasury**

Thank you for your letter, dated 6 May 2013, on EMs 13682/12 and 13683/12, on the proposal for a Single Supervisory Mechanism/Banking Union. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 14 May 2013.

We are grateful for your commitment to provide the Committee with updates as non-euro area Member States announce whether they intend to participate in Banking Union. We also note that information concerning the banks that would fall under direct supervision by the ECB has yet to be made public. We would be grateful if you could provide this information, including a numerical breakdown of the institutions affected by Member State, once it becomes available. Where banks remain under day-to-day supervision by national supervisors, what is the process by which the ECB will be kept informed of developments?

In an article in the Financial Times on 13 May 2013, the German Finance Minister, Wolfgang Schäuble, wrote that “a banking union of sorts can ... be had without revising the treaties, including a single supervisor; harmonised rules on capital requirements, resolution and deposit guarantees; a resolution mechanism based on effective co-ordination between national authorities; and effective fiscal backstops, also including the European Stability Mechanism as last resort. This would be a timber-framed, not a steel-framed, banking union. But it would serve its purpose and buy time for the creation of a legal base for our long-term goal: a truly European and supranational banking union, with strong, central authorities, and potentially covering the entire single market.” Do you share this
analysis? Would the advantages of being able to move more quickly towards a “timber-framed” banking union outweigh the drawbacks of not moving towards a “steel-framed” banking union in the short term? We would be grateful for a response to these questions by 3 June 2013.

In the context of our new inquiry into EU ‘Genuine Economic and Monetary Union’, we would be grateful to receive further updates as discussions on the banking union proposals continue.

14 May 2013

Letter from the Rt. Hon. Greg Clark MP to the Chairman

Thank you for your letter of 14 May 2013 and for your continued interest in the Banking Union.

Firstly I would be happy to provide you with a list of banks – including a numerical breakdown of the institutions affected by Member State – which will fall under the direct supervision of the European Central Bank (ECB), once this information has been made publicly available.

Secondly, the ECB will establish the supervisory framework for all banks in participating Member States, including for those where it does not carry out direct day-to-day supervision. The ECB is permitted to directly exercise the relevant powers in relation to banks which fall outside direct supervision, or those powers may be exercised at the request of the national competent authority of the participating Member State. The intention is that the ECB will become well informed of developments in all participating Member States.

Finally, you asked for comment on Wolfgang Schäuble’s article in the Financial Times (13 May 2013) on a Single Resolution Mechanism (SRM). I note that the European Commission has not yet published a proposal on the SRM but when it does we will provide an EM, as usual, and consider it carefully as we work hard to ensure both that it is fit for purpose and that it supports UK interests.

2 June 2013

Letter from Sajid Javid MP, Financial Secretary, HM Treasury, to the Chairman

I thought it would be useful to clarify the circumstances in which the Government formally agreed to adoption of the Single Supervisory Mechanism (SSM) package of legislative proposals at ECOFIN on 15 October.

The UK placed a scrutiny reserve on the SSM Regulation (EM 13682/12) and the Regulation amending the Regulation establishing the European Banking Authority (EBA) (EM 13683/12) at COREPER on 25 September.

We did this for two reasons.

Firstly, we wanted to ensure that Parliament had returned from recess prior to the package being agreed so that the draft Inter-Institutional Agreement between the European Central Bank (ECB) and European Parliament (EP) could be sent for information to the House of Commons European Scrutiny Committee and the House of Lords European Select Committee while Parliament was sitting. While both Regulations had already cleared scrutiny in both Committees in 2012, the EP had made clear that the IIA was central to their own approval of the package. We therefore took the view that although the draft IIA is formally outside the scope of the Scrutiny Resolution it was nevertheless appropriate, in this instance, to draw the attention of Parliament to this document. Since the IIA is a bilateral agreement between the ECB and EP, the Council was not required to approve the agreement, which is, in any case, consistent with the relevant provisions of the SSM and EBA Amending Regulations and will not have an effect on the substance of the SSM legislative package.

Secondly, before the Regulations were agreed we wanted a clear re-iteration, through a Council statement, of the agreement reached last year in the context of negotiations on the EBA Amending Regulation that the review of the double majority voting arrangements in the EBA would take place when the number of Member States outside the Single Supervisory Mechanism reaches four. In recent weeks we had become concerned that the EP may look to re-open this arrangement sooner, for example in negotiations over the Bank Recovery and Resolution Directive or in the context of ongoing negotiations on other legislative instruments relating to Banking Union, possibly with support from parts of the Commission and some in the Council.

We secured such a statement at ECOFIN on 15 October, which is appended to the Council’s formal decision to adopt the EBA Amending Regulation. It reads as follows:

“The Council welcomes the adoption of the SSM and the EBA Amending regulations. This represents a decisive step towards the banking union. The Council reiterates the principle of non-discrimination
of Member States regarding banking supervision and resolution as stated by the European Council in October 2012 and reconfirms the agreed new voting arrangements in the EBA regulation for these matters, which is reflecting an appropriate balance between the participating and non-participating Member States. The Council also reconfirms its agreement that the review on the operation of the voting arrangements will take place from the date on which the number of non-participating Member States reaches four.”

I hope that this letter clarifies the Government’s approach on this issue.

23 October 2013

Letter from the Chairman to Sajid Javid MP


We note that this letter was written before you had sight of our letter of 28 October 2013.

We are grateful to you for the useful update on discussions relating to the double majority voting arrangements on the EBA, and welcome your efforts to ensure that the commitment to review these arrangements is not reopened until the number of non-participating Member States reaches four.

We also note your statement that you wanted to ensure this document was drawn to Parliament’s attention before it was agreed. We would stress to you that, in cases where the Government cite parliamentary scrutiny as a reason for delaying agreement on a proposal, we expect you to keep us as fully briefed on negotiations before agreement is reached as afterwards.

We do not require a response to this letter.

5 November 2013

2013 BUDGET - DRAFT AMENDING BUDGET NO.2 (8041/13)

Letter from the Chairman to the Rt. Hon. Greg Clark MP, Financial Secretary, HM Treasury

Thank you for your Explanatory Memorandum, dated 23 April 2013, on EM 8041/13, on Draft Amending Budget No. 2 to the General Budget 2013. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 14 May 2013.

We share your disappointment that such an increase in funds is necessary. Whilst there is often a tendency for there to be a backlog of unpaid builds towards the end of an MFF period, this still seems a significant sum. Is Commissioner Lewandowski correct to assert that the discrepancy has built up over the entirety of the MFF period? Is this, in your view, more than just an inevitable symptom of coming towards the end of an MFF period? If so, what are the causes of such a large discrepancy?

We understand that, as part of the reform of its accounts in 2005, the EU shifted from cash accounting to accrual accounting. As you are aware, this means that transactions should be recognised when they occur, even if the payment is to be made the following year. We are disappointed that under such a system there still appears to be such a significant build up of unpaid bills. Has the transition from cash accounting to accrual accounting been fully effective? What further reform of the EU budget process needs to take place so that this problem does not recur in the future? What are the UK Government doing to ensure such reforms take place?

You highlighted that agreement to this Amending Budget is subject to Qualified Majority Voting (QMV) in the Council. Should we interpret this as an indication that you are unlikely to succeed in blocking this amendment? We welcome the fact that Jeroen Dijsselbloem, Dutch Finance Minister and President of the Eurogroup, has said that the European Commission should try to find extra savings to bridge the budget shortfall rather than turning to Member States for additional cash. Which other Member States support this position?
In our previous correspondence with you on the 2013 draft budget, we expressed concern that the relationship between payment and commitment appropriations had become confused and was in danger of breaking down. You responded to this by stating the importance of having a greater focus on payments since this is what directly impacts on the public finances. Our fears have been heightened by this proposal. Do you agree that the relationship has broken down? What has caused this breakdown? Has the relationship broken down irretrievably, or can steps be taken to repair it? If so, what are they?

In light of this, we note that your EM you did not mention the position of the European Parliament. We understand that it plans to tie agreement on this amending budget to agreement on the 2014-2020 Multiannual Financial Framework. We are concerned that the European Parliament is thereby seeking to secure greater budgetary flexibility between annual budgets in exchange for accepting such a large gap between commitments and payments in the next MFF. Do you share this analysis? Would this in practice provide the European Parliament with significantly greater influence in terms of negotiation of the EU budget? What can be done to prevent such a trade-off being established?

We would welcome a response to these queries as well as a general update on negotiations by 3 June 2013. In the meantime we will continue to hold this document under scrutiny.

14 May 2013

Letter from the Rt. Hon. Greg Clark MP to the Chairman

Thank you for your letter of 14 May 2013 on EM 8041/13 regarding Draft Amending Budget No. 2 to the General Budget 2013 (DAB 2/13). I am writing to update you and your Committee on DAB 2/13 following 14 May ECOFIN, which I hope also addresses the queries you raise.

As you know, on 27 March the Commission published the DAB 2/13 proposal for €11.2bn in additional payment appropriations in 2013. Ahead of ECOFIN, the Presidency released a ‘compromise’ proposal which consisted of a two-stage approach, with an agreement on €7.3bn now and a commitment to look at the requirement for further payment appropriations again later in the year. This would be contingent on the Multi-Annual Financial Framework (MFF) being agreed by the European Parliament (EP). On 14 May, ECOFIN reached political agreement on this proposal by Qualified Majority Voting (QMV). ECOFIN also agreed on a Council statement, which is included as an annex [not printed] to this letter and which clearly states that the deal is contingent on MFF agreement.

The Chancellor argued very strongly, both off and on camera, against the Presidency proposal and was supported by the Netherlands, Sweden, Denmark and Finland. It was decided in informal discussions with our core like-minded allies that the Chancellor would speak on behalf of those opposing the proposal. I have included the Chancellor’s on-camera remarks as an annex [not printed] to this letter.

I join you in welcoming Eurogroup President Jeroen Dijsselbloem’s assertion that the Commission should try to find savings from elsewhere rather than turning to Member States for additional cash. The Chancellor also made this point at ECOFIN. The UK worked closely with our like-minded Member States (the Netherlands, Finland, Denmark and Sweden) throughout the negotiations and formed a minority group against the Presidency proposal. This dissenting group made up 76 votes against the proposal and as this amendment was decided by QMV we were thus unable to block it.

As a result of this agreement, the total 2013 EU Budget will increase from €132.8bn to €140.1bn. This will approximately cost the UK an additional €0.9bn, which will mean an estimated post-abatement UK contribution to the 2013 EU budget of around €17.2bn. We do not as yet have the precise final breakdown of how these payments are allocated to the different EU Budget headings, but expect the focus to be on headings 1a and 1b.

On 16 May the EP reacted to the ECOFIN agreement by saying it rejects the Council compromise in its current form and that, whilst this is a step in the right direction, it is concerned that Council made the €7.3bn dependent on reaching MFF agreement. The EP has stated it expects adoption of the €7.3bn without further delay and with a solid guarantee on the remaining €3.9bn.

You asked about the Commission’s claim that there is a “backlog of unpaid bills”. The Commission has argued that €16bn of unpaid claims have been rolled over from last year, and which cannot be covered by the agreed 2013 Budget. The Commission and EP have used this line of argument to assert that low budget deals over the last few years have caused this €16bn “deficit” in the budget, and that DAB 2/13 is needed to tackle this and reduce the pressure on payments rolling into 2014. The Government does not accept this line of argument. In fact, based on previous data released by
the Commission on Member State payment claims, around €15bn of this figure was based on invoices received in the last two months of 2012. According to budget rules and usual practice, claims received in this period are not due to be paid until the following year. In the DAB 2/13 proposal, the Commission has said itself that it expects to “receive an increased share of payment claims very late in the year, too late for payment in 2013.”

You also asked about the transition from cash accounting to accrual accounting. As stated above, we reject the Commission’s claim of a build up of “unpaid bills”. Moreover, the UK Government continues to argue that pressures should be met through redeployments and reprioritisation within the EU budget, just as domestic governments in all other Member States do every day. With regards to accounting, in 2005 the Commission moved from cash-based to accruals-based accounting as part of an effort to improve and modernise the Community accounting framework. Since the introduction of the new system most of the Court’s concerns about the accounting system have been resolved. The new system shifts the focus of the accounts from the recording of cash transactions to the recognition of the ‘rights and obligations’ as soon as these are acknowledged. The financial statements are now established on the basis of information extracted from the accounting records and the accounts are kept based on the generally accepted accounting principles. The differentiation between capital and non-capital expenditure is yet another improvement arising from the introduction of the new accounting system.

As stated in its 2011 report the European court of Auditors (ECA) is of the opinion that the consolidated accounts of the European Union present fairly, in all material respects, the financial position of the Union as of 31 December 2011, and the results of its operations and cash flows for the year then ended, in accordance with the provisions of the Financial Regulation and the accounting rules adopted by the Commission’s accounting officer.

With regards to your question about the relationship between payment and commitment appropriations, the UK focuses on the level of payments because this is what determines the actual contribution made by Member States each year. Controlling payments is the only way to provide budgetary certainty to the Member States. It is also the only way to protect UK’s contributions in the future. The UK, along with other Member States, has long advocated bolder solutions for an EU Budget concentrated on payments.

Finally, in response to your concerns about budgetary flexibility, the European Council has said it is prepared to accept some flexibilities about how spending is divided between different budget years and different areas of spending, but we are absolutely clear that this must be within the framework that the member states have now agreed.

25 May 2013

Letter from the Chairman to the Rt. Hon. Greg Clark MP

Thank you for your letter, dated 25 May 2013, on EM 8041/13, on Draft Amending Budget No. 2 to the General Budget 2013. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 11 June 2013.

We understand that the European Parliament is not content with the political agreement reached at ECOFIN and has demanded a formal, binding decision by the Council on the full amount of €11.2bn before concluding the MFF negotiations. We note that, alongside its rejection of the Council position, the Parliament is insisting on progress towards a mid-term revision of the MFF, with the possibility of an upward adjustment of ceilings, and a need for flexibility in the budget between headings and between years. We therefore remain concerned that the European Parliament is thereby seeking to increase its influence by seeking to secure greater budgetary flexibility between annual budgets in exchange for accepting such a large gap between commitments and payments in the next MFF. We regret that the disagreement between the European Parliament and the Council has become such a major political issue. In light of this, and in light of the UK’s opposition to the original deal, how do you plan to take forward these negotiations? Are the UK Government going to continue to take a firm line? What is the position of Council in response to the European Parliament position? We intend to pursue these questions with you further at your forthcoming appearance before the Sub-Committee, on 9 July 2013.

We repeat our disappointment that we did not receive prior warning of the political agreement reached at ECOFIN on 14 May, and have written to you separately with a proposal that you should write to us before each ECOFIN outlining the likely agenda. We look forward to a response to that letter. Given that political agreement has been reached, and in anticipation of further Council consideration of the European Parliament’s response, we now clear this document from scrutiny.
However, we expect to receive timely updates on negotiations with the European Parliament as they proceed, as well as a response to our specific questions by 26 June.

11 June 2013

Letter from the Rt. Hon. Greg Clark MP to the Chairman

Thank you for your letter of 11 June on EM 8041/13 on Draft Amending Budget No. 2 (DAB2) to the General Budget 2013 and for clearing this document from scrutiny.

You rightly note that the European Parliament (EP) has responded negatively to the Council’s political agreement on a first stage DAB2 solution of €7.3bn. As you know, the UK opposed this. The Council has been very clear that this proposal is dependent on reaching agreement on the Multi-Annual Financial Framework (MFF) in the EP and that both the EP and the Council agree that “Nothing is agreed until everything is agreed”. Discussions are currently ongoing on the documents that give legal force to the expenditure deal of the MFF, the MFF Regulation and Inter Institutional Agreement. The UK Government has been absolutely clear that flexibilities must be within the MFF framework that Member States have now agreed. The Prime Minister in February set out to Parliament the UK Government’s position on the MFF ceilings; the payment limit is €80bn lower than the original Commission proposal and €35bn lower than the deal agreed in 2005. The Government believes that the MFF deal reached in February was good for Europe’s tax payers.

At the May ECOFIN meeting the Chancellor was very clear on the UK’s position and argued strongly against the Presidency’s proposal. The Government will continue to work with like-minded Member States and will oppose any such increase to the Annual Budget. Council discussed this at the May ECOFIN meeting. As part of the vote which, as said above the UK opposed, a declaration was adopted as annexed [not printed] to this letter.

You also asked about how best the Government could ensure your Committee and Parliament are kept appropriately informed of upcoming Council issues. When available, timetabling information is set out in EMs and in addition Treasury Ministers have written to inform your Committee of key issues coming to Council which have not yet cleared scrutiny, for example my letters of 17 May and 7 June to update on the Banking Recovery and Resolution Directive ahead of the June ECOFIN. However, as you know we do inform Parliament of the ECOFIN agenda through a Written Ministerial statement laid in both Houses of Parliament ahead of each and every ECOFIN, setting out the agenda items and also the likely action at Council.

27 June 2013

Letter from the Chairman to the Rt. Hon. Greg Clark MP

Thank you for your letter, dated 27 June 2013, on EM 8041/13 on Draft Amending Budget No. 2 (DAB2) to the General Budget 2013. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 9 July 2013.

We understand that political agreement has been reached on DAB2 in connection with the Multiannual Financial Framework, and a formal decision on the first tranche of DAB2 will be taken at the 9 July ECOFIN. We would be grateful for an update from you on negotiations ahead of your appearance before the Committee on 23 July 2013.

9 July 2013

BUDGET 2013 - DRAFT AMENDING BUDGET NO.5 (9166/13, 9167/13)

Letter from the Rt. Hon. Greg Clark MP, Financial Secretary, HM Treasury, to the Chairman

On 21 May I sent you and your Committee an Explanatory Memorandum (EM) on Council Documents 9166/13 and 9167/13, relating to DAB 5/2013 which proposed assistance from the EU Solidarity Fund to Slovenia, Croatia and Austria. I am writing to update your Committee on further developments in negotiating these issues.

The UK raised its concerns at the Council’s meeting of officials in the Budget Committee on 23 May. As stated in the EM, the UK opposes additional payments in this case and instead believes these can be met through redeployments. At the Budget Committee the UK together with the Netherlands and
Sweden sought for these payments to be met by redeployments. Germany and Denmark raised similar concerns but did not block the proposal. The UK reserved its voting position on scrutiny grounds. However, as there was no blocking minority against this proposal we now expect this to be agreed at COREPER this week.

9 July 2013

Letter from the Rt. Hon. Greg Clark MP to the Chairman

I am writing to update you on the outcome of Council negotiations on Amending Budgets 2 to 5 to the 2013 EU Budget. You will recall that I wrote to you separately updating you on the agreement reached on Amending Budget 1 on 30 June.

DRAFT AMENDING BUDGET 2 (DAB2)

On 27 March the Commission requested an increase to payment appropriations of €11.2bn in 2013 which it claimed was necessary to meet legal obligations arising primarily from Heading 1b claims left unpaid at the end of 2012, as well as to reduce pressures which it expects to arise later in 2013.

As you know, at May ECOFIN, a political agreement was reached on the Presidency’s compromise DAB2 proposal for €7.3bn. This was contingent on reaching MFF agreement. As explained in my letter of 24 May, the UK together with likeminded Member States opposed any such increase and the Chancellor argued strongly against it both on and off camera. The Government took this position throughout negotiations.

Following the agreement in the European Council on the MFF regulations and the IIA, DAB2 was voted on at COREPER on 4 July. The UK, along with Denmark, Finland, the Netherlands and Sweden voted against DAB2, expressing dissatisfaction with the Commission’s unjustified request for substantial additional resources. Whilst this has not yet cleared scrutiny in the Commons, awaiting the debate on July 16, the Government did not override scrutiny as it voted against the proposal. However, this proposal was accepted by a qualified majority of Member States. This was subsequently agreed as an a-point at July ECOFIN.

DRAFT AMENDING BUDGET 3 (DAB3)

On 15 April the Commission published DAB3, which proposed an upward revision to the statement of revenue for 2013 of €1.02bn. This resulted from the surplus arising from the implementation of the 2012 budget. This proposal will accordingly reduce Member States contributions to the financing of the 2013 EU Budget and the UK could therefore support. This was discussed at Budget Committee and was accepted by all Member States. At the time UK reserved its position on scrutiny grounds, but as this has since cleared scrutiny, the UK was able to vote in favour at COREPER on 4 July. This was subsequently agreed as an a-point at July ECOFIN.

DRAFT AMENDING BUDGET 4 (DAB4)

On 29 April the Commission published DAB4. This concerned three requests for additional staff from the European Global Navigation Satellite System (GNSS) Agency (GSA), the Education, Audiovisual and Culture Executive Agency (EACEA) and the European Court of Justice (CJEU). As all proposals are budget neutral and it cleared scrutiny, the UK voted in favour of DAB4 at COREPER on 11 July. This will now go to Council as an a-point.

DRAFT AMENDING BUDGET 5 (DAB5)

On 2 May the Commission presented a proposal for DAB5. This proposed the mobilisation of the EU Solidarity Fund for €14.6m in commitment and payment appropriations relating to flooding in Slovenia, Croatia and Austria in autumn 2012. The UK was clear that whilst it supported the broad principles of the Solidarity Fund, it opposed additional payments in this case and believed these should instead be met from redeployments. Although the UK voted against, this proposal was accepted at COREPER on 11 July. This will now go to Council as an a-point.

As is the case with all agreed Amending Budgets, the Council’s position on DAB’s 2-5 will need to be formally approved by the European Parliament.

14 July 2013
Letter from the Rt. Hon. Greg Clark MP, Financial Secretary, HM Treasury, to the Chairman

In your letter dated 28 June 2012 you noted that you would like to receive further updates as Council working group negotiations on the Central Securities Depositories Regulation (CSDR) progress. This letter provides an update.

BACKGROUND

The Commission published its proposal for CSDR in March 2012. My predecessor submitted to you an Explanatory Memorandum (7619/12) on CSDR on 23 March 2012 and a further letter on EM 7619/12 in May 2012. I submitted to you a further Explanatory Memorandum (13821/12) dated 30 September 2012 on the ECB opinion.

The objectives of CSDR are to establish a regulatory and prudential framework for CSDs, to increase the safety and efficiency of cross-border settlement and to create a single market for CSD services.

STATUS OF NEGOTIATIONS IN COUNCIL

The Lithuanian Presidency has held three working groups and tabled two compromise proposals with the aim of reaching a general approach. The Presidency aim to reach a general approach on CSDR in the coming weeks.

Letter from the Rt. Hon. Greg Clark MP to the Chairman

In your letter dated 28 June 2012 you noted that you would like to receive further updates as Council working group negotiations on the Central Securities Depositories Regulation (CSDR) progress. This letter provides an update.

BACKGROUND

The Commission published its proposal for CSDR in March 2012. My predecessor submitted to you an Explanatory Memorandum (7619/12) on CSDR on 23 March 2012 and a further letter on EM 7619/12 in May 2012. I submitted to you a further Explanatory Memorandum (13821/12) dated 30 September 2012 on the European Central Bank opinion (ECB Opinion) and a further letter on EM 7619/12 on 4 July 2013.

The objectives of CSDR are to establish a regulatory and prudential framework for CSDs, to increase the safety and efficiency of cross-border settlement and to create a single market for CSD services.

STATUS OF NEGOTIATIONS IN COUNCIL

The Lithuanian Presidency has held three working groups and tabled two compromise proposals with the aim of reaching a general approach. The Presidency aim to reach a general approach on CSDR in the coming weeks.
The three principal outstanding issues in Council negotiations, which I outlined in my letter of 4 July, remain under discussion:

— On the process for authorisation of banking services, the Government continues to call for a system in which there is close co-operation between relevant national authorities and which ensures that the home national authority plays a prominent role in authorisation decisions. Council has been trying to agree on the details of a process that achieves this objective.

— On the securities settlement regime, we have secured significant progress in ensuring there is sufficient flexibility in relation to less-liquid securities and markets. In particular, the time period to complete a mandatory buy-in will now be set out in regulatory technical standards according to asset type and liquidity of the relevant instrument.

— On the third country regime, the Government is seeking to ensure the regime for CSDs from non-EU jurisdictions does not unduly obstruct cross-border business and that the relevant national authorities have a key role in determining whether third country CSDs may provide CSD services in their jurisdiction.

On the resolution of other issues, some fundamental issues, such as the process for authorising a CSD for core services, the organisational requirements of a CSD, and the supervision of a CSD have been mostly settled, with only small technical tweaks under consideration.

10 September 2013

Letter from the Rt. Hon. Greg Clark MP to the Chairman

Following on from my letter of 10 September, I am pleased to inform you that a General Approach on the CSD Regulation was agreed on 25 September. The Government agreed to the General Approach on the basis that it represented a favourable agreement overall. I have summarised below the resolution of the three principal outstanding issues which I highlighted in my previous letter dated 10 September.

— On the process for authorisation of banking services, in line with the Government’s preference, the text provides for a process of close cooperation between relevant national authorities in which ESMA has only a non-binding mediation role and the home authority makes the final decision.

— On the securities settlement regime, the government has been concerned to ensure that the buy-in remedy (whereby securities which should have been delivered will be bought in the market and delivered to the relevant receiving party) is sufficiently flexible in relation to less-liquid securities and markets. The text provides for flexibility by allowing certain relevant time periods to be set out in regulatory technical standards according to asset type, the liquidity of the relevant financial instrument and the type of transaction, subject to certain parameters set out in the text. The levels of cash penalties will also be set in a similarly flexible manner in delegated acts.

— On the third country regime, the text provides for transitional arrangements for non-EU CSDs currently providing services into the EU, which should mitigate any perceived risk of obstruction to cross-border business. National rules will continue to apply to third country CSDs until the necessary decisions on recognition have been made by the Commission and ESMA.

As to next steps, I expect trilogues to begin within the next few weeks.

3 October 2013
Letter from the Chairman to the Rt. Hon. Greg Clark MP, Financial Secretary, HM Treasury

Thank you for your letter, dated 29 April 2013, in which you set out a proposal to end the automatic deposit of indirect derogation proposals for other Member States. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 4 June 2013.

We have considered your request and are content to accede to it, providing, as you propose, that HM Treasury officials seek agreement on a case-by-case basis from Committee officials on whether a particular derogation proposal should be deposited. It is important that Parliament retains the right to undertake scrutiny of such documents where it wishes to do so, and we are reassured that this will provide an adequate safeguard to that effect.

In addition, we would like to ask you to consider a further change to the scrutiny process. We have recently expressed disappointment that we were not kept informed when negotiations on the 2012 and 2013 EU budgets were scheduled for discussion at ECOFIN. A recent example relates to Draft Amending Budget No. 2 on the 2013 Budget, where political agreement was reached at ECOFIN on 14 May 2013. We regret that HM Treasury did not advise us that the Irish Presidency was seeking to reach political agreement in advance of this meeting. This was only made clear in your Written Ministerial Statement of 14 May, which was published too late to influence the Sub-Committee’s consideration of this document.

We understand that other Government departments write to other Lords EU Sub-Committees to inform them of the provisional agenda for forthcoming Council meetings. I have attached by way of illustration a communication from the Department for Energy and Climate Change to the Sub-Committee on Agriculture, Fisheries, Environment and Energy. This strikes us as a useful example to follow. We would therefore request that you commit to writing to the Committee at least a week before a Council meeting takes place to inform us of the provisional agenda and any issues likely to be of interest or note. We appreciate that agendas are subject to late alteration, and we would therefore also request that you ensure that HM Treasury officials contact Committee officials to inform them of any changes or developments between receipt of your letter and the Council meeting taking place.

I hope this proposal offers a sensible way forward, and would be grateful if you could write to me by the time of the next ECOFIN meeting on 21 June 2013 to advise me if you are willing to agree to this proposal.

4 June 2013

Letter from the Chairman to the Rt. Hon. Greg Clark MP

I am writing in response to your letters of 27 June 2013 on the UK Convergence Programme and the 2013 Draft Amending Budget No.2, where you raise issues pertaining to the scrutiny process. The House of Lords EU Economic and Financial Affairs Committee considered these documents at its meeting on 9 July 2013.

We note your response to our queries on the UK Convergence Programme, and acknowledge your clarification that early copies were deposited in the House. Yet we remain disappointed that there was no opportunity to debate the National Reform Programme. We welcome your commitment to finding a way to ensure this happens in the future, and invite you to open a dialogue with us about how this can be achieved well in advance of the 2014 debate.

We are disappointed at your response to our request for more information on upcoming Council meetings. You state that you provide information to the Committee on Council agendas in the form of EMs and correspondence, yet, as recent experience with regard to the 2012 and 2013 Budgets shows, such information as you provide is by no means comprehensive, as we expect it to be. We note that the Government provide a Written Ministerial Statement on upcoming Council meetings, but given that such statements are often published the day before a Council meeting at best, this does not give the Committee sufficient time to take the agenda in to account in its deliberations. We are therefore disappointed at your failure to accede to our reasonable request for you to write to the Committee at least a week before a Council meeting takes place to inform us of the provisional agenda.

We also note that your failure to agree to our request not only compares unfavourably with the attitude of other Government departments, but also stands in direct contradiction to the Cabinet
Office Guidance for Government Departments on Parliamentary Scrutiny of European Union Documents, which states (at Annex N) [not printed] that “the Committees should be informed three weeks before a forthcoming Council of items expected to appear on the (Council) Agenda. The Committee Clerks understand that it may be difficult to provide this information with any certainty at this point and are happy to be contacted informally to discuss provisional business. As soon as the agenda becomes clearer, Departments should provide a detailed assessment of the main agenda items using the annotated agenda pro-forma” along the following lines [not printed]

I am afraid that your response gives us the impression that you are reluctant to inform, let alone involve or use, Parliament in its longstanding role of scrutiny to advance UK national interests during negotiation of EU policy.

Why are you refusing to accede to Cabinet Office guidance? We urge you to reconsider your position. In the meantime we will advise the Minister for Europe of our dismay at your failure to accede to such a simple request. We invite a response to this letter ahead of your appearance before the Committee on 23 July 2013.

9 July 2013

Letter from the Rt. Hon. Greg Clark MP to the Chairman

Thank you for your letter of 9 July. I look forward to further discussions about how to move forward with the Parliamentary consideration of the National Reform Programme.

You asked me to look again at your request for more information on upcoming Council meetings. It may help if I set out some context to my letter of 27 June. The first time the Council Secretariat makes available a clear ECOFIN agenda of items which are reliably expected to appear is less than a week before the Council, at which point we prepare the Written Ministerial Statement to be laid in Parliament. There would be no purpose at that stage in also writing to the Committee with the same information.

I recognise however your concern to allow the Committee to prepare itself as far as possible in advance. I have therefore asked my officials to provide both the House of Lords and House of Commons European Scrutiny Committee clerks with a copy of the draft provisional ECOFIN agenda, as circulated by the Council Secretariat, on an informal basis when we receive them, which can be as early as three weeks before the Council. The Committee should however be clear that these early drafts are rarely a wholly reliable guide to the items which actually come forward to be discussed.

19 July 2013

Letter from the Chairman to the Rt. Hon. Greg Clark MP

Thank you for your letter, dated 19 July 2013, on changes to the scrutiny process. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 30 July 2013. We also took evidence from you on this matter at your appearance before the Committee on 23 July 2013.

We are grateful to you for reconsidering your position and agreeing to provide the Committee Clerk with a copy of the draft provisional ECOFIN agenda once it is received. We also understand your concern that there would be no purpose in writing to the Committee less than a week before the Council once a clear agenda has been made available. Yet there are further steps that we would ask you to consider, in particular in light of the request that you made at your appearance before the Committee on 23 July that we should consider means of informal cooperation between HM Treasury and the Committee.

You told us at that meeting that the final Council agenda is normally received on the Thursday before the ECOFIN takes place on the Tuesday. Would it be possible for officials to forward this agenda to Committee officials as soon as it is received? As we have previously made clear, the Written Ministerial Statement gives the Committee little or no opportunity to respond, whereas receipt of the agenda as soon as it is received may, even with as little as two or three working days’ notice, give the Committee the chance to consider any matters on an expedited basis. Likewise, we would invite you to pass on any other information that does come to light as regards the Council agenda as soon as it is received. This would go some way to meeting the point made in the Cabinet Office Guidance for Government Departments on Parliamentary Scrutiny of European Union Documents that “the Committee Clerks understand that it may be difficult to provide this information with any certainty [three weeks before the meeting] and are happy to be contacted informally to discuss provisional business.”
We note that the Cabinet Office Guidance goes still further, stating that, “as soon as the agenda becomes clearer, Departments should provide a detailed assessment of the main agenda items using the annotated agenda pro-forma” set out in our letter of 9 July. Whilst we appreciate that there may be a tension between providing information at speed and in detail, in particular if, as you state, the agenda is only finalised less than a week before the Council, we would ask you to provide as detailed an assessment of forthcoming agendas as possible within the time constraints.

Turning to the question of informal contact and cooperation between the Committee and HM Treasury more generally, as raised by you on 23 July, we should stress to you that informal contact is a supplement to, rather than a replacement for, the established scrutiny process. As such we expect you to abide by the standards set out in the Cabinet Office Guidance (and in particular paras 3.1.1.-3.1.3), as follows, which, we would note, already allows for (and indeed encourages) a great deal of informal contact between officials, in particular in cases of urgency and complexity:

— “EMs must normally be provided no later than 10 working days from the date of deposit of the document. Every effort should be made to submit the EM by this date. If an extension to an EM deadline is required you should consult the Committee clerks at the earliest point.”

— “For all documents which need to be agreed quickly the EM should be prepared as soon as possible – using an unnumbered EM if no official depositable text exists to ensure as much chance of scrutiny clearance as possible”.

— “If an EM is likely to be delayed beyond the 10 day deadline, the Cabinet Office and the Committee Clerks should be informed as early as possible of the reasons, particularly where this will have implications for the commitments set out above on opt-in decisions and on subsidiarity.”

— “If the UK policy has not been agreed or there are other areas of uncertainty, the EM should say so while giving as much information as is available at the time.”

— “Where a proposal is expected to progress rapidly, you should work to a shorter deadline and should, where possible, start to prepare the EM before deposit and keep the clerks informed.”

— “If a particular EM needs to be taken by the Scrutiny Committees as a matter of urgency, the Clerks (if forewarned) will normally find it helpful to receive an advance draft copy of the EM in anticipation of receiving the final EM in time for formal consideration by the Committees. ... However, if the final version is to differ from the draft submitted earlier, the Clerks must be notified at the earliest opportunity and provided with details of the changes.

One of our frustrations with HM Treasury’s performance is that, although there are undoubtedly examples of good practice, this guidance is not consistently followed. To give one recent example cited at your appearance before the Sub-Committee on 23 July, your communication on the 2014 Draft Budget was defective in a number of respects. First, the EM was four days late, which, being received at 21:30 on the evening before the Committee’s only available meeting, made it impossible for the Sub-Committee to scrutinise the document ahead of agreement at COREPER on 18 July. Second, no request for an extension was made – instead, we were simply informed (with regret) by officials that it would be late. Given the urgency, an extension would have been denied on this occasion. Third, the EM itself simply stated that “the Council will negotiate and agree a position on the budget by the end of July”, and, in spite of the fact that the EM was dated 15 July, made no reference to the fact that COREPER was expected to reach agreement as soon as 18 July. Nor was this vital information communicated to Committee officials, who instead learned of it through media reports. As we noted at our 23 July meeting, the various draft budget and draft amending budget documents appear to have been particularly susceptible to these problems. When proposals are as fast-moving and important as this, it is imperative that HM Treasury officials supplement the EM with as much background information and proactive informal contact with Committee officials as possible.

We should also stress that we expect to be kept informed in advance about proposals likely to go to Council for agreement regardless of whether the UK intends to vote in favour of the proposal. The Government should do all in its power to ensure that the Committee is given every opportunity to undertake its scrutiny function before agreement on a proposal is reached. In our 22 January 2013 letter on the 2012 and 2013 budgets we made the point that, in order to enable us to fulfil our scrutiny function effectively, deposit and production of EMs must occur on time, and certainly before
decisions in Council are reached. A failure to do so marks a breach of the spirit of the House of Lords Scrutiny Reserve Resolution. We understand that the UK maintained its scrutiny reserve in relation to the 2014 Draft Budget on the grounds that parliamentary scrutiny had not yet been completed. Can you also confirm that this remains the UK’s consistent practice in cases where parliamentary scrutiny has not been completed?

Having said all this, we recognise that our relationship is a two-way process, and if there are any ways in which either the Committee or its officials can assist you in your interaction with the Committee, then we would be pleased to consider any proposals.

We would be grateful for a response to this letter by 30 August 2013.

30 July 2013

Letter from the Rt. Hon. Greg Clark MP to the Chairman

Thank you for your letter of 30 July letter on “Changes to the scrutiny process”.

I confirm the undertaking I made at the evidence session to the Economic and Financial Affairs Sub-Committee, that my officials stand ready to forward to the Committee clerks draft ECOFIN agendas when we receive them. As I said in my letter of 19 July, clear agendas only appear a few days before the meeting at which point we lay a Written Ministerial Statement.

I believe providing these draft agendas as they appear, alongside existing practices, will significantly aid the Committee’s understanding of the likely items to be discussed.

As I said in the evidence session, I take the work of the Committee extremely seriously, and HM Treasury will continue to work to improve performance. In July, all 13 Explanatory Memorandums were submitted within three working days of the deadline, and we provided 22 separate items of correspondence to your Committee.

With regard the use of the scrutiny reserve, I assure you that HM Treasury always seeks to complete scrutiny prior to deliberation in Council.

4 September 2013

COMMISSION’S MANAGEMENT ACHIEVEMENTS IN 2012 (10806/13)

Letter from the Chairman to the Rt. Hon. Greg Clark MP, Financial Secretary, HM Treasury

Thank you for your Explanatory Memorandum, dated 16 July 2013, on EM 10806/13 on the Commission Communication: Synthesis of the Commission’s Management Achievements in 2012. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 10 September 2013.

Like you, we stress the vital importance of effective management of EU funds. It is vital that the reforms proposed by the Commission that are cited in this document prove effective in ensuring that systems of financial management are more effective, streamlined and transparent in the forthcoming Multiannual Financial Framework period. However, financial management can only be effective if there is an effective form of deterrent. Does any form of sanction apply either to Directors-General (DGs) or Member States for failing to ensure the effective management of EU funds?

You stress that the Government take the management of EU funds seriously and that you continue to call on the Commission to address the various management shortcomings that have been identified. Which shortcomings do you believe require most urgent attention, and what practical steps are needed to tackle them? You state that corrective measures need to be sped up. How can this be done in practice? You also state that Commissioners need to be “more proactive in proposing viable and concrete plans to improve their management controls”. What specific action would you wish to see Commissioner take in addition to the work they are already undertaking?

You also call on all Member States to improve the control environment to ensure that the delivery of EU funds is compliant with the Regulations. Can you also confirm the need to ensure compliance with accountancy standards? Can you confirm that the UK was once again subject to reservations in 2012, including in relation to the European Regional Development Fund/ Cohesion Fund and the European Social Fund? How many reservations was the UK subject to? What was the reason for these reservations? What steps is the UK taking to address these problems?
We would be grateful for a response to these questions by 7 October 2013. In the meantime we will continue to hold the document under scrutiny.

10 September 2013

Letter from Nicky Morgan MP, Economic Secretary to the Treasury, HM Treasury, to the Chairman

Thank you for your letter, of 10 September, regarding EM 10806/13 on the Commission’s Communication: Synthesis of the Commission’s Management Achievements in 2012.

On deterrents, a key instrument for Member States is the Commission’s ability to apply interruptions or suspensions, to programmes in a number of areas of EU spending, where problems have been identified in the management of EU funds. In addition, the European Parliament can refuse to grant the Commission ‘discharge’ for its management of EU funds in a given year.

The Government believes that all identified management shortcomings must be addressed. Of particular note is the European Court of Auditors’ (ECA) 2011 report recommendation that the Commission addresses weaknesses in ‘first level checks’ at the level of Managing Authorities (MAs) and intermediate bodies for rural development and cohesion funds (two of the largest areas of EU spending), through appropriate training measures and specific guidance material. They found that in regional policy, weaknesses in verifications by national authorities were detected, especially with regard to the ‘first level checks’ carried out by managing authorities and intermediate bodies. As such, the Government believes this management shortfall should be an area of focus for both the Commission and Member States, and hence supports the ECA’s call for training measures and specific guidance material to improve existing weaknesses in Member States’ ‘first level checks’.

You asked how corrective measures can be sped up in practice. The Government strongly supports the ECA’s 2011 recommendation that more focus is needed to ensure significant deficiencies in the functioning of the management and control systems in Member States are identified, and the Commission interrupts or suspends payments until remedial corrective action has been taken by the Member State (making financial corrections if necessary to recover those funds). The Government believes the Commission needs to refocus its efforts in improving and streamlining this process to ensure it is undertaken in a timely way.

With regards to your question on accountancy standards, the Government expects that all Member States (if they are not already doing so) should at the very least be ensuring compliance with accounting standards, if the management of the EU budget is to be upheld at the same high standards as many national budgets are.

Finally, you asked a number of questions regarding UK reservations in 2012. The Government takes reservations extremely seriously and continues to work closely with the Commission to ensure all concerns are addressed. However, the UK has raised concerns about the Commission’s level of transparency, the consistency with which it interprets the regulations, and its maintenance of good communication with Member States to enable MAs to respond quickly and positively where concerns over the management of the funds arise. In 2012, the UK was subjected to one reservation in relation to the European Regional Development Fund (ERDF), one in relation to the European Fisheries Fund (EFF) and three in relation to the European Social Fund (ESF). Specifically, these reservations relate to concerns identified in the management and control systems, and instances of ineligibility of declared expenditure.

The UK is taking a number of steps to address the problems identified as quickly as possible. The ERDF England MA has met all of the corrective measures raised by the Commission in relation to concerns about its first level management checks. The Commission has raised a new issue about the way that the MA has designed the control environment, although this design has not been called into question in the past. The MA is now working with the Commission to resolve their concerns. This issue has no financial risk to the EU budget. In 2013, the UK EFF undertook substantial additional audit testing, which was finalised in June. In July 2013, the 2012 reservation on the UK EFF programme was removed by DG Mare (Maritime Affairs and Fisheries) who acknowledged the satisfactory resolution of all issues associated with the reservation. The ESF England programme suspension and payment interruption was made due to error rates and concerns over the management and control systems for technical assistance funds, and those issues are currently being addressed. The Department for Work and Pensions has submitted an action plan to the Commission setting out key actions deemed needed to resolve this. The Scottish Government has taken a number of steps to address concerns over audit controls and error rates in its programmes and all interruptions relating to Scottish ERDF and ESF programmes have now been lifted. The Northern
Ireland authorities are also working closely with the Commission to resolve audit issues raised in relation to its ESF programme.

14 October 2013

**Letter from the Chairman to Nicky Morgan MP**

Thank you for your letter, dated 14 October 2013, on EM 10806/13 on the Commission’s Management Achievements in 2012 which provided detailed responses to the Committee’s questions. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 25 October 2013 and is content to clear this document from scrutiny.

28 October 2013

**COURT OF AUDITORS SPECIAL REPORT NO. 24 ON THE SOLIDARITY FUND - EU SOLIDARITY FUND’S RESPONSE TO THE 2009 ABRUZZI EARTHQUAKE (UNNUMBERED)**

**Letter from the Rt. Hon. Greg Clark MP, Financial Secretary, HM Treasury, to the Chairman**

I am writing to draw your attention to this document, on which we have today submitted an Explanatory Memorandum, to apologise that it was not deposited sooner, and to explain the circumstances and the action we are taking to prevent any repeat.

The document was circulated by the Council Secretariat in a new form, without being attached to a formal cover sheet highlighting that it had been published for submission to Council. As a consequence it was not picked up under the regular arrangements under which documents are automatically deposited. I understand the same issue has affected a number of documents across a range of Government Departments. We have now reached an agreement with the Cabinet Office that they will in the future ensure documents circulated in this form are deposited in the normal way.

While regrettable, in this case the policy implications are limited and there are no regulatory or financial implications. Timetabling issues relating to the progress of the report in Council are set out in the adjoined Explanatory Memorandum.

23 May 2013

**CUSTOMS 2020 (UNNUMBERED)**

**Letter from Nicky Morgan MP, Economic Secretary to the Treasury, HM Treasury, to the Chairman**

I am writing to update you on the progress of negotiations on the Customs 2020 proposal. Since my predecessor’s update in December 2012 the Council partial general approach was taken forward to trilogue discussions. The European Parliament looked favourably on this text, only proposing minor amendments, which are acceptable to the UK and which are also acceptable to the Council and the Commission.

The trilogue discussions did not cover the budget for the programme, which was dependent on the outcome of the Multi-Annual Financial Framework (MFF) negotiations. The Lithuanian Presidency has announced that it expects adoption of the MFF shortly, and along with the Commission it is starting to push ahead with files that are on hold, pending the outcome of these negotiations.

For Customs 2020 the Commission is proposing a 38% increase to the programme budget to €523m over seven years. This is a 5% reduction from the Commission’s original Customs 2020 budget of €548m. While this latest figure constitutes an increase from the Customs 2013 budget, the Commission must ensure that the overall budget for all its programmes is aligned with the MFF agreement. Therefore it is expected there will be increases in some programme budgets and reductions in others.

The current text is a good outcome for the UK. The Government has secured clarification on the voluntary nature of the programme and its activities, including participation in expert teams (which
could deliver customs services across the EU). The Government was also able to block a proposal from Eastern Member States for the new programme to include the funding of customs detection equipment (for example scanners), which would have created a new cost pressure and extended the remit of the programme into customs law enforcement (shared competence).

The Lithuanian Presidency plans to send the proposal to the Justice and Home Affairs Council on 5 December for final approval, and the Government would like to support the proposal. This proposal is subject to Qualified Majority Voting and all other Member States are expected to vote in favour, so the proposal will pass even if the UK were to abstain on grounds of scrutiny.

26 November 2013

DISCHARGE OF THE 2011 BUDGET (14289/13)

Letter from the Chairman to Nicky Morgan MP, Economic Secretary to the Treasury, HM Treasury

Thank you for your Explanatory Memorandum 14289/13, dated 22 October 2013, on the Report from the Commission to the European Parliament and the Council on the follow-up to the discharge for the 2011 financial year. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 5 November 2013.

We welcome this report as a means by which to help ensure sound financial management and budgetary discipline in relation to EU budget expenditure. We also agree with you concerning the necessity of the simplification of regulations so that policy objectives can be maximised and error rates in expenditure minimised. However, we would be grateful for your specific suggestions on how such simplification can be achieved. Given the significant progress that has already been made in setting out the programmes for the 2014-2020 Multiannual Financial Framework, how likely is it that such simplification can be achieved in the short term? Can you give us any examples of such simplification that has been achieved in the past twelve months? Do you agree with us that the British example of introducing cash limits over 30 years ago could usefully be applied to the EU Budget, in particular in the sense that cash limits for each individual programme would override any other budgetary consideration on a year-by-year basis?

We are grateful to you for your account of the steps taken in the UK to address issues concerning revenue collection. Member States as well as the Commission have a responsibility in ensuring sound financial management of EU expenditure, and we urge you to continue your efforts in this regard.

We would be grateful for a response to our questions by 28 November 2013. In the meantime we are content to clear the document from scrutiny.

5 November 2013

Letter from Nicky Morgan MP to the Chairman

Thank you for your letter of 5 November on the discharge of the 2011 budget.

You asked for examples of how rules around EU budget expenditure can be simplified to maximise policy objectives and reduce error rates. The Government is of the view that the Commission should increase its effort to work with Member States’ management and control authorities to identify potential excessive complexities in rules and procedures that can systematically cause errors. Additionally, the Commission should provide proper training and issue guidance on their subsequent simplification efforts to ensure effective and consistent implementation by the relevant Member State authorities. Also, Member States should be encouraged to establish their draft programmes in such a way that measures are clear, verifiable and controllable.

With regards to the feasibility of achieving these steps in the short term, the Government agrees with the Committee that significant progress has already been made in simplification in setting the programmes for 2014-2020. Indeed as we move into the 2014 budgeting year, it is expected that the Commission will make a visible effort to ensure these improvements embed at an early stage of the new Multi-annual Financial Framework (MFF) period. This should include cooperation between the Commission and Member States on an ongoing basis.

The following are some examples of the simplifications achieved in the past twelve months:

— In England, a single European Structural and Investment Fund programme is being set up. This will include England’s European Regional Development Fund and European Social Fund allocations and an element of the European
Agricultural Fund for Rural Development. As part of this work, the Managing Authorities are seeking to reduce bureaucracy for applicants through developing a single core business process and aligning the administration of the funds and relevant documentation as far as possible; and

— In the context of the Common Agricultural Policy (CAP) reform, the UK led the way in pushing for simplification and secured simpler provisions in how the CAP is managed and controlled in order to save farmers and paying agencies time and money. The Government has also made sure that disallowance has to be calculated proportionately, and that the current heavy handed flat-rate system should only be used as a last resort. However the regulations do not represent the genuine reform sought and as such the Government will continue to press the Commission to ensure that the more detailed implementing legislation is proportionate and effective and that the regulations and associated guidelines are interpreted in a flexible way.

On the issue of whether the domestic example, from over 30 years ago, of introducing cash limits could usefully be applied to the EU budget, the Government is of the view that the process of the EU annual budgets being negotiated beneath the ceilings set in the MFF plays an important role in achieving budgetary restraint. Also, within the MFF, individual annual payments are set to prevent excessive front loading of budgets. Nevertheless, the different delivery processes involved in the EU Budget and the UK Budget make it difficult to make a direct comparison between the two.

26 November 2013

DRAFT AMENDING BUDGET NO. 1 TO THE GENERAL BUDGET AND AMENDMENT TO THE INTERINSTITUTIONAL AGREEMENT DRAFT AMENDING BUDGET NO. 2 (7657/13, 7658/13)

Letter from the Chairman to the Rt. Hon. Greg Clark MP, Financial Secretary, HM Treasury

Thank you for your Explanatory Memorandum, dated 2 May 2013, on EM 7657/13 on Draft Amending Budget No 1/2013 and EM 7658/13 on the Amendment to the Interinstitutional Agreement. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 21 May 2013.

We commend the UK Government’s pursuit of fiscal discipline in the EU. We do, however, note that the increase in the payments ceiling is to accommodate the accession of a new Member State, namely Croatia, something that we strongly support.

We are content to clear this document from scrutiny but would welcome an update as negotiations progress.

21 May 2013

Letter from the Rt. Hon. Greg Clark MP to the Chairman

I am grateful for your Committee’s consideration of EM 7657/13 and EM 7658/13 on Draft Amending Budget No.1 (DAB 1) to the 2013 EU Budget and the proposed revision to the Inter Institutional Agreement (IIA), both of which relate to Croatian accession. I am writing to update you on the outcome of negotiations.

As you will know, Croatia accedes to the European Union on 1 July 2013, and DAB 1 concerns the incorporation of the commitments and payments agreed as part of the Treaty of Accession (€655m in commitment appropriations and €374m in payment appropriations). As I have previously stated, the Government believes it is right to support this proposal.

The proposal also included an amendment to the 2013 ceiling of the Multi-annual Financial Framework (MFF) to take into account the additional appropriations required for Croatian accession. As stated in the EM, Point 29 of the IIA states that if new Member States accede to the Union during the period covered by an MFF then the Council and European Parliament, acting on a proposal from the Commission, will adjust the MFF to take account of the expenditure requirements resulting from accession.

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As you will know, the UK and a number of other Member States have had some concerns about the element of the proposal relating to revisions to the overall MFF payment ceiling. However, the Government has been clear that it wholeheartedly supports Croatia’s accession into the EU and, as stated in paragraph 20 of the EM, that this proposal presents an exceptional case concerning accession of a new Member State, as envisaged in the IIA. The Government was able to secure a firm Council declaration which states that this increase shall only be spent on programmes relating to Croatia and that the Commission must provide clear evidence of this. The adopted statement is below:

“The decision to revise the payment ceiling by EUR 374 million is on the basis that this increase is only used for programmes related to Croatia after its accession. As part of its consideration of any further amending budget, the Council will require an update on the implementation of programmes related to Croatia”

According to the latest Commission estimates, Croatia will bring revenues to the EU budget of €234m (with an additional €34m financed from Article 302 – surplus own resources resulting from repayment of the surplus from the Guarantee Fund for external actions), as compared with the required expenditure of €374m. This leaves a balance which will fall on other Member States of approximately €100m. The UK’s financing share in this situation is estimated to be around 12.5%, or around €12m in 2013. There is a one-off sum and has no implications for the level of EU spending in the 2014-20 MFF deal.

The Government concluded that with this added contingency in place and given the relatively limited one-year financial implications, it was in the UK’s interest to support the compromise proposal and not block the exceptional adjustment at the start of Croatian accession.

Given Croatian accession on 1 July, final discussions and a Council vote were to a very tight deadline. Nevertheless, I regret that these new developments did not provide us with adequate time to pass through Parliamentary scrutiny prior to the agreement at Council, on Wednesday 26 June. Negotiations on the proposal, which I attach [not printed] to this letter for your information concluded in Coreper on Wednesday 26 June. The text was then agreed to by the Council that night.

30 June 2013

Letter from the Chairman to the Rt. Hon. Greg Clark MP

Thank you for your letter, dated 30 June 2013, on EM 7657/13 on Draft Amending Budget No 1/2013 and EM 7658/13 on the Amendment to the Interinstitutional Agreement. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 9 July 2013.

We are grateful to you for this response and for your courteous acknowledgment of the need to provide adequate time for parliamentary scrutiny.

9 July 2013

DRAFT AMENDING BUDGET NO. 8: 2013 (14093/13)

Letter from the Chairman to Sajid Javid MP, Financial Secretary, HM Treasury

I am writing with regard to EM 14093/13 on COM (2013) 669 on the Draft Amending Budget No.8 to the General Budget 2013. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 15 October 2013.

Notwithstanding the fact that we only received the EM on this document this morning, in light of the pace of negotiations and the considerable sums involved we felt compelled to write to you immediately. Given that Coreper agreed its position on 14 October (before the EM was received), we would stress to you, as we did to your predecessor, the importance of ensuring that the Committee is kept updated on the progress of negotiations, whether at Coreper or Ministerial Council, on the Annual Budget and Draft Amending Budgets, in particular if significant progress is anticipated in advance of receipt of the Government EM. It is vital that the Committee is given the opportunity to scrutinise proposals of such importance in advance of decisions being made. You state in your EM that the UK will vote against any increase. However, scrutiny overrides are to be avoided even if the UK votes against or abstains. We would also urge you to impress upon Council colleagues the vital importance of allowing national parliaments sufficient time to undertake their scrutiny process.
In terms of the substance of the proposal, how would you respond to the Commission's argument that the updated review of payment needs in the 2013 budget has confirmed a major shortage of payment appropriations, that implementation of payment appropriations is considerably more than at the same date in 2012, in spite of cash-flow constraints leading to temporary restrictions on the outflow of payments, and that "the current rate of implementation underpins the request for a substantial further reinforcement in payments"?

The Committee asked your predecessor about the implications of the MFF deal for future annual Draft Budgets, and in particular what would be the potential impact on budgetary discipline of the agreement to provide for flexibility in the MFF between years. At his appearance before the Committee on 23 July, we warned that, in the deal secured on the MFF, there may be the potential for problems in the future in terms of front-end loading, which would increase the pressure on the budget. In light of this proposal, what are your observations on these concerns, and in particular the potential for, and consequences of, front-loading of annual budgets under the MFF? How would you respond to our suggestion at that meeting that the headline deal achieved earlier this year was therefore not as good as at first sight?

Noting that the Coreper position will shortly go to Council for agreement, we would be grateful for an update on the outcome of negotiations by 29 October 2013. In the meantime we will continue to hold the document under scrutiny.

15 October 2013

Letter from Nicky Morgan MP, Economic Secretary to the Treasury, HM Treasury, to the Chairman

Thank you for your letter of 15 October on Draft Amending Budget 8 to the 2013 EU Budget (DAB 8/13).

You asked for the Government’s views on the arguments used by the Commission for DAB 8/13 following their latest review of payment needs in the 2013 budget. The Commission continues to argue that fast rates of implementation and restrained budget deals over the last few years have caused a shortage in payment appropriations and that in year amending budgets are therefore justified. This was also the argument used to get Council agreement to an additional €7.3bn in Draft Amending Budget 2 (DAB 2/13) earlier this year. The Government does not accept this line of argument and believes the Commission’s request for such large amendments to expenditure in 2013 are unjustified when so many Member States are required to make necessary economies in their domestic budgets. The Government believes these amendments show an inability to manage the budget within the limits carefully negotiated and agreed by the Council and European Parliament. The correct response to shortages would be to present the Budget Authority with real options for savings and reprioritisation to meet pressures that it anticipates throughout the year.

Finally, you note your Committee’s concerns on implications of the flexibilities within the MFF deal for annual budgets. As you may recall, the Prime Minister stated in his post-Council statement on the MFF that “Council has said it is prepared to accept some flexibilities about how spending is divided between different budget years and different areas of spending, but we are absolutely clear that this must be within the framework that the member states have now agreed.” What has been allowed, rightly, is some flexibility between years and between budget headings so that the EU can use its money better. Importantly for budgetary discipline, this flexibility is limited. The key limit is the payments ceiling, which has been cut by €35bn from the 2007-13 MFF period and remains binding. This is set out in the MFF Regulation, which can only be amended by unanimity.

22 October 2013

Letter from the Chairman to Nicky Morgan MP

Thank you for your letter, dated 22 October 2013, on EM 14093/13 on 2013 Draft Amending Budget No.8. The House of Lords European union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 29 October 2013.

We note your response to our questions, and in particular your statement that “the correct response to shortages would be to present the Budget Authority with real options for savings and reprioritisation to meet pressures that it anticipated throughout the year.” Can you be more specific about the “real options” you have in mind? Do you agree with us that the absence of cash limits on expenditure in the EU budgetary system, by comparison with the UK budgetary process, gives rise to a lack of constraint? Do you also agree that the relationship between commitments and payments has
been undermined, with likely deleterious consequences in the long term? Whilst we note your assertion that flexibility is limited by the payments ceiling, does there not remain a significant risk that front-loading of annual budgets will sow problems in ensuring budgetary discipline in years to come?

We also note media reports that Coreper made adoption of the Amending Budget conditional on the European Parliament giving its consent to the Multiannual Financial Framework deal. Can you confirm this? What update on negotiations can you give us?

We also note that, in relation to the 2014 Draft Budget, which we have previously cleared from scrutiny, the Council has informed the European Parliament that it cannot approve all its amendments for the 2014 EU draft budget, and that conciliation has now commenced. In light of this, we would be grateful for an update, both on negotiations up to this point, and on the outcome of conciliation.

In order to take account of the progress of negotiations on DAB8, and on the outcome of the conciliation period on the 2014 Budget, we would be grateful for a response to these queries by 18 November 2013. In the meantime we now clear EM 14093/13 from scrutiny.

29 October 2013

Letter from Nicky Morgan MP to the Chairman

Thank you for your letter of 29 October on Draft Amending Budget No.8 (DAB 8/2013) to the EU Annual Budget 2013 (AB2013). I am writing to offer answers to your questions on DAB 8/2013 and to provide you with further update on the EU Annual Budget 2014 (AB2014) negotiations.

On the Council agreement to DAB 8/2013, the UK voted against on 30 October by written procedure. Sweden, the Netherlands and Finland also voted against DAB 8/2013, but it was approved by a Qualified Voting Majority.

We strongly support your Committee’s view that the Commission and the Council Presidency must properly observe the requirements of Protocol No. 1 to the TEU/TFEU, to facilitate and provide sufficient time for national parliament scrutiny of Commission proposals. The Government voiced its strong opposition to this in Council and, on this occasion, we were able (procedurally) to prevent formal agreement being reached on the proposals until both European Scrutiny Committees of the UK Parliament had been given time to sufficiently consider the proposals. The Government did not allow the proposals to be added to existing Council agendas and did not submit its vote to the Presidency until after both European Scrutiny Committees had cleared the proposals from scrutiny.

Regarding your question on the specificity of the real options for in-year savings and reprioritisation in the EU Budget, the Government notes that it is for the Commission, which has ultimate responsibility for managing spending across the hundreds of budget lines in any one year, to come forward with proposals for resolving in-year budgetary pressures. With that said, the Government has made clear that considerable savings could and should be found across key areas of the budget, including Heading 5 (Administration) and areas of Heading 2 (Preservation and Management of Natural Resources).

You asked whether the absence of cash limits on expenditure in the EU budgetary system gives rise to a lack of restraint. While acknowledging your prior recognition of this point, I reassert that the process of EU Annual Budgets being negotiated beneath the ceilings set in the Multianual Financial Framework (MFF) plays an important role in helping to achieve budgetary restraint. As you know, at the February 2013 Council, the Prime Minister and other EU leaders agreed that the payment limit should be set at €908 billion for the 2014-2020 MFF. This is €35 billion lower than the deal agreed by the previous Government in 2005 for the current MFF period (2007-2013). The European Parliament now needs to give formal consent to the legal document setting out the new MFF.

Developing this point, within the MFF, individual annual payment ceilings are set. These annual ceilings act to prevent excessive front loading of budgets. However, as you correctly identify, the relationship between payments and commitments also impacts upon the budgetary restraint. The gap agreed between commitments and payments ceilings for the 2014-2020 MFF is just over 5%, which is comparable to the current framework.

The different delivery processes involved in the EU Budget and UK Budget make it difficult to make a direct comparison between the two. Nonetheless this Government has taken the same approach of prioritising fiscal consolidation on both. Taking the different processes into account, I would emphasise that it is the payment ceilings which can be said to act as cash limits in the EU Budgetary process. It is these annual ceilings which provide a check on the front loading of annual budget risks, which you highlight, and help to achieve budgetary discipline. The new ceilings set for the 2014-2020 MFF period are already having an effect, as we have seen in the Commission’s proposal for the AB2014.
With regards to the media reports on the conflation of MFF and Amending Budget adoption, it is the case that a series of complex and extremely sensitive negotiation processes are reaching conclusion in the coming period and appropriate sequencing of those processes is clearly important.

Finally, please accept the following update on the ongoing AB2014 negotiations which you requested. On 23 October the European Parliament voted to endorse the recommendation of the European Parliament Budget committee’s position on AB2014. I have attached [not printed] a table provided by the European Parliament setting out its proposal along with the positions of other institutions. The 21 day Conciliation period began after the European Parliament had voted on their position. The first Conciliation meeting took place on 4 November. Another conciliation meeting is scheduled alongside Budget ECOFIN on 11 November, where it is hoped that negotiations will be concluded. I will write to update you again on the outcome of negotiations.

I hope this letter offers a useful update for your Committee.

8 November 2013

DRAFT BUDGET 2014 (UNNUMBERED)

Letter from the Chairman to the Rt. Hon. Greg Clark MP, Financial Secretary, HM Treasury

Thank you for your Explanatory Memorandum, dated 15 July 2013, on an unnumbered EM on the 2014 EU Draft Budget. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 23 July 2013, at which you also answered questions on the Draft Budget.

We understand that agreement on a Lithuanian Presidency compromise was reached at COREPER on 18 July. Consequently we are disappointed that it was not possible to scrutinise this document ahead of agreement being reached. Although we appreciate that, given the delay in agreement of the 2014-2020 Multiannual Financial Framework, this was to an extent beyond your control, these problems were exacerbated by the fact that your EM was received four days late, making it impossible for the Sub-Committee to consider it before the COREPER agreement. Can you explain why the EM was received late? We have previously written to you about problems and delays within HM Treasury in relation to amendments to the 2012 and 2013 Draft Budget. Can you explain to us why budgetary proposals are particularly prone to such problems? What will you do to ensure we receive such documents on a timely basis in the future?

It is particularly disappointing that, in this case, the EM made no reference to the likelihood of agreement being reached at COREPER, stating only that “the Council will negotiate and agree a position on the budget by the end of July.” It is unacceptable that you have again failed to inform us when agreement on documents of such importance as this is imminent. These problems again demonstrate the importance of providing the Committee with advance warning of potential Council agendas. We have written to you separately in response to your letter of 19 July on changes to the scrutiny process. More broadly, what steps will you take to communicate to EU colleagues the importance of ensuring enough time is allowed for national parliaments to complete their scrutiny work?

Turning to the proposal itself, as originally drafted, like you, we welcome the fact that the Draft Budget respects the deal agreed on the MFF, and is within the 2014 ceiling. We also welcome the relative fiscal constraint shown in this Draft Budget. You stress that the Draft Budget constitutes a cut in cash terms from 2013, once Amending Budget 1 and the voted part of Amending Budget 2 are taken into account. However, in taking into account amendments to the 2013 Budget, this does not compare like-with-like. We note that, in comparing the 2013 Draft Budget as originally agreed with the 2014 Budget proposals, there has been an increase in payments from €132.8 billion to €135.9 billion. We understand that the Council compromise agreed a reduction in payments, to €134.8 billion, but this nevertheless constitutes an increase in payments from the 2013 figures as originally agreed of €2 billion. It is not valid to compare the amended 2013 Budget figures with the 2014 baseline figures. Can you give any guarantee at this stage that the 2014 Draft Budget will not also be subject to significant amendment?

We would also be grateful for further details of the implications of the MFF deal both for 2014 and for future annual Draft Budgets. What will be the potential impact on budgetary discipline of the agreement to provide for flexibility in the MFF between years? In the context of this and future Draft
Annual Budgets, what assessment would you make of the growing role of the European Parliament in budget negotiations, and its apparent attempts to use this flexibility to leverage its own power?

In our previous correspondence with you on the 2013 draft budget, we expressed concern that the relationship between payment and commitment appropriations had become confused and was in danger of breaking down. You responded to this by stating the importance of having a greater focus on payments since this is what directly impacts on the public finances. Our fears have been heightened by this proposal. Do you agree that the relationship has broken down? What has caused this breakdown? Has the relationship broken down irretrievably, or can steps be taken to repair it? If so, what are they?

We would also stress the importance of ensuring effective quality of spending as well as fiscal constraint. We therefore welcome the emphasis on Heading 1a (Competitiveness for Growth and Jobs), reflected in the proposed increase in commitments. However, do you agree with us that more needs to be done if the EU Budget is to be oriented towards growth and competitiveness? What practical steps are you advocating to ensure that this happens?

We would also be grateful for more precise details regarding your commitment to “limit EU spending, reduce waste and inefficiency and ensure that where EU funds are spent they deliver the best possible value for money for taxpayers”. What specific adjustments to the 2014 Annual Budget do you wish to see? In what practical ways can “better spending” be secured under Heading 1b (Economic, social and territorial cohesion)? How can it be ensured that payment allocations are “set at the minimum necessary to fund programme implementation”? How will you seek to scrutinise Heading 2 (Sustainable Growth: Natural resources) for possible cuts, and ensure that the level of payments proposed is consistent with the trend of actual spending? How will you ensure that payments under Heading 4 (Global Europe) are focussed on areas where the EU adds most value? We share your disappointment that Heading 5 (Administration) has risen again this year. In what specific ways will you “actively hold the Commission to account” in its commitment to reduce staff costs? In what other ways can administrative expenditure be reduced? Can you provide us with specific examples of savings on the budget, and in particular under the administration heading, that were achieved following UK pressure in the context of the 2013 budget?

In view of the fact that the Council’s position will not be formally adopted until September, we would be grateful for further clarification of these matters before agreeing to lift the scrutiny reserve. Consequently, we will continue to hold the document under scrutiny pending a response to this letter. We request a full response, including a full update on negotiations, by 30 August 2013.

24 July 2013

Letter from the Rt. Hon. Greg Clark MP to the Chairman

Thank you for your letter of 24 July, which you wrote in response to the EM on the 2014 EU Draft Budget of 15 July and the subsequent discussion at the sub-committee meeting of 23 July. I am of course happy to answer any outstanding questions and where helpful expand on answers which I provided at the evidence session.

Budgetary proposals are usually the most fast-moving, complex and lengthy of EU dossiers (the Preparation of the 2014 Draft Budget was 856 pages in length, most of which containing facts and figures that require careful analysis). As we take our scrutiny responsibilities very seriously, HM Treasury puts a great deal of effort into ensuring the accuracy and comprehensiveness of EMs and correspondence. This is done whilst also taking the necessary time to ensure we have an agreed Government position on proposals that also effect other Whitehall departments. Of course the delay in the submission of the 2014 Draft EU Budget EM was regrettable, however given these specific circumstances I hope you will appreciate why a short delay was not that unreasonable.

I similarly regret the delays to the submission of the EMs on DAB 1 and 2, which were exacerbated by Easter recess and prorogation, but I would note that we have also provided Parliament with EMs on DABs 3 to 7 and the MFF proposals within their respective deadlines. More generally, as I said in the evidence session on 23 July, these are dossiers that can move quickly and often unexpectedly and we will continue to endeavour to update the Committees throughout the process.

HM Treasury Ministers and officials take Parliamentary scrutiny seriously and constantly impress upon counterparts across the EU our obligations to national parliaments. I highlighted in EM 10062/13 on the Ireland 10th Review how the Government prevented written procedure taking place until we had cleared scrutiny in both Houses of Parliament, and this is not an isolated incident. We will continue to stress to EU colleagues the importance of allowing appropriate time for national parliaments to undertake their scrutiny work. I am also sure this is something your Committee will continue to raise
when you meet with others across the EU, perhaps even asking the question to Ollie Rehn when he appears before you in the Autumn.

THE 2014 ANNUAL BUDGET PROPOSAL

On the content of the proposal, you question whether the Commission’s proposal constitutes a reduction compared to the 2013 Budget. The Government is not convinced that the original adopted 2013 Budget provides a like-for-like comparator as it does not take account of the large margin with the 2013 ceiling. Whilst the 2013 proposal was constrained thanks to the actions taken by this Government and likeminded Member States, it was still set within the far too generous MFF ceilings agreed by the previous Government and thus the Council was able to increase the 2013 Budget substantially in-year through qualified majority voting (QMV), despite the UK voting against.

As a result of the new budget deal secured by the Prime Minister earlier this year, from 2014 the European budget payments ceilings will be on average around €5bn less than this year’s budget. As I stated at the evidence session on 23 July, the Commission’s proposal for payments in 2014 is a €4.6bn reduction compared to the 2013 adopted budget including accepted DABs. Of course in real terms the reduction is even greater.

MFF

On flexibility within the MFF period, the Government has been clear on the importance of the flexibility that has been agreed. What has been allowed, rightly, is some flexibility between years and between budget headings so that the EU can use its money better. Importantly for budgetary discipline, this flexibility is limited. The key limit is the payments ceiling, which has been cut by €35bn from the current MFF period and remains binding. The MFF regulation can only be amended by unanimity.

The fact that the European Parliament has accepted the ceilings agreed by the Prime Minister demonstrates the success of the MFF deal agreed at the February European Council. Before the introduction of the Treaty of Lisbon, MFF agreements (through the IIA) required agreement by all three institutions. Under the Treaty, negotiated by the previous Government, the MFF regulation requires formal consent of the European Parliament. What has not changed is the UK’s right to block agreement – the MFF regulation still requires unanimity in Council. We also still retain all of our powers to protect the UK abatement. The Own Resources Decision does not require the consent of the European Parliament – but it does require the consent of our Parliament in Westminster.

On the relationship between payments and commitments, the gap agreed between commitments and payments ceilings for 2014-2020 is just over 5%, which is comparable to the current framework. Actual payments have been significantly below the payments ceiling. The key constraint on spend is the payments ceiling for 2014-2020, which is already having an effect as we have seen in the Commission’s proposal for the 2014 annual budget.

I will continue to ensure the Scrutiny Committees are fully informed of progress as we approach the finalisation of formal texts in the coming months.

GROWTH AND COMPETITIVENESS

As I stated at the evidence session, I share your concern about subdued growth in the eurozone. However, I do not believe that competitiveness will primarily come out of EU spending, but rather from reforms such as labour market flexibility and forward thinking initiatives such as the transatlantic free trade agreement. The Government’s overall objective for the EU Budget continues to be a restrained budget, on par with domestic fiscal consolidation taking place across Member States in the EU. Overall, the new MFF is a better-framed budget in terms of growth, jobs and competitiveness. Research and development, and other pro-growth investment, will now account for 13% rather than 9% of the total budget. Funding for transport, energy and telecoms infrastructure has received a considerable increase compared to the current period through the new Connecting Europe Facility. The section of the budget that includes spending on research, innovation and university funding is up by over a third compared to the last MFF. To ensure these allocations are spent on this area alone, the Government will continue to closely scrutinise the Commission’s spending and ensure rules and regulations are adhered to.
Restricting EU expenditure

Whilst this Government's efforts in long-term negotiations are having an obvious effect in restricting EU spending, we will need to continue to work closely with likeminded Member States to fight against any extravagance in the EU budget.

Within Heading 1b, Structural and Cohesion Funding should be targeted to achieve greater discernable impact on the key drivers of economic growth and on employment, and must support national and local investment priorities in order to achieve 'better spending'. In negotiating new rules for EU funding streams under the Common Strategic Framework, the UK has supported efforts to simplify and harmonise the regulatory requirements where possible, to increase the combined impact of the funds and reduce administrative burdens on Member States. For example, within England, the Government announced alongside the Spending Review how €6.2bn of EU Structural & Investment Funds for 2014-2020 will be allocated to Local Enterprise Partnerships (LEPs) across England. This will be in the form of a single "Growth Programme", with the Government simplifying how the funds work together and support LEP plans to drive growth. The UK has supported efforts to target the funds more effectively on key drivers of growth across the EU with the introduction of a requirement for thematic concentration in programmes from 2014 and for preconditions to be put in place that improve the effectiveness of spend.

The 2014 Budget marks a transition point for Structural and Cohesion Fund programmes with 2007-2013 programmes nearing the end of their full commitments and 2014-2020 programmes not yet fully up and running. The Government believes that the Commission needs to ensure that Payment appropriations are set at the minimum necessary to fund programme implementation, and based on realistic implementation rates taking account of the transitional phase in which programmes find themselves, as well as estimates of Member States' absorption capacity.

Within Heading 2, the UK's position is that most of the Common Agricultural Policy (CAP) is poor value for money. Overall spending in 2014-2020 on the CAP will however fall by 13% compared with the last seven-year budget. This is roughly equal to the annual level of spending on the CAP budget and better than a real freeze. The Commission's budget proposals for Heading 2 in 2014 (€56,533m of which €43,777m is European Agricultural Guarantee Fund (EAGF)) indicate a reduction in the overall budget from 2013. The bulk of this consists of direct aids and is not discretionary as the financial ceilings for them are already set in the legislation, leaving little scope to negotiate further in this budget. The proposed budgetary changes for direct aids reflect past political agreements, notably the agreed phasing-in of direct aids in the new Member States and the accession of Croatia. The Commission has activated the financial discipline mechanism to keep within the EAGF sub-ceiling and the adjusted amounts for direct aids in the draft 2014 budget reflect this and the creation of the crisis reserve.

On Heading 4, the EU external budget should draw on the EU's collective weight to deliver poverty reduction and sustainable development, address humanitarian crises, further the EU's goals in the neighbourhood and on accession to the Union, build security and stability and ensure strong, sustainable and balanced growth and prosperity. To ensure the EU's money is focused on areas of most value added, the Government will continue to press for a substantial reduction to the budget for the Instrument for Nuclear Safety: while this has done valuable work, there are now a number of international agencies providing assistance in the field of Nuclear Safety. It will also continue to press for total cuts, or at the very least substantial reductions to the budgets of, the Instrument for Macro Financial Assistance (MFA) and the European Voluntary Humanitarian Aid Corps (EVHAC). We believe that MFA support should not be financed from grants from Heading 4 but should primarily consist of loans which are not funded from Heading 4. With regard to EVHAC, there is no evidence of need. During negotiations on the 2014 Budget proposal in Budget Committee, we pressed the Commission on these points.

The results on Heading 5 are indeed disappointing. During the negotiations on the Commission's proposal, the UK called for significant reductions in this heading in particular. Unfortunately, the Government is very limited in its ability to reduce Heading 5 spending as 70% of it comes from Staff Regulations, where we are limited in our ability to affect change. As the Committee is aware, the Staff Regulation proposals put forward by the Commission in December 2011 were very disappointing. The UK and other likeminded Member States argued for much more ambitious reforms that would have seen real savings and better prepared the Institutions for the 21st century. Whilst the Staff Regulations have yet to be agreed at Council, a Presidency compromise was endorsed by Coreper (without UK support) which sees very limited savings. This was deeply disappointing.

Despite this, it is absolutely necessary to ensure that what limited savings are going to be achieved – including a two year pay freeze, and a 5% reduction in staff numbers – are fully implemented. At the
end of this MFF in 2020, the EU Institutions must have 5% fewer staff than are currently present. Anything less will be unacceptable to the UK, and to many other Member States. To this end, the UK and other Member States have requested benchmark figures from the Commission in order to judge progress on the 5% reduction – whilst the Commission has provided some detail in the 2014 budget documents, we do not have a fully accurate global staff figure against which to judge the mandatory reduction. Whilst we anticipate a certain degree of flexibility on how the reduction is shared among the Institutions, the Government is adamant that this 5% reduction must be achieved, in full, over the next five years.

Outside of the Staff Regulations, reaching Council agreement to reductions has been challenging. However, the UK will continue to push for savings in this remaining 30%, which covers areas such as building works and rent. The Government remains committed to finding these wherever possible.

STATE OF PLAY

Finally, I want to update you on developments in the annual budget negotiations. The Presidency circulated its first proposal for a Council position on 8 July. This proposal saw a cut of €183m in commitment appropriations and €720m in payment appropriations from the Commission proposal; giving overall figures of €141.8bn in commitments and €135.1bn in payments in current prices. This proposal was the stepping stone for a series of discussions in Budget Committee from 9 to 15 July, with coordinated pressure from the Budget disciplinarian Member States on the size of the Presidency proposal.

The final Presidency proposal, which was taken to Coreper on 18 July and which I attach for your reference, was endorsed as a Council position that reduces the Commission’s proposed budget for 2014 by €240m in commitments and just over a €1bn in payments. This results in a proposal of €141.8bn in commitments and €134.8bn in payments. All but three Member States voted in favour of the Council position. As set out in the EM, the UK welcomed the fact that this proposal for the first Budget of the new MFF period respects the deal agreed by European Council in February and is within the agreed 2014 ceiling; but the UK abstained on domestic Parliamentary scrutiny grounds. Denmark welcomed the Council Position but also abstained while domestic Parliamentary scrutiny is completed. Belgium abstained as they thought that reductions to payments went too far.

As in previous years, formal agreement in Council will now be reached through a written procedure by the 2 September. Due to the timing of Parliamentary Recess, the Government will continue to abstain on scrutiny grounds. As you know, the Council Position forms the basis of negotiations with the European Parliament in the autumn with the aim of reaching a final agreement during Conciliation in November. As always, I will keep you updated on further developments as negotiations progress in the autumn.

5 August 2013

Letter from the Chairman to the Rt. Hon. Greg Clark MP

Thank you for your letter, dated 5 August 2013, on the 2014 Draft Annual Budget. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 10 September 2013.

Given that, as expected, Council did adopt its position on the Budget on 2 September, we now clear the document from scrutiny. However, we would be grateful for further updates on the progress of negotiations in the coming weeks.

10 September 2013

Letter from Nicky Morgan MP, Economic Secretary to the Treasury, HM Treasury, to the Chairman

I am writing to provide you with details on the outcome of negotiations on the 2014 EU Budget, and Draft Amending Budget No.9 to the 2013 EU Budget (DAB 9). I have, today, laid a Written Ministerial Statement (WMS), which updates both Houses on the overall outcome of Budget ECOFIN on 11 November and the UK’s voting position. In addition, this letter provides you with information on Amending Letters No.1 and No.2 to the Draft General Budget for 2014 (AL 1 and AL 2). I apologise for the delay in depositing AL 2 caused by an administrative error of oversight. I assure you that my officials are doing everything they can to ensure this does not happen again.
AL 1 was presented on 18 September, and proposes small revisions to the Commission’s original draft budget proposal for 2014. The key changes include implementation of the June European Council (JEC) agreement on frontloading of Horizon 2020, Erasmus and COSME (‘Competitiveness of enterprises and small and medium-sized enterprises’) and the corresponding backloading of CEF-Energy, ITER and ETC within the 2014-2020 Multi-Annual Financial Framework (MFF). This has no net fiscal effect over the 2014-2020 period. It also includes additional assistance to Cyprus through €100m of Structural Funds commitment appropriations in 2014 to address the particularly difficult situation of Cyprus, as agreed at JEC. The net budgetary impact of AL 1 is an increase in commitment appropriations of €100m compared with the Commission’s Draft Budget 2014.

AL 2 was presented on 16 October, and includes a revision to the forecast of Traditional Own Resources (TOR) to be received in 2014, and proposes a small downward revision to the Commission’s forecasts for spending needs in 2014 for agricultural expenditure. The net budgetary impact of AL 2 is a reduction in both commitment and payment appropriations of €4.9m compared to the Commission’s Draft Budget 2014.

Finally, let me set out the outcome on the 2014 Budget negotiations, which concluded on Monday 11 November at the Economic and Financial Affairs Council, with the Council and the European Parliament agreeing on the 2014 EU Budget. The final agreement on the level of spending in the adopted 2014 EU Budget was €142.6bn in commitments appropriations and €135.5bn in payment appropriations. As you know, this is the first annual budget agreed under the new MFF deal that the Prime Minister secured in February. And I am pleased to say that as a result, the 2014 budget is almost €9bn lower than the final budget for 2013, a 6% reduction in EU spending compared to last year.

During negotiations the UK maintained its clear position that any deal should not exceed the ceilings established in this agreement, and indeed should be lower. Working closely with our budget disciplined allies Germany, France, Finland, Austria, Czech Republic, Denmark, Sweden and the Netherlands, this was achieved. However, we wanted to go further than the final agreement to maintain pressure on EU spending, and to secure a bigger margin between the final payments for 2014 and the MFF ceilings themselves. For this reason, the UK, along with Sweden, the Netherlands and Denmark did not support and voted against the final deal.

A compromise proposal on DAB 9 was also agreed at Budget ECOFIN. DAB 9 payments were split between 2013 and 2014, with €250m paid from reprioritised spending from the Global Transfer in 2013 and the remaining €150m from the Global Transfer spent on heading 1a research spending. The remaining €150m of payments required for DAB 9 will be met by payments from within the adopted 2014 budget. The UK continues to oppose the financing proposals for this DAB, as I have set out in the Explanatory Memorandum and follow up letters.

These proposals are due to be formally approved at the General Affairs Council on Tuesday 19 November and voted on in the European Parliament November Plenary, which are currently taking place. I attach the Council’s press release, which includes further detail on the final budget figures.

20 November 2013

EU MORTGAGES DIRECTIVE (8680/11)

Letter from Sajid Javid MP, Economic Secretary, HM Treasury, to the Chairman

I am writing to update you on the European Directive on Credit Agreements Related to Residential Property (CARRP). I know the Committee showed significant interest in the Directive proposal in the past and the previous Financial Secretary to the Treasury agreed to update you once negotiations had progressed further.

As you know, the Government believes that it is vitally important that the European Commission only brings forward proposals that are within its competency on consumer financial services and will truly benefit the single market.

It is important to recognise, however, that as Council negotiations on the Mortgages Directive were subject to Qualified Majority Voting (QMV), the UK could not block the progress of this Directive without the support of a significant number of other Member States. Therefore, as you know, the UK’s negotiating priorities have focused on lessening the negative impact of this Directive on UK industry and consumers.
Since the previous Financial Secretary last wrote to you about this Directive, a political agreement has been reached. The compromise text was passed through at the Committee of Permanent Representatives (COREPER) on 8 May. There are still a number of formal processes to be completed over the coming months before the finalised Directive will be published. Member States will then have two years in which to implement the Directive requirements, and the Government and the Financial Conduct Authority will consult on the implementation in due course, including carrying out an impact assessment.

By the time negotiations had reached trilogues, the majority of the provisions contained in the Directive were already consistent with the existing regulation of the UK mortgage market. This followed strong negotiations in Council and support from UK MEPs in the European Parliament. During trilogue negotiations, the UK built on this and continued to make good progress against its negotiating objectives.

One key priority for the UK was to ensure an exemption for buy-to-let mortgage lending from the scope of the Directive. Buy-to-let mortgages are a product unique to the UK market and the Government believes that decisions concerning the regulation of these products should be left to the UK. We are therefore pleased to have achieved a full exemption for buy-to-let lending from the Directive’s requirements, as part of the political agreement.

The UK also opposed the requirements for Member States to introduce the European Standard Information Sheet (ESIS). As you know, the UK already uses the Key Facts Illustration (KFI) to ensure consumers have the relevant information when looking to take out a mortgage, and we do not believe that the ESIS will provide additional benefit to consumers. Disappointingly, the UK will not be able to continue to use the KFI in the future. As I have explained, as the Council negotiations are subject to QMV, we were unable to prevent this requirement. However, we have secured a 5 year delay to implementation and amended the ESIS to hold more similar content to the current KFI, which will provide a valuable reduction in the burden on lenders from introducing the ESIS.

9 June 2013

EURO AREA CRISIS UPDATE (UNNUMBERED)

Letter from the Chairman to the Rt. Hon. Greg Clark MP, Financial Secretary, HM Treasury

Thank you for your evidence before the House of Lords European Union Sub-Committee on Economic and Financial Affairs at its meeting on 23 July 2013, on developments in the euro area crisis. This letter forms the latest of our regular six-monthly updates in relation to the euro area crisis. You will be aware that the Sub-Committee also heard oral evidence on 2 July from: Ruth Lea, Economic Adviser, Arbuthnot Banking Group, Professor Stephen Haseler, Director, Global Policy Institute, and Vicky Pryce, former Joint Head of the Government Economic Service. In addition, the Sub-Committee held a private briefing with Reza Moghadam, Head of European Department, International Monetary Fund.

INTRODUCTION

A great deal has happened since we last explored the euro area crisis in February 2013. There was the poorly handled bailout of the Cypriot banking sector in March, a flare-up of the crisis in Portugal and Greece and more back-tracking by EU leaders from the important reforms necessary to mend the flaws in the euro area. In our previous letter to you on this subject we wrote that relative calm had been restored following ECB President, Mario Draghi’s commitment to do “whatever it takes” to stop the euro breaking apart. However we also warned against any false assumptions that the worst of the crisis was over. As we set out below, we are pleased to note indications of incipient improvements: though debt levels have increased, so has consumer confidence, and the squeeze on real incomes appears to be easing. But it is still far too soon to be complacent.

The key theme that emerged from our most recent discussions was the concept of “muddling through”: in other words, EU leaders were only motivated to act when a flare-up of the crisis occurred, and even then, they were only willing to do the bare minimum to tackle the most immediate problem. We are concerned that sufficient progress has yet to be made in truly reforming the euro area to ensure that crises do not continue to plague the EU.

You felt it unfair to accuse EU leaders of just muddling through, since the difficulty in reaching agreement was simply a reflection of the complexity of the negotiations. You pointed out in your
evidence to us that progress had been made, with agreement on the Single Supervisory Mechanism (SSM) and the Bank Recovery and Resolution Directive (BRRD), as well as the recently published proposal for a Single Resolution Mechanism. Whilst some progress has been made, implementation of these agreements will take much longer. The SSM will not be operational until mid-2014 at the earliest and the BRRD will not come into effect until 2018. Given the significant disagreement already evident on the SRM, progress on this dossier seems unlikely any time soon.

Ms Pryce pointed out the irony that we need “another good crisis” for any progress to be made. It should not have to come to this. Whilst we accept the difficulty of a group of sovereign states reaching agreement on such complex issues, it is imperative that the euro area moves towards a position of stability (let alone growth) as soon as possible.

AUSTERITY AND STRUCTURAL REFORMS

An issue that our previous update focused on was the poor performance of the euro area economies. Whilst there had been proclamations that the crisis was over, we argued that in some respects it was only just beginning. Austerity as a response to the crisis had been overemphasised and we highlighted the short term pain that structural reforms were inflicting on these economies. The real challenge now, we stressed, was how to restore much-needed growth and competitiveness to the euro area, and by extension, the EU as a whole.

The Commission has since eased its stance on austerity. In May 2013, the Commission announced that France, Spain, Poland, Portugal, the Netherlands and Slovenia would all have more time to complete their austerity plans. The June European Council conclusions confirmed this change of emphasis by stating that “for some Member States, the pace of fiscal consolidation has been adjusted to respond to economic conditions”. We welcome this shift. On 22 July 2013, Eurostat reported that euro area government debt had increased from 90.6% of GDP in the fourth quarter of 2012 to 92.2% of GDP in the first quarter of 2013, demonstrating that the emphasis on austerity had been self-defeating.

This flexibility was welcome but Ms Lea felt that it was merely a “prolongation of austerity rather than an abandonment of it”. There was a unanimous view in the evidence we heard that a short term stimulus was required. You highlighted the Commission’s work with the European Investment Bank (EIB) to increase support for small businesses as an example of where growth enhancing measures were being undertaken. Ms Lea was unimpressed with the Commission’s “feeble” effort to restore growth. She described the Commission-EIB initiative as a “very good idea” but it had come “pretty late in the day”. In her view “there is a terrible reluctance to grab hold of this thing and really make some serious difference to it”.

We have however seen some brighter economic data emerge from the region recently. On 25 July we learnt that euro area PMI data was at its highest levels in 18 months. Many have taken this as an indication that the euro area may return to growth this year. In addition, the reduction of the pressure on bond yields since the ECB’s commitment to “do whatever it takes” last year should not be underestimated. This may in turn enhance the economic performance of the countries in question. What further measures would you suggest the EU could take in order to promote growth?

In exchange for easing the terms of fiscal consolidation, there was a renewed drive for these economies to undertake structural reforms. In our previous correspondence we indicated that, whilst structural reforms would likely benefit these economies in the long run, they would create significant short term pain. We have seen progress in terms of structural reforms: there is a clear indication, for example, that real wages have fallen to more sustainable levels and competitiveness has improved in many of these countries. However, we remain concerned about the impact of structural reforms, not only on short-term economic growth, but also on the political stability of the Member States affected. In countries like Cyprus, Greece and Portugal there are warning signs still that citizens’ tolerance of austerity is being sorely tested. The political ramifications of this are as alarming as they are uncertain.

DIRECT BANK RECAPITALISATION

The meeting of the Eurogroup on 20-21 June reached agreement on the main elements of direct bank recapitalisation. At this meeting, the strict terms under which the European Stability Mechanism (ESM) could provide funds directly to euro area banks were agreed. Banks must have “an appropriate level” of bail-in applied, the country requesting assistance must not be able to perform the recapitalisation itself without “very adverse effects” on its fiscal sustainability, and the institution being bailed out must be systemically important. Furthermore, the bail-out must be viewed as indispensable to the stability
of the euro area as a whole. If these criteria are met, a maximum of €60 billion can be used for direct recapitalisation.

Despite this agreement, there are still a number of hurdles to overcome before direct recapitalisation can be used. The instrument will not be finalised until national parliamentary scrutiny procedures have been finalised and the Single Supervisory Mechanism (SSM) is in force. Securing national approval could be a major stumbling block since, for example, Article 2 of the German implementation law of the ESM treaty explicitly excludes direct bank recapitalisation. In addition, the SSM was seen as a prerequisite to direct recapitalisation, but it is not anticipated to come into force until mid-2014 at the earliest.

The figure of €60 billion was described as a “drop in the ocean” by Ms Lea. In her view it was “a pretty small number considering the size of the European banking system”. Ms Pryce indicated that the delay in reaching agreement on this had already been extremely costly. If Spanish banks, for instance, had been directly recapitalised much earlier, it would have eased the situation and prevented a great deal of pain. What is your view of the delay? Given the delay, and given the small amounts involved, how meaningful is this agreement in practice?

In your evidence to us you emphasised that the €60 billion should not be viewed in isolation, since the resources available to a country during a crisis would be much greater than this figure implied. For instance, an appropriate level of bail-in has to be arranged before direct recapitalisation can take place and sovereign states can also borrow directly from the ESM. We accept this but worry that relying on sovereign states to borrow from the ESM would increase their debt burden (i.e. the exact problem that direct bank recapitalisation was trying to avoid). Does this concern you? Can you provide further clarity on your view that the Eurogroup, if needed, can bring substantially greater resources to bear than just the €60 billion available from the ESM itself?

GREECE

The crisis in Greece has recently reignited. In June 2013, the Democratic Left party pulled out of the coalition government forcing the Greek Prime Minister, Antonis Samaras, to reshuffle his cabinet in order to avoid a snap election. At the same time, there was concern that the IMF might have to suspend its disbursements to Athens after a shortfall of €3-4 billion opened up in Greece’s bailout programme. This shortfall was eventually met but only after last-minute negotiations with the troika.

Meanwhile, the Greek economy remains in a dire condition. The economy is in its sixth year of recession, unemployment is near 27% and nearly two out of three under-25s are out of work. According to economists, current forecasts of GDP growth of 0.6% in 2014 are realistic, but this is far from the 3% annual growth rate the country needs to achieve from 2015 to 2021 to make its debt affordable.

Ms Pryce highlighted the problem of unemployment and the “continued disquiet of the population about things being imposed on them undemocratically by the Germans and others”. She stated that there was an impasse: “There is no way that Greece can actually get itself out of the problems it is finding itself in now”. She indicated that “the pressures that are coming from an economy that is really collapsing are too great for any politician to deal with, and with such a wafer-thin majority, we are going to get into trouble”. Ms Pryce called for a high degree of infrastructure spending by the EU. She accepted that structural reforms, in terms of reform of the public sector and pensions, were necessary but a proper industrial strategy was also key. Ms Lea was sceptical about the possibility of an industrial strategy being enacted. She instead foresaw major defaults, a third bailout and prolonged social pain.

The situation in Greece is arguably unsustainable and a change in approach is necessary. Further significant debt restructuring now seems inevitable. Do you have a view on what could be done to restore sustainable debt levels as well as decent growth and employment levels to this economy? We have noted your reticence in commenting on the domestic policies of other Member States, most recently in the context of Latvia’s accession to the euro. Yet as Greece’s own accession to the euro demonstrated, the consequences of such “domestic policies” can be dramatic indeed for all Member States. Given that a number of these policies are essentially imposed by the troika, and the fact that what happens to the Greek economy has systemic implications for the rest of the EU and the UK, we hope that you will be willing to engage in this discussion.

CYPRIOT BAILOUT

One of the most alarming events since we last explored this issue was the inept handling of the Cypriot bailout. In March 2013, the troika agreed a €10 billion bailout with Cyprus. As part of the
deal, a one-off bank deposit levy of 6.7% for deposits up to €100,000 and 9.9% for higher deposits was announced on all domestic bank accounts. This deal was subsequently rejected by the Cypriot parliament. The final agreement involved protection of deposits below €100,000 but forced losses on deposits over €100,000 in Bank of Cyprus and Laiki Bank. The deal also demanded the closing of Laiki Bank and a fundamental restructuring of Bank of Cyprus.

The negative reaction to the original deal and the ensuing uncertainty that it has created has been worrying. Capital restrictions imposed to prevent a run on Cypriot banks have been eased, but remain in place. Ms Pryce described this incident as the “worst bit of muddling through”, and said that the idea that insured deposits should foot the bill was “crazy”. You told us that everyone had learnt their lessons from this incident and the deal on the Bank Recovery and Resolution Directive would reflect the fact that deposits below €100,000 should be protected. Ms Pryce argued that, despite the protection now afforded to deposits below this threshold, there remained a problem of confidence in the Cypriot banking sector. A number of businesses, for example, have deposits above this threshold and so any kind of depositor bail-in has a huge impact on confidence. How would you respond to these concerns? How can the confidence that was shaken by these initial serious errors be restored?

ROLE OF THE ECB

The role of the ECB during the euro area crisis has been crucial, both as part of the troika and in terms of its commitment to buy unlimited amounts of bonds in the secondary market of a troubled country (known as Outright Monetary Transactions (OMT)). There was unanimous agreement that the ECB’s announcement last year had been instrumental in taking the heat out of the existential crisis that had engulfed the euro area. A recent Financial Times article highlighted the success of OMT in keeping a lid on markets in the context of the recent political and economic problems in Portugal. Unlike in the past, the issues in Portugal did not translate into increased borrowing costs elsewhere in the euro area.

Ms Pryce was complimentary about Mario Draghi’s role at the helm of the ECB in comparison with his predecessor, Jean-Claude Trichet, “in the sense that he lowered interest rates at a time when there was a recession ... whereas Trichet raised them at the time of a recession”. Though everyone celebrated the ECB commitment to OMT, Ms Pryce pointed out that “there has not been any serious purchase of bonds” implying that this relative calm may not last if no action is taken. The same FT article highlighted this and indicated that OMT may have to be tested soon. It also pointed out that few details had emerged on how the mechanism would operate; Mario Draghi shifted his stance from saying the ECB would publish OMT’s legal documentation “soon”, to saying it would only publish it once a country had applied. Going beyond OMT, Professor Haseler put forward the interesting suggestion that there might be a role for the ECB to undertake some form of quantitative easing as other central banks, such as the Federal Reserve, were considering tapering off this type of support. Does it concern you that the ECB has not been clear exactly how OMT would operate if it were to be used? Do you believe there could be scope for the ECB to undertake Quantitative Easing? Would you advise this in the right circumstances?

ROLE OF THE IMF

The IMF recently published a report evaluating the success of the first bailout programme for Greece, where it admitted that mistakes were made. In this it said it had been too optimistic in its growth assumptions and that a debt restructuring should have been considered earlier. This report was particularly critical of the European Commission, claiming it lacked experience of managing financial crises and fiscal adjustment programmes.

Ms Pryce was clear that the IMF “did not distinguish themselves in the way they handled the Greeks”. She did, however, highlight the inexperience the IMF had with dealing with developed economies, and the scale of the bailouts that such countries required. Whilst the IMF made a lot of mistakes, Ms Pryce applauded them for coming out and saying “perhaps we did not get it quite right”.

On a more general point, Ms Lea was unclear “why the IMF got involved in the first place”, since the euro area was a rich part of the world and not the usual target for IMF programmes. Professor Haseler agreed but added that it gave the European institutions some political cover. How would you assess the IMF’s performance during the euro area crisis? Is it both necessary and desirable for the IMF to continue in its role as part of the troika? If so, how can its interaction with the other troika members be enhanced?
THE IMPLICATIONS FOR THE UK

It is clearly important for the UK that the problems of the euro area are resolved. Reports that the existential crisis has receded along with the risk of euro area break-up are therefore welcome. The euro area is pursuing deeper integration in order to resolve its flaws and prevent another crisis, an issue that we are spending considerable time exploring as part of our current inquiry into Genuine Economic and Monetary Union. Given the vital importance of the German position, we will be visiting Berlin and Frankfurt, as well as Brussels, in the autumn to explore these issues. Leaving aside the question of how necessary and realistic these proposals are, they pose considerable implications for the UK.

Professor Haseler suggested that the UK should participate in this integration process. He highlighted that, whilst the euro area countries are talking about greater integration in the euro area, the UK is talking “the exact opposite language”. In his view, the UK’s participation in the single market but not the single currency was “ultimately unsustainable”. Ms Pryce disagreed with this. She argued that the UK was more integrationist than many realised. Indeed, the UK was often more open to integration in a number of areas than those in the euro area. For example, it was partly through the UK’s encouragement that integration in the retail banking, energy and services sectors had taken place. It was her view that the UK could continue to be part of the single market without being a member of the euro.

The UK has managed to maintain its position within the single market but outside the single currency for many years. Part of the reason for this co-existence has been the fact that, as many people often claim, the single currency has not been a ‘genuine’ one. As the single currency area becomes more integrated, it will be a huge challenge for the UK. Key euro area institutions, such as the Eurogroup, are becoming increasingly influential. There is a desire to build on this and create similar separate institutions elsewhere. In your evidence to us you touched on your relationship with the Eurogroup. Can you expand on how you interact with this group? To what extent are you able to influence its discussions? How will you ensure your voice continues to be heard as the euro area Member States contemplate deeper integration? How would you respond to suggestions that other non-members of the euro area seem to manage a more effective and constructive relationship with the euro area?

You emphasised the safeguards the UK Government secured in recent negotiations as evidence that it was possible for the single market to be preserved as deeper integration in the euro area progressed. How long can the protections for the single market and for non-participating Member States, secured for instance in the context of the Single Supervisory Mechanism, persist? Can you provide details of the types of safeguards you will be seeking during the negotiations on the Single Resolution Mechanism? Has thought gone in to developing a ‘blueprint’ for such agreements? If so, could you provide details of this?

It is important that the UK Government seriously consider how this country can continue to work effectively within an evolving European Union. The UK’s unusual position as a member of the single market but not of the single currency is coming under strain. It remains to be seen whether it can be maintained.

We would be grateful for a response to this letter by 30 August 2013.

1 August 2013

Letter from the Rt. Hon. Greg Clark MP to the Chairman

Thank you for your letter of 1 August 2013 on recent developments in the euro area. I was honoured as ever to have been asked to give evidence before the Sub-Committee on Economic and Financial Affairs.

I was however surprised to receive soon afterwards a lengthy letter, extensively trailed in the press, going over much of the same ground. In particular, I disagree strongly with the comments made by Lord Harrison to the press, the UK risks becoming marginalised while we remain outside the single currency and distant from any EU banking union, as well as the suggestion in your letter that the UK’s position as a member of the single market but not the single currency is under strain. There is no evidence for that. This Government has no intention of joining the euro, nor of joining the banking union. We will retain responsibility for our own currency and monetary policy and will ensure that the Bank of England and not the European Central Bank retains responsibility for the supervision of UK banks. It is entirely feasible to do that while remaining an integral part of the single market.

Your letter asked a number of further questions.
First, you ask what further measures the EU could take in order to promote growth. In his Bloomberg speech, the PM stated that “there is a crisis of European competitiveness, as the rest of the world soars ahead”. All EU Member States need to tackle unsustainable levels of debt, reform labour markets, and support business creation and innovation. At the EU level, the priorities are to complete implementation of the Single Market, push forward with new free trade agreements, and avoid new burdensome regulation.

Second, you ask about ESM direct recapitalisation. As I made clear in the evidence to the Sub-Committee on 22 July, the resources available through the ESM have to be seen in the context of the wider framework now agreed for bank resolution.

Third, you ask about Greece. The Government remains very closely involved in the discussions on how Greece can restore sustainable debt levels.

Fourth, you asked about the impact of depositor bail-in in Cyprus. As I set out in my evidence to the Sub-Committee, the Government made clear in all discussions the importance of protecting insured depositors.

Fifth, you asked about the ECB. The Government welcomes the ECB’s commitment to ensuring the proper functioning of the euro area monetary union, including the Outright Monetary Transactions mechanism, and are confident the ECB has the necessary capabilities. Specific monetary policy decisions are a matter for the ECB.

Sixth, you ask about the role of the IMF in the Troika. The Government supports the continuing involvement of the IMF, both directly supporting countries in economic distress, and in providing credibility, technical expertise and rigorous scrutiny to programmes.

Seventh, you ask about the UK’s relationship with the Eurogroup. As set out in my letter of 5 August to Lord Harrison, the UK works closely with all Member States. There is no basis for the suggestion that other non-members of the euro area are more effective in their interactions.

Eighth, you asked about the Single Supervisory Mechanism and Single Resolution Mechanism (SRM). The Government is currently considering the Commission proposal that has recently been published, on which we have already provided you an EM. In the negotiation we will seek to support the establishment of a practical and functional SRM whilst ensuring that appropriate safeguards for the Single Market are maintained.

29 August 2013

Letter from the Chairman to the Rt. Hon. Greg Clark MP

Thank you for your letter, dated 29 August 2013, in relation to our euro area crisis update. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 10 September 2013.

We were surprised by the tone of your letter. When conducting detailed scrutiny on a particular issue, it is normal practice to hear from the relevant Minister in a final evidence session and report the findings in the form of a letter to the Minister afterwards, with further questions relating to what was discussed. Many of the questions reflected our discussion with you on 23 July, and were asking for greater clarification on some of the points you made. We were disappointed at the quality of your replies. Finally, all our correspondence with Ministers is in the public domain and it is common practice for the activities of a parliamentary committee in relation to issues as significant as this to attract media attention.

10 September 2013
Letter from the Rt. Hon. Greg Clark MP, Financial Secretary, HM Treasury, to the Chairman

Thank you for your letter of 16 April 2013, on EM 6984/13, on the European Court of Auditors Annual Report 2011 and Member States’ replies to the Report.

You asked for examples of where steps are being taken to simplify the EU budget regulations and guidelines. I attach [not printed] for your attention my Explanatory Memorandum 7261/13 of 25 March 2013, regarding the Commission’s Multi-annual Financial Framework (MFF) ‘simplification scorecard’. This Explanatory Memorandum sets out the Government’s views on the Commission’s assessment of the simplification agenda for the next MFF period and the accompanying sectoral regulations, and the Commission’s consideration of how these have progressed since the publication of its last scorecard document in 2012.

14 May 2013

Letter from the Chairman to the Rt. Hon. Greg Clark MP

Thank you for your letter, dated 14 May 2013, on EM 6984/13, a Report from the Commission on Member States’ replies to the Court of Auditors’ 2011 Annual Report. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered these documents at its meeting on 4 June 2013.

In our previous letter we clearly asked for examples of where concrete progress had been made in simplifying regulations and guidelines. Your response only served to demonstrate what little progress has been made, since the EM you referred to provided a long list of issues where agreement had not been reached. We can only conclude that you are unable to provide us with concrete examples. We urge you to seek greater progress on this simplification agenda. This will require greater will from the Council, Commission and European Parliament to reach compromises.

4 June 2013

EUROPEAN GLOBALISATION ADJUSTMENT FUND (2014-2020) (15440/11)

Letter from Mark Hoban MP, Minister for Employment, Department for Work and Pensions, to the Chairman

I am writing to report on developments on the European Globalisation Adjustment Fund (EGF) for 2014-2020, prior to the EPSCO Council on 20 June where the Irish Presidency will push for a Common Position to take into co-decision negotiations with the European Parliament. As I explain below, while the detail of the deal will only emerge on the day, it is likely that the scope will be wider than the current Fund and the co-financing rate higher. Therefore, I want to alert you to this in advance given that this is not the outcome that the Government and the Committee wanted.

After the European Council (EC) agreed the overall Multiannual Financial Framework in February 2013 and established that the EGF would continue, there has been a good deal of uncertainty as to how the EGF would be resolved with the Blocking Minority (BM) that continues still.

The Irish Presidency has produced several compromise texts, all of which have been opposed by a Blocking Minority (BM) in Working Group and in COREPER and no agreement has been reached. They re-presented their last proposal to a further COREPER on Wednesday 12 June. When all delegations maintained their previous positions, the Presidency confirmed that the file will be debated publicly at EPSCO, unless negotiations with officials, planned for the morning of 20 June, produce an indicative QMV. Without agreement, negotiations will continue after the debate until there is a QMV.

It is unlikely that the blocking minority will hold and get agreement on its position on all three issues that are to be resolved:

—— on scope, in addition to coverage of mass redundancies that result from major structural changes in world trade patterns as in the current EGF, which the BM want to limit the EGF to, a majority want to include again the
terms of financial and economic crisis that were provided for by the derogation which ended in 2011, and also any new (undefined) crisis, for three years only.

— on co-financing, a rate of 55% whereas the BM support the current 50% (and where the European Parliament Employment Committee has supported a rate as high as 80%).

— on eligibility of beneficiaries, inclusion of the self-employed where their business was demonstrably dependant on the enterprise making the redundancies.

Clearly I cannot predict the outcome of these informal negotiations but I am clear that there will be no time to inform you before the Presidency takes a vote on 20 June, which they are determined to do. I can assure you that I will not vote for the proposal as we do not expect a text that reforms the EGF in line with our objectives. I will either abstain as there will be an EGF and, whilst I don’t like the detail, it will do some good for some Member States in the current economic and fiscal climate, or I will vote against the proposal because I don’t think the content sufficiently addresses the weaknesses of the EGF in key areas, thereby not offering sufficient value to the taxpayer.

I can foresee the European Parliament forcing the co-financing rate as high as possible therefore I judge it important that the BM aim at EPSCO to keep the rate at or close to 50%. On scope, I will press for language that restricts the cause of redundancies as far as possible, although applications under the current Regulation show that the Fund’s scope has been interpreted widely and matters are now past the point where we can narrow it further. It is probable that a crisis derogation, on which we opposed an extension in 2011, will be agreed in some form given that the main forecasts are for weak economic and employment growth in the Eurozone, particularly. On the self-employed issue, this is not relevant to the original Government position and my officials believe that they can be beneficiaries now under the coverage of downstream suppliers or producers, subject to how strictly “redundancy” is interpreted.

I will of course write to you again after Council.

19 June 2013

Letter from Mark Hoban MP to the Chairman

Following my letter of 19 June, I am writing to report on developments on the European Globalisation Adjustment Fund (EGF) for 2014-2020 at the EPSCO Council on 20 June. The Irish Presidency secured a general approach based on a last-minute joint Franco-German proposal. The proposal brought together optional additional support for young unemployed people, an extended scope to cover global crises as well as globalisation, and a single co-financing rate of 55 per cent. The Presidency made it clear that it would not consider changes to any other elements of the text.

No formal vote was needed. However, in the debate, I spoke to oppose the proposal, alongside six other countries, which was not enough support to block agreement. Specifically, I expressed concerns about the efficiency of the instrument, and that the fund had become less relevant through negotiations. I also highlighted the lack of any evaluation of spending as an unjustifiable gap in responsible spending.

The Presidency will now start trilogues with the European Parliament, whose position will be based on the draft report by the Employment and Social Affairs Committee (Rapporteur Marian Harkin). I believe that it will be important for the Council to defend its single co-financing rate of 55 per cent, in contrast with the Parliament’s proposed differentiated rates of 60, 70 and 80 per cent, with the latter being for countries receiving EU financial assistance. This provision is potentially the biggest risk to budget efficiency, in contrast to the widened scope given that EGF terms have always been interpreted loosely by applicants.

I will of course write to you again to update you on negotiations and if there are any significant developments.

27 June 2013
Letter from the Chairman to Nicky Morgan MP, Economic Secretary to the Treasury, HM Treasury

Thank you for the Explanatory Memorandum 12044/13, dated 11 August 2013, from your predecessor, Sajid Javid MP, on a proposal for a Regulation on European Long Term Investment Funds (ELTIFs). The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 19 November 2013. We are also grateful to you for allowing HM Treasury officials to appear before the Committee to explain the document in more detail.

We fully support the aim of boosting long term investment in infrastructure in the EU but worry that the current proposal is not best designed to do this. It appears to have mixed motives in seeking both to boost investment in infrastructure and provide assistance for SMEs. We are concerned that this risks making the proposal incoherent and ineffective. Do you perceive any confusion or conflict between these two motives? Given the market need for the investment of funds in relation to infrastructure-building, would it be more effective to seek to reduce the proposal’s scope so that it is more narrowly focused on infrastructure investment? What support do you have from other Member States in this respect?

We note your objections to the proposal excluding funds of funds and your argument that permitting a fund of fund in ELTIFs would make it easier to secure institutional participation and make the regime more likely to succeed. However, we are concerned about the implications of allowing funds of funds in this framework due to their problematic nature. How would you respond to these concerns?

The Alternative Investment Fund Managers Directive (AIFMD) has imposed some rather onerous conditions on firms and there have been significant costs of compliance. This proposal could be used as an opportunity to eliminate some of the more anachronistic elements of AIFMD. If you agree, can you outline how this might be achieved?

In addition, do you think there is scope to incorporate some form of attractive tax treatment to encourage participation?

We would be grateful for a response to our questions by 3 December 2013. In the meantime we will continue to hold this document under scrutiny.

19 November 2013

Letter from Sajid Javid MP Financial Secretary, HM Treasury, to the Chairman


I would like to start by confirming that I will continue to be the minister responsible for this dossier in my role as Financial Secretary.

You ask whether the scope of the proposal ought to be narrowed to focus on infrastructure investment. This regime is designed for fund managers with assets in excess of the threshold of €500 million. Venture capital funds typically fall below this threshold. There is also already a regime to cater for funds below this threshold investing in small and medium enterprises (SMEs): the European Venture Capital Fund Regulation.

We therefore agree that there is an argument that the ELTIF regime should focus on infrastructure rather than SME investment. However, we are not clear that we need to explicitly prevent ELTIFs investing in SMEs as eligible investments.

We note your concerns about the implications of allowing fund of funds structures in this framework. As noted in the Explanatory Memorandum, a fund of funds structure can be a simple way of achieving diversification for investors who do not have the expertise or resources to invest directly in a diversified range of investment funds. Removing this option would therefore restrict investor choice and potentially reduce participation in the ELTIF regime. However, we will continue to engage with industry and investors to consider these issues further.

We agree that some provisions of the Alternative Investment Fund Managers Directive (AIFMD) are not relevant to firms carrying out this activity, and so impose costs with little benefit. We will engage
closely with asset management firms, advisory firms, legal firms, and trade associations to identify what the non-relevant provisions of AIFMD are and how they might be reformed.

You asked whether there was scope to incorporate some form of attractive tax treatment to encourage participation in ELTIFs. In general, UK funds currently enjoy a favourable tax regime, as the overall objective for the taxation of funds is for investors to pay the same amount of tax as they would have done had they invested directly in the underlying assets. In practice, this means that little and in some cases no tax is borne by the fund itself. The Government will look into the tax treatment of ELTIFs once the details are finalised.

30 November 2013

EUROPEAN REGIONAL DEVELOPMENT FUND AND THE INVESTMENT FOR GROWTH AND JOBS GOAL (15249/11)

Letter from Michael Fallon MP, Minister for State for Business and Enterprise, Department for Business, Innovation and Skills, to the Chairman

I am writing to provide an update on progress of the negotiations on the above Regulation, which your Committee has cleared from scrutiny. As you may recall, successive Presidencies have agreed a series of partial general approaches covering different thematic blocks. The European Parliament has also voted in its Regional Development Committee on the amendments it wishes to see and I provided an assessment of these in my letter sent on the 31 January 2013. Since then, the Irish Presidency, and now the Lithuanian Presidency, has held numerous informal triilogue meetings with the European Parliament’s rapporteurs and the European Commission. The discussions have, as before, been undertaken on the basis that nothing is agreed until everything is agreed.

In my letter of 31 January, I mentioned that the European Parliament wanted 22% of the European Rural Development Fund (ERDF) spent on the low carbon objective in more developed and transition regions and 12% in less developed regions. The proposed compromise is 20% in more developed regions, 15% in transition regions and 12% in less developed regions. This provides greater flexibility and the managing authorities for ERDF in the UK believe these figures are workable. The European Parliament has also dropped its proposal that regions should be free to select the fourth thematic objective for which a minimum level of ERDF spend should be allocated, in addition to the three proposed by the Commission (innovation, SME competitiveness and low carbon). Instead it has agreed that the fourth should be ICT. The European Parliament and the Council have also both agreed that infrastructure should be within the scope of the ERDF in more developed regions, not just transition and less developed regions. This would provide flexibility if needed to support for example broadband investment in rural areas of more developed regions, subject to any state aid requirements. Finally, the proposed compromise keeps the flexibilities in the Council’s Partial General Approach to provide for lower levels of spend on the four main objectives or on the low carbon one in one category of region, if this is balanced by higher levels in other categories of regions.

The thematic objectives and the investment priorities that sit beneath them reflect in the main the position adopted by the Council, with some of the specific references to tourism and creative and cultural industries sought by the European Parliament dealt with in the recitals. The investment priorities for the low carbon thematic objective now also include promoting research, innovation and adoption of low carbon technologies and sustainable multi-modal urban mobility. These provide additional flexibility to meet the minimum spend requirements for low carbon. Under the transport thematic objective, the European Parliament has pushed for the inclusion of airport infrastructure, but a provision has been added to the article setting out the scope of the ERDF to make clear this is permissible only if related to environmental protection or accompanied by investments to mitigate the negative environmental impact.

The European Parliament, like the Commission, attached importance to the concept of sustainable urban development and the role of urban authorities. The Council in its Partial General Approach was more cautious about the scope of delegation to urban authorities because past experience had led to high error rates and financial irregularities. The proposed compromise encourages the development of strategies containing integrated approaches to deal with economic, social and environmental challenges in urban areas. There is a separate requirement for 5% of the ERDF to be allocated to such strategies where at least some tasks related to the selection of projects have been delegated to urban authorities. The scope of this delegation is much less broad than originally proposed by the Commission and minimises financial risks. I anticipate that in the UK this regulatory requirement will be met through London’s ERDF allocation. London, because of its size, is likely to receive more than
5% of the total UK ERDF and, although final decision yet to be taken, may be designated an Intermediate Body and have selected tasks delegated to it.

I would also like to provide you with an update on the budgetary settlement for each Fund. The February European Council agreed an overall budget for Structural and Cohesion Funds in commitments of €325,149million (2011 prices). This has been significantly reduced compared to the original Commission proposal for €336,020million.

Of this €66,362million is allocated to the Cohesion Fund. The remaining budget for ERDF and ESF is €258,787million. The precise split of this funding between ERDF and ESF is dependent on the final text of the Common Provisions regulation but is likely to see around 25% of the cohesion budget devoted to the ESF (€81billion) with the remaining 75% devoted to ERDF and the Cohesion Fund (€244billion).

To enable the Regulation to be adopted before 1 January 2014, there will need to be agreement at first reading. In terms of next steps, the European Parliament is expected to vote in plenary in the week beginning 21 October. The text will then pass to the Council. The proposed compromises in the informal trialogue, if accepted in the European Parliament’s plenary vote, should provide the basis for the Council to agree the Regulation at first reading.

13 August 2013

EUROPEAN SOCIAL FUND AND EUROPEAN REGIONAL DEVELOPMENT FUND
(15253/11)

Letter from Michael Fallon MP, Minister for State for Business and Enterprise,
Department for Business, Innovation and Skills, to the Chairman

I am writing to update you on the progress of the negotiations on the European Territorial Cooperation (ETC) Regulation, which your Committee has cleared from scrutiny. The Council has now adopted partial general approaches on all thematic blocks relevant to this regulation. I have kept Parliament informed at each stage when these were before Ministers at the General Affairs Council. Following this the Irish Presidency has conducted an intensive round of informal trialogues with the European Parliament. The discussions have, as before, been undertaken on the basis that nothing is agreed until everything is agreed. It is now expected that the European Parliament will vote in plenary on its first reading of the ETC Regulation during its October Plenary Session (the indicative date for the vote is 22 October 2013).

The Government has strongly supported the principle of thematic concentration throughout the negotiations. The Government therefore welcomes that at the present state of the negotiations the text states that at least 80% of the ERDF allocation to each cross-border cooperation and transnational programme should be concentrated on up to 4 thematic objectives as set out in Article 9 of the Common Provisions Regulation.

In the agreement reached by the February European Council on the multiannual financial framework, a specific allocation of €150million (all figures in 2011 prices) was made to the PEACE Programme (the UK part of the allocation is €106.1million). The Government welcomes the support for the PEACE Programme within the ETC regulation. Article 6 makes specific reference to the cross-border programme between Northern Ireland and the border counties of Ireland and acknowledges the special nature of the programme allowing it to support actions to promote cohesion between communities.

The resources for European territorial cooperation have not yet been specified in the draft regulation text as these need to be formally voted on by the European Parliament before they are included. The February European Council agreed that the resources for the “European territorial cooperation” goal will amount to a total of €8.948 billion which will be distributed as follows:

- a total of €6.627 billion for cross-border cooperation;
- a total of €1.822 billion for transnational cooperation;
- a total of €500 million for interregional cooperation.

This represents a reduction of around a quarter to the overall figure the Commission had proposed of €11.700million.
It is expected that the European Parliament will be voting on the multiannual financial framework regulation during its plenary session in September 2013. However, there has been a high level agreement between the European Parliament and the European Council on the multiannual financial framework reached in June on the multiannual financial framework.

Our provisional assessment is that the UK’s allocation for cross-border and transitional programmes (including the allocation for PEACE) is €757.2 million (in 2011 prices), compared to €735 million (in 2011 prices) for the 2006-13 period.

The Government considers that it is important that the regulations are adopted in a timely manner in order for programmes to be able to start early in the next programming period starting in 2014.

To enable the Regulation to be adopted before 1 January 2014, there will need to be agreement at first reading. As mentioned above, the European Parliament is expected to vote in plenary in the week beginning 21 October. The text will then pass to the Council. The proposed compromises in the informal trialogue, if accepted in the European Parliament’s plenary vote, should provide the basis for the Council to agree the Regulation at first reading.

13 August 2013

EUROPEAN SOLIDARITY FUND (12883/13)

Letter from the Chairman to the Rt. Hon. Greg Clark MP, Financial Secretary, HM Treasury


We recognise the importance of the European Solidarity Fund as a means by which the EU can provide support to stricken Member States and those involved in accession negotiations in dealing with the impact of natural disasters. We have previously expressed our support for measures to speed up the process of agreeing and making financial assistance available under the Fund, and to that end this appears a sensible proposal in meeting the Commission’s aims of making the instrument quicker to respond to disasters, more visible to citizens, simpler to use and with clearer provisions in place. However we would note our previous concerns about the Fund being placed outside the EU Budget.

You state that you will seek clarification on issues such as the proposed recovery framework and the source of funding for preventative measures, in order to ensure the Budget size is respected, before deciding on your position. We support you in these efforts, but would be grateful to know if you have any specific concerns at this stage that budgetary control will not be exercised. In that regard, we would be grateful if you can inform us of your position on that proposal once it is known.

You also state that there will be a clear definition of the scope of the Fund, limited to natural disasters including man-made disasters that are the direct consequence of a natural disaster. There is also a specific provision for slowly unfolding disasters such as drought and defining the start of such disasters as the date when public authorities took the first counter-measures. Is there any danger that these criteria are too wide-ranging? For instance, could the definition of a “slowly unfolding disaster” be a matter open for interpretation?

You state that care should be taken to ensure that the Fund does not act in the place of Member States or candidate countries, and you welcome the fact that the Regulation respects the principle of subsidiarity in that the Fund will only intervene to complement national efforts or to step in where the capacity of an affected country has reached its limits. Is there any reason to believe that the principle of subsidiarity will not be followed in the future? Has anyone argued to the contrary?

You state that the timetable for negotiations is not yet available. We would be grateful for an update as and when further details emerge.

We would be grateful for a response to these questions by 7 October 2013. In the meantime we will continue to hold the document under scrutiny.

10 September 2013
Letter from the Rt. Hon. Greg Clark MP to the Chairman

Thank you for your letter of 10 September 2013, on EM 12883/13 on a proposal amending Council Regulation (EC) No 2012/2002 establishing the European Solidarity Fund, and for your contributions at this early stage of negotiations.

You asked whether the Government has any specific concerns at this stage that budgetary control will not be exercised and that the principle of subsidiarity will not be followed in the future. The Government agrees with the Committee that these are both extremely important issues for the UK in considering its position on this proposal. However, as discussions have not yet begun it is not possible to say whether concerns will arise from the text. As I said in my EM, the Government believes that disaster response is primarily the responsibility of national governments and care should be taken to ensure the Fund does not act in the place of Member States or candidate countries and that budget size is respected. We will be working with our like-minded Member States to push for these UK objectives.

On the criteria used to define the scope of the fund, it is too early fully to assess this. But we will seek to ensure the scope continues to be aligned to the purpose of the fund when originally established, which was major disasters. In turn, defining a 'slowly unfolding disaster' will be an important element of any future negotiation, to ensure both that it does not inadvertently widen the scope of the fund, and that it is not ambiguous.

There have been no further developments on this proposal since I submitted the EM to you on 14 July, and we have not yet received a timetable for when discussions will begin. I will update you on negotiations in due course.

7 October 2013

Letter from the Chairman to Sajid Javid MP, Financial Secretary, HM Treasury

Thank you for the letter from your predecessor, Rt. Hon Greg Clark MP, dated 7 October 2013, on EM 12883/13, on the European Solidarity Fund. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on Tuesday 15 October 2013.

We note from the letter that discussions have not yet begun and that it is consequently difficult to answer our questions with any precision. We would therefore be grateful if you could write again with a substantive response to the questions and concerns that we raised in our 10 September once negotiations have begun. Although we would be pleased to receive a response sooner should progress be made before then, we would be grateful for an update on the progress of negotiations by 2 December 2013 at the latest. In the meantime we will continue to hold the document under scrutiny.

15 October 2013

Letter from Nicky Morgan MP, Economic Secretary to the Treasury, HM Treasury, to the Chairman

Thank you for your letter of 15 October on EM 12883/13 regarding a proposal amending Council Regulation (EC) No 2012/2002 establishing the European Solidarity Fund, in which you request a progress update on negotiations.

When the previous Financial Secretary wrote to you on 7 October, we had not yet received a timetable for when discussions would begin. The Government now understands that Greece will commence negotiations under their Presidency in the first half of 2014. The European Parliament are also shortly due to start discussing this regulation at committee level. Pending the commencement of these discussions, I remain unable to provide the requested update at this time.

28 November 2013

EUROPEAN STATISTICAL PROGRAMME 2013-17 (12663/13)

Letter from Nick Hurd MP, Minister for Civil Society, Cabinet Office, to the Chairman

I attach [not printed] an Explanatory Memorandum (EM) on a proposal for a Regulation amending the Regulation establishing the European Statistical Programme 2013-17 (ESP).
I also enclose a copy of a letter [not printed] to the Chair of the House of Commons European Scrutiny Committee explaining handling errors in previous correspondence with that Committee about negotiations on the parent Regulation (99/2013). If you would find it helpful, officials would be happy to meet with the clerks of your Committee to discuss how to ensure such errors do not reoccur in relation to correspondence with your Committee.

As you received copies of the correspondence in question, I offer you my apologies for any impact the errors may have had on the business of your Committee.

14 August 2013

EUROPEAN SEMESTER 2013: COUNTRY-SPECIFIC RECOMMENDATIONS
(UNNUMBERED)

Letter from the Chairman to the Rt. Hon. Greg Clark MP, Financial Secretary, HM Treasury


We note that these documents illuminate a number of issues that are at the centre of current UK party political discourse, including tackling the deficit, the programme of welfare benefits, capital investment and childcare costs. The Commission’s overall assessment is that “the United Kingdom is experiencing macroeconomic imbalances, which deserve monitoring and policy action. In particular, macroeconomic developments in the area of household debt, linked to the high levels of mortgage debt and the characteristics of the housing market, as well as unfavourable developments in external competitiveness, especially as regards goods exports and weak productivity growth, continue to deserve attention.” Is this an accurate assessment? We wrote to you on 21 May 2013 on the UK In-Depth Review, where we set out a number of the Commission’s specific concerns and criticisms about the UK economy, and asked for your response to its assessment. We look forward to a response to that letter shortly.

These documents also give rise to a number of cross-cutting issues that we wish to pursue with you. You state that the Commission has extended the deadline for a number of Member States in meeting their excessive deficits targets. Do you support the Commission’s decision? What are its implications? Does it in turn relax the impetus placed upon Member States to undertake necessary structural reforms? Does it constitute an official ‘relaxation of austerity’, or is it simply an acceptance of the inevitable? We note that the UK’s own excessive deficit deadline has not been extended. Why is this? Do you anticipate the UK being offered its own extension by the time of the deadline of 2014-15? Does it make sense for some Member States, but not others, to be given such an extension at this stage? You state that structural reforms at EU level are an essential complement to the reform efforts of individual Member States. What specific reforms do you have in mind?

You note that the Commission also refers to the particular role that Member States with current account surpluses could play in supporting demand. Are we right to assume that the Commission here has Germany in particular in mind? If so, how might Germany and other creditor Member States be expected to react to this advice? If they choose to ignore it, what does it tell us about the efficacy of the Semester process, and the Commission itself, in terms of influencing the future economic health of the EU? In this context, we would welcome your analysis of the proposals contained in the Franco-German paper of 30 May, entitled Together for a stronger Europe of Stability and Growth, on closer coordination of economic policy among the Eurozone Member States, and in particular its institutional implications, in particular for the UK.

Notwithstanding your statement that different rates of calculation have been used, European youth unemployment, including in the UK, now stands at a destructively high level. What urgent steps are being taken to tackle the consequential threat of an EU-wide ‘lost generation’? Is the Semester process (as well as the EU institutions more generally) equipped effectively to tackle such a massive issue, or is it, as some have warned, hard-wired for austerity? Does the process need to change in order to encourage “growth-friendly fiscal consolidation”? 

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Both the Commission and the Government cite the important role of the European Investment Bank. Yet we remain deeply sceptical about the impact it can have in the current economic climate. In evidence before us on 4 June 2013, Megan Greene, Chief Economist, Maverick Intelligence, told us that “the eurozone’s plan right now for alleviating unemployment is pretty lacklustre. It seems like they are pinning most of their hopes on the European Investment Bank, which will hopefully help fund SMEs. Of all the institutions I have ever looked at, the EIB is one of the most sclerotic, so I think anyone who is hoping that there is going to be a quick turnaround in unemployment in Europe is sadly mistaken.” How would you respond to this assessment?

We note that discussion of these documents will take place at ECOFIN on 21 June. In anticipation of this, we now clear these documents from scrutiny. We also now clear from scrutiny unnumbered EM on SWD (2013) 125 on the UK’s in-depth review. However, we would be grateful for a response to this letter, a response to our letter of 21 May 2103 on the in-depth review, and an update on the outcome of discussions at the 21 June ECOFIN, by 3 July 2013.

18 June 2013

EUROPEAN SEMESTER 2013: IN-DEPTH REVIEWS (8660/13)

Letter from the Chairman to the Rt. Hon. Greg Clark MP, Financial Secretary, HM Treasury

Thank you for your Explanatory Memorandum 8660/13 on the Commission Communication on the results of In-Depth Review on the prevention and correction of macroeconomic imbalances, and an unnumbered EM on SWD (2013) 125: the In-Depth Review of the United Kingdom. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered these documents at its meeting on 21 May 2013.

We are grateful to you for these documents, and for your summary of the European Semester mechanism and the 2013 process thus far. There has been considerable discussion recently about the future shape of the European Semester. What is your assessment of the Semester mechanism? How effective had the 2013 process been thus far? Are there any ways in which you would wish to see it reformed? What practical impact does it have on UK policy-making?

On EM 8660/13, we note that only two Member States, Spain and Slovenia, have been identified as having excessive imbalances. Do you agree with this assessment? In view of the continuing weakness of the EU economy, does it surprise you that only two Member States (aside from those already under enhanced surveillance) have been identified as having excessive weaknesses?

We note your summary of the Commission’s assessment as set out in the In-Depth Review of the UK. Whilst we welcome the fact that the Commission identifies a number of areas where the UK economy has been reformed or is strengthening, we also note that it sets out some concerns. For instance, the Commission finds that:

— The UK has experienced a slow, subdued and stuttering recovery from the financial crisis, and it is unlikely that the unemployment rate can continue falling given the weak growth outlook. The Commission believes that unemployment may have reached its trough.

— Low public and private investment, impaired credit flows, and a resulting low level of churn in the economy could all impair the effective reallocation of resources in response to the shocks that the UK economy has experienced.

— Labour productivity remains somewhat below that of France and Germany. In particular, productivity growth in the goods-producing sector lags behind that of the services sector.

— Net bank lending is still falling both for large firms and SMEs. In addition, access to non-bank lending remains largely restricted to bigger firms. Competition in the banking sector is also limited, which is more of a problem for SMEs. The UK private sector has tightened its lending more sharply than the euro area average. On current policies, the flow of credit may only be normalised once broader macroeconomic conditions improve.

— The UK’s poor export market share performance is due to “often underexploited growth possibilities”, and there is scope for increasing the
number of exporting SMEs. The Commission also notes that external performance in 2012 was worse than expected.

— UK infrastructure is struggling to meet the demands of the global economy, and investment in the UK has remained consistently among the lowest in the EU.

— UK producers are confronted with a significant skills gap, in particular in manufacturing.

— Household debt is likely to pick up again in the medium term, unless real progress is made in addressing housing supply shortages. The Commission states that it is not clear how effective the Government’s proposed measures will be in boosting the supply in housing. It also notes that some of the Government’s reforms initially caused further reductions in housing supply.

What is the Government’s view of this assessment of the UK economy, and the steps proposed by the Commission to address these points?

We note the Commission’s statement that recent developments in relation to the Government’s fiscal consolidation programme will be discussed in detail in the European Commission’s assessment of the UK Convergence Programme, in May 2013. We look forward to receiving full details from you of this assessment. When do you expect the Commission’s assessment to be published?

We are content to clear 8660/13 from scrutiny. However, we will retain the unnumbered EM on the UK In-Depth Review under scrutiny pending a response to our questions.

21 May 2013

Letter from the Rt. Hon. Greg Clark MP Treasury to the Chairman

Thank you for your letters of 21 May and 18 June regarding the above mentioned documents. The letters raise a number of very broad questions on the objectives and impact of Government economic policies. I have focused responses below on those aspects most closely related to the Commission documents.

TE THE GOVERNMENT’S VIEW OF THE 2013 EUROPEAN SEMESTER

You ask about the Government’s overall view of the European Semester. The analysis in the Semester is overall supportive of the urgent need for EU Member States to tackle their fiscal deficits and debt and improve their economic growth prospects. On the UK specifically, the European Commission stresses the importance of our tackling our deficit, pursuing ambitious structural reforms, and prioritising investment in infrastructure. These are exactly the priorities of the Government.

On the Semester process, while we share much of the Commission’s analysis, it is important that their Country Specific Recommendations give Member States enough flexibility to design appropriate policy responses. For example, as I made clear during a House of Commons debate on the Semester on 17 June, while we recognise the need to raise revenue, the Government has no intention of implementing the Commission’s specific recommendation on VAT. As you are aware, the Commission’s recommendations are not binding on the UK.

MACROECONOMIC IMBALANCES PROCEDURE

You ask about our view of the Commission’s assessment in the UK’s In-Depth Review. The report makes clear that while the UK economy is experiencing imbalances, these are not excessive or problematic. We share that view. The Commission also recognises that rebalancing is underway, and that the Government is taking decisive action to support household debt reduction and boost UK exports. The Government has made significant progress in reversing the unprecedented rise in borrowing and the deficit has been reduced by a third as a proportion of GDP over three years. Over one and a quarter million private sector jobs have been created and employment is around record levels, exceeding the pre-crisis peak.

As to the Commission’s assessment of risks in other EU Member States, it is right that those countries facing the most urgent reform challenges receive strongly worded recommendations.
EXCESSIVE DEFICIT PROCEDURE

You ask about the significance of the Commission’s decision to extend the Excessive Deficit Procedure (EDP) deadlines for a number of countries (France, Spain, Netherlands, Portugal, Poland, Slovenia). Our understanding is that this reflects primarily the Commission’s response to new economic data, and that the Commission decided to use the available flexibility in the Stability and Growth Pact to extend the deadlines. There has been no change to the Pact itself, and the Commission has been clear that the extra time to meet deficit targets must be used to enact ambitious structural reforms.

EU GROWTH AND THE SINGLE MARKET

You also ask about the structural reforms we consider necessary at EU level to complement the efforts of individual Member States. The UK Government considers that there needs to be a step change in structural reforms across Europe, and continues to argue for the importance and integrity of the Single Market with a pro-business, pro-growth agenda that fosters greater competition throughout Europe. All Member States must endeavour to deepen the Single Market, including completing the Single Market in services, while also prioritising integrated energy markets and a genuine digital Single Market. Improving the EU regulatory environment and driving forward ambitious and comprehensive EU Free Trade Agreements are further priorities for the EU growth agenda. The European Commission estimates that the EU-US Free Trade Agreement alone could be worth up to €119 billion a year to the EU economy.

Your letter also refers to a European Commission paper on the role of Member States with current account surpluses. The Government agrees with the Commission’s analysis that at stimulating domestic demand in surplus countries, such as removing barriers to the Single Market, could help to stimulate both faster and more balanced growth in Europe.

FRANCO-GERMAN PAPER

You also asked about the Government’s views of the Franco-German paper “Together for a stronger Europe of Stability and Growth”. The paper includes a number of interesting proposals, including on closer coordination of economic policy among euro area Member States. The Government has noted the proposal for a two stage approach to reforming economic coordination in the euro area, and especially welcomes its clarity that measures are intended for euro area Member States only.

However, as agreed in the December 2012 European Council Conclusions, proposals to complete EMU must be open and transparent towards Member States outside the euro area, and throughout the process, the integrity of the single Market must be fully respected.

YOUTH UNEMPLOYMENT

You ask specifically about youth unemployment. While the Semester process has a role to play in encouraging Member States to reform their labour markets, this is essentially a Member State competence. The Government has already taken decisive action by introducing the Youth Contract in April 2012, providing almost £1 billion to support young people into work in the UK. Over the last year, the level of UK youth unemployment has fallen and on average young people flow off Jobseekers’ Allowance faster than older age groups.

EUROPEAN INVESTMENT BANK

In your letter you refer to the role of the European Investment Bank (EIB) in an EU growth initiative. We believe the EIB can make an important contribution to UK investment and growth. Over the last 5 years the European Investment Bank has signed finance contracts worth in the region of €23 billion for UK-based projects.

The EIB rapidly increased its lending volumes across Europe in the wake of the crisis, mobilising finance for key infrastructure projects, utilities and supporting SMEs. In recognition of the potential benefits, the June 2012 European Council asked the EIB to further increase its support to the European economy, envisaging a capital increase and an additional €60 billion of lending over the next 3 years.
Finally, you asked to be kept in touch with consideration of these documents by Council. At ECOFIN on 21 June, the Council prepared the discussion by Heads of State or Government of country-specific recommendations to the Member States on their economic and fiscal policies. The Council also closed excessive deficit procedures for Italy, Latvia, Lithuania, Hungary and Romania, gave notice to Belgium on measures to correct its deficit, extended the deadlines for Spain, France, the Netherlands, Poland, Portugal and Slovenia to correct their deficits, and reopened an excessive deficit procedure for Malta.

6 July 2013

EUROPEAN STATISTICS (9122/12)

Letter from Nick Hurd MP, Minister for Civil Society, Cabinet Office, to the Chairman

I am writing further to the last update provided on 18 March, which followed your report of 23 January 2013, and your subsequent report of 26 March, on negotiations in the Council and European Parliament (EP) on the Reform of Regulation (EC) 223/2009.

The Irish Presidency has initiated a further hearing of Member States to seek support for its latest compromise text after trilogues. The government assumes the compromise text will be moved by the new Lithuanian Presidency to the next stages of the co-decision procedure. A vote at COREPER may therefore be required, and this letter sets out the government’s position with respect to that vote.

My previous letters to you reported that in general the government welcomed the proposal, in particular as it reinforced the professional independence of European statistics and the importance of producing statistics in strict accordance with a Code of Practice.

In detail, the government sought i) to amend the proposal to widen the effect of assured professional independence to all producers of European statistics in a Member State, with due recognition of devolved and decentralised arrangements in the UK, ii) to support the adoption of Commitments in Confidence as a way of ensuring the independent production of reliable European Statistics across the EU, while respecting national circumstances, and iii) to obtain clarity about the effect of the changes to the provision for access to administrative data.

The government considers the compromise text achieved in trilogue to have met the first two aims and is satisfied that provisions for access to administrative data, or other areas of the text, do not present a significant issue of subsidiarity

THE ROLE AND PROFESSIONAL INDEPENDENCE OF THE HEAD OF THE NATIONAL STATISTICAL INSTITUTE (NSI)

The latest trilogue compromise text carries forward the improvements achieved in the Council Working Party and reported to your Committee on 18 March.

COMPLIANCE WITH THE EUROPEAN CODE OF PRACTICE AND COMMITMENTS ON CONFIDENCE

The government argued in favour of Commitments on Confidence at the Council’s Working Party meetings. The compromise in trilogue has resulted in obligations for member states to either produce a Commitment in Confidence, or otherwise to demonstrate how full compliance with the Code of Practice is to be achieved. There will be a mandatory report to the EP and the Council on the adoption of Commitments (or alternatives), and this report will be published.

ACCESS TO ADMINISTRATIVE DATA

Further opinion of the HM Treasury Solicitor, advice of the Council Legal Service and the Commission Legal Service have all been obtained. This advice is consistent in indicating that the effect of the change in this proposal is to allow future Regulations for European statistics to specify the use of a particular administrative source of data. Where such a Regulation is made, national rules on the use of that source, which may inhibit access by producers of European statistics would be, in effect, disappplied. There are however a number of safeguards:

- The provision relates to future Regulations for particular European statistics, only,
Where there is no provision for access to a particular administrative source in a future statistics Regulation, the determination of the necessity of access to an administrative source remains, by definition, with the Member State. It is in this aspect only where some transposition into national law may be considered by the government. It is not clear how a UK producer of a European statistic demonstrates the necessity of the use of a particular administrative source of data, nor how the “right of access” to that source is then enabled. The government continues to consider the issues of data sharing in this and in other wider contexts.

The issue was and is a matter of subsidiarity and with the benefit of opinion and advice the government considers the amended proposal to be acceptable. Where a future Regulation for a European statistic is proposed, any element where the use of a particular administrative source of data is specified will be examined on a case by case basis from the perspective of subsidiarity as well as its statistical merits. In the absence of such proposals, the subsidiarity element in access to administrative sources is retained, as this continues to be a matter for the governments of Member States only.

In conclusion, the government considers the compromise trilogue text for the reform of regulation 223/2009 to be acceptable and intends to vote in favour should the matter come before COREPER before the summer recess and is cleared from UK Parliamentary scrutiny. I attach [not printed] a copy of the text from the key articles in the compromise proposal.

The 2014-20 Multi-annual financial framework for the EU has now been agreed. I will be analysing the implications of this in terms of the Regulation on the European statistical programme 2013-2017, also referred to in your report of 26 March, and will be writing to you separately about this matter.

16 July 2013

EURO AREA CRISIS- EVIDENCE SESSION 23 JULY 2013 (UNNUMBERED)

Letter from the Rt. Hon. Greg Clark MP, Financial Secretary, HM Treasury, to the Chairman

I am writing to provide further information on questions that arose in the evidence session on 23 July.

On the Multiannual Financial Framework 2014-20 questions raised by Lord Kerr, on the flexibility within the MFF period and the relationship between payments and commitments, you will find answers to these questions in the Draft Annual Budget 2014 update letter addressed to Lord Boswell dated 5 August.

Similarly, Lord Davies’ statements on flexibility in the Bank Recovery and Resolution Directive were addressed in my separate BRRD update letter dated 27 July.

Regarding the relationship between euro ins and euro outs and whether the latter can influence the former, I refer you to the answer I gave in response to Lord Kerr as part of my evidence.

The Government has been clear that as the euro area proceeds towards closer integration it will be important to ensure that the interests of those not participating are fully taken into account and, in particular, that the single market is fully protected. This is the approach that we are taking in negotiations. There are of course, as I said at my evidence session, sometimes mechanistic consequences that flow from the fact that we do not share the single currency with euro area members, and this can have implications for the negotiating positions of Member States.

However, where that is the case we are alive to that and where necessary have put in place arrangements to protect the single market and prevent the UK being outvoted by a euro area caucus, for example in the negotiations on the Single Supervisory Mechanism.

At the same time, I think it is important to recognise that, typically, the negotiations do not reflect the mechanistic division between ins and outs and that both of these groupings contain a diverse set of
Member States with a diverse set of interests, which do not fall neatly into those groupings. More generally, the UK can continue to be outside the euro and remain influential within the EU, as we are now. We work closely with Member States on the key issues of the day – improving Europe’s competitiveness, the single market, trade, taking tough action in Syria – and euro area members are often our closest allies.

Nevertheless, we are not complacent. The Prime Minister was clear in his Bloomberg Speech in January on the importance of fairness in the EU between its different groupings and the need to protect the interests of those outside the single currency. Any arrangements put in place to address the challenges the euro area faces must work for those outside the euro area as well as those within it. That is something that we will continue to pursue in individual negotiations and as part of the UK’s wider EU Reform agenda.

On the related question of HM Treasury’s engagement with the Eurogroup – and Mr Dijsselbloem in particular – the Chancellor and I meet regularly with all our EU28 Finance Minister colleagues at monthly ECOFIN meetings. ECOFIN meetings take place the day after Eurogroup meetings. The first item at ECOFIN is an informal breakfast discussion, at which there is a readout of Eurogroup from the previous evening, normally made by Mr Dijsselbloem, with contributions from the Commission and the ECB, after the readout there normally follows a wider discussion on all the pertinent EU Economic and Financial issues. In addition we hold periodic bilateral meetings with a number of EU Finance Ministers. As a result of these meetings we have strong working relationships with those both in and out of the Eurogroup.

With regard to the role and success of the European Investment Bank (EIB), the Government believes the UK benefits significantly from the lending activities of the EIB. Over the last five years (2008-2012) it has signed finance contracts worth in the region of €23 billion for UK based projects, representing an important contribution to UK Investment and to economic growth across the economy as a whole.

EIB investments in the UK have ranged from motorways and rail; to water supply and treatment, energy schemes, hospitals, universities, high tech development in industry, as well as support for small and medium sized businesses.

In addition, the European Investment Fund (EIF), the EIB’s venture Capital arm provides a comprehensive range of products (including microfinance, venture capital operations and guarantee facilities) to support financing of SMEs. The UK is one of the principal beneficiaries of EIF investments throughout the EU. The UK Government is a strong supporter & promoter of both EIB and EIF activities in the UK.

5 August 2013

EVALUATION OF THE UNION’S FINANCES (11859/13)

Letter from the Chairman to the Rt. Hon. Greg Clark MP, Financial Secretary, HM Treasury

Thank you for your Explanatory Memorandum, dated 14 July 2013, on EM 11859/13 on a Commission report on the evaluation of the Union’s finances based on the results achieved. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 10 September 2013.

We are grateful for your detailed Explanatory Memorandum, and would like to thank you for taking on board the Committee’s concerns about the standard of EM 16850/12 on last year’s equivalent report. We are pleased to note a marked increase in the standard of the EM.

In consideration of last year’s report, we noted that multiannual programmes should be evaluated at set milestones and against planned results. We welcomed the Commission’s review of the structure and content of the report and hoped that it would lead to improvements. We are therefore pleased to note that the format of the report has been adjusted in response to criticisms and concerns expressed by various bodies including the European Court of Auditors, and that the timing of the production of the report has been brought forward to align better with the adoption of the Synthesis Report of the Commission’s Management Achievements in 2012. We also welcome the reforms set out in the Action Plan for the Development of the Report. You welcome the improvement in this year’s report. Are you content that enough has been done to address the inadequacies highlighted in previous years? If not, what more can be done to make it an effective tool in ensuring the accountability and transparency of the EU Budget?
We note that the document present a mixed picture in terms of the effectiveness of EU spending. Whilst we welcome the Commission’s commitment to ensure that action is taken to improve monitoring, reporting and evaluation are in the next Multiannual Financial Framework period, it remains to be seen if these reforms will be effective. How confident are you that, in the words of the European Parliament, “a new culture of performance” at the Commission will emerge in the coming years?

We would be grateful for a response to these questions by 7 October 2013. In the meantime we are content to clear the document from scrutiny.

10 September 2013

Letter from the Rt. Hon. Greg Clark MP to the Chairman

Thank you for your letter of 10 September 2013, on EM 11859/13: the evaluation of the Union’s finances based on results achieved. I am pleased that you found the detailed explanatory memorandum helpful.

The Government has been clear that improvements are needed to the accountability and transparency of the EU Budget. We share the Committee’s hope that the report’s format will lead to improvements in that fashion, and will be looking to see whether a positive impact is made during future budget cycles. The Government does believe that the steps taken by the Commission in this report are encouraging and indicate that it has started listening to previous criticisms. However, this should not develop into complacency. The Government will continue to press the Commission to improve the quality of its reporting.

The Government notes the European Parliament’s view that a “new culture of performance” at the Commission will emerge in the coming years. This is something the UK and a number of other likeminded Member States have been calling for and would of course be welcomed. The Government notes the view of the Commission that development of a new culture will take several years to come into full effect and will monitor this closely, looking for progressive development overtime.

28 September 2013

FINANCIAL REPORTING AND AUDITING FOR THE PERIOD 2014-2020 (5213/13)

Letter from Jo Swinson MP, Parliamentary Under- Secretary for Employment Relations, Consumer Affairs, Department for Business, Innovation and Skills, to the Chairman

Thank you for your letter in response to the Explanatory Memorandum concerning the proposal for a regulation of the European Parliament and of the Council on establishing a Union programme to support specific activities in the field of financial reporting and auditing for the period 2014-2020. The letter went astray and I am sorry that you have had to wait for a response.

You raise a number of points in relation to the proposal, the institutions concerned and international accounting standards which I address below. Since you wrote the European Commission has appointed a special adviser to review the governance arrangements of EU bodies working in this field. I have provided some information on this, together with details of European Parliament interest in this portfolio.

CRITICISMS OF IFRS

You asked for my response to recent criticisms of IFRS by the Bank of England and the House of Lords and then about the Commission’s response to this criticism.

There is little evidence to suggest that international accounting standards were a significant factor in the financial crisis. However, we recognise that accounting standards need to evolve and respond to emerging issues. The Government is supportive of the International Accounting Standards Board (IASB) which has taken significant steps to improve its accounting standard, IFRS9, for financial instruments in the wake of the financial crisis. The new standard is expected to be finalised before the end of this year but will then be subject to the EU endorsement process before it becomes available for use in the UK. The Commission and the Accounting Regulatory Committee (ARC) is monitoring the standard’s development closely. Through the ARC, the UK is encouraging the Commission and other Member States to support prompt adoption of the revised standard when it becomes available.
Whilst not a direct response to criticism by the Bank of England or the House of Lords, the Commission has announced its decision to conduct a review of IFRS in the EU. In a press release, dated 19 March 2013, the Commission said “it will carry out a review of the regulation on the application of international accounting standards, in order to evaluate the actual effects of 8 years of international accounting standards (IAS/IFRS) in Europe – for instance, have these reached the regulation’s initial objectives of improving the functioning of EU capital market through increased transparency and comparability of financial statements”. Further, Philippe Maystadt has been appointed as Special Adviser to enhance EU’s role in promoting high quality accounting standards. His work “will focus on a review of the governance of EU bodies in the field of financial reporting and accounting (the European Financial Reporting Advisory Group (EFRAG) and the Accounting Regulatory Committee)” with the aim of strengthening the EU’s contribution to advocating global and high quality accounting standards”. A copy of the press release is enclosed with this letter (Annex A) [not printed]. The review is expected to report in November 2013.

PRIORITISATION ON FUNDING

In response to our intention to ask the Commission to explain what consideration had been given to linking funding to its policy priorities you asked for the Government’s views on how funding should be prioritised.

You also ask if such funding should be concentrated on Member States encountering most difficulty in relation to accounting standards.

As noted in the Explanatory Memorandum, we recognise the important roles that the IFRS Foundation, Public Interest Oversight Board (PIOB) and EFRAG fulfil. Our concern was simply whether a blanket increase was appropriate in each case. The EU’s contribution through the Commission to IFRS Foundation and PIOB - the global organisations – was 17% and 22% of their respective budgets for the 2011 fiscal year. The EU’s contribution to EFRAG – the body tasked with providing the Commission with independent technical advice – as a proportion of income is significantly higher. EFRAG received 55% of its cash income for the 2011 fiscal year from the Commission. (This figure reduces to 43% if one includes contributions in kind in the income figure.) This is an increase of 1.3% (1.7%) on the 2010 figures. Importantly the proposal to further increase the funding to EFRAG comes at a time when the Commission’s vision for EFRAG’s role is being questioned by some Member States. (See comments below under the section dealing with presentation of Member State views on international standards.)

This proposal is only concerned with the funding of specific bodies active in the fields of financial reporting and auditing. There is no direct support to individual Member States through this programme. However, there are varying levels of expertise across the EU in this subject area. Smaller member states, especially those without a national standard setter, may look to EFRAG or other national standard setters as a source of information and advice.

PIOB FUNDING

You asked specifically if the Government supports the EU funding of the PIOB.

It is important that there is effective influence by the EU in the international arena and we recognise the financial obligations that membership of bodies at this level brings. As with international accounting standards, it is appropriate that the European perspective influences the development of thinking internationally for auditing standards. Consequently, we are supportive of the Commission’s proposal to continue making a contribution to PIOB.

An extract from PIOB’s website (www.ipiob.org) of key facts concerning the organisation’s history and purpose is enclosed with this letter (Annex B)[not printed].

USE OF DELEGATED POWERS

You posed a number of questions in relation to the Commission’s proposed use of delegated powers to determine whether successor bodies merit continued funding. Specifically you — asked for my views on how such an assessment should be conducted; — requested an update on my consideration of the use of delegated powers and when a conclusion might be reached; and — asked about the views of other Member States on this issue.

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The Government’s preference is to avoid the use of delegated acts as this mechanism removes the opportunity for further Member State scrutiny in the decision making process. Such powers should, in our view, only be used where there is no room for discretion in the use of those powers. This does not appear to be the case in this instance and we do not consider that it should be too arduous to seek Member State agreement in the event it became necessary to consider the transfer of budget cover to another body. Any decision to transfer funding should be based on an assessment of need in the prevailing circumstances and the perceived benefit that would accrue to the EU and its Members from such an investment.

The UK’s opposition to the use of delegated acts was shared with the Commission at the February meeting of the ARC. One other Member State expressed concern at the meeting that, through the use of delegated acts, the Commission would be free to allocate funding to new bodies with similar objectives. We also know some other Member States share our general concern about the use of delegated acts from discussions of other proposals. We will raise a formal objection on this point when the proposal is debated by Council.

PRESENTATION OF MEMBER STATE VIEWS ON INTERNATIONAL STANDARDS

You requested more information on the work and operation of EFRAG, in particular in terms of its basis as a private organisation.

EFRAG is a private sector body, established under Belgian law in 2001 as an international non-profit association. Its objectives are to

“promote the knowledge, the adoption and implementation in Europe of worldwide applicable accounting standards through scientific and pedagogical activities and, in particular:
— to provide a proactive contribution to the work of the International Accounting Standards Board;
— to help developing and coordinating expertise of all stakeholder groups in the area of financial reporting within Europe;
— to contribute to the implementation of International Financial Reporting Standards (IFRS) in Europe.”

EFRAG was established to provide the Commission with technical expertise in financial reporting matters. It is the body which fulfils the function required by recital 10 of the IAS Regulation (1606/2002) which states that “an accounting technical committee should provide support and expertise to the Commission in the assessment of international accounting standards”.

An extract from EFRAG’s website (www.efrag.org) of key facts concerning the organisation’s history, its operating structure and membership is enclosed with this letter (Annex C) [not printed]. A key feature of EFRAG’s structure is the role of EFRAG TEG, its technical expert group, which acts as an independent committee endorsing advice to the Commission and EFRAG’s comment letters to the IASB. Any EFRAG position on international accounting standards must first be considered and approved by the TEG. TEG members are appointed in a personal capacity.

EFRAG has developed its role over time. For example, it has gradually taken on a role of pro-actively influencing the IASB’s standard setting work. In the introduction to its funding proposal, the Commission says “EFRAG will continue to develop means to ensure it becomes the leading platform to for a “single accounting voice of the EU” and to deliver the Union’s input to the IASB” and expresses the view that “it is essential that Europe “speaks with one voice” which is credible and technically sound”. This vision for EFRAG’s future role is not supported by all Member States.

In response to the statement in the Explanatory Memorandum that ARC may be more suited to presenting Member States’ views on standards than EFRAG you ask:
— what benefits do I believe would accrue from the ARC, rather than EFRAG, having the role of presenting Member States views on standards;
— what is the response of the Commission and other Member States to this suggestion;
— for a practical illustration of the sorts of problems you believe would ensue if EFRAG took on this role;
— for examples of problems that have arisen up to now; and
— which other Member States share the UK’s concerns?
The key to the question of why ARC is better suited than EFRAG to this role is accountability. Accounting standards have the potential to impact beyond the financial statements themselves. It is here that the views of Member States are important as one considers their wider social, economic and regulatory implications. Whilst it may be helpful for international bodies such as the IASB and PIOB to have a single point of contact for EU views, it is important that the “one voice” is truly representative of Member States views and that the range of different perspectives is communicated effectively. “One voice” does not mean one opinion. Failure to communicate diversity of opinion may result in poor decision-making.

The needs and interests of the UK, with London a key capital market, may be rather different to those of a smaller Member State whose major companies are less active on the international stage. It is clear from recent exchanges between EFRAG and the national standard setters of the UK, France, Germany and Italy – on issues such as accounting for financial instruments, for example - that positions brought forward by EFRAG are not always fully representative of the range of views expressed by Member States’ financial experts. If we are ever to achieve the goal of a single set of high-quality, global accounting standards then it is clear that the standards cannot be written to meet the needs of any one nation or economic block. Equally it is clear that Member State governments have a duty to ensure that the very real consequences for citizens and national economies are considered in the development of those standards. In our opinion, that is not a function that can be left to an independent third party, no matter how expert its members.

As noted in the Explanatory Memorandum, the UK and other member States have already expressed concern about the legitimacy of EFRAG taking on this role. This topic was debated at the November 2012 meeting of the Economic and Financial Affairs Council (ECOFIN) where the possibility of developing the ARC’s role for this purpose was put to the Commission by Council members. We also have concerns that it is not possible for EFRAG to provide the Commission with genuinely independent advice if it is also seeking to influence the IASB’s future work programme and is directly engaged in the development of the standards on which it is asked to provide advice. Clearly the Commission continues to see a strong role for EFRAG but it may be that Philippe Maystadt’s review makes recommendations about its future relationship with the Commission and other EU bodies.

**Sources of Funding**

You requested further details of the funding arrangements of each of the beneficiaries. In addition, you asked:

— What is the source of their non-EU funding?
— What other sources are being targeted by the IFRS Foundation?
— What is the source of EFRAG’s own resources; and
— You requested an update on PIOB’s efforts to diversify its funding and reinforce its independence vis-à-vis the audit profession.

Sources of funding vary considerably between the bodies. A breakdown of income for each of the beneficiary, for the most recent year available, is included in the appropriate annex B – D [not printed].

The IFRS Foundation was originally financed through voluntary contributions from over 200 organisations but now receives the majority of its funding based on national financing regimes relative to a country’s gross domestic product, GDP. In most cases a levy is applied to companies or there is an element of publicly supported financing. The IFRS Foundation is seeking additional funding for the future, primarily through increases in contributions for existing contributors but it is also seeking to increase the number of contributing countries. (It received contributions from 31 countries in respect of 2012.)

The EFRAG receives cash contributions from three sources - its member organisations; national, GDP-based funding mechanisms; and the Commission (on a co-funding basis to the maximum of an annual grant). EFRAG is seeking to broaden the basis of its national funding mechanisms beyond those already established.

The PIOB receives funding from IFAC and the Commission. In its proposal, the Commission notes its efforts to diversify PIOB’s funding. The Commission comments that several international institutions are expected to provide funds to the PIOB for the 2013 and that “a Task Force has been created to select and convince a group of donors from all over the world to providing funding…on a stable and long-term basis”. At this point, we have no further information about the success of these initiatives.
However, if successful, we level of the EU’s contribution to PIOB’s funding – currently 22% of its income – should fall over time.

INTERRELATIONSHIPS BETWEEN BENEFICIARIES

You asked for further clarification of the work of and interrelationships between the organisations which are the subject of the Commissions’ funding proposal.

There are no direct relationships between the IFRS Foundation, PIOB and EFRAG but each is concerned with promoting and protecting the public interest in the field of financial reporting and assurance. Annexes B, C and D [not printed] provide information on the operations/membership of each of these bodies respectively.

EUROPEAN PARLIAMENT

At the February meeting of the ARC, the European Parliament’s representative indicated that, without pre-empting the Council’s reaction, the proposal was likely to be approved before the end of 2013. However, the European Parliament’s Committee on Economic and Monetary Affairs has now reviewed the proposal and its draft report of 26 March 2012 included a number of possible amendments. These include, amongst others, proposed amendments deleting the provision empowering the Commission to use delegated acts to select new beneficiaries for this funding programme; requiring the Commission to evaluate and report on the International Accounting Standard Regulation 1606/2002 which sets the framework for the adoption of IFRS for use in the EU; requiring the Commission to submit a report on (EFRAG and ARC) governance reforms by March 2014; and requiring the Commission to submit a report on the achievement of the programmes objectives to the European Parliament by June 2019.

I will write again as the impact on the proposal of any recommendations from Philippe Maystadt’s review and the views of the European Parliament become clearer.

28 May 2013

Letter from the Chairman to Jo Swinson MP


We are grateful to you for your thoughtful and detailed response to our questions. We note in particular the Government’s concerns about the evolving role of EFRAG and the use of delegated legislation. How confident are you that your concerns in these areas will be addressed as negotiations progress?

We also note that the European Parliament’s Economic and Monetary Affairs Committee has proposed a number of amendments, and would be grateful for further updates as the Parliament’s position becomes clearer.

We also welcome the appointment of Philippe Maystadt as Special Adviser with responsibility for reviewing the governance of EU bodies in this field. We would be grateful for an update on his work, both before and after the presentation of his final recommendations in November 2013.

We would be grateful for further updates as negotiations progress. Given the controversial nature of elements of the proposal, and given that agreement remains some way off, we will in the meantime continue to hold the document under scrutiny.

11 June 2013

FINANCIAL SERVICES: TRANSPARENCY (16353/11)

Letter from the Rt. Hon. Greg Clark MP, Financial Secretary, HM Treasury, to the Chairman

The European Commission’s proposal amending the Transparency Directive was discussed in Council working groups and a general approach was agreed at the Committee of Permanent Representatives (COREPER) on 30 May 2012. Following the last Trilogue between the Presidency, European
Commission and European Parliament the Irish Presidency is intending to seek agreement to general approach at COREPER at the end of May.

The Presidency compromise, agreed at May 2012 COREPER, was consistent with the position outlined in earlier correspondence with the Committee and as such was supported by the UK along with other Member States at COREPER. In particular, the UK is supportive of high levels of transparency and many of the changes being made reflect the UK’s application of the Transparency Directive. Various clarifications have been made in the Presidency compromise which address UK concerns with the original proposal. These include: Member States continuing to be allowed to set lower national thresholds than those foreseen in the Transparency Directive to ensure appropriate transparency of holdings; and clarifying that the proposal is not intended to affect the UK Takeover Panel’s ability to regulate takeover bids. These have been maintained in Trilogue negotiations.

The European Parliament was particularly interested in a new requirement proposed in revisions to the EU Accounting Directive (COM (2011)684/2) for large companies in the extractives and forestry sectors to disclose the material payments they make to governments. However, the substance of this proposal is being negotiated in the EU Accounting Directive (covered in EM 16250/11) and is only cross-referenced in the Transparency Directive.

For information, during the review process other revisions have been made to Commission’s proposals, including introducing, in the future, a common electronic reporting format with a view to making reporting easier and facilitating accessibility, analysis and comparability of annual financial reports.

I hope that this further information is helpful. The European Parliament is expected to vote on the text at Plenary on 10 June.

21 May 2013

FINANCIAL TRANSACTION TAX (6442/13)

Letter from the Chairman to the Rt. Hon. Greg Clark MP, Financial Secretary, HM Treasury


We are disappointed that you have yet to reply to our letters of 27 March and 24 April 2013, in spite of us requesting a combined response to these as soon as possible, and by 7 May at the latest. Given the serious potential implications of the proposal, we urge you to respond to our letters as soon as possible. We would also take the opportunity to urge you to work closely with other non-participating Member States to ensure that concerns about the potential impact of the proposal not only on the UK but on the EU financial market as a whole are made plain.

14 May 2013

Letter from the Rt. Hon. Greg Clark MP to the Chairman

Thank you for your letter of 24 April, and before that of 26 March, regarding European proposals to implement a financial transaction tax (FTT) through enhanced cooperation, and the Government’s decision to apply to the European Court of Justice (ECJ) for the annulment of the Council authorising decision.

LEGAL CHALLENGE

I would agree that the grounds on which the Government has challenged the authorising decision are all points on which your Committee has previously flagged concerns. I attach [not printed] a paper which sets out more details of the grounds on which we have challenged, including an explanation of our concerns around the “deemed establishment” rule, and the interaction between enhanced cooperation and existing EU agreements on mutual assistance.

The Committee notes concerns about the insertion of an “issuance principle” in the EU Commission’s new proposal for an implementing directive, alongside the original “residence principle”. As you
know, the UK’s transaction tax, Stamp Duty on Shares, is based on an issuance principle. However, we do have concerns that the issuance principle envisaged in the Commission’s proposal is ambiguous. Construed literally, application of the principle as proposed would cover, for example, the conclusion of derivatives contracts between non-FTT zone parties referencing securities issued in the FTT zone, resulting in an extraterritorial effect beyond any reasonable link recognised in international law with the taxing jurisdiction. We have set out these concerns as part of our legal challenge.

In terms of process, the UK’s application to the ECJ does not prevent negotiations on the implementing directive continuing. However, participating Member States will need to be mindful that if the UK maintains and is successful with its challenge, the ECJ would annul the authorising decision and the Commission would need to drop its proposed implementing directive or submit a new authorising proposal.

As I set out in my letter of 19 April, the UK will continue to contribute proactively to Council discussions. We remain hopeful that this process can lead to changes in the design of the tax to address our main concerns and reduce the economic damage of the tax. If negotiations in Council result in a final design which addresses our concerns, we will reconsider our legal challenge.

A summary of our challenge will be published in the Official Journal in the next few weeks. The Council then has two months in which to reply. Beyond this, the timetable is set by the Court. However, on past precedent, the exchange of pleadings would continue until towards the end of the year, with an oral hearing sometime in the New Year. So a judgment might be expected around the middle of next year, if not later.

It is possible that the Court will decide that our application is premature. This will happen if the Court concludes that the implementing directive, once agreed, is the proper target for legal action. In these circumstances, while our case against the authorising decision would be rejected, we will retain the ability to challenge the implementing directive if necessary.

ECONOMIC IMPACTS

The Government continues to share the Committee’s concern that the Commission has not provided satisfactory analysis of the economic impacts on individual Member States, either participating or non-participating. We, along with other Member States (both participating and non-participating) have continued to express our concerns that the Commission has not provided such details.

In addition, we have continued to engage with a wide cross section of market users including corporate issuers, asset managers, banks and trade bodies to improve our understanding of the potential impact the tax on the UK.

Our general view is that while the tax could place the UK’s financial services sector in a better competitive position relative to those businesses in participating countries, it would also carry an array of significant negative impacts. It would increase funding costs for issuers, including UK issuers whose securities are traded by FTT zone counterparties. It would be highly disruptive to the “plumbing” of European financial markets including repo markets and money markets. It risks undermining elements of the G20 regulatory agenda. It implies major challenges for implementation, monitoring and collection which are bound to affect the UK.

In short any benefits that may accrue to the UK from the tax as currently proposed (from relocation of activity for example) need to be factored against these considerable risks. For this reason we cannot support the FTT in the form proposed by the Commission.

While we firmly believe the Commission should have made greater efforts to analyse these impacts before bringing forward the proposal, I should note that I do not anticipate it will be possible to estimate, quantitatively and with certainty, a net figure for the economic impact of the FTT on the UK. The data available is insufficient, the assumptions required are too great, and the adaptive behaviour of markets too unpredictable.

As you may be aware there are now a number of recent published analyses focusing on specific impacts of the tax. You note the analysis produced by London Economics on the impact of the FTT on corporate and sovereign debt. Further recent private sector analyses include those by ICAP (the International Capital Market Association) and others. I would be happy to forward this material if helpful.

In your letters you also noted some specific areas where the FTT may impact, which we would like to reflect on.
In his recent oral evidence to the Committee, Mr Bergmann postulated that only a small minority of SMEs would be affected by the FTT, given that the vast majority do not engage in the type of transactions caught by the tax. However, while most SMEs may not be directly subject to the tax itself, there are likely to be wider impacts. We would expect any increase in the costs of borrowing for financial institutions to be passed through to customers, including SMEs. Additionally, SMEs which have raised finance through securities issuance will be affected, via any impact of the FTT on the secondary markets in these instruments.

You will be aware that in the recent Budget, the Chancellor announced that he was removing the liability for stamp duty on shares on growth markets. This demonstrates the Government’s continued support for SMEs in the UK, and therefore any policy which would have a detrimental impact on SMEs is of course of concern.

As we have communicated repeatedly to both the Commission and other Member States since the first proposal for a FTT was published, we remain unconvinced of the Commission’s assertion that high frequency trading increases volatility in the markets. In fact, there is evidence that points to the contrary, as outlined in the Government’s Foresight project which looked into this, and which you reference in your 26 March letter. Further evidence questioning this assertion has been outlined in numerous academic studies, including the Institute for Development’s review of the evidence for a financial transaction tax published in 2011.

OPERATIONAL ISSUES

Even if the design of the tax were amended to address the UK’s concerns, the Government believes it critically important that the timetable for the introduction of the tax recognises the need to allow sufficient time and discussion to resolve implementation and operational issues. Practical understanding of how this tax would be collected and complied with is needed, and industry would require sufficient time to introduce and/or adapt collection and compliance systems.

In your 19 March letter, you noted a lack of clarity around the obligations on UK authorities to collect the tax, and the possibility that HMRC could be obliged to collect the tax under existing EU agreements on mutual assistance. I have already touched on the fact that one of the grounds for our legal challenge relates to the interaction between enhanced cooperation and existing EU agreements on mutual assistance. I should also add that, at this stage, it is difficult to assess what form these burdens would take in practice, as the monitoring and compliance mechanisms simply have not been developed yet.

POSITION OF OTHER NON-PARTICIPATING EU STATES AND THE US

As part of our engagement strategy, we have sought to identify common ground with other member states, particularly fellow non-participants, and ensure common concerns are recognised as such in Council discussions.

No other member states have currently taken legal action against the authorising decision, though others could request to intervene once the summary of the UK’s challenge is published in the official journal. Luc Frieden, the Luxembourg Finance Minister, has said that he is very sympathetic to the UK’s objections. Several other member states are privately sympathetic.

However, we need to recognise that, as we are the only member state with a major global financial centre, not all other member states will share our level of concern on all aspects of the tax. In addition, many non-participating states do not want to block others from introducing a FTT per se. Ahead of the January ECOFIN, it was clear that a qualified majority of member states were prepared to support the authorising decision, despite the concerns that we and some other member states raised at the time.

While we do not believe a sub-global FTT is a good idea, the Government attaches great importance to the principle of tax sovereignty, and therefore believes other member states should be free to set their own tax policies – provided of course that the Treaty safeguards and existing directives are respected. We also recognise that introduction of a FTT is of great importance to several of the participating member states.

Voting against the authorising proposal, rather than abstaining, could have undermined these messages. It is also worth recognising that, as the decision authorising the use of enhanced cooperation needed the support of a qualified majority of the Council, either an abstention or a vote against had the same effect. Similarly, our abstention did not prejudice our subsequent legal challenge.
You also note the continuing ambition to see a FTT adopted globally. I share the Committee’s view that at present the necessary international consensus does not exist. Indeed, the US administration has recently restated its opposition to such a tax.

US businesses themselves are highly concerned about the EU Commission’s proposal, and Treasury officials have had discussions with non-EU business representatives as part of our ongoing engagement with the industry. It is also clear the US administration is alive to the impact this proposal could have on their financial markets, sharing many of the UK’s concerns. I am sure the Committee is aware of the recent comments by U.S. Treasury Secretary Jack Lew at the House of Representatives Ways and Means Committee, where he noted he had already raised his concerns with European officials about the potential for the FTT to reach into the United States. We will of course discuss the proposal with US officials as appropriate.

OTHER ISSUES

Your 19 March letter also raised questions about the use of the revenues from the FTT. The Commission has proposed that part of receipts generated by the FTT be used as an own resource for the EU Budget. However, these own resources proposal, made under Article 311 TFEU, is separate to the proposal for a FTT implementing directive. As an area of Exclusive Competence, EU Budget issues cannot be taken under Enhanced Cooperation, and instead require agreement of all EU Member States.

At the February European Council, where the 2014-2020 Multiannual Financial Framework (MFF) was agreed by the Heads, Leaders agreed that there will be no new EU-wide taxes to fund the EU Budget in the next MFF period. We retain our right to veto any future proposals to introduce a new Own Resource, including an EU tax.

While participating Member States would be free to hypothecate a share of their FTT revenues to the EU Budget, this must be done at national level. The Government would not object to such national hypothecation, provided the final design of the FTT removed the extra-territorial features we have challenged.

You also asked for further details regarding our concerns that the use of enhanced cooperation does not meet the conditions of subsidiarity. As the Government has stated from the outset, we do not believe a broad-based FTT such as that proposed by the Commission is viable at either national or European level – but rather would need to be agreed globally. Therefore the objectives are not best achieved at EU level, or by a group of EU member states acting together through enhanced cooperation.

More narrowly applied transaction taxes can be successfully implemented at national level, as demonstrated by examples such as UK stamp duty and the taxe sur les transactions financières (TTF) introduced in France last year, both of which are based on an issuance principle. However, as previously stated, the Government does not wish stand in the way of those who wish to introduce a FTT through enhanced cooperation, as long as it does not infringe the UK’s rights under the Treaties.

Finally, you asked about the March European Council. European Council conclusion needs to be agreed by all Member States, and therefore, in this case, between participating Member States who are keen to advance the work, and non-participating Member States including UK. We made clear in discussions that we would not accept language which endorsed the current FTT proposal as an appropriate design on which to proceed. The Prime Minister has been following this dossier closely since the Commission first made their proposal for an EU wide FTT in 2011, and was briefed on the latest position in advance of March’s meeting.

25 May 2013

Letter from the Chairman to the Rt. Hon. Greg Clark MP


We are grateful to you for your letter, and for your recognition that the grounds on which the Government have launched a legal challenge against the decision to authorise use of the Enhanced Cooperation Procedure were all areas on which this Committee had previously raised concerns. We note in particular that the final ground for challenge reflects the arguments that we set out both in our March 2012 report Towards a Financial Transaction Tax?, and in correspondence with you since,
is that “implementation of the enhanced cooperation FTT will inevitably entail costs for non-participating states under Council Directive 2010/24/EU concerning mutual assistance for the recovery of claims relating to taxes, duties and other measures and Council Directive 2011/16/EU on administrative cooperation in the field of taxation.”

However, we remain unconvinced by your argument that it would have been counterproductive for the UK to have voted against the proposal authorising enhanced cooperation. You state that it was clear that a qualified majority were prepared to support the authorising decision. Whilst we recognise your desire to protect the principle of tax sovereignty, it is equally important to defend the interests of the UK financial sector. Given the uncertainty at that stage about what the Commission was going to propose, it would in our view have been appropriate for you to have tested the position of other Member States by seeking a blocking minority as a precautionary measure.

We would also be grateful for your reaction to recent media reports that even those Member States choosing to participate have expressed reservations about the proposal, and that it may be significantly watered down. You state that you remain hopeful that the negotiation process can lead to changes to the design of the tax to address the Government’s main concerns and reduce the economic damage of the tax, and that, if a final design addresses these concerns, the UK will reconsider its legal challenge. In light of concerns expressed both by participating and non-participating Member States, what do you think is the most likely final design of tax that will emerge at the end of the process? Is it reasonable to predict that some form of FTT will emerge, albeit in watered-down form?

You state that, while the tax could provide the UK’s financial services sector with a competitive advantage, it would also carry an array of significant negative effects. However, we do not believe that this provides sufficient clarity of your views. Given the UK’s obligations as an EU Member State, was the Commission wrong to assert, in its evidence to us on 19 March, that the effect on London would be no different to that on non-EU financial centres, such as New York and Hong Kong? Do you share our concern that the negative consequences of an FTT will outweigh any benefits that accrue? Are you concerned that even a watered-down FTT could have detrimental consequences for the UK financial sector, and if so, what will you do to combat this?

We would be grateful for a response to these questions. We would also be grateful for further updates on the UK’s legal challenge, including confirmation of the date on which the summary of the challenge is published in the Official Journal, details of the Council’s reply, and updates as to whether any other Member State chooses to intervene once the summary is published.

We would be grateful for a response to this letter by 19 June 2013. Given the potential ramifications of the proposal, as well as its uncertain prospects, we will continue to hold this document under scrutiny.

5 June 2013

Letter from the Rt. Hon. Greg Clark MP to the Chairman

Thank you for your letter of 5 June regarding European Union proposals to implement a financial transaction tax (FTT) through enhanced cooperation.

You note recent media speculation that participating Member States are considering ways to water down the current proposal. It is correct that Member States have raised concerns over different aspects of the Commission’s proposal, and the design of the tax continues to be discussed at Council working group level. The UK, alongside all participating and non-participating Member States, remains constructively engaged in the debate. However, it is difficult to predict how the design of the tax may evolve as talks progress. While it is highly likely that the final form of the tax will differ from the current proposal, we are still at a relatively early stage of negotiations and it would be premature to try and predict its final shape.

For our part we have been clear during discussions that a narrower tax akin to UK Stamp Duty and the French equivalent, based on the issuance principle and containing suitable exemptions – such as for intermediaries in order to mitigate the ‘cascade’ effect – would pose fewer risks to EU growth and to the Single Market than the proposal currently on the table. We have also been clear that reconsideration of our legal action would necessarily depend on changes regarding the residence basis of the tax being made, and that movement to an issuance principle would represent significant progress in this regard.

You raise another point regarding the potential impact of the FTT on the UK financial services sector compared to other countries’ sectors. While we agree with the Commission that the tax would,
technically, have the same application in New York and Hong Kong, we do expect that the impact of the tax would be more strongly felt in London than in other financial centres, primarily since London is very closely integrated with the EU financial services market. We do share your concern that the negative consequences of the proposed FTT could outweigh any benefits that accrue, but I believe that a significantly narrower tax (along the lines outlined above) would pose significantly lower risks to the UK.

On the UK’s legal challenge, the summary of the challenge was published in the Official Journal on 15 June. The Council has not yet replied but we would be happy to provide you with an update on this as it becomes available, along with subsequent updates on the progress of the case, including whether any other Member States have intervened.

6 July 2013

Letter from the Chairman to the Rt. Hon. Greg Clark MP


We are grateful to you for your response, and for the further clarity you provide on the UK position. We note your view that a narrower tax akin to the UK Stamp Duty, based in the issuance principle and containing exemptions to mitigate the cascade effect, would pose fewer risks to EU growth, the Single Market and to the UK itself, and welcome further updates on the progress of negotiations as to whether the proposal is indeed moving towards such a model.

We are grateful to you for agreeing to write to us again with further updates on the UK’s legal challenge, including the Council’s reply and whether any other Member States intervene. We would be grateful for such an update, as well as an update on the progress of negotiations, by 30 August 2013. In the meantime we will continue to hold the document under scrutiny.

17 July 2013

Letter from the Rt. Hon. Greg Clark MP to the Chairman

Thank you for your letter of 17 July regarding European Union proposals to implement a Financial Transaction Tax (FTT) through enhanced cooperation.

You requested an update on the UK’s legal challenge against the decision authorising a FTT under enhanced cooperation by 30 August. I am pleased to provide this, subject to the need to respect the confidentiality of proceedings in the Court which restricts applicants from disclosing details of other applicants and interveners and their submissions to the Court – although those applicants and interveners may independently release this information if they wish.

The Council, on 2 July, lodged its defence with the Court. The UK on 25 July submitted a brief reply, which focused on matters relating to the timing of the challenge and noted (in line with the UK’s original application) that the UK would be content for the Court to dismiss its application on the grounds of prematurity, should the Court agree that the UK’s ability to challenge any Implementing Directive were preserved.

The deadline for any applications by Member States, or other eligible parties, to intervene in support of either party to the legal challenge – either the UK or the Council – was 6 August. One Member State or other interested party has intervened to support the UK, while six Member States or other interested parties have intervened to support the Council.

With regards to next steps, the Council now has until 9 September to lodge its rejoinder. As parties, the UK and the Council will have the opportunity to submit observations on any statements in intervention which have been lodged by any intervener in the case, but beyond this there would be no opportunity to make further written submissions. The Court will then notify the parties of the close of the written procedure, and there would then be an opportunity for the parties to make a request for an oral hearing.

In terms of the negotiations themselves, there are no major developments to report since our most recent correspondence, and there have been no Council Working Groups since 2 July. Discussions will resume after the summer break, and the next meeting is scheduled for 9 September.

26 August 2013

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Letter from the Chairman to the Rt. Hon. Greg Clark MP


We are grateful for this update, and ask you to write again with any further updates on the legal challenge (including submission of the Council's rejoinder) and on the progress of negotiations, by 1 October 2013.

10 September 2013

Letter from the Rt. Hon. Greg Clark MP to the Chairman

Thank you for your letter of 10 September regarding European Union proposals to implement a Financial Transaction Tax (FTT) through enhanced cooperation.

You requested a further update on the UK's legal challenge against the decision authorising enhanced cooperation in the area of a FTT. The Council lodged its Rejoinder on 9 September. The Court has given the parties who have intervened in the case a month to submit their statements (we anticipate their deadline falls in late October). Following the lodging of the statements in intervention, the UK and Council will then be given the opportunity to respond to those statements, after which the written procedure will be closed. The timetable of the subsequent steps will be determined by the Court.

With regards to the progress of negotiations, since our last correspondence there has been one further Council Working Group – on 9 September. During this meeting, the first technical read-through of the proposal was completed. At this time, the Presidency has not scheduled any further Working Groups, nor given any indication that this will be brought back to ECOFIN before the end of the year.

You will be aware from news reports that the Council Legal Service issued an opinion regarding the legality of the ‘deemed establishment’ principle. This opinion, which was widely leaked, endorsed some of the main aspects of the UK's legal challenge, and made certain additional points. While the opinion is generally favourable to the UK position, it is non-binding. There has not yet been a formal discussion of it by Member States.

27 September 2013

GREEN PAPER: LONG-TERM FINANCING OF THE EUROPEAN ECONOMY (8398/13)

Letter from the Chairman to the Rt. Hon. Greg Clark MP, Financial Secretary, HM Treasury

Thank you for your Explanatory Memorandum, dated 6 May 2013, on EM 8398/13 on a Green Paper on Long-Term Financing of the European Economy. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 4 June 2013.

We were intrigued by your comment that some of the policies outlined in the Green Paper had been devised for various purposes, of which their capacity to support long term investment may be one, but not always the primary one. We would be interested to learn more about this: specifically, which policies are you referring to and what other motive are you implying there might be?

We would like to note that a number of key commentators have pointed out the huge opportunity that diversifying sources of long-term finance could present for the City of London, since building up Europe’s capital markets would mean greater business being routed through London. You state that there is a strong case to diversify sources of long-term financing of the economy but what do you plan to do to push this agenda forward? To what extent are you, and the Commission, working with institutional investors to identify opportunities and solutions to any obstacles that arise?

We would be grateful for a response to these questions by 1 July. In the meantime we are content to clear this document from scrutiny.

4 June 2013
Dear Chairman,

Thank you for your letter of 4 June granting clearance from scrutiny for the European Commission Green Paper on Long-Term financing of the European economy.

I attach [not printed] here for your information the Government’s response to the green paper which we have just submitted to the European Commission. I hope the response itself serves to answer the questions raised in your letter, and I agree that this agenda provides an important opportunity for the City of London to facilitate the deepening and strengthening of capital markets, bringing more business to the UK. I would bring to your attention the introduction to our response where the Government sets out the key areas where we see most scope for further activity to support the important long-term investment agenda, including by diversifying sources of funding. These include:

— Supporting institutional investors, including through trying to develop a private placements market, both nationally and across Europe. These have the potential to provide an alternative to bank lending and public bond issuance, potentially broadening the availability of finance and with beneficial characteristics for issuers and investors. Additionally, the Government has stressed the need to ensure EU legislation actively supports, rather than penalises, long-term investment by institutional investors – particularly insurers and pension funds. This means, for example, that there is a market consistent, risk-based approach in Solvency II for insurance. We also welcome the decision of the Commission not to apply a Solvency II-type prudential capital regime to occupational pensions, in recognition of the negative impact this is likely to have on their willingness to invest in the real economy.

— Supporting innovation in the securitisation markets and getting them working effectively again. This includes addressing the barriers to effective securitisation markets in Europe, most important of which is the penal regulatory treatment of securitisation compared with other asset classes such as covered bonds. Additionally it would be helpful to explore ways to generate effective securitisation instruments for SMEs, which also needs to start by addressing the current barriers which include a shortage of investor appetite for these instruments, partly due to a lack of data on SME loan performance.

— More generally our focus is on ensuring SMEs have better access to funding, including access to capital markets, as deep capital markets, where companies come to raise money, are an important alternative source of finance. Ensuring small and growing companies can access capital markets is an important component, and essential in supporting sustainable long-term growth in the EU.

Please let me know if you need any further information.

6 July 2013

HARMONISED PUBLIC SECTOR ACCOUNTING STANDARDS (7677/13)

Dear Rt. Hon. Greg Clark MP,

Thank you for your letter of 4 June granting clearance from scrutiny for the European Commission Green Paper on Long-Term financing of the European economy.

I attach [not printed] here for your information the Government’s response to the green paper which we have just submitted to the European Commission. I hope the response itself serves to answer the questions raised in your letter, and I agree that this agenda provides an important opportunity for the City of London to facilitate the deepening and strengthening of capital markets, bringing more business to the UK. I would bring to your attention the introduction to our response where the Government sets out the key areas where we see most scope for further activity to support the important long-term investment agenda, including by diversifying sources of funding. These include:

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— More generally our focus is on ensuring SMEs have better access to funding, including access to capital markets, as deep capital markets, where companies come to raise money, are an important alternative source of finance. Ensuring small and growing companies can access capital markets is an important component, and essential in supporting sustainable long-term growth in the EU.

Please let me know if you need any further information.

6 July 2013

HARMONISED PUBLIC SECTOR ACCOUNTING STANDARDS (7677/13)

Dear Chairman,

Thank you for your Explanatory Memorandum 7677/13, dated 11 April, on a Commission report entitled Towards Implementing Harmonised Public Sector Accounting Standards in member States – the suitability of IPSAS for the Member States. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 14 May 2013.

Like you, we support the use of accrual accounting by public sector entities, and therefore welcome the Commission’s efforts to move towards a system of harmonised accrual accounting standards across the EU. We also welcome the Government’s commitment to play an active role in assisting the Commission in developing its proposals. However, we observe that concern was expressed about the adoption of IFRS in the private sector, not least by Germany and France, and some concern was expressed about the impact of IFRS in relation to the banking crisis. In light of this, how do you account for the apparent general support for International Public Sector Accounting Standards (IPSAS) across Member States? How would you characterise the relationship between IFRS and
IPSAS? To what extent do they reflect each other, or are there any significant differences? Are there any weaknesses in IPSAS that justify moving towards a set of European Public Sector Accounting Standards (EPSAS)?

You state that the European System of Accounts that provides the macro-level statistical accounting framework for the government and non-government sectors in the EU is accruals based. What is your assessment of the use of accrual accounting by the Commission itself? Is the Commission itself compliant with IPSAS?

We note the view of both the Commission and the Government that further work is needed before such a harmonised system can be implemented. In that regard, we would be grateful for clarification of a number of points.

You state that the legislative basis for introducing EPSAS remains to be determined. What are your views on the most appropriate legislative basis for the introduction of EPSAS? You also refer to the need to determine the “conceptual framework” that will underpin the standards. What do you mean by this? What principles do you believe should underpin the governance arrangements to be put in place?

You state that the UK is over 90% compliant with IPSAS. How does that compliance rate compare to other Member States? What more needs to be done to achieve full compliance? Do you share the concerns, expressed in the Commission report, that “IPSAS cannot easily be implemented in EU Member States as it stands currently”? What in your view are the biggest obstacles to full compliance, both in relation to the UK and in relation to all Member states? You state that the Government would want to “retain commonality with the accounting standards used in the UK private sector”? Do you have any specific concerns in mind? How can equivalence in accounting standards be delivered? Is there any case for extending IPSAS provision to the private sector?

We would be grateful for a response to these questions by 17 June 2013. In the meantime we are content to clear the document from scrutiny.

14 May 2013

Letter from the Rt. Hon. Danny Alexander MP to the Chairman

Thank you for your letter of 14 May on the Explanatory Memorandum 7677/13: Harmonised Public Sector Accounting Standards that was considered by the House of Lords European Union Sub-Committee on Economic and Financial Affairs.

I am pleased you support both the use of accrual accounting by public sector entities and the Government's commitment to play an active role in assisting the Commission in developing its proposals to implement harmonised accrual accounting standards across the EU. Your letter asked a number of questions which I respond to below.

Support for IPSAS, Differences with IFRS, and the Need for EPSAS

— IPSAS have been developed from IFRS, with IFRS being adapted to meet the public sector context. The International Public Sector Accounting Standards Board (IPSASB) has a memorandum of understanding with the International Accounting Standards Board (IASB) which seeks to ensure that the standards are complimentary and that differences only exist where necessary due to specific features of the public sector and the needs of users of public sector accounts.

— IFRS and IPSAS to a large degree do therefore reflect each other, but there are a number of standards in each suite that do not have direct equivalents. For example there are IPSASs that require disclosure of financial information about the general government sector and the presentation of budget information in financial statements that are not relevant for private sector entities or users of private sector accounts so have no IFRS equivalents.

— Support for IPSAS across Member States is mixed. Many welcome IPSAS as an internationally recognised set of accrual accounting standards designed specifically for the public sector, but some Member States continue to use cash accounting, and others have concerns as set out in the Commission's Report. Despite these concerns there is general support for IPSAS as a reference point in developing harmonised European Public Sector
Accounting Standards (EPSAS). This is important, as utilising internationally recognised standards ensures that accounts are prepared in accordance with generally accepted accounting practice and that users of accounts can be sure that there has not been manipulation of standards for political or other gain.

There are some current weaknesses in IPSAS which have been cited as requiring the development of EPSAS. These specifically relate to (i) the Conceptual Framework on which IPSAS are based which is not yet complete, (ii) the governance arrangements for the development of IPSAS which is felt to suffer from insufficient participation of EU public sector accounting authorities, and (iii) that the suite of standards are insufficiently prescriptive and do not cover all public sector specific issues, with a major gap being accounting for social benefits.

While recognising the concerns raised by some Member States, particularly in regard to governance arrangements, the UK does not fully share them. According to the Commission’s Report the UK is 93% compliant with IPSAS, a higher compliance rate than any other Member State, and that is because the UK public sector takes a similar approach in the development of its accounting standards for the public sector, by using IFRS as its base.

**Accrual Accounting by the European Commission**

The European Commission, along with all other European Union Institutions, utilises accrual accounting standards for its own financial reporting. These standards are based on IPSAS and are applicable to all entities consolidated into the European Union’s annual accounts. These accounts are externally audited by the European Court of Auditors, and the most recent set that have been fully audited (financial year ending 31 December 2011) have been given a "presents fairly" opinion, meaning that the accounting rules were properly followed.

**Legislative Basis, Conceptual Framework and Governance**

The legislative basis for the introduction of EPSAS has yet to be determined. When IFRS were introduced as the required reporting standards for EU listed companies, it was via a regulation that supplemented earlier directives providing the legal framework for financial reporting by companies. Given the aim is to require all public sector entities in the EU to apply EPSAS, it is likely that a regulation rather than a directive would be required to prevent differences in implementation between Member States. We will examine any legislative proposals carefully as they emerge. In the short term it is possible that the Commission will issue an opinion on how the introduction of EPSAS can contribute to improving the quality of the statistical data on which fiscal policies are made.

I indicated that there was a need to determine the conceptual framework that will underpin EPSAS and also the governance arrangements that will have to be put in place and you asked what I meant by this. A conceptual framework sets out the principles that underlie the preparation and presentation of financial statements. It defines and explains accounting concepts like assets and expenses which are crucial for the creation of accounting standards. Without a conceptual framework accounting standards could develop in an inconsistent manner, undermining the value of financial statements. IPSASB has been working on its conceptual framework for almost seven years, so this is not an easy task.

With regard to governance, the most important issue once the legislative basis of EPSAS has been determined is the structure and powers of the standard setting body that would be required. The main principles that should guide this are:
— The need to include preparers, auditors and Eurostat as members of the body. It should also include some private sector experience to provide challenge;

— The need for the body to be proactive and take an influencing role in standard development, so that EPSAS can use as far as possible IPSAS;

— The body will have to ensure that differences in accountability, regulatory, governance and other financial management frameworks of Member States are addressed; and

— It should aim to minimise divergences between EPSAS and the European System of Accounts which underpins statistical reporting (i.e. The National Accounts from which fiscal measures are derived).

IMPLEMENTATION OF HARMONISED ACCOUNTING STANDARDS

— Implementing IPSAS or EPSAS will be challenging, as the starting point in each Member State is fundamentally different. Implementation will potentially involve significant cost, time and cultural change. Given the advanced state of accrual accounting in the UK public sector, the UK’s main concern would be that any set of harmonised standards would lead to a reduction in the quality and robustness of financial reporting by public sector entities.

— As noted, the UK compares very favourably with other Member States in terms of its level of compliance with IPSAS, although full compliance with IPSAS is not an objective of the Government, as IFRS is the framework adopted across the UK Public Sector. We would be concerned if EPSAS led to a set of standards that were fundamentally incompatible with IFRS. This is because whether within the private or public sector all entities operate within the same economy and the same economic events should be accounted for in the same manner, although due regard does of course need to be given to the different needs of users of financial statements of private and public sector entities. This is why there is no case for extending IPSAS provision to the private sector, as IFRS and private sector accounts are focussed primarily on the information needs of investors whereas IPSAS and public sector accounts are focussed on the needs of taxpayers and other resource providers and their representatives.

17 June 2013

Letter from the Chairman to the Rt. Hon. Danny Alexander MP

Thank you for your letter, dated 17 June 2013, on EM 7677/13, on a Commission report entitled Towards Implementing Harmonised Public Sector Accounting Standards in Member States – the suitability of IPSAS for the Member States. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 25 June 2013.

We are grateful to you for your helpful and informative response to our letter of 14 May 2013. However, there is one point on which we would like to request further clarification. We are pleased to note that the UK has a higher compliance rate with IPSAS than any other Member State, at 93%. You also state that full compliance is not an objective of the Government, as IFRS is the framework adopted across the UK public sector. Yet you also state that there is an effort to ensure that IPSAS and IFRS are complimentary and that differences only exist where necessary due to specific features of the public sector and the needs of public sector accounts. The differences you cite are standards contained in IPSAS that apply to the general government sector but are not relevant for private sector entities, and therefore have no IFRS equivalents. In light of this, why has IFRS rather than IPSAS been used as the framework across the UK public sector? In which specific areas of IPSAS is the UK not compliant, and what is the consequence of this? We would be grateful if this information could be provided in tabular form. Is there any sense in which the adoption of IPSAS rather than IFRS as the framework across the UK public sector would constitute a dilution of accounting standards? If not, why are the Government not seeking 100% compliance?

We would be grateful for a response to these questions by 23 July 2013.

26 June 2013
Letter from the Rt. Hon. Danny Alexander MP to the Chairman

Thank you for your letter of 26 June relating to the Explanatory Memorandum 7677/13: Harmonised Public Sector Accounting Standards that was considered by the House of Lords European Union Sub-Committee on Economic and Financial Affairs.

— I am pleased to provide this response to your query regarding the application of International Financial Reporting Standards (IFRS, including the International Accounting Standards or IASs) in the UK public sector, rather than International Public Sector Accounting Standards (IPSAS).

Adoption of IFRS by the UK Public Sector

— Accrual accounting in the UK public sector has a long history in local government but was first introduced into central government under the Government Resources and Accounts Act 2000 (the Act). The Act, unless the Treasury directs them otherwise, requires all central government bodies to account in accordance with Generally Accepted Accounting Practice (GAAP). At the time of the Act, GAAP was taken to be UK GAAP which comprised the accounting standards issued by the Accounting Standards Board. These standards were followed by private sector entities in the UK reporting under the Companies Act.

— From 2005 the reporting framework for listed companies in the UK changed following an EU directive that required the application of IFRS.

— As a consequence, the decision was made to adopt IFRS within the public sector, with central government and health sector bodies adopting IFRS for the 2009-10 financial year and local government adopting for the 2010-11 financial year. As noted in my explanatory memorandum the adoption of IFRS was undertaken to allow the public sector to be measured consistently with significant private sector entities.

Non-Adoption of IPSAS

— While the decision to adopt IFRS over IPSAS was primarily to ensure consistent measurement with the private sector, it also reflected a number of significant weaknesses with IPSAS. IPSAS did not constitute a complete suite of standards, did not have a stable and mature conceptual framework and was not adequately resourced to meet accounting developments, nor did it have appropriate governance arrangements. Instead IPSAS are used as a reference where IFRS is silent on public sector issues, such as non-exchange transactions.

— Since 2007, when the decision was made to adopt IFRS, the IPSASB has matured significantly, but as noted in my explanatory memorandum a number of concerns remain. For example, the conceptual framework that is being developed to underpin IPSAS will not be completed until at least 2014, and without a stable conceptual framework upon which standards can be developed and interpretations made, the adoption of IPSAS rather than IFRS would constitute a dilution of accounting standards. It is possible that the completed IPSAS conceptual framework may also lead to standards being developed that prevent consistent measurement across the whole economy.

Specific Areas of IPSAS Where the UK is Not Compliant

— There are a number of areas where following IFRS leads to minor divergences with IPSAS. For example a difference in the basis of discount rates used for measuring defined benefit pension schemes. Also, there are instances where IPSAS has not been updated to reflect recent changes in IFRS standards, but there is an intention to do so.

— There are three main areas of non-compliance. The first relates to the boundary for consolidating entities into the public sector. Boundaries are set by the Treasury in accordance with the Government Resource and Accounts Act (GRAA) 2000. Treasury bases the boundary on classification of bodies...
to the public sector by the Office of National Statistics (ONS). This enables accounts based data to complement other fiscal data and provide a clear line of sight across government spending. The second and third areas are disclosures of financial information about General Government and presentation of budget information in Financial Statements. Consolidated statements for the UK Public Sector are on a whole of government basis, and no separate statements are produced for General Government. General Government disclosures are therefore not appropriate. As regard budget information, specific UK guidance is issued to support the budget management structure. These structures vary within the public sector and cannot be aggregated. Accordingly this is not reported at an aggregated level. I have included in Annex [not printed] two tables that provide (i) an overview of those IPSAS where there is specific non-compliance and the reason why, and (ii) an overview of those IPSAS where there are minor divergences from the standard and the reason why. An overview of the application of IFRS in central government reporting can be found in the Financial Reporting Advisory Board (FRAB) annual report, last published in May 2013.

18 July 2013

Letter from the Chairman to the Rt. Hon. Danny Alexander MP

Thank you for your letter, dated 18 July 2013, on EM 7677/13: a Commission report entitled Towards Implementing Harmonised Public Sector Accounting Standards in Member States – the suitability of IPSAS for the Member States. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 30 July 2013.

We wish to thank you for your commendably detailed reply, which we believe provides a model for the sort of response from Government departments that we expect to receive in relation to our scrutiny of EU documents.

30 July 2013

INDICES USED AS BENCHMARKS IN FINANCIAL INSTRUMENTS AND FINANCIAL CONTRACTS (13985/13)

Letter from the Chairman to Sajid Javid MP, Financial Secretary, HM Treasury

Thank you for your Explanatory Memorandum, dated 14 October 2013, on EM 13985/13: Proposal for a regulation on indices used as benchmarks in financial instruments and financial contracts. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 29 October 2013.

We note that you raise concerns relating to subsidiarity. On the one hand you state that action in relation to benchmarks can be more effectively taken at national level but on the other you state that benchmark reform is an international issue given the use of many benchmarks across borders. Can you clarify at what level you think it is best to legislate in relation to benchmarks? Does it depend on the type of benchmark, for instance if it were to operate across borders? If so, we would welcome more detail on which types of benchmarks you believe should be dealt with at national level and which are best dealt with at international level.

We recognise your point that this proposal is very far-reaching and believe that it might be in breach of the principle of proportionality. Can you provide clarity as to the number of benchmarks that will be covered by this proposal? We would be interested to know your views on how best to reduce the scope of this proposal during negotiations? For example, would it make sense for the coverage to be limited to critical benchmarks? Is there an argument for the proposal to take the form of a directive rather than a regulation?

Overall, we would welcome clarity on the Government’s position: both on the proposal itself, and in particular whether you will be minded to support it in Council; and also as to whether, following further consideration, you believe this proposal is in breach of the principle of subsidiarity or the principle of proportionality. In addition, what specific changes do you propose to make to this dossier during negotiations?
We are aware that, in early drafts of this proposal, there were plans to put the LIBOR lending rate under the direct control of the European Securities and Markets Authority (ESMA) in Paris. We understand these plans were dropped due to pressure from the UK Government. Can you provide further details on this? Are you now happy with the proposed role for ESMA, particularly in relation to its role as binding mediator?

We note your concern relating to the appropriate use of delegated acts and we would welcome updates on this as the text evolves. We would also appreciate more general updates as negotiations proceed. How likely is it that agreement will be reached before the European Parliament elections in May 2014?

In order to allow us to consider your concerns about subsidiarity in good time before the Reasoned Opinion deadline, we would be grateful for a swift response to this letter, by 7 November 2013. In the meantime we will continue to retain this document under scrutiny.

29 October 2013

Letter from Sajid Javid MP to the Chairman

Thank you for your letter of 29 October in response to the Government’s Explanatory Memorandum on EM 13985/13: Commission proposal for a regulation on indices used as benchmarks in financial instruments and financial contracts.

The Government believes that there is scope for action at an EU-wide level in relation to some benchmarks subject to various factors. These would include issues such as the geographical spread of contributors or the potential impact of the failure of those benchmarks across different Member States.

After further consideration I consider that this proposal does not comply with the principle of subsidiarity under Article 5(3) of the TEU. This proposal, which is so broad in its application, is not necessary and does not address a common issue in all Member States, rather it seeks to regulate the production and use of benchmarks which is so varied in nature that a harmonised solution, of such broad application, would be harmful. The measures would impose new burdens on administrators, contributors, regulators and others, with very limited regard for the nature of the relevant benchmark. Some benchmarks may cease to be produced, and the proposal might discourage new benchmarks being produced. Furthermore, for the vast majority of benchmarks, actions by Member States alone would not conflict with or hamper the objectives of the proposed action. Action at national level would allow each relevant Member State to address the particular problems associated with specific benchmarks and the benchmark-setting process in its jurisdiction.

In particular, the Government strongly objects, including on the ground of subsidiarity, to the inclusion of benchmarks produced by national statistics authorities. Such authorities are independent producers of official statistics relating to the economy, population and society at national, regional and local levels. Their special features, and the role they play, mean it is not appropriate for them to require authorisation, and to be supervised, in the manner proposed by the Commission. The Government will continue to argue robustly for the removal of national statistics authorities from the scope of the legislation.

You asked the Government to provide clarity as to the number of benchmarks covered by the proposal. It is currently unclear how many benchmarks would be captured by this proposal. Given the broad scope, which captures any published index referenced in a financial instrument, financial contract or investment fund, and following discussions with market participants, we estimate the number of benchmarks captured could potentially number in the tens of thousands, if not more.

The Government is a strong proponent of benchmark reform having taken action domestically to reform LIBOR and playing an active part in the work of the International Organization of Securities Commissions (IOSCO) in developing its Principles for financial benchmarks. The Government supports action at the European level in this area, however that action must be appropriately targeted in order for it to be effective.

As you identify in your letter, it appears the Commission had at one stage placed responsibility for the supervision of critical benchmarks (‘critical benchmark’ means a benchmark, the majority of contributors to which are supervised entities and that reference financial instruments having a notional value of at least 500 billion euro) with the European Securities and Markets Authority (ESMA). This would have captured LIBOR as well as other benchmarks. Upon further consideration, the Commission decided to change this and other provisions, and supervision of all benchmarks now lies with the home competent authority of the administrator. In the case of LIBOR, that will be the
FCA. The Government welcomes this change and firmly believes that the home competent authority is best placed to supervise benchmark administrators. The Government recognises that authorities from around the EU have an interest in the functioning of critical benchmarks, but it is important that the pre-eminent role of the home competent authority is not undermined.

With regard to the timetable for agreement, the Government believes that whilst it is likely that the European Parliament will agree a text ahead of the European Parliament elections in May 2014, it is unlikely that a final agreement will be reached between them and Council before that date.

Negotiations have yet to commence in Council. As negotiations progress, the Government will continue to pursue effective benchmark reform.

7 November 2013

KEY INFORMATION DOCUMENTS FOR INVESTMENT PRODUCTS (12402/12)

Letter from Sajid Javid MP, Economic Secretary, HM Treasury, to the Chairman

I am writing to update you on the progress of the European Commission’s proposal for a Regulation on Key Information for Investment Products, also known as Packaged Retail Investment Products or PRIIPs.

Negotiations were effectively on hold for the first four months of the Irish Presidency while they focused on higher priority files. Discussions resumed in April and a general approach was agreed at the Committee of Permanent Representatives (COREPER) on 26 June.

The Presidency compromise was consistent with the position outlined in earlier correspondence with the Committee and as such was supported by the UK along with other Member States at COREPER. Pensions were excluded from scope and the proposals for Alternative Dispute Resolution deleted.

During the final two months of negotiations there were also improvements the format and content of the Key Information Document.

The European Parliament is expected to finalise its position in October.

5 July 2013

LATVIA’S ADOPTION OF THE EURO (10713/13, 10715/12, 11075/13)

Letter from the Chairman to the Rt. Hon. Greg Clark MP, Financial Secretary, HM Treasury

Thank you for your Explanatory Memorandum, dated 27 June 2013, on EMs 10713/13, 10715/13 and 11075/13 which relate to Latvia’s adoption of the euro. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered these documents at its meeting on 9 July 2013.

Notwithstanding the fact that the UK does not have a vote on this proposal, we are surprised that you did not provide any indication of the Government’s position on these documents, particularly on the ECB’s convergence report. Whilst we commend the progress Latvia has made, this report highlighted some significant economic issues relating to Latvia’s adoption of the single currency. Inflation is unlikely to remain as low as it has been and the ECB also alludes to the Cypriot banking crisis when it discusses the reliance by a significant part of Latvia’s banking sector on non-resident deposits as a source of funding. What analysis have the UK Government undertaken to assess the implications of Latvia’s adoption of the euro? In light of the ongoing euro area crisis, what is the Government’s view of the continued expansion of the euro area?

We are content to clear these documents from scrutiny but would welcome a response to this letter by 24 July 2013.

9 July 2013

Letter from the Rt. Hon. Greg Clark MP to the Chairman

Thank you for your letter of 9 July 2013 regarding Latvia’s adoption of the euro.
The Government’s view is that the issue of whether to seek membership of the euro area is for each Member State – notwithstanding Treaty provisions that mean all Member States, the UK and Denmark aside, are expected to do so in time. Further, decisions on membership are for the euro area itself and I do not believe it would be appropriate for the UK to comment on this.

You refer to risks around inflation and the reliance on non-resident deposits by the banking sector. With regard to the former, I would note that this is a challenge common to any country joining the Economic and Monetary Union, with interest rates set by the ECB for the euro area as a whole. However, as Latvia’s currency has been pegged to the euro since 2005, its economy has been effectively tied to euro area monetary policy for eight years, and indeed 90% of mortgage lending in the country is denominated in euro. With regard to the banks, I would note that whilst rising non-resident deposits are a source of vulnerability for the banking sector, it does not necessarily point towards distress. In addition, the relative size of Latvia’s banking sector (total assets equal to 135% of GDP in 2012) is a fraction of that in Cyprus (950%) and significantly smaller than the average for the euro area (370%).

19 July 2013

MARKET ABUSE (13023/12, 13037/12, 16000/11, 16010/11)

Letter from the Rt. Hon. Greg Clark MP, Financial Secretary, HM Treasury, to the Chairman

I am writing to provide an update on the broader negotiations of the Market Abuse Regulation (MAR) and the Criminal Sanctions Market Abuse Directive (CSMAD).

The Irish Presidency took forward MAR trialogues and reached an agreement at COREPER on 26 June 2013. The UK is satisfied with this agreed text. The Commission’s proposal, which was a constructive starting point, has been improved in several areas - the powers for Competent Authorities have been maintained; the offences are much broader in scope (now encompassing, for example, tips on the basis of inside information and benchmark manipulation); and legal certainty has been enhanced.

More specifically, the MAR text maintains the basic levels of harmonisation and specifies that sanctions apply to both actual and attempted market abuse. These provisions are consistent with the UK’s sanctioning regime and do not adversely affect the capacity of the FCA to impose robust penalties against misconduct.

The Irish Presidency focused on MAR and did not take CSMAD trialogues forward. It is likely that the Lithuanian Presidency will commence trialogues for CSMAD in the second half of 2013. The UK will conduct an assessment of whether to opt-in to CSMAD, once agreement has been reached.

I trust that this further information is helpful to the Committee.

14 July 2013

MiFID II (15938/11, 15939/11)

Letter from the Rt. Hon. Greg Clark MP, Financial Secretary, HM Treasury, to the Chairman

I am writing to update you on the progress of the European Commission’s proposal for a review of the Markets in Financial Instruments Directive (MiFID II). The proposals have been discussed extensively in Council working groups and a general approach was agreed at the Committee of Permanent Representatives (COREPER) on 17 June.

The Presidency compromise, agreed at June 2013 COREPER, was consistent with the position outlined in earlier correspondence with the Committee and as such was supported by the UK along with other Member States at COREPER.

We expect Trilogues to commence in July under the Lithuanian Presidency. In previous correspondence I outlined the European Parliament’s position on the various issues, which in some cases is different from Council’s. We are therefore currently preparing for a second round of negotiations, which we expect to last until the end of the year or possibly longer.
Letter from the Chairman to the Rt. Hon. Greg Clark MP

I am writing in response to your letter, dated 30 June 2013, on EMs 15938/11 & 15939/11: MiFID II. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 9 July 2013.

We are surprised by the brevity of your letter. You state that the Presidency compromise was consistent with the position outlined in earlier correspondence. Yet given how fraught negotiations have been over the past two-and-a-half years, we would have expected a fuller account of the nature of the deal that was agreed. What parts of the deal reflected the UK’s position? What compromises was it necessary for the UK to make in order to reach agreement?

We are particularly surprised that your letter makes no reference to the reported inclusion of a clause stipulating that no proposal or policy from any regulator, or from the European Securities and Markets Authority (ESMA), should “directly or indirectly, discriminate against any member state or group of member states as a venue for the provision of investment services and activities in any currency.” Why did you not refer to this in your letter? Do you not think that the addition of this clause is something that should have been brought to the Committee’s attention? Although we welcome this addition, it does reflect what is already in the Treaties. In light of this, what extra protection do you believe it will provide? Is there any danger of unintended consequences in terms of an inference from the absence of a provision in one piece of legislation when a similar provision has been included in another? We would be grateful for a full account of the inclusion of this clause and a response to our questions.

There were also reports about a cap on the volume of trading in dark pools in the EU, and we understand from media reports that there remain sticking points with regard to access to clearing houses and the scope of organised trading facilities. What update can you give us on the outcome of negotiations in these areas? What was the nature of agreement on third country provisions, and was it satisfactory from a UK point of view?

In light of this we expect to receive a full account of the outcome of deliberations, both on these specific issues and on the agreement as a whole, by 23 July 2013.

9 July 2013

Letter from the Rt. Hon. Greg Clark MP to the Chairman

Thank you for your letter, dated 9 July, on EMs 15938/11 & 15939/11: MiFID II. I provide further information below on the specific questions you have raised.

THE COMPROMISE REACHED AT GENERAL APPROACH

As you know, MiFID II is a technical piece of legislation that covers a wide range of investment services and activities, meaning that negotiations in Council were necessarily extensive. Ultimately the multiple rounds of negotiations have, across all areas, resulted in a compromise that we are content with. In trilogues we will continue to argue for the position outlined in earlier correspondence with the Committee.

Final negotiations in Council were focussed particularly on open access provisions and market structure issues, as set out in the relevant sections below. A number of other issues, such as the third country provisions, had been resolved at an earlier stage of negotiations. I can confirm that the UK objectives in these areas were also met.

TRANSPARENCY IN THE EQUITY MARKETS

Transparency for equity markets proved to be a particularly intensive, technical area of negotiation. The debate focussed on how excessive use of waivers from transparency rules might harm the process of price discovery in equity markets. There was intense pressure from several Member States to remove some or all of the waivers entirely. However, we believed that such a solution would harm end investors’ ability to get best execution in the markets. After lengthy negotiations, we achieved our preferred outcome of retaining all four waivers with an agreement to cap the usage of two of the waivers (the reference price waiver and the negotiated trade waiver).
A number of Member States were strongly opposed to the open access regime for trading venues and central counterparties (CCPs) and wanted to delete the provisions entirely. The main concern of these Member States was that the open access provisions could result in risks to critical market infrastructures. While the Government has always believed that the Commission’s proposal gave sufficient powers to supervisors to be able to prevent such risks from arising, we worked constructively with these Member States to include specific measures that would address these concerns. Notwithstanding these safeguards, the Council compromise broadly maintains all the key elements of the Commission’s proposal on access, and the UK is satisfied that the compromise will meet our objective of enhancing competition between trading venues and CCPs in the EU.

THE SCOPE OF ORGANISED TRADING FACILITIES (OTFs)

The Council agreement retains the Commission proposal for an OTF category covering both equity and non-equity instruments. However, Council agreed to allow two derogations from the prohibition on dealing against own capital: when operating on a “matched principal” basis in most non-equities and when dealing directly as principal in illiquid sovereign bonds.

THIRD COUNTRY PROVISIONS

With regards to third country access to the Single Market, you may recall that the Commission had proposed a new system of EU-wide access, conditional on an “equivalence assessment”. Our main concern over the equivalence test, as proposed by the Commission, was that it could result in the erection of unnecessary barriers to cross-border trade in financial services. We are therefore satisfied with the Council’s approach which removes the Commission’s proposed EU-wide regime, and leaves access to financial markets in the hands of individual Member States.

THE NON-DISCRIMINATION CLAUSE

In final Council negotiations, the UK also managed to secure the addition of a clause to support the principle of non-discrimination for the provision of investment services within the Single Market.

The provision of investment services is ever-more reliant on investment firms and market infrastructures being able to provide services across borders. It is vitally important that there are no artificial barriers to the ways in which these services are provided. In particular, it is important that there are no location requirements related to the currency of financial instruments over which investment services are provided. This provision builds on the Treaty base, and will ensure that the principle of non-discrimination is rigorously applied for the specific challenges faced by the Single Market in investment services.

Trilogues have now commenced under the Lithuanian Presidency, and we expect further meetings in September.

23 July 2013

MULTIANNUAL FINANCIAL FRAMEWORK (MFF) (UNNUMBERED)

Letter from Nicky Morgan MP, Economic Secretary to the Treasury, HM Treasury, to the Chairman

The European Parliament (EP) gave its formal consent on 19 November to the expenditure side of the 2014-2020 Multiannual Financial Framework (MFF) agreed in February 2013. The financing aspects of the EU Budget (the ‘own resources’ system) remain to be finalised. There will be three pieces of EU legislation, which will underpin the own resources system:

— Council Decision on the system of own resources of the European Union. Referred to as the Own Resources Decision (ORD), this legislation will be subject to unanimity in the Council and ratification by all Member States according to their constitutional requirements. In the UK this will take the form of primary legislation. The EP will be consulted, i.e. no EP consent is required.
— Council Regulation laying down implementing measures for the system of own resources of the European Union. Referred to as the Implementing Regulation (IR), this legislation will be adopted by qualified majority voting (QMV) in the Council and will require EP consent.

— Council Regulation on the methods and procedure for making available the traditional, VAT and GNI-based own resources and on the measures to meet cash requirements. Referred to as the Making Available Regulation (MAR), this legislation will be adopted by qualified majority voting (QMV) in the Council, requiring an opinion from the EP.

Since the June European Council, which confirmed the February MFF deal and clarified some of the details, officials have been engaged in the process of translating the political agreements on the own resources system into legal ones. This process is still ongoing and the draft proposals are not yet final. However, the current Presidency is keen to finalise the legislative process under their Presidency; and they are working towards the adoption of the three proposals before the end of the year. This means an accelerated time frame for adoption, with the Presidency aiming to send the draft proposals to the Council in December.

The proposals are not yet subject to automatic deposit, since they remain draft Presidency proposals. Unfortunately the Presidency’s proposed timetable may not provide your Committee with sufficient time to scrutinise the final proposals fully. Therefore in order to ensure the Committee has early sight of the content of the proposals I intend to deposit proactively the Presidency’s revised proposals as soon as we receive them, and provide you with an Explanatory Memorandum to give your committee the opportunity to start scrutinising the legislative proposals.

The Presidency is currently updating its texts to reflect the latest round of comments from Member States and is expected to circulate the updated proposals shortly, which is likely to be very close to the final texts. I will, of course, inform you of any changes to the proposals. Moreover, once the Council has adopted the new ORD, this must be ratified by individual Member States. For the UK, that involves primary legislation, which will give Parliament an opportunity to debate and vote on the proposals.

As you will recall, on the financing side of the MFF, the Prime Minister protected the UK rebate and prevented any new EU taxes to finance the budget at the February European Council. Our view on the current draft legislative proposals on own resources is that they are faithful to the February deal and accurately reflect what has been agreed, including on the UK rebate.

26 November 2013

PROVIDING FINANCIAL ASSISTANCE FOR MEMBER STATES WHOSE CURRENCY IS NOT THE EURO (12201/12)

Letter from the Rt. Hon. Greg Clark MP, Financial Secretary, HM Treasury, to the Chairman

You will recall that when I submitted the Explanatory Memoranda on the Commission proposal on EUBoP (EM 12201/12 of 18 July 2012) and on the ECB opinion of the proposal (EM 5477/13 of 24 February 2013) there was no timetable for discussion for this dossier. The Lithuanian Presidency have indicated that they intend to progress this during their Presidency with the aim to reach a Council General Approach by the end of the year. Therefore, I am now in a position to provide further details on the government position on this proposal.

The proposal introduces the possibility for financial assistance to be available in the form of precautionary credit lines (Precautionary Conditioned Credit Line, or PCCL, and Enhanced Conditioned Credit Line, or ECCL), similar to the precautionary instruments already available from the IMF. These precautionary programmes would allow Member States who meet a set of pre-qualification eligibility criteria (that I set out in my letter of 16 December 2012) to access a credit line with lighter conditionality than that of a full macroeconomic adjustment programme.

Precautionary programmes can provide a safety net to help countries, with sound economic fundamentals but moderate vulnerability, to cope with adverse shocks in order to prevent a crisis from occurring or deepening. This will complement the crisis resolution function of traditional programme types with more effective tools for crisis prevention. Precautionary programmes also avoid the stigma sometimes associated with more traditional programme types. Countries will be
encouraged to make approaches for assistance in a more timely fashion, reducing the risk of contagion in order to help prevent a deeper, more damaging, crisis developing.

The Chancellor welcomed the reforms to the IMF’s precautionary credit lines in recent years, as the IMF’s lending frameworks need to be flexible enough to deal with individual country problems and systemic shocks, while providing the right incentives for countries to adopt sound policies in the good times. The introduction of the PCCL and ECCL would allow the EU to provide precautionary assistance alongside the IMF.

The proposal as currently drafted extends the participation of the ECB beyond what has been the practice under the existing regulation. This role is not justified in the case of those Member States who do not intend to adopt the euro and have no obligation to do so, and in negotiations I will seek for it to be removed. You may recall that the ECB itself in its Opinion on the proposal argued that it should have less involvement than envisaged in the proposal. In addition, it is important that arrangements for the monitoring of any financial sector conditionality included in a programme, such as stress tests or assessment of supervisory capacity, are consistent across banking union members and those Member States that are not part of banking union.

With respect to the roles of other institutions, it is the established practice for EU Balance of Payments assistance to be provided alongside an IMF programme, and for the Commission and IMF to cooperate on programme design and monitoring (with the involvement of the ECB for ERM II countries). Having considered the role foreseen for the ESAs and the ESRB, I believe they have useful expertise in the areas identified by the proposal, and that the proposal is consistent with the existing remit of those bodies.

In addition, it is important that throughout the negotiations the role established for the Council in the existing Regulation is preserved.

As with any proposal for legislation with a legal base of Article 352, this proposal would require not only unanimous support from the Member States in Council but also an Act of Parliament.

3 October 2013

Letter from the Chairman to Sajid Javid MP, Financial Secretary, HM Treasury

Thank you for the letter from your predecessor, Rt. Hon Greg Clark MP, dated 3 October 2013, on EM 12201/12: the proposal for a Council Regulation establishing a facility for providing financial assistance for Member States whose currency is not the euro. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 15 October 2013.

We are grateful to you for this clarification of the Government's position. However we would wish for further elucidation on a number of points arising from the letter. We agree with you that the proposed role for the ECB is not justified for “those Member States who do not intend to adopt the euro and have no obligation to do so”, and note that the ECB itself has raised concerns in this regard.

Are you referring in practice to Denmark and the UK? How would Sweden be affected? What is the position of those two Member States on your proposal to amend the proposal? What is the position of other Member States on the UK’s efforts to amend the proposal? Are all other non-euro area Member States content for the ECB’s role to be extended in the way envisaged?

Given that this is the only concern you raise in your letter, and given your support, in principle, for the introduction of the PCCL and ECCL, are we correct to assume that, in the event that this point is satisfactorily addressed, you will be content to support the proposal? On the other hand, are we right to assume that, in the event that it is not addressed, you will seek to exercise the UK’s veto?

We would be grateful for a response to these questions, as well as an update on negotiations, by 31 October 2013. In the meantime we will continue to hold the document under scrutiny.

15 October 2013

Letter from Nicky Morgan MP, Economic Secretary to the Treasury, HM Treasury, to the Chairman

Thank you for your letter of 15 October on EM12201/12: the proposal for a Council Regulation establishing a facility for providing financial assistance for Member States whose currency is not the euro.
You ask about the proposed role of the ECB. As highlighted in Greg Clark’s letter to you of 3 October 2013, the ECB had itself raised concerns regarding its role as specified in the original draft proposal. The UK has continued to raise our concerns in discussions in Europe, and continues to seek for the removal of the ECB’s role as it was originally specified. Negotiations are ongoing, but there seems to be general support across Member States for the role of the ECB to be more limited. One option under consideration is for the role of the ECB in surveillance to be limited to ERM II Member States. Sweden, like the UK and Denmark, are not members of ERM II and would therefore also be excluded from ECB involvement.

Further to Greg Clark’s letter, I would also like to update the committee on a further amendment to the proposal. Since it was originally published, the European Parliament has called for the new Balance of Payments facility to be used not only for balance of payments support, but also to provide loans for the recapitalisation of financial institutions (similar to the ESM facility used to provide financial assistance to Spain). I do not support the introduction of such a facility which, in my view, goes beyond the intention of the EU Balance of Payments mechanism, and I will argue for the removal of any such facility.

1 November 2013

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PROVISION AND QUALITY OF STATISTICS FOR THE MACROECONOMIC IMBALANCES PROCEDURE (11177/13)

Letter from the Chairman to Nick Hurd MP, Minister for Civil Society, Cabinet Office

Thank you for your Explanatory Memorandum, dated 8 July 2013, on EM 11177/13: A Proposal for a Regulation on the provision of statistics for the macroeconomic imbalances procedure. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 30 July 2013.

We recognise the importance of high quality, robust statistics, in particular given the serious failures that came to light in the context of the economic crisis. Can you confirm that the proposal has its genesis in the problems encountered with regard to statistics in relation to Greece, for instance? Notwithstanding this, we are concerned at the apparent flaws in the Commission’s proposal that you highlight.

We are disappointed that the delay in deposit of this document until 21 June (two weeks after the proposal was published) meant that our ability to consider whether the proposal is consistent with the principle of subsidiarity before the expiry of the Reasoned Opinion deadline has been constrained. What was the reason for the delay in deposit? You state that the proposal is in accordance with the principle of subsidiarity. What is the basis for this assessment?

Can you provide us with more specific details of your concerns about this proposal, in particular in terms of the potential disproportionate effect? What do you mean when you state that “extensive application of wide-ranging and burdensome quality procedures risks failures of quality control in areas where the impact of policy outcomes may be greatest”? Can you give us some practical examples of the “failures of quality control” that you think may result?

You state that a systematic assessment of existing assurance processes would allow a clear view to be taken as to where strengthening is required. Can you give us more precise details of the alternative approach that you are advocating? You state that National Statistical Institutes (NSIs) and National Central Banks (NCBs) are already undertaking this work. What weaknesses have they identified? What work have UK institutions undertaken in this field? What in your view are the areas most in need of strengthening?

You state that concerns about the proposal are widespread among NSIs and NCBs across Member States. Which Member States have been most vocal in their concerns? Is there any sense of a consensus of opinion amongst NSIs, and also amongst NCBs? Are such concerns universal, or have some such bodies and Member States expressed support for the proposals? What efforts are you making to work with like-minded Member States to achieve the UK’s policy goals, and either redrafted or removed altogether?

We would be grateful for a response to these questions, as well as an update on negotiations, by 30 August 2013. In the meantime we will continue to hold the document under scrutiny.

30 July 2013
Letter from Nick Hurd MP to the Chairman

Thank you for your letter of 30 July seeking clarification about a number of issues in relation to my Explanatory Memorandum (EM) EM 11177/13: Provision and quality of statistics for the macroeconomic imbalances procedure (MIP). Please find my responses to your questions below.

You asked for confirmation that the proposal has its genesis in the problems encountered with regard to statistics in Greece, for instance.

The proposal does not appear to be the direct result of the issue of Greece’s public finance statistics, although that may have had a significant impact on the Commission’s general attitude to enforcing compliance on the quality of economic statistics. However, EU Governments have set up the MIP Scoreboard because the global economic and financial crisis has demonstrated that compliance with the Stability and Growth Pact is not sufficient by itself to ensure balanced growth in the EU’s economies. There are several other sources of macroeconomic imbalances, relating to private sector behaviour, which can be economically destabilising. In a globalised and highly interconnected world, the resulting instability can readily infect other economies. The Commission has therefore introduced this new mechanism on the provision and quality of related statistics as a means to ensure effective surveillance of a range of macroeconomic imbalances, including private sector debt, trade and current account balances, the exchange rate, unemployment and house prices.

You asked for the reasons for the delay in the deposit of the document, being two weeks after the proposal was published.

The proposal was transmitted to the Council Secretariat on 7 June and distributed by them on 18 June, eleven days later. It was deposited in Parliament on 21 June. The standard ten working day timetable for EM preparation and distribution to the scrutiny Committees was then adhered to, except in this case an unfortunate additional delay of one working day occurred.

You asked for further information on my assessment that the proposal is in accordance with the principle of subsidiarity.

In order to ensure that MIP relevant data are of comparable quality, and therefore facilitate EU policy decisions based on accurate evidence, which is in the United Kingdom’s interests, action at the EU-level can be justified according to the subsidiarity principle. Although, for instance, the UK may be seen to have relatively robust quality assurances processes, this cannot guarantee comparability with the official statistics of other Member States. The Government therefore agrees with the Commission’s assessment in principle. National action alone cannot provide for the harmonised quality assurance procedures required for the EU policy decisions in question.

You asked me to provide more details on potential disproportionate effect of the proposal and the effects of wide-ranging and burdensome quality procedures.

The Government believes that the aim of EU-level action should be the identification of major issues affecting the quality and comparability of MIP-related statistics, and then to put in place plans that address these issues as quickly as possible. The Commission’s current proposals instead have the effect of identifying all issues, minor and major, and put equal priority on fixing all issues. This lack of effective prioritisation means there is a real risk that it will take longer to make the most important improvements as effort is diluted. Therefore it will take longer to achieve the aim of comparable and high quality statistics.

Moreover, the type of statistical expertise required for the production of the statistics in question is highly specialised and necessarily limited in all Member States (for example, National Accounting skills are rare and take many years to develop). The diversion of such stretched resources in National Statistical Institutes (NSIs) and National Central Banks (NCBs) towards potentially unnecessary, open-ended, and onerous activities risks undermining efforts to address major quality issues and indeed maintain quality in other areas. These risks are further enhanced as Member States are facing a period of major change in delivering economic statistics, for example through implementing the recent Regulation on the European System of National and Regional Accounts in the EU (ESA 2010).

You asked for more precise details of the alternative approach advocated by HM Government; what weaknesses have already been identified by the work being undertaken by NSIs and NCBs, and in my view which areas require strengthening; and what work have UK institutions already undertaken in this field.

At its plenary meeting on 4 July 2013, the advisory body the Committee on Monetary, Financial and Balance of Payments Statistics (CMFB) decided to set up a Task Force on the quality of the statistics underlying the MIP indicators. As the MIP is already in place and the indicators are being used, the CMFB agreed the work of the Task Force needs to be undertaken without delay, particularly in the
light of the new cycle of the MIP Scoreboard in November 2013 and the next Alert Mechanism Report (AMR). The Task Force is mandated to:

— propose a framework and contents of a quality assessment report on MIP statistics to communicate key messages to policymakers and the public at large;
— propose priorities, based on established principles, to enhance the quality management of the statistics underlying the MIP indicators, including reference to their main policy uses; and,
— provide an overview of relevant existing inventories and statistical domain quality reports of the European Statistical System (ESS) and European System of Central Banks (ESCB).

It is planned that the proposal for a quality assessment report should become available in the first part of September 2013 and the Task Force dissolved at the next plenary session of the CMFB in January 2014. It is right that the results of the Task Force’s work should inform any assessment of which areas of MIP-related statistics require strengthening and the proportionate processes required to rectify any significant weaknesses.

The Office for National Statistics (ONS) and the Bank of England are members of the CMFB and have contributed to its deliberations on quality issues related to MIP statistics. Representatives of ONS and the Bank are members of the aforementioned Task Force, along with 13 other NSIs and 9 other NCBs. I am not aware of any work carried out independently by UK institutions on the quality of MIP-related statistics across Member States. The UK Statistics Authority is responsible for providing independent assessments of the quality of UK official statistics.

You asked which Member States have been most vocal in their concerns and is there a consensus of opinion among National Statistical Institutes and National Central Banks, about the efforts we are making to work with like-minded Member States, and for an update on negotiations.

The Government’s concerns were echoed by the vast majority of Member States at the level of the European Statistical System Committee (ESSC), the ESS’ comitology committee. None offered support for the Commission’s proposal. The CMFB, representing all NSIs and NCBs, also mirrored our concerns at the ESSC, which its Chair also attends.

The next possible date for discussion of the dossier in Council is at the next Council Working Party meeting on statistics (STATIS) on 13 September. The Lithuanian Presidency has yet to release an agenda for this meeting. However, it has launched an informal written consultation of Member States to prepare for a first Working Party discussion. Although no Member State indicated a rejection of the proposal in its entirety, the results did indicate a continued consensus among Member States to reject all aspects of the proposal which were disproportionate, open-ended, and introduced a separate sanctions regime to that already established under Article 338 of the Treaty.

Negotiations on EU statistical regulations normally take place in an environment of close cooperation and coordination between the NSIs of Member States, both before and during Council negotiations. In this case, UK officials have helped coordinate efforts to ensure as much consistency as possible among a wide group of Member States in the development of Government positions, negotiating tactics in Council, and briefing to Members of the European Parliament. I expect this to continue during future negotiations on this dossier.

22 August 2013

Letter from the Chairman to Nick Hurd MP

Thank you for your letter, dated 22 August 2013, on EM 11177/13 on the Provision and Quality of Statistics for the Macroeconomic Imbalances Procedure (MIP). The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 10 September 2013.

We are grateful to you for this detailed and informative response. We note in particular the important work being undertaken by the Committee on Monetary, Financial and Balance of Statistics (CMFB) Task Force on the quality of statistics underlying the MIP indicators. We note that its proposal for a quality assessment report is expected shortly, and would be grateful if you could write to us again to summarise its findings, in particular as to which areas of MIP-related statistics require strengthening, and what steps are required to correct weaknesses. In the meantime, can you tell us
whether the Commission has given any commitment to take the views of the Task Force into account?

We also note your statement that negotiations on EU statistical regulations normally take place in an environment of close cooperation and coordination between the NSIs of Member States, and we are pleased to hear that UK officials have played a key role in such cooperation.

You state that the vast majority of Member States have echoed the Government’s concerns. However you also state that no Member State has indicated a rejection of the proposal in its entirety. Is it your judgement that the proposal is therefore more likely to be amended than dropped, as you suggested you would argue for in your EM? If so, what steps will you take to ensure that any disproportionate elements of the proposal are eliminated?

You state that the next possible date for discussion in Council is on 13 September. We would be grateful for an update on negotiations, as well as a response to our questions, by 1 October 2013. Given the controversial nature of the proposal and the uncertainty over the outcome of negotiations, we will in the meantime continue to hold the document under scrutiny.

10 September 2013

**Letter from Nick Hurd MP to the Chairman**

Thank you for your letter of 10 September on the above matter.

You asked me to tell you whether the Commission has given any commitment to take the views of the Task Force of the Committee on Monetary, Financial and Balance of Payment Statistics (CMFB) into account.

The Council has asked the European System of Central Banks (ESCB) and European Statistical System (ESS) to work together to ensure the successful achievement of the data quality required for Macroeconomic Imbalances Procedures Scoreboard (MIPS). The CMFB encompasses members of both systems and they will be working together to meet this aim. The Commission has supported the formation of the Task Force but has continued with its commitment to advancing the regulation in question before the results of the Task Force are known. This could be because it is responding to pressure from users of the MIPS, such as the Economic and Financial Affairs Council (ECOFIN), by prioritising the speedy implementation of a regulatory framework, rather than establishing an effective and proportionate framework as soon as possible.

You also asked if the proposal is more likely to be amended rather than dropped; for an update on negotiations following the Council Working Party on 13 September; and, what steps are the Government taking to ensure that any disproportionate elements of the proposal are eliminated.

The Council Working Party meeting on 13 September revealed that the UK’s concerns were shared by every Member State except one. We expect, along with these other Member States, that the Commission will either have to compromise significantly in line with these concerns or withdraw the proposal completely. We will continue to work with other Member States in support of these aims.

We are awaiting the formal opinion of the Council Legal Service, on the legal concerns we share with other Member States, the formal Opinion of the European Central Bank on the proposals, the views of the European Parliament, and the Commission’s response to this range of initial formal positions. These will then feed into our approach to, and expectations of, the negotiations.

I will write to you again to summarise the findings of the CMFB Task Force once they are understood, as requested in your letter, and with news of any further significant developments in negotiations in the meantime.

1 October 2013

**SINGLE RESOLUTION MECHANISM (12315/13)**

**Letter from the Chairman to the Rt. Hon. Greg Clark MP, Financial Secretary, HM Treasury**

Thank you for your Explanatory Memorandum, dated 27 July 2013, on EM 12315/13 on the proposal for a Regulation establishing a Single Resolution Mechanism and a Single Resolution Fund. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 10 September 2013.
In our report European Banking Union: Key issues and challenges we emphasised the importance of establishing a Single Resolution Mechanism in order to resolve the inherent flaws in the euro area banking sector. Such a mechanism, however, must be well-designed, legally sound and avoid any distortion of the single market.

We welcome the fact that, despite only being applicable to a subset of Member States, this proposal must be agreed by all Member States. This is the optimal approach to such negotiations and ensures non-participating Member States, including the UK, have a seat at the table and can ensure the interests of the single market are protected.

We note your concern over the use of Article 114 TFEU since it would not apply to all firms in the relevant sector throughout the single market. What alternative would meet your objectives of legality and enabling the exclusion of UK firms?

With regards to the role of the Single Resolution Board, we would welcome further clarification and, in particular, could you highlight provisions which you consider might give rise to incompatibility?

On the role of the Commission, we are unconvinced by your legal objections since the Treaties often and typically describe the functions of the Commission in quite broad terms. In the light of this, do you still believe there are legal obstacles to granting this role to the Commission? We do, however, accept there is a risk of a conflict of interest given the Commission’s role in monitoring state aid. The Commission has argued that it would apply exactly the same standards when examining whether resolution action envisaged under the SRM was compatible with state aid provisions as it would apply when examining envisaged action by national authorities. Are you convinced by this? What safeguards could be put in place to avoid a conflict of interest?

We will continue to scrutinise this document in the context of our continuing inquiry into European ‘Genuine Economic and Monetary Union’ and its implications for the UK. We would welcome a response to this letter by 27 September 2013. In the meantime we will continue to hold this document under scrutiny.

10 September 2013

SINGLE SUPERVISORY MECHANISM: INTER-INSTITUTIONAL AGREEMENT
(UNNUMBERED)

Letter from the Chairman to Sajid Javid MP, Financial Secretary, HM Treasury


We understand from various media reports that the Government delayed agreement on the Single Supervisory Mechanism to allow the United Kingdom Parliament time to review the Inter-Institutional Agreement (IIA) between the European Parliament and the ECB. We also understand that you delayed approval because you were worried that the voting rules in the European Banking Authority (EBA) would be watered down once the SSM was agreed, either in the context of the Review of European Supervisory Agencies or in future legislative proposals. Can you provide more detail on this? Why were we not informed of your concerns? What update can you give us on the outcome of negotiations? What assurance can you give us that the UK’s concerns have been met?

Whilst claiming that you were delaying approval of this dossier to provide the UK Parliament with more time to consider it, you failed to keep us informed of the more substantive concerns you had. Why was it not possible to keep us informed? We are content to clear this document from scrutiny but expect a substantive response to our questions by 5 November 2013.

28 October 2013
Letter from the Chairman to David Gauke MP, Exchequer Secretary, HM Treasury


We note your concern about the scope of the proposal, in particular your concern that it is not consistent with the principles of fiscal sovereignty, subsidiarity and proportionality. We also note your concern that the effectiveness of the proposal may be limited by the degree of optionality that the Commission has understandably sought to retain.

However we are supportive of the Commission’s efforts to harmonise practice across the EU, and consequently we have decided not to recommend that the House issue a subsidiarity Reasoned Opinion. In doing so we took into account the fact that the Government are sympathetic to action at EU level to meet the Commission objective of facilitating cross-border trade. Insofar as the proposal also seeks to reduce the burden on all businesses, whether involved in cross-border trade or not, it appears to us likely, on present information, that the benefits to EU businesses will outweigh the costs to business and Member States, even allowing for some exaggeration on the part of the Commission of the benefit of this proposal. We should, however, be interested in the Government’s estimate of the benefits and costs of this proposal.

We also took into account that whilst the UK has successfully simplified the administration of VAT other Member States may not have. An EU wide simplification of VAT could benefit UK businesses involved in cross-border trade and the proposal incorporates some flexibility, which the UK could exploit in order to maintain, to some extent, its simplified system of VAT administration. What efforts are you making to ensure that the UK system is used as a model and benchmark across the rest of the EU?

You state that the Government are not convinced that a legislative solution is the right way forward, and that you will continue to work with the European Commission, other Member States and UK businesses to see if there are better ways to respond to business concerns. You also restate your own commitment to “cut red tape for businesses and to encourage them to increase their cross-border trade.” We would therefore be interested in your assessment of the prospect of success for this exercise and how you believe that the legitimate aims of the proposal can be met, if not via a legislative approach. To what extent does harmonisation though EU legislation meet your aim of providing clearer information about the VAT declarations and underlying rules in operation across the 28 EU Member States? What is the view of EU businesses, and in particular UK business (including SMEs) on the Commission’s proposal? Do they support a legislative approach? What is the position of other Member States?

We should also be grateful for further information on your comitology concern. Given that comitology (subject to qualified majority voting) is only intended to be used in relation to technical detail, how much threat would its use actually pose to the principle of fiscal sovereignty? Can you give us an example of a significant decision on which the UK could be outvoted through its use?

We would be grateful for a response to this letter by 10 December 2013. In the meantime we will continue to hold the document under scrutiny.

26 November 2013

STATUTORY AUDITS OF ANNUAL ACCOUNTS AND CONSOLIDATED ACCOUNTS (16971/11), STATUTORY AUDIT OF PUBLIC-INTEREST ENTITIES (16972/11)

Letter from Jo Swinson MP, Parliamentary Under-Secretary for Employment Relations, Consumer Affairs, Department for Business, Innovation and Skills, to the Chairman

I write to update you on the negotiations on this dossier. I attach [not printed] Presidency compromise texts on the Directive (reference 9379/13) and the Regulation (reference 9380/13) which are both Limité. These are not for publication and I would be grateful if you would keep these confidential.
In the following paragraphs I set out the key ways in which the Presidency’s proposed compromise text on the Directive differs from the original proposal.

— We have been successful in securing a definition of Public Interest Entities (PIEs) that is less extensive than that in the proposal. Unlisted undertakings for collective investment in transferable securities (UCITS) and unlisted Alternative Investment Funds are now excluded from the definition, as well as payment institutions, electronic money institutions, investment firms, central securities depositories and central counterparties. Member States will now have the flexibility to designate other entities as PIEs. We support these changes.

— In line with our negotiating aim of moving elements of the proposal from the Regulation to the Directive, articles on increasing independence, professional scepticism and clarifying the appropriate internal organisation of auditors have been transferred from the Regulation to the Directive. This will make them easier to reflect in existing UK Ethical Standards.

— Similarly, enhanced sanctioning powers for national competent authorities are now moved from the Regulation into the Directive and therefore apply to non-PIE audits as well as PIE audits. However these powers are still more specific and stronger than we believe are necessary.

— EU ownership rules under which audit firms must be majority owned by licensed auditors have been retained. We did not support this retention, but the view of most Member States was that this was important to ensure the independence of the auditor.

— A pan European “passport” for statutory auditors to allow audit firms to provide statutory audits in Member States other than the Member State in which they have been approved. Discussion in the working groups is as to whether the choice of aptitude test and adaptation period should be the candidate’s or the Member State’s. We prefer the latter.

— Removal of the original proposal’s prohibition of the inspection of non PIE audits being delegated to professional accounting bodies. We support this removal.

— The requirement for Member States to ensure that audits are carried out in accordance with adopted international auditing standards have now been moved from the Regulation to the Directive, which we welcome. This should enable Member States to apply stricter standards at national level, since the Directive is minimum harmonisation. The process of EU adoption of auditing standards is still subject to negotiation.

Changes have also been made to the Regulation by the proposed compromise text.

— Fees for permitted non-audit services are now limited to 70% (up from 10% for “related audit services” in the original proposal) of the audit fee paid by the audited entity. We oppose a cap for two reasons: first, both auditor and audit committee have to be satisfied that there is no issue of independence before these services are provided; and second, in circumstances such as the merger of two global businesses, the fee for the reporting work that is most practically and rapidly done by the auditor could easily be more than the audit fee.

— There is now a “black list” of forbidden non-audit services, but in contrast to the original proposal, no “white list” of services that are always permissible, or “grey list” of services that are permissible subject to the approval of the company’s audit committee. We agree with the principle of having a black list only, which sets out services where there is a lack of independence, but we do not agree with the list as currently drafted. The current list would prohibit almost all non-audit services, including reports to prudential regulators, due diligence work and comfort letters to investors, none of which create conflicts of interest. We would like Member State audit authorities to be able to add to the black list to reflect national concerns. We are content that all permitted non-audit services are subject to approval.
by the audit committee, the auditor having first assessed the threats and safeguards to independence.

We have successfully achieved the removal of the proposal to force audit firms which exceed certain size criteria to turn into "pure audit firms".

We have managed to negotiate that some elements of the audit report requirements should move into the Directive, which will enable them better to align with existing requirements. Other elements which only apply to PIEs remain in the Regulation, but the precise requirements are still being discussed in the working group. One of the most onerous requirements, to assess the entity’s internal control systems, has been removed and replaced with a more acceptable requirement to report on significant deficiencies in the entity's internal financial control system. Drafting of the requirement for the auditor to report on going concern and risk is changing and we are seeking to ensure that it ends up as useful to the reader of the accounts whilst not imposing unnecessary additional audit requirements which may be costly for companies, but deliver little benefit.

Some elements of the audit report in the original proposal (details of the audit work undertaken) have been moved to the private report of the auditor to the company’s audit committee, which we welcome. This will cut clutter in the annual report and accounts as well as enable the auditor to bring confidential information formally to the attention of the audit committee.

The requirement for large audit firms to publish a corporate governance statement has been deleted.

The requirement for PIEs to have one member of the audit committee with competence in auditing and another member with competence in accounting/auditing is retained. We and a number of other Member States continue to find this requirement too burdensome.

Audit firms are now appointed for a minimum of one year, which we welcome, rather than the two years originally proposed.

Audit firms were originally to rotate off the engagement for PIEs after 6 years, unless joint auditors have been in place, in which case rotation must occur after 9 years. The audited entity could exceptionally ask the national audit supervisor to reappoint the auditor for a further 2 years (or in the case of joint audit, 3 years). In the compromise text rotation is now 14 years (for joint audit 16 years), provided there has been either a tender process after 7 years (for joint audit 8 years). The Government’s position on this was set out by my Ministerial colleague Lord Green at an open session of the Competitiveness Council on 28 May. Whilst believing that tendering is the better solution, in the interests of compromise, and provided satisfactory agreement is reached on other areas of the dossier, we may be able to accept mandatory rotation of the auditors of systemic companies. However we would prefer 25 years, which is the period proposed by JURI Committee of the European Parliament. Some Member States are very much in favour of mandatory rotation, others want to limit the number of companies that rotation applies to but are content with the number of years that the compromise text proposes.

The requirement for the largest audit firms to produce and submit a contingency plan to the competent authority, has been removed.

The compromise text still gives ESMA a significant role and duties as a pan-European audit supervisor. The only change has been to establish a sub-Committee of ESMA made up of national audit supervisors. As set out by Lord Green in the Competitiveness Council we continue to believe that ESMA should not be involved at all, and a cooperation between national audit supervisors should be improved by an enhancement of the role of the existing European Grouping of Audit Oversight Bodies (EGAOB), which consists of the national audit supervisors. This would be a less expensive and
lighter touch regime than that proposed in the compromise text. Our view is shared by a significant number of Member States.

— There is still negotiation as to whether or not competent authorities will be permitted to contract practising auditors to inspect audits done by other firms as part of the competent authority’s quality assurance role.

— The JURI Committee of the European Parliament has now reported, adopting the report by 15 votes to 10. Particular elements of the JURI Committee report are as follows:

— that there should be mandatory rotation of all Public Interest Entity (PIE) audits every 25 years, provided there has been a tender after a maximum of 14 years;

— in favour of a Public Interest Entity (PIE) definition comprising all listed companies, banks and insurers, which will include listed Alternative Investment Funds (AIFs) and listed UCITS;

— to move certain elements of the proposal to a Directive;

— to remove the proposed 10% cap on audit related services as a proportion of the audit fee. To allow Member States to add to a black list of prohibited non-audit services.

The Presidency will try to reach compromise on the outstanding areas of disagreement before the summer in order to reach a General Approach and then move rapidly to trilogue with the European Parliament.

12 June 2013

Letter from the Chairman to Jo Swinson MP

Thank you for your letter, dated 12 June 2013, on EMs 16971/11 & 16972/11, on statutory audits of annual accounts. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 25 June 2013.

We are grateful to you for this update. Are we correct to ascertain from your letter that Member States are moving towards a compromise on the proposals? Do you anticipate that agreement will soon be reached? You state that you do not support the “black list” of forbidden non-audit services as currently drafted as it would prohibit almost all non-audit services. Can you be more specific about the services that will be prohibited? How can the correct balance be struck between ensuring an effective system of auditing, and that there is sufficient transparency in terms of the activities undertaken?

You also state that there are various proposals in terms of a mandatory rotation period. Will these periods begin from the moment a firm was first appointed, or from the moment the regulation comes into force? You state that you would prefer a 25 year rotation period. If mandatory rotation is introduced, how can it be ensured that the period chosen provides sufficient balance between providing firms with stability and certainty on the one hand, and delivering transparency and fresh insight to the audit process on the other? We would be grateful for a response to these questions, and an update on negotiations, by 23 July 2013.

26 June 2013

Letter from Jo Swinson MP to the Chairman

Thank you for your letter of 26 June about the negotiations on this dossier. I apologise for having missed your proposed deadline for a response but I hope I can answer your questions satisfactorily in the light of recent developments. I attach [not printed] the most recent Presidency compromise texts on the Directive (reference 12612/13) and the Regulation (reference 12662/13) which are both Limité. As with the previous versions that I sent, these are not for publication and I would be grateful if you would keep them confidential.

To answer your questions in the order they were asked:
PROGRESS TOWARDS AGREEMENT

The Member States are moving towards a compromise on the proposals, though not at the pace the Commission or the new Lithuanian Presidency would like. Both the Competitiveness Council and the Committee of Permanent Representatives have held “orientation debates” on the most contentious proposals in the package (the two you have identified in your letter and the proposal on a new pan-European coordinating body for auditor oversight). These have exposed clear differences of view across the members of the Council on all three issues.

However the Presidency is working hard to broker a compromise and showing signs of willingness to take a stand when needed against the Commission. They appear still to hope to reach agreement at the start of the autumn but there are a number of hurdles to overcome, not least in relation to the issues you raise.

NON-AUDIT SERVICES

On the “black list” of forbidden non-audit services that are not permissible, we are closer to reaching agreement on the list as it is now drafted. The list is now more specific, providing certainty for auditors, and more focussed on services giving rise to a conflict of interest. It can be found at Article 10(1) of the latest text of the Regulation. Member State audit authorities are now able to add to the black list to reflect national concerns, which we welcome. However these changes have come at the cost of some provisions being applied to all audits in the Directive preventing non-audit services being provided at-all where certain important but common threats to the auditor’s independence arise. The UK objects to this prohibition (Directive Article 22d(2) subparagraph 1) as it is too broad and assumes that there are no cases where sufficient safeguards to independence are available.

You may wish to note that the UK’s position on these issues is consistent with that of the Competition Commission, which yesterday published its provisional decision on remedies as part of its investigation into the market for statutory audit services to the largest companies.

On the question of transparency of the services provided this is improved in both Articles 22 and 23 of the proposed EU Regulation by requirements for the Audit report on a “public interest entity” to declare that prohibited non-audit services were not provided. The report must also set out any non-audit services that were provided and which have not been disclosed in the audited entity’s annual report and financial statements. There is also a considerably enhanced role for the audit committee, which the UK has supported.

MANDATORY AUDIT FIRM ROTATION

On mandatory rotation of statutory auditors and audit firms, in the latest compromise text rotation is set at 16 years (for PIEs that are not financial services providers or that are subject to joint audit) or 13 years for financial services providers that are not subject to joint audit. Where there is no joint audit these periods apply providing there has been a tender process before the expiry of 10 years.

The Government’s position on this has not changed since it was set out by my Ministerial colleague Lord Green at the Competitiveness Council on 28 May. We continue to share the Parliament’s preference for a mandatory rotation period around 25 years.

I take some comfort from the fact that this is consistent with the findings of the Competition Commission, which has decided not to pursue the mandatory switching of audit firms, though it has endorsed more frequent retendering of the largest audits (every 5 years).

On your question as to how to achieve an appropriate balance, you will observe that the general preference in the UK for periods that are multiples of 5 years is a result of the fact that this is the mandatory partner rotation period in the UK. We have now successfully negotiated sufficient flexibility for this to continue under the framework in the Regulation (in Article 33). There is also welcome flexibility in this Regulation for other Member States that prefer, or already have, shorter retendering and firm rotation periods, to continue with these. In my view the key here is to provide for harmonisation around appropriate maxima, where these can be agreed, while recognising Member States may wish to exercise flexibility within these.

I anticipate the Presidency will try to reach a General Approach and then move rapidly to trilogue with the European Parliament in the autumn.

24 July 2013
Letter from the Chairman to Jo Swinson MP

Thank you for your letter, dated 24 July 2013, on EMs 16971/11 & 16972/11, on statutory audits of annual accounts. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered these documents at its meeting on 10 September 2013.

We are grateful to you for this useful update, and for your efforts in keeping the Committee informed. We would be grateful if you could write again to advise us of the progress of negotiations as the Lithuanian Presidency attempts to secure a General Approach.

10 September 2013

Letter from Jo Swinson MP to the Chairman

I write in reply to your letter of 10 September to update you on the negotiations on this dossier. I attach [not printed] the Presidency compromise text on the Directive and Regulation (reference 14053/13) which was the subject of a mandate from the Council at COREPER on Friday 4 October for the Presidency to begin informal trilogues with representatives of the Parliament and the Commission. Please note that this text is Limité as these are informal trilogues being taken forward with a view to achieving a 1st reading deal. It is not for publication and I should be grateful if you would keep it confidential.

If agreement can be reached, the Council will not need to adopt a General Approach, but will confirm the agreement by accepting a European Parliament first reading. However, if a first reading deal is not possible through the current process and the European Parliament adopts a first reading that Council cannot accept, the Council may yet have to adopt a common position as the basis for future negotiations. These would be unlikely to recommence much before the end of next year after the new European Parliament has organised itself after the European elections in May.

At Annex A [not printed] I set out the key areas where the Presidency's compromise text differs from the original proposal. I have also included an Annex B [not printed] on the key differences between this text and that proposed by the JURI Committee of the European Parliament.

19 October 2013

UK CONVERGENCE PROGRAMME 2012-2013 (UNNUMBERED)

Letter from the Chairman to the Rt. Hon. Greg Clark MP, Financial Secretary, HM Treasury

Thank you for your letter, dated 18 April 2013, on the 2012-13 UK Convergence Programme. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 14 May 2013.

Your letter makes reference to the 25 April 2013 House of Lords debate on the Convergence Programme. The Sub-Committee Chairman, Lord Harrison, raised a number of points in the debate reflecting on the EU Committee's 2011 report on The EU strategy for growth and the UK National Reform Programme, which recommended that “the production of the Convergence Programme and the NRP should be synchronised, and that the annual debate on the Convergence Programme under the European Communities (Amendment) Act 1993 should also, in this House, cover the NRP.”

I would wish to repeat the regret expressed by Lord Harrison in the debate that neither your letter nor the Motions before the House made any mention of the National Reform Programme. I also regret that it was not possible to facilitate a debate on the National Reform Programme alongside the Convergence Programme, in spite of the Government’s commitment, in their response to the above report, to look favourably on this recommendation in principle.

In his reply to Lord Harrison, Lord Newby stated that “we do not think that there is a legal obligation to debate the basis for the national reform programme, and we are not aware of any occasion on which it has been submitted for parliamentary clearance, including under the previous Government. Of course, the national reform programme does not include any material that has not previously been published and debated.”

This reply is unsatisfactory on a number of fronts. First, it fails to reflect the Government’s agreement to look favourably in principle on the Committee’s recommendation that the NRP be debated in conjunction with the Convergence Programme. Second, it unhelpfully muddies the waters by referring
to a legal obligation, when neither the Committee report nor Lord Harrison in the debate argued for any such obligation. Indeed, the Committee report specifically states that “we do not recommend that the NRP should be presented for approval; this would require primary legislation, and would be unnecessary, since the NRP does not contain new policy. We recommend only that it should appear on the Lords Order Paper and should form part of the material for the debate. This would fit the logic of the European Semester approach, and would require no additional parliamentary time.” Third, in light of this, whilst the Minister was inevitably correct to state that the NRP has not been submitted for parliamentary clearance (since no-one had requested that it should be), the 2011 debate did reflect the Committee’s request. The then Commercial Secretary to the Treasury, Lord Sassoon, opened that debate by stating that:

“I welcome this opportunity to debate the information that will be provided to the European Commission under Section 5 of the European Communities (Amendment) Act 1993. I also welcome the chance to exchange views on two closely related topics: the UK’s National Reform Programme 2011, the NRP; and the Government’s response to the Lords EU Select Committee’s 5th report. ... I assure noble Lords at the outset that the Government look favourably, in principle, on both the committee’s recommendations. While it might not be possible to synchronise the national reform programme and the convergence programme, since they are intrinsically different documents and therefore produced according to markedly different internal procedures, we will give careful consideration to debating the NRP alongside the convergence programme again in future years.”

(House of Lords Hansard, 12 May 2011, cols. 1065-6)

I regret that neither the Convergence Programme nor the National Reform Programme were published in time for the debate. Whilst you are correct to state that there is no legal obligation to do so, it would evidently make the work of the House easier if it possessed in advance the material so intrinsic to the debate in question. Indeed, we can find no record of you meeting the commitment of your 18 April letter that early copies of the Convergence Programme would be provided to Parliament prior to the debate. Can you therefore confirm whether or not the commitment in your letter was fulfilled?

In light of this, I would repeat the questions posed by Lord Harrison in the 25 April debate. Why did it not prove possible to facilitate a debate in this House on the NRP alongside the Convergence Programme? Why was it not possible to publish the Convergence Programme and National Reform Programme in advance of the debate? Will you seek to facilitate a debate on the NRP in the House of Lords? What steps will you take to ensure that these problems are not repeated next year, and to ensure that it is possible for next year’s debate to feature both elements, and for them to be published in time?

14 May 2013

Letter from the Rt. Hon. Greg Clark MP to the Chairman

Thank you for your letter, dated 14 May 2013, in which you follow up on the House of Lords debate of 25 April on the 2012-13 UK Convergence Programme and the European Semester.

First, I would like to confirm that pre-publication copies of the Convergence Programme document were delivered to the Printed Paper office in the House of Lords on 19 April, meeting the Government’s commitment, as set out in my letter of 18 April, to provide early copies of the document to Parliament prior to the debate.

The Government does not formally publish the document before obtaining Parliamentary approval of the economic and budgetary assessment upon which it is based.

Regarding the National Reform Programme, you asked in your letter why it was not possible to facilitate a debate on this document alongside the Convergence Programme. As you are aware, the National Reform Programme is not a document formally subject to Parliamentary scrutiny. In this case, the proximity of the publication date to the Budget meant that it would not have been possible to publish the National Reform Programme prior to the debate on 25 April.

However, I recognise that the Committees may want the opportunity to consider the National Reform Programme, as it did in 2011, and the Government remains open to finding a way to make this possible.

27 June 2013
Letter from Lord Deighton, Commercial Secretary to the Treasury, HM Treasury, to the Chairman

I am replying on behalf of Lord Newby to your letter, dated 14 May 2013, in which you follow up on the House of Lords debate of 25 April on the 2012-13 UK Convergence Programme and the European Semester.

First, I would like to confirm that pre-publication copies of the Convergence Programme document were delivered to the Printed Paper office in the House of Lords on 19 April, meeting the Government's commitment, as set out in my letter of 18 April, to provide early copies of the document to Parliament prior to the debate.

The Government does not formally publish the document before obtaining Parliamentary approval of the economic and budgetary assessment upon which it is based.

Regarding the National Reform Programme, you asked in your letter why it was not possible to facilitate a debate on this document alongside the Convergence Programme. As you are aware, the National Reform Programme is not a document formally subject to Parliamentary scrutiny. In this case, the proximity of the publication date to the Budget meant that it would not have been possible to publish the National Reform Programme prior to the debate on 25 April.

However, I recognise that the Committees may want the opportunity to consider the National Reform Programme, as it did in 2011, and the Government remains open to finding a way to make this possible.

2 July 2013

UPDATE ON CAPITAL REQUIREMENTS REGULATION AND DIRECTIVE 4 (13284/11, 13285/11)

Letter from the Chairman to the Rt. Hon. Greg Clark MP, Financial Secretary, HM Treasury

Thank you for your letter, dated 15 April 2013, on EMs 13284/11 & 13285/11: Capital Requirements Regulation and Directive (CRD IV). The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 14 May 2013.

We are grateful for the update you provide. Given that the relevant element is contained in the Regulation, will there be any legislative vehicle for discussion of the agreement on remuneration provisions in the UK Parliament? Are there any rules within the European Parliament as to whether any amendments to a piece of legislation need to be considered to relate to the scope of a proposal in order to be judged to be in order? Were any such procedural concerns raised in relation to this amendment?

We would be grateful for a response to these questions by 10 June 2013.

14 May 2013

Letter from the Rt. Hon. Greg Clark MP to the Chairman

Thank you for your letter, dated 14 May 2013, on EMs 13284/11 & 13285/11: Capital Requirements Regulation and Directive (CRD 4). You asked three questions:

— Given that the relevant element is contained in the Regulation, will there be any legislative vehicle for discussion of the agreement on remuneration provisions in the UK Parliament?

— Are there any rules within the European Parliament as to whether any amendments to a piece of legislation need to be considered to relate to the scope of a proposal in order to be judged to be in order?

— Were any such procedural concerns raised in relation to this amendment?

First, the provisions concerning remuneration are contained in the Directive, not the Regulation (with the exception of the disclosure requirements), and as such have to be transposed into UK law rather than being directly applicable. The Government will decide the transposition method for this specific provision once the CRD 4 text has been finalised. The method of transposition selected will
determine whether or not there will be any legislative vehicle for discussion of the agreement on remuneration provisions in the UK Parliament.

Second, the institutions operate on the basis that Council and Parliament’s amendments must not go beyond, or “denature”, the original Commission proposal, as that is an interference with the Commission’s right of initiative with respect to legislative proposals. Thus, the Secretariat to the European Parliament Committees examines amendments to assess whether they are consistent with this principle.

Third, we are not aware that any such procedural concerns were raised about the scope of the amendments in relation to the remuneration provisions. However, the UK did make clear it does not consider the provisions on remuneration to be consistent with the intention of CRD 4, which is to promote financial stability and there had been inadequate assessment or discussion of the impact of these provisions.

7 June 2013

**Letter from the Chairman to the Rt. Hon. Greg Clark MP**

Thank you for your letter, dated 7 June 2013, on EMs 13284/11 & 13285/11: Capital Requirements Regulation and Directive (CRD IV). The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 18 June 2013.

We are grateful for you for the update you provide. We remain deeply concerned about the impact of the remuneration provisions upon the UK financial sector, and predicted that it is likely simply to lead to an inflation of fixed salaries. We are concerned to see such interference by the EU institutions into the remuneration policy of financial institutions. You state that the Government will decide on the transposition method for this specific provision once the CRD IV text is finalised, and that the method of transposition selected would determine whether or not there would be any legislative vehicle for discussion of the agreement of remuneration provisions in the UK Parliament. We would be grateful for confirmation of the transposition method chosen, and whether Parliament will have an opportunity to debate this agreement, as soon as you have made a decision.

18 June 2013

**VAT FRAUD: QUICK REACTION MECHANISM (13027/12)**

**Letter from David Gauke MP, Exchequer Secretary, HM Treasury, to the Chairman**

I am writing further to my letter dated 16 April to update you on negotiations in relation to the VAT fraud Quick Reaction Mechanism (QRM) proposal.

Since my previous letter, a real willingness on behalf of Member States to engage and resolve our reservations has emerged. The May European Council conclusions which look for agreement at the June ECOFIN have also provided impetus towards a compromise that will enable the Member States to adopt measures which will be useful to all, including the UK, in controlling VAT fraud. The revised Presidency proposal now on the table enjoys a wide measure of support amongst Member States and looks as if it could provide the basis for an agreement, possibly without further discussion. Crucially the revised proposal does not allow for any decisions to be made by QMV and would also be quick and efficient.

In common with the Commission’s original proposal the revised QRM would provide for a domestic reverse charge. This would take the form of an option which a Member State could choose to exercise. To do so they would notify their intention to the other Member States and the Commission, providing the information set out on a standardised form. Once all the relevant information has been provided the Commission would have one month to consider whether the notification met the criteria for applying the option. Member States would be able to register their views with the Commission during this time. By the end of the month the Commission, taking into account the views expressed, would either confirm they had no objection to the use of the option or would notify an objection. In the latter case the Member State would not be able to proceed but in the former instance the Member State would implement the option for a period of 9 months. The legislation envisages that the Member State would apply for a normal derogation at the same time as notifying the option and that the timetable for the production of the proposal by the Commission would be shortened to six months.
The system would be temporary, lasting until December 2018 and subject to a review, reporting at the end of 2017. This would be consistent with the deadlines in the accompanying “Reverse Charge Mechanism” (RCM) proposal and with putting pressure on the Commission to work towards their VAT strategy objective of reform of the VAT system to make it more robust and more fraud-proof.

Such a QRM is attractive. It would be as quick as the QRM outlined in the Commission’s proposal. It would also allow for the same reverse charge. The envisaged procedure eliminates, however, the use of a comitology committee and any associated qualified majority voting. The Member States would have greater direct involvement in the assessment of the notification than envisaged under the original proposal, whilst the short lifespan of the notification, combined with the accelerated timetable for the replacement, ensure that a normal derogation is more quickly in place than would usually be the case.

As I mentioned above, the European Council is looking for agreement on this dossier at the ECOFIN on 21 June. There is thus quite some political impetus behind the proposal. The current proposal is attractive and represents a significant improvement on the original, while agreement would deliver two useful anti-fraud measures (the QRM and the linked RCM). I am currently consulting colleagues to ensure that the compromise does not raise any wider issues but, in view of the urgency, thought that it would be helpful to give you this update and an indication of the timetable at this stage.

3 June 2013

Letter from the Chairman to David Gauke MP

Thank you for your letter, dated 3 June 2013, on EM 13027/12: VAT: Quick Reaction Mechanism. The House of Lords European Union Sub-Committee on Economic and Financial Affairs considered this document at its meeting on 11 June 2013.

We are encouraged that you have managed to achieve such progress in relation to this dossier. However we would like you to expand on the compromise proposal. We understand that, throughout the negotiations, you have sought to retain the principle of unanimity in relation to tax matters. We recognise that this compromise proposal would allow for greater Member State involvement in a decision relating to the Quick Reaction Mechanism. However, we are not clear what would happen if a Member State were to object. Would the Commission be obliged to take this into account or could this objection be ignored?

Since you indicate that agreement is likely to be reached at ECOFIN on 21 June, and many of the outstanding issues have been resolved, we are content to clear this document from scrutiny. However, in our order to come to a clear view about the impact of the proposal, we expect to receive further details from you about the compromise proposal and a response to our questions before the ECOFIN meeting takes place.

11 June 2013

Letter from David Gauke MP to the Chairman

Thank you for your letter of 11 June acknowledging the progress achieved in negotiations and confirming that your Sub-Committee is content to clear this document from scrutiny.

I agree with you that the compromise proposal set for agreement at ECOFIN would indeed allow for greater Member State involvement under the Quick Reaction Mechanism. Under the Commission’s original proposal, other Member States would have had no input prior to the Commission sanctioning the introduction of a reverse charge by a Member State. They would instead have had to amass a qualified majority to repeal such a measure already introduced. Under the compromise proposal, all Member States are kept fully informed of any one Member State’s notification and the information supplied in relation to a special measure. They then have the opportunity to submit views to the Commission as it appraises the notification. It should also be noted that the compromise proposal makes a link to the existing derogation system under the VAT Directive, such that any further application of the reverse charge beyond the special measure’s nine months would require a Council implementing Decision decided by unanimity.

You specifically ask what would happen if a Member State were to object to a special measure notification. Under the compromise proposal, the Commission is obliged to take this into account when appraising the notification, but ultimately has the discretion to object or not. Were a Member State’s objections sent to the Commission well-founded and backed up by clear evidence, or were a large number of Member States to submit objections to the notification at this stage of the procedure, then that is more likely to influence the Commission’s appraisal accordingly and be a factor in any negative opinion where the Commission objects to the special measure; should a special measure be
cleared by the Commission under similar circumstances, and were such objections by other Member States to persist, it is likely that a subsequent Council implementing Decision would not be agreed easily.

The compromise proposal includes under Article 3 a provision for a review of the Quick Reaction Mechanism before 1 January 2018, so that the process and impact of the mechanism in addressing sudden and massive fraud may be examined.

I hope you find this information helpful.

12 June 2013

Letter from David Gauke MP to the Chairman

I am grateful for your flexibility and understanding in considering and clearing EM 13027/12 from scrutiny so speedily following my letter of 3 June. I subsequently wrote on 12 June with responses to the points you had raised on your clearance letter of 11 June.

You will be interested to learn that, having been able to raise our scrutiny reservation, the VAT Fraud Package proposal received political agreement at the ECOFIN meeting on 21 June in Luxembourg.

27 June 2013