UK IN A CHANGING EUROPE

UK-EU REGULATORY DIVERGENCE TRACKER

7th edition – May 2023

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INTRODUCTION

This is the seventh edition of the UK in a Changing Europe's regulatory divergence tracker, covering developments since January 2023. There are seven cases of active divergence (where the UK, or some part of it, changes its rules); two of active convergence (where the UK, or some part of it, aligns to EU rules); 17 of passive divergence (where the EU changes its rules and the UK, or some part of it, does not follow); and one of internal divergence (changes in rules between different parts of the UK).

In addition, the Windsor Framework is significant case of 'managed divergence': a UK-EU agreement which alters the regulatory border between Great Britain (GB) and Northern Ireland (NI), as created by the Protocol. As well as minimising customs procedures, it is now possible, in many cases, to export food, plants and medicines which meet UK standards (rather than EU ones) to NI from GB, and certain UK VAT and state aid reforms can also apply in NI. This means the UK can now pursue regulatory divergence in these areas without imperilling GB-NI trade, and, likewise, GB exporters will not have to align with so many new EU regulations to maintain access to the NI market.

Yet the early signs are that the practical impact may be limited. Following new **EU restrictions on arsenic levels in food**, GB and NI companies have said they will adhere to the new EU rules, in order to maintain EU market access, even though the Windsor Framework negates the need to do this when trading GB-NI. This is an early example of the 'Brussels effect' - where companies comply with EU rules to maintain access to the single market – trumping the Windsor Framework in shaping business behaviour. A similar test could occur once the EU implements its **import ban on goods treated with two 'neonicotinoid' pesticides**. Another issue is that GB exports to NI must still follow EU law in many areas, for example on animal and plant health, and on manufactured goods - where the EU is an active regulator. This means GB exporters to NI (and, indeed, the EU) will have to meet potentially significant new administrative and financial costs entailed by the EU's planned new **general product safety regulation**. Similarly, they would have to comply with the planned **restrictions on up to 10,000 synthetic chemicals** affecting a wide range of goods including textiles, cosmetics, car batteries and cookware. Will the 'Brussels effect' mean that British companies adhere to these changes, once implemented, to maintain EU market access? Or might Northern Irish Assembly Members, if restored, apply the 'Stormont Brake' to block the application of changes like these in NI?

In terms of active divergence, one key development is the **updated environmental land management scheme** in England. This subsidy scheme - which rewards farmers for sustainable practices - has long been touted as a benefit of Brexit but has been slow to implement, leaving farmers financially precarious. The update provides clearer detail on what actions farmers can take for what reward, and could help the scheme properly take off. There have also been developments in trade policy, with the UK joining the **CPTPP trade bloc**. This removes almost all tariffs on trade with eleven other countries, though there are concerns that liberalised trade will undermine UK food and environmental standards, for example by incentivising imports of Malaysian palm oil at a time when the EU is imposing a de facto ban on it.

Though Sunak's government has so far pursued les active divergence, it appears to have a clearer plan for regulatory reform. Following the articulation last November of five priority 'growth industries' for reform in 2023, the Chancellor has now announced plans for **fast-tracking approvals for new medical technology**; a **regulatory sandbox for AI development**; an **updated regulatory framework for crypto-assets**; and **regulating 'buy-now-pay-later' credit platforms**. What these have in common – apart from a focus on emerging technologies – is that they do not deviate significantly from EU regulation, instead seeking to be more flexible or less risk-averse than the EU in limited, defined areas. In particular, divergence will focus on early-stage regulation, to try and boost innovative development; followed by convergence at later stages; reflecting a that recognition alignment with EU standards for finished goods will ultimately help UK tech exports.

This, however, remains theory rather than practice. There are several other areas where the UK has higher ambitions than the EU - on **HGV emissions reductions**, **restrictions on bottom-trawling** and **energy efficiency targets** – but where the EU has recently taken more concrete action towards achieving its goals. The EU also continues to be more active in regulating new corners of tech markets, be it **regulation of 'U-space'** to facilitate drone traffic, **ensuring the safety of products in online marketplaces** like Amazon and eBay, or pushing **big tech companies to pay for the upkeep of internet networks** (of which they are the predominant users). The UK is likely to move in a similar direction (albeit more slowly) in the first two areas - but may see an opportunity to attract more tech investment by not imposing EU-style network maintenance charges. The UK government has also exercised its freedom not to follow a Court of Justice of the European Union ruling which in effect bans **publicly accessible registers of beneficial ownership**.

The most significant EU measures in this edition are, however, its response to the US Inflation Reduction Act (IRA - a $369bn package of tax breaks and subsidies for green investment in the US) which prompted EU concerns about the competitiveness of its own industry. It has swiftly responded with targets to majorly increase domestic green technology production (under the **Net-Zero Industry Act** and **Critical Raw Materials Act**) supported by a relaxation of state aid rules (the **Temporary Crisis and Transition Framework**) to help fund investment. To many, the EU investment plans are a wake-up call for UK green industries, which risk being unable to compete with EU, US and Chinese firms in receipt of heavy subsidies. Yet the UK government says a full response will arrive only this autumn, preferring targeted private capital to going 'toe-to-toe' in a subsidy race. Indeed, some argue that the EU's green production targets are too high and could slow its net-zero transition while increasing consumer costs, yet there is little evidence of the UK having thought about what its strategic priorities will be, nor how it will attract investment at a time of intense global competition. Action so far has instead focused on energy security and price control, through measures to **reduce energy costs for heavy industry** and to **'rebalance' gas and electricity prices** via contracts incentivising the use of renewables (though in both cases the EU/member states have moved in a similar direction, more quickly).

The surge in EU subsidies could also be in violation of 'level playing field' commitments under the UK-EU Trade and Cooperation Agreement, yet the UK has shown no sign of wanting to raise this as an issue. This could stem from a British desire to maintain more cordial EU relations – and indeed avoid invoking a trade war – following the Windsor Framework agreement. In this context, it will be interesting to watch whether the UK seeks greater formal or informal alignment with other EU reforms which correspond with its own priorities. Overlap could be found as the UK consults on a potential **Carbon Border Adjustment Mechanism** and the EU expands its **emissions trading scheme**, or on the European Defence Agency's plans **joint procurement of ammunition**.

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Joël Reland, 3 May 2023

ISSUE	SOURCE & STATUS	IMPLICATIONS & IMPACT	TIMELINE & REGION
1. TRADE **MANAGED DIVERGENCE** **INTERNAL IMPACT** *The Windsor Framework.*	**Summary:** The Windsor Framework agreed by the UK and EU revises the terms of the Protocol on Ireland/Northern Ireland. This has significant implications for regulatory divergence between Northern Ireland and Great Britain. Under the original Protocol, Northern Ireland remained aligned to EU single market regulations, in order to guarantee a free flow of trade across the Irish border. This in turn created trade friction between GB and NI, in terms of customs checks and declarations on GB exports to NI, and suppliers having to ensure compliance with EU regulations which they did not have to meet to sell to the rest of UK. The Windsor Framework reduces this trade friction in a couple of ways. First, it simplifies customs processes. Traders who can prove their goods are 'not at risk' of entering the EU (through real-time data tracking goods movements) will be able to use a new 'green lane' which requires customs paperwork to be submitted only monthly rather than on each consignment, and eliminates checks on	**Impact:** The Windsor Framework, if applied, should reduce the extent of divergence between GB and NI both now and in future. This would reduce the financial and administrative costs associated with GB exports to NI, which should boost the level of trade across the Irish Sea. The trade costs created by the original Protocol meant that some GB exports to NI became loss-making or less commercially viable, leading to an overall drop in NI imports from GB. However, the main impact is not necessarily the macro effect on trade. Indeed, 50% of people in NI currently think the Protocol has been positive for the economy, whereas 39% say it has been negative. NI is the only part of the UK still which retains access to the EU single market, and modelling by the University of Sussex suggests NI's economy will be 2.2% larger than had Brexit not happened. Perhaps more crucially, the Framework addresses the significant 'trade diversion' of certain goods (like sausages, cakes with the E171 food colouring, seeds or medicines) which were acutely affected by the original Protocol. Some	**Timeline/region:** The UK and EU must translate the Framework into their respective legal orders. This will include a vote in the UK Parliament. Once adopted, the provisions would take effect from Autumn 2023.

	goods (except where there is a suspicion of criminality) and requirements to prove the 'nationality' of a good's content. Agrifood (plant and animal) products still face some additional requirements, though these are significantly simplified. Supermarkets and many other businesses delivering food and drink for retail will now be able to complete a single, digital document per consignment confirming that goods are staying in Northern Ireland (instead of up to potentially 500 certificates per truck) and there will be no on-site checks or wider 'attestation' documents. 'High-risk' products (like fresh meat and dairy which could spread diseases into the EU) will be labelled as such from October 2023, reducing inspections of lorries from 100% at present to 10% in 2023, and 5% in 2025. A second key change is the EU agreeing to carve-outs where certain imports from GB which meet UK (not EU) standards can be placed on the market in NI (as long as they are labelled as not for sale in the EU). Imports of retail food and drink will be subject to UK rules on public health, safety, marketing, organics, labelling and genetic modification (though EU standards on animal and plant health still apply). This disapplies over 60 EU food and drink rules in NI, and	of these were impermissible in NI (unless temporarily exempted) while others were subject to new, convoluted approval processes. Under the new Framework, many such goods would be subject to much simpler export processes or fall under UK-wide regimes, which should boost and secure supply long-term. This is especially significant for vital goods like food and medicines, where NI is highly dependent on supplies from GB. Another question is what the Framework means for overall divergence at the UK-EU level. Prime Minister Boris Johnson has called the original Protocol (which he negotiated) is a 'drag anchor' on divergence. Under the original Protocol, many cases of UK divergence from EU rules implied new GB-NI divergence and thus trade friction; and NI could not benefit from UK rule changes like removing VAT on solar panels. The Windsor Framework does not end the application of EU law in NI, but it does reduce the scope of it. This means fewer areas where UK-EU divergence also means to GB-NI divergence, and more cases where UK reforms will apply in NI. Thus, the proverbial 'drag anchor' has been lightened, but not removed. Whether it encourages the UK	

	means many potential future EU rule changes won't apply, maintaining higher alignment with the rest of the UK. Plants moving from GB to NI will now move on the UK, not EU, plant passport scheme and banned items (like seed potatoes) will once again be available. Manufactured goods, by contrast, will still have to adhere to EU law wherever it applies in NI. The UK government notes there are only 'minor differences' between the UK and EU on 0.3% of goods standards. New medicines are to be licensed for use in Northern Ireland via a UK-wide scheme, and medicines in NI no longer have to meet EU labelling and anti-counterfeit requirements, reducing the risk of supply shortages through suppliers failing to complete the necessary documentation. No similar, permanent solution has been found for veterinary medicines. A few specific UK VAT and excise changes, like the removal of duties on solar panels and the reformed regime for alcohol duties, will now apply in NI, and the UK has secured some greater flexibilities for future reform. However, in	government to pursue greater divergence remains to be seen. One other divergence-related impact of the Framework would be to give NI representatives a greater say in whether and how updated EU legislation should apply in NI. Under the original Protocol, the UK has a say over whether or not *new* EU legislation should apply in NI, but not over reforms of already applicable legislation. Such reforms can increase GB-NI divergence: for example, the planned update the EU 'ecodesign' regulation would impose new efficiency and labelling requirements on IT goods entering NI from GB. In response to this issue, the Windsor Framework introduces a 'Stormont Brake' which is triggered when 30+ NI Assembly members from 2+ parties register their objection to an updated EU regulation. The UK government would then notify the EU, automatically suspending the updated rule, pending further discussions. If no solution is found, the regulation is permanently suspended in NI. This might sound like a strong veto allowing NI to systematically disapply new EU regulations and thus potential new divergence with GB, but there are a couple of	

	many cases goods moving from GB to NI are still subject to EU VAT rules. On subsidies, EU state aid rules still apply to subsidies in Northern Ireland that might affect trade with the EU, but new tests will be established to prove a 'genuine and material link'. This is intended to significantly limit the application of EU state aid rules, though the legal status of the declaration is uncertain. Finally, pets can now travel from GB to NI (but not on into Ireland) with a lifetime-lasting document, rather than needing individual certifications for each journey.	factors which might limit its use. First, it is explicitly a tool of last resort, and the relevant rule change must have a 'significant impact specific to everyday life in a way that is liable to persist'. Second, the EU would be entitled to take 'appropriate remedial measures' where the Brake is triggered. This might be new trade bureaucracy (checks or labelling on goods imported from GB to NI where EU rules have been disapplied) or even trade sanctions against the UK.	

2. AGRICULTURE **ACTIVE DIVERGENCE** *Update to Environmental Land Management Scheme in England.*	**Summary:** In January 2023 Defra updated its environmental land management system (ELMS) in England, which is replacing the EU's Common Agricultural Policy (CAP) of subsistence payments for farmers, providing more detail on the payments to be made available. ELMS, which was first announced in 2018, has the overarching aim of providing 'public money for public goods' rather than basing payment on land being farmed. The latest update provides outlines the specific actions farmers will have to take to qualify for different payments. There are 280 measures in all, across three different schemes. The 'Sustainable Farming Incentive' rewards farmers for adopting sustainable practices which 'protect and enhance the natural environment alongside food production'; 'Countryside Stewardship' supports 'targeted actions relating to specific locations, features and habitats'; and 'Landscape Recovery' rewards 'bespoke, longer-term, larger scale projects to enhance the natural environment'. Payments range significantly, for example from £3 per 100 metres for assessing and recording hedgerow condition, to £537 per hectare for creating fen on lowland peat soils. Farmers can undertake multiple actions simultaneously.	**Impact:** Plans for ELMS have previously been praised for being much more ambitious in their pursuit of environmental and sustainability goals than the EU CAP. However, major questions have also been asked about the impact on farm incomes. CAP basic payments constituted 60% of farmers' net income before Brexit but support was cut by an average of 22% last year, with the reduction set to rise to 36% this year. ELMS is yet to significantly make up the shortfall, with government reporting that 32,000 businesses accessed one of the schemes in 2021/22 - equivalent to around a third of all farmers in receipt of CAP basic payments. Defra's latest update is thus a crucial moment for the implementation of ELMS. It gives England's farming sector a much clearer framework and timeline for the new payment scheme. The Country Land and Business Association said the announcement 'will encourage many arable farmers to take the leap into the new agricultural schemes', but also warned that government will have to ensure the scheme is 'accessible to all types of farms'. This suggests that concerns remain within the industry around delivery, ease of applications and timeliness of payment. Some commentators have also questioned whether the structure of the payments	**Timeline/region**: Defra's announcement applies to England only, with separate new agricultural payment schemes being developed in Scotland, Wales and Northern Ireland.

	Farmers have to apply for payments, with the first application windows having opened in February 2023 and the rest gradually being rolled out across this year and next.	will, as promised, create a more 'level playing field' where smaller farms receive equivalent support to larger ones: for instance because support payments for some of the more economically precarious sectors may not be sufficient to meet their needs. Scotland, Wales and Northern Ireland are developing their own new payment schemes, which have been subject to similar concerns about a lack of clear definition and support.	

3. CONSUMER PROTECTION **ACTIVE DIVERGENCE** *UK regulation of 'buy-now-pay-later' offers and updated EU consumer credit directive.*	**Summary:** The Treasury has announced plans to regulate 'buy-now-pay-later' (BNPL) offers, where consumers pay for a product through a series of interest-free instalments covering a period of up to 12 months. At present, these loans are exempted from consumer credit rules which apply in many other cases. The Woolard review for the Financial Conduct Authority (FCA) looked into this 'unsecured market' and found that the volume of BNPL offers almost quadrupled in the first year of the Covid pandemic, during a boom in online shopping. It concluded that this growth in the market carries a range of potential harms. In particular, there was found to be an increasing risk 'that consumers could take on unaffordable levels of debt' because it is possible to take out several BNPL agreements at once with different providers, and many providers plan to expand BNPL offers to higher-value products or in-store purchases. The review therefore concludes that 'it would be relatively easy to accrue around £1,000 of debt' and many customers thus risk taking on unaffordable levels of debt. Moreover, it	**Impact:** The move has been widely welcomed by consumer rights groups, despite some criticism of the 'painfully slow' development of legislation which was first proposed in 2021. Nonetheless, the UK and the EU are the first two major authorities to specifically regulate BNPL offers. There is significant alignment between the UK and EU approaches to regulation. The EU is in the process of updating its consumer credit directive – which sets harmonised rules on the provision of credit – to cover BNPL products, interest-free loans and loans under €200. Similarly to the UK proposals, the updated directive would require BNPL lenders to assess a consumer's creditworthiness and to provide consumers with clear, accessible information about the total costs of the credit they are taking on. There could, however, be some divergence over the respective scope of UK and EU regulations. In the UK, BNPL offers for single items worth under £100 will be exempt from regulation, whereas the EU is removing exemptions for loans below €200. This lack of coverage for relatively small loans means somewhat weaker consumer protections in the UK than the EU. Yet the UK government might argue that it is taking a more flexible approach which does not apply	**Timeline/region**: HM Treasury's consultation closed in April 2023. The government will next provide a summary of responses and next steps. The update to the EU consumer credit directive is subject to political agreement before formal adoption procedures.

	is invisible to credit rating agencies when they make assessments about the suitability of providing other forms of credit to an individual. The government has now published a consultation paper on draft legislation for BNPL markets. It proposes that providers of BNPL offers be brought under the supervision of the FCA, meaning they will have to obtain FCA authorisation for offers, carry out affordability checks on potential customers and ensure customers are treated fairly. Companies who fail to adhere to rules could be banned from operating. The FCA has also previously raised concerns about adverts for BNPL loans which do not convey the consequences of failing to repay. The proposed reforms would see the advertising and promotion of BNPL offers be subject to the financial promotions regime (which sets standards on how offers are communicated). Customers would also have the right to ultimately take complains to the Financial Ombudsman Service. The government proposes, however, that regulation should not apply to all BNPL offers. Its draft paper sets out that legislation should apply only to third-party lenders, i.e.	regulation which detracts from the use of innovative payment methods for relatively small-sum transactions. Potentially more significantly, the draft UK plans apply only to third-party providers, meaning that, in the UK government's own words, 'a potentially large number' of merchants entering directly into BNPL agreements with customers will not be subject to new regulation. The EU's initial proposals from 2021 outlined a similar exclusion for 'deferred payments', which it defines as 'a commercial practice [which] allows the consumer to pay for goods or services in instalments, free of interest and without a third party offering credit'. Whether this exemption makes it into the official draft text remains to be seen. Even if the UK and EU do develop similar exemptions, the exact wording of their respective legal texts will matter. This is because BNPL markets are evolving rapidly, and future payment options may or may not be considered 'third party' or 'deferred payment', depending on exactly how these terms are legally defined. For example, Apple is planning to roll out its own payment system (called 'Apple Buy Later') allowing customers to spread the cost of a purchase across four instalments over six weeks. This could	

	financial services companies like Klarna which facilitate BNPL offers (managing the agreement and taking on the credit risk) on behalf of merchants. The government deems that regulating BNPL deals which are made directly between a merchant and customer would create a 'disproportionate… burden of regulation' for a 'potentially large number of small, independent merchants', which could 'possibly lead to them stopping offering useful, low-risk agreements to consumers as a result of needing to become authorised'.	spark similar moves from competitors, including major mainstream banks. It is not clear whether such new providers of BNPL offers would be considered third parties or not under future UK and EU legislation (for example, if Apple Buy Later was used for purchasing Apple-related goods it would not appear to involve any third party; but this distinction is less clear if it used to buy another company's app from the Apple App Store). Much will depend on the wording of future legislation, and it is not inconceivable that Apply Buy Later or other similar schemes might be exempted from regulation in one of the UK or EU but not the other. This is unlikely to have any major economic effects, but would create disparities in comparative levels of consumer protection.	

4. DIGITAL & DATA **ACTIVE DIVERGENCE** *Pro-innovation Regulation of Technologies Review: Digital Technologies.*	**Summary:** Alongside the Spring Budget, the UK government published Pro-innovation Regulation of Technologies Review: Digital Technologies, by Chief Scientific Adviser Sir Patrick Vallance. The Review identifies 'digital technologies and applications which require a distinct regulatory approach', and makes nine recommendations, all of which the government is taking forwards. The first of these is that government should develop a 'multiregulator sandbox for AI to be in operation within the next six months'. A sandbox is a 'live testing environment', where certain regulations are relaxed in order to allow companies to test and innovate new products and services. The time-limited AI sandbox will focus on areas close to a 'major breakthrough' which offer solutions to societal challenges or where the UK is poised to be a world leader'. It is suggested that it 'could initially focus on areas where regulatory uncertainty exists, such as generative AI, medical devices based on AI'. The Review states that 'our engagement with industry [shows] there is clear appetite for the UK to rapidly launch an AI sandbox to enable experimentation and encourage greater co-operation between regulators'. Because of the distinct features of AI technology and fast pace at which it	**Impact:** The Vallance Review and AI white paper reflect the priority which the Sunak government is giving to emerging sectors when it comes to regulatory divergence. The Review outlines the rationale: sectors like digital technology and AI will be vital to UK growth, but do not fit naturally within existing regulatory structures. This gives the UK the opportunity to get ahead of others, by being quicker and nimbler in its creation of regulation, making it an attractive place for investing in technological development. The AI sandbox reflects this thinking. The Review states that 'for emerging digital technologies, the industry view is clear: there is a greater risk from regulating too early'. Sandboxes thus seek to allow experimentation and innovation in a controlled setting, with regulators learning together from this to gradually build up regulations and standards. This stands in contrast to the EU's approach, which has sought to impose more comprehensive definitions and frameworks for AI technologies from the outset. The hope for the UK is that its more flexible, piecemeal approach to rule-setting will allow it to get ahead in setting regulatory norms for technologies as they develop, making it a more attractive environment for developers to invest in, and potentially	**Timeline/region**: The UK government says it will take forward the recommendations, though no timescale has been provided.

	develops, the Review notes it is hard for regulators to keep up with the nature and pace of change. Sandboxes thus offer a more flexible space for innovation alongside the 'continuous refinement' of regulation. The Review also argues that AI poses challenges because it cuts across the remit of multiple regulators, meaning that regulation can become overlapping and contradictory; hence the sandbox will be overseen by four regulators (Ofcom, the Information Commissioner's Office, the Competition and Markets Authority, and the Financial Conduct Agency). The UK government has said it will engage regulators immediately to prepare for launch and has since published a white paper on 'a pro-innovation approach to AI regulation'. In line with the Vallance report, it says that responsibility for AI governance should not be given to a single new regulator, with existing ones instead to be guided by five principles. Regulators are expected to lay out practical guidance to affected sectors in the coming year. This principles-based approach to regulation - rather than setting out a fixed definitions of technologies and behaviours, as the EU has done - is designed to make rule-making more flexible, and was explained in a previous divergence tracker.	shaping industry standards. There is, however, an acknowledgement that harmonised regulation is preferable for more developed technologies, as companies will want to sell these into as many markets as possible. The Ada Lovelace Institute notes, however, that the flexible approach outlined in the white paper carries risks, as it will not have any statutory footing: 'this means no new legal obligations on regulators, developers or users of AI systems, with the prospect of only a minimal duty on regulators in future'. It further notes that substantial investment will be needed in existing regulators to support their new responsibilities. Meanwhile, a partner at the law firm Dentons argues that the UK's lighter-touch approach makes it an 'outlier' globally, with others including the US, EU and China passing more specific laws. While this could give the UK some advantages as a location for development, it also carries the risk of weaker user protection against unwanted effects of AI.	

5. DIGITAL & DATA / FINANCIAL SERVICES **ACTIVE DIVERGENCE** *Phase 2 of UK regulatory regime for crypto-assets.*	**Summary:** HM Treasury has started to set out the second phase of its approach to regulating crypto-assets. Phase 1 – covered in a previous divergence tracker – aimed to introduce a regime to regulate fiat-backed stablecoins (which are considered more reliable as they hold bank-based financial reserves) used for payments through the Financial Services and Markets Bill (FSM Bill - also covered in our fifth divergence tracker). Plans for Phase 2 are set out in a consultation paper, which shows the intention to regulate broader crypto-asset activities, including the trading of and investment in crypto-assets. Included in this paper are plans for crypto activities associated with higher degree of risk such as crypto exchanges (which covers firms like FTX which dramatically collapsed late last year) to be subject to specific regulations such as detailed data reporting requirements and establishment of bankruptcy process. In addition, steps are being taken to ensure market abuse practices specific to crypto are caught under existing financial regulations. These include 'pump-and-dump' schemes (which attempt to artificially increase the price of an asset using false and misleading information) and wash-trading (where fictitious transactions are carried out to give	**Impact:** On the one hand, the UK's second phase of crypto-asset regulations continues its stated ambition of being 'more nimble and proportionate' than the EU, with government pointing to the fact that is using secondary legislation to bring crypto regulation into existing financial services regulation, rather than 'hard-coding' an entirely new set of regulations, as the EU is doing. The fifth divergence tracker discussed the potential pros and cons of this less comprehensive approach, which generally seeks to encourage greater investment in and use of cryptocurrencies and related technologies by imposing fewer wholesale restrictions on practices. For example, the EU has de facto restricted the use of 'decentralised finance' technologies on which crypto-assets rely, by not allowing stablecoin issuers and crypto-asset service providers to grant interest to holders of their tokens. The UK, by contrast, appears to be planning no such restrictions. But on the other hand, it should be acknowledged that Phase 2 of the UK regulation also marks a convergence with the EU in establishing a more wide-reaching regulatory regime for crypto, in contrast to the Phase 1 which focused quite narrowly on stablecoin used for payments. Phase 2 will	**Timeline/region:** EU rules still require a final vote in the European Parliament and are expected to take effect this summer. The Treasury's consultation is open for comment from crypto firms, financial institutions, academics and others until 30 April.

	the false impression of higher trading volumes, thus increasing prices).	develop a regulatory approach to a wider suite of crypto-assets through the FSM Bill; though it differs from the EU model as implementation moves in stages rather than as a single policy package. Yet in some respects the UK seeks to be even more explicit in areas that the EU leaves ambiguous, such as requiring crypto exchanges to publish a white paper of investor disclosures for widely-trades assets like Bitcoin. Finally, the Treasury's consultation paper implicitly notes some potential challenges to long-term divergence between the EU and the UK crypto-asset regulations. For example, the 'globalised and borderless' nature of decentralised finances makes it hard for 'typical systems of financial services regulation' to determine when activities fall under its jurisdiction. The paper notes that 'over time market abuse prevention and enforcement capabilities could be enhanced through the adoption of new technologies and international coordination'.	

6. ENERGY **ACTIVE DIVERGENCE** *UK financial support for energy-intensive industries.*	**Summary:** The UK government has announced plans for new financial support for 300 businesses, employing 400,000 people, to help with high energy costs. Called the 'British Industry Supercharger', it is aimed at sectors especially exposed to the cost of electricity: including steel, metals, chemicals and paper. The three main measures proposed are a reduction in network charges for electricity supply; a reduction in costs for maintaining generating capacity; and a potential increase – from 85% to 100% - in exemptions on costs from renewable energy obligations. The support is expected to eventually be paid for through increases in consumer energy bills – on average £3-5 per household per year. The measures are being consulted on this spring, with the intention of rolling them out in spring 2024. In the meantime, businesses have access to the Energy Intensive Industries Compensation Scheme, which was extended last year until 2025. It reduces the costs applicable to businesses with high energy usage under the UK Emissions Trading Scheme and Carbon Price Support mechanism.	**Impact:** The aim of the 'Supercharger' is to reduce the gap in what British heavy industry pays for electricity compared to European counterparts. There is no EU equivalent, but some member states have taken steps to shelter their industry from rising energy costs, supported by looser EU state aid rules. For example, Germany has spent €265bn to support businesses and households, including a measure which covers around 70% of industrial companies' gas costs. The French government has renationalised the energy company EDF, significantly limiting gas and electricity price rises, and recently announced €2bn to support high energy-consuming companies with their costs. The per capita level of energy support provided by the UK (to households and businesses) is about average by EU standards – roughly in line with France and Italy. However, the decision to introduce the supercharger reflects the fact that energy-intensive industries still face higher costs in the UK. Britain industry is more exposed due to its significant dependence on gas for producing electricity. Around 40% of UK electricity is produced from gas, compared to 15% in Germany, and last summer it was nine times more expensive to produce electricity from gas than renewables.	**Timeline/region**: The plans will be consulted on this spring, and are expected to be rolled out in spring 2024.

7. TAXATION **ACTIVE DIVERGENCE** *Changes to UK alcohol duty structure.*	**Summary:** In his Spring Budget the UK Chancellor Jeremy Hunt announced an increase in 'draught relief', which reduces the duty paid on draught alcohol (from containers of 20 litres or more) at 'on-trade' venues (like pubs). From August 2023, the relief on draught beer and cider products will rise from 5% to 9.2%, and for 'wine, spirts-based and other fermented draught products' it will rise from 20% to 23%. Because alcohol duties will increase by the RPI rate of inflation at the same time, the increase in draught relief in effect freezes the duty applied to those products at the same level as now. The government will also implement changes to 'rationalise' the structure of alcohol duties from August 2023. This proposal was first announced in the 2021 Autumn Budget (covered in a previous divergence tracker), and will see reduced rates for some lower-strength products and increased rates for some higher-strength ones. For example, a bottle of wine at 14% ABV will now accrue a higher duty than an 11% ABV bottle.	**Impact:** The Chancellor noted that the increase in draught relief would not have been possible in the EU. The structure of EU alcohol duties means that the duty applied to beer (including any allowance for a reduced rate) is set by its alcoholic content rather than by the quantity of the finished product. Similarly, the wider 'rationalisation' of alcohol duties would not have been possible within the EU, as duties on wine above 8.5% strength are determined by the volume of the finished product, not its alcoholic content. The increase in draught relief is designed to shelter pubs from the inflation-pegged increase in alcohol duties which applies from August, increasing supermarket prices. Yet some drinks sold in supermarkets will nevertheless become cheaper due to wider reforms to the structure of alcohol duties. For example, the price of a bottle of 12% ABV sparkling wine is expected to fall by 19p from 1 August (because it is relatively low-strength). On the other hand, the price of a bottle of port is expected to rise by £1.29. Incentivising the consumption of lower-strength products has potential public health benefits. And because of the Windsor Framework, the reforms will now apply in Northern Ireland, which was not possible under the original Protocol.	**Timeline/region**: The new reforms all come into force in August 2023.

8. TRADE **ACTIVE DIVERGENCE** *UK joins CPTPP trade bloc.*	**Summary:** On 31 March 2023, the UK announced it would join the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP). This makes the UK the 12th member of the free-trade bloc which, with the UK having joined, now accounts for 15% of global GDP. The 11 other members of the bloc are: Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, and Vietnam. Membership of the CPTPP provides almost complete liberalisation of tariffs for partner countries except for certain sensitive industries (ie. Japanese rice or Canadian dairy). As a result, 99% of Britain's exports to CPTPP countries will now be eligible for zero tariffs. The CPTPP does not have a single market for goods and services, meaning there is less regulatory harmonisation compared to the European Union. Instead, regulatory cooperation comprises of a narrower set of shared rules for domestic regulations concerning trade; and conformity assessment obligations — which will require some products to be certified by independent assessment bodies to prove that they meet UK standards.	**Impact:** The UK's accession to the CPTPP is not expected to have a major impact on its trade overall. The UK already has bilateral trade deal with 9 of the 11 other member countries of the CPTPP, Malaysia and Brunei being the only countries that the UK had no previous agreement with. According to the UK government's own analysis, joining the CPTPP will add 0.08% to UK GDP long-term. This is one fiftieth of the Office for Budget Responsibility's estimate of what Brexit has so far cost the UK's economy. However, this could increase if more countries join —Thailand and South Korea may both become members in the future. There will be some benefits for specific UK exporters. For example, previously high tariffs imposed by Malaysia on British whisky and cars will be removed, which opens up a new market for companies in this area. The UK's meat and dairy industries are also expected to benefit. Conversely, the UK has made some concessions on environmental protection, for example by agreeing to Malaysia's demand that UK tariffs on its palm oil products be cut to zero (at the same time as the EU is implementing a de facto ban on such imports due to its links to deforestation).	**Timeline/region**: The formal signing of UK membership is expected later in 2023.

	The CPTPP also imposes a single set of 'rules of origin', requiring a certain proportion of a good's components to be of 'local' origin, in order to qualify for tariff-free trade. These rules are 'cumulated', meaning that, for a good to qualify as 'local', it can originate from any CPTPP member state – rather than just the country exporting the good. There are some provisions on services, such as the removal of regulatory barriers for various service organisations and reduced tariffs on financial services. Membership will also facilitate more efficient data flows between the UK and partner countries. CPTPP countries are committed to removing data localisation requirements, which will allow businesses to deliver services more efficiently without the need for establishing overseas data storage centres or computing facilities. There is no equivalent to the European Court of Justice for the CPTPP, meaning no formal court responsible for ensuring that countries fulfil their obligations or handing out fines if they fail to do so. Instead, an ad-hoc arbitration panel will be convened in the case of a dispute between participants in the free-trade area.	CPTPP membership does not, however, automatically entail major regulatory divergence with the EU. Indeed, many CPTPP members have trade agreements with the EU, and the UK has opted to maintain its existing regulatory standards on food and animal welfare, even though this will prevent it benefiting from some liberalised trade terms under the CPTPP. For instance, the government says it will not amend its food standards to allow imports of hormone-treated beef from Canada; nor will it import pork from Mexico, which has lower animal welfare standards. One area of possible UK-EU divergence is on data regulation. The CPTPP requires members to permit the cross-border electronic transfer of data, which could in turn compromise the EU's data adequacy decision for the UK, which allows data to flow freely between to the UK and EU and is of considerable economic benefit to the UK services industry. It should be noted, that other CPTPP members have maintained their EU adequacy decisions. Nevertheless, there is potential for greater divergence with EU regulation over time, as the CPTPP rulebook develops. CPTPP membership is also effectively incompatible with membership of the EU's customs union, as this requires	

		alignment with the EU external tariff regime. Some Brexit supporters have argued that joining the CPTPP makes it harder for future governments to re-join the EU's customs union and/or the EU itself, as it would necessitate British withdrawal from the CPTPP, damaging those trading links. CPTPP accession also gives some British manufacturers greater flexibility over where they source goods from in their supply chain, because of the 'cumulated' rules of origin. There is an added benefit for trade with countries where the UK has pre-existing post-Brexit trade agreement (e.g. Japan, Canada, Mexico). Under those post-Brexit deals, components sourced from the EU (e.g. a Belgian-made car battery) count as local content. Now, in addition, components sourced from a CPTPP country (e.g. a Japanese-made car battery) also count as local – meaning British firms can source 'local' parts from the UK, EU, or a CPTPP member. On the other hand, however, the cumulated rules potentially open the UK up to imports of cheaper, lower-quality goods from CPTPP members.	

9. CLIMATE **ACTIVE CONVERGENCE** **INTERNAL IMPACT** *UK consultation on a carbon border adjustment mechanism.*	**Summary:** The UK government has launched a 12-week consultation on the introduction of a carbon border adjustment mechanism (CBAM). This would impose tariffs on imports of certain goods, to ensure they pay the equivalent price for their carbon emissions as if they had been produced in the UK. The UK has an emissions trading scheme (ETS) requiring manufacturers in a range of sectors to pay a price on their carbon emissions, but many other countries have no such scheme. The risk is that, without a CBAM, imported goods which subject to less stringent climate regulation are able to undercut UK-made products; and that British companies might move their manufacturing processes abroad to avoid regulation (known as carbon leakage). At present, sectors which are vulnerable to carbon leakage are granted a certain proportion of free allowances under the UK ETS (meaning they don't have to pay for some or all of their emissions).	**Impact:** The UK proposal to a large degree mirrors EU plans for its own CBAM (covering cement, iron and steel, aluminium, fertilisers, electricity and hydrogen) which begins in simplified form in October 2023. At this stage, data will be collected on imports, but no tariffs will be applied. A date for full implementation has not been set. Sam Lowe of Flint Global argues that, once the EU introduced its CBAM, the UK was always likely to follow. This is because the EU CBAM makes carbon-intensive imports more expensive – and thus less competitive – and manufacturers are thus likely to seek to divert their goods to different markets (like the UK). This leaves the UK at risk of carbon-intensive goods being increasingly dumped upon it unless it takes similar action to the EU. The question remains as to how a future UK CBAM aligns and interacts with an EU one. One possibility is that they have their own similar but distinct regimes. This would protect the UK against the dumping of carbon-intensive goods generally, but creates potential new trade friction between the UK and EU. EU importers of British goods would have to provide data on the carbon emitted during the manufacture of the product and, if the carbon price paid in the UK is	**Timeline/region**: The EU CBAM enters into provisional force from October 2023, but no date has been set for its full implementation. The UK CBAM consultation runs until 22 June 2023.

		lower than it would have been in the EU, the importer would also have to top up the difference. The same issues apply for trade in the other direction, and there is an additional, potentially highly-vexed question, over whether the EU CBAM applies in Northern Ireland. A second option is therefore for the UK and EU to 'link' their ETS regimes, which would likely exempt UK exports from EU CBAM requirements by creating broad-scale alignment on carbon pricing. Prime Minister Rishi Sunak has told the House of Commons Liaison Committee that 'there may be opportunities for cooperation', and a UK official briefed the Financial Times that serious consideration was being given to the idea. However, the UK and EU ETS regimes are at risk of diverging somewhat in scope (see entry #14), which could make them harder to link in future. A third possibility is to establish a group of pro-CBAM countries, within which trade is not subject to additional carbon tariffs. The UK has intimated that it would prefer a common international approach to carbon pricing, but one major challenge is that one of the obvious members of such a group – the USA – currently has no domestic carbon price. A joint approach on CBAMs between the UK and EU (and	

		potentially other partners) also has diplomatic benefits. Because CBAMs are politically controversial, with some countries concerned about the trade discrimination entailed, coordinated diplomatic action by CBAM proponents is likely to be key them becoming accepted internationally.	

10. MEDICINES **ACTIVE CONVERGENCE** *Planned new UK approval processes for medicines.*	**Summary:** In the Spring Budget it was announced that, from 2024, the UK Medicines and Healthcare products Regulatory Agency (MHRA) will move to a new model allowing it to grant 'swift approval' to medicines and technologies approved by 'trusted regulators' from other countries. This is based on the recommendation Sir Patrick Vallance, following his 'Pro-Innovation Regulation of Technologies Review'. According to the speech, sign-off will be 'near automatic', and the supporting policy statement says the MHRA is currently exploring partnerships with the USA, Europe (presumably meaning the EU) and Japan. The plan will be supported by £10m of extra funding over two years. The government hope that this process will minimise the duplication of decision-making already made by other trusted partners, thus freeing up UK resource to focus on other areas of medicines regulation. To this end, the Chancellor announced that: 'At the same time from next year [the MHRA] will set up a swift new approval process for the most cutting-edge medicines and devices to ensure the UK becomes a global centre for their development.'	**Impact:** The 'trusted regulators' plan addresses a post-Brexit challenge, whereby the UK was falling behind in the pace of its approvals of new medicines. In 2021, the UK – which can now longer rely on the EU regulator - approved fewer new medicines than the EU or US. The need for pharmaceutical firms to submit a separate application to get drugs approved for the UK market created further risks of delayed UK access to certain drugs. Granting near-automatic sign-off to goods approved by the EU limits the risk of similar issues in future. It could be argued that this is merely a convoluted exercise in replicating EU decision-making from the outside. Yet the UK will likely seek to replicate this with other jurisdictions. The MHRA is working with Australia, Canada, Singapore and Switzerland to create a new 'regulatory partnership'. Moreover, this would free up capacity to focus on other areas of regulation, in particular new, faster approval process for 'cutting edge medicines', as the Chancellor alluded to. This could allow the UK to get quicker access to new medical technologies and make it a more attractive destination for early-stage development, than would have been possible under EU regulation.	**Timeline/region**: There are few concrete details on the new system, which is set to take effect from 2024.

11. ANTI-CORRUPTION/ HUMAN RIGHTS **PASSIVE DIVERGENCE** *CJEU rules EU public registers of beneficial ownership unlawful.*	**Summary:** The Court of Justice of the European Union (CJEU) has ruled that the EU's public registers of beneficial ownership are unlawful. Beneficial ownership registers record the ultimate financial beneficiary of assets, and are designed to stop individuals from concealing the full extent of their wealth behind anonymous companies which they place in control of assets. Such practices are often used to launder money and avoid anti-corruption legislation. The EU's Fourth Money Laundering Directive required all member states to establish a central register of beneficial owners of companies. However, Transparency International reports that, once journalists began investigating the registers, it became clear that many 'politically exposed persons' were not being identified. Thus, in 2018, the EU's Fifth Anti Money-Laundering Directive guaranteed public access to the registers, to increase the transparency and integrity of the system. In response, a handful of named owners took a case to court after their application to have their names removed from the register (on security grounds) was rejected. This ultimately ended up at the CJEU, which ruled that 'the general public's access to information on beneficial	**Impact:** The ruling has implications for the UK, because it too has publicly accessible registers of beneficial ownership, for both UK and foreign entities. Moreover, it has obligations under the European Court of Human Rights (ECHR) to uphold privacy rights equivalent to the EU treaty articles on which the CJEU ruling was made. This means the CJEU ruling calls into question the lawfulness of the UK's own registers. However, outside the EU, the UK no longer has to adhere to CJEU rulings, and the government instead undertook its own review, which found the open registers to be permissible under EHCR obligations. This is thus a clear case of the UK using its freedom from the jurisdiction of the CJEU to avoid a ruling which has been heavily condemned by anti-corruption campaigners. The UK government had already acknowledged that its public registers 'represent an intrusion into Article 8 ECHR privacy rights'. However, it was assessed that 'the intrusions were limited and necessary in a democratic society for the prevention and detection of crime and in for the economic well-being of the country.' (Unlike EU CFR Article 7, Article 8 ECHR has a public interest exemption.) Following the CJEU ruling, it re-evaluated its conclusions but found the public	**Timeline/region**: The CJEU ruling was made in November 2022, and some EU member states have since removed their publicly-accessible registers.

	ownership constitutes a serious interference with the fundamental rights to respect for private life and to the protection of personal data, enshrined in Articles 7 and 8 of the Charter [of Fundamental Rights of the European Union]' (known as EU CFR). Following the ruling, several EU member states have removed public access to their beneficial ownership registers.	registers to still be compatible with the UK's obligations in relation to ECHR privacy rights. Dan Neidle, of Tax Policy Associates, has called the UK government decision to maintain open registers a 'benefit of Brexit'. He stated that his recent work investigating the tax affairs of former Conservative Party Chair Nadhim Zahawi, which ultimately led to his resignation, would not have been possible without open beneficial ownership registers. Similarly, Transparency International states that the CJEU ruling 'impacts not only the general public but especially specific groups of professionals who work hard to stop the flow of dirty money', including journalists, civil society, academics and domestic and foreign authorities investigating local and cross-border crime. The absence of access to public registers will make investigations into complex ownership structures much more cost- and time-intensive.	

12. AVIATION **PASSIVE DIVERGENCE** *EU Drone Strategy 2.0.*	**Summary:** A key pillar of the EU's updated 'Drone Strategy 2.0' took effect in January 2023. Drones have, since 2018, been subject to harmonised EU safety rules, which allow them to be used for a variety of purposes including infrastructure surveys and soil sampling. However, the EU anticipates the use of drones becoming more frequent and wide-ranging by 2030, for example extending to emergency services, deliveries of goods and air taxis for people. The updated strategy thus seeks to establish an integrated regulatory framework for the airspace used by drones, to safely manage the anticipated rapid increase in traffic. To this end, the EU's new 'U-space' (standing for 'unmanned space') system came into force in January 2023. It in effect creates the legal groundwork for member states to start regulating their U-space. This requires them to first define the volume of airspace which constitutes their U-space and who the 'services providers' will be. They will then have to develop governance systems and standards which enable the identification of drone operators and the location and trajectory of their drones; the provision of air traffic alerts and information on operational conditions; and the avoidance of conflicts between drones in the same U-space.	**Impact:** The U-space system has been described by the Financial Times as 'the first law to govern unmanned airspace' and is, alongside the wider Drone Strategy 2.0, an example of the EU moving before the UK to establish regulatory norms around an emerging technology. The EU's ambition is to create an environment for 'large-scale commercial drone operations': for example allowing for the transport of key supplies like medicines, and for air taxis as a viable alternative to plane and helicopter travel. One manufacturer is planning to roll out air taxis at the 2024 Paris Olympics, travelling distances of up to 20km. Overall, the EU claims that, by 2030, its drone services market could be worth €14.5 billion and create 145,000 jobs. The UK has not come as far in the development of its own regulation. A government policy paper has a similar 'vision' to the EU for 2030: where drones are 'commonplace' in the UK, used across a variety of sectors (like construction, public services and agriculture) and for connecting remote communities. Yet the main calls to action are around generating funding for drone technology and sector-specific skills. There are no plans for a regulatory framework for emerging drone technologies which are comparable to the	**Timeline/region:** The EU Drone Strategy 2.0 took effect in January 2023.

	Member states also have the option to establish services providing weather information and monitoring compliance. Beyond the U-space system, the Commission is beginning work on '19 operational, technical and financial flagship actions' to create a regulatory environment to facilitate the wider use of drones. These include common rules for airworthiness, training requirements, an online platform to support stakeholders, a technology roadmap identifying priority areas for research and innovation, and establishing a voluntary security label for drones.	EU's. Professor Hussein Kassim notes that the UK has struggled to get its drone regulatory environment up to speed post-Brexit, with the UK having 'issues concerning drone certification, and recognition of drone operators in the EU and the wider global marketplace'. He adds that 'arguably the key developments on drone technology are taking place in the rest of Europe and in the US'. However, drone regulation is not necessarily an area where the UK and EU are in competition. Their respective aviation authorities both participate in international working groups focusing on the harmonisation of drone regulations, and the UK remains a member of EUROCONTROL (a European body supporting safe air traffic) and the European Civil Aviation Conference. There are strong incentives to align airspace regulations throughout all of Europe, and the EU has tended to take the main steering role on this. The UK has instead sought to encourage greater innovation on drone technology (rather than airspace governance), with the aim of becoming more agile in introducing new services: for example the Civil Aviation Authority's sandbox helping operators trial applications under restricted conditions.	

13. CHEMICALS **PASSIVE DIVERGENCE** **INTERNAL IMPACT** *EU proposed new restrictions on polyfluoroalkyl substances.*	**Summary:** The European Chemicals Agency (ECHA) has published a proposal for restricting around 10,000 substances commonly known as 'forever chemicals'. Initially prepared by regulators in Denmark, Germany, the Netherlands, Norway and Sweden, the proposal relates to per- and polyfluoroalkyl substances (PFASs) – a group of synthetic chemicals which are known to pollute water and soil and remain for a very long time in the environment due to their resistance to degradation. PFASs are widely used in the automotive and aviation sectors and within a wide range of consumer items like cosmetics, textiles, food packaging, lubricants and medical devices. They are regularly released into the environment through every day use and humans come into contact with them in their food and drinking water. The ECHA warns that 'people, plants and animals will be increasingly exposed' if their releases are not minimised. Increased exposure to certain PFASs is linked to internal organ damage, water and wildlife contamination, and lower sperm count in men. The new proposal would restrict around 10,000 substances, implementing a ban on their manufacture, placing on the market and use. There would be an 18-month transition	**Impact:** The move is part of an EU ambition, under its Green Deal, to phase out the use of PFASs except where 'essential for society'. It is a major regulatory change which the German Environment Agency has dubbed 'the broadest restriction proposal in history'. Indeed, previous estimates put the PFAS family at around 4,700 chemicals, so the latest announcement is a major enhancement in scope from the EU. The restriction of up to 10,000 substances would entail changes to the manufacturing processes behind a wide range of goods, which has unsurprisingly evoked strong reactions from industry and consumer groups. The European Consumer Association supports the proposed restrictions whereas the Fluoropolymers Product Group within Plastics Europe argues that Fluoropolymers' 'environmental and toxicological profiles are distinctly different' to most other PFASs and thus should not be restricted. Fluoropolymers are widely used in sectors such as electric vehicles, aviation and electronics, and fluoropolymer manufacturers claim a restriction on their use could cause 'global disruption' in such high-end industries and increase the cost of goods.	**Timeline/region:** The EU proposal is still in consultation and any restrictions are unlikely to take effect before 2026.

	period for industries to adapt to the new restrictions, but there could be potentially longer time-limited derogations for specific uses (for example implantable medical devices) where alternatives are under development but not yet available. In practice, the restrictions would mean items like cookware, food packaging, lubricants and cosmetics would no longer be able to contain PFASs following the end of the transition period. The ECHA estimates that this would lead to, for example, a 95% reduction in PFAS emissions from the textiles industry over the next 30 years. For now, the proposal remains a long way from becoming law. The next step is for two ECHA committees to determine whether the proposals meet the legal requirements of the EU's REACH regulatory regime for chemicals, followed by a sixth month scientific evaluation consultation. This process will then inform two committee decisions on 1) whether the proposed restrictions are 'appropriate in reducing the risks to people's health and the environment' and 2) the socio-economic impacts. Once adopted the opinions will be sent to the European Commission and member states to decide on the exact terms of future restrictions. This means they are unlikely to take effect before 2026.	This naturally has consequences for the UK. Though Westminster has not indicated any intention to follow the EU restrictions, British industries will have to adhere to it if they want to export their goods to the EU. For example, the EU is the UK electric vehicle industry's biggest export market. If British electric vehicle batteries continue to use PFASs once EU restrictions take effect, those vehicles will no longer be exportable to the EU. The same issue applies for British manufacturers of other goods containing PFASs like semiconductors, aircraft, medical equipment and frying pans. The full extent of the impact will depend on the final form of the EU legislation and the extent of any derogations agreed for specific products. Moreover, even if a good is destined for sale in GB, it will not be able to cross into the EU during the manufacturing stage if any of its components contain PFASs. It is therefore likely that many British (and other non-EU) manufacturers, including those which contribute components to the supply chains of goods, will automatically align with EU requirements to avoid such issues. A similar issue arises in Northern Ireland. Even under the Protocol as revised by the Windsor Framework,	

		manufactured goods in NI will still have to adhere to EU standards, and thus new PFAS restrictions. This means any goods made in GB containing PFASs would not be exportable to NI. This poses a particular risk for NI importers who are a small part of a GB based-company's export market, because the GB-based company might decide that the costs involved in stopping uses PFASs are greater than those incurred from no longer exporting to NI. There are also three PFAS manufacturing plants in the UK. Whether they will remain economically viable after any EU ban will depend on the extent of international demand. Many international firms (especially in fashion) are likely to remove PFASs from their supply chains in response to any EU restrictions. But one other potential impact could be that goods which continue to use PFASs are increasingly 'dumped' in Great Britain once the EU market is closed to them.	

14. CLIMATE **PASSIVE DIVERGENCE** **INTERNAL IMPACT** *Update to EU Emissions Trading Scheme.*	**Summary:** The European Council and Parliament have agreed on an update to the EU emissions trading scheme (ETS) which sets a price on carbon emissions through company trading permits. The latest update increases the target rate of emissions reduction for sectors covered by the ETS - to 62% by 2030 compared to 2005 levels. This is up from an initial target of 45%. As a result, the ETS' overall emissions ceiling has to fall faster, with the annual reduction in the cap on emissions permits now set to fall by 4.3 % per year from 2024 to 2027 and 4.4% from 2028 to 2030. It was previously set to fall by 2.2% from 2021 onwards. Certain sectors are entitled to free allowances under the ETS because they are deemed vulnerable to carbon leakage – where competitors from the rest of the world who are not subject to such stringent emissions regulations are able to undercut them. These allowances will now be phased out between 2026 and 2034 as the EU introduces its Carbon Border Adjustment Mechanism (CBAM), which is an alternative form of preventing carbon leakage based on taxing imports of goods from ETS-covered sectors. For aviation, free allowances will be much more rapidly phased out by 2026.	**Impact:** These updates create divergence between the UK's ETS, which largely replicated the EU scheme, and the EU ETS - with potential implications for their carbon prices. The EU ETS will become wider in scope than the UK's, by covering maritime emissions, and also see a faster reduction in permitted allowances. The total permitted allowances under the UK scheme will fall by 3% in 2024, increasing gradually to a reduction rate of 3.5% by 2029. This is lower than the EU's rates of 4.3% from 2024 and 4.4% from 2028. Up to now, the price of permits under the UK and EU schemes have broadly tracked one another, yet the changes in scope to the EU ETS are expected to cause some volatility in its carbon price. In the longer term, divergence in the price and scope of the UK and EU ETS regimes may make it harder to link them. Failing to do this could increase barriers to trade between the UK and EU once the EU introduces its CBAM, as UK exports would be subject to new carbon-based export tariffs and paperwork. It would also make it harder to link the EU CBAM to a UK one (which the government is consulting on and which it would prefer to be part of a common international scheme – see entry #9).	**Timeline/region:** The law was formally adopted on 18 April 2023 and will now be signed into law by the Council and Parliament.

	The scope of the ETS will also be gradually expanded to cover maritime shipping – with allowances required for 40% of emissions from 2024, 70% from 2025 and 100% from 2026. A separate emissions trading system, starting from 2027, will also be created covering the buildings and road transport sectors, as well as fuels for 'additional sectors' which 'have been difficult to decarbonise so far'.	The phasing out of free allowances for the aviation sector is also likely to have a knock-on effect on consumers in both the EU and UK. Analysts predict that the cost of compliance with ETS requirements for the six biggest airlines within the EU will rise from €0.5bn in 2019 to €5bn in 2027. This is estimated to increase ticket prices by around €8-10 per return flight. While this would mostly affect intra-EU flights, it would also apply to flights from the EU to the UK which are covered by the EU ETS up to the start of 2027.	

15. CLIMATE / INDUSTRY **PASSIVE DIVERGENCE** *EU Net-Zero Industry Act.*	**Summary:** The European Commission has proposed a new Net-Zero Industry Act (NZIA), with the overarching aim that at least 40% of the EU's net-zero technology is manufactured inside the EU by 2040. The central pillar is the simplification of the administrative and permit-granting processes for investment in net-zero technologies. This will be done by obliging member states to create online 'one-stop shops' where. Assessments of similar applications may also be bundled together. Permits must be assessed within 12 months for projects with capacity of under 1 gigawatt, and within 18 months for those above. Priority will be given to 'strategic projects', selected on the basis of their potential to contribute to increasing net-zero manufacturing capacity in areas where the EU depends on a single country for its imports, or where they could significantly increase the competitiveness of EU supply chains. Such projects must be approved in 9-12 months. Applicants can propose themselves as 'strategic projects', with the status granted at member states' discretion. The EU has defined the eight technologies which will benefit from the streamlined approval processes: solar technologies;	**Impact:** Though not explicitly presented as such, the NZIA is part of the EU's response to the US Inflation Reduction Act (IRA): which seeks to boost US green investment through a $369bn package of tax breaks and subsidies, and prompted widespread concerns within the EU about the impact on its own green industry. Because IRA benefits are conditional on production and final assembly occurring in the US, some fear a major relocation of European green industry to the US. Tesla and Volkswagen have recently paused plans to build battery plants in the EU in favour of expansion in the US. The EU has reacted faster than the UK to the US IRA, managing to secure a carve-out allowing EU-made electric vehicles sold on lease deals in the US to qualify for an IRA tax credit. The US has also agreed that five critical minerals used in battery making can qualify for IRA subsidies if they were mined or processed in the EU. However, major EU concerns remain that the IRA gives US green tech a significant advantage over EU competitors. Thus, the NZIA seeks to boost the EU's own green production capacity, to ensure it remains internationally competitive with the US and China (which has long poured subsidies into its own industry). The NZIA is supported by other recent	**Timeline/region:** The NZIA will now be discussed by the European Parliament and Council.

	onshore wind and offshore renewable energy; batteries and storage; heat pumps and geothermal energy; electrolysers and fuel cells; biogas/biomethane; carbon capture and storage; and grid technologies. Nuclear technology is excluded, with only small modular nuclear reactors and nuclear plants included as second-tier priorities – a likely disappointment to France in particular, as nuclear is a key part of its energy mix. Beyond this, 'sustainability and resilience criteria' will be introduced for public procurement and auction processes. Bids will be deprioritised for using suppliers from a country with a 65%-or-more share of specific EU supply chains - in effect reducing China's dominance of certain markets like heat pumps and solar panels. Companies bidding for power generation tenders or subsidies will have to source 40% of their equipment from the EU. There is also an objective to be able to store 50 megatonnes of CO2 a year by 2030. Carbon capture and storage (stripping CO2 out of emissions) is a developing technology which is not yet deliverable at scale but will be vital in future for emissions-heavy industries like concrete to become emissions-neutral. The EU wants to increase its storage	reforms, which seek to reduce reliance on foreign imports and boost domestic investment. The relaxation of state aid rules allows member states to leverage more public funding in aid of green investment and match foreign subsidies, while the Critical Raw Materials Act (see entry #16) seeks to boost EU production of materials critical to certain green technologies, thus reducing the Union's reliance on China in particular. This could signal an 'arms race' between the EU, China and US for dominance in green technology. Such dynamics naturally have consequences for the UK, which has not (so far) introduced comparable incentives and protections for domestic green industry, and lacks the economic clout to compete with the US, EU and China in a subsidy race. The recent collapse of the company Britishvolt, which was planning to build electric car batteries in Northumberland, has been seen as indicative of the struggles of the UK green tech industry to access adequate investment. The government says it does not want to go 'toe-to-toe with our friends and allies in some distortive global subsidy race' and prefers targeted 'strategic' investment, financed through private capital, with a more complete response to be set out this autumn. Yet	

	capacity to 'reassure industry investors that their captured emissions can be stored in the EU' in future. Member states will be permitted to set up 'regulatory sandboxes' to test innovative net-zero technologies in a contained, lower-regulation environment; and new 'Net-Zero Industry Academies' will also be set up train people to work in the production of relevant technologies. Underpinning this is a new 'Net-Zero Europe Platform', aiming to help member states and the Commission exchange information, foster contacts and coordinate action on net-zero activities. It will also be a forum for identifying financial needs for projects, and securing private financial support. Indeed, a clean technology industry group argues that the NZIA 'falls short of the clarity of funding associated with the [IRA]', and the EU admits that projects 'may require public support, including in the form of State aid', which will be aided by the recent further relaxation of EU state aid rules (see entry #27). Smaller member states are concerned that the more liberal use of state aid could increase economic disparities within the EU - as the largest economies will be able to pile greater resources into their	environmental experts and industry groups have argued that such a 'business as usual' approach is ill-suited to the exceptional circumstances created by the IRA and NZIA, where green tech investors are making unprecedented financial commitments. Whether Britain will remain competitive is a major question mark. The opposition argues that much greater investment is necessary to enhance the UK's green industrial strengths, like wind power, and help industries decarbonise; and has called for a publicly-owned UK energy generator. There is certainly a case to be made, however, that the UK could in theory produce a plan better suited to its own needs than the EU NZIA. The Brussels-based economic think tank Bruegel argues that the NZIA's 40% domestic production target could set back the green transition, because it is slower and less cost-efficient to try and scale up domestic manufacturing of things like solar panels (where currently around 10% of the EU's stock is produced domestically) than to procure them on international markets. This could pass on higher costs to consumers, especially if, as some have predicted, the EU struggles to compete with China and the US - which have	

	domestic industry, while those with more limited resources are left behind. Given these concerns, the Commission says a 'more structural answer' will be provided by a 'European Sovereignty Fund' to facilitate joint borrowing. This is an idea which has stoked controversy within the EU, especially among more fiscally frugal member states opposed to more common borrowing by to finance landmark measures (following the €750bn borrowed by the Commission to support the post-Covid economic recovery). It should be noted that the EU has so far not identified any specific projects which are to be paid for from a future sovereignty fund, nor stated when such a fund will be established.	greater resources and (in China's case) a long head start in supporting domestic industry. Others have argued that it is a mistake to treat green technology as a zero-sum game between different countries. Martin Sandbu in the Financial Times argues that European firms investing in the US due to the IRA does not preclude them from continued investment in the EU too, and Zach Meyers of the Centre for European Reform argues that the IRA could even help turn several European manufacturers into EV market leaders (because their more limited current dependence on China means they will find it easier to qualify for IRA support than US competitors). In this context, some in the UK might consider it preferable to not be subject to EU plans, which potentially make the procurement of green technology more expensive and inefficient than necessary, and harm trading links with international partners. The UK would likely have joined Germany and the Netherlands in opposing the EU plan for greater common borrowing via a European Sovereignty Fund in aid of the NZIA.	

16. CLIMATE / INDUSTRY **PASSIVE DIVERGENCE** *EU Critical Raw Materials Act.*	**Summary:** The EU has announced plans for a 'Critical Raw Materials Act' (CRMA), setting domestic production requirements for 16 'strategic raw materials'. Such materials are defined as crucial to 'strategic sectors' (such as energy, digital, space and defence) and likely to be subject to future supply risks due to demand outstripping supply. The 16 materials include cobalt, copper, battery-grade lithium and nickel, magnesium metal and silicon metal. The EU has thus set voluntary targets that, by 2030, of the strategic raw materials consumed annually by the EU, 10% will have to be extracted domestically; 40% will have to be processed domestically; and 15% will have to be recycled domestically. No more than 65% of the EU's annual consumption of a specific raw material may come from a single non-EU country. At present, only 3% of critical raw materials are extracted in the EU, while '0-20%' is processed in the EU. There are also wider measures to support the supply of 'critical raw materials' – a wider group than the 16 'strategic' raw materials which are classified as top priority. Member states' administrative and permitting processes for projects related to critical raw materials will be simplified,	**Impact:** The CRMA is part of an EU strategy to reduce its reliance on foreign imports of goods which are vital to the digital and net-zero transitions. The EU is concerned that heavy reliance on a single country leaves it vulnerable as demand for such materials is expected to surge. By 2030, demand for rare metals required to make wind turbines is expected to increase by 4-5 times, while demand for lithium, used to make batteries for electric vehicles and other devices, is expected to increase by 11 times (and by 57 times by 2050). This entails increased competition for supplies over which the EU currently has little control. Often upwards of 90% of its supplies of certain critical raw materials come from a single country. China, in particular, dominates the global market for many of these materials, with control of 60% of the world's rare earth production and 80-90% of lithium refinement, and the EU is almost entirely dependent on it for imports of magnets. It is thus highly vulnerable to supply curtailment, be it unintended or deliberate (for example as a result of a hypothetical future dispute over Taiwan). The issue has been given even greater impetus by the EU Net-Zero Industry Act (NZIA - see entry #15) – published on	**Timeline/region:** The UK Critical Minerals Strategy will publish a delivery update in 2024.

	with all processes carried out at a single 'one-stop-shop'. Certain priority projects will have access to financial support and shorter fast-tracked permits, which have to be approved in under 24 months for extraction projects, and under 12 months for processing projects. Member states will have to develop national programmes for exploring geological resources and a board will be established to monitor critical raw material supply chains and advise the Commission on where to 'stress test' supplies. There will be a mechanism for option joint purchases of strategic materials by member states, and the Commission has the power to gather information about stocks of such materials. Large companies that manufacture technologies with strategic raw materials will have to audit their supply chains every two years. The Commission says it will discuss with member states means of sourcing more private finance to support critical raw materials projects, but that increased state aid (facilitated by the EU's recent further relaxation of its rules – see entry #27) will also play a vital role.	the same day as the CRMA - which aims for 40% of the EU's green technology to be produced domestically by 2030. However, the fact that the targets are non-binding has already led to concerns that that they will have little material effect. The EU also acknowledges that it will never be able to produce all its required raw materials domestically, and is thus seeking supply agreements with key partners like Chile, a major lithium producer. Some energy experts suggest the most significant impact of the CRMA could be the joint purchasing of raw materials, potentially giving the EU a more influential position in global markets. Questions have also been raised about the environmental and social costs of the plan. Energy infrastructure and strategic mining, refining and recycling projects can be given a prioritised status which allows them to override existing EU regulation around nature conservation and water protection. The Act raises major questions about what the UK is doing and whether it risks being left behind in the pursuit of critical material supplies. In the same week as the EU Act, the UK published its 'Critical Minerals Refresh', which bears some similarities to the EU approach. An independent group will investigate 'critical mineral dependencies and	

		vulnerabilities across UK industry sectors' and government is seeking new supply partnerships similar to those agreed with Canada and South Africa. However the UK has, unlike the EU, not set targets for domestic production and processing of critical minerals, instead providing £15m for making supply chains more resilient and £65.5m to promote relevant mineral technologies in developing countries. The concrete steps forward are far more limited, with the Strategy promising only an update on progress in 2024.	

17. CLIMATE **PASSIVE DIVERGENCE** *E-fuels exempted from EU combustion engine phase-out.*	**Summary:** The European Council has signed off on the EU's plan for all cars sold from 2035 to be zero-emissions, but only after an agreement was made between the European Commission and Germany that combustion engines running on 'e-fuels' are not covered by the ban. Germany (supported by Italy, Poland, Czechia and Bulgaria) had been blocking final approval on the 2035 phase-out – the plans for which were covered in a previous divergence tracker – until an exemption on e-fuels was granted. Germany has pushed for the exemption to protect its car industry. Under the initial proposals, the sale of new vehicles powered by internal combustion engines (which burn fossil fuels) were to be banned from 2035. Germany sees this as a threat to its car industry, which employs 800,000 people in the production of combustion engine vehicles, and 68% of its public oppose to the ban. Having to re-orient Germany's car industry towards battery-powered electric vehicles threatens its dominance, opening it up to greater competition from the likes of China which are further ahead in developing electric vehicle technologies. The appeal of e-fuels to Germany is that combustion engines are able to run on them. E-fuels are synthetic alternatives to	**Impact:** The UK has set a phase-out date of 2030 for fully petrol and diesel cars – five years earlier than the EU – with a date of 2035 for hybrids. Though it may come under some pressure to do so, the UK government seemingly has no plans to replicate the EU decision on e-fuels. The EU's decision is likely to hamper its net zero transition on the roads. One issue is that e-fuels are up to four times less efficient in their use of energy than electric car batteries, according to the International Council on Clean Transport (ICCT). Given energy grids are still far from 100% renewable, increased demand for renewable energy to create e-fuels means it cannot be deployed elsewhere in the energy mix. Moreover, while e-fuels can be generated using renewable technology, there is no guarantee that this will be the case. Another issue is that e-fuels will only make a marginal impact to vehicle decarbonisation. The NGO Transport & Environment estimates that e-fuels could power at best 2% of cars in the EU by 2035. Yet, by permitting the use of e-fuels, the EU Commission is incentivising its car industry to slow their development of electric vehicle technology – *the* key element of vehicle decarbonisation - in favour of a	**Timeline/region:** The Commission will bring forward its proposed amendments to the legislation by the autumn, with ambitions to complete the process by the autumn of 2024.

	fossil fuels, made from CO2 (which is captured from the atmosphere) mixed with hydrogen (generated by using renewable energy to split water). While vehicles burning e-fuels to emit CO2, the proponents argue this is the same CO2 which was captured from the atmosphere, meaning no new CO2 is added overall. However, the claim that they are carbon neutral is as yet unproven, and they are widely seen as damaging to the net zero transition, as is covered in the next section. Following the agreement, Germany allowed the original legislation, on phasing out combustion engine vehicle sales by 2035, to pass unchanged. However the Commission has said it will follow up with 'legal steps', which is likely to involve creating a new category of 'e-fuel-only' vehicles. Formal proposals are then set to brought forward this autumn to amend the law, via delegated act, to create a carve-out around e-fuels. The Commission has said it needs time to work on a proposal that is 'robust and evasion-proof' enough that it strictly permits the use of combustion engines for e-fuels only. Germany says it expects the entire process to be completed by the autumn of 2024.	marginal, unproven technology. Porsche has already invested $24m into an e-fuel project in Chile. A key reason why supplies will be so limited is that e-fuels are very expensive to produce and relatively difficult to deploy. The electrolysers used to split water into hydrogen and oxygen remain very expensive, and a literature review commissioned by the ICCT found that there is no evidence of industry claims that prices are set to suddenly drop. Transport and Environment estimates that an e-fuel powered car will cost the average user an additional €10,000 over five years compared to an electric vehicle. Moreover, whereas electric vehicles can be recharged from charging points, electric fuels have to be transported from production sites to filling stations, requiring further vehicle usage.	

18. CLIMATE / ROAD TRANSPORT **PASSIVE DIVERGENCE** *EU emissions reduction targets for heavy-duty vehicles.*	**Summary:** The EU has proposed new emissions reduction targets for heavy-duty vehicles (HDVs). By 2030, average CO2 emissions for new HDVs will have to be 45% lower than 2019 levels (an increase from the previous target of 30%). This target rises to 65% by 2035; and 90% by 2040. The proposal is being expanded to cover city buses and long-distance buses (above 7.5 tonnes) alongside trucks (above 5 tonnes) and trailers. All new city buses will have to be zero emissions by 2030. The targets apply only to *new* vehicles, not emissions across the EU's entire fleet of HGVs. It in effect sets benchmarks for what proportion of newly manufactured vehicles must be zero emissions in a target year. So, for example, a 90% emissions reduction target for 2040 means that the vast majority of HDVs manufactured that year will have to be zero-emissions. The targets are, however, much less ambitious than the EU's 100% emissions reduction target for cars and vans by 2035 – which in effect bans the sale of new petrol and diesel cars and vans from that date. There are exemptions from the targets for certain groups including small volume manufacturers; vehicles used for mining, forestry and agricultural purposes; vehicles designed	**Impact:** The EU proposal is less ambitious the UK's, where new HGVs will have to be zero emissions by 2035 (or by 2040 for those weighing over 26 tonnes). However, the EU has taken clearer steps towards achieving its goals. Indeed, the British Vehicle Rental and Leasing Association noted after the UK announcement that 'the barriers remain huge' to achieving the 2035 target. The UK is also yet to set out a clear plan for how it will proceed, with a consultation launched in May 2022, but no response yet published. The EU, by contrast, is more advanced in this respect, with it currently working to finalise plans to introduce electric charging points every 60km on major highways – a necessity for a widescale transition to electric HDVs. HDV emissions are a key area for the EU to tackle in its ambition to reduce carbon emissions by 55% by 2030. HDVs are responsible for an estimated 6% of EU CO2 emissions and 28% of EU CO2 emissions from road transport, despite making up only 2% of vehicles. Indeed, 99% of HDVs in the EU run on fossil fuels, meaning there is significant scope for electrification of vehicles. The EU acknowledges its previous reduction targets were 'no longer in line with the EU's climate objectives' and did not,	**Timeline/region:** The Commission's proposals will be subject to negotiation within the EU institutions before being finalised.

	and constructed for use by armed forces, civil protection, fire services and forces responsible for maintaining public order, or urgent medical care; and vocational vehicles like rubbish trucks.	in its view, 'provide a sufficiently clear and long-term signal to investors' or take account of developments in HDV manufacturing which allow for a greater transition to zero-emissions vehicles. However, some campaign groups have criticised the EU proposal for failing to match the target for cars and vans: where all new vehicles must be zero-emissions by 2035. The group Transport & Environment says the more flexible targets for HDVs mean there is a weaker incentive for fleets to be electrified and thus the 'electric car surge will not be repeated' with HDVs. This is despite Europe's seven largest truck manufacturers having already pledged to stop selling vehicles that produce CO2 emissions by 2040. The Financial Times also notes that, because HDVs are used for 18 years on average, 'lorries emitting CO2 could still be on the road in 2050 when the EU is meant to hit its net zero goal.' On the other side, it is argued that more stringent targets could harm the haulage sector which has a large reliance on small- and medium-sized companies which cannot easily afford to upgrade their fleets.	

19. DIGITAL & DATA **PASSIVE DIVERGENCE** *EU proposal for a Gigabit Infrastructure Act.*	**Summary:** The EU has published plans for a Gigabit Infrastructure Act to replace the 2014 Broadband Cost Reduction Directive. The central aim is to reduce the administrative costs of rolling out 'gigabit' broadband (ultra-fast 5g networks) across the entire EU. A key means of achieving this is simplifying the administrative barriers to creating high-speed networks. A new, online 'single information point' will allow network operators to access all relevant planning information in one place, and to submit digitised permit applications. Permit decisions will have to made in four months (with the completeness of an application to be confirmed within 15 days) unless there are exceptional circumstances. Another aim is to make it easier to access existing infrastructure, reducing the need for new developments. Under the current Directive, operators of relevant networks (e.g. energy utilities) must grant broadband network providers 'fair and reasonable' access to their infrastructure (e.g. manholes and poles) and spaces (e.g. rooftops) for rolling out high-speed internet. To increase the transparency around this, the relevant information about this	**Impact:** Despite digital technology being one of the 'five growth industries' prioritised for reform by the UK government, the latest EU package is far from the first case of Brussels moving faster than Westminster in thinking about the upcoming challenges of tech regulation. The Gigabit Infrastructure Act itself is not especially radical, aiming to enhance the efficiency of an existing framework. Nonetheless, it is central to an EU aim to make high-speed broadband connectivity available to all EU citizens and businesses by 2030. As of 2021, 91% of EU citizens had access to internet speeds sufficient for internet browsing, but the EU argues that inconsistent access to higher-speed networks inhibits cross-border investment, especially in activities that require consistent high-speed connectivity, such as autonomous vehicles. An increased rollout of high-speed networks also has climate benefits, as it allows the switching off of older networks which have almost twice the carbon footprint of modern alternatives. The UK has a similar ambition to make gigabit broadband available to 'at least 99%' of premises by 2030, with a target of 85% by 2025. Planned reforms to aid this include easier access to land for installing infrastructure, though the UK	**Timeline/region:** The Gigabit Infrastructure Act will be examined by European Parliament and Council. The consultation on the gigabit connectivity recommendation closes on 19 May 2023, following which the European Commission will report on the results and consider next steps.

	infrastructure (location, route, type etc.) will have to be made available via the new single information point. To enable more joint operations between sectors, operators will have to make available certain information about planned or ongoing works. For projects financed in part or fully through public funds, operators will be obliged to meet any 'reasonable request' to coordinate works, as long as it does not entail additional costs or impede their control. New rules will also require almost all newly constructed and majorly renovated buildings to be equipped with infrastructure to allow high-speed broadband networks, and once the standards are met buildings will receive a 'broadband-ready' label. In addition, a new draft 'gigabit connectivity recommendation' will give updated guidance to member states' regulatory bodies on establishing a regulatory framework which ensures dominant operators (which own large amounts of network infrastructure) grant sufficient access to competitors. Though guidance is yet to be fleshed out, the EU says it aims to strike a balance between rewarding such operators for their investment and ensuring	appears to have taken fewer active policy steps in support of gigabit rollout than the EU, so far relying mostly on private companies to deliver. Whether this is sustainable as rollout comes to focus on the hardest-to-reach areas remains to be seen. The more radical EU proposals lie in the consultation on future connectivity, which could result in a greater divergence between the EU and UK over the costs big tech incurs for network upkeep. Thierry Breton – the Commission's Internal Market chief – has argued for the need for big tech to pay its 'fair share', as it increasingly dominates EU-built internet networks despite having paid nothing for their development or maintenance. The EU telecoms giants estimate the cost of network usage by big tech to be €15bn a year, and the proposed contributions from big tech are seen by the EU as key to funding the rollout of high-speed internet to all EU citizens by 2030. As it is still at consultation stage, the question of how to ensure big tech pays its 'fair share' is yet to be ironed out: either in terms of which companies are subject to the requirements, or how much (and how) they would	

	there is sufficient competition to incentivise investment in networks. Finally, the EU has announced a consultation 'on the future of the connectivity sector', addressing 'the potential need for all players benefitting from the digital transformation to fairly contribute to the required investments.' In essence, this raises the question of whether big tech, which requires increasing amount of connectivity for its services, should pay for the upkeep of the networks on which it is so reliant, but which were built largely by EU telecoms firms. Indeed, 57% of global internet traffic was taken up by Google, Netflix, Facebook, Apple, Amazon and Microsoft in 2021.	contribute. One proposal is direct negotiations between telecoms companies and tech firms. However big tech firms have unsurprisingly pushed back against the proposals, arguing that paying for the maintenance of networks will mean them having less money available for investment in delivering content to European audiences (the threat of 'degraded' services like lower-quality video has been raised), and that they already invest in other key networks like undersea cables.	

20. ENERGY **PASSIVE DIVERGENCE** *Updated EU Energy Efficiency Directive.*	**Summary:** The European Parliament and Council have reached provisional agreement on a reform of the EU Energy Efficiency Directive, establishing a target to reduce energy consumption in 2030 by 11.7%, compared to a 2020 forecast for consumption levels in 2030. This in effect almost doubles the energy savings targets for member states. From 2024 to 2030, they will have to reduce energy consumption by almost 1.5% a year on average, up from the current level of 0.8%. Member states will have to establish indicative national contributions and trajectories, based largely on a pre-set formula based on criteria like GDP per capita and development of renewables. The target is now also in part legally binding – for the 43% of the target which is made up of 'final energy' used by consumers. The rest of the target relates to 'primary energy' used for the production and supply of energy, where the target remains indicative. There are some new requirements for the public sector, with an annual energy reduction target of 1.9%, and the obligation to renovate each year at least 3% of the total	**Impact:** As a previous divergence tracker outlined, the UK and EU have taken similar steps to enhance their energy security following the Russian war in Ukraine, except on energy efficiency. The EU set a target to cut electricity and gas consumption by 10% and 15% respectively up to spring 2023, whereas the UK offered no similar targets. The updated EU Directive thus represents another case of divergence on energy efficiency, albeit this time more in terms of means than ambition. The UK actually has relatively high long-term ambitions on energy reduction, aiming to reduce total UK energy demand by 15% from 2021 levels by 2030 in buildings and industry. The European Parliament initially proposed a 14.5% target for the EU, but a compromise of 11.7% was settled on after the Council pushed for 9%, leaving campaign groups disappointed. Yet the UK's strategy to reach its goal is less developed than the EU's, having only so far only published the terms of reference and membership for the 'Energy Efficiency Taskforce' to oversee the ambition, as of February 2023. By contrast, the EU's updated directive sets out concrete and,	**Timeline/region:** The provisional agreement will be submitted to the Committee of Permanent Representatives in the Council and the Parliament's ITRE committee for approval.

	floor area of public-owned buildings has been extended to regional and local levels. Member states will also have to implement energy efficiency measures as a priority for those affected by energy poverty as well as for other vulnerable and low-income households; and promote local heating and cooling plans in municipalities of over 45,000 people. Meanwhile, companies with over 85 terajoules of annual energy consumption will have to introduce energy management systems or else be subject to an energy audit, and large data centres will have to report on their energy performance.	in some cases, legally binding steps which member states must take. Whether the EU's greater progress so far translates into larger usage reductions remains to be seen. Its voluntary targets for energy usage reduction over the last winter had a patchy impact, with many member states doing little in response. Overall, EU natural gas demand fell by 12% in 2022 from its 2019-22 average, compared to 9% in the UK. The EU's electricity consumption fell by 3.5% in 2022 from the previous year, compared to 5% in the UK. Campaign groups are concerned that EU member states may do similarly little to implement the updated energy efficiency directive in practice.	

21. ENERGY **PASSIVE DIVERGENCE** **INTERNAL IMPACT** *EU electricity market reform and UK Review of Electricity Market Arrangements.*	**Summary:** Both the EU and the UK have begun processes to reform their electricity markets. On 14 March, the European Commission released a proposal to revise the EU's electricity market design. The central objectives are, first, to protect consumers and industries from future energy price spikes like those seen throughout 2021 and 2022; and, secondly, to encourage the necessary investment in renewable technology in order to transition to a net zero economy. To this end, the suggested reforms seek to 'decouple' electricity prices from gas, which are naturally linked because of the 'merit order' system of the EU's electricity market. Under this system, the last and most expensive input needed to meet energy demand sets the price of electricity, which, for the EU, is usually natural gas. This has created a perverse situation where non-gas powered energy, which is much cheaper to generate, costs consumers the same as gas. The EU's proposed reforms aim to decouple gas and electricity prices without fundamentally changing the merit order system: by increasing the proportion of renewables in the electricity-generation mix. This would mean that gas is less often required to meet demand and, therefore, will	**Impact:** The Commission's proposed reforms are significantly less radical than the overhaul initially suggested by Commission President Ursula von der Leyen, who had called for a 'deep and comprehensive reform of the electricity market' that was 'no longer fit for purpose'. Such reform could, for example, have entailed caps on consumer prices, with states compensating energy producers for the difference; caps on revenues for low-cost producers, to fund wider consumer support; or a new pricing structure based on a weighted average of fossil fuel and renewable costs. These reforms are, however, more targeted, making little effort to foster more EU-wide collaboration. As a result, there are doubts around whether they will reduce high electricity prices, and could even prolong them, as member states with less credibility on financial markets may find it harder to secure long-term contracts with clean electricity producers and, therefore, be forced to sign contracts which lock-in high electricity prices for the foreseeable future. Furthermore, while the EU's reforms encourage the future use of capacity mechanisms, they do not offer proposals to	**Timeline/region:** The draft conclusions from the EU council summit in March 2023 suggest that the EU will try and adopt these electricity market reforms by the end of 2023. However, there have been some requests (namely from the German government) to delay reform until after the 2024 European elections. The UK government says

	determine the price of electricity for significantly shorter amounts of time. The main tools that the proposals focus on are various forms of long-term contracts, such as Purchasing Power Agreements (PPAs) and Contracts for Difference (CfDs). PPAs are long-term bilateral contracts between companies that generate energy and consumers (usually energy-intensive businesses). The Commission's proposals attempt to ensure the availability of market-based guarantees for PPAs by removing entry barriers (such as credit risk) for customers. With regard to electricity, CfDs are a two-way contract (usually) between the state and electricity producer, where a fixed reference price is agreed for electricity. If market prices fall below that price, government pays the difference to producers; and if market prices exceed it, producers pay the surplus to government. This ensures that the CfD holder receives a fixed price for the electricity they produce, with the idea being that guaranteed capital and a predictable price horizon encourages industry investment (thus bringing prices down further). In the Commission's proposals, CfDs are set as the default provision of state support for non-	create an EU-wide harmonised market and still require a complex approval process. Therefore, these reforms are, as they stand, unlikely to do much to guarantee the security of energy supply for all EU nations during periods of scarcity. In contrast, the UK government's Capacity Mechanism proposals, released in January 2023, indicate that the UK is making a greater effort in expanding capacity. The government confirmed that an optimised capacity market will remain under consideration (this involves changes to auction design and alternative policy mechanisms for ensuring capacity adequacy). However, the UK also looks likely to opt against a more radical market overhaul, with government noting a lack of clear support for more radical market design options such as splitting the market or nodal pricing. As with the proposals of the European Commission, there appears to be greater demand for expanding CfDs, such as by extending contract lengths or allowing existing generators to bid for a CfD. The shared UK and EU emphasis on long-term contracts means that there is little fundamental divergence in the structure of their energy markets. Questions had been raised about the implications for energy-sharing if one side adopted	in its 'Powering Up Britain' that a clear approach to gas vs. electricity 'rebalancing' will be committed to by the end of 2023/24.

	fossil generation, while there is also a suggestion to make it mandatory for all new developments to sign a CfD. The document also suggests granting EU member states more freedom to set electricity prices for consumers in crisis periods, to control the kinds of surges seen following Russia's full-scale invasion of Ukraine. The UK government has also started the early phase of reforming its electricity markets. On 9 January, the Government set out proposals to reform Great Britain's Capacity Markets. Capacity Mechanisms (also referred to as Capacity Markets) are a state subsidy which ensures that there is sufficient reliable electricity capacity by paying power plants to be available to generate electricity to meet peak demand when needed, particularly during periods where there is low wind and solar availability or other generators are on outage. The UK government has set out its intention to incentivise greener technologies to compete in Capacity Market auctions by promoting multi-year contracts for low-carbon flexible capacity and a stricter lower emissions limit. These proposals form a part of the Review of Electricity Market	a fundamentally different approach to price-setting compared to the other, as this might have made energy trading more complex; or have led to the hoarding of supplies by one side if it became unwilling to share cheaper/subsidised energy – generated through market reform – with the other. Britain's electricity market may, however, benefit from the recent adoption of the Windsor Framework. Upon leaving the EU, the UK also left the EU's Internal Energy Market, which created a single price for electricity by automatically balancing the needs between countries using computer algorithms to match bids and offers. Northern Ireland stayed in Ireland's Single Electricity Market and its participation was not affected by the dispute over the Protocol. Now the UK is on a backup system where traders have to buy and sell energy separately in different regions. This has decreased competition and efficiency, which, as a result, is thought to have somewhat increased electricity costs. The UK has struggled to finalise a new electricity trading framework with the EU while post-Brexit trade rules in Northern Ireland were still being resolved. Now that the	

	Arrangements (REMA) led by the Department for Energy Security and Net Zero, which the government describes as the 'biggest electricity market reform in a generation'. On 8 March, a summary of its consultation was published and the conclusion of a second consultation is planned to be released later this year. In light of the feedback from the consultation, the government has also said that smaller, short-term changes to the electricity market may be made 'more quickly where it is viable to do so'.	Windsor Framework has been signed, the UK government has placed renewed focus on this.	

22. ENVIRONMENT **PASSIVE DIVERGENCE** **INTERNAL IMPACT** *EU rules on maximum residue levels of two pesticides in food imports.*	**Summary:** The European Commission has adopted new rules which effectively ban the import of foodstuffs treated with two pesticides (clothianidin and thiamethoxam). The two newly restricted pesticides belong to the neonicotinoid family of substances (which are chemically similar to nicotine). Neonicotinoids are already banned from outdoor use in the EU, but the new restrictions mean products imported to the EU can only have the very lowest traceable levels – which is in effect zero – of these two specific pesticides. The move reflects a new regulatory approach being taken by the EU, under its Green Deal and Farm to Fork Strategy, to consider environmental impacts (and not just consumer health) when setting limits on the presence of substances in imported goods. Neonicotinoids are restricted because they are deemed by the European Food Safety Association (EFSA) to pose a high risk to pollinators, like bees. As systemic pesticides, they are absorbed throughout the plant, meaning that an imported crop which has been treated using neonicotinoids will still carry traces that can be passed on.	**Impact:** The rule changes have been described by Professor Alan Matthews as 'a hand grenade into global agri-food trade' because they effectively ban the import into the EU of any agricultural goods treated with two common pesticides. Neonicotinoids are the world's most widely used insecticides, with an estimated 24% market share, applied to a range of crops including cotton, corn, cereals and oilseed rape. Import restrictions will not apply before 2026, to allow adaptation time for non-EU countries including, of course, the UK. The UK has restricted the use of all but one neonicotinoid, meaning the EU import ban poses relatively little immediate risk to the British agricultural produce. However, in 2022 and 2023 it adopted emergency measures allowing the use of thiamethoxam (one of the two pesticides subject to the EU import ban) to protect sugar beet crops from the yellow virus. Should similar exemptions be triggered in future years (or, indeed, should wider restrictions on neonicotinoids be lifted as part of the Retained EU Law Bill or separate regulatory reform), this would prevent those crops from being exported to the EU. Similar exemptions have been applied in some EU member	**Timeline/region**: The EU measures will apply to imported products as of 2026.

		states but many are set to be ended under a new European Court of Justice ruling. Producers in Northern Ireland will also have to adhere to the new EU restrictions under the terms of the Protocol, which could put them at a disadvantage if they cannot use pesticides which competitors in Great Britain can (although on the other hand they would retain access to the EU market). One other major uncertainty is whether GB-origin food treated with such pesticides would still be exportable to NI (which depends on GB for three quarters of its supermarket food). Under the Windsor Framework, retail food which meets UK rather than EU rules can in many cases now be exported from GB to NI, so long as it is labelled as not for EU. However, goods still have to align completely with EU requirements on animal and plant health, to prevent the risk of transmissible diseases into Ireland and thus the EU. Given the new EU restrictions are based on the harm caused to bees and other pollinators, it *might* be considered a matter of animal health – meaning goods treated with those pesticides would not be exportable to NI. On the other hand, it could be deemed an environmental rather than animal	

		health risk. Moreover, a neonicotinoid-treated beetroot on a Northern Irish supermarket shelf (as opposed to growing in a field) does not seem to pose much risk to pollinators across the island of Ireland. If it can be argued that the restrictions amount to an update of existing EU legislation, and that they will have a significant and persistent impact on daily life in NI, its application in NI could be blocked by Assembly Members under the Stormont Brake (once the Assembly is re-established). Given the EU imports much of its food, there is a risk of supply shortages or price increases if producers worldwide do not largely stop using the two newly-restricted neonicotinoids. The EU will be relying on the Brussels effect: where non-EU operators conform with new EU rules to maintain access to its single market. There are also suggestions that the restrictions could be challenged at WTO-level, as it sets a significant new precedent on using trade rules to pursue environmental objectives.	

23. FISHERIES **PASSIVE DIVERGENCE** *EU restrictions on bottom trawling.*	**Summary:** The EU has set out a plan to ban the practice of bottom trawling in protected marine areas by 2030. Bottom trawling involves towing nets along the sea floor to catch fish. This can damage the seabed and result in the unintended capture of many species (including up to 41% of all invertebrate life). The restrictions will be phased in from this year, with member states required to take action to ensure greater protection for 'species in dire situation'. From 2024 this expands to cover a wider set of species, and by 2030 member states will need to establish 'measures that reduce or eliminate incidental capture of all species in unfavourable conservation status or threatened by extinction and protected under EU law, and any other sensitive marine species in need of protection.' The protections will apply only to Marine Protected Areas (MPAs), which are defined zones subject to specific protection objectives. The initial focus will be on 'Natura 2000' sites, which cover 12% of the EU's marine territory, and for which member states must adopt protective measures by 2024. By 2024, all EU member states will have to have defined at least 20% of their marine waters as MPAs,	**Impact:** The EU and UK share a common ambition to effectively protect 30% of their respective seas by 2030, yet their respective regulations on bottom-trawling reflect some differences in approach. The UK has moved much faster than the EU to designate around a third of its offshore waters as MPAs (whereas the EU only intends to reach 30% by 2030). However, both the UK and EU have been criticised for doing little to meaningfully protect MPAs, meaning these designations for now have limited effect. The EU itself notes that 'MPAs cover only 12% of EU seas, however they are not all effectively managed and less than 1% are strictly protected'. Meanwhile, a Greenpeace report from December 2022 found that '90% of MPAs [in the UK] are protected in name alone, with no meaningful, site-wide regulation on the most destructive fishing activity'. Recent developments show both the UK and EU seem to be trying to address these deficiencies, albeit in different ways. The UK appears to be opting for piecemeal restrictions, starting last year with bans on bottom trawling at four sites including Dogger Bank, which is considered a key site for marine biodiversity, followed by 13 more in early 2023 (albeit with the majority of these only offering partial	**Timeline/region:** The plan will be phased in gradually up to 2030.

	and, by 2030, protection measures must be implemented for all MPAs, with the target of covering 30% of EU waters. Similar, but for now more limited, proposals are under consideration in England. The UK has 76 offshore MPAs overall, covering 36% of its waters, and last year a trawling ban was introduced for four sites. The Marine Management Organisation (a non-departmental body sitting under Defra, responsible for English waters) is now seeking views on a draft byelaw restricting the use of bottom-towed fishing gear in a further thirteen MPAs. However, the plans have been criticised for only introducing full bans in three areas, with the other ten subject to partial bans on reefs and rocks (which are not sites suited to trawling in the first place).	protection for MPAs). The EU, meanwhile, has opted for a more comprehensive package with a fixed goal of banning bottom trawling in 30% of marine areas by 2030. Thus, the EU has a more concrete long-term 'action plan', but it offers little guarantee of protection in the shorter term. Indeed, the marine conservation group Seas at Risk says this 'is the first time the Commission is so clear about the problem' yet also sounded caution over the fact that the plan relies on the implementation of current environmental legislation which it says has so far 'not delivered effective protection'. The advocacy group ClientEarth has also criticised 'the lack of control and sanctions at sea' which has seen member states 'keep on ignoring scientific advice and… fishing limits'. The fact that member states have responsibility for devising and enforcing their own plans increases the risk of ineffective or inconsistent implementation across the EU. They will likely be subject to major pressure from fishing groups, many of which are actively opposed to the proposal. Indeed, the Commission seems to acknowledge the risk of member states taking limited action, as it notes that it will assess progress in 2024 and may 'consider whether further	

		action or legislation is needed to improve the implementation of the action plan'. The UK, through its more piecemeal introduction of protections, may thus be able move faster than the EU in imposing bottom trawling bans in the next few years.	

24. FOOD STANDARDS **PASSIVE DIVERGENCE** **INTERNAL IMPACT** *EU restrictions on maximum levels of arsenic in certain foods.*	**Summary:** The EU has adopted amendments to its regulation on maximum levels of arsenic in certain foods, reducing the level of arsenic permitted in baby food and infant formula by 80% and limiting its presence in certain other foods such as rice, juice and salt. The move is part of the EU's Beating Cancer Plan, which aims to reduce or remove the presence of chemicals associated with carcinogenic risk in food. It is based on a 2021 report by the European Food Safety Authority (EFSA) calling on member states to monitor the presence of arsenic in foods. Arsenic cannot be removed entirely from food but levels can be controlled. The EU first imposed restrictions on arsenic in food in 2015, after an EFSA finding that inorganic arsenic (found in soils and groundwater) may be linked to certain types of cancer.	**Impact:** The amendment is an interesting early testcase of the impact of the Windsor Framework, and how it changes processes for GB-NI trade. Under the original Protocol, GB-based food suppliers would have had to comply with the new EU arsenic restriction levels in order to continue selling into NI. Yet, under the Protocol as revised by the Framework, they will be able to continue exporting foods with arsenic levels higher than permitted by the EU, as long as they meet the wider criteria for access to the 'green lane'. This eliminates a potential new barrier to food exports from GB no NI. However, it is not yet entirely clear whether businesses in NI will also be able to choose whether to produce food to UK or EU arsenic standards. An initial analysis by Viviane Gravey and Lisa Claire Whitten at Queen's University Belfast concludes that exemptions from EU rules will not extend to NI producers. Regardless, the Northern Ireland Food and Drink Association says its members would likely adhere to the new EU's higher standards even if they have the freedom to diverge, in order to maintain access to the EU market. Moreover, the UK-wide baby food trade body BSNA says its members will also meet the new EU arsenic standards in	**Timeline/region**: The EU rule changes took effect from March 2023. The Windsor Framework is set to take effect in Autumn 2023.

		order to maintain EU market access, and points out that much of the baby food in the UK is already imported from the EU. So, while the Windsor Framework gives NI-facing businesses greater flexibility to align with GB standards instead of EU ones, this is an early indication that they may reject this in favour of continued alignment with the EU, for commercial reasons.	

25. PRODUCT STANDARDS **PASSIVE DIVERGENCE** **INTERNAL IMPACT** *EU general product safety regulation (GPSR).*	**Summary:** The European Council and Parliament have come to a provisional agreement on a general product safety regulation (GPSR). The GPSR applies to products – for example furniture, textiles and bicycles – which are not already subject to product-specific regulations. It updates the existing general product safety directive (GPSD), turning it into a regulation – creating a firmer legal framework with clearer responsibilities for certain actors – and expanding it to cover new technologies and online marketplaces (like Amazon and eBay). This reflects the regulation's core aims of putting greater responsibility for product safety standards on such marketplaces (rather than leaving it in the hands of individual sellers) and imposing tighter safety controls on goods bought online from outside the EU. Like the GPSD it replaces, the GPSR imposes a general requirement that manufacturers and importers 'only place on the market products that are safe'. This means conformity with product-specific safety standards which are developed independently by 'European Standardisation Organisations' and approved by the Commission. However,	**Impact:** As an EU member the UK adhered to the GPSD, and those regulations were copied over after Brexit, meaning there is presently a high degree of alignment in product standards. However, the updated GPSR will establish new safety standards in the EU – in terms of stricter requirements and wider product coverage – which do not apply in the UK. This has a range of potentially significant implications, which have been outlined by the Commons European Scrutiny Committee (ESC). First, UK manufacturers will have to adhere with the new EU regulations to continue exporting into the single market. This means an expansion of existing safety assessments, for example to consider risks associated with AI and software updates. They will also need to appoint someone within the EU to take responsibility for issues of compliance with safety standards, which is a significant new administrative and financial cost, and opens up the risk of being sued if a product does not comply with the necessary standards. There could also be new administrative and financial costs in establishing systems to meet new requirements around the traceability and recall of unsafe goods.	**Timeline/region:** The agreement was formally adopted in April 2023. It will shortly enter into force and member state will have to apply the new rules from 18 months later.

	the GPSR also introduces specific new safety requirements for a range of actors. Manufacturers will now have to consider risks related to AI and software updates in product safety assessments and adhere to new standards around traceability and recall of products; vendors will have to inform consumers when a product they have bought is being recalled and the consumer will be entitled to a repair, replacement or refund; online marketplaces must carry out due diligence on the sellers of products on their sites; importers of products (from within our outside the EU) must ensure a 'responsible person' (i.e. a legal representative) is charged with ensuring the correct technical documentation, instructions and safety information is in place; market surveillance authorities must now proactively sweep for unsafe products (rather than simply responding to complaints); and trading standards bodies may order the removal of a product found to be unsafe (including, for the first time, all identical products) from a website or disable access to the offer. The requirement around a 'responsible person' significantly increases the liabilities of non-EU manufacturers exporting goods into the EU, who now risk legal action if their products	Taken together, this all adds up to potentially significant new barriers to trade with the EU, especially for smaller businesses that have fewer means of meeting the new requirements. Indeed, the ESC notes that the UK textiles sector (which will be covered by the GPSD) exported £6.7 billion worth of goods to the EU in 2016 and 'is dominated by SMEs and micro businesses'. It is also worth noting that the new EU standards would apply to British businesses that form part of the supply chain for goods ultimately destined for the EU single market – meaning the application of the GPSR in the UK is likely to be quite wide-reaching. A second issue is the impact on Northern Ireland. The Protocol as revised by the Windsor Framework still requires NI to adhere to EU rules on manufactured goods, meaning the updated GPSR should apply. Thus, the new financial and administrative costs described above would apply equally to the trading of goods from GB into NI. There is, however, a heightened risk in the case of NI that GB-based suppliers do not bother complying with the new rule, because NI is a relatively small market and some may deem that compliance with the GPSR incurs higher costs than the amount of trade that would be lost from ending	

	do not meet the necessary safety requirements. It also creates distinct new responsibilities for online marketplaces, which did not exist when the directive was originally devised in 2001. They will now be expected to remove unsafe products within two days of being ordered to by a trading standards body, and allow users to flag potentially unsafe products.	exports to NI. The risk is thus a reduced supply of certain goods from GB to NI. However, the Windsor Framework's Stormont Brake allows NI Assembly members to seek to block the application of an updated EU regulation in NI if it entails a 'significant impact specific to everyday life in a way that is liable to persist'. The GPSR could thus be an important test case for the Stormont Brake. A third issue flagged by the ESC is that the UK has parallel plans in this area. A UK Product Safety Review policy paper was published in November 2021, promising a 'multi-faceted' reform programme to address many of the same regulatory challenges around product safety which the GPSR identifies, including goods bought online and market surveillance. The ESC also notes that the paper recognises that 'many of the challenges' around product safety are 'global in nature', meaning the UK 'will need to continue to take an international approach to tackling these'. We are yet to see what approach the UK will take and to what extent, if at all, it will align with the EU's GPSR. Should it become largely aligned, this would reduce the extent of new UK-EU and GB-NI trade barriers. However, the ESC notes that should the UK create its own enhanced safety	

		requirements which are different from the EU's, this could create yet more barriers to trade, as businesses would need to comply with two separate product safety regimes to access the GB and EU markets (rather than EU standards automatically being sufficient for GB). This creates a risk that a range of goods approved for the EU market are not re-approved for GB, though the GB market would still be open to goods produced in NI that meet EU standards.	

26. SECURITY & DEFENCE **PASSIVE DIVERGENCE** *European Defence Agency joint procurement of ammunition.*	**Summary:** 23 EU member states, plus Norway, have signed up to a European Defence Agency (EDA) project for the joint procurement of ammunition. This will include a two-year fast-track procurement of 155m artillery rounds, as well as a seven-year project focused on ammunition; soldier systems; and chemical, biological, radiological and nuclear equipment. Funding will be provided by the European Peace Facility (EPF) which is separate to the EU budget but is funded by member states. The collaborative procurement plans are the second of a three-track EU strategy for delivering more ammunition more quickly. The other two are to reimburse member states who send ammunition from existing stockpiles, and to increase the European defence industry's manufacturing capacity. The announcement follows a European Council commitment made in March 2022, shortly after Russia's full-scale invasion of Ukraine, to 'develop further incentives to stimulate Member States' collaborative investments in joint projects and joint procurement of defence capabilities'.	**Impact:** This is a significant moment in the EU's joint defence policy, as it is the first time joint procurement, based on common funding, has been used for ammunition. EU High Representative for Foreign Affairs and Security Policy, Josep Borrell, described it as 'breaking a taboo'. From an EU perspective, it is questionable whether it would have been as easy to move forward with taboo-busting joint procurement had the UK still been a member state, given its historic opposition to common defence policy. From the UK perspective, there is the countervailing question of whether it would have been happy to see this development as a member state. Yet, more relevant for the UK today, is the question of how to respond to the joint procurement plans as a third country. The 2019 UK-EU Political Declaration, largely agreed by Theresa May's government, included an ambition for UK collaboration in relevant projects of the European Defence Agency; and for the participation of relevant British entities (not – not the UK itself) 'in collaborative defence projects bringing together Union entities supported by the European Defence Fund'. However the Johnson government rejected any structured approach to external security cooperation in	**Timeline/region:** The first phase of the project – the fast-track procurement process – lasts for the next two years. Unspecified 'further steps' need to be taken before the project formally begins.

		the subsequent negotiations and access to the new EU procurement scheme is not included in the TCA. It is not clear whether the possibility of UK participation is now back on the agenda after the Windsor Framework agreement.	

27. STATE AID & SUBSIDIES **PASSIVE DIVERGENCE** *EU Temporary Crisis and Transition Framework.*	**Summary:** The EU has adopted a new Temporary Crisis and Transition Framework (TCTF) which loosens restrictions on state subsidies for sustainable technologies. Until the end of 2025, member states may provide enhanced subsidies for 'batteries, solar panels, wind turbines, heat-pumps, electrolysers and carbon capture usage and storage as well as for production of key components and for production and recycling of related critical raw materials.' The size of subsidies is limited to a certain proportion of investment costs, and varies according to a recipient's location and size, and the size of and type of grant. Grants can reach €150m (and up to 35% of the investment cost) in areas not in receipt of EU regional aid. This rises to €200m (and up to 40% of investment costs) in 'c-Regions' in receipt of some regional aid to support economic development; and to €350m (and up to 55% of investment costs) in 'a-Regions' receiving the highest levels of regional aid. In exceptional cases, 'where there is a real risk of investments being diverted away from Europe', member states may either match the subsidy on offer in another location (called 'matching aid'), or provide the amount	**Impact:** The TCTF reflects a further loosening of EU subsidy regulations following Russia's full-scale invasion of Ukraine. Rules were first relaxed in March 2022 to allow member states to support certain industries critically affected by the costs of the war. The original provisions remain applicable until the end of this year, but the new support for sustainable technologies lasts until the end of 2025, as part of a wider strategy – led by the Net Zero Industry Act (see entry #15) – for the decarbonisation of industrial production processes. The economic policy think tank ZOE Institute called it 'really good, really necessary, and really needed' in terms of supporting green investment. From a divergence perspective, this is a marked departure from the EU's usual approach to subsidies – also called 'state aid' – where it has traditionally sought to prevent awards which distort competition within the single market. Indeed, under the terms of the UK-EU TCA, a 'level playing field' must be maintained on state subsidies – meaning one side cannot allow awards which distort competition with the other. The UK could potentially argue that some awards enabled by the TCTF amount to a distortion of the TCA's level playing field, but so far it has not done so.	**Timeline/region:** The TCTF is effective immediately and runs to the end of 2025.

	needed to incentivise the company to remain in the EEA (the 'funding gap') – whichever is lower. This support can only be provided to projects in regional aid areas, or as part of projects involving at least three member states (with a 'significant part' taking place in at least two regional aid areas). It cannot be used to move investment to another member state and the recipient must also not have moved to that location in the two years prior. A revision has also been made to EU rules exempting the new awards from having to seek prior approval from the European Commission.	The relaxed rules under the TCTF have, however, led to concerns among smaller EU member states that it allows the largest member states to grant much larger subsidies which they cannot come close to matching – leading to greater imbalances in support across the EU. Indeed, 77% of subsidies approved under the initial Temporary Crisis Framework have come from France and Germany alone. The EU's response has been to allow higher awards for less economically developed regions, but it has been argued that this does little to address the disparities in how much member states have to spend on subsidies in the first place. There are also concerns that, despite higher subsidies being permitted for small- and medium-sized businesses, larger companies will capture the majority of the newly freed-up aid because they are more experienced at and better resourced for obtaining such funding. The new provision allowing member states to match subsidy awards from other countries has also led to concern that multinationals will game the system to their advantage. For example, by prevaricating on where to build a major new electric battery plant, in order to push the EU and another country (like the US or China) to outbid each other in a subsidy race.	

28. ENVIRONMENT / TRADE **INTERNAL DIVERGENCE** *Scottish deposit return scheme for drinks bottles.*	**Summary:** Following Humza Yousaf's appointment as First Minister of Scotland, the Scottish government has delayed its planned 'deposit return scheme' until March 2024. The new scheme will require retailers in Scotland to add 20p to the price of single-use drinks cans and bottles, which the customer can then reclaim by returning the used item for recycling. The legal framework was created in 2020 and the scheme was initially due to take effect on 16 August 2023. The delay reflects concerns from Scottish drinks businesses about the additional costs they will face - for instance the need to add new barcodes to products and to pay a £365 registration fee; or pay a 1p surcharge per item if no barcode is added. The scheme would also contravene UK Internal Market Act (IMA) principles which a) guarantee that goods produced or imported legally into one part of the UK can be sold into any other part; and b) prevent the enforcement of regulatory requirements which discriminate against goods from another part of the UK. The scheme requires a drinks container in Scotland to have a barcode (to prove where it was first bought), but under IMA principles this cannot result in barcode-less containers made elsewhere in the UK being	**Impact:** This issue highlights how the UK internal market makes it more difficult for the Scottish government to impose a piece of environmental legislation. If no exemption is granted for the regulation under the UK IMA, Scottish businesses will be at a competitive disadvantage (because of greater regulatory requirements) once the scheme comes in in March next year. The Scottish government could take several courses of action between now and then. One option is to continue with the scheme, accepting the competitive impact on Scottish businesses as a price worth paying for what it calls 'one of the most environmentally ambitious [schemes] in Europe'. Another option would be to open the dispute resolution process under the appropriate 'Common Framework' (used to manage potential policy divergence between Westminster the devolved governments post-Brexit) and seek an IMA exemption. Alternatively, the scheme could be reformed to regulate goods purely at the point of sale in Scotland, rather than imposing requirements (such as the imposition of a new barcode) during the manufacturing process. This would mean the regulation could apply to goods irrespective of where	**Timeline/region**: The deposit return scheme is set to take effect in Scotland on 16 August 2023.

	banned from sale in Scotland. Scottish manufacturers would thus face regulatory requirements which competitors in the rest of the UK would not, and, as 85% of drinks sold in Scotland are made elsewhere, the deposit scheme would likely have had limited immediate effect. The Scottish government sought an exemption to the IMA, which would require drinks containers made in other parts of the UK to comply with the new Scottish requirements. There is precedent for this (certain single-use plastic items made in England cannot be sold in Wales and Scotland, where they are banned), but UK Secretary of State for Scotland Alister Jack argued that the bar for approval 'very high indeed' and the UK government appeared set to reject the request. Jack had also publicly 'urged the Scottish Government to pause the scheme' due to 'legitimate concerns raised with me by businesses across Scotland and by stakeholder groups'. In theory the UK government could even try and block the deposit scheme in Scotland, under Section 35 of the Scotland Act, as it did with the Gender Recognition Reform (Scotland) Bill – though there is no indication that this is being mooted.	they had been produced, but would likely mean delaying the introduction of the scheme while it is redesigned. It is also important to note that the Defra is planning a similar scheme (though glass bottles will be exempted) for England, Wales and Northern Ireland, to begin in 2025, which the devolved governments have openly cooperated with Westminster on. Many of the difficulties around the impact on the UK internal market would be allayed if Scotland were to align its scheme more formally with Defra's. There is also the potential for some divergence with the EU, if a future Scottish/Defra deposit scheme requires bottles and cans to have new, specific markings added during the manufacturing process. This could create issues with importing drinks that do not have the necessary markings (though it is possible to design a scheme without such requirements). There is currently no EU-wide deposit scheme, but many EU countries have a scheme or are in the process of developing one.	

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