
ESSAYS IN REGULATION

Brexit and the political economy of regulation

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Preface and summary

This essay is a developed version of the Zeeman Lecture given at the Regulatory Policy Institute's Annual Conference on 26 September 2017 at Lady Margaret Hall, Oxford University. The motivation for the Lecture was that, in the period since the Brexit Referendum on 23 June 2016, politicians, interest groups, journalists and commentators have fed the public a steady diet of alternative facts and false or misleading propositions. The Lecture focused on three of a much wider set of such assertions and propositions. All are relevant to the future conduct of regulatory policy, though each in different ways. Each is associated with a cognitive style that I have called *convenient, selective myopia*.

The propositions are that: the European Economic Area Agreement will automatically no longer apply to the UK after Brexit Day; there will be a 'regulatory dividend' from Brexit; and the UK will be a 'rule-taker', if it remains in the Single Market. Most attention is focused on the second of these.

An implication of the evidence and reasoning is that the UK faces systemic problems in the ways in which its institutions approach economic regulation. In many policy areas the UK is not nearly as good as it likes to think it is, or that it pretends to be: there are tendencies toward an institutional complacency and smugness that is dysfunctional and inimical to adaptive and innovative rule-making.

The main point made is that there is no basis for expecting significant improvements in regulatory performance from Brexit *per se*, whatever form it eventually takes. EU regulation cannot safely be assumed to be a root cause of poor UK regulatory performance or of the deterioration in UK regulatory capabilities that has been evident for ten years or more now. These things do, however, warrant a 'made in the UK' label.

A target-driven culture has become embedded in the relevant practices and institutions, with a strong emphasis on 'delivering' specified outcomes. This culture, which comes from the central planning playbook, is increasingly far removed from the kinds of approaches to regulation that are most likely to promote the flexibility and adaptation called for in swiftly changing economic conditions.

Convenient, selective myopia means decision making based on a narrow field of vision. It fails to see things that are relevant to its assessments/decisions, particularly when myopia is convenient for the beholder, and it proceeds on an unexamined assumption that highly limited information sets are often sufficient to reach safe conclusions.

The paper ends with some speculative conjectures as to why there is now a political appetite for regulatory measures that can be expected to harm economic welfare. Explanatory factors identified include selective myopia, the signaling properties of regulatory measures, low public trust in government, low government trust in the public, and absence of clearly identified strategic policy purposes.

George Yarrow
9 October 2017

Brexit and the political economy of regulation

George Yarrow¹

1. Introduction: why political economy?

My principal point is that it is naïve and unrealistic to expect that there will be any easily available regulatory dividend consequential on Brexit. There will be opportunities for improvements in the conduct of regulatory policy post Brexit, but equally there will be opportunities for regression. What eventuates will depend chiefly on the UK's own efforts and that is not an immediately comforting thought: over the past ten years or so UK authorities appear to have become more inclined to pursue opportunities for regression.

The title of this essay refers to the political economy of regulation, because political economy is the name first used for a mode of thinking that sees economic policy as an exercise in the stewardship of a complex, adaptive, socio-economic *system*. The study of such systems requires examination not only of their individual agents and the more directly immediate interactions between agents, but also of: the wider webs of connectivities; the connecting principles in play; the rules that determine or guide interactions between agents; and the ways in which those rules adapt and change over time. The relevant rules include both the formalised, system-wide rules that we call law and regulation and the less formal (frequently more variegated) rules that might fall under headings such as ethical standards, social norms, common understandings and even habits. The discipline draws on thinking in economics, political science, law, sociology, psychology and ethics, and the general approach can be described as ecological in nature: it is interested in the functioning of a whole system.

Notwithstanding this generality, political economy has a specific focus and purpose, reflecting a particular feature of the ecosystems of interest: they are characterised by the presence within them of a Leviathan, a sub-structure or sub-order that holds and exercises very substantial power over the system as a whole. We generally refer to the relevant part of the overall social order as government or the state. Regulation is a major, but far from the only, aspect of its activity.

Political economy's focus is Leviathan's power and the exercise of that power. Its purposes are first to understand how the scope and exercise of the relevant monopoly or system-wide power affects the evolution of the ecosystem as a whole and second, at least in the classically liberal tradition, to assist in guiding the evolutionary development of the Leviathan in ways that will serve to *promote the flourishing of the ecosystem in all its significant parts*.

I will argue that UK regulatory governance is currently mal-adapted for this latter task and that Brexit will not, by and of itself, significantly alter this situation. Whatever form it takes, Brexit will necessarily bring changes to which the ecosystem will need to adjust and those required

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adjustments will differ as between the different ways in which Brexit might happen. However, the adaptive capacities/capabilities of the system are themselves chiefly determined within the system itself. Fundamental and systemic reform in the ways in which the UK Leviathan approaches its regulatory tasks are called for, irrespective of the eventual outcome of the Brexit negotiations.

2. Background context

Membership of the EU can be viewed as entailing commitments to three, broad strands in public policy which rest on:

- Enhanced Free Trade and Economic Cooperation Arrangements (EFTECA) aimed at reducing cross-border impediments to exchange transactions within the EU.
- A Customs Union, entailing the setting of common external tariffs and the establishment of immediately concomitant trade regulations (CU).
- A Programme of Political Integration (PPI).

The first of these accords with long established British commercial policy objectives and with a much longer tradition of ‘market development’. Reducing the costs of effecting exchange transactions is the primary purpose or function of those economic institutions we call markets.

In contrast, the centre of gravity of British public opinion has never been comfortable with the third aspect of the EU, i.e. political integration, and this discomfort appears to have tended to increase since the Treaty of Maastricht (1992) as the political goals of the EU have become more prominent. (It is notable that these goals were de-emphasised during the 1975 UK referendum campaign by those favouring EEC membership: attention was directed instead to the merits of an EFTECA + CU bundle, i.e. of what was then referred to as the Common Market.)

Public attitudes to the customs union element of the EU are less clear cut than they are for the EFTECA and PPI aspects, possibly because they are less widely understood. Customs unions can have trade expanding or trade contracting effects depending on the particularities of the relevant context and the specific details of the arrangements concerned. They might be likened to gated communities that reduce the height of internal fences, but which surround themselves with a communal wall. Much depends on the height of the communal wall.

The EU customs union has been problematic for Britain chiefly because of the high degree of protection it establishes in the agricultural sector. At the time of UK accession to the EEC in 1973 adoption of the Common Agricultural Policy (CAP) amounted to a sharp shift away from the unilateral free trade position that had been established by the repeal of the Corn Laws in 1846. In the course of the lead up to the UK’s first attempt to accede to the EEC (at the beginning of the 1960s) the then Labour Party Leader Hugh Gaitskell (an economist) said of the CAP that it was “*one of the most devastating pieces of protectionism ever invented.*”

The CAP has been subject to incremental reforms since Gaitskell’s time and significant further adjustments may occur if President Macron’s more ambitious aspirations are achieved. For the

moment, however, the EU Customs Union continues to sustain a highly protectionist agricultural policy.

Apart from its upward effects on domestic food prices, the CU element of the EU is also relatively unattractive for the UK in that it precludes the pursuit of an independent commercial policy by a nation with a high degree of global connectivity. The EU sets the common external tariff and acts as the sole representative of the UK (and of other Member States) in at least some global, regulatory organisations, e.g. the World Trade Organisation (in other international bodies there may be ‘double representation’, which itself is not always helpful). It is not so much the loss of voting rights in these bodies that is the problem – the UK vote is after all only one among many – but rather the shrinkage in the network of connections via which dialogue and mutual influence occur.

The EU has always been clear that membership is a bundle – EFTECA + CU + PPI – and that no cherry picking is possible. The referendum indicated that the dissatisfaction of the British electorate with the PPI and (less certainly) CU aspects of the bundle had reached a level sufficient to induce a majority of those voting to reject the whole package and to take their chances with what would follow next (no single, clear post Brexit policy strategy was articulated in the lead-up to the referendum and there has been no crystallization of such a strategy in the period since, i.e. up to end September 2017).

The Referendum has, however, provided an opportunity for the UK Government to unbundle its choice of commitments. An established EFTECA already exists in the form of the multilateral European Economic Area Agreement (EEAA), although it does not cover agricultural and fisheries products. It would be eminently feasible for the UK to continue to be a party to this Agreement in the immediate post-Brexit period (see section 3.1 below). The regulatory governance structure of the EEA is discussed in section 3.3 below.

The EEAA could also be readily combined with a re-negotiated customs union agreement or with some looser form of customs agreement, either for the very short-term as a matter of administrative expediency or for a longer period as a matter of strategic choice. In that case, only PPI would be ditched in the short term.

The Government has, however, expressed a desire to negotiate a new EFTECA on a bilateral, bespoke (‘made to order’) basis, although the reasons for this preference have never been clearly articulated. For the UK it is a slightly unusual preference, given that a succession of past governments of differing political stripes have tended to prefer multilateral approaches to international cooperation whenever they are feasible.

There are at least three difficulties with the bespoke approach: (a) it would likely not be possible to reach agreement in time for Brexit Day, (b) it might be resisted by the EU, particularly if it were seen as yet another attempt at ‘cherry picking’ (and EU resistance to cherry picking is not irrational – see the discussion of the Port Services Regulation at the end of section 3.2 below), and (c) even if feasible, as an analogy with bespoke garments might suggest, it could come at a much higher cost than an available ‘off the shelf’ alternative (e.g. the EEAA). There would also be the matter of future trade arrangements with Norway, Iceland

and Liechtenstein to sort out: leaving the EEAA would amount to abandoning an existing, EFTECA with those countries.

3. Misunderstandings, alternative facts and false propositions

Given this background, let me turn to three misunderstandings that have been well to the fore in public discourse in the post-Referendum period. The second and third are directly to do with misunderstandings of regulatory processes, the first is to do with the interpretation of the European Economic Area Agreement (EEAA). I start with interpretation of the EEAA both because of its high, immediate, policy salience and because it provides a vivid illustration of the ill-effects of a narrow field of vision when approaching public policy issues.

3.1 The post Brexit applicability of the European Economic Area Agreement

In the later part of 2016 the UK Government took an early view that withdrawal from the Treaty of Lisbon (Brexit) implied automatic withdrawal from the EEAA. The EEAA is a distinct, multilateral, international Treaty that allows non-EU States to participate alongside EU Member States in a Single Market, albeit a market with a narrower scope than the EU's Internal Market (the EEAA does not cover the agricultural and fisheries sectors and does not entail a customs union).

The rationale for this initial view is unclear. It may, for example, have developed from a simple, early confusion between the Single Market defined by the EEAA and the EU's Internal Market defined by provisions in the Treaty of Lisbon and the associated Treaty on the Functioning of the European Union (TFEU). Alternatively, it may have been founded on an inappropriately narrow, initial legal reading of parts of the EEAA's text. Then again, it could have represented a Machiavellian attempt to 'bury' a potentially contentious political issue.

Whatever the origins of the view, its subsequent 'justification' has been linked to legal interpretation. The principal reasoning is based on a narrow reading of Article 126(1) of the EEAA which says:

"This agreement shall apply to the territories to which the Treaty establishing the European Economic Community²⁰ is applied and under the conditions laid down in that Treaty²¹, and to the territories of Iceland²², the Principality of Liechtenstein and the Kingdom of Norway²³."

The argument is as follows. This is sufficient to show that the EEAA will not apply to the UK after Brexit, i.e. *no other factors need be considered*. The UK will no longer be a member of the European Economic Community and, unlike Iceland, Liechtenstein and Norway, the UK will not be separately identified in Article 126(1). Just as the EEAA does not apply to (an unreferenced) Australia, so it will no longer apply to the (soon to be unreferenced) UK.

This type of reasoning has an uncomfortable feel to it from the outset: in regulatory slang, it might be said that it does not pass the smell test. Should a major issue concerning the application of an international Treaty really be settled on such a narrow basis?

Consider, therefore, the following potentially relevant information that is revealed by a wider field of vision.

- The function of territorial provisions in international Treaties is to clarify the precise scope of the territorial commitments *of the Contracting Parties* when they sign and ratify the Treaty (and here the UK obviously differs from Australia, being one of the Contracting Parties listed at the opening of the EEAA and having signed and ratified the Agreement at the outset). The UK's territorial commitment was made around twenty-five years ago and can be changed only by agreement among the Contracting Parties to modify the EEAA itself. Such modification requires the unanimous consent of all parties, *including the UK*. Unless and until that happens, the commitment remains.
- Over 80% of the text of Article 126 of the EEAA, appearing at Article 126(2), is dedicated to the Åland Islands, a Swedish speaking archipelago in the Baltic Sea that is part of the territory of Finland. Whilst provisions for EU Member States' 'special territories' (such as Gibraltar and the Faroe Islands) are expediently made at 126(1) via the words "*under the conditions laid down in that Treaty*", the Åland Islands' provisions were necessitated by the fact that Finland and Sweden were originally non-EU Contracting Parties to the EEAA: in the absence of Article 126(2), new potential ambiguities, not previously addressed in an EEC context, could have been created.
- The EEAA has not in the past been interpreted in the narrow way apparently favoured by the UK Government, which, in the light of past practice, can only be regarded as a novel interpretation. Initially Austria, Finland and Sweden were listed alongside Iceland, Liechtenstein and Norway in Article 126(1), but their names have since been deleted, as explained in footnote 23 of the Article.
- Revealingly, the same footnote indicates that the deletion did not take place until 2004, over nine years after the accession of these three countries to the EU. The three countries were double counted for more than nine years! Amendment of the text of the Agreement, which requires unanimity, was done when it was expedient to do it, simply to bring the text back into line with realities. That exercise can easily be repeated, whenever convenient.
- Even more revealingly, the three States were not required to re-apply to join the EEAA when they acceded to the EU in 1995, in flat contradiction to what a narrow interpretation of Article 128(1) might suggest should have happened. Article 128(1) says "*Any European State becoming a Member of the Community shall ... apply to become a party to this Agreement. It shall address its application to the EEA Council*". So far as can be ascertained, no such application was made by any of the three States. The reason is obvious: Austria, Finland and Sweden did not have to apply to become parties to the Agreement because they were *already* parties to the Agreement, as the UK currently is and as it will remain unless the Government gives notice to withdraw according to the procedure laid down in Article 127 of the Agreement.

- Many international Treaties have not included explicit territorial provisions. In the age of European empires the UK and France signed Treaties that did not contain such provisions, the presumption being that the rest of the world would recognise that the signature of ‘France’ meant metropolitan France whereas the signature of the ‘United Kingdom’ was, in the absence of specific provisions to the contrary, meant to include the UK’s overseas territories.

What does all this add up to? The answer is, I think, ‘common sense’. International agreements necessarily take the form of incomplete contracts: they cannot feasibly provide for all the contingencies that may arise. The force of a Treaty or Agreement comes chiefly from the commitments of the Contracting Parties to shared purposes, not from textual niceties. The Vienna Convention on the Law of Treaties (VCLT) recognises this and EU jurisprudence shifts interpretation even further in the direction of giving a high weight to aims and objectives: the ECJ’s approach has been variously characterised as purposive, teleological, dynamic or as tending toward the *effet utile* approach to interpretation of French administrative law. It is clear that a narrow interpretive approach would serve to defeat the aim/purpose of the EEAA, as set out in Article 1(1), which is to strengthen trade and economic relations between the various Contracting Parties, a set of States that includes the United Kingdom. It would therefore be a wrong approach, under both international law and EU law.

The most that can be concluded from Article 126(1) is that its single sentence will be silent about the post-Brexit territorial commitments of one of its Contracting Parties, namely the UK, and that this could be a possible source of ambiguity (as for Austria, Finland and Sweden, the text will no longer be perfectly aligned with realities). However, it was precisely to address this type of eventuality that the VCLT, informed by the earlier UN Waldock Report, sets out in its Article 29 the normative principle that: “*Unless a different intention appears from the treaty or is otherwise established, a treaty is binding upon each party in respect of its entire territory.*” [My emphasis]

The challenge for those who would seek to cling to the exclusionary interpretation of Article 126(1) is therefore to establish a “different intention”. That, I think, is an impossible task, except insofar as the different intention (to the “entire territory”) could reasonably be held to be the territory defined by “the conditions laid down” in the EU Treaties (the words of Article 126(1)) from which the UK will be withdrawing. Either way, the EEAA will apply to the vast bulk of UK economic activity.

The Article 1(1) aim of the agreement is unambiguously expansionary, as was the policy lying behind the development of the EEA itself. It was, after all, the creation of the Delors Commission in the historical period following the fall of the Berlin Wall and the liberation of countries across central and eastern Europe from Soviet domination. There is no revealed intention other than to expand trade and deepen economic cooperation within Europe, first among the Contracting Parties to the EEAA and then possibly to other European nations (and the EEA was, in fact, considered as a possible option for central and eastern European countries).

If there is any residual doubt about this, a simple test is to ask those involved in relevant European Commission work on these issues at the time. That would almost certainly reveal that the contingency that is now in the process of eventuating was not even contemplated as a possibility at the beginning of the 1990s. Article 50 itself did not appear in an EU Treaty until around 15 years later. It would be difficult indeed to “establish” an ‘intent to exclude’ from a single sentence (and from that sentence only) that was drafted without having given any consideration whatsoever to the relevant issue.

Comments

The narrow legal mode of interpretation is unsystematic (it doesn’t consider the wider context to be relevant) and its dysfunctional effects have made appearances in some very different contexts. The Competition Appeal Tribunal (CAT) has given us a different metaphor for understanding its failings, based on an analogy with a digital image. The CAT has argued that the grounds of appeal in some of its merits-based cases can lead to ‘pixelated’ assessments. By this is meant that the ground of appeal can serve to limit the Tribunal’s field of view by focusing attention on a restricted set of matters (a cluster of pixels) in what might be a much larger picture. One of the points here is that the wider picture may well contain information that is relevant to assessing the significance and implications of the identified, small cluster of pixels themselves (in the limit it is easy to see that a single pixel would provide a viewer with very limited information indeed).

In regulatory contexts, when it is calculated and intentional, a reliance on narrow legalism in interpretation is often referred to as ‘gaming’ the rules. More generally in human affairs, there is a strong tendency, without any such conscious calculation, to believe that which it is convenient to believe. Thus, inconvenient facts disappear from the field of vision and attention is narrowly focused on observations and information that serve to support a maintained belief. This is usually referred to as *confirmation bias*. It can eventuate at both an individual and a social level, in the latter case for example in consequence of organisational or institutional attachments. It can be said to be prevalent in Leviathan’s domain. As the American historian Barbara Tuchman has put it: “*Once a policy has been adopted and implemented, all subsequent activity becomes an effort to justify it.*”

I will refer to the tendency, whether at an individual or at a cultural level, as *convenient, selective myopia*. It is highly inimical to good regulatory practice.

3.2 *The myth of a regulatory dividend*

Convenient selective myopia is a ubiquitous cognitive style and there is no very good reason for thinking that it is significantly less prevalent in the UK than in the country’s near neighbourhood. An important question for regulatory performance is therefore: how effective are the structures and cultures of regulatory processes in mitigating the myopia’s more dysfunctional tendencies? The relevant regulatory governance structures of the EU and a post-

Brexit Britain will differ in some fairly obvious ways, but there is scant evidence that this differentiation will lead easily and quickly to improved regulatory performance.

For example, any notion that a simple strategy of <deregulation> will do the trick can be quickly set aside: <deregulation> is an ideograph, not an operational principle of policy making (see Annex A). Moreover, as a matter of observation, the economic freedoms of commercial societies are in practice sustained by *longer*, not shorter, rule-books than are the tyrannies of command-and-control economies that organise themselves around the diktats of the very few who sit atop egregiously inegalitarian structures of economic power.

What we empirically observe are complex structures of commercial rules that have evolved over time, mostly by trial-and-error, sometimes by intelligent design, and sometimes by unintelligent design. As social and physical environments change over time, parts of the rules tend to become ill-adapted to their contexts, i.e. they become less fit for purpose. In some contexts, when judged in terms of their intended consequences the rules will be found to have become excessively constraining on economic conduct: in other contexts they will be found to be under-constraining, as for example when technological change gives rise to unintended, harmful side-effects that are avoidable via innovative rule-making. It is the effectiveness of rule-books in promoting the flourishing of the ecosystem as a whole that matters, not their lengths.

Looked at in this light it quickly becomes clear that recent UK rule-making performance has been wanting and that the chief problems have not emanated from Brussels. I will sketch out a few comparative examples drawn from my own experience of regulatory decisions, particularly, but not exclusively, in the energy sector. Considered together, they should be sufficient to cast severe doubt on the notion that there will be a regulatory dividend from Brexit.

The implicit evaluation criteria underlying the comments are drawn first from the generally agreed principles or characteristics of good regulation as set out in OECD, EU and UK official documents and as embodied in existing UK legislation. The most important of these for current purposes are proportionality, targeting and necessity. The meanings of these terms are indicated by the questions: Would the assessed costs of a proposed measure be substantially in excess of (disproportionate to) its assessed benefits? Can it be expected that a proposed measure will serve its intended purpose without creating significant unintended and unwanted side effects, e.g. distortions of competition? Are there less costly/harmful ways of achieving the same purpose?

To these I will add the more dynamic criterion of flexibility or adaptability, the capacity for policy strategies or rules to accommodate changes in the economic context in an uncertain future. That best practice regulatory guidelines do not draw attention to this aspect of things is perhaps an indication that selective myopia is a problem ‘all the way up’ the regulatory chain, right up to the formulation of principles themselves.

We may lack knowledge of what the future will bring, but we *know of* and should recognise this lack of knowledge (i.e. we know and should recognise that the future is highly uncertain).

That itself is valuable knowledge: it implies for example that, if the effectiveness of a strategy or regulation is assessed as being heavily dependent upon a particular long-term forecast being right, it is likely that the strategy or regulation will turn out to be ineffective. Some progress is also possible in assessing the nature, extent and implications of the uncertainties: for example, the longer the future time horizon the more likely it becomes that major, unanticipated events will occur. All this knowledge is potentially relevant to regulatory decisions, but it very frequently falls outside the field of vision.

3.2.1 Energy sector examples

Smart meters

The EU Third Energy Package (2009) called for 80% coverage of premises by smart meters by 2020 “*wherever it is cost-effective to do so*”.

In stark contrast, in 2009 DECC announced a UK target of 100% coverage without any equivalent cost-effectiveness condition.

Later governments have reaffirmed the policy and hence each of the Conservative, Labour and Liberal Parties has given it their endorsement. In effect, the programme amounts to a ‘ten-year plan’ in the mould of the Soviet system (the target is a quantity, not an economic value), but for a period twice as long as the five-year plans of old.

The difference between the two (EU/UK) approaches is substantial, for at least four reasons. First, as every network regulator knows, achieving the final 20% of coverage is liable to be much more costly (per installation) than the first 80%, greatly increasing the risks of disproportionate regulation. Second, the size of the cost disparities among installations implies a degree of cross-subsidisation (of some energy consumers by other energy consumers) that a competitive market might not be able to accommodate. This points to consequential potential distortions of competition in seeking to implement the policy. Third, doing more in any prescribed time interval generally implies higher per-unit costs. Fourth, and most important, the lack of a cost-effectiveness qualification implies very substantial loss of flexibility in responding to changing technologies and costs in the ten-year plan periods.

In consequence of the cost-effectiveness qualification, EU policy might reasonably be characterised as ‘*Install smart meters wherever it is cost-effective/economic to do so*’, which is not at all dissimilar to the Australian policy stance. The role of the 80% target is most likely just to act as a signalling device (see the conjectures at the end of section 4 below).

In fact, Germany and some other EU Member States have declined to implement national smart meter roll-out programmes at all. *Prima facie* these States might be labelled ‘cheats’ and compared with ‘virtuous’ Britain, but a more careful, second look at the position indicates that it is the UK that is the potential violator of the EU legislation (by opting for a disproportionately costly policy). Germany and the others will be in full compliance provided only that meters are installed “*wherever it is cost effective to do so*”.

The EU policy formulation is entirely sensible. Technologies have moved on since 2009 and there are now alternative ways of developing more intelligent grid networks in energy systems that can contribute to achieving the public policy aims at which smart meter programmes were originally directed. It makes sense to adjust an existing smart meter programme in the light of changing circumstances – that is just flexible/adaptable regulation – or even not to launch a programme built around quantitative targets in the first place, e.g. so as to maintain technological neutrality in the choice of means to reach a desired end.

What is not sensible is to plough on toward a specified target regardless to circumstances, turning a blind eye to the wider economic and technological changes that might be occurring. That is inflexible, non-adaptive regulation. It is the UK policy stance on this particular aspect of energy regulation.

Carbon abatement

The EU introduced the world's first major cap-and-trade arrangements (EU ETS) for greenhouse gas emissions (GHGs) in 2005, but then took a seriously wrong turn in 2007 when it added a second, target-based approach, inclusive of a renewables target for each Member State. In this case, the taking of the turning was chiefly initiated by German domestic politics: coalition-building in Berlin led to a decision that there should be an accelerated run down of output from the country's nuclear plants.

Unfortunately, these national, quantitative targets are dysfunctional *when combined with an existing cap-and-trade system*. It is the latter that sets the cap on EU emissions as a whole: the national renewables targets serve only to increase per-unit abatement costs. For example, a successful-but-costly Stakhanovite attempt to push the share of renewables output to higher levels in, say, country A than in other countries within a cap-and-trade system will lead to the sale of emission certificates that are surplus to requirements in A. Buyers of certificates will use them to support higher (than otherwise) emissions in other countries, offsetting the emissions reduction in A. What change are (a) the locations of the sources of the emissions, not the aggregate level of greenhouse gases emitted, and (b) the real incomes of consumers (lower in A, higher elsewhere).

In 2007 the Government agreed a renewables target for the UK of 15% of energy consumption, which was lower than the EU's target level of 20%. Stopping the clock at that point, it could be said that the UK had been able to mitigate, through negotiation, some of the ill effects of a misguided EU decision. As with smart metering, however, from 2007 onwards the UK has exhibited enthusiasm for going beyond EU quantitative targets, i.e. an enthusiasm for Stakhanovism. For example, in preparing for the Climate Change Act 2008, the Government's first intention was to commit to a 60% reduction (from 1990 levels) in GHG emissions by 2050, but, under no great external pressure, this was then tightened in the legislation itself to an 80% reduction.

The carbon policy approach now embedded in the UK system sets a sequence of five-year carbon 'budgets' aimed at establishing a long-term, time profile of emissions reduction from

UK sources. The word ‘budget’ is itself a misnomer: these are not budgets in the normal sense of the word (which are measured in currency units), but rather quantitative targets or quotas (measured in tonnes of carbon equivalent). They are currently set for a period through to 2032. Interactions with emissions in the rest of the world are largely ignored in the process, as is the evolution of the costs of carbon abatement over time as new technologies are discovered and applied. In consequence of this selective myopia, the feedback loops between prices and quantities that are characteristic of market systems are absent and the conceptual approach can reasonably be described as ‘central planning in one country’.

Given that technologies are changing rapidly and abatement costs are falling quite quickly, all this makes little sense. The facts could change substantially, but Leviathan would plod on with its pre-set plans, whereas adaptation calls for flexibility, including in the timing of carbon reduction efforts, not wooden-headedness.

As well as being costly and ineffective (in achieving its stated aim), UK carbon abatement policy has had distorting effects on competitive markets. Shortly after becoming Secretary of State for Energy and Climate Change in 2016, Amber Rudd said pointedly that: “*We now have an electricity system where no form of power generation, not even gas-fired power stations, can be built without government intervention.*” In other words, one of big sources of economic benefit, in my view the major source of benefit, from wholesale market liberalisation has been effectively destroyed.

Retail energy price control

The ‘default’ policy position of the EU in regard to retail energy markets is that prices should be determined by competitive processes that balance supply and demand. Until 2017, this was the default UK policy position too: indeed, alongside the Nordic countries, the UK pioneered the policy and persuaded the rest of the EU of its merits.

The relevant EU legislation does, nevertheless, provide for derogations that permit price controls to be implemented, provided that the relevant authority can justify the derogation on proportionality grounds by demonstrating that:

- the intervention is limited in duration to what is strictly necessary in order to achieve the public policy objective,
- it goes no further than is required in order to achieve the objective being pursued,
- it takes proper account of the categories of beneficiary supported by the intervention and of the differences between them that might call for differences in treatment.

The policy position is therefore broadly in conformity with the principles of good regulation.

Price controls in UK retail energy markets were fully removed about fifteen years ago, but a price cap has recently (1 April 2017) been reintroduced for customers using pre-payment meters. This followed a lengthy investigation of the sector by the Competition and Markets

Authority (CMA) and, whilst I personally did not favour the measure, the intervention can reasonably be said to have been made in conformity with best practice regulatory principles.

Extraordinarily, in the June 2017 General Election each of the two major political parties campaigned with manifestos calling for the introduction of much more comprehensive price controls in the retail energy market, which is characterised by the presence of six major suppliers and tens of smaller suppliers. In developing the price-control proposals there is no indication that the politicians concerned had any sense at all of regulatory principles or of relevant EU law. It was simply a case of populist politics in a context where living standards had been squeezed for an extended period, indicating that, as in respect of smart meters, the road to be travelled was signed ‘central planning’ (price controls are the concomitant of quantitative targets or quotas in Soviet-type systems).

A point for students of regulation to note here is that the squeeze of living standards itself was, in large part, attributable to previous poor regulation in other areas of government, prudential banking supervision being top of the list of culprits with climate change policy probably in second place. *This is a positive feed-back loop*: poor regulation begets more poor regulation. Better regulatory systems and cultures seek to establish *negative* feed-back loops, based on error correction, not error amplification. One possible characterisation of the current state of UK public policy is that it has managed to introduce a whole nest of positive feed-back loops into the ecosystem.

Undue price discrimination

EU energy legislation contains a general exhortation not to discriminate between groups of customers supplied on the basis of different types of retail tariff (standard variable, fixed contract period, pre-payment meter, etc.) The exhortation does not establish a ‘hard’ constraint, not least because competitive markets are characterised by (sometimes substantial) differences in price-cost margins in supplies made to different groups of customers. Rather it is an injunction against disproportionate (or what in older language might have been called ‘undue’) differences in these margins.

The general view of the UK energy regulator (Ofgem/GEMA) through until the end of 2007 was that competitive energy markets had not led to differences in price-cost margins that called for any corrective regulatory actions: they were not judged disproportionate/undue. Thereafter, the regulator came under increasing political and media pressure to ‘do something’ about rising energy prices, themselves largely caused by rising world prices of primary energy inputs, not by suppliers’ pricing strategies (retail margins were very low at the time). The ‘something’ that it was chosen to do was a prohibition on price-cost variations between customers *located in different regions*, i.e. a prohibition of *spatial or geographic price discrimination*.

The factual position at the time was that, reflecting the immediate, post-privatization economic landscape, each of those major retail suppliers that was a successor to a publicly owned electricity supplier had a high market share in one or more regions, but a very modest market

share in others. Suppliers tended to offer discounted prices (i.e. set low price-cost margins) in areas where they were weak in order to build business there. Each supplier was effectively a cross-entrant into territory held extensively by others.

Both internal and external economic (to Ofgem) advice pointed out that the proposed prohibition would be inherently anti-competitive – a new entrant building market share in a region where it was initially weak would be impaired in its ability to attract new customers. Lawyers pointed to the implied violations of both UK and EU policy principles. It was suggested to Members of the Gas and Electricity Markets Authority (GEMA) by some of its own that political and media pressures could be at least partly addressed by doing a less harmful ‘something’ in the form of a licence condition that would reflect the inter-tariff provisions of the EU Directive, *but would go no further than that*.

GEMA nevertheless opted to go much further than the EU Directive. Retail margins increased as anticipated by economic advice and the new licence condition was subsequently withdrawn, but not without first causing both immediate and enduring consumer harm. Retail margins have been significantly higher since the time of the intervention.

What is revealed here is a shift in regulatory focus from the large set of pixels that might be labelled ‘statutory duties and guiding principles’ toward the pixels of pleasing a Secretary of State and of seeking more favourable media coverage for the regulator. Notwithstanding legislation that pointed in another direction, GEMA chose to act in the manner of traditional civil servants, i.e. as a servant to a minister, not as an independent regulator. That this could have happened so easily in the face of internal opposition and outside professional opinion points to the existence of fundamental flaws in the current UK regulatory arrangements.

Counter examples

It is possible, of course, to find counter-examples to the above cases: there are contexts in which an EU Regulation or Directive has hindered the pursuit of UK policy objectives. The regulation of gas storage would be the first of my own experiences to spring to mind. In that case, at the relevant time the UK had liberalised the market to a significantly greater extent than other Member States and the EU legislation necessitated some backward steps.

If the aim were to draw up a detailed, overall balance sheet, much more time and space would need to be devoted to the evaluation exercise, but the aim here is more limited. It is simply to test whether it can safely be assumed that there will be an easily obtainable regulatory dividend from Brexit. More abbreviated comments will therefore suffice, not least because the points about to be made find corroboration in the discussion of non-energy sector examples in section 3.2 below.

My own experience of them indicates that that EU Regulations and Directives:

- tend to have relatively clear purposes with which UK domestic policy is very frequently aligned and,

- at least where they address substantive policy issues, i.e. are not very narrowly technical, tend to exhibit a degree of flexibility as to the means adopted to achieve those purposes.

It is to be stressed that these are tendencies only: it is easy enough to find examples where purposes are muddled (see above on renewables targets) and/or the prescribed means lack flexibility (ditto).

The combination of the above two characteristics is partly a consequence of the structure of the EU rule-making process. The legislation applies to 28 different countries, each with its own, distinct set of economic conditions. The general aim is rule harmonisation – and rule harmonisation is a near ubiquitous aim in ‘enhanced’ international trade agreements (because rule differentiation can be a major source of non-tariff barriers to trade) – but, for the most part, it is not ‘perfect’ harmonisation that is sought. In a sense, EU rule-making relies on an implicit proportionality/necessity test: if there are alternative ways of doing things that would achieve the purposes of the legislation, it would be disproportionate to select only one of them and to establish a blanket prohibition on the rest. In taking this approach, however, it is crucial that the purposes of the regulation be clear.

Another way of looking at this rule-making process is to see it as implicitly relying on the same sorts of ‘equivalence’ considerations that arise in the negotiation of Mutual Recognition Agreements (MRAs) in world trade more generally. It ‘internalises’ these considerations at a first, multilateral rule-making stage and the result is a degree of flexibility that allows for variations in implementation and interpretation.

The result is that, although a regulation may not be fine-tuned to the idiosyncrasies of a specific Member State, the flexibility that is afforded allows for mitigation of the effects that would be implied by a rigorous, one-size-fits-all approach. Such was the case for gas storage: there was an avoidable increase in regulatory burdens in the UK for sure, but the impacts could be (and were) mitigated by (legitimate) work arounds.

3.2.2 Other examples

Integrated pollution prevention and control (IPPC)

In 2004 the RPI published the results of a study for the Cabinet Office of the burden of regulation on (mostly small) businesses in the surface engineering sector. In the course of the study, compliance with the requirements of the EU IPPC Directive emerged as a major issue: at the time the Environment Agency was engaged in the process of implementing the Directive.

A general finding of the research was that businesses were rather more concerned about the *rate of introduction* of new regulations than about the length of the regulatory rule-books. Compliance with a long, but well established, rule-book could be routinized and, once it was discovered which parts of it were most salient for a specific business, the relevant provisions could be reflected in everyday procedures. New rules required substantially more time and effort to interpret, particularly at the proprietor or senior manager level.

EU Directives are typically a long time in the making and their general provisions are usually reasonably well foreshadowed. Once a decision is taken the Directive becomes a given. In interviews with the businesses, the IPPC Directive itself was not raised as a source of regulatory uncertainty: by the time of the study (2004) it was a given (it appeared in 1996). Of much more concern was the implementation process, which lay in the hands of UK authorities and which would settle much of the detail relevant to compliance. A Member State authority has considerable discretion at this stage of the process and here there was a knot of problems that were perceived to be potential sources of significant regulatory burdens and of disincentives to investment.

For example, the UK arrangements featured a split jurisdiction, with the Environment Agency (EA) taking the lead for businesses above a certain ‘size’ and the relevant local authority for businesses below that size. ‘Size’ was typically measured in volumetric (i.e. quantity) units such as the capacity of vats and varied according to the type of surface coating activity involved. EA jurisdiction entailed much higher compliance costs than local authority jurisdiction. There was, therefore, a discontinuous jump in regulatory costs at the relevant thresholds, which was an obvious barrier to expansion for small firms. There was much mention by businesses of strategies based on remaining small ‘to stay below the radar’, and even mention of consideration being given to investment projects that would *reduce* the capacity of plant in the event that the EA came to a particular conclusion on an issue.

This last comment raises another, generic point. Decisions about implementation details made by a Member State at the national level often appear to small businesses to be arbitrary, and hence difficult to anticipate. That is not, of course, how things look to the administrative agency concerned, because many of the decisions will hinge on considerations of administrative expediency and the agency will be familiar with the trade-offs in that dimension. However, business perceptions of arbitrariness translate into regulatory uncertainty: a decision is coming, but it is difficult to anticipate what choices will be made. The natural tendency in such circumstances is to hold back on making investment decisions whenever the payoffs from the investment will be materially affected by the decision to come. This is a phenomenon that we now observe at the macro-economic level in consequence of the Brexit process.

There is a widespread tendency for businesses to cry wolf about regulatory uncertainty, but it might be remembered that in Aesop’s fable the wolf is real enough. For those who haven’t seen regulatory uncertainty close up, here is a paragraph from EA draft guidance (issued for consultation purposes) on the surface treatment of metals and plastics, published in February 2004. It illustrates the kinds of problems our interviewees were grappling with.

“(THIS PARAGRAPH TO BE REMOVED FROM THE FINAL VERSION OF THIS GUIDANCE NOTE). On December 2003 Defra issued a consultation paper setting out a series of proposals to amend the PPC regulations. The amendments may affect the regulation of some installations in this sector of industry. As the consultation does not have any draft regulations it is difficult to know any specific details. Any operators potentially affected by this should respond to Defra. The closing date for responses is 12 March 2004.”

Roughly translated, the EA was in the same position in relation to Defra as the surface engineering businesses were in relation to the EA. It knew that Defra decisions would be forthcoming and that they would have implications for its own work and for the businesses that it was addressing in the consultation document, but it did not have clear sight of what those decisions might be. Regulatory uncertainty often comes in layers and one part of Leviathan is often blind to what another part of Leviathan is thinking and doing.

Going back to the Directive itself, it can be noted that it applies to all EU Member States, including Germany, which has continued to have an outstanding record in the development of small and medium sized engineering businesses. There were some complaints from surface engineering businesses that (pre-IPPC) EU regulations were less strictly enforced in some other Member States than in the UK, but neither Germany nor other, longer established Member States were mentioned in this regard. It is therefore difficult to conclude that the Directive itself was a major burden on small surface engineering businesses, other than it had the general effect associated with all *changes* in rule-books, from wherever they originate. On the other hand, we found that the implementation processes did give rise to adverse effects on investment and on competition.

The regulation of immigration or residency

The EU position on free movement of workers/persons is not itself entirely clear cut: it has evolved over time, is still evolving now, and can be expected to change again in the future, possibly even in a new and different direction. The expression <freedom of movement> tells us little about this process because it is an ideograph: it is necessary to look at relevant Treaty provisions and at their interpretation by the European Court of Justice to progress further.

When that is done, it seems clear enough that (a) the Treaty of Lisbon allows for some cross-border restrictions to be imposed, but (b) the ability of national governments to do so has become more constrained over time, particularly since the introduction of the concept of EU citizenship, formalised in the Treaty of Maastricht (whether or not this trend will continue is, as indicated, uncertain). The ‘wriggle room’ now is most probably insufficient to satisfy those Leave voters who attach a significant weight to immigration issues, notwithstanding Mr Blair’s attempts to persuade them otherwise.

The belief that the freedom of movement entailments of the EEA Agreement have broadly similar force as those of the Treaty of Lisbon may account for the maintained Government view that the UK should ‘leave the Single Market’. It is unfortunate for the public that this stance implies rejection of the EFTECA most easily available to the UK in the immediate future and doubly unfortunate in that the supposition on which it is based is quite wrong (and possibly the most damaging to public welfare of all the ‘alternative facts’ that are currently in wide circulation).

In actual fact, the EEAA allows national governments significantly more scope for *unilateral* imposition of limitations on movements across borders than the Treaty of Lisbon, not least because it does not entail a common EEA citizenship. The clearest simple indication of this is

to be found at EEA's Article 112. It implies that, if Britain had been a member of the EEA, but not the EU, Mr Cameron could have applied his desired 'emergency brake' on immigration *unilaterally*. Whether he could have enforced it effectively is a different matter (see below).

On the UK side of things, the Westminster Government has long had powers to implement a national immigration policy and to develop regulatory arrangements of its own choosing for non-EU immigrants. Immigration has indeed been controlled or regulated, but in ways that have, by a very large margin, failed to satisfy the Government's stated aspiration/objective that net migration per annum should be no more than 100,000, i.e. in the tens of thousands..

Since the recently leaked Home Office document indicates a post-Brexit intention to extend to EU citizens / EEA nationals something resembling the existing arrangements for non-EU immigrants, there is no immediate basis for an expectation that the changes would lead to any substantial increase in the degree of control that can be exerted over numbers. Doing the same thing over again and expecting different results is, if not necessarily insanity, at least highly questionable. What appears much more certain is that the suggested policy would increase bureaucracy and distort labour markets, the latter via the manifest discrimination that comes with what, in more gender-biased language, used to be called 'manpower planning'. It would be another step along the road to central planning, in this case of labour markets.

The political and administrative proclivity to favour more costly ineffectiveness is not dissimilar to that identified in discussing smart meters and carbon abatement. A common factor appears to be a degree of enthusiasm for regulation based on quantitative targets and administrative methods, coupled with an aversion to placing reliance on pricing mechanisms to allocate things that are scarce.

The evidence points again to failings in UK regulatory capabilities and capacities and to the conclusion that, because of these, there is no firm basis for believing that Brexit will improve matters. It is most probably the case that the provisions of the Treaty of Lisbon would preclude a UK Government introducing what might be judged a 'first best' policy by that part of the electorate most concerned about immigration. But UK immigration policy and its enforcement have shown no capacity to achieve anything close to such a 'first best' policy. The Lisbon Treaty has not been the major constraining factor, domestic policy capability has been.

The situation is much more clear-cut in relation to the EEA. There is, in fact, nothing in the Agreement that suggests that it would do anything other than hinder poor regulatory practices (i.e. policies characterised by undue discrimination, disproportionality, poor targeting, or refusal to contemplate potentially better alternatives). Non-EU members of the EEA can legislate unilaterally and the high-level test for EEA compliance is the "*good functioning of the Agreement*" (Article 97), which in turn ultimately turns on the effect of the national policy on the Agreement's Article 1(1) aim "... *to promote a continuous and balanced strengthening of trade and economic relations between the Contracting Parties ...*".

There is nothing necessarily "balanced" about large migration flows and nothing inherently contrary to the Article 1(1) aim in legislating to dampen them. The Brexit immigration debates

have drawn attention to the potential benefits to the UK of inflows of young workers, particularly skilled workers, but they have turned a blind (conveniently and selectively myopic) eye to the other side of the coin, the stripping out of younger, skilled workers from labour forces elsewhere, particularly in Central and Eastern Europe. The results in areas of out-migration are an older and de-skilled workforce, higher dependency ratios, worsening fiscal positions and, in some regions, depopulation. Those effects are not conducive to economic development in the countries and regions concerned, nor to the “balanced” strengthening of trade between the UK and the adversely affected countries.

The kind of proposals indicated by the recently leaked Home Office document are poorly crafted and so would likely prove problematic, i.e. not EEA-compliant. However, to argue that the UK must leave the EEA because the UK is incapable of developing better (EEA-compliant) immigration/residency policies is to point the finger straight at the real problem: a domestic policy system that is apparently unable to develop better regulation. To accept such an argument without making any serious attempt to design an EEA-compliant policy would simply be defeatism: for President Obama’s “Yes we can”, substitute “No we can’t”.

Listening to and watching debates on whether or not the UK would be able to control inward migration once the <freedom of movement> yoke has been removed reminds me of an old joke:

Patient with an arm in plaster: “Doctor, when the plaster comes off will I be able to play the violin?”

Doctor: “Yes, I am sure you will.”

Patient: “That’s great, because I have never been able to play it before.”

The limitations of the Home Office in the relevant regulatory matters have long been recognised. The newly appointed Home Secretary, John Reid, giving evidence in Parliament on the immigration directorate of the Home Office in 2006 said: “*Our system is not fit for purpose. It is inadequate in terms of its scope, it is inadequate in terms of its information technology, leadership, management systems and processes.*” It was and is also inadequate in terms of its policy design capabilities, although that is a problem that could probably more quickly and easily rectified: policy design can be contracted out by competitive tender. Improving on that past policy performance is where any potential regulatory dividends lie and, as already stated, where existing performance is little short of dismal, the dividends could be very large.

Food Safety and Animal Welfare: Regulation (EC) 2004/882

Regulation (EC) 2004/882 nicely brings together some of the pathologies and tendencies identified in the earlier examples. One of its principal concerns is the performance of the inspection regimes developed to meet food safety and animal welfare objectives, including the adequacy of financial resources made available to the relevant inspection authorities to fund their work. Specifically, the Regulation responded to concerns that some Member States were devoting insufficient resources to their domestic inspection regimes and that this in turn served

to increase risks of unsafe products entering the food chain and of animal suffering being caused.

The aims and purposes of the Regulation are widely shared. Few want to eat foodstuffs that are dangerous to health and few would want to see animals slaughtered in ways that entail suffering. Given international trade in the relevant products, inspection activities also introduce issues of economic externalities. Country A might cut inspectorate budgets and charges so as to benefit its own taxpayers or local farmers and food business operators (who might be at the margin of survival), even at the cost of increased health risks to its own population. However, at least some of the consequential, incremental risk (but not the benefits) would fall on consumers in other Member States to which food products are exported. There is therefore a clear, cross-border interest in the integrity of inspection regimes, indicating that the issues are such that international cooperation is potentially beneficial.

While the objectives of the Regulation are clear and are clearly stated, in its later sections the text becomes more convoluted and messy in its drafting. This is in part the familiar consequence of the fact that compromises were made among 28 Member States in the construction of its text. The default position established by the Regulation is a rather clumsy one: it is the specification of minimum rates that inspection authorities should charge food business operators for the authorities' inspection activities (these are in the nature of administrative charges, not prices determined in a competitive market).

As is to be expected, one size did not fit all and individual Member States pressed for provisions that would better fit with their own circumstances, giving rise to a familiar trade-off between rule-harmonisation and rule-differentiation. The UK and some other Member States sought flexibility to set more cost-reflective charges in accordance with the principle of risk-based regulation. That is, facilities that were operated in ways that gave rise to less risk of breach of standards, often in consequence of additional investment, can be inspected less frequently and/or less intensively and the lower costs of inspection can, to at least some degree, be passed back to the operators as a reward for their efforts and as a financial incentive to reduce risks by improving operational practices and performance. Provision for a risk-based approach was therefore explicitly endorsed in the mix of possibilities allowed for in the Regulation.

Thus, what emerged was a form of multilateral recognition agreement that accepted that alternative charging regimes were sufficiently 'equivalent' in their implications as to be generally acceptable to other parties. The UK Food Standards Agency (FSA) was therefore not hindered by the Regulation in seeking to pursue a risk-based approach.

What *did* hinder the FSA in its pursuit of risk-based regulation was Defra policy. The Department had, likely under pressure from UK food business operators and other interested parties, instituted a charge capping regime that operated *at the individual facility level*, not a cap on the total revenue that the FSA could obtain from food business operators in aggregate. The facility-level charging structure could not, therefore, feasibly be adjusted in the way the FSA wanted, although the arrangements did allow some very limited scope for adjustment in the desired direction.

At this point the FSA went back to the text of the Regulation and, in effect, made the same mistake as has been made in the interpretation of Article 126(1). That is, it took a pixelated view of the text of the Regulation, focusing on one sentence concerning the setting of minimum prices, which it read as a black letter prescription. Other parts of the Regulation, which contradicted this interpretation, were ignored, as were the clearly articulated aims and purposes of the Regulation. The result was a charging system characterised by some substantial, arbitrary variations in charge-cost margins, as was pointed out in a subsequent, highly critical National Audit Office (NAO) Report. The NAO Report on the matter is written in restrained language, but in reading through its various points a less restrained judgment might be that what the FSA had done was beyond crazy.

For the FSA, the Defra charge controls were a given, but the interpretation of the Regulation was not. It would, for example, have been easy enough to send an email to the relevant section of the European Commission to seek guidance on whether an implementation of the Regulation that at least edged a little toward risk-based regulation (which, given the Defra policy, was the best the FSA could achieve) would or would not have been compliant. Had the FSA done so, I think that it is highly probable that it would have heard back that it (the FSA) was much less constrained in what it could legitimately do than a pixelated approach to the Regulation would suggest. EU interpretation of legal documents is, as discussed earlier, notoriously purposive, not pixelated.

To summarise, the poor regulatory outcome in this case was not attributable to the constraints imposed by the Regulation, but rather to a combination of Defra charge controls and *a failure to understand* both the Regulation and EU interpretive methods applied to legislation.

Counter examples: the Port Services Regulation

As in relation to energy regulation, it is possible to find situations where EU or EEAA legislation gives rise to more prescriptive or higher-cost regulatory outcomes than the UK would opt for on a unilateral basis. These tend to occur in contexts where the UK has reached a substantially more liberalised market position than other Member States, as was the case in gas storage around 15 years or so ago. An obvious sector to look in this regard is telecoms, where Oftel blazed a trail in the later 1980s and the 1990s.

The number of contexts in which the UK is significantly further down the road signed ‘market development’ than many other EU Member States has, however, diminished substantially over the past ten years or so. That is a consequence of the UK taking a turn-off along the road toward ‘central planning’ and developing embedded regulatory cultures whose limited field of vision has been increasingly centred on quantitative targets and price or charge controls. Where once the UK was at the front of the group of walkers on the market development road, it is now wandering off in a quite different direction in a range of regulatory policy areas.

My chosen counter example will therefore be the Port Services Regulation (PSR), which covers an area of commercial activity in which UK has not (yet) become a laggard in regulatory practice. It may be the last major EU Regulation to come into force before Brexit Day – it is

due in March 2019 – and may therefore come to be afforded some prominence and symbolic significance around that time.

The Regulation has been about fifteen years in development, reflecting the contentious issues that it seeks to address. British port owners have been critical of a number of its aspects and have lobbied against them. They have a case, but the strength of the case depends what questions are being asked.

The underlying issue is that privatization and liberalisation have led to an ownership structure in the UK that is materially different from that typical in much of continental Europe, where ports tend to be publicly owned and financially supported from public funds, often in highly non-transparent ways. The continental structure gives rise to potential distortions of competition between ports and to issues to do with discriminatory access to port services among those who would use them. The PSR is directed at these market-distorting effects of what is, in effect, a systematic pattern of State Aid.

Viewed from a UK perspective (the UK pixels) and *assuming other things are equal*, the PSR appears to be disproportionate. The problems it addresses do not eventuate, at least to anything like the same degree, in the UK ports sector and some of its provisions are therefore overly restrictive and burdensome. UK port owners would therefore like to see more fine tuning in the Regulation to reflect the UK context, for example via the possibility of exemptions.

Now view things from a wider perspective, however, and note the *other things equal* assumption. The intended effect of the PSR is to hinder the pursuit of discriminatory and market-distorting competitive strategies on the part of publicly subsidised ports. If achieved, that effect would be favourable to UK ports: they would be able to compete on a more level playing field with continental ports. Considering its effects in their entirety, therefore, it is not immediately clear whether the PSR would or would not be net beneficial to UK port owners (compared with an outcome in which it was binned). There are costs to UK port owners that could be avoided by binning, but there are also potential benefits to UK port owners from this (non-optimized) Regulation in the form of an improvement in their competitive positioning relative to continental ports. There are swings and roundabouts to assess.

Of course, what would be best for the UK ports would be for the Regulation to bite on continental ports, but not on British ports. There is certainly a case for that based on regulatory principles: regulation should be focused only on identified problems and shouldn't do more than necessary to address them. That, however, is an approach that is typically taken as normative when there is a *single* decision-making authority that does not require the consent of others to act. Whatever its longer-term aspirations, the EU is not close to satisfying that condition right now: a wider consent is required to proceed with any given draft Regulation.

In circumstances where the consent of more than one party is required – and bilateral trade agreements satisfy this condition too – agreement is not to be expected if, notwithstanding an overall benefit, there are net losses to parties who can veto the agreement. Nor is agreement necessarily to be expected even if all parties benefit, if the benefits are distributed in a highly

asymmetric way. That is the implication of the now very extensive empirical results in the research literature on the Ultimatum Game. A belief that agreements will almost necessarily be reached wherever it is mutually beneficial to do so – a frequently expressed view in Brexit debates – is just another example of selective myopia: it ignores a large body of evidence that this is frequently not so, it requires that a blind eye be turned to some important aspects of human nature

Brexit offers no escape route from the trade-off: in any complex agreement there will usually be swings and roundabouts. One party (e.g. UK port owners) cannot necessarily expect to be able to fine tune an agreement to get a greater benefit without offering something of significance to others in return. Other things are almost never equal in these processes of agreement, and they are not in the ports case. Other parties may balk at an agreement that is overly favourable to the interests of one party, even if it would, in some overall sense, be beneficial and *even if there would be benefits all round*.

3.3 UK rule-making influence in the Single Market

It has been repeatedly asserted in Brexit discourse that, if it remained a Contracting Party to the EEAA, the UK would be a ‘rule-taker’ with no control over a swathe of market-related regulation, but the proposition is manifestly false (as also is the similarly repeated assertion that the EEAA entails substantial financial contributions to the general EU budget).

A full understanding of why it is false requires a detailed examination of the provisions of the EEAA and the rule-making and adjudication structures and processes that it has established. Here I will swerve around most of this exercise by simply listing the channels of influence that would be available to the UK as an EEA member and by drawing attention to Article 102 of the Agreement, a copy of which is attached at Annex B. These channels encompass some aspects of influence/power that can be described as ‘hard’ and other aspects that can be described as ‘soft’.

3.3.1 Channels of influence

Indirectly via international rule-making bodies

As has been correctly pointed out by some commentators, post Brexit the UK will acquire its own seat at global rule-making bodies such as the World Trade Organisation where it is currently represented by the EU. Since the decisions of such bodies affect EU Regulation, this will provide an indirect channel of influence on EU rule-making itself. The same is true for international bodies for which there is double representation: with a fully independent voice, the UK may become more influential even in bodies where it already has a voice.

A good example of these points is Norway’s seat at the International Maritime Organisation, whose “... *main role is to create a regulatory framework for the shipping industry that is fair and effective, universally adopted and universally implemented.*” Shipping is, of course, a

relatively important sector in the Norwegian economy and the country has a strong, fully independent voice at the IMO. And IMO regulations have influence on EU regulations.

'Decision shaping'

The EEAA gives non-EU members of the EEA rights to appoint their own experts to participate in the preparation of EU legislation that might be 'EEA relevant' (see further below). This largely means participation in work of the European Commission.

Those attached to the rule-taking assumption tend to emphasise the UK's prospective loss of voting rights in the European Council – which, it can be noted, is an outcome implied by all Brexit options and therefore an irrelevant factor when comparing one Brexit option with another – but in reality the vast majority of decisions on regulatory matters, in which the devil is very, very frequently in the detail – are not made at Council level or via formal voting: they are made prior to the Council stage. Indeed, it is precisely because of this that the European Commission is itself such a powerful body. That the Commission *should* have such power can be questioned, but for EU Member States it does and decision shaping provides access to the relevant processes.

No other, currently articulated Brexit option does this. The EEAA may provide less rule-making influence than membership of the EU, but it gives more rule-making influence than other Brexit options. If the resulting EU Regulation or Directive comes to be adopted by the EEA (see below), such participation in the first-stages of rule-making would not only provide a channel of influence on market rules in the UK, but also on the market rules in the UK's major export market (i.e. other EEA countries, including non-EU members), which currently accounts for around 50% of UK exports. Assessed relative to other enhanced free trade agreements around the world, this would be a highly *privileged* position.

Incorporation of EU legislation into the EEA

The two-pillar governance structure of the EEA is illustrated in the table below. The left-hand column shows the EEA EFTA States and their institutions, while the right-hand column shows the equivalent institutions of the EU side. The joint EEA bodies are in the middle. The European External Action Service (EEAS) is the EU's diplomatic service. The 'EFTA' label does not signify that European Free Trade Association (EFTA) membership is a condition for participation of non-EU States in the EEA: it is, in the context of the EEA, simply used as a convenient, collective label for three independent States in the manner of the usage of the term 'Baltic States'.

The Agreement does not prevent non-EU Contracting Parties legislating independently in areas covered by the Agreement, e.g. free movement of workers/persons (see Article 97). Nor is incorporation of EU legislation in the EEA rule-book automatic. It has to be approved by the EEA Joint Committee. The UK would, as a member of the EEA, sit on the Joint Committee and would, under current arrangements, chair the Committee for six months in every four years.

Non-EU governance pillar	Joint Bodies	EU governance pillar
Iceland Liechtenstein Norway	EEA Council	EU Council Presidency and EEAS
EEA-EFTA Standing Committee	EEA Joint Committee	EEAS
EEA-EFTA Surveillance Authority		European Commission
EEA-EFTA Court		European Court of Justice
Committee of MPs of the non-EU States	EEA Joint Parliamentary Committee	European Parliament
EEA-EFTA Consultative Committee	EEA Joint Consultative Committee	EU Economic and Social Committee

Much EU legislation does not make it as far as the Joint Committee, because it is plainly not EEA relevant, i.e. not relevant to the operation of an agreement that has a much narrower objective and much narrower scope than the EU Treaties. Automatically excluded regulation includes swathes of EU legislation to do with agriculture, fisheries, the customs union, the euro, EU citizenship, foreign affairs (including trade negotiations), home affairs and justice, and taxation.

Those regulations that do come to be considered by the Joint Committee can be, and in practice often are, amended before incorporation into the EEA rule-book. Where they occur, these amendments are mostly of a technical nature (e.g. replacing the words ‘EU citizens’ with the words ‘EEA nationals’), but they can be more substantive. In the event of particularly substantive disagreements, the EEAA (signed as long ago as 1992) allows for the possibility of proceeding by reference to considerations of ‘equivalence’ (see Article 102(4) in Annex B), i.e. a judgment that, although a significantly amended EU regulation or EEA alternative might

differ from an EU original version, it nevertheless effectively serves the same purposes. Equivalence assessments underpin Mutual Recognition Agreements in international trade.

Differences in interpretation

The same words can have different meanings or interpretations in different contexts and the EEAA and EU Treaties establish two different contexts. Their provisions differ and, perhaps more fundamentally, so do their aims.

The most salient illustration of recognition of the possibility of different interpretations is the EEA Joint Committee's Declaration that accompanied the incorporation of the EU's Free Movement of Persons Directive in 2007. The Directive was subject to technical amendments only. However, the Joint Committee made a Declaration that explicitly drew attention to the almost inevitable bifurcation in future interpretations of the same text by the EEA-EFTA Court on the one hand and the European Court of Justice (ECJ) on the other. The Declaration opened by stating that "*The concept of Union Citizenship as introduced by the Treaty of Maastricht (now Articles 17 seq. EC Treaty) has no equivalent in the EEA Agreement*" and went on to state that the EFTA Court could not be bound by ECJ interpretations on free movement issues which depended on citizenship rights. In a second paragraph the Declaration of the Joint Committee also said that "*The Contracting Parties agree that immigration policy is not covered by the EEA Agreement.*"

The de facto veto

The EEAA provisions state that, in reaching decisions, the non-EU members of the EEA must "*speak with one voice*". What this implies is that each non-EU member has a *de facto* veto on the incorporation of EU legislation (after appropriate amendment) into the EEAA since, if the non-EU parties are unable to reach a *consensus* among themselves and are therefore unable to speak with one voice, incorporation will not occur.

The power afforded by the veto is contingent on the size of the economy wielding it. It can only prevent the application of a Regulation to the EEA, not to the EU's internal market. Thus, whilst it has been referred to as the 'nuclear option' by some Nordic commentators, the harm that would be caused to EU Member States by its use is currently very limited. The power/influence that it affords is likewise limited. However, one of the effects of the UK staying in the EEA would be to greatly leverage that influence (for other non-EU members of the EEA as well as the UK), because of the much greater significance of UK markets to EU Member States.

Parliamentary sovereignty

The establishment of the two-pillar governance structure of the EEA was heavily influenced by the refusal of the non-EU Contracting Parties to surrender any aspect of the sovereignty of their national parliaments. Even if EU legislation or an amended/equivalent version thereof has been accepted by the EEA Joint Committee, for non-EU Contracting Parties the legislation ultimately requires national parliamentary approval: there is no 'direct effect' of EEA

legislation and, unlike the ECJ, the EEA-EFTA Court has no ability to impose financial penalties on an EEA member in the event that its parliament denies approval for agreed legislation.

In practice, matters are usually sorted out at the earlier Joint Committee stage, but it is possible to envisage circumstances in which a national government speaking at the Joint Committee might be out of tune with its own parliament on a politically sensitive issue (in the UK right now it is perhaps all too easy to envisage the eventuation of such circumstances).

The EEAA's Financial Mechanism

The one, material financial entailment of the EEAA for non-EU Contracting Parties involves the provision of support to reduce economic and social disparities between EEA regions. The sums of money involved are negotiated periodically, in alignment with the EU's budgetary cycle.

The resulting 'EEA Grants' provide a 'soft' channel of influence in that the supported schemes and projects are agreed, managed and operated by the non-EU EEA States themselves, together with the individual, beneficiary States: the EU is not involved. This provides for *direct* contact and cooperation between States, a channel that can serve to develop deeper mutual understandings.

This type of soft influence/power can be seen where such mutual understandings have already been developed to a high level. Norway has no vote in the European Council: Denmark does. Norwegian government officials talk to Danish government officials, just as Adam Smith (a Scottish customs official) corresponded with Andreas Holt (a Danish customs official) over two hundred years ago. People in the same trade influence each other and the more channels of interaction the more the influences. The EEAA Financial Mechanism provides multiple channels of communication and interaction on matters of mutual interest, because a significant number of EU Member States are beneficiaries: Bulgaria, Croatia, Cyprus, Czech Republic, Estonia, Greece, Hungary, Latvia, Lithuania, Malta, Poland, Portugal, Romania, Slovakia and Slovenia.

Sequential and cumulative effects

Taking a European Council vote as the zero point, some of the points of influence set out above occur at an earlier time and some at a later time. The sequencing is significant because, for example, at the decision shaping stage, which is prior to the EU voting stage, participants will know that, so far as EEA matters are concerned, there will be stages to come *after* the EU voting has occurred. This, I think, serves to leverage influence at the earlier, decision shaping stage. Any inclination to think that the views and sensitivities of non-EU states can be disregarded in the development of Regulations, on the ground that they have no votes at the European Council, is mitigated by the foreknowledge that there will be a later stage at which the non-EU States will have a *de facto* veto, at least in relation to the application of a Regulation to non-EU territories in the EEA.

When all of the above points are taken together, it seems difficult to conclude other than that the UK could potentially have significant rule-making influence. As always, however, the extent to which it could take advantage of the opportunities would depend on the UK's own capabilities.

3.3.2 *Norwegian complaints*

In considering this conclusion, it is reasonable to ask: why then have Norwegians, who are in a good position to appreciate the EEAA arrangements, complained about having to be rule-takers and having to endure 'fax diplomacy' (Brussels faxes the Regulation to Oslo and Oslo has to adopt it – and note that the technological reference dates the complaints a little)?

There are some immediately obvious responses to this question, starting with the point that, given the economic sizes of the current non-EU Contracting Parties to the EEAA, it is pretty much what anyone who has sat through an A-level course in economics or Economics 101 at university might expect. Economics students are taught, reasonably enough when establishing some first footholds in the subject, that small firms in a market tend to be 'price takers' who have little influence on the determination of market prices. In contrast, businesses with substantially larger market shares tend to have price influence.

Rule-making is not so easily reduced to algebra or geometry as price-setting, but the underlying reasoning, which is about relative power, is the same. The *de facto* veto leverages the power of the non-EU members of the EEA, but the initial base that is leveraged is very low indeed. One reason for this lies in the economic structures of Norway and Iceland. Oil and Gas dominate Norway's exports and are traded globally. Shipping is another important sector, but much the most important source of relevant shipping regulation is the IMO, at which the country has its own seat, not the EU. Fishing is important for both countries, particularly for Iceland, but the EEAA does not cover fisheries policy. Adjusting for these factors, the level of trade on which EU/EEA regulation has a major bearing is very small indeed relative to any EU comparator.

Looking at matters from a policy perspective, whilst Norway can make use of each and all of the channels of influence just listed, it is easily understandable why it doesn't choose to devote significant resources to each and all of them.

These considerations are important in thinking about a possible future in which the UK continues to be a Contracting Party to the EEAA, at least in the early post-Brexit years. It is unfortunate that discussions of the 'Norway Option' have been so heavily focused on how things are now and have been in the past, when there is every reason to think that the possible future would be rather different. The balance in the weight of numbers in the EEA would change substantially and any cost-benefit assessments will likely point to active UK participation in decision shaping and in the Joint Committee (think of the weight to be attached to the UK's interests in financial markets, for example). It would therefore be less misleading to speak of the 'EEA option', not the 'Norway Option', and to pay more attention to the future opportunities that would be opened up by it.

4. Final reflections

The notion that UK economic performance has been held back by a regulatory <Brussels yoke> did not, I think, play a significant role in the Referendum outcome. To the extent that the issues were covered they were largely subsumed within the exhortation to <take back control> and the force of that ideograph came chiefly from other elements such as control of immigration, parliamentary sovereignty, legal supremacy and budget payments.

The regulatory issues have, however, come more to the fore in the post-Referendum period, because they are much more salient to the question *what next?* In particular, they are relevant to evaluation of the EEAA option, which is opposed by both hard-line Brexiteers and hard-line Remainers alike. For both these groups the propositions considered in sub-sections 3.1 and 3.3 above are convenient, because, if true, they would weaken the case for an option that is a potentially attractive alternative to their own, most favoured options. As I hope I have shown, both of the propositions are false, but they are nevertheless sustained by convenient, selective myopia.

That cognitive style is also heavily implicated in the poor regulatory practices explored in section 3.2, which directly addresses the <Brussels yoke> thesis. The examples given are not suggestive of any easily available regulatory dividend from Brexit and point rather to a conclusion that UK regulatory practice is nowadays suffering from systemic dysfunctions.

One of the issues not touched upon in the paper is the decline in UK participation in EU regulatory processes: the proportion of Commission staff accounted for by the UK has fallen sharply over the years (some decline was to be expected from EU enlargement, but the reduction in numbers goes far beyond anything that can be accounted for by that factor). I mention this here because it might be an indicator of systemic failures that go rather wider than the kinds of regulatory decisions discussed.

For example, in his Speaker's Lecture of 12 September 2017, Francis Maude said this of his expectations of the civil service on his return to Ministerial Office in 2010: "*Based on my experience as a Minister in the eighties and early nineties my expectations were high. And the disillusionment was steep and distressing.*" Lord Maude made it clear that this remark was not a criticism of individual civil servants, and indeed that bright young civil servants were among those who were adversely affected by institutional failures. It was a critique of a *system*, carrying with it the implication that *systemic* reform was required. The remarks of Dr Reid and Ms Rudd, cited earlier, add to this sentiment.

Irrespective of the Brexit outcome, improvements in regulatory practice will depend on confronting the realities of poor *system* performance. The first step along the way is to recognise that there are large potential improvements to be made: a smug complacency is not an attitude that will promote progress. A useful image to hold in mind might be a Ferguson/Guardiola/Mourinho dressing room. Fortunately for them, those gentlemen have had

the discipline of competition to assist them in their work, whereas the servants of Leviathan, the ultimate monopoly, do not. Leviathan can do what it will and the ecosystem will suffer what it must, for a while at least (but civil society will not tolerate indefinite haplessness: there are negative feedback loops in the wider ecosystem).

Emphasising the scope and depth of current dysfunctions may be dismissed as doom mongering, but that would just be yet another example of selective myopia. Looking at the other side of the same coin, an immediate implication of the points made is that there are opportunities to achieve very substantial improvements in performance, and for this purpose, as Churchill put it in rather gloomy circumstances, “Facts are better than dreams”.

A realistic appreciation of how things stand is, of course, only the starting point in charting a path forward. A next step is to develop an understanding of how things came to be as they are, and after that there is the task of developing effective reform strategies. Those are tasks for tomorrow rather than today, but let me end with one or two general thoughts about them.

We have a broad knowledge of what types of regulatory stewardship work in promoting a flourishing economic system, drawn from earlier thinking and from historical experience. In its specifically commercial aspects, the most effective strategy can be referred to as ‘market development’. It is the painstaking and never-ending process of seeking to provide support for one of the foundational institutional forms of civil society, the market. Leviathan is a servant, not a master, in this process and it should serve a specific purpose – the facilitation of exchange transactions between market participants – not serve the interests of particular agents involved in those transactions, other than indirectly, by promoting a favourable environment in which they can go about their activities. Contrary to a commonly held supposition, this strategy does not entail a ‘minimalist state’. An effective Leviathan has a fairly full agenda.

We also know that central planning does not work at all well (from historical experience) and we know why that is so (from the works of political economists), although that knowledge appears to be less widely shared than it once was.

The existence of this knowledge base only serves to make the first task – understanding how the UK got to its current position – more puzzling. Why, in the relatively recent past and across a number of policy areas, did Britain take the side road signed central planning? On this, and in ending, let me put a two-part, speculative conjecture on the table as an invitation to further thinking. It is that the standard instruments of planning – quantitative targets, price controls, financial budget allocations, etc. – have value to decision makers as signalling mechanisms and that this value tends to be particularly high when the public has very low levels of trust in the relevant decision-makers.

There is an adverse positive feedback loop here: the measures that carry the clearest signals cause harm to the functioning of the economic system which, over time, contributes to further public dissatisfaction and lower trust. Observing this, a visiting alien familiar with revealed preference theory might infer that the underlying policy aim is to demonstrate that Marx was right. That may well be the aim of a few, but I think a better, shorthand diagnosis is that there

is simply a lack of vision. And by that I don't mean that we lack visions of <sunlit uplands>, which seem to be in plentiful supply, but rather that there is a failure to see and appreciate the factual realities and behaviours of complex systems.

Annex A: Ideographs

From Wikipedia: “An ideograph or virtue word is a word frequently used in political discourse that uses an abstract concept to develop support for political positions. Such words are usually terms that do not have a clear definition but are used to give the impression of a clear meaning. An ideograph in rhetoric often exists as a building block or simply one term or short phrase that summarizes the orientation or attitude of an ideology. Such examples notably include <liberty>, <freedom>, <democracy> and <rights>. Rhetorical critics use chevrons or angle brackets (<>) to mark off ideographs.”

In political rhetoric other examples include <equality>, <capitalism> and <austerity>.

To convert these idiographs into the stuff of substantive discourse they need to be given greater specificity. For example, as the American legal philosopher Gerald MacCullum has pointed out, to talk meaningfully about <freedom> it is necessary to specify ‘an agent, certain preventing conditions, and certain doings or becomings of the agent.’

When considering the EU’s <four freedoms>, including <free movement of workers/persons>, it is important to recognise that these are ideographs. As Mrs Thatcher put it in her speech at Lancaster House in 1988 launching the Single Market Campaign, EU officials had a tendency to speak in “slogans and lofty tones”, i.e. ideographs. She, in contrast, wanted to focus on concrete realities and actions.

The specifics required for conversion of the <four freedoms> into non-ideological language are, in fact, set out in the relevant provisions of the EU Treaties and the EEAA. It is the provisions that are relevant for those interested in concrete realities and actions. The specifics differ as between the two Treaties, reflecting two substantially different texts and two substantially different objectives. Thus, for example, rights to free movement of persons/workers can be:

- limited to some extent under provisions in the EU Treaties (Tony Blair is right on this point),
- limited to a significantly greater extent under provisions in the EEAA and, for purposes of comparison,
- limited to a greater extent still under the free movement provision of the Universal Declaration of Human Rights (UDHR Article 13).

It is, therefore, simply wrong to infer that when the words ‘free movement of persons’ appear in the EEA Agreement they carry the same entailments as they do when they appear in the EU Treaties. That the same words can have different meanings when used in different contexts is a phenomenon that is familiar to all of us who use the English Language. And it is why the interpretive principles of the Vienna Convention on the Law of Treaties explicitly state that interpretation should be guided by the ordinary meanings of terms used in a treaty in their context and in the light of the treaty’s object and purpose.

Annex B. Article 102 of the EEA Agreement

Article 102

1. In order to guarantee the legal security and the homogeneity of the EEA, the EEA Joint Committee shall take a decision concerning an amendment of an Annex to this Agreement as closely as possible to the adoption by the Community of the corresponding new Community legislation with a view to permitting a simultaneous application of the latter as well as of the amendments of the Annexes to the Agreement. To this end, the Community shall, whenever adopting a legislative act on an issue which is governed by this Agreement, as soon as possible inform the other Contracting Parties in the EEA Joint Committee.
2. The part of an Annex to this Agreement which would be directly affected by the new legislation is assessed in the EEA Joint Committee.
3. The Contracting Parties shall make all efforts to arrive at an agreement on matters relevant to this Agreement.

The EEA Joint Committee shall, in particular, make every effort to find a mutually acceptable solution where a serious problem arises in any area which, in the EFTA States, falls within the competence of the legislator.
4. If, notwithstanding the application of the preceding paragraph, an agreement on an amendment of an Annex to this Agreement cannot be reached, the EEA Joint Committee shall examine all further possibilities to maintain the good functioning of this Agreement and take any decision necessary to this effect, including the possibility to take notice of the equivalence of legislation. Such a decision shall be taken at the latest at the expiry of a period of six months from the date of referral to the EEA Joint Committee or, if that date is later, on the date of entry into force of the corresponding Community legislation.
5. If, at the end of the time limit set out in paragraph 4, the EEA Joint Committee has not taken a decision on an amendment of an Annex to this Agreement, the affected part thereof, as determined in accordance with paragraph 2, is regarded as provisionally suspended, subject to a decision to the contrary by the EEA Joint Committee. Such a suspension shall take effect six months after the end of the period referred to in paragraph 4, but in no event earlier than the date on which the corresponding EC act is implemented in the Community. The EEA Joint Committee shall pursue its efforts to agree on a mutually acceptable solution in order for the suspension to be terminated as soon as possible.
6. The practical consequences of the suspension referred to in paragraph 5 shall be discussed in the EEA Joint Committee. The rights and obligations which individuals and economic operators have already acquired under this Agreement shall remain. The Contracting Parties shall, as appropriate, decide on the adjustments necessary due to the suspension.