



## **Response to the Competition and Markets Authority Draft Guidance on the Office for the Internal Market**

### **Summary**

- The opportunity to comment on the Competition and Markets Authority (CMA) Draft Guidance on the Office for the Internal Market (OIM) is welcomed by the Royal Society of Edinburgh (RSE). The RSE has previously responded to the UK Government White Paper on the UK Internal Market. The response noted the current divergence and the limits that should be placed on the scope of the legislation. While recommending that subsidiarity and proportionality principles should be added to the internal market concept, exceptions to the principles of mutual recognition and non-discrimination to protect certain areas of public policy and institutions should be introduced. Moreover, an independent secretariat for intergovernmental arrangements should be established to improve the institutional framework for intergovernmental relations.
- Notwithstanding the UK Internal Market Act, there remains a lack of data around the internal market and how it operates. Therefore, the RSE believes that the CMA should conduct or commission research to understand the different levels of the market, with a specific focus on regional economies, and examine, in more detail, the nature of trade across the UK and within the different nations and regions. There remains a lack of clarity as to what the OIM objective to reduce divergence will mean for the devolved administrations. The OIM should respect the legislative and consumer choices within each nation of the UK.
- There is a lack of clarity around governance arrangements of the OIM and CMA more generally. The governance of the OIM will be important in addressing highly political issues; therefore, it is crucial that the OIM be independent and that its activities be transparent. Further clarity is needed on how the CMA/OIM will work with other regulatory bodies, judge what an internal market looks like, and ensure transparency around its decisions.
- Within the legal framework, it is unclear how the CMA envisions that the even-handedness obligation contained in s31(4) of the Internal Market Act will be reflected across all the OIM's functions to pursue its objectives. Additionally, we recommend that the scope for discretionary reports be widened and not limited to areas of the Act where the twin principles of market access and non-discrimination apply if an impact on the UK's internal market can be seen.
- The principles included within the analytical framework are narrow and limit the oversight of the OIM when conducting its analytical work in important ways. The RSE would recommend that the OIM should explore how widely it can use Section 33 of the Internal Market Act at its discretion.
- While the prioritisation principles are welcomed, these should reflect that policy divergence is a legitimate outcome as part of a union state; and this should be reflected in the even-handedness principle. The welfare of consumers and products should be

considered when judging the effectiveness of the market, and this should be reflected within the principles.

## Introduction

1. The Royal Society of Edinburgh (RSE), Scotland's National Academy, welcomes the opportunity to provide its views on the Competition and Market Authority (CMA) Draft Guidance for the new Office for the Internal Market (OIM). The guidance will be crucial to ensuring that the CMA, via the OIM, can discharge the statutory duties imposed upon it, to ensure that the UK's internal market operates effectively between the four UK nations and diverse regulatory authorities and that the internal (or UK domestic) market continues to bring benefits to consumers.
2. As Scotland's National Academy, the RSE has consistently provided advice and input on constitutional affairs since the UK voted to withdraw from the European Union. Notably, the RSE submitted a response to the UK Government consultation on the White Paper for the Internal Market<sup>1</sup> and has submitted evidence on Scotland and the Internal Market<sup>2</sup> and on UK-wide 'common frameworks'<sup>3</sup> to the Scottish Parliament.
3. In response to the UK Government consultation on the White Paper for the Internal Market, the RSE noted that in anticipation of the adoption of the UK Internal Market Act, more attention ought to be given to the limits that should be placed on the scope of any new legislative obligations and on the exceptions to them which would allow different regulatory authorities to justify measures on the grounds of public policy, public health, environmental protection and other exceptions. Such an approach could draw fruitfully upon what has been learnt over decades about the management and development of an internal market through the operation of EU law. Moreover, the principle of 'frictionless trade' must be balanced with other important social goals (for example, the protection of public health through policies seeking to tackle alcoholism or obesity, environmental protection, food standards), measures about which can legitimately vary in different parts of the UK, both according to the scale of the problem and to the legislative priorities set within the political process in each political unit of the UK. Certain types of choices have now been firmly established within certain parts of the UK, and it would require an overwhelming political reason now to disturb them. Furthermore, these choices have resulted in divergence, from which, to date, no evidence of resulting trade barriers has flowed.
4. The response recommended that if a legislative route for securing the identified objectives is adopted, then the subsidiarity and proportionality principles should be added to the concept of the internal market. The UK Government should introduce legislative exceptions to the principles of mutual recognition and non-discrimination to protect the public policy, public health and other core values of each of the political units in the UK. Furthermore, we recommended that a much stronger institutional framework for intergovernmental relations and the development and enhancement of the UK internal market should be established by creating an Independent Secretariat

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<sup>1</sup> Royal Society of Edinburgh. (2020). 'UK Internal and Market'. URL: <https://www.rse.org.uk/advice-papers/uk-internal-market/>

<sup>2</sup> Royal Society of Edinburgh. (2020). 'Scotland and the UK Internal Market'. URL: <https://www.rse.org.uk/advice-papers/scotland-and-the-uk-internal-market/>

<sup>3</sup> Royal Society of Edinburgh. (2018). 'Common UK Frameworks'. URL: <https://www.rse.org.uk/advice-papers/common-uk-frameworks/>

for the intergovernmental arrangements. It is a matter of regret that these recommendations were not reflected in the final text of the Act.

## General Comments

5. Notwithstanding the enactment of the UK Internal Market Act, there remains a lack of clarity and an insufficient understanding of the nature of the UK's internal market. As the RSE noted in our response to the White Paper, 'UK internal market' is a contested term with no single agreed definition. This contrasts sharply with the EU single market, which has been based on the clearly defined 'four freedoms'. Arguably, the term, UK internal market, is still contested and has no single agreed definition to date. In contrast to the EU single market, which was a legislative creation (driven substantially by the UK), the UK domestic market has developed organically over a long period, largely without central regulatory intervention. Of course, there has, especially in recent years, been significant regulatory intervention in relation to the operation of various markets within the UK internal market.
6. Given that the UK's internal market was integrated within the larger EU single market for more than 20 years, there is surprisingly little data and knowledge about the UK's domestic internal market. Therefore, it will be important for the CMA to conduct research into the UK's internal market to understand its main features before determining precisely how the OIM should operate and what it should focus on. Specifically, the CMA should conduct or commission research to understand the different levels of the market, with a specific focus on regional economies, and examine, in more detail, the nature of trade across the UK and within the different nations and regions. This will require co-operation and contribution from other regulators in the UK. The RSE would assume that the economies of England, Scotland and Wales are likely to be highly integrated as they are part of mainland Britain. In light of the NI protocol to the Brexit agreement, Northern Ireland's economy may become somewhat less integrated than those in the mainland. Previous research from the London School of Economics has found that the trade between Scotland and the rest of the UK is six times higher than predicted by a standard gravity trade model.<sup>4</sup>
7. The lack of data on the UK's internal market may lead to assumptions that divergence in policy may lead to barriers in the market, which in turn need to be addressed through regulatory measures. However, within the EU single market, there is no standard presumption that policy divergence and autonomy within the EU leads to barriers in the marketplace and that the lack of any EU regulation reduces economic efficiency. On the contrary, within the framing of the EU single market, it is clear that there are trade-offs to be made. Meanwhile, the UK domestic market has operated very effectively despite regulatory divergence across the nations, even before political and legislative devolution.
8. In sum, there remains a lack of clarity as to what the OIM objective to reduce divergence will mean for the devolved administrations. On its own, it is a potentially flawed objective. As the UK is a union state with different levels of government, different regulations and policy divergence should not always be viewed as unfavourable, as they are likely to be related to a legitimate policy objective adopted by a devolved administration and often approved as a political choice via the electoral

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<sup>4</sup>Huang, H; Sampson; T; Schneider P. (2021). 'Disunited Kingdom? Brexit, trade and Scottish independence.' London School of Economics

process. Notably, there is already significant policy and regulatory divergence, some of which is guaranteed by treaties between the UK nations, such as the Scottish legal system and higher and further education. This should not be threatened by the internal market or work of the OIM. Additionally, divergence may flow from consumer choices, which are also voter choices. The OIM should be mindful that it cannot, and ought not, limit the divergence that results from consumer and legislative choices.

### *Governance*

9. The CMA's reporting, advisory, and monitoring functions mean that it will substantially influence the trajectory of regulatory policy-making in the UK. However, the guidance does not address some key aspects of the governance of the OIM, which will influence its credibility. Due to the political context of the UK, the development of the UK Internal Market Act has been overtly politicised. The governance of the OIM will be important in addressing highly political issues; therefore, it is crucial that the OIM be independent and that its activities be transparent. However, the guidance fails to mention how the CMA will ensure that the OIM will be independent and not be politicised.
10. The guidance provides no information on how the new OIM will consult and co-operate with other bodies responsible for ensuring that the UK internal market works effectively. It would be helpful if the guidance were to clarify if the OIM will work with these bodies or via other external methods. There is only one mention of when the OIM will interact with other bodies. Paragraph 5.7 states that the OIM will refuse a request from a national authority when another body is better placed to provide an independent report. However, there is no additional information on how the OIM will decide this or how such a decision might be challenged.
11. Moreover, the guidance does not include how the OIM will judge what an effective internal market will look like. Presumably, this will require a baseline against which judgements will be made, and data will be needed from other regulators and consumers. It would be helpful if the guidance were to clarify how the OIM will identify what an effective internal market looks like, how it will collect the data necessary to analyse its effectiveness and its relationship with regulatory bodies.
12. It is our view that the notion of effectiveness of a market needs to be far better articulated, and recognition is given to the fact that markets may only be effective if buttressed by certain regulatory behaviour and 'corrective' taxes and subsidies. Markets are quite effective at providing incentives for producing a vast array of goods and services, distributing these to final consumers and providing incentives to innovate and produce better goods and services. This is in contrast to more centralised command and control mechanisms. However, left to themselves, markets can be less effective at providing goods and services at prices that are affordable by the vast majority of consumers. To counter this lack of effectiveness, we have policies such as competition policy as well as taxes and subsidies. Equally left to themselves, markets are not particularly effective at dealing with environmental pollution and major challenges such as climate change. It is for this reason that we need deft regulatory and tax policies, which are designed to handle these issues. The big challenges for the OIM are:
  - determining when certain policies improve the effectiveness of the market in meeting these challenges and when they hamper it through poor design.

- how trade-offs between certain objectives can be addressed – e.g., tackling environmental issues can drive up prices; some types of desirable activity can be improved by companies co-operating rather than competing.
13. Transparency in the OIM decision-making process will be essential to help build confidence and understanding of the devolved authorities in the OIM. Governments, businesses and consumers must understand why the OIM has come to its conclusions; this will ensure its credibility in their reporting and advice.
  14. In sum, the guidance is narrowly focused on the market and economic-based approach of the OIM. It does not address the highly political nature of its role and how it will cover other areas of public policy, as explained in paragraph 12. If the OIM is going to complete its tasks, it will be required to comment on the interaction between different areas of public policy and how this results in divergence or convergence. This should be clarified within the guidance. The nature and implications of such a comment, in the form of a report or advice, is likely to be politically contested. As established by the Act, the framework does not create options for formal 'recourse'. This will remain a source of tension within the UK's devolution settlement and more broadly across those authorities responsible for market regulation.

## **Legal Framework**

15. This section of the draft guidance documents the legal framework within which the OIM must interpret its role and functions to deliver its objectives around market access and non-discrimination principles. The primary objective of the OIM will be to support the effective operation of the internal market: in pursuing this objective, however, per s31(4) of the Act, the CMA must also "have regard to the need to act even-handedly as respects the relevant national authorities". In the consultation, this obligation is referred to only in respect of prioritisation principles (see below).
16. However, the relevant provision of the Act applies to *all* the CMA's functions under Part 4 of the Act, i.e., including in pursuit of the objective of supporting the 'effective operation of the internal market... in the interests of all parts of the United Kingdom.' Accordingly, it is not obvious why the consultation appears to suggest that the even-handedness obligation should be reflected principally in the OIM's prioritisation principles as opposed to, e.g., even-handedness more broadly, including as regards respecting the pursuit of legitimate – and potentially differing – policy objectives by the UK's various national authorities. It would therefore be helpful to understand how the CMA envisions that the even-handedness obligation contained in s31(4) will be reflected across all the OIM's functions in pursuit of its objectives.
17. The guidance states that the OIM will produce reports on request and report annually and every five years on its work. The OIM will also produce its own reports at its discretion; however, the guidance states this will only be on areas within the UK Internal Market Act. This limits the scope of the work of the OIM and excludes areas of public policy that will impact regulation and trade or areas of devolved competency which were not included in the Act but which may be highly relevant to the effective operation of the UK's internal market. The RSE would recommend that the scope for discretionary reports be widened and not limited to areas of the Act where the twin principles of market access and non-discrimination apply if an impact on the UK's internal market can be seen.

18. The OIM will produce reports at its discretion that explore and promote the effectiveness of the UK's internal market. While this is welcome, there is a need to define 'effectiveness' in the context of the current constitutional framework. Further information which defines what an effective internal market is and looks like within a multi-government system will be required.
19. In paragraph 2.20, the guidance documents the discretion of the OIM when providing reports based on a request from a national authority; this states that the 'OIM may consider, among other things, the potential economic effects of proposed regulatory provision on the effectiveness of the internal market in the UK'. This reflects the wording of s34(4) of the Act. The wording of paragraph 2.21, immediately following, however, notes that 'The OIM will only consider economic effects and only those effects of the regulation in so far as they impact the effectiveness of the internal market.'
20. This could be understood as specifying *which* economic effects the OIM will consider when it considers such effects per 2.20. This is not altogether clear, however: 2.20 could alternatively be read as suggesting that the OIM will *only* consider economic effects and when it does so, '*only* those effects... in so far...'.
21. As s34(4) of the Act grants discretion to the OIM to consider effects on the operation of the internal market that go beyond economic effects, our understanding is that the latter interpretation cannot be correct as it would be inconsistent with the Act. Clarity on this point would, however, be helpful. Additionally, it would be helpful to understand what other non-economic considerations the OIM may consider in performing its functions under s34 of the Act and how this will be done.

### **Analytical Framework**

22. The analytical framework section of the guidance presents the principles governing what the OIM will deem to be the 'effective operation' of the internal market. These principles are narrow and limit the oversight of the OIM when conducting its analytical work in important ways. As mentioned above, there are several areas of public policy which have an unavoidable relationship with trade and regulation that will be left out of account if these principles are not expanded and structural reasons why markets may not be left alone to resolved public policy questions.
23. Therefore, concepts like the 'effective operation of the internal market' need to be much more clearly defined, and a benchmark of what a successful internal market looks like should be identified. This will require cooperation with national authorities, other regulators and bodies, and consumers.
24. The guidance states that it recognises that there is a balance to be struck between frictionless trade and devolved policy autonomy. However, the RSE would highlight that there has always been significant policy autonomy within the EU single market for EU countries, which did not lead to greater barriers or friction. There will likely always be differences in a multi-level governance system, but these will not always result in trade barriers. Thus, it is important that work to identify trade barriers proceeds in close cooperation with work to identify appropriate common frameworks.

25. There is a lack of clarity on which institutions (whether the UK Government or other bodies) have the responsibility to report on policy objectives and decisions by the OIM. The lack of clarity could undermine the effectiveness of the devolution settlement as it could limit the responsibilities of the devolved governments in achieving their policy objectives. Furthermore, as the UK has a dual responsibility to act as both the UK Government and the voice of England in an asymmetrical devolution settlement, there could be a lack of clarity on the relationship between the UK Government and the OIM.
26. Crucial to the credibility of the OIM may be how the CMA interprets its broad discretion in s33 of the Internal Market Act to review ‘any matter it considers relevant to assessing or promoting the effective operation of...the internal market in the United Kingdom’. This appears to give the OIM a wider remit than the guidance suggests, and the RSE would argue that the guidance should explore in more detail how the OIM/CMA intends to use the s33 discretion.
27. As noted above, the UK’s internal market is not simply a matter of trade and economic regulation. The devolution settlements and choices made in many (non-devolved) areas of public policy affect the nature of the market as a whole. However, the guidance does not cover the impact of positions taken regarding CMA/OIM analytical work on the devolved administrations. The RSE would thus reiterate its previously stated position that the impact of political choices within the internal market on the devolved administrations must be fully considered.<sup>5</sup> Although the OIM is not a regulatory body as such, it can nonetheless influence the development of the devolution settlement. Ultimately, this may require a widening of the scope of the OIM’s work or acknowledging that some other body, such as an independent secretariat, will need to be established, which will analyse the impact of policies and the balance of policy decisions.

### **Prioritisation Principles**

28. The prioritisation principles for the OIM are to be welcomed and should help to ensure that it targets its resources on issues and areas of the most relevance to businesses, consumers, and public authorities. However, we would note that these principles would be better placed at the start of the guidance rather than in chapter four.
29. The principle of even-handedness needs to be drawn out further, and consideration given to how this obligation can be integrated across all the OIM’s functions in pursuit of its objectives (see paras. 14-15 above).
30. Furthermore, as mentioned above, policy divergence can result from a legitimate policy objective of devolved administrations due to the expression of citizens’ consumer preferences at the ballot box. For example, in Scotland, the principle of minimum unit prices for alcohol resulted from voter choice and is now entrenched in law.<sup>6</sup> This type of policy divergence can be justified and should not be viewed as negative or simply a barrier to trade. Within the even-handedness principle, it should be reflected that policy divergence is legitimate.

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<sup>5</sup> Royal Society of Edinburgh. (2020). ‘UK Internal and Market’. URL: <https://www.rse.org.uk/advice-papers/uk-internal-market/>

<sup>6</sup> Alcohol (Minimum Pricing) Scotland Act 2012.

31. As noted above, from these guidance and principles, the objective of the OIM is to reduce trade barriers which will lead to the effective operation of the internal market. This objective is too narrow and misses one of the main aims of the CMA: to improve growth and performance and provide a well-functioning market that will improve consumer welfare and choice. Additionally, it assumes that even existing policy divergence is potentially illegitimate in market terms. The legislation specifically provides otherwise, and, as noted above, the scope for devolved policy divergence cannot simply be rendered illegitimate because of potential market impacts. The RSE believes that the scope should be widened to ensure that the welfare of consumers and products (e.g., animal welfare, crop production, etc) are considered when judging if the market is effective or not, and this should be reflected within the principles.

### **Procedural Arrangements**

32. The OIM will need to gather evidence for its reports and advice. Given that the guidance, as it currently stands, is narrowly focused on economic effects, this will limit what types of evidence the OIM can and will collect. The evidence gathered will be subjected to the questions and role of the OIM as defined in the guidance.

33. Paragraphs 5.3 to 5.6 describe the OIM procedures when handling requests for advice or reports from national authorities. The guidance describes what should be included within the requests from national authorities on regulations for the OIM to accept the request and produce a report. Requests will require the national authorities to document how the regulation falls under their devolved competencies. However, it is unclear if the OIM will have the expertise or ability to judge if the regulation does not fall under the devolved competence.

### **Concluding Remarks**

34. Overall, the consultation on the Draft Guidance for the Office for the Internal Market is welcomed by the RSE. However, we believe that the CMA should consider several points before finalising the guidance:

- The CMA should conduct an initial investigation to explore the nature of the UK's internal market by researching and analysing existing research. This will assist it in understanding what the market looks like to ensure the OIM has a well-defined remit and is adequately resourced from an informational perspective.
- The guidance should note that policy divergence is a likely outcome within a multi-level governance system and that this should not automatically be viewed unfavourably. There is little evidence that divergence and lack of central regulation lead to trade barriers.
- The guidance should recognise that other public policy areas will impact regulation and trade and present how the CMA/OIM will interact with these via the national authorities. Although the OIM is an advisory and not a regulatory body, it must cover devolved aspects and market aspects. This may require the OIM to broaden its scope or, if not, require another body, such as an Independent Secretariat, to be established. This is a change that the RSE has consistently recommended would be beneficial.