HOUSE OF LORDS

EUROPEAN UNION COMMITTEE

EXTERNAL AFFAIRS SUB-COMMITTEE AND INTERNAL MARKET SUB-COMMITTEE

Brexit: the options for trade

Evidence Volume

Contents

Dr Pinar Artiran, Assistant Professor, Istanbul Bilgi University, and World Trade Organization Chair Holder – Written evidence (ETG0012)

1. We were informed by one of our witnesses that Turkey is obliged to sign free trade agreements with the countries that the EU signs an agreement with. Could you please clarify the legal basis under which Turkey becomes obliged to sign such free trade agreements; is this part of the EU-Turkey Customs Union agreement? What are the implications?

In accordance with GATT Article XXIV, Turkey and the EU should apply the same duties to the third countries as a principle of the Customs Union under WTO system. Moreover, Turkey, in accordance with Article 16[1] of the Decision No 1/95[2], is expected to align itself progressively with the preferential customs regime of the EU. However, this does not function properly for several reasons. Similarly Article 54 requires Turkey to align its commercial policy with the EU's Common Commercial Policy which includes, inter alia, FTAs of the EU. Moreover, on the basis of Article 56 of the Decision 1/95, Turkey and the EU are jointly responsible for the proper functioning of the Customs Union.

The World Bank's 2014 Report puts forward that "A key asymmetry in the CU's design in that the EU is permitted to negotiate FTAs with third countries, but Turkey is not permitted a seat at the negotiations because it is not an EU member. This situation is not particularly problematic if both parties are able to obtain the same agreement from trading partners. In practice, however, it has proved to be difficult for Turkey because parallel negotiations with 3rd countries have not always been concluded, e.g. EU-Mexico agreement. This asymmetry is potentially very costly for both parties as it risks the introduction of origin controls, the absence of which have been a key source of the benefits from the CU."[3]

Turkey has indeed been in the past and currently is involved in several FTA negotiations in an effort to conclude parallel agreements to the ones of the EU in order to comply with its common commercial policy. The launch of FTA negotiations with a third country typically occurs following the EU Commission's initiation of its own negotiations with that country. As it stands, Turkey's alignment with the EU's FTAs can be deemed to be partly successful due to a mixture of countries with which the conclusion of a parallel FTA was possible whereas the possibility did not occur in other instances where the approached country did not reciprocate the interest in entering into a parallel FTA with Turkey. Therefore, this undesirable asymmetrical occurrence in the common commercial policy created complications for both parties, but in particular for Turkey. Asymmetry between the parties result in the time gap in the entry into

[1] Article 16, paragraph 1 reads as follows: "With a view to harmonizing its commercial policy with

[2] Decision No 1/95 OF THE EC-Turkey Association Council of 22 December 1995 on implementing the final phase of the Customs Union (96/142/EC)

[3] World Bank Report on the Evaluation of the EU-Turkey Customs Union, 2014, para.6. See the implications for Turkey of the asymmetrical relationship in the FTA process: World Bank Report, 2014, paras.48-55, including Box 5 on page 27.

force of some FTAs, a potential gap in economic terms as well as, what Turkish trade officials call "a moving target" by creating disadvantages for Turkish exports in third country markets, unfair competition conditions within the CU due to the disadvantage in the access to low-cost raw materials. Moreover, the value chains established within the CU cannot benefit from the FTAs. In relation to trade deflection, the implications of the EU-Mexico FTA for Turkey and the way in which Turkey tried to overcome the negative effects is pretty illustrative.

Our witness also informed us that there are exception clauses in the case of the EU having a free trade agreement with a country and Turkey not having one. This is a right that the Turks have but do not want to exercise. Could you elaborate on the significance of this exception clause and when it might apply?

I am not sure whether I understand what your witness meant by the "exception clause". In any event, there currently exists a clause named "Turkey clause" that is expressly indicated in some of the EU Commission documents, among others in former DG Trade Catherine Ashton's Action Plan of 2008:

"Turkey clause, enhanced bilateral dialogue, taking into account Turkey's sensitivities, impact assessments, feasibility studies etc."

Similarly, the European Parliament Resolution of 21 September 2010 includes the following:

"Acknowledging the difficulties faced by Turkey and calling the Commission and the Council to ensure that Turkey is included in the impact assessment studies of prospective FTAs and to further strengthen the transmission of information"
Again, as a way to acknowledge the problem regarding asymmetrical relationship between the parties as far as the negotiation and conclusion of the FTAs are concerned, the Strategy Papers from 2011 and 2012 highlight the following:

Strategy Paper-2011: "Seeking closer coordination in the negotiations on free trade agreements"

Strategy Paper-2012: "The Commission is examining ways to address Turkey's concerns under the CU, including on the FTAs concluded by the EU with third countries"

The way in which this clause has been inserted into the EU's trade agreements have been formulated as the following:

EU-Algeria FTA (2005): In the Joint Declaration annexed to the Agreement, EU invites Algeria to negotiate an FTA with Turkey. Algeria takes notes and commits to consider the matter when the time comes.

EU-Albania FTA (2006): In the Agreement, Albania undertakes to conclude FTA with Turkey within a pre-defined period of time.

Ashton's Proposal (2008): EU invites the FTA partner to start negotiations with Turkey as soon as possible.

EU-Central America FTA (2012): In the Joint Declaration, EU invites Central America to start negotiations with the States with which EU has established a Customs Union. Central America responds that they shall make best efforts.[4]

Basically, this Clause signals the intention for EU FTA partners to start negotiating an FTA with Turkey on the basis of the findings of a joint feasibility study. It was first employed while the EU was negotiating its own FTA with Algeria but the clause proved to be inefficient and not suitable for enforcement since it does not enjoy the capacity to force third countries to conclude an agreement with Turkey.

Given that third countries are not obliged to sign a deal with Turkey, what demands is Turkey faced with in the negotiations with third states? Does the EU take account of the fact that Turkey is in a weak negotiating position with the third parties given that it is under an obligation to align its FTAs with those of the EU and exert pressure on the third states to sign a deal with Turkey?

In Turkey, main arguments on the CU in earlier periods were largely focusing on preference erosion in the EU market vis-a-vis third countries which cannot be compensated through Turkey's exports into these markets. The nature of EU FTAs does not impose a legal obligation for the FTA-partner to provide reciprocal market access for Turkey's exports, simply because Turkey is a party to CU with the EU. Some of the EU's partners have refrained from negotiating agreement with Turkey. Its ramification for Turkey is larger and its commercial implications for the Turkish economy are more significant. Algeria, Mexico, and South Africa are some cases with which Turkey had trade imbalances. In the case of the US, the negotiation of TTIP has created concerns among Turkish policy-makers with respect to its potential impact on bilateral trade balance between the US and Turkey.

Moreover, Turkey in many instances cannot start parallel negotiations with the EU, leading to time differences up to several years. Under these circumstances, Turkey's obligation to align itself with the CCT becomes a unilateral commitment, in practice.

The World Bank's 2014 Report also refers to the FTA asymmetry problem arguing that the implications for Turkey will grow because "there will be more and deeper agreements". Several options are cited by the Report as to reduce the asymmetrical effect, such as the EU and Turkey negotiating jointly; the EU is negotiating on behalf of Turkey; both parties entering parallel track negotiations under a "reinforced Turkey clause". However, they all suffer from considerable institutional and political shortcomings.

As mentioned above, the EU has taken some initiatives to insert a clause as to encourage its trading partners to conclude parallel deals with Turkey, however at the end of the day, the EU cannot force a sovereign state to conclude an agreement with another country just because they already signed one with it no

[4] See also World Bank Report, 2014, para. 55 as well as Box 6 on p. 30 on "Turkey Clause" and the example of a revised Turkey Clause.

matter how strong the Union may be as a trade player. Moreover and as also pointed out by the World Bank in its 2014 Report, since helping out Turkey with the conclusion of parallel FTAs with third countries "is not part of the EU's negotiating mandate, the "Turkey Clause" sometimes dropped from the negotiations."[5] Consequently, Turkey puts forward the idea of a introducing a "legally binding instrument in its FTAs, such as a Reinforced Turkey Clause that would require the EU to invite its FTA partner to negotiate and conclude parallel FTA with Turkey as nearly as possible the same time with the EU, while it provides, in the meantime, the Turkish products in free circulation benefit from EU's FTA reciprocally. This solution is considered to be applied until Turkey and the concerned third country conclude an FTA as to prevent the application of different duties by the CU Partners that would constitute a breach of the CU partners' WTO obligations under Art. XXIV of the GATT. Moreover, the World Bank's 2014 Report suggests that the EU Commission could be empowered with a clear mandate to negotiate a strengthened Turkey Clause, however given the state of play as far as the EU itself and its trade policy is concerned, it is doubtful whether such empowerment would indeed take place.

In actual practice, how aligned are Turkey's preferential trade deals with those of the EU? Has Turkey signed FTAs with third countries that have no FTA with the EU? Or not signed deals with countries that the EU does have deals with? How can the differences be explained? If there are significant differences, what are the implications for the trade of goods with the EU, are rules of origin a problem in that respect?

Turkey is obliged to undertake and implement a great deal of the EU acquis without really taking part in the decision shaping let alone decision-making. Asymmetric structure has substantial consequences on FTAs to be negotiated and concluded by Turkey since Turkey's FTA policy is indexed to that of the EU's. While Turkey is obliged to follow EU's FTA perspective, EU decides the FTA partner, the scope and timing of the negotiations based on its own priorities without necessarily taking into account its Customs Union with Turkey. Turkey becomes a vulnerable market for all countries which signs FTA with the EU since goods originating in those countries enjoy market access advantages in Turkey via EU-Turkey CU; however, Turkish goods do not have the same opportunity since the FTA puts rules of origin into place that will act as a trade barrier for goods originated in Turkey. Moreover, the countries that already made FTAs with the EU are reluctant to establish FTA with Turkey, consequently Turkey loses its comparative advantage in more competitive EU markets. The latter issue is of particular concern for Turkey (at least with regard to important trading partners, such as Algeria, Mexico or South Africa), where the absence of an agreement between Turkey and the third country puts Turkey at an asymmetrically disadvantageous position. On a different note, Turkey signed an FTA with Malaysia that did not yet have an FTA with the EU. For instance the EU has an FTA with Algeria that Turkey is very keen on concluding its own FTA with, however Algeria appears to be reluctant, thus creating an undesired and disadvantageous outcome for Turkey. If concluded, the TTIP, will be a major game-changer and trade diversion, trade deflection element for Turkey, given the strategic importance and major trade capacity of the US. In a scenario where

[5] Ibid, para. 55.

TTIP is concluded, Turkey becomes an attractive market for the American goods but Turkish goods lose their comparative advantage in the EU markets as a result of the structural difference between Customs Union and FTA. US goods who obtain free circulation rights in the EU will have free access to Turkey due to EU-Turkey Customs Union; whereas, Turkish goods will not enjoy the same access facility when exported to the US market via the EU due to the rules of origin implied by FTA.

Turkey has been in the past and currently is involved in several FTA negotiations in an effort to conclude parallel agreements to the ones of the EU in order to comply with its common commercial policy. The launch of FTA negotiations with a third country typically occurs following the EU Commission's initiation of its own negotiations with that country. As it stands, Turkey's alignment with the EU's FTAs can be deemed to be partly successful due to a mixture of countries with which the conclusion of a parallel FTA was possible whereas the possibility did not occur in other instances where the approached country did not reciprocate the interest in entering into a parallel FTA with Turkey. Therefore, this undesirable asymmetrical occurrence in the common commercial policy created complications for both parties.

A substantive comparison of Turkey's FTAs with the ones of the EU indicates that they are not as comprehensive to cover trade in services, investment, public procurement and several other issues which are commonly covered in the EU's more recent trade agreements. For example, anti-fraud measures (as developed, for example in the EU's agreements with Chile and Vietnam) so far have not been incorporated into any of Turkey's FTAs, including the recent ones with Malaysia and South Korea. However, Turkey recently started to incorporate these issues in its next generation of FTAs. Similar to the trade deal with South Korea, Turkey is pursuing FTA negotiations with Ukraine, Peru, Japan, and Mexico (but some of these are at the exploratory stage yet) which also foresee, as they stand, services and investment chapters. The FTA that has been signed with Singapore on 14 November 2015 features the same characteristics. This Agreement covers, inter alia, Chapters on Public Procurement, Services and Investment.

2. Would it be correct to say that Turkey is obliged to apply the same bound and applied tariffs as the EU in its dealing with third countries (unless there is an FTA) for goods covered by the Turkey-EU Customs Union? Which goods are covered?

Within the framework of its commitments under the CU and upon the date of entry into force of the Decision 1/95, Turkey was obliged to, in relation to countries which are not members of the Community, align itself on the Common Customs Tariff. Accordingly, Turkey also had to adjust its customs tariff whenever necessary to take account of changes in the EU's Common Customs Tariff. (Articles 13-14 of the Decision 1/95).[6] The EU has provided duty-free access in a large number of products to an increasing number of trading partners

[6] By way of derogation from Article 13 and in accordance with Article 19 of the Additional Protocol (dated 1970), Turkey might have retained until 1 January 2001 customs duties higher than the Common Customs Tariff in respect of third countries for products agreed by the Association Council

under its FTAs. Turkey has negotiated preferential trade agreements (generally in the form of FTAs) with many of the EU's trading partners, granting the same preferential access to its market of goods imported from these countries. Indeed, In addition to Articles 13-14, **Article 16** of the Decision No 1/95 stipulated that Turkey ought to take necessary measures and negotiate agreements with the countries concerned to align itself progressively with the preferential customs regime of the Community. Consequently, Turkey is expected to grant tariff-free access to goods from a third country with which the EU has negotiated an FTA, without necessarily having a vote or a say in its negotiations. However, this market access freedom does not apply to Turkish products en route to the market of that third country. The possibility, if any, depends on whether Turkey is able to negotiate a parallel FTA with that country. (See Article 16.1 of the Decision 1/95).[7]

EU Regulation No 978/2012/EU forms the basis of Turkey's GSP scheme through which it should offer unilateral preferences in parallel to those of the EU. The Commission's 2015 Progress Report for Turkey notes that the country has taken positive steps in aligning its RoO in the context of the GSP to that of the EU, although rules on surveillance and management of tariff quotas have not yet been fully aligned. The EU's initiatives related to the GSP+ and Everything But Arms (EBA) also cover agricultural products, which are not covered under the CU. In this context, Turkey has been offering unilateral preferences since 2001, limited to industrial products and industrial components of processed agricultural products only. However, Turkey applies additional duties, including on imports eligible under the GSP, which amounts to a non-alignment of its preferential tariff regime with the EU.

As opposed to the CU where trade of industrial products between Turkey and the EU takes place on the basis of the principle of free circulation of goods, trade between Turkey and its FTA partners is set up on the basis of RoOs. In other words, the FTA parties are required to fulfill the FTA agreement's norms that apply to the RoOs in order to benefit from the tariff concessions as foreseen in the FTA. Customs duties and charges having equivalent effect are abolished between the EU and Turkey in accordance with Article 4 of Decision No 1/95 (and also mindful of the GATT Article XXIV). For the third country products that will be deemed to be in free circulation in accordance with Article 3 of Decision No 1/95, both Turkey and EU will make an assessment of whether the import formalities have been completed and the customs duties or charges having equivalent effect, where applicable, have been levied in the EU or in Turkey, and also whether a total or partial reimbursement of such duties or charges has taken

[7] Art. 16 para. 3 of the Decision provided for the possibility for Turkey within five years as from the date of entry into force of the Decision whereby "Where, ..., Turkey maintains a tariff policy different from that of the Community, goods imported from third countries into the Community and released for free circulation with preferential treatment by reason of their country of origin or of exportation shall be subject to the payment of a compensatory levy if they are imported into Turkey, in the following circumstances:
- they have been imported from countries to which the same preferential tariff treatment is not granted by Turkey, and
- they can be identified as imported from these countries, and
- the duty to be paid in Turkey is at least five percentage points higher than that applicable in the Community, and
- an important distortion of traffic related to these goods has been observed."

place.

The CU covers "products other than agricultural products". The EU-Turkey Association Council Decision No 1/95 has established the CU, covering industrial and processed agricultural goods. Therefore, agricultural and fishery products are excluded and only industrial goods may benefit from the CU. Agricultural and fishery products are covered by Decision of the EU-Turkey Association Council No 1/98, and coal and steel products by the CSA of 1996. For ECSC products, Turkey signed a free trade agreement (FTA) with the EU in July 1996, and, as a result, ECSC products have received duty-free treatment between the parties since 1999. A specific treatment is provided in Decision No 1/95 for processed agricultural products which are only partially liberalised. When adopting the CCT of the EU, the 'sensitive products' were initially excluded from the alignment. With the alignment of Turkish duty rates on 'sensitive products' with the CCT in 2001, Turkey has completed the alignment with the CCT. In addition, negotiations on Turkey's accession to the EU began in 2005, also covering trade between the parties.

3. Could you please explain to us in which circumstances Turkey would be able to use the trade deflection clause in its Customs Union agreement with the EU to put extra duties on goods coming from a third country into Turkey via the EU? How is that clause used in reality? Would it be correct to state that in reality a third country concluding an FTA with the EU automatically gets access to the Turkish market as well?

Turkey has to apply the EU's CCT for imports coming from third countries in accordance with Article 13 of the Decision No 1/95. Accordingly, a third country that has an FTA with the EU but not with Turkey, is entitled to export an industrial product to the EU benefitting from the concessions accruing it through the FTA and making its product subject to free circulation within the CU as long as it complies with the necessary import formalities. Consequently, a product that is in free circulation will have access to the Turkish market at zero tariff rate by way of escaping from the CCT that is typically applied by Turkey for third country imports. Notwithstanding this, there has recently been an exceptional application where an additional fiscal duty has been and is currently being imposed on motor vehicles that originate in Mexico and that are exported to the Turkish market via the EU. It appears that this exceptional application is not being used frequently nor systematically and is based on Article 58.2[8] of

[8] Article 58 of the Decision 1/95 stipulates: "1. If, at the end of the consultations undertaken under the procedure provided for in Article 56 (2) or Article 57 (4), a mutually acceptable solution cannot be found by the Customs Union Joint Committee and if either Party considers that discrepancies in the legislation in question may affect the free movement of goods, deflect trade or create economic problems on its territory, it may refer the matter to the Customs Union Joint Committee which, if necessary, shall recommend appropriate ways of avoiding any injury which may result.
The same procedure will be followed if differences in the implementation of legislations in an area of direct relevance to the functioning of the Customs Union, cause or threaten to cause impairment of the free movement of goods, deflections of trade or economic problems.
2. If discrepancies between Community and Turkish legislation or differences in their implementation in an area of direct relevance to the functioning of the Customs Union, cause of threaten to cause impairment of the free movement of goods or deflections of trade and the affected Party considers that immediate action is required, it may itself take the necessary protection measures and notify the Customs Union Joint Committee thereof; the latter may decide

Decision No 1/95 that foresees the possibility for the parties to take measures to remedy the injury where discrepancies in the implementation of the commercial policy cause to impairment of free circulation of goods or deflection of trade. However, having used the possibility earlier on at least once, Turkish authorities might be interested in extending such measures to other products/countries in similar cases where trade diversion can possibly occur. Whether the usage of Article 58.2 on such occasions complies with the parties' treaty obligations is subject to disagreement among them. However, since both the institutional and the dispute settlement structure foreseen by the CU is far from being perfectly functional and operational, such disagreements do not appear to be solved easily.

Notably, Article 60 of the Additional Protocol[9] lays down a system that provides for the usage of "emergency safeguards".

4. To what extent is Turkey able to adopt a trade policy independent of the EU in areas not covered by the Customs Union agreement?

Normally, Turkey is able to adopt a trade policy that is independent of the EU in areas not covered by the Decision 1/95. However, one should be mindful of the special relationship between the EU and Turkey in the sense that Turkey is also a candidate country for the full membership to the EU, therefore the obligations that stem from the Customs Union and membership may require Turkey to undertake more commitments towards the EU compared to what a typical, regular CU relationship would require. (TURKISH OFFICIALS WOULD BE BETTER PLACED TO ANSWER THIS QUESTION)

5. How burdensome are rules of origin in relation to the EU-Turkey Customs Union?

In accordance with the CU, Turkey applies the same RoOs as the EU to third countries. As far as the non-preferential RoOs are concerned, the Turkish Laws and regulations lay down measures such as surveillance, quotas, safeguards, etc. in a way to comply with the EU practices. As for the preferential agreements,

whether to amend or abolish these measures. Priority should be given to measures which least disturb the functioning of the Customs Union."

[9] Article 60 reads as follows:

"1. If serious disturbances occur in a sector of the Turkish economy or prejudice its external financial stability, or if difficulties arise which adversely affect the economic situation in a region of Turkey, Turkey may rake the necessary protective measures.

The Council of Association shall be notified immediately of those measures and of the rules for their application.

2. If serious disturbances occur in a sector of the economy of the Community or of one of more Member States, or prejudice the external financial stability of one or more Member States, or if difficulties arise which adversely affect the economic situation in a region of the Community, the Community may take, or authorize the Member State or States concerned to take, the necessary protective measures.

The Council of Association shall be notified immediately of such measures and of the rules for their application.

3. In the choice of measures to be taken in pursuance of paragraphs 1 and 2, preference shall be given to those which will least disturb the functioning of the Association. These measures shall not exceed what is strictly necessary to remedy the difficulties that have arisen.

4. Consultations may take place in the Council of Association on the measures taken in pursuance of paragraphs 1 and 2."

Turkey applies preferential RoOs. Turkey is a party to the Pan-European Origin Cumulation System since 1999, whereby diagonal cumulation is extended to Euro-Mediterranean countries. Turkey also extends it to Kosovo, through its FTA, and to Algeria although there is no FTA in place.. Turkey's alignment for GSP-related RoOs is advancing, but further steps in product and geographic coverage are needed. However, Progress Reports by the Commission in 2014 and 2015 state that although Turkey's level of alignment with the EU's customs legislation is overall high and its implementation and enforcement capacity is adequate, Turkey still has to fully align some of the customs rules with the acquis, especially in the areas of free zones/duty relief, duty free shops, surveillance and management of tariff quotas, and authorized economic operators. Turkey's requirement to present proof of origin for some goods in free circulation in the EU, such as woven fabrics and apparel, when imported to Turkey; and designation of specialised customs offices to complete import formalities in certain goods are other challenging issues that need to be tackled.

6. What happens to customs revenue in the Turkey-EU Customs Union? Is there some arrangement for pooling/distribution of such revenues?

The parties agreed from the outset that the CCT revenue would be collected by each party at the initial port of entry and that the CCT revenue would accrue as income to the party collecting that revenue.[10] (TURKISH OFFICIALS WOULD BE BETTER PLACED TO ANSWER THIS QUESTION)

7. To what extent do Turkey's standards need to be aligned with those of the EU? What level of mutual recognition is there in practice? Regarding mutual recognition of standards, if any EU FTA partner has automatic access to the Turkish market through the Customs Union, does this mean implicit acceptance by Turkey of that third country's standards?

The regulatory convergence between Turkey and the EU through the CU is structured principally around Chapters I to IV of Decision No 1/95 of the EC-Turkey Association Council, together with some regulatory amendments, as well as reforms in administrative practices (primarily in Turkey). According to Decision No 1/95, Turkey undertook an obligation to fully align its laws to the EU acquis in a wide range of issues including the abolition of TBTs in industrial products, competition, and industrial and IP issues. Articles 8 to 11 of Decision No 1/95 address Turkey's commitment to align its legislation and administrative practice related to TBTs and conformity assessment with EU rules. Article 9 of the Decision stipulated that "when Turkey has put into force the provisions of the Community instrument or instruments necessary for the elimination of technical barriers to trade in a particular product, trade in that product between the parties shall take place in accordance with the conditions laid down by those instruments." Thus, the CU regime clearly defined the framework within which trade between the EU and Turkey was regulated. It

[10] See Statement by Turkey on Article 3 (4) of the Decision 1/95:
Turkey undertakes to ensure that customs duties or charges having equivalent effect levied pursuant to the second subparagraph of Article 3 (4) are not allocated to any specific purpose but accrue to its national budget in the same way as other customs revenue.

was Turkey's responsibility to incorporate the EU legislation into its domestic regulations, so that Turkish products can enter into the EU market without further hindrance in terms of technical barriers.

The CU has eliminated import tariffs for trade between Turkey and the EU in relation to most of the industrial goods, and the TBTs are expected to have become less relevant where Turkey has aligned its legislation to the EU's *acquis* in the areas covered by the CU. Delays in alignment of Turkish legislation with EU technical regulations under the CU can be a source of NTBs. Turkey is informed of legislative developments in the EU in the normal course; nonetheless, Turkey has raised issues in this regard and the World Bank (2014: iii) comments on a "notification deficit", which hampers Turkey's prompt and efficient adoption of the *acquis*, In the non-harmonised area, where mutual recognition is applied to prevent domestic regulations develop into TBTs, Turkey adopted the relevant legislation that entered into force on 1 January 2013. This was an important step to apply the mutual recognition to trade in products for which no significant harmonisation was achieved.

Under the CU, harmonization has been unilaterally determined by the EU within the context of the Single Market as opposed to negotiated – or commonly agreed-harmonization. Turkey has committed itself to align with the EU regulations as they stand and can only be in the position to influence them once it accedes to the EU, hence another component of the asymmetrical relationship between the parties.[11] The EFTA countries for instance, while not in a customs union with the EU, also benefit from access to the Single European Market and are obliged to apply the EU acquis for which, similarly to Turkey, they cannot pronounce on how it is defined nor do they have a voting right. However and differently from the CU, Protocol 12 of the EEA Agreement guarantees that when the EU takes the initiative to negotiate MRAs that it will negotiate on the basis that the third countries concerned will conclude parallel MRAs with the EFTA countries, equivalent to those to be concluded by the EU. Such a procedure, which grants simplified market access to 3rd countries and EEA countries does not exist in the CU. With Switzerland, also not in a customs union with the EU, there is a bilateral agreement on goods trade that covers 20 regulations. It is not a general agreement but covers specific sectors. Each year, the agreement is amended and new sectors are updated as are Swiss regulations so items manufactured in Switzerland can be exported to the EU without the requirement of an EU conformity assessment certificate.[12]

Istanbul, 26 October 2016.

[11] World Bank Report on the Evaluation of the EU-Turkey Customs Union, 2014, para. 57-58.
[12] Ibid.

Lord Bridges of Headley MBE, Parliamentary Under-Secretary of State, Department for Exiting the EU (DExEU), and Lord Price CVO, Minister of State for Trade Policy, Department for International Trade (DIT) – Oral evidence (QQ 40-67)

Evidence Session No. 5 Heard in Public Questions 40 – 67

Thursday 13 October 2016

Watch the meeting

Members present (External Affairs Sub-Committee): Baroness Verma (Chairman); Baroness Armstrong of Hill Top; Lord Dubs; Lord Horam; Earl of Oxford & Asquith; Lord Risby; Lord Stirrup; Baroness Suttie; Baroness Symons of Vernham Dean; and Lord Triesman

Members present (Internal Market Sub-Committee): Lord Whitty (Chairman); Baroness Donaghy; Lord German; Lord Lansley; Lord Liddle; Lord Mawson; Baroness Noakes; Lord Green of Hurstpierpoint; Baroness Randerson; Lord Rees of Ludlow; and Lord Wei.

Examination of witnesses

Lord Price and Lord Bridges of Headley.

Lord Whitty took the Chair

Q40 **The Chairman:** Welcome. We are at some distance from you at the moment. We try not to be confrontational, but we would like to be nearer than we are. Nevertheless, you are very welcome, and welcome to our visitors and officials. Thank you very much for giving us this time. It is helpful at this stage in our relatively short initial inquiry for you to be here and, indeed, for both departments to be represented here. We appreciate you doing this and will try to fit all our questions within the time that we have told you.

This is a public session. It is being recorded. There will be a transcript, and we all have to bear that in mind in our discussions.

Could I perhaps open and allow you to expand on my specific questions? We had the Prime Minister's statement last week, which has moved things on in one sense. We also had a debate in the House of Commons, which

may or may not have moved things on, but has set a context in some respects. Could you start by telling us how you see the sequence of events in both the period between now and the triggering of Article 50? More importantly, after the triggering of Article 50 are we then in negotiations both on the withdrawal treaty and on the trade treaty, or at least a framework for the trade treaty, or, as some from Brussels have hinted, do they have to be sequential? Is there a possibility of the trade treaty being in a number of stages, possibly with transitional arrangements? Also, have we reduced the number of potential models that people have been talking about in the light of the Prime Minister's statement, or have we not in the sense that the Prime Minister seemed to say we want a bespoke UK agreement, not a Norwegian or Swiss agreement? There are other agreements around, of course. Balancing the different needs of the different sectors with which your departments are engaged, have we limited the number of options as yet, and, specifically, does the Prime Minister's reference to being kept out of the European Court of Justice and control of immigration being of paramount importance mean that some of the models are not available, or are the Government still considering those various options?

Lord Bridges of Headley: First, thank you very much for inviting us both here. It is very good to see you and I hope that this is the first of a number of appearances. Forgive me for saying this, but I am going to say it all the same: I want to try and manage expectations from the off. We have a lot of work under way. We will be talking about that in due course. Secondly, as the Prime Minister has said, we are not giving a running commentary, but we will try to give as much certainty and clarity wherever possible. We are absolutely intent on ensuring that we keep our negotiating position and the national interest paramount as we go along, while balancing that with the need for accountability. Forgive me if you leave this session frustrated, but let me start by saying that.

This is, as you say, extremely complicated as a challenge. In my mind there are five dimensions that we are operating on, which makes the Schleswig-Holstein question look relatively like a GCSE question. There are two dimensions that are related to Article 50. The first is the exit negotiation and the second the negotiation over our new relationship. The third is the repeal of the European Communities Act (ECA) and subsequent legislation that might be required as a result of that. The fourth in my brain is the WTO and what we need to do there. The fifth is the Free Trade Agreements (FTAs) and future trade arrangements. Clearly, as you will all know, these are entangled in certain respects.

In terms of the timetable that we are in control of—let me come to that as the first question—the Prime Minister has set out that we are not going to trigger Article 50 this side of the new year but we will before the end of March. Within that time we are doing the work that we are going to be talking about, coming back to this afternoon.

On the question of what then follows, there will obviously be the need for discussions about the framework of those negotiations and how they are set out. Then we will be within the two years and the framework as set

out in Article 50. Your point about wishing to ensure that my first and second strands—that is, the conversations on the exit treaty and the new relationship—are conducted together is a very good one. Indeed, when you read Article 50, it would appear that that is also what is intended. Obviously we would wish to clarify that. It makes it difficult to see how one can do one without the other.

We are looking at all options. The Prime Minister has set out very clearly the overriding aims and objectives, as you say, and we are looking for a bespoke—I am sorry; that is a word I will use a lot this afternoon—approach to this and an agreement at the end of it, because we perceive ourselves as being in a unique position as regards the EU. We are looking to control our borders and our laws, as the Prime Minister has said. Although I know it may not necessarily be the focus of these Committees, we wish also to maintain co-operation on the common challenges that we and Europe will face in the years and decades ahead, and at the same time we will be aiming to achieve the freest possible relationship as regards trade for our businesses right across the UK. We are not ruling out options at this point. Clearly, there are noises from various quarters that certain things are and are not possible, but we are assessing everything, and we will come on to some of those points in due course.

I do not know if Mark wants to add anything.

Lord Price: On the sequencing for FTAs, which was the last of George's points, and the WTO before, both the Secretary of State and I have met Roberto Azevêdo from the WTO and had constructive conversations. Officials have met with the WTO. We have also had constructive meetings with officials at the EU. We know that one of the first things we have to do in the sequence is strike our own schedules with the WTO. We were of course a founder member of the WTO. We do not need to accede to the WTO as we are already a member, but we need to go through the technical process of adopting our own schedules. Clearly, that is the first thing we need to do.

The second important thing is to come to an agreement with the EU on our trading relationship with the EU. Once those two things are shaped, we can of course begin negotiations with third parties, cognitive of the tariff or the non-tariff barriers, or the other regulations we have put in place. That would be the sequence. The Secretary of State has been very clear that negotiations on the signing of any deal that we do will be after leaving, so we are clear on when we can sign and move to ratification, and we are clear on the sequence of things we need to know before we can fully strike FTAs with third-party countries.

The Chairman: On the last point about third-country FTAs, does that mean we could negotiate but not reach the point of conclusion and signature in parallel with our relationship with the EU, or does it mean we cannot negotiate until the conclusion of a withdrawal treaty?

Lord Price: Clearly, we would want to have a discussion with the EU about some of our arrangements, because we are tied with the EU. As I said, the discussions with the WTO are very constructive and consultative.

The formal position is that we cannot sign and ratify until after we have left, but we can have discussions ahead of that.

Baroness Symons of Vernham Dean: We cannot sign any FTAs with third parties until we are no longer a member of the EU, but there are such things as memoranda of understanding, which can provide building blocks on the way, surely. Those are the sorts of things that are being mooted by the people who are interested in FTAs with us at the moment. Do you see that as a useful way of protecting ourselves in the interim, so that once we are out of the EU we can go forward pretty quickly in doing what we will have to do in getting FTAs elsewhere?

Lord Price: As the Prime Minister and the Secretary of State have said, we want a smooth transition, particularly for business. We currently have FTAs with the EU, so we are thinking about how they might be adopted. In addition, on new FTAs, we are thinking about what we might want to do in advance of leaving. Working groups have been formed—we have said that publicly—with a number of countries, and we will start working through the art of the possible over the next two years.

Lord Green of Hurstpierpoint: To what extent is there a problem in the parallel negotiation, in that the third party will find it difficult to crystallise what they want of us until they know what our relationship with the EU is going to be? In that sense this is sequential, even if the process is not sequential.

Lord Price: As a former Trade Minister, you know that absolutely to be the case. One of the requirements to sign an FTA is that we have clarity on what our own tariffs and non-trade tariffs are going to be, so crystallising our agreements with the WTO and understanding better our agreement with the EU will lead us to be able to do those FTAs. One can imagine a scenario where those things become clearer over a number of years, and as they become clearer our discussions can clearly strengthen.

Q41 **Lord Dubs:** May I ask about the specific situation in Ireland? We do not know whether there will be a hard border, a soft border or no border, so I suppose your answer will depend on that. Do you see any need to look at the situation as regards Northern Ireland and the Republic and trade between the two differently from anything else, or do you think it will be entirely taken over by the total discussion with the EU?

Lord Bridges of Headley: That is a very good question, Lord Dubs. In a sense, I would say that we have to look at it from the perspective of our overall approach, and within that the context of Ireland and Northern Ireland. On Monday I cited at the Dispatch Box Protocol (No 20) on the application of certain aspects of Article 26, which sets out that the EU recognises the common travel area—I need to check the specifics—as a specific case. I think there is a widely held view not just obviously in this country, in Northern Ireland and in the Republic but across Europe that we need to think about the challenges faced in Northern Ireland and the Republic as regards the border there. We are absolutely clear that we do not want to return to the hard border, and we are looking very carefully at the solutions and approaches that could entail.

I am sorry, but I cannot be more precise than that at this juncture. We are in very close co-operation with the Irish government on this. As was also raised in the House the other day, Ireland itself is a big exporter of goods to the UK, so it is a question not just people but of goods.

Q42 **Lord Liddle:** This is a follow-up to the question I asked you in the Chamber the other day. Clearly, any interim arrangement that we make on trade, given that it is most unlikely we will be able to negotiate a comprehensive free trade agreement within two years with the EU, is of extreme importance. What options are the Government considering for that interim arrangement?

Lord Bridges of Headley: I am so sorry, forgive me for smiling. I am not going to go into lots of options, but I can certainly give you comfort in that—and here I will repeat what I said the other day—we are intent on this being smooth and orderly. A number of business organisations have indeed come to us and flagged with us the need for transitional arrangements. Those could take a number of forms, which people have mooted. I am not going to be drawn into that right now, if you do not mind, but I will say that we are cognisant of the need for us to look at this, not just for the reason that you gave but because when we come to agree a new treaty there will obviously be a time when that will need to be ratified across Europe, as you so rightly say. There are various meanings of this term 'transitional arrangement', and I am trying to pick my words with extreme care here so that we do not start confusing these things. We are looking at options and are considering various things, but it is part and parcel of an entire package.

I am sorry that I cannot go further, but I completely heed not just your question but the concerns that businesses have about this point.

Q43 **Lord Liddle:** Could I come back on one point? I am not trying to be difficult; I am very encouraged by what you say about smooth and orderly and all that. But does that not mean that the Government have ruled out as an outcome the possibility of simply being dependent on WTO rules after two years for trading?

Lord Bridges of Headley: We want this to be smooth and orderly and in the best interests of the entire British economy, and we believe that if we obtain the right deal it will also be in the best interests of the European Union. We are looking at all options but, as I say, it is of paramount importance that we make sure that this is smooth, orderly and in the economic interests of this country.

Q44 **Baroness Randerson:** It has been put to me that WTO schedules are already quite seriously out of date and that there are a significant number of countries that would be likely to use any agreement that we make on a new set of agreements with the WTO, which will have a knock-on effect across the world and could mean a serious and lengthy renegotiation across WTO member countries. I am interested in your comments on that.

Lord Price: That is a point I have heard. I am pleased to say that the advice we have is that what we intend to do is predominantly technical, moving from an EU schedule to a UK schedule. I am also pleased to say that since the referendum I have talked to 19 Trade Ministers in the EU and outside, and all have been very supportive of the need in the first instance for us to have our own schedules. To that extent, I am not anticipating any major issues with that piece of work being completed in good time.

Q45 **Baroness Armstrong of Hill Top:** My main question has been asked by Lord Liddle, but I want to push you a little further on transitional arrangements, because the reality is that, for example, in the automotive industry, which I am having to learn far more about than I ever wanted to know, it is very clear—I come from Sunderland—that investment decisions leading up to 2024, and I have a list of them here, will be made within the next two and a half years. That means that their knowledge and understanding of how we intend to proceed is absolutely critical to the retention of the car industry in this country, and certainly, I might say, in Sunderland. I am sure you are aware that Renault is now a major investor in Nissan, and it has factories in France that are only at 40% capacity. It could transfer production within a month. That means that the lack of clarity around interim arrangements is potentially hugely damaging.

How are the Government approaching this, and what are you going to do? This is not only the automotive industry; I am giving that as an example, for obvious reasons. What are you going to do to make sure that that level of uncertainty does not lead to massive disinvestment in our manufacturing capacity?

Lord Bridges of Headley: I am sorry to disappoint you. Let me first of all say that I am entirely aware of the automotive sector and the kinds of investment decisions that it is taking, and, as you rightly say, it is not just in those sectors. I worked in business myself and know that you make decisions right across the board for two or three years ahead. So you are absolutely right.

We are really very focused on this, balancing the need, as I say, for us to create as much certainty and clarity in the process as possible with the national interests in our negotiating position and the realism of entering into a negotiation that may take two years or more. We need to try to get that clarity and certainty. I completely agree with you. I am very sorry to say that, as we sit here right now, I cannot go further but, believe me, we are very focused on it.

This is not related directly to your point, but the determination to provide this clarity and certainty is embodied in our approach to the repeal of the ECA and the transposition of EU law into UK law. I know that that is unrelated to the precise point you are making, but it also shows our intent on certainty.

Forgive me. I totally take your point, but I cannot go further on that.

Lord Price: I certainly cannot go further on ultimately what will happen with the EU, but I would like to give you some confidence about the British Government's investment of time into understanding the issues for the car manufacturers. We are very well aware that the North East exports more cars than Italy. I have spoken to all the leaders of our car businesses in the UK. I have seen the Japanese ambassador twice. I have seen Minister Suzuki and Minister Katase. I go to Japan next week, and we have heard very clearly what they would like to achieve. We are clear on what that is.

Another thing that I think is comforting is that these points are also understood across Europe. I was in Slovakia two weeks ago, and Jaguar Land Rover is going to open a £1 billion facility in the Czech Republic, in Slovenia, and in Germany. The automotive manufacturers and suppliers are very well aware of the interconnected trade in Europe. This is an issue for all of Europe and not just for the UK. We clearly understand the points that are being made by business, and we also understand the impacts and the ramifications across Europe.

Q46 **Lord Lansley:** Could I explore the mechanism for creating a transitional arrangement and how that might work in practice? I should declare an interest: I am co-chair of the UK-Japan 21st Century Group, although but I am not really talking about Japan as such in this question. Conversations that I have had in Brussels have suggested that the way the European institutions might look at it is like an accession in reverse, whereby you leave and under the Article 50 agreement there is a process by which one subsequently drops out of each of the chapters. It is a bit like the 35 chapters of an accession process.

The question is: do you anticipate that it will be possible, pending a treaty on the future relationship, for the Article 50 agreement—nobody has ever done it before; nobody knows precisely how it is supposed to work—to have legal force by way of an agreement from the point at which the United Kingdom leaves over a period of time while that transition, which is based on the principles of the Article 50 agreement, is being worked out in detail?

Lord Bridges of Headley: Forgive me. A number of options have been mooted. That is one, and I have seen others, such as one about a customs union or something like that. Various options have been mooted. I am very sorry, I know it is not what the Committee wants to hear, but I am not going to start speculating on what may or may not happen. These are all things that we are looking at in the round and in the wide parameters of options open to us.

On the point overall, I have to say that it is not only the automobile sector that tells us this; the financial services sector, and others, also tell us this. I would echo Lord Price's point that irrespective of where or when such an arrangement, were that to be needed, would come in, it would be, one would think, in our interests and in those of our partners in Europe to have a very smooth and orderly process. We are very much approaching this from that standpoint.

Lord Lansley: But would it be fair to say that that points to the need to be thinking not only in sector-by-sector terms—sectoral analysis—but, perhaps at least as importantly, about the structures of regulatory co-operation? Free movement of labour is one of those, but there are a dozen at least of those for everything from competition policy on the one hand to mutual recognition on the other.

Lord Bridges of Headley: Yes, you could certainly look at it like that. You are right that there are areas where such agreement would be in everyone's absolute best interests to ensure that on day one, things continue to function. Looking at points of activity or regulation is certainly one way one could look at it. I am sorry; I do not wish to be obtuse here. I am just not in a position to go into much greater detail than that. These are very good points you are making.

The Chairman: The next question is from my co-Chair, Baroness Verma.

Q47 **Baroness Verma:** Can I take you back to the WTO and have a little more clarity about schedules and tariffs, and your approach to splitting the tariff rate quotas that we currently share with the EU and agricultural subsidies? Would the UK be likely to increase or decrease tariff rate quotas following Brexit? In your own view, would that be subject to separate negotiations with the other WTO members?

Lord Price: You raise an excellent point. One of the things that we will have to clarify is how quotas are split out. The Commission knows that we need to do that and has been constructive in early conversations. The WTO also knows that we need to do that, so that is part of our dialogue going forward, but I think it would be fair to say that, as of today, we have not resolved how that should fall out.

Baroness Verma: Basically, I am trying to draw out the point that we keep being told that there are a lot of things that we cannot discuss openly at this moment because you have not decided on them, and Lord Bridges gave the five options that he is mooting on, but it leaves great difficulties for other Member States, first and foremost, to look at their own responses to our response. It would therefore be useful perhaps to prise out of you a little more about EU tariffs and whether they are temporary measures, whether they are going to be retained after Brexit, whether we are going to continue with them. How do we start shaping relationships with our EU partners if we are not quite clear even at this stage in our thinking what we are going to be doing? There are a lot of grey areas that we need to be prised out a bit.

Lord Price: On the WTO tariffs, the simplest thing would be to adopt the current tariffs that we have with the EU, but, as you rightly draw out, there are things like quotas, which have to be handled separately. We are aware of that; we are aware of the options. The EU wants to be supportive of our finding our own schedules, and we have approximately two and a half years from now, if Article 50 is triggered at the end of March, to work those things through. We think that is entirely doable, we think it is a technical issue, and the WTO and the Commission are both saying that this is a reasonably straightforward thing that they want to

help us to do. If you want me to say today that we have agreed that it is X, Y and Z, I simply cannot do that, because we have not begun the formal process of those conversations.

Q48 **Baroness Verma:** On an issue that is totally unrelated to the previous question, we are already seeing an impact of Brexit with food prices and Unilever this morning trying to raise its price structures with the big multiples here. What is the thinking behind currency fluctuations, inflation and the impact on British consumers going forward? We need to have some fair idea of the understanding and the thought processes behind that, because these things will become more and more common as we go forward.

Lord Price: Lord Bridges may have something more specific to say, but I can only repeat what the Chancellor said very publicly, which is that the markets are reacting and the markets are the markets. Sterling will go up and sterling will go down, and businesses will respond to that. I have no crystal ball; I cannot tell you what will happen to sterling next week or the week after or the year after. We are where we are.

Lord Bridges of Headley: I would just like to add that it is a very fair question. The analysis that we are doing is—to use a word I do not much like—holistic in many respects. It is holistic in the sense that we are trying to ensure that we also look at building up a picture of the challenges and opportunities that the UK faces in the round—we will come on to talk about the sectoral analysis—and then, as the Chancellor has said already in public, how the Treasury, in things like the Autumn Statement and other fiscal events, can use the tools in its toolbox to help to strengthen or address those problems and challenges. We are doing all this work. I am sorry about your frustration that it is taking us time, obviously, but we want to do it well and with due deliberation but due speed. I am sorry that I cannot go further than that.

Q49 **Baroness Verma:** Apologies, but I have one final question. It is basically to ask whether the Government are going to consult industry on whether to change or charge tariff rates.

Lord Price: One of the things that we have tried to do from the outset is to make it clear that we want to engage with industry over the free trade agreements that we are going to sign. The truth is that what we will take on will be different for every country, for every FTA, for every trading bloc, simply because the countries that we decide to pursue FTAs with will already have different schedules in the WTO, a different regulatory regime and a different legal regime. A typical trade deal is made up of 30 chapters that are broken down between goods, services and legal. The decisions that we will have to make are which of those chapters we want to pursue, which are going to be straightforward, which have the best impact on British business.

It would be very misleading of me to try to give you a general answer to that question, because to a large extent the input of business will depend on the country and the sector, but we are committed to doing that. We

have said very openly in the DIT that we will be drawing industry in to help us when we look at particular chapters and particular industries to make sure that what we agree is in the best interests of that industry, both in the UK and in the third party. The simple answer to your question is yes, but the far more complicated answer is that it will vary by country and by chapter.

Q50 **Lord Horam:** Can I come back to the important question of the transitional arrangements? Can I clarify what you are saying, or maybe not saying, on this subject? Is it clear that there will have to be a transitional agreement?

Lord Bridges of Headley: I am saying that we are looking at all the options on the potential outcomes. What is clear in my mind is that given the speed at which the ratification would work—Lord Liddle made this point—and it depends if one calls that a transitional arrangement, there would be a process by which that would have to be covered and at which point the treaty comes into play. So you could see signing of the negotiations ending and coming in at a certain point, what happens between X and Y.

Lord Horam: That could be at the end of two years?

Lord Bridges of Headley: It could be. That is where I am. There is a separate point that people are trying to tease out, which is—correct me if I am wrong, Lord Liddle—what if we have left but are still negotiating the new treaty.

Lord Horam: Exactly.

Lord Bridges of Headley: That is where we are looking at what the options might need to be.

Lord Horam: For a transitional arrangement?

Lord Bridges of Headley: For a transitional arrangement on that point.

Lord Horam: Which may last some time?

Lord Bridges of Headley: It may or may not. Does that clarify it? You are quite right to pick me up on it.

Lord Horam: There is also the question, which relates to what Baroness Armstrong was saying, about decisions being made by companies over the next two and a half years. They will need to know something about the transitional agreement, or how can they make decisions?

Lord Bridges of Headley: I totally agree, which is why we are focusing so much on this point. You are absolutely right. I agree with you 101% that there is this concern in a number of sectors. Yesterday, I was in the Thames Valley and people were asking me precisely this question.

Lord Horam: A hope was expressed in the *Financial Times* yesterday that there might be some embryonic transitional agreement understanding by next summer.

Lord Bridges of Headley: I am very sorry, but now we are into me speculating on what someone else might have said. I am not going to do that. All I will say is that we are really focused on this as an issue. Exactly as Baroness Armstrong said, there are decisions that companies need to take. As Lord Price said, it is in all our interests to make this smooth and orderly. When I say 'all our interests', I mean both here and in Europe. Forgive me if I cannot go further, but I hope that begins to clarify what we are talking about.

Lord Price: If I may build on Lord Bridges' point, it is a commonly held concern around the world that businesses want to have some reassurance that they can continue trading, and they are talking to their governments about how that is achieved. It is something that we are all aware of, and we want to achieve the right outcome.

It would be remiss of me not to say that, wherever I have travelled, the fundamentals about the strength of the UK economy and the UK as a place to invest and grow a business have not been forgotten. For a number of companies, these [trading] arrangements are not necessarily the most important thing in their mind when they are investing in the UK. Instead, they talk about the fact that we have four of the top 10 universities in the world, we have a competitive corporation tax rate, the UK is sixth in the world for ease of doing business, geographically we are well-located, our time zone means you can trade east in the morning and west in the evening. There is a whole host of things that companies are looking at in their investments. What is encouraging for all of us is that since the vote on 23 June we have continued to see strong investment into the UK from Veolia, Hutchison Whampoa, Wanda Group, SoftBank buying ARM, et cetera—a whole host of companies. There are many factors in businesses choosing to headquarter and grow in the UK, besides the very obvious concerns and questions that are being raised about our future trading relationships.

Q51 **Lord Liddle:** The Prime Minister was extremely clear in her conference speech that an eventual deal with the EU must involve some British sovereignty over free movement and no longer accepting the jurisdiction of the European Court of Justice. I hope I am right in interpreting her speech in that way. Are these to be treated as long-term objectives, or would they be essential requirements in any transitional arrangement?

Lord Bridges of Headley: I am very admiring of your ability to get me to answer the question in a slightly different way.

Lord Liddle: It is a very legitimate question.

Lord Bridges of Headley: It is a totally legitimate question; I am very impressed by how you are phrasing it to try to get me to comment. They are the aims that the Prime Minister has set out for the future relationship between us and the EU, and what we wish to achieve. I cannot go further in talking about a putative transitional arrangement. You raise some interesting points about immigration, for example: who can come here at what point. This goes to the point Baroness Armstrong made about businesses interested in what access they will have to skills. I talked to

universities yesterday and they were interested in a similar point about academe. These are all important points. It is part of the same thing, but I cannot go further now.

Q52 **Baroness Noakes:** My question moves beyond transition, so we may be heading into slightly easier territory in focusing on future trade arrangements. On 27 September, the Secretary of State for International Trade spoke of "pursuing a more liberalised trade agenda … free to help shape an even more transparent, more open and more liberal trading environment". Dr Fox also stated that the decision to leave the EU is "not symptomatic of looking inwards but a people who want to take more control over our laws", which is all very uplifting. Could you put a little more flesh on the bones of what that means in the context of trade with the EU and, indeed, with non-EU countries?

Lord Bridges of Headley: Tempting though it is to unpick words and put a Kremlinologist interpretation on to them, I would rest on what the Prime Minister has said many times, which is that we are looking for the freest possible access to our European partners' markets. As we might come on to, we are looking at a whole range of options and scenarios from the perspectives of the sectors that we have picked out and what that would mean for our relationships at the moment and how they will need to change. Frustrating though it will be for you, I cannot go much further than that. Maybe Lord Price can talk about the non-EU side.

Lord Price: I think what the Secretary of State was encapsulating in that comment was the report from the OECD for the G20 meeting. The OECD said that in 2009 world leaders promoted free trade as a way to drive the global economy, but the fact was that the world had become more protectionist over the previous six years. While everybody realised the economic opportunities globally for free trade—what it does for consumer choice, for prices, the exchange of knowledge, building competition and greater skills—the reverse had been happening. I believe that in that speech he was talking about wanting to try to achieve what was set out by world leaders in 2009, and it has been repeated by the Prime Minister: that we want to be a beacon for open and free trade. That is what lies behind the comments.

Baroness Noakes: Looking forward, do we have a vision of a different form of trading arrangement with EU and non-EU countries? Are they the same principles that operate in all our trading arrangements?

Lord Price: George can speak for the EU.

Baroness Noakes: Why is there a difference once we have left the EU?

Lord Price: DExEU is responsible for policy with regard to the EU and I am responsible for policy outside the EU. I want to be clear about our briefs for today. Our position is that we do think that open and free trade, the reduction of tariffs and making sure that there is mutual recognition of standards all help business perform better. They reduce the costs of doing business. We believe that that is to the benefit of consumers and businesses. That is what we want to promote.

Q53 **The Chairman:** We have this vision of a hugely liberalised world. I speak as Minister for Agriculture at the early stages of the Doha round, which was supposed to be a great liberalisation. Agriculture was the first hurdle and we never jumped it. The issue of our quotas and tariffs for agricultural produce is not only an internal EU issue, because until we resolve it we cannot do deals with large numbers of nations around the world. You have a serious sequencing event, whatever the eventual Valhalla that we are aspiring to. You have to solve some of these nitty-gritty problems with the EU before anybody else can seriously negotiate with you.

Lord Price: We are well aware of that. Defra is very involved in these discussions. We understand clearly the views of the agricultural sector. You are right when you say this is a global issue, not a UK issue. If the primary responsibility of any Government is to defend their population, the second responsibility must be to feed its people, so you find that across the world a high level of subsidy tends to go into agriculture. Those subsidies and the protectionist nature of governments in feeding their people lead to the kinds of barriers you are talking about, which were particularly prevalent in the last round of the WTO. You are right to draw it out as a something that we have to consider. We are very aware of that and have taken representation already.

Q54 **Lord German:** Could I take you to your opening comments? You have repeated throughout that the UK Government have ruled nothing out, and conversely, therefore, you have ruled nothing in. In answer to Lord Lansley you said that looking at regulation is one of the approaches that you might take. Would it be fair to assume that the British Government are deeply engaged in putting the research and understanding behind each one of these alternative approaches that might be adopted? Very specifically, what work has been done and is being done on EU standards that are relevant to trade? Do we need to maintain or change those standards? What work, if any, has gone into the potential costs of compliance with rules of origin, which are absolutely crucial for British trade, if we decide as one of your options, given that you have said that it is still on the table, that the UK will leave the customs union?

Lord Bridges of Headley: I completely agree on both points. Both are key and pivotal. We are doing a lot of work both on standards and rules of origin.

I will deal with standards first. We are looking through each of the sectors on standards and qualifications. Yesterday, for example, someone talked to me about recognition of medical qualifications. This is an issue that we absolutely have to address. There is mutual benefit for us and our EU partners in the current situation and how that might therefore pertain in the future, and to consumers both here and across the EU. You probably know that 75% of European standards have been developed voluntarily entirely by industry; the remaining 25% are still voluntary and provide business with a universally accepted means of meeting specific EU rules. We are absolutely aware of the importance of interoperability and the

benefits that standards bring, and qualifications. We are looking at that for each of these sectors, and thinking generically about where we might wish to go on that point.

Rules of origin, again, are very important to the decisions that we may or may not take as regards our future relationship and the customs union, et cetera. I have been in conversations with those involved in shipping and customs and business itself about exactly how those rules of origin operate. We are looking at this sectorally, but as a generic point, as I said earlier, I am very struck by the means by which we now have digital technology and data to help in the customs process. We are very focused on that and are bearing it in mind, but likewise, as you may be alluding to—this comes back to the automotive point—these supply chains are very sophisticated now and are fast and just-in-time. You see goods coming in, being assembled, going out, being assembled a bit more, and coming back for the final goods to be made up in some cases. We are looking at this sectorally and generically and, in the case of rules of origin, from the bottom up.

I am very keen to get out and about—I was out yesterday and last week, and I am going on tours next week—to talk to people who are at the cutting edge and coalface of these issues. There is a real danger that we will be stuck behind our desks and look at these facts, which may be facts, figures and percentages. When it comes to things such as rules of origin, customs processes and everything else, I want to be sure that we are absolutely aware of the administrative and implementation processes involved and what the various options might therefore entail.

Lord German: Can I return to the costs of compliance? If you take the motor vehicle industry, where all parts of the UK have very specific contributions to make to the motor industry throughout the whole of Europe, should we leave the customs union, which is one of the options—you have not ruled it out or in—how on earth do you manage to identify and overcome that identification issue, when who knows what the eventual answer might be to the question of where the point of origin is for the finished article or the process by which you export it into another country where the customs barriers are against you? Have you made some effort to understand the costs of that?

Lord Price: Specifically in answer to your question, I had a meeting with the Swiss Trade Minister, who has talked precisely about this point and about the complexities of being outside the customs union in Switzerland, the procedures that they have to go through in importing and complexity in the costs. Yes, we do understand the complexities for the car industry. All those things are being fed into the deliberations at the moment.

Lord German: Forgive me, but the word was costs. Do we understand yet how much it would cost to be able to comply in each of these sectors if we left the customs union? These are the options that you have given us.

Lord Bridges of Headley: That is absolutely right, and those are exactly the kinds of things we are looking at and working on as we speak. I am

sorry, but I am sounding obtuse again. Your concern is my concern, and we are working on them.

Lord German: I presume, therefore, that it will be completed by the time we trigger Article 50?

Lord Bridges of Headley: We are working with due and deliberate but precise speed on these issues.

Lord Green of Hurstpierpoint: Lord Price mentioned that you have had conversations with your opposite number in Switzerland. Have you had conversations with your opposite number in Turkey, the relevance being that it is inside the customs union but not part of the Single Market?

Lord Price: I have meetings in the very near future with representatives from Turkey. In fact, we should have a Joint Economic and Trade Committee (JETCO) quite shortly. We are very aware of it. Thank you very much for your letter to the Prime Minister setting out your thoughts, which was very helpful, Lord Green.

Lord Green of Hurstpierpoint: I am pleased to be of service.

Q55 **The Chairman:** On the same theme but relating to another option that we have not mentioned, have you also had discussions with your opposite numbers in association agreement countries such as the Ukraine?

Lord Price: No, I have not met with the Ukraine yet. We could go round over 200 countries. I want to be careful about who we have and have not spoken to. More broadly, we want to understand all the options to inform the best decision for the UK, and that means talking to countries that have a relationship with us. I am particularly keen to talk to as many countries as I can over the next five or six months to inform decision by DExEU and others regarding what we have to do.

The Chairman: Given the degree of constraint on the Ministers, we have covered the issue of the various options. I congratulate both Ministers on not mentioning the terms 'hard exit' or 'soft exit' as part of their presentations. Can we move on to the processes and resources?

Q56 **Lord Mawson:** I welcome the considered way in which you are conducting this process and working through the detail, and I understand that it is very early days. I am reassured that you are resisting the temptation to put everything out there, which is totally sensible—this process must not be run by 'Peston on Sunday'— but there are checks and balances. The EU has significantly strengthened its policy on transparency in trade negotiations, including public consultations, civil society dialogue, a sustainability impact assessment and the European Parliament. What initiatives will the UK Government undertake to match and surpass the EU's transparency and democratic involvement when negotiating their new agreement with the EU?

Lord Bridges of Headley: First, as a rider, I should say that I am a strong believer in transparency. The purpose of transparency is obviously to improve accountability, and I am a big fan of that. In this case, as we

have been saying and as the Lords Select Committee has said in its report, we have to balance the need on the one hand for accountability and transparency, which is totally justified—and this Committee is one aspect of delivering that accountability—with the need on the other for us to ensure that we can negotiate in the national interest and are not displaying our hand or giving things away that might put us at a disadvantage in the negotiations. Your question shows the struggle that we are having doing this. That is not an excuse but a simple statement of fact that we need to put on the record.

On practical steps, David Davis, my Secretary of State, said in November, and reiterated yesterday in the Commons, that this Parliament would at least have the information available to the European Parliament. I know that sounds like, 'He would say that, wouldn't he?', but it is important that we make this clear. As regards what information that is, it is still early days. My investigations into this have revealed that we were one of the countries pressing the European Parliament for the transparency and accountability that now exists. That shows our level of intent. You will have seen what happened with the Transatlantic Trade and Investment Partnership (TTIP) negotiations and the levels of accountability and transparency. I am not going into specifics as to whether they are going to be copied now, but that is an interesting point to bear in mind.

I am sure you have all read the European Commission's factsheet on trade negotiations, which I will quote. This is about trade negotiations: "The negotiations and their texts are not themselves public. This is entirely normal for trade negotiations, not just those involving the EU. There are several reasons for this. First, a certain level of confidentiality is necessary to protect EU interests and to keep the chances of a satisfactory outcome high. When entering into a game, no one starts by revealing his entire strategy to his counterpart from the outset: this is also the case for the EU. Second, negotiators have to trust each other to come to a deal that satisfies both sides. For the EU, this means the result must meet the objectives set out in the instructions from the Council. If there is no climate of confidence, then negotiators on both sides cannot work together to come to the best possible deal". That is the EU's position, and there is a lot of sense in that.

We need to bear in mind that that is with regards to a trade negotiation. This negotiation is more expansive than that. I am not making these points to create excuses in advance, but this is very much our overriding approach.

We will come on to talk about consultation in more depth, but the entire government machine is consulting different parts of industry and civil society. It is very important that we do not look only at business. I have met charities, the Church of England, universities and NGOs. It is very, very important it is not only the four Ministers in DExEU, otherwise we would not sleep—we do not sleep very much at any rate—but we need to make sure that we are involving the whole of government in that and that the process is done with deliberate speed to obtain the views of everyone on board. Sorry, that is rather a long answer.

Baroness Armstrong of Hill Top: The public view was expressed in the referendum, but my experience of talking with them is that they have very different ideas of what it means. What are the Government going to do—otherwise, a lot of people will be angry—

Lord Bridges of Headley: About?

Baroness Armstrong of Hill Top: —about understanding where the public are in different areas of the country, and what they are looking for?

Lord Bridges of Headley: We are undertaking a wide-ranging consultation with groups that represent different bodies of the public. That is a good, proportionate way to approach this. In the debates that are being had in this House or the other House, the representatives of the public are also making their voices heard.

Q57 **Lord Green of Hurstpierpoint:** Can I turn to the question of how you are organising this very considerable effort? You referred earlier to the division of labour between the two departments, one focusing on trade negotiations with other countries and the other focusing as part of a wider mandate on the Brexit arrangements, of which trade is a part. Could you update us on how you are progressing with making sure you have the right level and quality of resources and how far the division of labour works in practice on a day-to-day basis as any given issue comes up? I might have a supplementary or two depending on how you respond.

Lord Price: Clearly DExEU is involved in far more than a trade negotiation; it is much wider than that. The trade policy team in the Department for International Trade is supporting DExEU with specialist knowledge to fulfil their responsibilities. Outside of that we are looking at the WTO schedules in the first instance, and we are also looking at the FTAs to come. We had a team of 40 people in trade policy on 23 June. We now have about 110 people in that team, and there will probably be about 150[13] by the end of this year as we build resource and competence. We have had a lot of people apply to come and be part of the trade policy team. Over 800 have voluntarily written to us, which is fantastic.

The other thing to say, as you will be aware Lord Green, is that our work will not be just on the FTAs. There is a whole host of other ways in which we look to improve the trading environment between countries. Next week I am off to Vietnam for a JETCO, where we are looking at some key issues such as mutual recognition of standards. In addition, in the not-too-distant future we have an EFD—an Economic and Financial Dialogue—with China. We are doing lots of things that are not FTAs that are about building and improving the business relationship between countries.

I think we are making really good progress. We have now visited a number of countries around the world. We have been to Switzerland, Australia, New Zealand, the USA, Canada and South Korea to understand how those countries, which are very good at this and have been doing it for a long time, have structured themselves so that we clearly understand

[13] Figure corrected by witness

where we need to be optimal in our negotiating arrangements over the next few years.

Lord Bridges of Headley: May I add that this is key if you are interested in the machinery of government, because it is important that we make sure that all of government is joined up? As regards the first locus of decision-making, obviously there is a Cabinet Committee on EU Exit and Trade, and that is a core decision-making body of Ministers. To ensure that our departments are working together on a day-to-day basis, at official level, that Cabinet Committee is supported by a Trade Policy Steering Board of officials, chaired by Lord Price's department and jointly run with my department. This meets fortnightly to pool thinking on specific issues such as the ones we have discussed, and to track the way ahead. So far we have found that to be working well. We are confident about where we are, but we are absolutely not complacent. Lord Green, you know what it is like working in government and outside government in large organisations. You should never be complacent when you think you have an organisational structure that works. It can always be improved. In a relatively short time we have come, what I see as, quite a long distance.

Lord Green of Hurstpierpoint: I have two quick supplementaries, one general and one more specific. The general one is that you mentioned, Lord Price, that you expected 130 trade policy officials to be in place by the end of the year and that you have had 800 applications from people who are keen to join. Do you have a view as to how many officials you would want in place when you get to full complement?

Lord Price: That is an almost impossible question to answer, because it depends how negotiations go over the next few years. If you look at other countries you can see that the EU has around 500 people who work in trade policy. Canada had 100 people working on the Canada-EU FTA. Thus we have been able to size what other people have to do the trade deals that they have been doing in terms of quantity and quality. That will allow us over the next two years to build a team based on how we progress with the FTAs we decide to pursue.

Lord Green of Hurstpierpoint: If Canada needed 100 people just for the negotiation with the EU—and I am very well aware of how complex that was—that suggests that 130 is nowhere near enough, given the number of agreements that we are going to be progressing over the next few years. It suggests that 130 is the early foothills of where we need to get to.

Lord Price: That is right. We had 40 just four months ago.

Lord Green of Hurstpierpoint: Sure, I recognise the increase.

Lord Price: As we escalate our activities, so those numbers will build. We are pretty flexible in the way we are building numbers at the moment.

Lord Green of Hurstpierpoint: My more particular question is that I have just come back from South Korea, where of course they were talking about the EU FTA with South Korea and the British question in relation to

that. One of the comments made there is that the South Korean implementation of the EU FTA has shown a fair degree of foot-dragging in certain sectors, particularly in key services sectors and the legal sector, as I understand it. The implication is that we will need not only experts in negotiation but enough resources to handle the constant process of lobbying when you have a deal signed to ensure that the other party delivers on its commitments. South Korea would not be the only trade deal in the world where there is a need to press for full-blooded implementation in the years after it has been signed.

Lord Price: That is right. You put the point beautifully that it is not just about signing a deal but about making sure that there is compliance with it. I was in South Korea two weeks ago for a meeting with Ministers, and one of the points they made to us is just that: that you should think not only about completing the deal but about how you make sure the deal is enforced as you go forward. I agree with you.

Lord Green of Hurstpierpoint: Again, I think the resource implications are self-evident.

Q58 **Baroness Suttie:** Going back to the recruitment of trade negotiators, have we made an estimate of the total costs of how much we expect this to cost in the bill to the taxpayer? Are we recruiting from abroad?

Lord Price: We need to put forward our budget for the Autumn Statement so that we understand how much the department will cost. Everybody talks about trade negotiators, but you actually do not need that many. I will set that out a little more. Typically you would have up to 30 chapters in a trade agreement, split between goods and services and legal, and you would have a lead in each chapter and an individual who sits above those 30 chapters. One individual could cover a number of FTAs.

It depends what people mean by a trade negotiation. The reality is that the work is more about having the right number of economists, analysts and people working on the legal frameworks. When you do a round, typically you bring that back and discuss it around Whitehall with different departments on what needs to be done. I think it would be wrong to think about it as just what is in the DIT. As Lord Bridges said earlier, it is more whole of government. We will need to talk to Defra and other departments about the impact of any particular negotiating round. I think we are very clear at the moment on what structure we need. We feel very confident that we can recruit that over the next two or three years. We have not said explicitly that you have to be a UK national to do the deal. I suspect that when we get to advertising it may well be one of the things that we think about, but for now we are not at that stage.

Q59 **Baroness Donaghy:** Lord Price, you talked about the whole of government, but the number of civil servants has been reduced considerably throughout the Civil Service. What reassurance can you give us, bearing in mind that you are going to be putting the budget in in the normal way, that there will be sufficient resources to do this job?

Lord Price: I have been given every encouragement that whatever we require will be provided. Clearly there will be a good level of scrutiny, but the requests that have gone in so far have been met with understanding. I feel confident that we will get the resource that we need to negotiate trade deals for the UK in the future.

Q60 **Lord Risby:** It is really excellent to hear that 800 people have come forward, and undoubtedly many of them have done trade negotiations for countries or corporations, which is very gratifying. I just wanted to understand the mechanism for getting information into you. Some of us are involved in export promotion, et cetera. Baroness Symons has an exceptional set of contacts in the Middle East, for example. What is the best mechanism to feed in information? I know the embassies are there to assist. It sounds as if you are travelling like Marco Polo, which is fantastic, but for those of us who want to feed in pragmatically, is there a unit exactly, and how do we get to know about it? Parliamentarians have a great range of contacts. Is there some way in which we could be informed collectively? After all, there is a great desire for Parliament to be involved in this, we keep noting, in a way that takes the burden off you but goes directly to where there is a practical suggestion. I think it would be very helpful to us all to know that.

Lord Price: Thank you very much for your question. I will handle outside the EU and Lord Bridges will pick up inside the EU. In my visits I have been meeting with investors into the UK and UK businesses that are based in that country, and I have to say that the ambassadors everywhere have been absolutely first rate. We have asked that the ambassador be a conduit for that information to flow back into DIT. John Alty, who is heading up the operation, is also setting out the routes that we will take as we start to negotiate—which of course we have not started yet—regarding the feedback that we need from business in the UK and elsewhere. The ambassadors are keen to be involved, and we will set up a process for businesses to be involved, as we do for negotiations outside the EU.

Lord Bridges of Headley: It is a very good point. Just taking a step back, when we collect and collate evidence, ideas and thoughts, if you take a specific example of, say, agriculture, Defra will talk to the NFU and other organisations, and I am sure the Agriculture Ministers have open arms and doors in wanting to take ideas and views. Those views are fed into the Business Intelligence Unit in the Department for Business, Energy & Industrial Strategy (BEIS). That unit is bringing in all these views from different departments, and my officials are working absolutely hand in glove with that unit to assess what is coming in, and to make sure that it is assessed properly. At certain points my officials, and wherever possible my colleagues, in my department sit in round tables and other meetings with sectors to hear what specific groups and organisations are saying. In the case of Defra, for example, we have co-hosted a round table. I could give you other examples. It is done by each department because otherwise our department and the four Ministers would be completely deluged with lots and lots of ideas and would not have the time to see

everyone and do everything possible—and, more to the point, we need to draw on the expertise in departments. I hope that addresses your question.

Lord Risby: It seems to me that people are really anxious to assist you in a very positive way. There is no question about that. I think it might be an idea to have a letter sent to all parliamentarians saying, "If you have something to feed in in one way or another along the lines that we have been talking about, this is the email address to do it", or whatever. I think it would be good for parliamentarians to feel that they were helping you in this huge national endeavour.

Lord Price: I think that is a good thought. If I were more fleet of foot I would have said that Lord Puttnam is coming with me to Vietnam next week. He is the trade envoy to Vietnam. Also when the Secretary of State held a meeting for parliamentarians he was very clear that he welcomes input from all quarters regarding what we need to achieve. Given your prompt, I will go back and look at the formal mechanism to do that to make sure that views can be collected.

Q61 **The Chairman:** In respect of Lord Risby's initial question, I was reminded that Marco Polo took a long time to get to China and then spent two decades working for the Chinese government. I wonder whether the latest reports that we are not prepared to recruit advisers who are not British nationals is inhibiting it. There was an early suggestion that the New Zealand government had offered some of their personnel to help the British Government out here. How absolute is that prohibition?

Lord Price: I do not think it has been discussed. We are not even close to thinking about advertising and going out. That is a long way off. I would rather think of Sir Francis Drake or Sir Walter Raleigh from the Elizabethan era, who were given the task of circumnavigating the globe and North America.

The Chairman: They were, of course, pirates.

Lord Price: One person's pirate is another person's hero.

The Chairman: It is the buccaneering spirit. Lord Mawson.

Lord Mawson: In my experience, sometimes Government 'over-loves' policy-makers, economists, academics and lawyers. What proportion of your team is going to be business people with real, practical experience on the ground of trade? What proportion of those people are going to understand the modern IT-based economy of which we are just in the foothills, and all that that is going to mean over the next couple of decades? How do we ensure that this practical knowledge is placed in the middle of all this, rather than just theoretical knowledge?

Lord Price: The best way to answer that is to say that we recognise that we need that expertise within the team as we develop it. As I was saying, for every FTA there is likely to be an individual that leads every chapter. Each chapter is going to be different. The automotive chapter is going to be different from the agriculture chapter, which is going to be different

from the financial services chapter. We need the expertise, and the Secretary of State has been very clear that he wants somebody with real expertise in that particular sector to lead that particular chapter. Those people have to be supported with economists and analysts, and they may need to be supported with lawyers. We want to make sure that we have that practical experience. It is one of the reasons why we want to take the next period to really understand where we think we can get the greatest advantage for the UK regarding the various FTAs that we might want to do. We are very aware of your point, and the Secretary of State already in speeches has talked about wanting to bring that expertise in to lead all of the chapters.

Lord Green of Hurstpierpoint: I may have misunderstood about trade negotiators. You said that you had not yet advertised and that was a long way off. I am surprised to hear that, given the urgency of building up the resource base. Secondly, I had missed the point that people had to be UK citizens in this new era. That was certainly not true earlier. When I was in your role I remember having at least two French citizens employed in the department involved in trade matters.

Lord Price: You will have to forgive me, but I have lost the point about UK citizens. I am certainly not aware as the Minister responsible for bringing people in that we have specified that we will only have UK citizens. Regarding my timeframe, as you know, I was formerly a grocer and for me a week is a very long time, so in talking about our plans I am really referring to the next three or four months. It is not our plan to bring in specific negotiators on FTA agreements with any particular country. When we come to that, clearly we will consider who the best candidate for the job is.

The Chairman: The point about non-British nationals was in the press, so it would be useful to clarify that if you could.

Lord Bridges of Headley: May I jump in? If you are referring to the LSE academics, we will write to you. I think this was based on a lot of misunderstanding.

The Chairman: If that could be clarified, that would be helpful.

Lord Bridges of Headley: We will certainly make sure that is clarified.

Q62 **Lord Wei:** We have touched on this already, but I want to bring a focus to the impact on industry. The Rt Hon David Davis MP told the EU Select Committee that industries will be asked to identify the risks and opportunities of Brexit and quantify the impacts of different trading arrangements on their business, and that the Government will do some analysis on this. Officials at the Department for Exiting the EU have provided a list of 51 market access sectors relating to this. What were the criteria for selecting those sectors? Do you have the resources to work with industry to get all this done before triggering Article 50?

Just to add a little to this, obviously today in the news we have seen within a particular industry—and it is an industry that has a globalised

supply chain—there may be some activity even as this is all happening. Are you speaking to the regulators and whoever is watching and working with these industries to make sure that Brexit and currency fluctuations are not being used as an excuse to make sure that Marmite is more expensive than it should perhaps be?

Lord Bridges of Headley: I am not going to comment on Marmite, if you will forgive me. We are talking to all regulatory bodies and agencies as part of this process. As regards how we arrived at the 51 sectors, I can write to the Committee if you are interested in this. We have used the method used by the Office for National Statistics to record economic activity, which is to use standard industry classification codes, and these have segmented the UK economy into roughly 100 production sectors. We have looked at those to understand the size and contribution that each of these sectors makes to the economy and used that to support our analysis of the impact on them of Brexit. The codes are used by the Bank of England, BEIS and others across government. That is the right starting point as regards the codes.

As regards how we have done some of the sifting, we have looked at the way those sectors are treated in EU law and how future negotiations might bear down on them. Just to be absolutely crystal clear, when I talk about the 51 sectors, it is all the sectors. It is not the 51 that are the most important or the biggest. It is an attempt to try to get this into a manageable format so that we can analyse what Brexit might mean for those particular sectors. There was a second question, which I might have missed.

Lord Wei: It was about resources.

Lord Bridges of Headley: It comes back to what Lord Price said. I am confident we have the resources but I am not complacent. That is how I would answer that. Going back to the earlier point I made about how we are approaching this, we have a very strong core team in my department and we should not forget the excellent officials in UKRep. They are analysing a lot of this material in conjunction with the experts in the various departments. We cannot and should not try to create an enormous department that sucks the life blood out of Whitehall. We need to keep expertise in those departments and draw on it as much as we can using experts of our own in the centre. I hope that answers your question.

Q63 **Lord Wei:** This may be more suitable for a written answer, but I would be very keen to know about your discussions with the various industry regulators. As more news comes out, for example about businesses not being able to contact counterparts in Europe and beyond, and as this whole picture emerges, are the regulators and bodies that have that responsibility in discussion with government about how to manage that aspect, because obviously that is one which is creating a lot of anxiety?

Lord Bridges of Headley: That is a very good question. Sitting here now, I cannot answer for the day-to-day activity of the regulators, but I am happy to come back to you. I will have to make some inquiries.

The Chairman: We have two more specific questions and we are coming up towards the time limit. Lord Horam.

Q64 **Lord Horam:** I think my question has pretty well been covered, Chairman, so I will not ask the question written here. What you have described to us today is quite encouragingly a fairly technical process, looking at the real issues of industry and trade and so forth. That is happening at your level, but we are also aware that there are political noises going off. President Hollande has said, "They must be made to pay", et cetera. How far are you confident that you are being allowed to do the important technical job that you really have to do without too much interference from the big politics aspect of it?

Lord Bridges of Headley: If you will forgive me, I am not going to comment on specific comments made by our European partners or others. All I would say is that we are absolutely resolute and determined to do this work, with due consideration to the timeframes, the need for certainty and clarity and the need for thoroughness at the same time. This is a hard-headed, cool, calm look at what the impact of various options might be. I was a journalist myself so I know how things get written up and the need for stories. I can assure you that work is continuing and the departments of Whitehall and that other agencies are really putting their shoulders into this, so it is going ahead.

Q65 **Baroness Symons of Vernham Dean:** Earlier on, Minister, you quoted either from the EU or somewhere else—I do not know which—that in relation to TTIP the outcome, i.e. what people were looking for in the negotiation, was an outcome that satisfies both sides. Those are the words that you used.

Lord Bridges of Headley: Are you talking about TTIP?

Baroness Symons of Vernham Dean: It was a quote from the document you read to us earlier. You said it was an EU document. I do not know whether it was referring to TTIP or what, but that was the rubric you gave us, because I wrote it down. It sounded quite remarkable. In the end this may be a technical question for you, following on from what Lord Horam said—and I am glad you are approaching it like that—but it is an existential issue for some of our European partners, because they think that if we are satisfied it threatens others following suit. Forgive me, but it just sounded like a touch of the Polyannas to say that in the end it was going to be able to satisfy all sides, because if it satisfies us it means that others may want to follow suit, and that is an existential issue for the European Union hierarchy.

Lord Bridges of Headley: First, the quote I referred to was in regard to the transparency question that I was being asked about on what processes we will follow.

Baroness Symons of Vernham Dean: No, it was not the process; it was the outcome that you referred to.

Lord Bridges of Headley: The outcome we are after is the best possible deal for the United Kingdom, and that is where we are intending to get to. As Lord Horam said, there are lots of noises on and off about how others across Europe might respond to this. Of course we are mindful of those kinds of points, but we have to do this analysis to start off with to ensure that we are working on the best possible strategy for the negotiations.

Q66 **Lord Green of Hurstpierpoint:** Building on Lord Horam's question in a slightly different way, you have reassured us, I think it would be fair to say, about the focused technical and detailed nature of the work being done in the UK. Do you have a sense that there is an equal and opposite amount of very detailed and specific technical thought going on in the key Member States and in Brussels or not?

Lord Bridges of Headley: I would be misleading you if I gave you a precise yes or no answer on that. Clearly we know that a team is being assembled in the Commission, and quite a considerable team. I could not comment, to be absolutely honest Lord Green, on what is going on in each Member State. Certain Member States are focusing on this a lot more than others, but when I say that I would not be able to give you a clarification now as to exactly how many people are working on this in each Member State. I think that some are very focused on this, as you would expect.

The Chairman: The politics of it require us to have a pretty clear idea where our soon-to-be former partners in Europe are actually standing. That effort is rather vital. Can we go on to the final formal question from Baroness Donaghy?

Q67 **Baroness Donaghy:** As you know, the Prime Minister at the Conservative Party conference mentioned possible new free trade agreements between the UK and third countries outside the EU. She ticked off a number of countries in her speech. In addition, the Rt Hon Liam Fox spoke of a "post-geography trading world", the meaning of which I do not understand, I must admit. What is the Government's assessment of the impact of losing access to existing EU free trade agreements? Will the Government be seeking to access them as a third party? Secondly, are the Government seeking to replace trade currently undertaken with the EU through new FTAs with non-EU countries? In this case, would the priority countries be the same as named by the Prime Minister?

Lord Price: At the moment, around 11%[14] of UK exports go to countries with which the EU has an FTA. There are a number of FTAs currently being negotiated by the EU; you will be aware of those with Canada, the USA and Japan. If those FTAs nearest completion or awaiting ratification were signed before we were to leave the EU, that would be another 25%[15] of UK exports. We are aware of the quantum and scale of exports that happen through those FTAs. As the Prime Minister has said, we want to

[14] Figure corrected by witness
[15] Figure corrected by witness

make sure that we have the best possible transition from where we are today to the new world, and part of our responsibility in DIT is to look at what we might do with those countries that currently have an FTA with the EU, to see how we might have some kind of transition to make operations smooth for business. On my and the Secretary of State's trips around the world, we are talking to businesses and Governments about how we might mitigate the impact of that going forward. It is part of our thinking.

The Chairman: Thank you very much indeed. Your earlier responses indicated the constraints you were under and the limits to which you could say certain things. Could I give you an opportunity in reverse to say anything you feel you wanted to register with us which questions have not really allowed you to?

Lord Bridges of Headley: No. All I would like to say is it is a welcome opportunity to come here. I have registered the concerns that people have raised on various points and I hope that you do not read into my answers, if they struck you as evasive, that we are not very much focused on the issues. I wanted to say that once again for the record. Thank you very much.

The Chairman: We have been told that we are not getting a ball-by-ball commentary, but you have played a fairly straight bat to some of these questions and you have also been very informative on others. We owe you a debt of thanks in that regard. We will be calling you back and, as I say, in this whole lengthy and as yet undefined process, without a ball-by-ball commentary we sometimes need to know the score at lunchtime. We would hope that at the key stages there will be some sort of report back both to us and to our equivalents in the Commons. I hope that is the Government's intention and we will certainly be pressing you if it is not. On that note, thank you very much and thank you to your officials for backing you up. We will see you again.

Lord Bridges of Headley MBE, Parliamentary Under-Secretary of State, Department for Exiting the EU (DExEU), and Lord Price CVO, Minister of State for Trade Policy, Department for International Trade (DIT) – Supplementary written evidence (ETG0013)

Thank you for inviting us to attend the joint EU External Affairs and Internal Markets sub-committee on the 13th October to submit evidence on your inquiry in relation to *Brexit: future trade between the UK and the EU*. At the session we agreed to provide further information raised by the Committee at the meeting and also on two points raised subsequently.

Firstly, to address the point raised by Lord Wei about discussions with various industry regulators: DExEU Ministers are working closely with their colleagues across Government to ensure that we are all speaking to every sector, from small family businesses to multinational companies and trade bodies, as well as industry regulators.

The Government meets with regulators regularly and this engagement has continued since the referendum. The decision to leave the EU has of course featured in our recent discussions.

Bodies that Ministers and officials have met with in recent months include:

- British Standards Institute
- Competition and Markets Authority
- Food Standards Agency
- Health and Safety Executive
- OFGEM

Details of Ministerial meetings will be published in the Department's Quarterly Transparency Returns, which will be made publicly available on gov.uk.
The Committee were also keen to understand about the nationality rules in relation to the recruitment of advisors and staff; and, in addition, the LSE story on foreign academics and restrictions on the appointment of non-British trade negotiators. As the Government has made clear, it is categorically wrong to suggest that the FCO would not work with non-British nationals, including EU nationals. The FCO regularly works with academic institutions to assist in its research and training; nothing has changed as a result of the referendum. The FCO has been in touch with the LSE to clarify the situation, and the LSE has acknowledged that clarification.

This same principle is true for DIT. The department has not reserved any posts for UK nationals in DIT recruitments to date, including the searches for Chief Economist, Permanent Secretary or Director of Communications. The Secretary of State for International Trade announced on 8 September that the recruitment for a new Permanent Secretary would be a global search for the best possible candidate. We will continue to hire the brightest and best talent from within the

UK civil service and from elsewhere in order to deliver the best trade outcomes for the UK.

The Committee has subsequently requested information on the number of staff DExEU expects to be in place by the end of 2016 and when it expects to be at full strength. All departments are equipping themselves with the resources they need to get the best deal for the UK. DExEU now has over 250 staff. We are not in a position to give a final total for particular groups of staff as recruitment is ongoing. Our aim is to have a streamlined Department, while hiring in the right skills and experience to get the best outcome for the UK.

Turning to Lord Wei's point about how the 51 market access sectors had been selected. We have set out publicly that we are considering the impact of leaving the European Union on 51 sectors and areas of cross-cutting regulation, and I (Lord Bridges) undertook to explain how we have arrived at the sectoral breakdown we are using.

We have structured our approach by sector because it is a robust way of breaking down the economy into units, which lend themselves readily to analysis. These 51 sectors were chosen so as to break economic activity down into the lowest levels at which they had reasonably common relationships with the EU regulatory framework. In addition, we took into account the way that the Office for National Statistics records economic activity. We are using these categories to develop a rigorous understanding of the size and contribution of sectors to the economy, and use that to support our analysis of the impact on them of leaving the EU.

Lastly, in relation to how information from business can be fed into the departments, we recognise the importance of making it easy for colleagues in both Houses to share this information with us and be confident that it is reaching the right people. Our stakeholder engagement teams work closely with colleagues across Whitehall to ensure that information from business and other organisations is passed to the right policy teams in DExEU, DIT, and across Government. Parliamentarians can contact the DExEU stakeholder engagement team at stakeholder.engagement@dexeu.gov.uk and the DIT stakeholder engagement team at trade.consultation@trade.gsi.gov.uk.

Please do let us know if there is anything further we can help you with.

9 November 2016

Andrew Duff, Visiting Fellow, European Policy Centre – Written evidence (ETG0014)

MEMORANDUM OF EVIDENCE TO THE HOUSE OF LORDS EUROPEAN UNION EXTERNAL AFFAIRS AND INTERNAL MARKET SUB-COMMITTEES BY MR ANDREW DUFF: EU ASSOCIATION AGREEMENTS

I will argue that, following Brexit, the best mutual arrangement for the United Kingdom and the European Union is to negotiate an association agreement. As far as the EU is concerned, an association agreement with its former member state would be neat, relatively straightforward to negotiate, and consistent with its treaty commitment to "develop a special relationship with neighbouring countries, aiming to establish an area of prosperity and good neighbourliness".[16] Early acceptance that an association agreement is to be the final destination for the UK will greatly ease the negotiation of the Article 50 withdrawal agreement (which should take into account the framework for the future relationship). As far as the UK is concerned, an association agreement with EU 27 would reflect the verdict of the referendum that the country should leave the EU. It would not presage re-accession. It would avoid falling into the embrace of WTO. In the hierarchy, an association agreement would leave the UK less engaged with the EU than Norway but more so than Canada (and tidier than Switzerland).

A useful template, which creates a precedent, is the recent EU Ukraine Association Agreement.[17] At the heart of that agreement is a deep and comprehensive free trade area (DCFTA). If Ukraine respects three of the four principles of freedom of movement, it will enjoy tariff free access for goods, cooperation on VAT and customs procedures (including the complex rules of origin), trade remedies, mutual recognition of equivalent technical standards and joint observance of EU policies on public procurement, competition, state aids and intellectual property. Under the framework provided by the association agreement, Ukraine can elect to deepen its economic cooperation in services (including passporting for the financial industry), as well as transport, energy, employment, consumer protection, environment and climate change policies. Ukraine can choose to buy its participation into EU common programmes such as Horizon 2020 as well as to join EU agencies such as Europol and the European Food Safety Authority. The movement of labour is subject to work permits against the backdrop of visa liberalisation.

The Ukrainian DCFTA is more flexible and allows for a wider scope of trade relationship with the EU than the Canadian CETA. Just how deep the UK wishes its commercial engagement with the EU to be will only become clear once the job of filleting the corpus of EU law begins at Westminster. The closer the UK maintains its conformity with the acquis, sector by sector, the greater will be the capacity of British business to operate across the single market. One might assume, for example, that the UK would elect to retain its observance of the

[16] Article 8 TEU. Article 217 TFEU provides the specific legal basis for an association agreement. Article 218 lays down the negotiating procedure.
[17] Official Journal L 161, 29-05-14.

2006 Services Directive (and its successors) while ditching its participation in the common agriculture and fisheries policies. In so far as the UK keeps up its current standards of technical and regulatory equivalence with the acquis, in the most sensitive sector of financial services the DCFTA will protect the utility of the City of London for eurozone and non-eurozone players.

While Ukraine, unlike Turkey, is not a member of the EU's customs union, such membership could in theory be added to a DCFTA. Continuing membership of the customs union would minimise disruption to business and travellers, and greatly help the situation at the UK's land borders with Ireland and Spain. It would also lower the necessity of embarking on separate trade negotiations with dozens of third countries.

On top of the DCFTA struck with Ukraine are very important provisions for future political cooperation in the field of justice and home affairs as well as foreign, security and defence policies (including CSDP missions). The former should prove attractive to ex-Home Secretary Theresa May. The latter might prove to be invaluable to the UK as, along with the rest of Europe, it adapts to President Trump – and, for that matter, President Putin.

An association agreement on the Ukrainian model would include useful institutional machinery of an intergovernmental not supranational type. This comprises an annual summit meeting, a ministerial council, technical committees and a joint parliamentary body between Westminster and the European Parliament. Procedures would be in place for updating the bulky technical annexes of the DCFTA in order to manage divergences between the EU and UK as and when they arise. There would be a judicial process to arbiter disputes. The Ukrainian agreement has a tribunal of three (including one 'neutral' judge): the role of the European Court of Justice is vital though discreet.

While it is not a question of 'cut and paste', the Ukraine association agreement offers an expedient model for the UK as it struggles with Brexit. For EU 27 the Ukrainian deal provides a precedent which it would be difficult to deny its former member state. All being well, a UK EU association agreement could be negotiated fairly quickly and enter into force provisionally before all member states had ratified it – thereby limiting the duration of an interim arrangement negotiated under Article 50.

19 November 2016

Professor Piet Eeckhout, Professor of EU Law, University College London, and Richard Eglin, Senior Trade Policy Adviser, White and Case LLP – Oral evidence (QQ 1-10)

Evidence Session No. 1 Heard in Public Questions 1 – 10

Thursday 8 September 2016

Watch the meeting

Members present (External Affairs Sub-Committee): Rt Hon the Baroness Armstrong of Hill Top (Chairman)[18]; Lord Balfe; Lord Dubs; Lord Risby; Lord Stirrup KG GCB AFC; Baroness Suttie; Baroness Symons of Vernham Dean; Lord Triesman

Members present (Internal Market Sub-Committee): Lord Whitty (Chairman); Lord Aberdare; Baroness Donaghy; Lord German; Lord Green of Hurstpierpoint; Lord Lansley; Lord Liddle; Lord Mawson; Baroness Noakes; Baroness Randerson; Lord Rees of Ludlow; Lord Wei

Examination of witnesses

Professor Piet Eeckhout and Mr Richard Eglin.

Lord Whitty took the Chair

Q68 **The Chairman:** We have an array of legislators and a wide range of questions. This is a public session. Therefore, there will be a record, it will be transcribed and you will have sight of it, but we need to bear that in mind in anything we say. We have invited you to contribute your expertise to try to clarify to our two Committees the situation we now face, in dealing both with the WTO and with wider trade organisations. We are focusing in particular on the WTO. I will start with an opening question, but if you wish to elaborate on general points, please use that question so to do.

Our understanding is that we as the UK will have to renegotiate the terms of our WTO membership upon exit from the EU at whatever point that takes place. Some people say that is pretty much the same as being a new entrant into the WTO. Could you give us your views on what we will be faced with, how difficult it would be, how long it would be likely to take, which parts of our current arrangements with the EU we could carry over and which we could not under WTO rules, and the implications

[18] Baroness Armstrong of Hill Top was chairing in place of Baroness Morris of Bolton, who was unable to attend the meeting.

thereof? I would like both of you to reply to that and give your views. Who wants to start?

Professor Piet Eeckhout: Seniority?

Mr Richard Eglin: Seniority meaning that I am older not wiser. I think there is a basic misunderstanding in what you have just said, Lord Chairman. The United Kingdom is withdrawing from the European Union. It is not withdrawing from the WTO. It was an original member of the GATT in 1947, it was an original member of the WTO in 1995, and it fulfils in my view—I cannot really see any other view to hold—the two conditions that are necessary to be a member of the WTO. One of those is that it has ratified the WTO agreement, and the second is that it has market access schedules, one for goods and one for services. It undoubtedly has those; they are the EU schedules at the moment.

The job ahead of us is to extract our schedule from the EU schedule and present it to WTO members. We can go into detail, but I would suggest it as a rectification of the schedule, not as a modification. On a best-case scenario, it could take three months in the case of the goods schedule and 45 days in the case of the services schedule. Those are the procedures. In the best of circumstances, where nobody objects, we extract our schedules and present them to WTO members. We keep the initiative. We make the presentation so that they have to react, and if nobody reacts, within three months in the case of goods and 45 days in the case of services, the schedules are approved and certified. That is the best-case scenario. I do not doubt that there will have to be a negotiation of some sort, but we do not have to renegotiate our membership. We need perhaps to renegotiate our schedules.

The Chairman: Thank you very much. That is very clear.

Professor Piet Eeckhout: I agree with that, to the extent, of course, that the United Kingdom Government are happy to continue to apply the current commitments of the European Union as to tariff schedules and services commitments. If the United Kingdom were to choose a different trade regime on the tariff side, it would involve a modification of the current tariffs and we would no longer be in the territory of simply transitioning from EU tariffs applying as EU tariffs to a position where the United Kingdom was applying those same tariffs. There is a political question to be decided that determines the extent to which those negotiations might be straightforward or rather more difficult.

There are a couple of further but more technical points to which attention could be drawn in the scenario that the United Kingdom were to adopt the EU schedules for goods and services. There is an issue potentially of tariff quotas in the framework for agricultural goods in particular, in the sense that the EU has tariff import quotas, which are the amounts of goods that come into the country under a particular tariff—for example, bananas, which in the past have given rise to many difficulties; crafting an EU trade regime on bananas—and precisely how they would be divided up between the European Union and the United Kingdom, and whether they would be divided up.

Similar questions may arise in relation to the European Union's current export tariff quotas. Other WTO members have tariff quotas on exports from the European Union. Would those be divided between the EU, or would the European Union keep those quotas and would the United Kingdom have to negotiate preferential access itself? Those are uncertainties, I think. On subsidies in agriculture, where the commitments are about the aggregate measurement of support, which is currently not a big issue because the European Union ceiling is very much above the current actual subsidies, the UK commitments would have to be determined. The agreement on government procurement is also one where potentially the United Kingdom would have to negotiate its entry, because it is not an agreement that the United Kingdom has concluded. It is a plurilateral agreement. It is not part of the overall package of WTO agreements. Not all WTO members have signed up to it. As I understand it, the European Union has signed and concluded it, not the individual Member States of the European Union. In contrast with general WTO membership, where both the EU and the individual Member States are members, that is not the case with the government procurement agreement, so potentially there would need to be a negotiation.

I noted another couple of points, but they are related as much to the relationship between the European Union and the United Kingdom post-Brexit as to the WTO position. I am uncertain what would happen, for example, with the current antidumping measures that the European Union applies to imports from other WTO members, which have been the consequence of an EU-wide investigation into dumping. Lots of those currently apply, particularly to China. Whether the United Kingdom could simply continue to apply those or would not apply them may also be an issue that comes up in defining the UK's WTO status.

The Chairman: Thank you. I think you have pre-empted part of Lord Wei's question, but we could perhaps generalise and ask how much is dependent.

Q69 **Lord Wei:** What do you see as the most contentious points or obstacles to the renegotiation or rectification of WTO membership terms? What elements of that renegotiation would be contingent on the nature of the UK-EU relationship?

Mr Richard Eglin: I do not think that 'contentious' is quite the right word. Parts of it will need to be renegotiated. For the market access schedules, the bulk of the goods schedule and, in my view, all the services schedule can simply be extracted and laid on the table as the UK's schedule. That again is assuming that we are not going to change it—I agree with Piet—and that we simply want to replicate what we already have as an MFN schedule. The parts that will need to be renegotiated are the tariff rate quotas and farm subsidies—the quantitative elements of those schedules—where we will need to reach a deal with the EU on how they are shared out. On the face of it, the EU presumably will want to give us as much of the tariff rate quotas as possible and as little of the farm subsidies as possible. That needs to be

sorted out, and it would have to be done before we could complete our schedule and present it in the WTO to other WTO members.

We have to reach agreement first with the EU. Having presented the schedule, I am sure other WTO members will see opportunities, particularly in agriculture, to look for better access to the UK market, and it will be up to us, or the UK Government, to decide whether they continue to insist on rectification, whether they are prepared to negotiate. My advice would be certainly to show openness, to listen to anybody who comes to us and says that they want bigger access for their beef, butter, milk or whatever it might be. That is the key part of the negotiation on market access. There may be other specific tariff lines. I can imagine a situation where another WTO member would say, "When I negotiated this concession with the EU in 1995 it was on the presumption that the UK was part of the EU market. Therefore, I gave a lot to get this access and now the UK on its own does not offer me that kind of reciprocal benefit". They may say they want to negotiate on something. You cannot predict at the moment how that would work, but there may be individual tariff lines. It is a matter of negotiation. I am not sure it is contentious.

On the government procurement agreement, I agree. Very honestly, I think that the UK will have to accede as a member, but that can all be done. It is not contingent upon us having first reached agreement with the EU. We could work that out. Most of the work in the WTO, most of the negotiation, is informal. Therefore, we should start to talk to the five, six, seven or eight key members, other members who are first of all decision-takers in the WTO and who are major trading partners, and work it out with them. Again, there are the rules, to go back to the Chairman's original question of how long it takes: after the United Kingdom has ratified a new government procurement agreement, it takes 30 days before it enters into force, so we are not looking at a great gap.

Lord Wei: Just to clarify, what you are saying seems to be counter to popular conception, and, to simplify, if we cut and paste much of what is already there into the WTO discussion, we can start with that as a baseline and work from there.

Mr Richard Eglin: Absolutely.

Lord Wei: How much of the sequencing of the discussion is contingent upon our negotiation with the EU?

Mr Richard Eglin: Very little of it. As I said, the only part is sharing out the quotas. We need to extract our schedules from the common EU schedule. Part of the common EU schedule is quantitative—the limitations on how much butter gets into the EU at what tariff rate. That was set at EU level; it was not negotiated member by member. The members of the EU and the UK need to decide who gets what, and how much gets taken over by the UK. That has to be done before we can present a completed schedule to the rest of the WTO members. There is nothing to stop us informally starting to talk to other members without a completed schedule. Before anything could be done formally, we would need to have presented a full schedule. If the EU is not going to object, that would have to include whatever agreement we reach with the EU on farm subsidies

and tariff rate quotas, but only that part, as far as I can see. If we are not going to change anything else, I do not see why there should be anything contentious in the rest of it. The government procurement agreement will need to be renegotiated. Again, I do not think that is a big problem.

Piet said, and I agree, that one major issue is going to be re-establishing in the UK an investigating authority that is capable of undertaking trade remedy investigations and protecting the UK's interests in any trade remedy measures that are taken against the UK. That, to my mind, is the biggest problem, but it is a capacity-building problem, not a negotiating problem. We do not have to agree on that with the rest of the WTO membership. There are WTO rules. Our investigating authority has to be set up and obey those rules—to be in conformity with those rules. Then the question is whether, if we have, as I think we do at the moment, antidumping duties in place from the EU on Chinese steel, we try to take them over and continue to apply them. If I were the Chinese, I would object vigorously if the UK tried to do that. I would say, "No, you have to carry out a new investigation and demonstrate domestic injury and unfair trade. Until you have done that, I will challenge any trade remedy measure". Those are important measures for the steel industry and so on. Frankly, getting that done in two years is not too long a time. There is a lot to be done to put that in place, and I would say that although it is not contentious it is probably the most difficult thing facing the UK at the moment.

Professor Piet Eeckhout: Can I add something on what might be contentious and how it relates to the EU-UK relationship? There may be some political dependency as to how the other WTO members look at the UK's position in adopting the EU schedule, in the sense that it makes a massive difference whether the United Kingdom remains in a customs union with the European Union, where you would continue to have one external tariff applying; whether there is a free trade agreement between the United Kingdom and the European Union, in which case there will be rules of origin that determine which goods produced in the United Kingdom have access free of tariffs to the EU internal market; or whether trade will initially be between the European Union and the United Kingdom on WTO terms. Richard has a lot more expertise inside the WTO and can perhaps express a view on that. I am uncertain about the extent to which other WTO members may just take the position: "Before we start looking in the WTO at the UK's schedule, we want to know how UK-EU trade will be conducted and what the terms of trade will be". I guess to the extent that the future may be one of trading between the United Kingdom and the European Union on WTO terms, there will be one party, one member of the WTO, for whom the tariffs in the UK will be new: the European Union, which of course currently exports to the UK in the context of the internal market, and you would have new tariffs. That again would depend on how the negotiations between the EU and the UK run. We have seen, for example, the position paper by the Japanese government on Brexit, which has drawn attention to the fact that Japanese companies have invested in the United Kingdom from the perspective of access to the internal market, and that for a number of companies the terms of trade between the United Kingdom and the EU

are terribly important. To what extent that might affect discussions about the new UK schedule in the WTO, I do not know, but it could give rise to problems.

The Chairman: You have pre-empted parts of Lord Green's question.

Q70 **Lord Green of Hurstpierpoint:** Yes, indeed. I would like to explore, particularly with Mr Eglin, your views on what would happen if there is an objection or a set of objections when we table a new set of market access schedules. I have dealt with the WTO. It works largely by consensus and what happens is all very unclear. Usually it is a matter of the proverbial smoke-filled rooms when there is a disagreement. What is the probability of serious objections to the UK tabling a market access schedule, assuming it is basically cut and paste, and how do you see that being resolved?

Mr Richard Eglin: I do not think there are any serious objections. If I were doing it, I would put the schedule on the table. First, I would talk informally to other key players. The reality is that the bulk of the WTO membership will have no problem, or possibly any interest, in what is going on here, but there will be 10 or 12 other key players, and I would first deal with them informally. You do not make objections in an informal setting, so it is not a question of objections being raised. They may well say, "Well, very interesting. I see that you have the same or similar market access schedules to the ones you had before with the EU, but I would like to talk to you about this, that or the other part of it", and the UK should say, "Absolutely, with pleasure". Our proposal, as a schedule, is the terms on which we continue to trade regardless of whether it has been certified or not—that is our MFN schedule—and nobody is going to object to that. They may ask for renegotiation of parts of that schedule and for additional concessions. That, to me, is an opening for free trade agreement negotiations, not so much a question of trying to sort it out in the WTO. If they do, we should willingly go ahead and say, "Yes, of course, we will come to one of the famous smoke-filled rooms and talk about it. We will see what you want and what we want and go from there". It is a matter of negotiation.

The important thing in the WTO is that it works from consensus. You are right. There are fine points of law that I am sure one can draw out and say, "Ah, but this means that we do not have this, so you will have to re-accede to the WTO". It does not work like that. The WTO is a commercial contract. It is there for the benefit of all members' businesses. Chaos would break out if anybody were to suggest that the UK does not have a schedule and therefore they will not trade with the UK. It would be absolute pandemonium. It is not going to happen. The reality is that it is a matter of negotiation. It could take years before the schedule is actually certified by consensus, as you say, but in that period we would continue to trade on the terms in which we proposed we should trade, as long as they were reasonable. We cannot come out and slap on restrictions all over the place, put it on the table and then say, "Okay, we are going to restrict all your imports but we expect to be able to access your markets".

You cannot do that. As long as it is reasonable, I see no problem whatever.

Lord Green of Hurstpierpoint: That is very helpful.

The Chairman: You have made it sound a little easier than perhaps we came into this room thinking it would be. Nevertheless, Lord Stirrup is going to ask if there are difficulties.

Q71 **Lord Stirrup:** Yes. You started to address the problem, Mr Eglin. Let me postulate the situation where we have triggered Article 50, the two years have expired and they have not been extended, so we are out of the EU but, for some reason or another, we do not have a ratified schedule. If I understand you correctly, you have just said that is okay because we just continue with what we laid on the table and people continue to work at all the issues. First of all, is that a correct interpretation of what you said? Secondly, if I can expand it a little, as the Chairman said, you have made this sound rather straightforward and easy, and you do not foresee any significant road bumps. The press are, I think, sounding a little more cautious. Could I explore a little more deeply what sort of issues could derail the process? You said, "provided that we do not want to change anything", but what if we do want to change things? Are we likely to want to change things, what might they be, what effect would that have and how would that impact on the period between leaving the EU and getting final ratification?

Mr Richard Eglin: The answer to the question is yes. If, after the two-year period expires, there is no agreement with the EU and we have not had our schedule—we may not even have presented it formally—and had it certified, is that possible? Yes, it is possible. Does it pose a problem? In my view, no, none whatsoever. We continue to trade at that point on MFN terms with the rest of the world under WTO rules. We have uncertified schedules of goods and services. There may be some unhappiness and there may be some difficulties. There always are in the WTO. There is always some friction, which is all to the good. As long as we address that in an open way and are willing to discuss with other members the problems they foresee and to take into consideration their concerns—if they think they really have been dealt an injustice and we can see what they are on about—we should talk to them and negotiate with them. What was the second part of the question?

Lord Stirrup: Suppose we want to change things.

Mr Richard Eglin: If we want to liberalise, there is no problem whatsoever; we can simply go ahead and do it. Nobody would object in the WTO. The WTO is a commercial contract and it is based on reciprocal concessions. If I want to increase restrictions, and I believe I have a balance at the moment of reciprocal concessions with the EU and the UK splits off, I will look at it and ask whether that balance still holds. If I reach the conclusion that, no, it does not, I will want to talk to you and negotiate with you and find how we can redress the imbalance that I perceive. You may say there is no imbalance. It is a negotiation. It is not a legal matter. A lot of it is in the eye of the beholder. Trade remedies—antidumping—are a different question, but if we intend to introduce

greater restrictions in the schedules, we will have to offer to negotiate, under Article XXVIII of the GATT and Article XXI of the GATS, with any other member that says their interests have been damaged by what we have done. We need to think about it carefully, but that does not mean you should not do it. Maybe we should. Maybe we are better off raising a tariff. By the way, the exchange would be that you would have to lower a tariff somewhere else. It is not a question of monetary compensation; it is a question of reciprocal bargaining to establish the basis on which we trade with each other. If we are prepared to raise a tariff here and lower one there, that is the game.

The Chairman: Lord Aberdare, do you think your question has been already answered, or is there a point that you wish to pursue?

Q72 **Lord Aberdare:** I think it probably has been answered. I was going to ask what would happen if we wanted to raise, in particular, or lower tariffs, and you have just answered that. If we wanted to retain the EU's external tariffs, presumably no negotiation would be needed.

Mr Richard Eglin: Let us assume that we want to. We are going to have problems with the quantitative element of those schedules. We will have to sort them out with the EU first. Otherwise, there is nothing in the WTO rules that says you cannot adopt somebody else's schedule. That is our schedule. It is the schedule upon which we trade today. It is a pretty good schedule. The US and Japan trade on that basis with the EU all the time.

One of you said that I was making it sound easy. I do not want to make it sound easy. A good deal of negotiation is going to be involved—probably clever negotiation as well, in parts—but the world is not going to end. Nothing is going to happen if the two-year deadline passes, or we have presented schedules and they have not been certified. It does not work like that. People want to continue to trade with each other and they will continue to do so.

Lord Aberdare: Could I ask a supplementary question on whether we have the skills needed to undertake those kinds of negotiations? You mentioned the issue of the investigating authority. Could you say a little more about the realities of being in a position to undertake those kinds of negotiations at the level required?

The Chairman: Lord Liddle also has a supplementary, so you can wrap them all up.

Lord Liddle: In my very simple reading of all this—tell me where I am wrong—I thought that if we wanted to have FTAs with other countries outside the EU, we had to come out of the customs union. Does that not mean, therefore, that we can no longer certify the EU's tariffs and be part of that?

Mr Richard Eglin: We cannot negotiate FTAs with anybody at the moment and for as long as we remain a member of the EU. Once we have withdrawn from the EU, we can negotiate FTAs with whoever we want.

Lord Liddle: That means coming out of the EU's customs union.

Mr Richard Eglin: Yes.

Professor Piet Eeckhout: It does not necessarily mean that, because the European Union currently has a customs union with Turkey, and Turkey is very much encouraged to conclude free trade agreements with the countries with which the EU concludes free trade agreements. There is no complete match. Turkey continues to conclude its own free trade agreements with other countries around the world. That is another model, even with a customs union.

Mr Richard Eglin: But that is bringing us back to the customs union, is it not? We would have to get out of the EU.

Professor Piet Eeckhout: Yes. Essentially, of course, for a free trade negotiation the other parties will want to see what the baseline is, what the UK's tariff commitments are under WTO law, because that is the baseline from which you negotiate a free trade agreement. Conceptually, that needs to be sequenced. Whether it necessarily needs to be sequenced in time is a different matter. One of the difficulties is how concurrent it all is; the WTO talks need to be concurrent with the negotiations with the European Union on the future relationship. That may be a particular difficulty.

The Chairman: Moving further down the line, Baroness Randerson has a very specific question, and I think Lord German wants to come in as well.

Q73 **Baroness Randerson:** Professor, in your blog post on Brexit and trade you made the point that radically cutting tariffs would put the UK in a weak position, because the UK would have nothing to offer in relation to future negotiations on FTAs. Given that we already have a relatively open market, what do you see as the UK's main leverage in negotiations?

Professor Piet Eeckhout: On the assumption that the United Kingdom keeps the current EU schedule, which, as you say, is already fairly liberal, definitely in the field of industrial goods and services, I think the UK is an attractive market, but of course it is not as big a market as that of the European Union, so it would be in a comparable position to the European Union in its free trade negotiations but with a smaller market to offer to others. That in itself does not preclude any negotiations.

The other point I would like to add, which is the wider question of how international trade policy develops, is that we have seen a tendency in recent years for mega-regional free trade agreements, the Trans-Pacific Partnership (TPP) and the Transatlantic Trade and Investment Partnership (TTIP). There is a big question mark as to whether they are going to be successful or not, but there is certainly a lot of emphasis in the EU's trade policy, and in its policy to conclude free trade agreements, on focusing on regulatory issues and not so much on tariffs. Of course, there are many regulatory issues that the EU includes in its free trade negotiations, and convergence on regulatory issues or even attempts to be hegemonic and trying to persuade other countries around the world to adopt concepts of EU regulation. Many parts of that are EU law and EU regulation, and we do not know at this point how the United Kingdom will regulate its economy independently from the European Union. That also, to some degree, may reduce the attraction of concluding free trade agreements with the UK. On the other hand, it may make it easier if the UK is not a

big demandeur at the level of regulation simply to have free trade agreements that are focused on removing tariffs and do not achieve much else. The size of the market is definitely a big determinant in how attractive you are as a party in potential future negotiations.

The Chairman: Before we leave this, I am not sure I heard a clear answer to Lord Aberdare's question about resources and how well placed we are to negotiate ourselves through this complexity.

Mr Richard Eglin: I will deal with it with pleasure. Could I add one comment on the answer to the last question? I agree. I do not think that tariffs are really the focus of modern free trade agreements. Conformity assessment, technical regulations, regulations in general, intellectual property rights and geographical indications are the sort of things that are at the heart of TTIP, the Canada-EU agreement and other major FTAs or plurilateral agreements around the world. There is some bargaining part; you should not give it away for free. A trade negotiator will pick your pocket for anything he can get out of it, but do not give it away for free. On the other hand, one should not worry about keeping the bound rate at 4%—reducing the applied rate to zero but saying "I can put the bound rate up to 4% if I want to". That is the beginning of the negotiation, not zero.

The question on capacity is a good one. I do not know well enough the capacity of the UK Government—I must say that from the beginning—and I am sure there are plenty of clever people around who can do it. To explain what I think is needed, the UK will need to resource an investigating authority for trade remedies. That is specialised work. The UK will need trade negotiators, trade analysts and statisticians and trade diplomats with a general background, but there will also need to be expertise in certain areas: one is dispute settlement, another is intellectual property and another is certain parts of services. Those are specialised areas. You tend to find that people specialise in those particular areas through their career. We will need to get up to speed rather quickly on that. Dispute settlement lawyers do not grow on trees. We have plenty of good lawyers, I am sure, but whoever is doing it will need to go back and will need to know the last 20 years of dispute settlement cases in the WTO, and you do not learn that overnight; you do not pick it up that quickly. There is probably a big capacity gap, because we have not been doing this for so many years. I am sure it can be made up—we are not short of clever people—but there will need to be some rather targeted capacity-building, particularly in the investigating authority for trade remedies.

More important to me than capacity is joining it all up. If you are going to negotiate, the negotiator needs to be in the WTO armed with a set of instructions that represent government policy. In the WTO you are covering almost every ministry, every department of government. It will need to have been sorted out with agriculture, with the technical regulation people, the veterinary people and customs and so on. It all needs to have been brought together in the first place before instructions can be given to the negotiators. Clear instructions are absolutely paramount to being able to negotiate cleverly or properly. There needs to

be a big effort, and with business of course, to find out whether certain parts of business need an increase in a tariff or whether we can live without the tariff rate quotas on this, that or the other. It needs to involve farmers. It all needs to be worked out very carefully beforehand. The capacity is not just people and specialists; the capacity to negotiate is more than that.

The Chairman: In that context, we have two questions about the impact on different sectors.

Q74 **Lord Risby:** If we turn to the services sector, which is so crucial to the economy of this country—almost dominant in many ways—a number of things arise. The first is to preserve the success of the services sector. There was criticism anyway about our ability to protect our full range of service industries in the Single Market as such. Secondly, of course, there is now real concern, at least among people running organisations in the services industry, that parts of it may need to be hived off to protect their bottom line. For us, the whole area of services is absolutely crucial. It would be very helpful for the Committee to understand and have a qualitative assessment of how you think that might work in the context of WTO rules and of the European Union, because this is going to be a very serious matter for us to have to deal with.

Professor Piet Eeckhout: I am not sure that I am capable of giving answers across a different range of service sectors as to what the potential impact might be of not being in the internal market with the European Union and being subject to WTO schedules. In any event, the GATS agreement has liberalisation schedules that I think it would be really very straightforward for the UK simply to extricate from the EU schedule, because in fact their restrictions are indicated per member state, so it is clear which ones apply to the UK. In 1995, when the WTO was created, that was the current state of restrictions on international trade and services in nearly all sectors. The schedules in themselves were not a major liberalising force. It was good to have in 1995 a new agreement worldwide on trade and services, but the commitments did not go further than the current state of domestic liberalisation. It varies from sector to sector, but access to the internal market is qualitatively very different. There are issues with the extent to which the internal market covers services. There are services that are less liberalised and there are some that are more liberalised, but there is a huge difference. I will take one example of the sectors mentioned in the questions—aviation. Aviation is hardly touched upon by WTO commitments. There are no commitments, basically, on rights to fly from one WTO member to another, whereas currently, with membership of the European Union, you have a full Single Market in aviation, and any EU airline, wherever it is established—in this country or anywhere else—can perform freely any flights across the European internal market. That is a huge contrast.

In financial services—passporting—on the WTO side, there is not much at all on liberalisation and there are, of course, further attempts: the TiSA negotiations are under way and many of the FTA negotiations also cover services, but we would have to see the extent to which the United

Kingdom was able to take part in that. It really requires detailed analysis sector by sector as to what the level of access to the EU market currently is and what the baseline of WTO commitments would be. That may be different, but there is definitely a lot more liberalisation within the European internal market than is the case with WTO rules.

Mr Richard Eglin: I agree. We will be inferior if we are trading on WTO terms, MFN terms, with the EU, there is no question about it, both for goods and services. I agree, too, that it will vary by service. You cannot just say in a global sense, "It will be this". Professional services are very important for the UK, and relatively liberal within Europe. Europe is no longer fortress Europe, as I think it was 10, 15 or 20 years ago. There has been a great deal of liberalisation. Certain sectors are relatively open, others are relatively closed, and there will need to be a calculation. That is where government officials need to talk to business and find out which services are affected, the main restrictions that will face the service suppliers and how they can be overcome. It may involve not simply working from London and flying over and delivering services wherever, but instead investing in Europe to set up local offices. It may require a change in the way services are delivered, but all those things need to be calculated at a very detailed level. Before you go into the negotiation, you need to have done that homework, to know exactly what you want, what the fallback position is and where the red lines are—the sorts of things that you should not do.

The one piece of advice I would give is this. As Piet mentioned, at the moment the EU is negotiating with about 20 other major countries the Trade in Services agreement—the TiSA. Of all the big negotiations around the world, this looks as if it has more legs than the others—the TTIP, for example. It is a piece of narrow advice really: the UK should make sure that, if and when the TiSA is concluded, the EU Commission does not sign it but the Member States each sign it, and then the UK is a member of the TiSA. Whether the other TiSA participants would allow the UK to become an independent, separate member of the TiSA would need to be sorted out, but I cannot see any particular objection to it if the UK is prepared to undertake it. We need to make sure that the UK signs the thing and that it is not done by Brussels.

The Chairman: I have taken that point. Lord Dubs.

Q75 **Lord Dubs:** My question is similar to the previous one but focuses on the UK goods sector and trading with the EU on WTO rules. Are there any differences in the answer you would give as regards the UK goods sector, automotive, food industry, and so on, from the one you have given about services?

Mr Richard Eglin: Yes. In some respects one can be a lot clearer about goods because they are more homogeneous. Even so, you need to separate two parts: agriculture and manufactured goods. We withdraw from the EU and we face the MFN tariffs, which vary enormously. The average for the EU on industrial goods is about 4.5%. For agricultural goods it is about 14.5%, and the agricultural schedule is riddled with quantitative restrictions. We will be taking out a certain part of those

quantitative restrictions to put into our own schedule, so it gets quite messy. In food processing, the average tariff in the beverages and confectionery sector, if I remember correctly, is 45% into the EU market, which is very high. That is an average across all sectors. Certain products, sugar and poultry, are very heavily restricted. The ad valorem equivalent tariff on certain kinds of poultry is over 200%. That will be our tariff as well, by the way, if we just take it; that will be what we are applying. There will be much more severe restrictions in certain sectors, primarily agriculture, than we face at the moment as a member of the Single Market. We will need in the negotiations to sort out with the EU whether we get a share of their tariff rate quota for exports of butter from the UK to the EU in the future and how does all that work.

For food processing, another element needs to be considered. A lot of our food processing industries import raw materials duty free, and sugar is a good example. When we withdraw from the EU, we can maintain duty-free import of sugar, but if we do we will have to apply it on a WTO MFN basis. At that point, Brazil will supply us entirely with sugar. At the moment, we give preferences to certain Caribbean countries, for example, and under EU free trade agreements with groups of what are called ACP countries we can offer them duty-free tariff access for sugar without offering the same thing to, for example, Brazil. We will not be able to do that unless we renegotiate FTAs with the Caribbean countries, African countries and Pacific countries. For food processing, in a sense, there is no problem—we can get duty-free sugar—but if we apply it on an MFN basis we would not be able to choose who we get it from, and that would be the same for quite a lot of other products.

Automobiles, again, are quite a heavily restricted sector, with average tariffs of 10% on cars and much higher ones on trucks, on lorries—about 22%, I think. Yes, we will face greater restrictions in those areas on tariffs. Regulatory restrictions generally are much more important than the tariffs, although clearly when you get up to 22% you are talking a high tariff, but in most instances they are regulatory issues, and we meet the regulations. We are exporting with those regulations in place now, so I do not see that having an immediate impact. If you have an average tariff of 4% and the pound depreciates by 10%, the tariff does not really matter, so exchange rate movements will need to be taken into account as well in trying to assess what the level of protection really is.

To me, the biggest problem, in a sense, or the biggest change we will face, is that we will not be able to influence future regulations. We can comply with existing regulations, and in future we can comply with whatever regulations are set, but we will not be able to influence those regulations, which is particularly important for services but is also important for goods, both agricultural and manufactured, and for technical regulations such as sanitary and phytosanitary measures—those sorts of things. We will have lost our influence on that. Again, the US and Japan trade perfectly happily with the EU without influencing its regulations, although that is exactly what TTIP is very largely about, setting a framework of rules for the US and the EU for the future. It would

be good to find a way, if we can, of maintaining some influence over those rules.

Q76 **Lord Lansley:** Can I follow up on the import of goods? Where the WTO is essentially reciprocal, if we are in a situation where we and the EU separately are applying the same external tariff, on the face of it you might ask what has changed. The answer is that origination has changed, and there will clearly be a difference, from the point of view of people importing goods in a supply chain to the United Kingdom, in their ability to incorporate it in goods that are then freely circulating within the rest of the EU. Viewed not only for investment but for trade purposes, for people outside the EU, dividing the EU and the UK in that way creates an impediment to their trade, so it is not a straightforward shift into a new system. How large is that effect, in your view, potentially, and given the principle of reciprocity, what would our major external trading partners feel about it? What would they look for by way of compensation or reciprocal access in order to reflect the problems that complying with rules of origin might create for them?

Mr Richard Eglin: If I understand the question correctly, I am not quite sure where I see the rules of origin clicking in, because the EU will maintain its existing rules of origin for imports coming in. Let us say that we are talking about the US exporting to the EU. Certain rules of origin will be incorporated into EU law saying that, when it comes in from the US and it meets the rule of origin, that is the tariff, or whatever it is, that applies.

Lord Lansley: But if you are bringing engines and other parts for a car manufacturer to the United Kingdom, for example, you might not necessarily acquire the ability to re-export elsewhere in the EU as you would have done.

Mr Richard Eglin: I see; I am sorry. It is the change.

Lord Lansley: It is the gateway, in effect.

Mr Richard Eglin: Yes. It is a matter for negotiation, I would say. You need to know precisely the kinds of areas where industry needs a supply chain to be maintained as key parameters for the renegotiation, either with other WTO members but more importantly with the EU. Yes, it will have an effect. I have not answered your question properly.

Lord Lansley: What might they look for as a compensation for that?

Mr Richard Eglin: For giving us better access—who might, the EU?

Lord Lansley: No, third-party countries outside the EU, because in effect their gateway into the EU market and the ease of access for their goods inside the EU market has been somewhat restricted, regardless of the tariff regime.

Professor Piet Eeckhout: Japan, for example, has invested in the car manufacturing sector here, and those companies may be subject to tariffs on their imports of parts from Japan. If there is an add-on tariff when they want to export the car to the European continent, they might want to negotiate on the tariffs on imports. They might want to ask the United

Kingdom, "Could you please bring down your tariffs on the components of cars so that we do not suffer from the fact that those cars no longer have free access to the European market?" That is the sort of potential question that may come up in determining the United Kingdom's future schedule, even if it adopts purely the EU schedule. That seems to me to be a modification in the terms of trade from the perspective of exporting nations to the UK and to the European Union—the fact that in so far as you are talking about parts and components, you do not acquire access to the Single Market. As a law professor, I find it very difficult to see economically how important that is and to what extent, and legally whether there would be a case to be answered for the United Kingdom in those terms. It is possible for the European Union to expand and take more members into the customs union. It must also be possible for that customs union to diminish and for members to leave it, and that must be the case generally with WTO members where they have a free trade area or a customs union. We have not seen many examples, but it should be possible.

The Chairman: We are running out of time. I need to get at least one more question in, about dispute resolution.

Q77 **Baroness Donaghy:** At present, UK businesses can go to the European Court of Justice if they feel that the principles of the Single Market have been violated. As you know, under WTO rules, arbitration is only possible under the dispute settlement mechanism, and cases need to be brought forward by government, as opposed to business. What impact would that have on UK businesses, in particular small and medium-sized enterprises? Could you comment on the efficacy of the World Trade Organization arbitration system?

Professor Piet Eeckhout: Yes. Thank you for the question. In actually enforcing your rights within the WTO, particularly from the perspective of private companies, there is an enormous difference with the EU Single Market simply because the Single Market rules are part of domestic law. In this country and in other Member States of the European Union, you can use domestic courts to enforce any rights you have, and, if need be, domestic courts can refer cases to the European Court of Justice. None of that exists within the context of the WTO. There is a very robust system of dispute settlement in the WTO, which I think works reasonably well. There seems to be a consensus among commentators that there is good compliance with WTO dispute settlement, but when we think of the myriad trade issues that may arise for companies in different markets, the WTO dispute settlement system does not have the capacity to deal with all those questions in the way in which, at present, companies may take their individual cases to court.

I think the question alludes to what would be a matter for UK policy: namely, to decide how actively the United Kingdom wants to make use of dispute settlement, and to what extent it is willing and able to take up at the WTO cases that result from issues in international trade, and with Europe, which are experienced by smaller enterprises as opposed to bigger ones. We see a tendency in the WTO for disputes to be taken to

panels in the WTO when larger companies are behind the dispute, although one cannot generalise too much. I see the main difference in the fact that, by definition, in the WTO you need to be somewhat selective with the disputes you bring. The other main difference is that there is no automatic enforcement. It is an international law system. You rely on compliance by the member of the WTO that has been found to violate its commitments. There are ways to exercise pressure by imposing trade sanctions when you have won a dispute, but that takes many years and is of uncertain effect. It does not have the force of domestic law in the way EU internal market law has.

The Chairman: Thank you very much. There is a very quick supplementary question from Baroness Symons, and then I am going to have to draw the line.

Baroness Symons of Vernham Dean: On that last point, what proportion of cases are SMEs? The impact of this could be huge in one sense. The real issue is whether it is a mechanism that is being used by small and medium-sized companies at the moment. If it is, it is a serious deterioration in their access to arbitration.

Professor Piet Eeckhout: My view is that it definitely is used. It is not used massively, but I think that is a consequence of the mere fact that EU internal market law has been established over decades, that Member States of the European Union simply are aware that they cannot violate those rules and that their own domestic courts will enforce EU law domestically. There is a very stable legal framework, and when there are issues many companies can approach governments with an argument based on EU law. If governments see that they have no chance of ever defending their position in the courts, they will just accept that that is the state of the law. With international trade law at the WTO, that is very different. Governments are aware that having a case against them at the WTO is one thing. What happens next and whether and to what extent you comply is a very different matter, and there is not the same sort of mechanism.

The Chairman: Thank you very much. We have run out of time. We notified you of two other questions. If you have any points on those or indeed any other general points you wish to give us, could you please do so in writing? I am sorry that we are rushing, but we now have another session. After accusing you of making it sound too simple, I do not think we have entirely come away with that impression. Nevertheless, it has been informative and we will need to follow it up. If there is anything you wish to draw to our attention, please do so in contact with the secretariat here. Meanwhile, I will wave you from this side of the room because I have some new visitors coming in at the other end. Thank you very much indeed.

Professor Piet Eeckhout, Professor of EU Law, University College London – Written evidence (ETG0003)

1. Does the fact that the EU's current WTO quotas have not yet been certified complicate the process of the UK renegotiating its WTO schedules?

I would not think it does.

2. The Institute for Government has written that some countries, including the US, "are legally bound only to agree FTAs with countries with certified WTO commitments". Does this apply to both goods and services? Is this truly a barrier to negotiations, given that the EU and US are negotiating TTIP although the EU's current schedules have not been certified?

I'm not sure what type of certification the Institute of Government is referring to. The only US requirement for certification I am aware of is not concerned with WTO schedules, but with the actual implementation of FTAs which the US concluded. The relevant congressional legislation usually provides that the President must first certify that the other parties are implementing their commitments, before proceeding with US implementation. But that is irrelevant for Brexit, at this point in time.

3. You told the Committees that "Turkey continues to conclude its own free trade agreements with other countries around the world", and that "Turkey is very much encouraged to conclude free trade agreements with the countries with which the EU concludes free trade agreements". Are there restrictions on Turkey's ability to so do, as a result of its Customs Union Agreement with the EU? Does membership of the Customs Union have an impact on Turkey's leverage in such negotiations?

To further clarify, in a customs union the parties are required to have "substantially the same" regulations of commerce. The EU-Turkey customs union arrangements therefore require that Turkey adopts the same tariffs as those of the EU (except for agriculture) and that it concludes preferential trade agreements with the countries with which the EU has such agreements. Turkey is, at present, finding that difficult, (a) because of the pace with which the EU negotiates and concludes such agreements, and (b) because it is finding it difficult to persuade the EU's FTA partners to negotiate agreements with it. There is also an issue of deflections of trade: as there are no rules of origin with Turkey, preferential EU partners can export to the EU, and then benefit from free circulation with Turkey to access the Turkish market. There is a revenue side to this, as Turkey loses customs revenue from such deflected trade. A further point to note is that the EU does not allow Turkey to participate in its free-trade negotiations, as a kind of third party (see for example the TTIP negotiations). Query whether in a UK-EU customs union that might be different.

29 September 2016

Richard Eglin, Senior Trade Policy Adviser, White and Case LLP, and Professor Piet Eeckhout, Professor of EU Law, University College London – Oral evidence (QQ 1-10)

Transcript to be found under Professor Piet Eeckhout, Professor of EU Law, University College London

Richard Eglin, Senior Trade Policy Adviser, White and Case LLP – Written evidence (ETG0001)

1. **Does the fact that the EU's current WTO quotas have not yet been certified complicate the process of the UK renegotiating its WTO schedules?**

From a narrow legal point of view this could perhaps be seen as a complication, but in practical terms I do not believe that it would matter or create any particular difficulty. In any case, the UK could use the EU-15 schedule, which includes the UK and which has been certified, as its independent schedule, ignoring the uncertified changes that have been made to the EU schedules subsequently to accommodate new EU member states. The key point is that the WTO is a commercial contract that everyone has an interest in seeing work effectively, and in my view no WTO Member is remotely likely to allow such a narrow legal issue to stand in the way of its overall trade relationship with the UK.

2. **The Institute for Government has written that some countries, including the US, "are legally bound only to agree FTAs with countries with certified WTO commitments". Does this apply to both goods and services? Is this truly a barrier to negotiations, given that the EU and US are negotiating TTIP although the EU's current schedules have not been certified?**

I am not familiar with US law on this point, but the fact that the US is negotiating TTIP with the EU (and surely would agree to TTIP if the US were satisfied with the results) suggests that it would not create a barrier for the US or others with similar legal commitments to negotiate an FTA with the UK.

16 September 2016

Dr Markus Gehring, Lecturer, Faculty of Law, Cambridge University, Luis González García, Associate Member, Matrix Chambers, and Raoul Ruparel, Co-Director, Open Europe – Oral evidence (QQ 11-19)

Evidence Session No. 2 Heard in Public Questions 11 - 19

Thursday 8 September 2016

Watch the meeting

Members present (External Affairs Sub-Committee): Rt Hon the Baroness Armstrong of Hill Top (Chairman)[19]; Lord Balfe; Lord Dubs; Lord Risby; Lord Stirrup KG GCB AFC; Baroness Suttie; Baroness Symons of Vernham Dean; Lord Triesman

Members present (Internal Market Sub-Committee): Lord Whitty (Chairman); Lord Aberdare; Baroness Donaghy; Lord German; Lord Green of Hurstpierpoint; Lord Lansley; Lord Liddle; Lord Mawson; Baroness Noakes; Baroness Randerson; Lord Rees of Ludlow; Lord Wei

Examination of witnesses

Dr Markus Gehring, Mr Raoul Ruparel and Mr Luis González García.

Baroness Armstrong of Hill Top took the Chair

Q78 **The Chairman:** I welcome our three visitors for this session. I am chairing it because our normal Chair is not well this morning, so I hope you will just run with me; I do not normally chair these sessions. We are very grateful to you for coming in. We are trying to learn at a fairly fast rate so that we can discharge our responsibilities for holding the Government to account on how they are approaching the negotiations both with the EU and with the rest of the world, in a sense, on the new status that we have to seek to achieve. You bring some important experience and we have had a look at some of the work that you have already done, so thank you for that. Thank you for spending time with us this morning. We may lose members, but that is not about you; it is simply that there are other issues going on in the House that members need to go to, so I hope you do not feel affronted that people are getting up and leaving. I am not sure that too many people need to, but there is

[19] Baroness Armstrong of Hill Top was chairing in place of Baroness Morris of Bolton, who was unable to attend the meeting.

other business on the Floor.

We wanted to start with you, Mr García. Is it okay if I call you that?

Mr Luis González García: That is fine.

The Chairman: As I said, we have read one of the articles that you have written and we wondered if you would talk us through the practicalities of negotiating a free trade agreement with the EU. As you heard, we looked in the previous session at the whole issue of the WTO and the different relationship that we will need to negotiate with it, but the relationship with the EU in any of those other negotiations and the stand that we take are going to be very important. Could you elaborate further on precisely what we will need to negotiate with the EU, and on the order or process of what we need to do for any FTA to be agreed and to take effect?

Mr Luis González García: The negotiation process with the EU has four phases. The first phase is the planning. The planning phase, or the pre-negotiation strategic planning, requires the Government to engage in consultations with three big sectors. The first is the public sector, or the relevant government and department offices, bodies and agencies that may be affected by the negotiation of a free trade agreement and/or are responsible for the policy item that would be subject to the negotiation. The second element is the consultation process with the private sector, which is an extremely important aspect of the planning of the negotiation. As a trade negotiator, the first thing you need to do is to absorb information—statistics, information about supply chains—from the industry, listening to consumers associations, importers and exporters, farmers associations, industries, universities and science. It is hard work and a tremendous and complex exercise. Once you get that information, the third element is Parliament. Normally, trading countries engage with Parliament, especially in 21st century free trade agreements where there is more transparency. Before, there was not that much transparency and governments would just negotiate in a very confidential manner.

With those three elements, once the Government have absorbed all the information, they define their negotiating objectives. Once they define their negotiating objectives, they need to conduct analysis of the economic, legal and political implications of the trade model they want to propose to the other side. When the Government have established their negotiating objectives in the particular circumstances of the UK and EU negotiation, they will be in a position to decide when to trigger Article 50.

Then we go to the second phase of the negotiation, which is the negotiation of the guidelines that will be adopted by the Council. On trade issues, there are two important elements. One is the WTO. Negotiation of the UK's WTO status would form part of the guidelines. The second aspect is guidelines as to what should be covered by reference to the word "framework", the future framework. That is extremely relevant and would need to be clarified in the guidelines, and assuming that the Council agrees that the framework includes the negotiation and conclusion of a free trade agreement, it should be covered by Article 50, and in my opinion it is. That is one negotiation.

Then the Council will establish timelines and working groups. The second phase of the negotiation is the negotiation of the mandate of the Commission. The Commission will negotiate with the UK what should be included in the free trade agreement. In practice, the negotiation of those working groups takes a long time, exchanging ideas of what should be included in the FTA. Obviously it is a different negotiation. Time is ticking, so I would not look at how long it took the US and the EU to agree on the mandates, or Canada; this is very different. It is the second negotiation.

The third negotiation is the actual negotiation of the text, the substance of what would be included in the FTA once the Commission sends the recommendation to the Council, and the Council agrees and issues its mandate. Once the Council issues its mandate, the technical negotiation starts. The last aspect of the negotiation, which is a very complicated one, especially with the EU, is that there is very likely to be a mixed agreement, so at the end of the technical negotiation you need to engage with or negotiate with the legal services of the Commission. That, in my experience, is a long process; it is not easy. Then, when you have dealt with the legal services, it needs to be approved by the European Parliament and the Council. That is a different aspect, because there is also a political negotiation and you might have to go back and revisit some issues that had been agreed from the technical side. Once it is agreed, if it is a mixed agreement, all the other 27 national parliaments will have to approve the FTA.

Q79 **The Chairman:** Very straightforward. It has never been done before, so we do not know how much will need to be done before the two years are up. What do you think are the main challenges facing the UK? I ask the other two witnesses to come in when they want to. Because we have such a tight amount of time, we are trying to be fairly direct.

Mr Luis González García: From a trade negotiator perspective, on the technical side—I am not going to deal with the political side—I envisage challenges on agricultural goods. It should be straightforward. I see no problem with zero tariffs in agricultural goods and fisheries, but in fisheries I see a challenge with market access and fishing rights. That is the challenge in agricultural goods. In industrial goods I see no problem. I do not see why there should be barriers or obstacles in the automotive industry, which would be a sensitive area; I do not see why that should be a complex issue. In industrial goods, I see no problem. In services, trading services, full access to the EU market is probably a very sensitive issue. Apart from that, it really depends whether the two sides want to include dispute settlement in the investment chapter. If they take that out, as they did in the Ukraine-EU FTA, things would be easier on the continent. As we know, CETA and the TTIP dispute settlement on investment protection, even in this country, is an extremely sensitive issue. If that is excluded, considering the fact that the UK has BITs—bilateral investment treaties—with most of the eastern European countries, it will remove one of the biggest challenges in the negotiation of an FTA.

Mr Raoul Ruparel: You cited the time issue, Chairman. It will be important to try to get some feeling up front of how long this will take. I think it will probably take more than two years, so there needs to be some idea of the willingness either to extend the Article 50 period or to consider some kind of transitional period after those two years. That is the biggest technical risk, from my perspective, and the UK should endeavour to get a clearer position from the EU on that up front. On content, I echo the points on services. That will clearly be the most difficult sector, particularly financial services, as there is no precedent for third-country access to the Single Market in financial services and other services.

Dr Markus Gehring: I am struggling to summarise what we teach in a graduate law course during an entire year in a five-minute statement, so I invite you all, or your staff, to follow the EU external relations course that is offered across the UK in many universities. It is a very complicated area, because on many of these technical details we have jurisprudence by the Court of Justice, so the Commission is not only bound by the political will of the Member States and driven by what might be in the best interests of the European Union; there are also legal limits as to how far the Commission can go in certain areas that the Commission will have to observe, or it will have to amend the treaties in order to accommodate such a new agreement with a former Member State. That is an entirely different kettle of fish. Renegotiating the foundational treaties of the EU is no small feat; some commentators have said it is virtually impossible.

For example, there could be an interest in the UK to have a Swiss model for dispute settlement. The Swiss model is that notionally you have a market issue that arises in the Swiss-EU relationship that is first decided by the Court of Justice and then that decision by the Court of Justice goes to a joint committee—a committee between Swiss officials and Commission officials—which decides how the issue has to be viewed in the bilateral relationship between the EU and Switzerland. The practice over the last 10 years has shown that Commission officials are very reluctant; it is basically impossible for the Swiss side to get any change negotiated in the joint committee, because the Commission officials feel legally bound by the definitive judgment of the Court of Justice.

The issue of dispute settlement and who can access it is going to be a huge area for negotiation. Might competition rules apply? We said that with industrial goods there should be no problems, but the Canada-EU agreement, for example, includes a provision that none of the parties is allowed to lower their taxes so significantly as to attract investments purely on the ground of very low taxes. In many of the modern FTAs, which are not aimed at integration of national economies, there are very technical rules that try to prevent gaming the system, as it were, and really try to establish a level playing field.

Q80 **Lord Liddle:** This question is on the relationship between the withdrawal treaty and the FTA. Lord Kerr gave evidence to the main Committee on Monday, and he stressed the importance in Article 50 of the clause that talks about the framework for the future relationship as setting out, or

potentially agreeing, the framework for the future economic relationship between the EU and Britain with the possibility that the kind of hard detail of the FTA would be agreed at a later date. What do you think about what could be included in those framework principles that would later determine what was in the FTA?

Mr Luis González García: In my opinion, the broad reference to a framework includes the negotiation of a comprehensive free trade agreement. It makes sense in its logic that the negotiators of Article 50, if they wanted just to narrow the scope of what can be negotiated under Article 50, could have set guidelines or principles, but the framework is broad enough to include the future trade rules. That, I think, is a sensible interpretation considering that you withdraw, but at the same time you have to give stability and certainty to the businesses, investors and consumers of Europe. In the spirit and objective of Article 50, I would say definitely that you need clear, permanent and predictable rules for the future relationship between the two sides. That definitely would need to include trade.

Lord Liddle: Does that mean that you think we could have an FTA agreed within the two-year timeframe of Article 50? That is what I do not quite understand.

Mr Luis González García: The two-year timeframe is not very realistic. I think it is highly unlikely that in two years you can negotiate it because, as I mentioned before, there are three phases. Once Article 50 is triggered there are three phases: negotiating the guidelines, negotiating the mandate—that might take a long time—and then negotiating the substantive issues. That is why it is difficult in the two-year timeframe, but, as my colleagues said, they need to agree on an extension to the two-year deadline.

Dr Markus Gehring: I agree with my colleague that it would be desirable, if that were agreeable to the European side. The information we have received in recent weeks seems to agree with Lord Kerr. You can probably establish a programme of negotiation and the broad outline of what a free trade agreement with the then former member state looks like, but it is not very realistic either to use Article 50 as a legal basis for such an agreement or to hope to conclude those negotiations within the two years. The Commission is firmly of the view that first you leave and then you negotiate the future relationship. It would be very difficult for the UK to convince the Commission otherwise.

Mr Raoul Ruparel: I think there is leeway in Article 50 to negotiate as much as Mr García suggested. The Commission has its view. I think the Member States have a slightly different view. Ultimately, the mandate will be tasked by the member states, and if they set a wide and broad mandate the Commission will have to fulfil it, so I think there is scope there. Looking at this from a political perspective, from the UK's negotiating approach, there is a clear advantage for the UK in trying to keep the withdrawal agreement and the trade agreement as linked as possible. The types of areas where the UK has significant leverage in these negotiations—foreign policy, security, contributions to the EU

budget, what we do on immigration—are both a constraint and an area of leverage, but a lot of those areas will tend to be grouped in the withdrawal agreement. If we negotiate that on a narrow basis, when it comes to negotiating the trade agreements, because the EU is going to be a much larger trading block the leverage will be more skewed in its favour, so keeping the two linked will be vital for the UK in maximising its leverage sin the negotiations.

Mr Luis González García: I am not entirely sure that the Commission's position is that first you exit and then you negotiate an FTA. That was the Trade Commissioner's view and she has not repeated it since the interview at the BBC. The President of the Commission has never said anything like that. It is quite telling that she has kept very quiet about the position she gave in an interview back in June.

Q81 **Lord Triesman:** In your sequence of events, Mr García, you said that it would be very important to specify what should be included in the FTAs. Are there issues or sectors that you think can be readily accommodated in FTAs, and are there sectors that you think would not normally be included in FTAs? Do you feel that there is a boilerplate of standard terms from EU FTAs that we could export into any that we were thinking of developing ourselves, given the patterns of trade that the UK follows?

Mr Luis González García: Yes. There are aspects of FTAs that are common to most agreements, so you would find it very easy to agree on market access, agricultural and industrial goods, rules of origin, customs procedures, customs facilitation and co-operation. You would agree to investment protection, leaving aside the arbitration and dispute resolution aspect. On services, you have telecommunications and e-commerce. Obviously you can expand it to other areas. You have cross-border services and you have to negotiate modes 1, 2, 3 and 4. Mode 4 includes movement or presence of natural persons—businessmen, skilled or lower-skilled workers. You would also include government procurement as one of the issues in the FTA, as well as competition, intellectual property rights and geographical indications. Land transportation, maritime transportation and air transportation can be included in the treaties in FTAs. In EU comprehensive FTAs, the 21st century EU agreements, you would have to include sustainable development, human rights, environmental protection and labour rights, because that is EU trade practice. Those are issues that the EU always negotiates in its FTAs.

Lord Triesman: Is there anything that you think would not commonly be in an FTA but which might be pursued by the United Kingdom?

Mr Luis González García: In the negotiation of an FTA you can include many things that are related to trade. I have seen FTAs that included issues such as access to the Rome statute of the International Criminal Court or anti-corruption provisions—anything that could provide co-operation, transparency and due process. There are many elements; it depends on the objectives of the negotiation. The EU negotiates three different FTAs: FTAs with a political dimension; FTAs with a developmental dimension, such as FTAs with the Caribbean countries or with central America; and FTAs for security and political reasons, such as

the ENP—the European Neighbourhood Policy—with all the former Soviet countries. They are different FTAs. There are FTAs with an economic objective, such as with Canada, Mexico, Chile and obviously the United States. You have different elements. There is also the fact that some FTAs form part of a global agreement; the EU negotiates a global agreement, a political co-operation agreement and part of it is an FTA. In some cases it is just the FTA and there is no political co-operation or scientific co-operation in the FTA, and there are no security aspects in the FTA. There is a lot of creativity in the negotiation of an FTA.

Dr Markus Gehring: Let us be honest: the current *acquis* of EU rules is normally much broader, so your right not to be discriminated against on the basis of your language would not normally be included in an FTA. We have seen in Canada that some mild form of mutual recognition of qualifications, which might be very important for UK universities, for example, is included, but that is the first time to my knowledge. There are quite a few areas of the existing EU *acquis* that I have not seen in any FTA in a bilateral relationship but which might be important for the UK. Certain forms of linguistic rights might be interesting for UK companies that do not necessarily operate in Romania.

Q82 **Baroness Noakes:** We have mentioned a couple of times the free trade agreement with Canada, and people have looked at that as a potential model for the UK. Would you comment on what market access would be like under the CETA versus access to the internal market, and what the impact would be on particular sectors in the UK?

Mr Raoul Ruparel: There is no doubt that it is the most comprehensive agreement the EU has sought to strike, but, as was hinted at, it still falls some way short of the *acquis* and the Single Market as it is. It includes relatively good access in terms of industrial goods and scrapping 100% of tariffs, albeit over a number of years. It involves a relatively good reduction of tariffs in agricultural goods, although some exclusions apply in poultry and certain other specific agricultural goods. It includes, as was hinted at, some mention of professional qualifications, although it is nowhere near as advanced as in the EU, but even the EU falls short of its aims in that area. It is fairly good on opening up public procurement markets at all levels in Canada and in the EU, although there are some restrictions on certain provinces in Canada.

On areas such as services it is fairly limited. It provides some rights of establishment, and the ability to set up subsidiaries and entities in the EU, but it is far short, particularly in financial services, of providing a passport and being able to provide a service from your home base in the UK, for example. In all other areas of services it is relatively limited, and there are hundreds of pages of restrictions on the services that are not opened up. Although it is a comprehensive agreement, it would be a big change for the UK, particularly on the services side. On the goods side, if you had phasing in over time, there would be a significant change over time, but if we presumed that the rules were applied from the get-go, there would be a change but not as big as in services. It is a starting point if you are looking at what type of agreement framework to use, a comprehensive

living agreement. It is a modern agreement in that sense and I would consider it preferable to some of the piecemeal bilateral deals we have seen before, but in content the UK would probably be aiming a lot higher.

Baroness Noakes: Could I clarify that? You said there would be a big impact in services. If we strip out financial services, how big an impact would there be, given that the EU is not actually a perfect internal market for services?

Mr Raoul Ruparel: That is an important point. The Single Market in services is far from as effective as the UK would like or has pushed for over the past decade or so. In my understanding, there are certain sectors, as may have been mentioned in the previous session, such as aviation where there is fairly good integration, but there are also more precedents for non-EU countries having access to Single European Sky and the European Common Aviation Area (ECAA). There are more precedents for agreement on that. In areas such as broadcasting, there is reportedly very good access for broadcasters, and services provided across borders.

Looking at professional services, the services tend to be provided on the ground more than passported from a home base, so that would mean maintaining free movement of people to provide those services on the ground, and maybe recognition of the qualifications and the skills of those people, and the ability to open subsidiaries. There seems to be a tendency in a lot of the professional services to provide the service more via subsidiaries and local companies in countries. The reasons may be to do with accessing local markets and trust relative to a local partnership, but my understanding, particularly in areas such as accountancy or the big four, is that they tend to provide via subsidiaries and local companies rather than a passport, as it were, from London.

In a number of other areas, we know that there are many protected professions across the EU. In that sense, it is not necessarily easy to be a professional in the UK and provide that service across countries. In some countries—Germany, for example—the protected professions extend to being a butcher, a baker and all kinds of things that we might not consider a protected profession. The opportunity cost in services, beyond financial services and certain things such as aviation and broadcasting, is much lower, and as was hinted at there needs to be wider consultation on exactly how deep that will go, but financial services are a very large sector.

Baroness Noakes: Would either of you like to add anything?

Mr Luis González García: It is going to be a unique negotiation. From a trade negotiation perspective, it is unprecedented because the whole idea of a free trade agreement negotiation is to start from the status quo and then go forward for integration. It can be simple integration, very limited integration or deep integration. The question is how much I am going to open my market to your country, to your businesses. This is going to be a negotiation where the offensive position of the UK in many aspects is to maintain the status quo and in other aspects to go backwards; this is unique in negotiations. One of the reasons why FTAs are very complex

and difficult and take a lot of time is that it is not only about the negotiations. It is not only about access and opening your sensitive sectors. It is about regulations; it is about the other country modifying its regulations or complying with your regulations, or harmonising our legislation. That is a very sensitive issue, from a legal perspective and a political aspect. That is why we see difficulties in the negotiation between the US and the EU; it is about regulation, and no one wants to give up their legal framework. In this instance, that is not the case, because the UK adopts EU legislation—it is part of EU law—so on the most complex issue of the negotiation, which is regulation, it is the same regulation. It is a unique negotiation.

I would not use CETA as our starting point. In many aspects, it is very innovative and it would be useful, but in other aspects I would look to an FTA with the Caribbean states, for example, where the UK would give access to midwives, doctors, nurses, engineers, fashion models, et cetera. Part of the work of a trade negotiator is to look at what you have negotiated in other agreements and take the bits that would accommodate your interests and the interests of the other side. That is why I would not say, "Okay, CETA, and from there we begin the negotiation".

The Chairman: I think you have led us into the next area that we wanted to look at, which is the relationship between free movement and an FTA.

Q83 **Lord Liddle:** You say that most free trade agreements do not offer full access in services, and that in a lot of sectors, under the existing Single Market, setting up subsidiaries is as important as passporting. That raises the question of free movement. If you have a single company with subsidiaries, are there precedents for including free movement rights within FTAs? The other thing, I suppose, is that if we want full access to the Single Market, our EU partners might say that we should still be paying into the budget. Is there any precedent within FTAs for budgetary contributions?

Mr Luis González García: On the question of free movement of persons, the short answer is no. Under an FTA you cannot include free movement of people. The EU would not be able to negotiate free movement of people in an FTA. Why? Because it can negotiate only what is included in the Common Commercial Policy (CCP). Not only that, it must take into account the objectives and principles of the EU External Action Service. Free movement of people is not included in the CCP or in the EU External Action Service. That is why it would be outside the scope of an FTA, and there are no precedents; there is no FTA where free movement of people is negotiated. On the budget issue, there is one precedent: for example, the agreements that the EU negotiates with potential members of the EU, countries that are in the process of seeking membership of the EU. A good recent example is Ukraine. It is an FTA within a global political agreement. In the FTA part of the agreement, there is no budget, but in the agreement signed between the EU and Ukraine there is an obligation for Ukraine to contribute to the budget of the EU. Why? It is for two

reasons. Ukraine is interested in European funds and in European programmes, so if the UK is interested in continuing, for example, the Erasmus programme, you have to contribute. That is part of the deal. If you want to be part of EU funds, you have to contribute to the budget, but these are different kinds of contributions. It is the same thing with all the other European agencies providing funds and programmes; you have to contribute to those programmes.

Dr Markus Gehring: In an ideal world and with the agreement of European partners, a lot of things would be possible. The WTO GATS agreement itself includes Mode 4, as we said, which includes the physical movement of people. If you liberalise architectural services, you allow an architect to come to the United States and work on a project knowing that once their services are no longer required they go back to the country they came from. Very few countries in the world have liberalised Mode 4. It is normally under a lot of restrictions. I think the most liberal GATS schedule is that of the United States of America, and if you have tried to work in the United States or provide services there, you know what the restrictions are. A lot of thought should be invested in participating in regulatory agencies. There are now quite a few EU regulatory agencies that the UK also benefits from at the moment. Recreating all those agencies in the United Kingdom would easily eat up a chunk of the budget that seems to be overly generously allocated already. There would be precedent to accept not having any governance input into those agencies but just using them for their decision-making power and paying for that kind of service, so that would be another level of contribution.

Baroness Symons of Vernham Dean: I have a quick question. You mentioned the Erasmus arrangements. This has been one of the main focuses of a tremendous amount of anxiety among our academic community. You said that if the UK wanted to continue with Erasmus, we would have to contribute to the EU budget. Would that be negotiated only as part of a comprehensive agreement, or could one put it to one side and make a discrete agreement around something like the Erasmus arrangements? I raise it simply because we raise it constantly on the Floor of the House and clearly our colleagues in the academic world are seriously concerned.

Mr Luis González García: Yes, you can put it aside. You do not need to sign an FTA and you do not need to sign a global political comprehensive agreement to have access to Erasmus. That is independent.

Baroness Symons of Vernham Dean: Thank you.

Mr Luis González García: In all the other European agencies, most cases are done by bilateral agreement. There is a huge list. You choose the programme that you like and you sign a bilateral protocol.

I want to clarify that there are two different issues: the free movement of persons as a principle of EU law and the internal market, and Mode 4 on supply. They are completely different things.

Q84 **Lord Whitty:** Can you take us a bit further on the disputes resolution process in FTAs? At the moment we have the ECJ and the incorporation of

EU law to be enforced by national courts. The smallest company or an individual can enforce it that way. This has not been the case in most FTAs, as I understand it, and the prospect of its being there to some extent in the TTIP has caused, shall we say, some political controversy. Do we have a model for disputes resolution of an FTA for the UK and the EU that allows access but would not run into those political difficulties?

The Chairman: In five minutes.

Dr Markus Gehring: The dispute settlement clauses in FTAs are as diverse as the FTAs themselves. The standard model is very similar to the WTO. You normally have a panel. It is a state-to-state process.

Lord Whitty: Only states can apply.

Dr Markus Gehring: If your small or medium-sized company has direct access to the Government and can easily sway the entire United Kingdom to take on, say, the United States or the EU in a small matter where it feels it was not well treated by the trading partner, that is great. Most small and medium-sized companies that I know do not have that level of access. I think Piet Eeckhout mentioned Airbus. There was the famous Fujifilm case where Fuji and Kodak were battling, or Airbus and Boeing were battling, in the WTO because they could convince their Government that it was in their political and economic interest to fight the case. Some countries have streamlined that, including the EU, and the US. If you make a complaint about mistreatment in another trading partner, the US has a domestic law that facilitates that kind of process, and if the US wins the WTO dispute at the end, part of the proceeds or the gain from the retaliation could flow back to the company. It is normally a much more difficult process, and usually companies prefer the WTO process because some of the FTAs just have the first phase; they do not have an appellate body. There is no mention of retaliation at the end, so you do not get compensation if you win the case. Most would prefer the WTO dispute settlement where you can even get carousel sanctions; you change the sanctions every three months in order to convince the trading partner to bring their laws and their administrative practices in line with WTO law.

You could look at a model like the EFTA court. There could be a UK-EU court. The UK is a country that prides itself on its very stable and secure legal system, so it might be something that the UK negotiators want to explore. A joint court between EU judges and UK judges to administer the new comprehensive relationship could be possible. Some of those court arrangements have run into EU law problems, because the Court of Justice has said that not even the Strasbourg court should be above the Court of Justice in Luxembourg. The creativity may run into slight difficulties on the EU law side rather than what is possible in an ideal world.

Mr Luis González García: We need to look at dispute resolution and at the rights of businesses, investors and consumers faced with regulations and measures that may be affected by the measures adopted by the other side, the EU in this case, without the European law framework. I would say that we need to look at an FTA. There are a lot of dispute resolution provisions in each chapter, so it really depends. For example, if

we are talking about an importer or an exporter, in the chapter on customs procedures there are rights for importers to file, and the treaty provides for the right to challenge and appeal the decision by an impartial, neutral administrative tribunal, in quasi-judicial or judicial proceedings. If it is competition, there is another chapter; if it is IP rights, there is another recourse for small and medium-sized enterprises; and if it is investment, there is another set of provisions that deal with the rights. Let us not forget that FTAs provide better rights to businesses, not fewer rights. They do not go backwards; they go forwards. An FTA gives more rights to businesses and investors, whether they are small importers, consumers or IP rights holders, et cetera.

Markus was talking about the big picture of interstate dispute resolution, but there are many mechanisms. As a trade negotiator and having implemented an FTA with the European Union, I know that the process is very simple. There is constant communication between the ministries of the two countries—the international departments and the trade departments dealing with the issues on a daily basis—where many of your concerns are going to be resolved. One of the good things about an FTA is that it provides for an additional forum where the state will call the other state to say that they have an issue. That is why you will see sub-committees, committees, working groups and subgroups in FTAs; it is all about exchanging and trying to resolve all the issues, because there are plenty of technical issues.

The Chairman: We are going to be training a lot more lawyers.

Mr Raoul Ruparel: Can I add one point to build on the UK/EU court point? We have to bear in mind the withdrawal agreement. There will be lots of horizontal issues where previously ECJ jurisdiction applied and there will be need for arbitration, on security co-operation and things like that. A big court—some version of institution-building—and more advanced arbitration, given the depth and breadth of the agreement likely between the UK and the EU, will probably be needed.

Q85 **Lord Risby:** I want to come on to an extremely difficult area. You said, Mr García, that regulation on the TTIP discussions has been a huge issue. Equally, we heard in our previous session that many parts or elements of the Single Market were very open and liberal, so there is a mixed picture despite what public opinion might be. In that context, to what extent do you think that, if there is an EU-UK FTA agreement, the level to which the goods and services provided by this country would be subject to a broad EU set of regulation?

Mr Luis González García: A great deal. This is a very important aspect that needs to be clarified by the Government at the negotiating table with the EU. I imagine that in the negotiation the EU is going to ask, "You want access to financial services. Which of my directives are you going to implement and replicate in your law?" That is a decision for the UK Government, because it is an open economy and one of the most liberal economies in the world, and due to the convergence of legislation in the application of EU law I can see that as a problem. In financial services or in services in general, the easiest thing would be for the UK to adopt the

EU law; in that way, the level of access to EU services would be greater. Obviously, the more integration you want and the more you want to be in the Single Market, the more locked into EU law you would be. That is a policy decision, because more integration or fuller access to the Single Market means less flexibility in negotiation with third countries.

Dr Markus Gehring: Sometimes the EU allows for equivalence. If you have equivalent standards that are equally stringent and you do not like, say, the EU ETS on climate change—an area I know quite well—and you would rather have a carbon tax, but the overall price of carbon between the two systems was similar, there could be an equivalence negotiation. You can see that in other areas. Even the Technical Barriers to Trade (TBT) and the Sanitary and Phytosanitary Measures (SPS) agreements, the standards agreements on trade and goods in the WTO, favour international standards over unilateral standards. Of course, the closer you get to the EU Single Market, the more there will be demand on the EU side to follow the EU standards to the letter. Politically, that is very difficult, because sometimes you do not have political input into how the standards are made. You have heard or read what the Norwegian Foreign Minister said; you have to phone your friends in Helsinki and Stockholm to get into the 15th annexe the little issue that is really important for Norway. It is a very uncomfortable situation, and more often than not partner countries that are in the EU will say, "Actually, we have our own little battles to fight in these standard negotiations, so we cannot also take care of your aspects".

Mr Raoul Ruparel: It is worth mentioning that in a number of free trade agreements the EU tries to export its products, standards and rules of origin. In CETA, Canada has to sign up to EU standards and rules of origin. The rules of origin were discussed in the previous session, but basically they are about proving where a product is manufactured and if it is sufficiently manufactured in your own country. There are accumulation rules on how much of other products from outside is brought in and whether the tariffs have been paid on that and what-not. Those are rules that you have to meet, and that will be an additional administrative burden for businesses and goods exporters.

On services, the equivalence side is quite limited and specific. I will speak on financial services, an area I know better. For example, certain regulations have equivalence and third-country access built in; MiFID II and MiFIR, which is coming up, are well documented and can give pretty wide access if you meet the equivalence standards, which is a political not a technical decision. That can allow you to have passport-like rights in applying investment services. Equally, the capital requirements directive does not have any third-country equivalent, so you cannot passport in your banking services. In that case, if you want to apply those services, you have to deal with all the local authorisation and local rules and regulations. How the rules and regulations you have to meet on services will work is a patchwork.

The Chairman: We are running out of time, but I want to broaden us out from the EU and ask Lord Stirrup to put his question.

Q86 **Lord Stirrup:** Some people have suggested that legally the UK could remain a party to existing EU free trade agreements even after it had left the Union, so they would become agreements between the EU plus one and a third party. Is that a credible path? What would the third parties be likely to think about it, and would it be in the UK's interests to follow that?

Dr Markus Gehring: I think members have seen the blog that I wrote in March. Not much has changed from my point of view since I wrote that. There are four or five aspects that make a simplified version of, "We are a party to these free trade treaties", and some are more complicated. The first aspect is that some FTAs, or some trade agreements, are just concluded by the EU, so there would be no access to the UK. Even some of the mixed agreements specify that the application of the agreement is really restricted to EU Member States, which then makes it very difficult just to partake in those agreements. Of course, if your Article 50 negotiations result in some form of understanding on the 50 or so FTAs that the EU has concluded, everything is fine and you can continue as before. Even if that is not the case, there is the added problem that either the EU or the third-country partner would probably have a right to request some form of renegotiation. I tried to explain that in the sense the EU negotiated as a customs union with the internal market at its heart. If the UK can no longer participate in the EU internal market, in my view it can no longer fulfil a good chunk of those free trade obligations, and that triggers the renegotiation. Some partner countries might not have an interest in renegotiation but you still have the EU at the table. The EU could take the very drastic step of either withdrawing or terminating those kinds of agreements, if the partner still lets the UK as a non-EU member state participate in that relationship.

Lord Stirrup: It is an approach that could be pursued under the Article 50 renegotiation.

Dr Markus Gehring: That would be my advice, yes.

The Chairman: We have not covered everything. If there are things that you would like to contribute and you have not had the opportunity to do so today, please write and the secretariat will make sure we hear about them. We are sorry that we have had to squeeze everything so much, but we are, as I said, trying very quickly to get a fairly comprehensive view and understanding of things so that we are then able to deal with the Government more effectively. Thank you enormously for coming. I thank colleagues too, because you have had a long session this morning; Larry and I appreciate that. Thank you very much indeed.

Luis González García, Associate Member, Matrix Chambers, Dr Markus Gehring, Lecturer, Faculty of Law, Cambridge University, and Raoul Ruparel, Co-Director, Open Europe – Oral evidence (QQ 11-19)

Transcript to be found under Dr Markus Gehring, Lecturer, Faculty of Law, Cambridge University

Luis González García, Associate Member, Matrix Chambers – Supplementary written evidence (ETG0006)

1. **Does the fact that the EU's current WTO quotas have not yet been certified complicate the process of the UK renegotiating its WTO schedules?**

   Response: First I would like to express my view on one aspect which was discussed by the previous panel. I disagree with the expert, Mr Richard Eglin, who said that the process of negotiation of the schedule of commitments should be a conducted as a "rectification" and not a 'modification'. I disagree. Rectification of schedules can only occur in situations of 'purely formal character' ie a change which do not alter the scope of the concession [see Procedures for Modification and Rectification of Schedules of Tariff Concessions, Decision 26 March 1980]. The UK's negotiation will alter the EU schedule and therefore cannot be considered a rectification.

   I will now respond to the specific question above. Getting an agreement on TRQs (quotas) with the WTO members will potentially become a problematic exercise. If the EU agrees to share some portion of its quotas on agriculture to the UK then it is likely to complicate the UK's negotiation of its schedule with WTO members because (1) some third countries will feel unfairly affected by the allocation of quotas (depending on their exports some third countries will feel that they deserve a bigger share of the UK or EU market), and (2) if such allocation is based on the certified EU-15 schedule or the non-certified EU-25 schedule because these are outdated schedules. It may be less complicated for the UK if the schedule is based on the proposed 28-EU schedule. However, the EU-28 schedule has not been agreed and it is managed by the EU Commission on a bilateral basis in a non-transparent manner. This is likely to trigger further discussions between the WTO members and the EU which will have an impact in the UK's WTO renegotiation.

2. **The Institute for Government has written that some countries, including the US, "are legally bound only to agree FTAs with countries with certified WTO commitments". Does this apply to both goods and services? Is this truly a barrier to negotiations, given that the EU and US are negotiating TTIP although the EU's current schedules have not been certified?**

   Response: I am not aware of a formal policy in the US or any other country. I don't know what is driving this comment by the Institute of Government but what is clear is that this alleged policy is not a WTO rule. Under Article XXIV of the GATT, WTO members can negotiate FTAs with another WTO member or with a non-WTO member. A good example is the current EU FTA negotiation with Serbia (a non-WTO member). If a WTO member can negotiate an FTA with non-WTO countries why WTO members would want to have a policy which restricts its trade negotiations only with those with WTO certified commitments. It doesn't make sense. One would expect that all WTO members would have the same policy, not just the US.

3. Please would you give your thoughts on Lord Stirrup's question, and the responses made Dr Gehring? (Excerpt below)

Lord Stirrup: Some people have suggested that legally the UK could remain a party to existing EU free trade agreements even after it had left the Union, so they would become agreements between the EU plus one and a third party. Is that a credible path? What would the third parties be likely to think about it, and would it be in the UK's interests to follow that?

Dr Markus Gehring: I think members have seen the blog that I wrote in March. Not much has changed from my point of view since I wrote that. There are four or five aspects that make a simplified version of, "We are a party to these free trade treaties", and some are more complicated. The first aspect is that some FTAs, or some trade agreements, are just concluded by the EU, so there would be no access to the UK. Even some of the mixed agreements specify that the application of the agreement is really restricted to EU Member States, which then makes it very difficult just to partake in those agreements. Of course, if your Article 50 negotiations result in some form of understanding on the 50 or so FTAs that the EU has concluded, everything is fine and you can continue as before. Even if that is not the case, there is the added problem that either the EU or the third-country partner would probably have a right to request some form of renegotiation. I tried to explain that in the sense the EU negotiated as a Customs Union with the internal market at its heart. If the UK can no longer participate in the EU internal market, in my view it can no longer fulfil a good chunk of those free trade obligations, and that triggers the renegotiation. Some partner countries might not have an interest in renegotiation but you still have the EU at the table. The EU could take the very drastic step of either withdrawing or terminating those kinds of agreements, if the partner still lets the UK as a non-EU member state participate in that relationship.

Lord Stirrup: It is an approach that could be pursued under the Article 50 renegotiation.

Dr Markus Gehring: That would be my advice, yes.

Response: from both, legal and practical point of view, I don't think it is possible for the UK to remain a party to existing EU FTAs. The UK signed mixed FTAs as a 'Member State' of the Union not in its own right (different situation from GATT and WTO). The language of the EU FTAs makes it clear that the parties to the treaties are the EU and its Member States as 'one contracting party', and the third country as the 'second contracting party'. If a country ceased to be part of the Union the FTA is no longer applicable to that country.

Even if one can argue from a legal theory point of view that certain EU FTAs may continue to apply to the UK after exiting the EU, and even if that is an agreement reached in the Article 50 Withdrawal Agreement the reality is that it's practically impossible to separate the rights of the UK with the rights of the EU in an FTA. The language of the FTAs does not leave room to differentiate which commitments belong to the EU and which ones for the individual Member States. One only needs to look at the agricultural quotas in the agreements to see that it is impossible to disentangle the rights and obligations of the EU with those of the

UK in the FTAs. Also it's important to point out that under customary international law a unilateral declaration by a State to remain a party to an existing treaty is not sufficient. The UK will need the approval of the EU and the third country to remain a party to existing EU treaties.

In reality there are only two possibilities:

1) a trilateral agreement between the EU, the UK and the third country. This scenario is highly unlikely to happen because it will require a rebalancing of concessions of the original FTA which is something third countries will not accept; or
2) the UK will have to negotiate a separate FTA with the third country which might not look like the original FTA between the EU and the third country. I believe this is the most likely scenario and one that third countries are likely to prefer.

28 September 2016

Dr Peter Holmes, Reader in Economics, University of Sussex, and Dr Ulf Sverdrup, Director, Norwegian Institute of International Affairs – Oral evidence (QQ 20-29)

Evidence Session No. 3 Heard in Public Questions 20 – 29

Thursday 15 September 2016

Watch the meeting

Members present (External Affairs Sub-Committee): Baroness Armstrong of Hill Top (Chairman)[20], Lord Balfe, Baroness Brown of Cambridge, Lord Dubs, Lord Horam, Earl of Oxford & Asquith, Lord Stirrup, Baroness Symons of Vernham Dean

Members present (Internal Market Sub-Committee): Lord Whitty (Chairman), Baroness Donaghy, Lord Green of Hurstpierpoint, Lord Lansley, Lord Liddle, Lord Rees of Ludlow, Lord Wei

Examination of Witnesses

Dr Ulf Sverdrup, Director, Norwegian Institute of International Affairs, and Dr Peter Holmes, Reader in Economics, University of Sussex

Lord Whitty took the Chair.

Q87 **The Chairman**: Welcome. While you make yourselves comfortable I will just run through the process. You have been notified of a number of questions and we will run through them. Principally, the customs union questions will go to Dr Holmes. I hope that both of you will feel free to comment but, if possible, not repeat each other as we are fairly constrained by time.

This is an open, public session. It is being recorded and there will be a transcript of it. I hope that will not inhibit you too much but you need to know that.

If you have no questions about the procedure, I will kick off with the first question, which is directed principally at Dr Holmes. In fact, we will be concertinaing the first two questions and I hope that you have received notification of that. It is about the customs union.

[20] Baroness Armstrong of Hill Top was chairing in place of Baroness Morris of Bolton, who was unable to attend the meeting.

From the UK point of view, what are the key benefits and drawbacks of being in the customs union as a non-EU country? What are the important distinctions that you see between a free trade area and a customs union, and what is the effect of being outside the customs union on trading with non-EU countries, particularly in relation to things like rules of origin, customs procedures and so on? That is directed principally at Dr Holmes but perhaps both of you can comment, for our elucidation, on what you see to be the advantages and disadvantages of a customs union and what the distinctions are.

Dr Peter Holmes: First, let me thank you for inviting me. It is a great privilege to be here and I hope I do not make too many mistakes in talking to you.

The Chairman: I am sure you will not.

Dr Peter Holmes: First, you have to be careful about talking about 'being in the customs union' as a non-EU country. I do not think that that is a possibility. Andorra, Vatican City, San Marino and Monaco are physically inside it and are effectively part of it, but the only country that is linked to the EU in a customs union relationship which is not a member is Turkey. It is not a member of the customs union; it is a country that has a customs union with the customs union. That is quite different, because the coverage of the customs union with Turkey is different from that of the EU customs union. As you point out, it does not cover services or agriculture, and, very strikingly, anti-dumping is still possible between the EU and Turkey. There was a WTO case some years ago involving relations between India and Turkey—I can perhaps send you the details—which highlights the incomplete nature of the EU-Turkey customs union. It is an important distinction but, if one moves away from that, the fundamental point is that a customs union is a trade bloc where the partner countries agree to remove tariff barriers on each other's goods and to have a common external tariff against third countries, whereas a free trade agreement is where countries agree to remove tariff barriers on each other's goods but they do not have a common policy against third countries. The consequence is that within a free trade agreement you have to have customs barriers to check whether a product really comes from the partner or whether it is a third-country good, in which case it is not entitled to duty-free access. With a free trade area, you have to have rules of origin to check whether a product originated within the free trade area. With a customs union, in principle you do not have to have rules of origin, so the goods can flow completely freely.

So it sounds as though a customs union is an attractive arrangement because you do not have to stop goods at the border. In reality, however, the Turkish-EU customs union does have customs posts because it is not a complete customs union in the way that the one inside the EU is. So the advantage of the customs union is that you get complete exemption from tariffs for all goods across the border, but in principle you have to have exactly the same external trade policy as your partner, which means that Turkey has to sign free trade agreements with everybody that the EU signs an agreement with. It has, in principle, to accept any negotiating outcomes that the EU secures at the WTO. If there ever is another WTO

round, Turkey will have to go along with the EU position. Basically, in a customs union you completely lose your ability to have your own independent external trade policy.

Secondly, although a customs union gives you tariff-free access for your goods, it does not necessarily give you exemption from non-tariff barriers. The European Economic Area (EEA) is a different matter: it is what I would call a regulatory union. Dr Sverdrup is a much bigger expert on the EEA than I am. The EU-Turkey customs union was not a complete regulatory union, so for many years after it was signed Turkey was obliged to accede to all EU rules and regulations governing the internal market in industrial goods. However, that did not get Turkey free access for its products into the EU market because—I am sure that some of you know more about this than I do—the EU did not recognise Turkey's conformity assessment on testing and certification. So, even though Turkish goods, under Turkish regulations, had to comply with EU standards, the EU did not recognise the Turkish certificates that confirmed that. It was only about 10 years after the customs union agreement was signed that this recognition was given. That is probably more than you wanted.

The Chairman: It is more complicated than we wanted; nevertheless, it is very helpful.

Lord Green of Hurstpierpoint: I have a question just to clarify matters in respect of the Turkish agreement. My understanding is that, because it covers only certain sectors, it is those sectors only in respect of which Turkey loses its freedom to negotiate independently with third parties.

Dr Peter Holmes: That is basically correct. For any goods, any areas covered by the customs union Turkey must align themselves with the EU.

Lord Green of Hurstpierpoint: So if Britain had a customs union arrangement with the EU for certain key sectors, there would be a whole range of other sectors of the British economy for which we would have complete freedom with third parties to do FTAs.

Dr Peter Holmes: That is right.

The Chairman: The customs union has no direct implication for services in that sense.

Dr Peter Holmes: If it is a customs union that covers goods only, it will not affect services. But it is worth mentioning—I think that we both have comments to make on value chains—that more and more trade today consists of goods and services bundled together. They are either physically incorporated or you need to send the engineer to service the thing. You cannot quite separate goods and services as much as you could in the past.

The Chairman: Would Dr Sverdrup care to comment on Norway, which is outside the customs union but still trades heavily with the EU?

Dr Ulf Sverdrup: Yes. As you know, Norway is not a member of the customs union. It is a member of the EEA and a member of the internal market. To my knowledge, this has worked pretty well. The Norwegian

government have to stick to the rules of origin, and there are three main difficulties arising from that. The first is that it introduces a bit of bureaucracy or paper-shuffling, so it increases the transaction costs for business. Secondly, as the economies become more integrated, they also engage much more in value chain economics, so it is a bit more challenging to determine where things are produced. The final point relates to consumers. In e-trading, for instance, you have customs at the border. For the individual consumer importing goods from amazon.com, or something like that, there will be a threshold for doing that. So you have to have a mechanism for declaring custom, which is a bit of a hassle.

Q88 **Lord Lansley**: Dr Holmes, if a non-EU country is part of the customs union for goods but not otherwise, what does that mean in practice? There are very few examples of this; perhaps Turkey is the only one. In practice, has that meant that Turkey has been able to enter into bilateral free trade agreements, or does the restriction on the flexibility of its external tariffs make the negotiation of bilateral free trade agreements extremely difficult?

Dr Peter Holmes: As I said, you have to distinguish between having a customs union with the EU and being part of it. My understanding about the deal with Turkey—and you would probably need someone from Turkish customs here to explain it fully—is that Turkey is obliged by its relationship with the EU to sign free trade agreements with everyone that the EU signs a free trade agreement with; this is about industrial goods, not agricultural goods, I believe. But there are all kinds of odd little anomalies in this. For example, Turkey was interested in signing a free trade agreement with Georgia, and the EU said, "Okay, you can do that", but, strictly speaking, if the customs union with the EU was a complete customs union, that would have been impossible. I have heard stories that Turkish manufacturers of television sets were selling them across the border into Georgia, getting them Georgian certificates of origin, and then sending them into the EU, because the EU had put anti-dumping duties or other restrictions on Turkish televisions, but if they came across as Georgian ones they would not be affected. The general principle is that Turkey has to sign agreements with countries that the EU signs agreements with, but those countries do not have to sign agreements with Turkey.

If there was a TTIP agreement between the EU and the US, Turkey would not automatically be included. That would mean that US goods could come into the EU and be trans-shipped into Turkey without paying Turkish customs duties, but Turkey could not send its goods into the US duty free. There is a special derogation clause somewhere in the EU-Turkey customs union that would allow Turkey to put extra duties on goods coming from the US into Turkey—it is called trade deflection—but it is very messy. Basically, Turkey has very little freedom to sign agreements with third countries. The pressure is on to sign agreements with countries that the EU has signed with. Turkey has to follow behind, as you rightly said, in the areas that the customs union covers.

The Chairman: Is that what is about to happen with Canada?

Dr Peter Holmes: I have not read anything about this, but I assume that the Turkish government will have to wait and see what is in the agreement with Canada and then start their own negotiations with Canada, which is not legally obliged to sign an agreement with Turkey but would in principle get market access into Turkey so that anything going into Piraeus could be put on a lorry. Whether the Turkish customs would in fact wave it through or find some technical reason for not doing so, I do not know, but there is no great incentive for Canada to sign an identical agreement with Turkey.

Lord Lansley: But in so far as the EU-Canada agreement is a comprehensive agreement including agriculture and services, conceivably would Turkey be able, as a non-EU member, to carve out those areas that are not part of its customs union relationship with the EU? Would trying to negotiate something different be unacceptable from the Canadian point of view?

Dr Peter Holmes: You would have to speak to the Canadians about that, but in principle it is possible. The Canadians would probably want to get the Turkish market for those things opened up to them, but I cannot answer that question, I am afraid.

The Chairman: Lord Balfe has questions on another aspect of Turkey.

Q89 **Lord Balfe**: I have some factual questions. First, what access do third countries have to free trade agreements with the EU and what access do they have to Turkey's market? Secondly, does Turkey retain the right to retain non-tariff barriers? Thirdly, 20 years after the customs agreement there are complaints in Ankara that it is now out of date, anomalous and affecting Turkey adversely, and that it needs to be either renegotiated or ended. Do you have any comments on the durability on these sorts of agreements? Would they need to be permanently renegotiated?

Dr Peter Holmes: That is a very difficult question. In principle, a country that has a free trade agreement with the EU should have the same access to Turkey in the covered areas as it does to the EU, but whether there are compliance issues I really could not say. With regard to Turkey's ability to impose non-tariff barriers in the covered areas, clearly Turkey has to have the same regulations as the EU whether or not it can operate non-tariff regulatory barriers in areas such as mutual recognition and testing certification. I do not know the answer, but it would be logical because mutual recognition is technically outside the customs union; it is additional to it. The mere fact that the EU and Turkey recognise each other's standards and infrastructure as equivalent would not necessarily mean that Turkey has to recognise equivalence with a third country.

It is quite complicated. In principle, the Turks have some wiggle room on anything that is not directly mandated by the customs union, but exactly how it would work is a very technical matter. For example, the use of exception clauses in the case of the EU having a free trade agreement with a country and Turkey not having one is a right that the Turks have but do not want to exercise. Clearly, as you say, as the nature of

commerce and value chains evolve, it is quite clear that the way in which rules of origin were done for third-country products in the 1990s, for example, is not the same as you would need today, so I do see the need for this to evolve, particularly considering the greater importance of services and the bundling together of services and goods. I am sure that is important.

The Chairman: Unless either of you wants to add something on the customs union dimension of this, we will move on to the European Free Trade Area (EFTA) and the EEA.

Dr Peter Holmes: Could I just add one reminder that customs unions are really about tariffs and the EEA is essentially about regulations? That is quite an important distinction.

The Chairman: That is a very good point.

Q90 **Baroness Donaghy**: What is your assessment of the appetite of the members of EFTA for the UK possibly to join EFTA and the EEA Agreement after it leaves the EU? Just to complicate things, do you think it would be possible for the UK to be a temporary signatory to the EEA Agreement as a transitional measure after negotiating its exit from the EU but prior to agreeing an FTA with the EU? If so, how would this work, and what would be the view of other EEA signatories? You have five minutes.

Dr Ulf Sverdrup: A brief question there. On the political appetite, first, I am not representing the Norwegian government; this is my assessment of it. I do not think they would be eager to go out and try to recruit the UK into the EEA, but the question then is: if it is served on the plate, would they take it? There is no tradition of expansion of the EFTA side of the EEA. That has never been done before. For instance, when the EU was about to enlarge, some countries in eastern and central Europe asked if they could join the EEA first, but the EFTA countries were reluctant to let them do that.

Secondly, although there are many people in EFTA countries who love the Brits—of course—and share a lot of cultural sentiments and orientations, et cetera, there are some very significant differences in size, geography, history, et cetera. That is a factor. In addition, there are differences of interests in agriculture, political interests and political orientation. There would be some concerns about that. Finally, there would be some concerns about the functioning of the EEA institutions, because one reason why the EEA has been fairly successful is because there have been few attempts to play against the rules. We have been playing within the rules in a very co-operative spirit with the EU. The optics of the EEA for the EFTA countries have been to use the agreement to promote integration, not as a step away from integration. This is a slightly different approach. There are some difficulties but, that said, at the end of the day if the EU and the UK think that this a nice and attractive political solution, I do not think they will object to it.

You asked me whether this would be a suitable transitional arrangement. I will make two points on that. First, my background is that I have been reviewing Norway's agreements with the EU. I was head of the secretariat

for this government report. One thing that struck us was the enormous complexity. Norway at that time had around 10,000 legal acts covering all ministries and all parts of society. Imagining that you could find a rapid solution to these problems in a short period of time seems very difficult. Looking for a transitional arrangement is probably a good strategy. Secondly, you should keep in mind that the EEA was at first signed as a temporary agreement. When you say "temporary", do you mean 25 years or two years? Transitional arrangements tend to stay on. Should I say something about the practicalities as well?

The Chairman: Yes, please.

Dr Ulf Sverdrup: In general, for more than 25 years Norway has been trying to square the circle—how to be inside but at the same time be outside. We have learned that you have to put an emphasis on political will and then there are some legal elements, and these things have to be balanced. In general, if there is strong political will and commitment from the parties, it is possible to find all kinds of solutions. Legally, there are two options for joining the EEA, but first let me remind you that the UK is already a member of the EEA; not everyone in the UK knows that. All EU members and the EFTA EEA countries are members of the EEA; they are contracting parties to the EEA.

In principle, there are two options. The first is to remain in the EEA as a contracting party but leave the EU. The second is to leave the EU, remain in the EEA and just switch sides and go into EFTA. This could be done automatically or you would have to re-enter. The first strategy of moving from the EU, while not into EFTA, but remaining an EEA partner, I do not think is feasible. In addition, it would be unacceptable to the UK, because you would have no voice in new legislation coming into the EEA because that would be a deal between EU countries and EFTA countries. The question then is how to switch sides from the EU into EFTA. There are no rules in the EFTA treaty regulating entry. It has to be via treaty change and based on unanimity. There are three different treaties you will have to enter into. The first is the EFTA treaty from 1960. There are four contracting parties to that: Switzerland, Norway, Iceland and Liechtenstein. In addition, you have to enter into an agreement on the surveillance mechanism in the EEA and the EFTA Court. There are three contracting parties: Norway, Iceland and Liechtenstein. Finally, you will probably have to make an agreement with the EU on the financial contributions.

The Chairman: The financial contributions to EFTA or to the EU?

Dr Ulf Sverdrup: Probably both. The financial contribution to EFTA is very modest, just running a small secretariat in Switzerland and Brussels. I am referring to the EEA grant mechanism to the EU. That is an agreement with the EU. The big question—and I am not sure about the answer—is: what would the voice of the EU be on this? Could the EU object to this? Will it be necessary to have some kind of ratification by the EU on moving from one side to the other of the EEA Agreement, from one pillar to the other? I am not sure about that. We have never seen this before so we are entering uncertain territory. But you should keep in mind

that Sweden, Austria and Finland were members of EFTA prior to joining the EU. That at least happened very smoothly.

The Chairman: Things that happen smoothly in one direction are not necessarily the same in the other. We have covered some of this territory—Lord Rees?

Q91 **Lord Rees of Ludlow**: I think my question has been mainly answered, unless you are prepared to hazard a guess as to how long joining the EEA might take?

Dr Ulf Sverdrup: First, I do not think it can happen before you have left the EU. It should not take too long. You probably need ratification and parliamentary approval in the various EFTA EEA countries. That probably could be done in a year or so. Some of the EFTA EEA countries might make some claims and have some desires about what they want to achieve. It could be fish or something else.

The Chairman: I heard someone at a seminar yesterday saying that if you go into EFTA and the EEA, you are substituting a veto by Slovenia for a veto by Liechtenstein, which might be important in financial services and elsewhere. Is there usually unanimity within the EEA?

Dr Ulf Sverdrup: Yes.

The Chairman: That is what I thought.

Dr Ulf Sverdrup: This is a very important point. The mechanics of the EEA are that the EU makes a legal act that it considers relevant for the EEA Agreement and presents it to the parties on the EFTA side; they then, speaking with one voice, accept it. So in reality the Prince of Liechtenstein has a veto power over Norway, and vice versa. They speak with one voice. You are right: there will be a veto power for the Principality of Liechtenstein.

Baroness Symons of Vernham Dean: Just to follow up the point about practicality, you imply that the UK would have to conclude all its business with the EU before even beginning a discussion with the EEA. Is that really the case? Obviously, you could not conclude an agreement with the EEA unless you had finished with the EU, but would it not be possible to have negotiations running alongside each other, and when one set is finished, you conclude the second one? This has real implications for how long this is going to take.

Dr Ulf Sverdrup: What I said was that I do not think you can enter into that agreement while being an EU member. I did not say that you cannot start reflecting upon these things. If you moved in the direction of the EEA, I am pretty sure the EU would be quite happy with that. There have been various studies from the EU about the preferred model of association for third countries. As seen from the EU, the EEA is the most preferred model. But of course that would not solve all the difficulties relating to free movement of persons, parliamentary sovereignty, et cetera.

Q92 **Lord Horam**: Thank you for what you have said already, Dr Sverdrup, about the EEA Agreement and so forth. It is extremely interesting. For the

sake of our thinking and clarity about what it implies, in your view to what extent does the EEA Agreement provide full access to the Single Market? Which sectors are accommodated and which are not? I am thinking particularly of services, which are so important to the UK. What would be the advantages and disadvantages to the UK of being in the EEA Agreement?

Dr Ulf Sverdrup: The EEA Agreement provides not only full access to, but membership of the internal market. It includes all four freedoms, as well as competition policy, public procurement, and other elements concerning the internal market. There are some exemptions. Norway is not part of the common agricultural policy, the common fisheries policy or the taxation policy. But even in those areas, for example on veterinary standards Norway is a member. When we reviewed Norway's relationship with the EU, we concluded that Norway is pretty much a member of the internal market, subject to around three-quarters of all EU legislation.

Lord Horam: Three-quarters?

Dr Ulf Sverdrup: Yes. Of course, there are different ways of measuring that, but Norway is deeply integrated in the EU. The EEA is not the only agreement Norway has with the EU. Norway has agreements in other areas, such as justice and home affairs, and security and defence. In total Norway has around 80 agreements with the EU in various fields. In a sense, it is this totality that makes up the Norwegian model.

Lord Horam: I noticed that in your paper to the European Council on Foreign Relations you concluded: "Like some local products with an acquired taste, Norway's odd ties with the EU should be tagged as 'not for export'". Could you elaborate on that?

Dr Ulf Sverdrup: It has worked for Norway, but you have to understand that Austria, Finland and Sweden left because they felt it was not attractive. Switzerland rejected it because it did not feel that it was attractive. You also have to understand the EEA as part of a domestic compromise in Norway. It is a deeply political conflict. As you know, political compromises are often not very nice. They are not elegant, they reflect special histories and concerns, and they tend to be very messy. Nobody really loves them but most of us can accept them because the alternatives are not so attractive. After joining the EEA, Norway considered applying for EU membership and it was rejected in a referendum in November 1994. The day after, the political leadership moved to, "Let's maintain the EEA and promote integration through that path". It has been a compromise.

The Chairman: Essentially, Norway has the same problem as us: the politicians wanted to be in the EU but the population did not agree, and that remains broadly the case.

Lord Liddle: And the business elite.

The Chairman: And the business elite, yes.

Dr Ulf Sverdrup: Yes, you have to look for second-best solutions and you have to find solutions that basically work for you, not ideal solutions. Another element that we have learned in Norway is that there is no free

lunch. You cannot have it all. You have to decide what you would like to have and play hard to try to get that, but at the same time you have to accept that others have legitimate interests as well.

Dr Peter Holmes: It is fascinating to hear what Dr Sverdrup says. I will add three small points. The first is a reminder that Norway is part of the Single Market but, because of rules of origin, there is incomplete access for goods that incorporate components produced outside the EU. I think this is less important for Norway and for the EU in facing imports from Norway, but the Japanese government in their recent submission pointed out that Japanese firms would risk losing the ability to sell freely into the EU if they had to comply with rules of origin.

Secondly, it is worth thinking about the comparison we looked at regarding the customs union issue. If you are looking at temporary solutions, it might be worth asking yourself whether staying temporarily in the customs union before making any new arrangement would make sense. Negotiating into the EEA and then out again sounds very complicated. One option would be to stay inside the customs union temporarily.

Thirdly, I had great difficulty finding this out about Turkey. I was reminded when Dr Sverdrup mentioned grants. In a true customs union, customs revenue is pooled. In looking at even a temporary arrangement, it is worth asking: what would happen to customs revenue in an EU-UK customs union? My understanding is that with Turkey there is no pooling of customs revenue, but it is a bit of an anomaly. Mercosur for a long time did not; it has now set up a revenue-sharing arrangement. The Southern African customs union (SACU) has a revenue-sharing arrangement. If you are talking about a customs union, you have to ask: what happens to customs revenue on third-country goods? Does it go to the place where the good is actually consumed or is it shared? Those are just some small extra points.

The Chairman: That is probably rather an important point, politically.

Q93 **Earl of Oxford and Asquith**: I have more questions on trade procedures. To what extent does being a member of EFTA limit member states' ability to independently negotiate FTAs with third countries? In particular, if the UK joined EFTA, would it be able to participate in existing FTAs with third countries, or would it be in the UK's interest not to do so or to negotiate bilateral FTAs?

Dr Ulf Sverdrup: There is no limitation on this. As an EFTA member you are free to make FTAs by yourself. Historically EFTA has tried to do things together because it is easier to be invited into negotiations if you have a slightly bigger market, and there are benefits from negotiating together. But in reality they can make agreements themselves; for instance, Iceland has signed an FTA with China, as has Switzerland. Norway also negotiated an FTA with China but the negotiations terminated after the Nobel Peace Prize was awarded to Liu Xiaobo. In terms of sequencing, there is a history where EFTA has negotiated free trade agreements after similar agreements have been signed with the EU. Recently, in the past 10 years, EFTA has signed some FTAs in advance of the EU; for instance,

I think the agreement with South Korea was signed a year or a year and a half prior to the EU's.

Most of the FTAs in EFTA have different elements to them. For industrial production, for example, EFTA agrees on it but when it comes to agricultural production and fisheries, that adds a bilateral element into the FTAs, because the Swiss do not sell that much fish and Norwegians are not that interested in international property rights, et cetera. So there are some differences. This also answers the second part of your question about whether the UK could join these agreements. I would say: no, there is not so much to join because there are also these individual agreements. In addition, third countries would probably like to look into it and see whether they would like to renegotiate those agreements.

The Chairman: Lord Wei has a specific question about the mechanism of EFTA.

Q94 ***Lord Wei***: What is the role of the EFTA Court? Can you comment on its efficacy? What opportunities, if any, does it provide for businesses to seek arbitration or dispute resolution if they feel that the principles of the Single Market have been violated to their detriment?

Dr Ulf Sverdrup: One of the unique elements of the EEA agreement is that there is this court system and the EFTA Surveillance Authority. It is like a micro-version of the European Commission and the European Court of Justice. You asked how the EFTA Court works. In principle, it should be more or less similar to the European Court of Justice, but it is much smaller, of course, with only three judges. Their caseload is much smaller and their offices are much smaller. The idea is that it should work to make sure that there is homogeneity. I think it has been fairly successful in doing that. It has established itself as an international court and is considered to be autonomous and independent, acting in the capacity of taking care of the EEA agreement.

There are three kinds of cases. The first is instances where there might be deviation between EEA law and EU law so it might have to make a ruling on interpretation. The second set of cases relates to whether there might be differences in geography that require different rulings in the EFTA Court. The third kind are cases that have not yet been clarified by the European Court of Justice, and that are first popping up in the EFTA legal system. Then the court has to reason: what would the European Court of Justice have ruled in a case such as this if it were presented with one? The idea is to make sure that there is some kind of homogeneity and to rule in the same way. The overall line is that the EFTA court has been trying rather forcefully to put forward this idea that the main principle is to secure homogeneity.

Lord Wei: To clarify—and this is probably a very technical question so I understand if it cannot be answered now—does the framework that the court uses ever have to draw on the European Court of Justice's framework of human rights, which in Britain is a big area of discussion, or are the cases generally more of a commercial or trade nature and you never really need to get into the issue of the European court's framework of human rights? That is a very technical point but of political interest

here.

Dr Ulf Sverdrup: You should probably ask somebody else but in general the court deals with all kinds of issues, not only economic or commercial law. It covers all the issues where the EEA is relevant—a wide number of areas.

Q95 **Lord Liddle**: On the question of the extent to which the court and the EEA interfere with Norwegian sovereignty, as it were, my understanding, on the basis of various discussions I have had with friends in the Norwegian Labour Party, is that Norway has pursued a more active industrial policy; for example, some elements of public ownership and using the sovereign wealth fund to try to ensure that Norway has some remaining competitive strengths in manufacturing, which is also a British concern. Has the state aid policy, or the court, tried to interfere with Norway in doing this as a member of the EEA?

Dr Ulf Sverdrup: As I said, Norway is part of the internal market and therefore also part of the EU state aid regulations. It is not the EFTA Court but the EFTA Surveillance Authority that looks into this. In the issues that are related purely to the EFTA countries, you have to notify the EFTA Surveillance Authority and it has to accept it. If it is a trans-border issue, the state aid competence will be decided by the European Commission. The rules are not more lax in Norway than in the EU. They are exactly the same.

Lord Green of Hurstpierpoint: Does that also apply to government procurement regulations—it would also be the EU framework, even if it is tagged differently?

Dr Ulf Sverdrup: Yes. Norway is part of the public procurement rules. It is part of the same tendering mechanism so if you have a procurement above a certain threshold you have to announce the calls throughout the whole EEA area.

Baroness Brown of Cambridge: Perhaps I might ask a supplementary question. Are there therefore different implications between a customs union and the EEA; for example, for a Government's ability to support a company's R&D? At the moment, we are constrained to pre-competitive research because of state aid issues. Would that be different if we were just part of a customs union?

Dr Peter Holmes: Again, it depends what you mean by being part of a customs union. The EEA is what I would call a regulatory union. It covers all aspects of regulation, public procurement, technical standards, and so on. In principle, a customs union covers tariffs. For example, Turkey is obliged to set its technical standards on the EU basis. It is supposed to have the same state aid and competition rules as the EU but that is because the customs union extends to that.

If we were part of the EU customs union, we would have all the rules of the EEA plus no ability to change tariffs. If I may follow up on one point that Dr Sverdrup and I corresponded about before this session, a member of the EEA is completely free to sign free trade agreements in so far as they affect tariffs. I think I am right in saying that you would not be free

to sign a free trade agreement with regard to non-tariff components as a member of the EEA—all these other things that we are talking about, such as public procurement. For example, you frequently hear complaints from developing countries that EU food safety rules are too restrictive: the famous aflatoxin in peanut butter case that came up some years ago. The UK as a member of the EEA, although it could reduce all its tariffs on Chinese products to zero, would not be able to relax the conditions under which Chinese goods, or anyone else's goods, could be imported and put on the market—in terms of technical inspections and so on—because the EEA gives free circulation to all goods put on the market in the EEA, and to put them on the market in the EEA you have to comply with EU standards. The agreement to include non-tariff elements in a free-trade agreement would definitely be restrictive. I think that was the point that Dr Sverdrup was making in our correspondence.

The Chairman: So, in effect, all this shadowing of EU legislation and procedures is not only within the EEA countries but also to some degree prescribes the FTA so that they can line up with third parties?

Dr Peter Holmes: The Chancellor recently gave an interview in which he said that the UK could sign an agreement with China like the New Zealand agreement. The New Zealand agreement says that any product—in a number of sectors, electronics in particular—certified in China by a Chinese inspector in order to be in conformity with New Zealand standards could then be imported into New Zealand. However, because of the nature of the free trade agreement between New Zealand and Australia, that product can then circulate freely into Australia. I suspect it is unlikely that as a member of the EEA, the EU would allow us to import stuff from China that had not been inspected according to EU norms rather than merely Chinese norms. It is very messy and complicated, but those are the things that one would have to look into in looking at the ability of the UK as a member of the EEA to sign third-party agreements. As I said, we had a brief discussion about this earlier.

Lord Green of Hurstpierpoint: Just to get something clear, in my mind at least, if the UK were a member of the EEA and signed a free trade agreement with China that set all the tariffs on Chinese imports into the UK at zero, transhipment to the rest of the EEA would be possible as a member of the EEA, but that would get stopped by the rules of origin procedure?

Dr Peter Holmes: You could move them freely, but you would have to pay the common external tariff on those goods.

Lord Green of Hurstpierpoint: So we are not bound by the common external tariff in respect of the UK market, but would be bound via the rules of origin in respect of the rest?

Dr Peter Holmes: Yes, and where it gets really complicated is where you have a value chain. If you have an electronic product that says "Made in Britain" but it contains 45% Chinese components, or a car made by a Japanese-owned company—Nissan, of course, is controlled by the French government, which is a twist—how do you separate these things out? The

component that says "Made in Malaysia" will in fact have had bits coming from China, and so on.

Lord Green of Hurstpierpoint: The realistic conclusion is that the UK would in fact be bound by the tariff rates set by the EU as a matter of practice, because of supply chains and rules of origin.

Dr Peter Holmes: That is something for Dr Sverdrup.

Dr Ulf Sverdrup: The main point is that if you look around the world, you see that tariffs are not a big issue. The big issue is technical barriers to trade.

Lord Green of Hurstpierpoint: Ten per cent in the case of autos.

Dr Ulf Sverdrup: Of course tariffs are important. But a big issue relates to non-tariff barriers to trade, standards and so on.

The Chairman: Have you covered your subsequent question, Lord Green?

Lord Green of Hurstpierpoint: We have talked about the ease with which the UK could become a member of the EEA, but of course the UK Government—or at least some of them—are publicly musing whether they would even want to take a single template, or whether they would want add-ons to or subtractions from the current EEA-type arrangement. Would it be right to presume that in the event of whatever the UK Government seek to negotiate, or do indeed negotiate in the end, is EEA-like but not identical—so it is either plus because we have sought to negotiate voting rights in certain key areas or minus because we have sought in particular to curtail freedom of movement in some way—this would significantly further complicate the process of joining the EEA and could conceivably lead to a need to revise the whole EEA arrangement?

Dr Ulf Sverdrup: Again, there are two options, if I understand you correctly. One is that the UK finds another platform than the ones we know of—more voting rights, for instance. The other EFTA countries would then be interested in that and would say, "Okay, this is something for us as well". The question is then therefore whether the UK should try to negotiate together with the others. The other element of your question is whether it is possible, if the UK enters the EEA, to attempt to renegotiate the EEA agreement in a significant way. So far in the past 25 years, the main framework of the EEA agreement has never been renegotiated. In some sense, that is a bit surprising because in the same period the EU treaties have been changed several times. So there has been a growing gap between the EU treaties and the EEA agreement, and the parties have tried to compensate for that.

There are three reasons why they have not attempted to renegotiate the EEA agreement. First, the EFTA countries basically think that they cannot get a better deal. You have to take into account that at the time when the EEA agreement was signed, the EU consisted of 12 countries and EFTA consisted of seven. At that time the EFTA countries, I believe, accounted for 50% of the EU's external trade—they were the EU's biggest trading partner. Now the pillars have shifted, so the EU consists of 500 million people and the EEA is only 5 million, so it is more asymmetrical. The

second reason is the sentiments in the EU. Why should the EU give voting rights to a non-member? Why would an EU member country accept being outvoted by a non-member? It is not very likely to be accepted. That said, there is the element of the Schengen agreement. In Schengen there is a slightly different mechanism for representation: non-EU members sit in on Council meetings. They have a right to share their views, listen in and talk, but they do not have a vote. That is slightly more representation than in the EEA, so that may be possible. In addition, of course, a revised EEA agreement has to be ratified by all member states, which is not very easy. So the assessment in Norway so far has been that we have what we have, and it is very difficult to negotiate it 'up' or 'down'.

The Chairman: Mentioning Schengen takes us on to freedom of movement.

Q96 **Lord Liddle**: There has been some discussion in the British press that under the EEA it would be permissible to negotiate some control on freedom of movement. Basically, we want to know whether you think that is possible and whether, as a member of the EEA, Britain could negotiate some kind of emergency brake, for instance, and how the example of Switzerland and Liechtenstein, which I believe are the countries for this, has all worked out, and what the lessons are for us.

Dr Ulf Sverdrup: That is also a big issue. As you know, the EEA provisions on free movement of persons are fairly similar to the ones in the EU. To that I would just add a small footnote: you have to bear in mind that free movement of persons also relates to the free movement of services. A lot of people moving around are employers in a company, so suspending the free movement of persons will probably also include the suspension of free movement of services.

There are two differences between the rules on the free movement of persons in the EEA and those in the EU. The first relates to non-EU citizens, or those from third countries, and the second relates to Union citizenship. The rules for non-EU citizens, or those from third countries, are not part of the EEA agreement, but the EFTA states incorporate elements of that through Schengen and the Dublin agreement. On Union citizenship, it is a bit trickier because, as you know, the Union citizenship directives give rights to people moving around as citizens, not just as economic actors operating in a market. This was not included in the EEA agreement because, politically speaking, it would have been a bit strange to give Union citizen rights to citizens who are not members of the Union.

For the last 10 years there has therefore been a gap in the legal framework in the EEA agreement and the EU on this. During that time the court has tried to look into that gap. In my understanding, the general policy of the EFTA court has been to make rulings in the direction of homogeneity. So although there are formal differences in the legal framework on the free movement of persons in the EEA and the EU, in reality they are interpreted similarly. They parallel the developments in the EU.

You also asked about the emergency break in the EEA agreement: Article 112. This is a standard safety clause, and basically says that in certain

circumstances a country can move back from some of its obligations. Such a country has to notify its partners and its measures should be temporary and proportionate, et cetera. I do not know how frequently this special clause has been used. I suspect that it was used in relation to suspending the free movement of capital in Iceland after the financial crisis.

I am also aware that is was used in relation to the free movement of persons in Liechtenstein. As you know, when Liechtenstein entered the EEA agreement they asked for a special exemption on the free movement of persons. Their argument was that Liechtenstein is a very small country but, at the same time, has a very high proportion of non-Liechtensteinians working there. They said that they had to have some restrictions. They were granted a temporary exemption from the free movement of persons. This expired in 1998 and the EU would not extend it further. Then Liechtenstein used Article 112 to say that they needed a limitation on free movement of persons. But when the EU was enlarged in 2004, the parties made some sort of adjustment as an annex to the EEA agreement—you will have to check on that—basically accepting that this exception is going to be integrated permanently into the agreement.

In general, I do not think the Article 112 strategy is designed for countries that want to be left out of the free movement of persons.

The Chairman: Thank you very much for all your comments. We are right at the end of our time so perhaps you could make any final comments that you may have.

Dr Peter Holmes: Very quickly on free movement, it is worth looking at the WTO obligations. We would still have whatever Mode 4 GATS commitments to allow people to come in. That is not relevant at the moment for European citizens but, if there was no agreement on free movement, those rights would still remain. It is worth checking what the implications of that would be.

Dr Ulf Sverdrup: I have just a few short remarks. First, Norway's experience has clearly indicated that it is possible to be outside the European Union. That is the good news. Secondly, it is fairly easy to get out of representation but getting out of integration is a slightly different and more difficult issue. Thirdly, it will require hard work. There will be no free lunch and it will probably be very messy and technically complicated. Therefore, searching for second-best solutions, compromises and transitional arrangements would be of critical importance.

The Chairman: Thank you very much for that general indication of the complexity of the Government's task which we are due to scrutinise. I think we all realise that these areas are a bit complex. You have brought clarity to the complexity but we have probably ended up realising this morning that it is even more complex than we thought an hour ago. It has been very useful to us, and if you think there is anything more that we should take into account, please send us it in writing. Thanks a lot for your time and for your written material. It has been a very worthwhile session.

Dr Peter Holmes, Reader in Economics, University of Sussex – Supplementary written evidence (ETG0007)

1. **You mentioned in your oral evidence an example of a case between India and Turkey which demonstrates the incomplete nature of the Customs Union. Please could you summarise this for us?**

Basically after signing the Customs Union with Turkey, the EU insisted that Turkey apply the same NTBs as itself to trading partners. Under the WTO Multifbre Agreement the EU still had quotas on Indian textiles and clothing and insisted Turkey put on equivalent measures. India challenged these as an unauthorised restriction of trade. Turkey claimed this was made inevitable by the signing of the CU with the EU. Otherwise Indian goods could enter the EU via Turkey. But in exploring that facts the WTO Dispute settlement panel found that there were so many continuing barriers between Turkey and the EU that even if cheap goods came into Turkey the EU could use the customs controls on the Turkey EU border to stop this "trade deflection". This highlighted the gaps in the CU.

(See WTO DISPUTE DS34 Turkey — Restrictions on Imports of Textile and Clothing Products).

2. **You said that "The general principle is that Turkey has to sign agreements with countries that the EU signs agreements with, but those countries do not have to sign agreements with Turkey." Could you clarify what that means in practice?**

The CU agreement obliges Turkey to apply the same trade policy as the EU and enjoins it to sign FTAs with any country that the EU has signed one with. But there are no equivalent provisions in deals with other countries to force them so sign FTAs with Turkey. Not all countries the EU has signed FTAs with have signed FTAs with Turkey. Where the EU has signed a deal but Turkey not, it appears to be the case that Turkey and the 3rd country continue to levy tariffs on each other's goods. If the EU signed a TTIP FTA, then until an equivalent Turkey-US FTA any US goods imported into the EU would be entitled to free circulation and hence duty free access to Turkey, but Turkish goods would not be entitled to duty free access to the US.
(See World Bank Report No. 85830-TR Evaluation of the EU-TURKEY Customs Union (2014), para 49 p.25)

See World Bank Report No. 85830-TR Evaluation of the EU-TURKEY Customs Union (2014)

"49. However Turkish firms have not received automatic reciprocal access to some of those markets with which the EU has negotiated FTAs, leaving them at a competitive disadvantage to EU exporters, weakening Turkey's trade negotiating position with these countries and causing trade deflection that risks the imposition of origin controls that could undermine the benefits of the CU. Where the EU has provided leverage to Turkey in concluding FTAs with third countries

that might not have otherwise happened in the absence of the CU, this has brought important benefits. However, in those cases where the EU has concluded an FTA with a third country but Turkey has not, exporters have an incentive to transship goods via the EU resulting in trade deflection. For imports of cars from Mexico, Turkey has introduced a protection measure based on ROOs to reduce trade deflection but the use of such measures, especially if they were to proliferate, undermines one of the key advantages to the CU discussed earlier: the elimination of costly origin requirements. Turkey has also decided to apply additional customs duties for some textiles products originating from some countries outside the EU and EU FTA partners. The additional duties vary for countries benefiting from the GSP scheme, LDCs and others. In order to apply these differentiated duties, origin controls are being conducted based on customs declarations but no physical check is yet being conducted. Market access opportunities have also been lost for Turkey. The main ones to date have been in Algeria where Turkey has lost market share vis-à-vis European firms, Mexico and also South Africa (Box 4). In 2012, Turkey purchased US$1.3 billion worth of goods from South Africa while selling US$382 million. It imported US$867 million worth of products from Mexico during the same period, but exported US$206 million there. It exported US$1.8 million worth of non-energy goods to Algeria while importing US$2.6 billion (Daily Hürriyet, 2013). Turkey also faces preference erosion in the EU market as the latter signs FTAs with countries that actively compete with Turkey e.g. Chile, Morocco."

http://www.worldbank.org/content/dam/Worldbank/document/eca/turkey/tr-eu-customs-union-eng.pdf

25 September 2016

Dr Peter Holmes, Reader in Economics, University of Sussex – Supplementary written evidence (ETG0011)

The Customs Union vs *A Customs Union*: possibilities for the UK and the EU[21]

Many commentators have suggested that the UK might continue to be in the EU Customs Union whilst outside the EU.
This note tries to elucidate the implications of this. It suggests that remaining within the EU Customs Union for more than a short transition period is hard to envisage and what is in principle available is to have a Customs Union with the EU Customs Union.

The example of this is Turkey and this note argues that such an arrangement would be highly unsatisfactory. It is in principle possible to imagine a Customs Union arrangement including the EU and the UK that was closer to the status quo than to the Turkey arrangement.

What is the EU Customs Union?

The EU's Customs Union encompasses its member states plus Monaco and the Isle of Man. Strictly speaking Andorra, San Marino and the Vatican City are not part of the Customs Union, but San Marino is treated as part of Italy's Customs territory. [22]
The Rome Treaty stated that the EU (then EEC) member states would form a Customs Union. The Customs Union is not a separate entity that EEC member states all happen to belong to.

But the primary non- EU territory linked to the EU in a customs union relationship is Turkey. Turkey is not part of the EU CU. Rather it has a Customs Union agreement with the EU that differs sharply from the EU Customs Union itself.

If the UK left the EU, it is extremely hard to see how it could be part of the EU CU, except as part of a transition process. Actual EU Customs Union membership requires full application of the EU's common external tariff, including preferences and services. (The EU does permit national variations in services however where individual national variations are possible in GATS schedules). Within the Customs Union all EU originating goods and imports that have paid duty have the right of free circulation, so there are no rules of origin within the EU. There is no possibility of anti-dumping duties etc. Since the EU is also a "Regulatory Union" there is no scope for goods being stopped for technical inspections: the direct effect of EU law means that EU technical norms must be applied in the

[21] A note of warning: the author is not a lawyer and this note represents personal opinion only. I am grateful to colleagues in the UK and Turkey for advice, but only the author is responsible for errors
[22]For details see "Territorial status of EU countries and certain territories" http://ec.europa.eu/taxation_customs/business/vat/eu-vat-rules-topic/territorial-status-eu-countries-certain-territories_en

production process of goods. And Customs revenues on goods from third countries must be handed over to the Commission. The EU Customs Union is defined in the Treaties as being made up of members of the EU. Of course it is imaginable to think of a relationship which replicates the obligations of members of the EU without having any of their rights. It is a little hard to see why this would be desirable.

As long as we stayed in the Customs Union or in an equivalent relationship we would have to follow all changes in trade rules set by the EU. Applying these conditions would constitute de facto continuing membership of the EU. Before 1993 the member states of the EU had a Customs Union with a common commercial policy (CCP)[23] but continued to have customs borders. The borders ended when the single market rules came into force. Logically it is possible to have a Customs Union with a CCP and no tariffs on internal trade but to retain technical inspections at the border. In the EU the two types of union have been merged.

The Turkey EU Customs Union

Turkey however is not part of the EU Customs Union, but has a Customs Union with the EU. This Customs Union is very different from the EU's own CU. It excludes agriculture. This alone means that there have to customs posts at the border. It includes a great a great many general exceptions to the principles of a customs union. It also excludes services and free movement of labour. There is no sharing of customs revenue.[24]

The rules of the Customs Union are set out in a 1995 document that lists the rights and obligations of both parties.[25] It removes all tariffs between the parties and also provides for harmonisation of external trade rules.
It provides in Art 12 :
"*From the date of entry into force of this Decision, Turkey shall, in relation to countries which are not members of the Community, apply provisions and implementing measures which are substantially similar to those of the Community's commercial policy*"

"Substantially similar" means there can be exceptions.

Andre Sapir recently observed: "As a result, the EU-Turkey customs union is in fact a hybrid between a genuine Customs Union and an FTA. This is demonstrated by the fact that Turkey has adopted the EU's common external tariff for most, but not all, industrial products and only for some agricultural products; it applies additional customs duties for some textile products from countries outside the EU and the EU's FTA partners; it applies trade defence

[23] Technically there were some exceptions on quotas and pre 1990 on Trade with East Germany.
[24] For detailed information on the EU Turkey CU see Bringing EU-Turkey trade and investment relations up to date?
http://www.europarl.europa.eu/RegData/etudes/STUD/2016/535014/EXPO_STU(2016)535014_EN.pdf
I am grateful to the authors of thois document for advice
[25] DECISION No 1/95 OF THE EC-TURKEY ASSOCIATION COUNCIL of 22 December 1995 on implementing the final phase of the Customs Union (96/142/EC)
http://www.avrupa.info.tr/fileadmin/Content/Downloads/PDF/Custom_Union_des_ENG.pdf

instruments, such as anti-dumping and countervailing duties, in a totally different manner (for different products and countries) than the EU; and it has not concluded FTAs with some EU FTA partners (including Mexico, South Africa and Ukraine)." http://bruegel.org/2016/08/should-the-uk-pull-out-of-the-eu-customs-union/

Anti-dumping duties are important. According to a recent World Bank study[26] for the European Commission, only about 15% of Turkish and EU AD investigations were on the same product (para 74) in the period 1995-2011.
The EU in 2014 had AD duties in place or proposed on $500m worth of Turkish exports to the EU and Turkey had actual or proposed AD duties on $1bn of EU exports. Over the period 1995-2011 the World Bank found that of "219 different products that Turkey investigated under its antidumping policy during 1995-2011, just seven (three percent) targeted exports from the EU. Approximately nine percent of the total number of products that the EU targeted with antidumping investigations over 1995- 2011 were aimed at Turkey. "World Bank para 75.

Article 16 of the Customs Union text states that Turkey "will" sign FTAs with countries that have signed agreements with the EU, but this does not require third countries to sign such agreements, and as Sapir notes there are several important exceptions. In the case of Korea, the Turkey Korea agreement was signed several years after the EU-Korea deal. There is no obligation on a third country partner to sign an FTA.

Where the EU has signed an FTA but Turkey has not, there is a risk of Trade Deflection. Goods may be imported into duty free the EU and sent on duty free into Turkey. According to the World Bank: "For those countries with which the EU has agreed an FTA but Turkey has not, imports can also enter Turkey duty-free via trade deflection. But for those imports arriving directly at Turkish ports, import tariffs are charged", (Fn 16 p. 24)[27].Obviously this would induce third countries to send goods in transit via the EU. Mexico has apparently refused to sign an FTA with Turkey. The World Bank reports (para 74) that in this case as in several others Turkey has been able to invoke a little known exemption clause Article 16(3) which allows Turkey to put import surcharges on third country goods in such circumstances.

The EU can introduce measures against third country goods coming via Turkey. This led to a very important WTO dispute settlement case brought by India against Turkey[28]. After the Customs Union Turkey under EU pressure had introduced quotas on textiles from India to come into line with the EU's MultiFibre Arrangement quotas. India brought a case at the WTO. India won with the Appellate Body in effect saying the EU Turkey Customs Union had so many barriers that if the EU wanted to stop trade deflection via Turkey it had many border controls at its disposal. In effect it implied the EU-Turkey Customs Union was not a true Customs Union in WTO terms.

[26] http://www.worldbank.org/content/dam/Worldbank/document/eca/turkey/tr-eu-customs-union-eng.pdf
[27] In principle this violates the obligation to harmonise tariffs but appears to be the practice.
[28] DISPUTE DS34 Turkey — Restrictions on Imports of Textile and Clothing Products, https://www.wto.org/english/tratop_e/dispu_e/cases_e/ds34_e.htm

The EU-Turkey Customs Union is not a "Regulatory Union"

The 1995 agreement abolished customs duties but not technical barriers. The Customs Union agreement did not create a Regulatory Union as did the EEA agreement. Turkey was required to harmonise technical regulations with the EU, but the EU did not automatically recognise Turkish compliance and grant exemption from controls. A series of Mutual Recognition Agreements on conformity assessment starting in 2006 has gradually allowed more Turkish goods to enter the EU without further technical inspections, but an excellent survey by Togan notes that these agreements facilitate entry only where the EU has harmonised its rules internally. Where separate national rules are applied by member states, the customs authorities can insist on the right to inspect Turkish goods[29].

Clearly for the UK, at the point of Brexit, all our standards would still be aligned with the EU, but new EU rules would not automatically be incorporated into UK law and on exit the EU's compliance would cease to be supra-nationally enforced without an arrangement such as the EEA's EFTA court. For Turkey compliance is enforced by Turkish courts and the threat of trade sanctions.

The contrast with the EEA.

The EEA is a regulatory union but not a customs union, so that there are customs duties on third country goods and any goods whose import content does not meet the rules of origin. So at the borders with Norway Iceland and Liechtenstein goods are checked for origin but not for compliance with EU technical rules, because membership of the EEA implies full legal compliance with all EU rules.

By being a Free Trade area not a Customs union the non-EU EEA members have the right which Turkey does not have to sign whatever Free Trade Agreements they wish. But this only applies to tariffs. As we have seen, regulatory measures are extremely important and a UK in the EEA but not the EU could not sign any agreement that lowered technical barriers to trade with the EU. A recent Bruegel paper notes:

"What would be the consequences for the EU of China signing an FTA with the UK while the UK maintains at least an FTA with the rest of Europe, if not full participation in the single market? This 'status quo' scenario should raise concerns for the EU about whether Chinese exports could use the UK 'back door' to enter the EU market without China signing a bilateral FTA with the EU." [30]

This would not be allowed by the EU. Norway is thus restricted in its ability to sign "deep" trade agreements with third countries that include relaxation of technical barriers and so too would the UK be. .

What are the overall Implications for the UK?

[29] S Togan "Technical Barriers to Trade: The case of Turkey and the European Union" Journal of Economic Integration 2015 March;30(1) :121-147

[30] A Sapir "What consequences would a post-Brexit China-UK trade deal have for the EU?" http://bruegel.org/2016/10/what-consequences-would-a-post-brexit-china-uk-trade-deal-have-for-the-eu/?emailid=577bc2bcc0350c0300f8b09d&ftcamp=crm/email//nbe/Brexit/product

Being part of the EU Customs Union but not in the EU makes no sense. It is logically possible to have an arrangement with the EU that mimics the effects of the current situation whilst denying the UK any rights as a member. This is imaginable as a transition arrangement but would clearly need to be negotiated as such an arrangement does not exist so far.

In principle the UK could sign a customs union agreement with the EU as Turkey has done, but I would argue that this is wholly unsatisfactory from a trade perspective. The Turkey Customs Union is not really a full CU. It does not allow fully free trade in both directions. It takes away the right to have an independent trade policy with third countries, but allows third countries that have signed an FTA with the EU to enter the Turkish market unless special derogation provisions are used. This would surely be unacceptable to the UK.
A closer customs union arrangement between the UK and the EU is not unimaginable

By contrast the EEA agreement offers market access to the EU free of technical barriers, but duty free access only for goods meeting origin rules. It necessarily means full supranational implementation of EU acquis, as well as free movement of labour. The EEA appears to allow more freedom to sign FTAs with third countries but this is only partially true as respect for EEA regulatory rules means only tariff barriers can be negotiated with third countries.

12 October 2016

Professor John Manners-Bell, Chief Executive, Transport Intelligence Ltd, and Dr Christos Tsinopoulos, Senior Lecturer, Durham University – Oral evidence (QQ 30-39)

Evidence Session No. 4 Heard in Public Questions 30 - 39

Thursday 15 September 2016

Watch the meeting

Members present (External Affairs Sub-Committee): Baroness Armstrong of Hill Top (Chairman)[31], Lord Balfe, Baroness Brown of Cambridge, Lord Dubs, Lord Horam, Earl of Oxford & Asquith, Lord Stirrup, Baroness Symons of Vernham Dean

Members present (Internal Market Sub-Committee): Lord Whitty (Chairman), Baroness Donaghy, Lord Green of Hurstpierpoint, Lord Lansley, Lord Liddle, Lord Rees of Ludlow, Lord Wei

Examination of Witnesses

Professor John Manners-Bell, Chief Executive, Transport Intelligence Ltd, and Dr Christos Tsinopoulos, Senior Lecturer, Durham University

Baroness Armstrong took the Chair.

Q97 **The Chairman**: Good morning everyone, and welcome to our two witnesses. I just remind the witnesses that this is a public session, so it is on the record and there will be a transcript, but we hope that will not make you feel that there are things you cannot say. I would also just say that inevitably in sessions such as this, Members come but then need to leave, as there is other business going on in the House. If people leave, that is not about you as witnesses but because they have other commitments. We get used to it, but very often people who are visiting wonder what is going on, so I just thought I would mention that.

We are trying to get a better understanding of the challenges in renegotiating trade in both goods and services. The External Affairs Committee is looking particularly at goods, while the Internal Market Committee is looking mainly at services. Inevitably, as we have just been hearing, there is some crossover, and we come together so that we can

[31] Baroness Armstrong of Hill Top was chairing in place of Baroness Morris of Bolton, who was unable to attend the meeting.

deal more effectively with the whole issue. That will be reflected in the reports that come out. This is a learning exercise for everyone. It is not that we expect you to have the answers; it is that, if nothing else, we need greater clarity on the right questions to be asking the Government.

As you know, we have a range of questions. Members will come in to ask particular questions, but I wanted to start by asking what you think the overall effect or impact of Britain's decision to leave the European Union will be on the supply chains of the UK's non-financial services industries and of UK manufacturers. Perhaps you could just give us an example so that we can understand it more easily. Which procedures of trade—tariffs, administrative procedures, non-tariff barriers, rules of origin, customs controls and so on—would be the most burdensome, if we have to change? We are happy for either of you to answer. Because we are fairly short of time, if one person has said what you would like to say, we hope you leave that, but we are happy for you to both come in and contribute.

Professor John Manners-Bell: Thank you very much Lord Chairman, and the other members of the Committee, for allowing us this opportunity. Before I answer the question, I will say very quickly that I have worked in supply chains rather than in trade, and the two, as you will all know, are very different. The supply chains that we are used to in the industry are hugely fragmented virtual networks. Over the last 20 years, there has been an unbundling of industrial processes, and outsourcing of them, right around the world, not just within Europe. So the supply chains that we recognise are already very globalised. If you look at the figures that are available from Eurostat or other trade statistics bodies, you will see that probably a third of inputs of intermediate goods are coming from around the world. So, in fact, supply chains are already operating very effectively both in the EU and outside it.

My colleague will probably talk a little bit about the automotive sector, but that has a range of different structures in place, including domestic suppliers supplying the automotive sector, European suppliers and, especially in the case of the Japanese manufacturers based in the UK, suppliers from Japan, China and the US. So the logistics and supply chain industry in the UK is already hugely flexible, very agile, and able to make decisions and to work within the structures that are being provided.

Over the last 20 years, or beyond that, right the way back to the beginning of the WTO, we have seen tariffs being reduced. We do not see tariffs as a particularly major issue at the moment—although we may come back to that later in the session—but non-tariff barriers are the key concern for everybody.

You asked about the areas in which we would like to see some sort of clarity or some sort of solution. We certainly do not want to see non-tariff barriers such as rules of origin or other areas of standardisation being rolled back, but I do not believe that is going to happen, because European standards are already in line with international standards, and manufacturers that move goods around the world are already working in line with those international standards, as are UK manufacturers. I may have a rosier and more confident picture than many, but as to where we

are in forging a new relationship with the EU, we already have everything in place when it comes to customs procedures and harmonisation and standardisation for products. I see negotiations probably being a lot easier, if the will exists, than many people think.

Dr Christos Tsinopoulos: Thank you very much for inviting me. My views on the overall assessment are not far from those of my colleague's here. The UK sector has in general built up significant strengths over the last few years. I have been visiting various companies—I am an academic, so I tend to visit companies rather than doing what my colleague does—and their main concern has always been about tariffs, barriers, challenges to trade and so on.

The UK's strengths come in several sectors. I am going to talk about the automotive sector because in preparation for this meeting I talked to several of my contacts at manufacturers in the automotive sector. They have their own concerns and views but I presume those will come up later in the questions that we will be asked. The point I would make, however, is that we are talking about supply chains, which tend to be as weak as their weakest link. Sometimes the weakest link is in the UK, sometimes it is outside the UK; sometimes it is in the EU and sometimes outside the EU. The issues like those suggested by my colleague are important: about standardisation and making sure that you can identify where, for instance, that weakest link exists and what you can do to build on it. But all my comments in the past, which very much echo those of my colleagues, were that those aspects of standardisation in common legislation that goes across is something that a lot of the manufacturers I have spoken to see as a significant benefit.

Another key aspect, which again echoes some of the comments that my colleague made, is associated with the degree of integration of global supply chains. One thing that many supply chain managers would tell you is that, when a supply chain is well integrated, it performs better.

If you want part of my overall assessment, it is that if that integration is compromised then there is the potential for a hit on competitiveness. I am also optimistic—this is my guess—that this is not going to happen. There will not necessarily be a hit on the weakest link in the integration aspects of the supply chain.

The Chairman: Can you give us any direct examples of where you think there might be problems that we should look at?

Professor John Manners-Bell: As I mentioned before, there may be on the rules of origin and other elements of non-tariff barriers. Having said that, to give a little summary of the rules of origin, they would mean that any parts or components which are imported into a country would have to have some sort of certificate if they are to be re-exported to the EU. For example, if they were to come into the UK from any country around the world, such as China, then that part may need to have a certificate of origin and if the overall amount of imported goods from non-EU countries made up more than a certain proportion of that particular good, it would have a tariff imposed on it. The problem with that is that, if the system becomes very bureaucratic and administrative, it can add a large amount

of costs to the overall process of the export of the good. I think that some people have estimated it as anywhere between 5% and 15%, in which case the exporter may decide that it is easier to accept a tariff rather than go through all the administrative burden of getting certificates of origin for all the different parts of these products, which are then assembled and re-exported. So in theory—this is what a lot of the literature has been warning about the impact of Brexit— that could be a major cost. However, we could look at a trade deal with South Korea. The negotiations for that started in 2007 and ended in 2009, so there were only two years of negotiation, and it then came into force two years afterwards in 2011. But rules of origin and non-tariff barriers were all integrated into that agreement. It can be done. We are always thinking about it from the UK perspective, thinking that others will insist on this burden, but to be honest it is more an issue for EU exporters to the UK because of the trade deficit. So if they insisted that we must have rules of origin—other non tariff barriers (NTBs) on our goods—presumably the reverse would apply as well. In which case, there would be bigger hit for EU exporters. I cannot see that being an acceptable state of affairs for the major European manufacturers such as BMW, Mercedes and the like.

Dr Christos Tsinopoulos: The only thing that I would add that is that they are looking to expand into the same areas as well, so maybe they will see the same levels of growth elsewhere. However, I would add that the manufacturers and supply chains I have spoken to seem to have two levels of concern. One is the immediate one associated with things such as the exchange rate, for instance. That has been a blessing for some and a curse for others. That is clearly not only an issue of Brexit. Fluctuations happen all the time so it is not something that should be of immediate concern, but it is of immediate concern to those who are in it at the moment. Some love it and clearly some hate it. So one thing is the exchange rate fluctuation. The other is the uncertainty over these past months. You were asking about manufacturers and the motor manufacturers in the north-east. Some contracts are coming up for renewal, for instance. There is a concern that they have to make long-term decisions in a state of uncertainty. For instance, decisions have to be made by Christmas and they do not know what the rules of the game will be. Those are the immediate concerns. The longer-term concerns are very much associated with tariffs. Tariffs are the main thing people have spoken about. They do not want any tariffs or any kind of barriers associated with trade. They have been used to low-tariff trade. The other thing that has been mentioned a few times—and you have probably heard this on various occasions—is associated with free, easy movement of labour, particularly skilled labour. You have probably heard this story again and again but there is a real shortage of skills, particularly engineering skills. A lot of engineering companies are doing a lot to fix that, but that is a long-term process of engagement and quite often the free movement of labour has allowed people to sort this out. That is another message that I am receiving. There are shorter-term problems such as exchange rates, and the level of uncertainty that we have at the moment, but also longer-term problems with what to do about skills and tariffs.

Q98 **Baroness Brown of Cambridge**: Thank you. I would like to explore a little more with you which sectors you think might be most and least affected. Of course, you have already mentioned the automotive industry and I would be interested to hear a little more about that. We would also clearly be interested in aerospace, which is particularly critical to us. Offshore wind is an interesting area where we are rapidly developing the world's largest installation base for offshore wind and looking to become a significant part of the supply chain for that—many of the suppliers being Siemens in Europe. Will it affect our ability to bring in jobs and investment in support of that industry? You have already mentioned the north-east and I am also interested. As a result of some of this, are there any particular geographical areas in the country that could be more significantly affected? I have lived for many years in Birmingham where we make a large percentage of the engines for the European automotive industry. If there were a problem there, it would have a big impact on the West Midlands economy. Are there other particular areas of concern? Sorry, that is quite long and complex, but if you could address parts or all of it, I would be delighted to hear more.

Professor John Manners-Bell: I will certainly let my colleague here deal with some of the automotive industry, as he is an expert on that particular sector. For my part, I have taken two sectors that he did not mention which I think will be most effective. The first is on the agriculture side—food products, for example. As a country we import 40% of our food requirements; a large proportion of that comes from France and Ireland. So any change in the trade system would obviously have a significant impact. On the world market, agricultural food products are much lower than they are available within the EU due to the barriers around the edges of the EU, so I imagine that if we are moving to free-trade areas with certain big producers such as Brazil or the USA in some sort of hypothetical post-Brexit scenario, we will see far more intercontinental movements of goods, which will have some major benefits for shipping lines. It will also have a major benefit for airlines in the movement of perishable goods, and the refrigerated movement of goods will increase. We will see consequent impacts on ports and airports, which will become the gateways to these intercontinental movements of goods.

On the flipside, it will impact on cross-channel movements, in particular on the movements at the moment between the UK and France, where we will certainly see fewer volumes in this particular scenario. If we see tariffs imposed on food products coming from the EU—to go back to my original point, I do not think that we will—this may well be of benefit to UK domestic producers. So overall there would be some major changes, not only to agricultural supply chains but to the logistics providers that serve them, and to the transport infrastructure that will be required to facilitate the movement of these goods.

Baroness Brown of Cambridge: In the context of us needing to reduce our CO_2 emissions to meet our climate change targets, and of course the significant challenge that both aviation and shipping deliver in that area, do you not think that increasing costs associated with the CO_2 emissions from those modes will be a problem?

Professor John Manners-Bell: Yes, that is an excellent point, which I did not raise because I was not sure whether it came within the remit of this Committee. Yes, that will certainly lead to higher CO_2 emissions from the shipping and air cargo movements. This is already a major issue for those motor transports, and it would be exacerbated.

Dr Christos Tsinopoulos: I tried to prepare for this question and to identify a number of sectors that might be more directly affected. I would touch on some sectors specifically, but there is another aspect, which is some of the research that we have done in Durham. I would like to go back a step and focus on some of the ways in which the supply chains are structured. Many of us think of supply chains as streamlined and that they produce a high volume of goods, and all that kind of stuff, and of course that is a big factor in supply chains. But a big proportion of supply chains do not do that. They are based on projects; they make large, project-based equipment, such as the construction of a house or a building. Looking at it like that, I would not consider quite a few of the project-based supply chains a threat, because they are largely based on location; you are trying to supply customers who are relatively close to you. For instance, many of the manufacturers that we have done a lot of work with in recent years supply construction companies in London, for example, so they are not necessarily affected directly by decisions like this. I guess your question is more about the high-volume supply chains such as those in the automotive industry—fast-moving consumer goods and that kind of thing. Whether and how those would be affected would depend not just on the location of the factory but on the decision about where, or where not, to produce a new product. I do not have a personal prediction about any immediate decision by any company to shift production elsewhere simply because the UK has voted to leave the EU. My concern would be about a decision being made at some point in the future about where to produce a new model. These are already very competitive decisions. Even within the EU, they are significant competitive decisions. When a decision is made within the EU, it is usually based on the economics; now, you have politics in there as well, and I do not want to go there.

Baroness Brown of Cambridge: So what about the Nissan situation?

Dr Christos Tsinopoulos: Yes, the Nissan situation is just such a decision, and a lot of those will be coming up in the future.

There is another question which I am sure you are asking, which is: how long will it be before we see the impact? I think that that question should be answered by looking at the life cycles of the products that are manufactured across the UK. They will vary across sectors and across different situations. I am not necessarily pessimistic but that would be my immediate concern—whether, in the current environment of uncertainty, a manufacturer would simply say, "I want to go to a more certain environment". It is about decision-making more than anything.

To summarise, focusing on sectors is of course important but you might also want to focus on the different structures that different supply chains have—project-based supply chains versus high-volume supply chains, and new products versus older products—and maybe deal with them in a

slightly different fashion rather than have one monolithic approach to supply chains.

Q99 ***Lord Wei***: I just want to follow up on that with a hypothetical scenario. For example, where the negotiations are not really completed in time, we go to a WTO scenario and industry gets affected by tariffs as we export into Europe, could the Government put in place emergency temporary measures to unilaterally remove tariffs on import materials for our manufacturers, such as our car manufacturers—for example, on imports of steel or whatever—such that they could try to cushion the impact of immediately having tariffs imposed on exports to Europe?

Professor John Manners-Bell: Obviously, as the Committee members are very well aware, there would be no punitive measures by the EU because that would be against WTO rules. So far as I can see, the UK Government could do whatever they wanted. If they wanted to lift tariffs on a particular commodity, acting unilaterally, there would be no issue with that. Straying on to the political side of things, if they did that they would throw away whatever leverage they had in terms of passing on the pressure to European producers to force the hand of the EU negotiators. So the European manufacturers have more to lose in this than the UK manufacturers. We have to be very confident and assertive on this in our future trade relations and trade negotiations with the European Commission. That is the nature of trade with this country—we have a trade deficit; they need us more than we need them. I do not think that it would come to that.

Going back to the South Korean example, South Korea managed to negotiate a deal from scratch in two years where there were large tariffs in place—really significant levels of duty were imposed. There were also significant non-tariff barriers, which they needed to come up with a new way of reducing, and they did that in two years. As far as I can see, we need to move on to this stage very quickly.

I just want to come back to the point about confidence and certainty, which my colleague has been talking about. We need to move on. The worst thing about this whole situation is the lack of confidence and certainty that has been created. If we were able to move on to the negotiations and give manufacturers and retailers in the UK and elsewhere some sort of timeline, that would help them with their investment decisions.

Dr Christos Tsinopoulos: I would not disagree with that although I have a slightly different take on it. I think your question also implies whether you need a plan B in case such things do not work. A plan B is always a good strategy. I teach project management, where they all talk about contingency planning. I would also like to go a little bit on to the university sector, where I come from. There was an announcement last month saying that we will cover any money lost from investment on research. That is important because it gives confidence to the education sector, for example in universities and research, that you can continue investing, recruiting people and looking for talent even though that money might not be needed—I imagine that as a result of the negotiation

we might have access to, for instance, EU funding. So some sort of confidence-boosting plan B that is known to a degree to the wider public and industry would not necessarily be a bad idea.

Q100 **Lord Stirrup**: Professor, I am very glad that you mentioned the wider trading interests throughout Europe. Far too often we tend to concentrate on just what this means for us and what the difficulties are for us. As you say, there is a lot of mutual self-interest involved in this whole issue. In light of that, and of the fact that sometimes politics, particularly within the EU, can tend to trump industrial self-interest, what do you think would be the most appropriate relationships for us to retain with the EU to be able to get the best solution to all of this that satisfies everybody's mutual self-interest? That is without asking you to predict or specify particular institutional arrangements. What are the most important parts of the relationship that would allow us to drive this forward and instil the sort of confidence you are talking about as quickly as possible?

Professor John Manners-Bell: If you are in the supply-chain industry, one of the most important things for you as a business is inventory and being able to keep inventory levels as low as possible. For that to take place, you must have frictionless moment and slick transportation, so any barriers to the cross-border movement of goods will impact on inventory levels and that will impact on companies' competitiveness. So we would need to retain movement of goods without being stopped at borders. Given that goods from right the way round the world come into the UK and in many cases are not stopped at borders but go on to a distribution centre, I think that is achievable. Most clearance and documentation will take place due to new IT systems introduced over the past few years. So the process is really technology-driven. To come back to the system or future trading relationship that we have with the EU, I think we have to retain some level of free trade agreement, which is one step on from the WTO. At the same time, to return to the non-tariff barriers, we must go back to a place where both sides agree to standardisation and some level of homogenisation of regulations. As I say, because most regulations are internationally agreed, I do not see that being a problem either. We could put together some sort of loose free trade agreement which, at the same time, would allow us to trade with the fast-growing and emerging markets around the world and strike our own deals with those countries.

If we look further, people talk about the Norway arrangement or agreements such as the one that Turkey has with regard to being part of the customs union, but that comes with many other disadvantages as well. We would have rules and regulations imposed on us by the EU but without having any influence on actually setting them. At the same time, we would have to pay; in Norway's situation as part of the European Economic Area, for example, it has to pay a substantial amount of money for that privilege. Although it is not for me to comment on the political situation, if we had that level of integration with the EU, which in the case of Norway and Switzerland also includes the free movement of people, it would probably be politically unacceptable given the result of the referendum. So what I would envisage if I was put on the spot, which I am, is some sort of loose free trade agreement in terms of eliminating

tariffs or ensuring that no tariffs come back into the structure, as well as harmonising standards or keeping them harmonised as we move forward but allowing us to trade with the rest of the world at the same time.

Lord Stirrup: Perhaps I could put you on the spot a bit further. This might be slightly unfair, but I am just asking you for speculation. In your view, would the major manufacturing companies in Germany that export to us feel that that solution would be in their best interests?

Professor John Manners-Bell: I think they would accept it. I do not see why it would not be in their interests; they would have everything that they already have at the moment. They would not want the extra burden of any tariffs or problems with moving the goods on a just-in-time basis between their suppliers across Europe and their manufacturing plants in the UK. If we avoid that, they will accept it.

Q101 **Lord Liddle**: This is addressed to Professor Manners-Bell. The key assumption underlying your confidence is that the harmonisation of standards is already there, and that this harmonisation will be retained. There are a couple of points there. First, at present the EU is a global standards setter so, when you talk about global regulations, a lot of this is the rest of the world following standards that the EU has set. We will no longer have any influence over those standards if we are outside the EU. I know of recent instances in the car industry where you get a situation where the French and German manufacturers are setting standards in their interests without British-based manufacturers having any say. Is that a concern for you?

Secondly, a lot of the political argument about coming out of the EU—and many distinguished people, like Lord Lawson, make these arguments—is that the real opportunity of Brexit is for us to go through another wave of Thatcherite deregulation and set our own much looser standards in order to make our economy more competitive. Presumably, though, if that strategy were to be adopted by the British Government, the confidence that you have would completely disintegrate because we would not be able to maintain global access in the same way.

Professor John Manners-Bell: Coming back on the first point, yes, obviously the EU has been ahead of the game in setting international standards. To return to the South Korean scenario, one reason why negotiations could be concluded within two years was that South Korean standards were very close to EU standards, and both related to international standards. In electronic machinery, for example, in which South Korea is an important global manufacturer, those standards were very close to those already in place in the EU, so not much in the way of harmonisation was required. The issue was that products should not be tested once in South Korea and again when they got into the EU. If you are a South Korean manufacturer, you certainly do not want your product having to meet the requirements of different standards for the USA and around the world, so you have a variety of different products. That is why bringing them into line with international standards is so important.

I stress that it is all about international standards. If the EU has been at the forefront of developing them, that is all to the good, as long as they are adopted internationally, and in many cases—not in all, but in many—they are.

In terms of loosening standards, the vast majority of UK manufacturers never export and look to their domestic UK market, but at the moment they have to conform to EU standards. If there was some sort of Thatcherite revolution, as you put it, burning all these standards, regulations and bureaucracy, that would be one area it could look at, but I, for one, have not seen any appetite for that at the moment. I would envisage that the standards will remain the same for a significant time.

Dr Christos Tsinopoulos: I have a different angle on that. If you look at the EU emission standards, they are set by and for the European Union, and they are at the forefront of technology, so they are not just standards for operating procedures but for manufacturing cars to be produced and sold in the EU, so I sympathise with that argument. At the moment, the UK does have a say in what the EU emissions standards are; perhaps later, it will not.

Let us go back to the trade deficit argument, because I have heard it a lot and partly agree with it. Clearly, the argument that they need us more than we need them exists, but it is also temporary. The reason they need us more than we need them is that they make BMWs and Mercedes, which are good cars that we want to buy that are at the forefront of innovation. I am not saying that the UK does not have that, it does. I spent the whole of last week in a Jaguar and it was a brilliant car. The point is that this is shifting, and perhaps we will need them more than they need us. That will change over the years. Simply trying to second-guess the other person's negotiating position on the basis that they will need us more is short-termist.

Lord Lansley: On them needing us more than we need them and the South Korea analogy, first, on the point that we buy more from them than they buy from us, there is the question of the extent to which what is bought is substitutable by other products within the same market. If the terms of trade and the relative competitiveness shift, in a market of 500 million consumers, even if it goes down to 440 million, the likelihood of there being substitutable goods is relatively high compared to inside the United Kingdom, where there may not be alternative producers for that type of good. Therefore it has to be imported, and the question is where it comes from, and the EU would have a similar basis for trade as other countries. Does that point to a shift over time?

Secondly, on South Korea, how far does that agreement extend into trade in services? From the EU countries' point of view, if they continue to sell us goods, that is great; if we cannot sell them services so readily, that may also be great, but it may not be great from the British point of view.

Dr Christos Tsinopoulos: Sorry, what is the question?

Lord Lansley: First, is the issue of substitutable goods a reason why things might shift over time? Secondly, with South Korea, what does the analogy say to us about services in arriving at a two-year agreement?

Dr Christos Tsinopoulos: I think there is an area of substitution that can happen; I would not disagree with that. I guess that my point is more that we should go back a step. One thing that I am hearing again and again in the UK supply chain is that the engineering sector is great at doing things. I am judging for an award, for instance, and I see some excellent manufacturers around the UK. It we take that a little bit further, if they are as good as they say they are—and I believe that they are—they would like to export. So we would like to be in the situation where we export more to Germany more than Germany exports to us, in which case we need them more. If we do well and innovate, and the supply chain innovates and is creative and makes excellent products, it will be the other way around—and that would be a great position to be in, because you export more than you import, and that is what everybody aspires to do. On the exciting, high-end and high-value products—the Jaguars, Land Rovers and all that kind of stuff, which people want to buy, it is not easy to substitute. But when you go down the value chain, the substitution is a lot easier to make—I would not disagree with that.

Professor John Manners-Bell: I know that South Korean services were included in the agreement with South Korea. Perhaps I can call on a personal example. I run a consultancy, and we consult all over the world. We have no problems—we have worked with South Korean companies before, and we work with Chinese companies and companies around the world, providing them with consulting services. We sell reports all over the world. The most difficult region for us in selling our reports is in the EU, because of some of the more recent VAT regulations that have come through, which is bizarre in many cases. At the moment, as an exporter, I imagine that about 80% of our revenues are generated abroad, and we have no problems there; there are no challenges to doing business for us. Services are obviously hugely important for the UK, and they have to be part of any sort of free trade deal. But it is not the same level of issue that is impacting on the trade and movement of goods.

The Chairman: Thank you very much. I am going to have to ask colleagues not to ask so many supplementary questions, because we are miles behind time.

Baroness Donaghy: This is a question for Dr Tsinopoulos. You have been quoted on the importance of common legal frameworks and standardisation within the EU for the development of integrated supply chains. What impact would Brexit have on those common legal frameworks and standardisation, in your view?

Dr Christos Tsinopoulos: We have discussed common legal frameworks and standardisation to a degree already—but a nice analogy, which I have used with my classes over the last few months, is with the driving licence. I had a Greek driving licence and I could use it here, but I swapped it eventually with a UK one, because I had been here for long enough—but it is easy to do. There is no burden or problem associated with that. The same applies, to extend that a little further, to hauliers, who can just travel around the UK; the logistics industry knows that well. Another, more sophisticated, example is the one that I mentioned earlier about the

European car emissions standards, which allow automotive manufacturers to focus on the same standard across Europe. My concern is that, if that changes, the UK has no say in it—but, more importantly, if there are different standards in the UK versus the EU, which is a possibility, that creates significant complexities. I was talking to one of the automotive companies via a colleague yesterday, and one of the things that he told me was that this was a concern. At the moment, it is relatively simple, but if you look at what has happened for us trying to export to Japan, which has different standards, you see that that creates complexities in the supply chain. They are happy with that—it is not an issue. They have two or three different parts of the world to which they export, and they have two or three different standards. But if they had more of those, it would create significant complexity across the supply chain, which we would like to avoid. That is the rationale for my comment.

Q102 ***Lord Wei***: You have said that "the most pressing trade agreement should be one that prioritises access to innovation". Could you please elaborate on that? How would the UK lose or retain access to innovation through Brexit? What does innovation entail? Could your answer focus on financial services and areas the UK is particularly strong in or reliant on?

Dr Christos Tsinopoulos: I come from a business school with a strong reputation for finance work. Although I am not in finance myself, I hear some of the arguments. I would like to answer by bringing in a couple of examples. Example one is Nissan and example two is JLR. Although Nissan has research and development in the UK, based in Cranfield, for instance, a big part of its research and development of new cars—cars that the UK economy sometimes does not see—comes from Japan. It develops a car in Japan, asks you to make it here and sells it here. It is a little more sophisticated and complicated than that because they did some development here. The Qashqai, for instance, was designed in the UK, but across the product ranges that is not always the case. At the other end of the spectrum we have JLR. JLR designs a car in the UK and works closely with the likes of Warwick, Birmingham and Coventry Universities. They retain the R&D here in the UK. The consequence of that is a lot of knowledge spillover in the economy. For instance, PhD students and engineering students are being trained on high-production technologies and so on.

My point is that any free trade agreement should acknowledge that and allow access to, for instance, institutions that have knowledge. The frequent comparison is made with Germany and quite rightly so. Germany has an excellent university sector that is very well and closely linked with industry. If the prioritisation is based on trade and trade alone and forgets there is a knowledge spillover that happens across the board, it is potentially a short-termist view that misses some of the key points.

To give an additional point, coming from a research-based university, I think that one of our major concerns is we are going to lose the input we have on Horizon 2020. I use this as an example. It is not to moan about not being able to get money from Horizon 2020 in future, but more about the access to innovation that happens through Horizon 2020. Any free

trade agreement should acknowledge the fact that this innovation happens at the high end and find ways of integrating further down the supply chain. That is the rationale for my comment.

The Chairman: That is very interesting, thank you.

Q103 **Lord Horam**: Obviously, post Brexit we hope many of the supply chains will remain in place because it is in people's self-interest that they should do so. But, as you have emphasised, they might change. For instance, there might be some change in agriculture, although France has big advantages in keeping it the same, as do we. How quickly and easily can a supply chain be changed?

Professor John Manners-Bell: It really depends on the type of supply chain. Some of the supply chains that my colleague has been talking about, such as the automotive sector, have required large amounts of investment, for example in new facilities. Maybe those are the sorts of judgments or decisions that are being delayed.

Lord Horam: So they would be quite difficult to change. You would not want to do it unless you really had to.

Professor John Manners-Bell: Exactly. But a large proportion of supply chains are much more flexible and agile than that. For example, retail and fashion supply chains are being changed on almost a weekly or even a daily basis depending on a whole range of different factors in terms of cost and quality as well as risk, which is increasingly is factored into these sorts of decisions. Those are really flexible at the moment and they will reach out not just to Europe. For the majority, if we look at fashion, they will be looking at north Africa, south-east Asia and China. The supply chain managers in those companies will be making their decisions very frequently and the factors will change a lot. They will be changing all the time and therefore their decision-making on what goods to buy from which sources has to be flexible to meet the requirements of a fast-changing market.

Lord Horam: So to a degree it depends on the complexity of the supply chain; that is, whether it can change quickly or not.

Professor John Manners-Bell: Yes, and I would say that over the last 10 to 20 years supply chains have become much more complex than they were. Supply chains now rarely mean goods being manufactured vertically in one location and then moved to another export market or whatever it might be. You have fragmented ecosystems that have built up in which there are many different parties and tiers of suppliers, in many cases all supplying each other as well. Especially with technological advances in terms of visibility throughout the supply chain, you need to be able to make decisions very quickly and flexibly. The supply chains that you see in the electronics, fashion and retail sectors are the ones that will be making decisions tomorrow. If there are any more tariffs, that will be one of the additional factors, or if a non-tariff barrier is imposed, that is another factor. But I would say that they are not the key factor. There may be another 10 before you get to that.

Q104 **Baroness Symons of Vernham Dean**: You have answered the question about changing supply chains in terms of the sector you are dealing with. Obviously it is easier if you are dealing with children's clothes than it is if you are dealing with complex engineering. You have referenced several times the EU-South Korea free trade agreement during the course of your evidence. Of course UK business currently has access through EU free trade agreements with South Korea, Mexico and so on, but how difficult is it going to be? Will we on behalf of our business be able to conclude bilateral preferential agreements with other third countries—perhaps India or China? How difficult will that be and, if we are able to do it, what are the implications for non-tariff barriers?

Professor John Manners-Bell: Obviously we are getting into areas of supposition.

Baroness Symons of Vernham Dean: And politics.

Professor John Manners-Bell: Yes, and politics. It will be as difficult as we want to make it. In a lot of the countries which already have some sort of agreement with the EU, you could say that everything is already in place so it is just a case of finding out whether the country we will trade with unilaterally would want to enter into a free trade agreement. I cannot see why not because we are a big and important market. Consequently, if there is a free trade agreement in place that covers all the different headings and details which have been negotiated by the EU, does it meet our needs? If it does, I do not see why we cannot just transfer those types of agreement across, if there is the will to do so on both sides.

In terms of doing a deal with India, there is certainly already the will. If we look positively at the decision which has been made to break with the EU, we have to look for opportunities on a worldwide basis. If we ignore them and we make putting these trade deals into effect more difficult, we will be shooting ourselves in the foot.

Q105 **Lord Balfe**: A big part of the UK economy is focused on adding value to products, which requires highly skilled labour. I live in the city of Cambridge and at the moment we are constantly getting representations from industry about the difficulty of getting visas for high-skilled labour to come into the country. If value chains are interrupted as a result of Brexit, would you expect this to wash over into the high-skilled labour market? Also, do you have any words of caution about people who see Brexit really just in terms of stopping foreigners coming to Britain, given that this brain pool is a vital part of our future economy?

Dr Christos Tsinopoulos: I can answer that question on many levels. As someone who works in a university, I can say that we have this challenge all the time. We struggle to recruit people internationally because of the issues associated with visa problems. That is the experience from within the university sector. That is something that I am also hearing when it comes to engineering and the skills associated with that sector. It is actually very difficult to recruit people. There is always a preference to take people from the EU because it is easier to recruit them. Often, people who come from the EU are highly skilled and highly educated and,

of course, are welcomed by many of these organisations. I have to be careful here, but my prediction is that there will be an immediate spillover. But the other thing I should say—maybe because I am from the university sector—is that the UK has an amazingly strong university sector, with a lot of knowledge kept here. So in the longer term my prediction may be a little more positive—that in effect there will be the skill base, assuming that the university has the appropriate capacity to build the skills locally. But in the immediate aftermath of Brexit, if once that happens we ask for a visa from everybody who comes from the EU, for instance, I do not see how this issue would not be with us.

Lord Balfe: To follow that up, you would confirm then that we need a reasonably liberal visa regime for continuing to bring in highly-skilled workers?

Dr Christos Tsinopoulos: If you ask me, I think it should be expanded across the world, not just within the EU. But, yes, I would agree with that.

Professor John Manners-Bell: Perhaps I can focus on a slightly different area, the low-skilled sector, because to my mind this is the biggest threat to the logistics and supply chain of anything, putting tariffs and non-tariff barriers to one side. At the moment, the logistics and supply chain sector is powered by employees who are largely migrants who come in from eastern Europe. I am sure that you watched the Sports Direct inquiry with interest. You would have seen that of the 1,000 people working in that distribution centre, the vast majority—I think 800 or 900—were eastern European migrants. That is the same throughout the industry. If that supply of people willing to work on a very low-paid basis were to dry up, it would have a very significant impact on costs—more so, I feel, than many of the other things that we have been talking about today. It is the same in the transport industry. Everyone knows that the e-commerce sector has really taken off over the last few years, and that has meant there has been a huge demand for van drivers. A lot of those van drivers come from eastern Europe. They are fulfilling an essential part of the industry's function and they are doing it very cheaply, to put it bluntly. It is the same for the agricultural sector as well, I know. But certainly we have to take into account the people who are staffing those warehouses and driving those vans, because if that huge supply were to dry up it could really push up costs, and that would make UK manufacturing and retailing uncompetitive.

Dr Christos Tsinopoulos: It is a major concern. I have examples of manufacturers that are first tier suppliers with 60% of people not from the UK. We had a project with a local business recently but no one from the UK applied. If we had a regime where we asked for visas we probably would not have been able to fill the post. What the reasons were for that is another matter – we would have to make a guess.

The Chairman: A huge issue. Lord Green, your question has sort of been answered, but is there anything you would like to follow up? We are nearly at the end of our time.

Q106 **Lord Green of Hurstpierpoint**: The question as stated has sort of been

answered, or we have a least covered a lot of the ground. Since we all agree that the automotive and aerospace industries have particularly deeply embedded supply chains across Europe and we have seen the Japanese Foreign Affairs Ministry recently produce a 15-page treatise on the subject of the supply chain and the danger of disruption, I would be interested in any comments that you can make about the automotive sector, in particular, and anything that the Government should be wary of with regard to automotive and aerospace as they go into negotiations.

Dr Christos Tsinopoulos: I will have a go at giving my view on that. I find that we did not touch on aerospace as much as I would have liked, but I see the aerospace supply chain as being slightly different from the automotive supply chain. The aerospace is largely European or in the UK—there is one in the UK. It is highly competitive and linked with universities here, so I would be very surprised if anybody talked about this supply chain having a high level of risk. The automotive supply chain is considerably more fluid and much easier to move. To echo the point that my colleague made—or to contradict it; I am not sure if I want to echo or contradict it—it is relatively easy to move the automotive supply chain. Yes, it would take a while, and yes, it is a big decision, but there is spare capacity across the world, or so we hear. So it is relatively easier but I would not treat the two supply chains—aerospace and automotive—in the same way. The aerospace is much higher in value and is very much dependent on what we were saying before about innovation, the universities sector, and the knowledge sector. It does apply across the whole of the automotive supply chain; it applies, but not across the whole of the supply chain.

Professor John Manners-Bell: I do not really have anything to add to that other than to say that an increasing amount of components used in the automotive sector are high-tech components and they will be increasingly sourced from Asia. I think this is a trend that we will see in a number of other sectors as well.

Dr Christos Tsinopoulos: Brexit or no Brexit.

Professor John Manners-Bell: Yes, absolutely.

The Chairman: Baroness Brown, I think we have covered most points. We have come to the end of our session, so I say thank you very much. Is there anything that we have not asked you that you would like to say now? If you think of anything later, do write to us, but do you have any concluding remarks?

Dr Christos Tsinopoulos: No.

Professor John Manners-Bell: No, I think that we have covered a lot of ground. Thank you very much to the Committee.

The Chairman: We have not lost everybody from here yet, so thank you very much indeed. We will have our private session now.

Professor John Manners-Bell, Chief Executive, Transport Intelligence Ltd – Written evidence (ETG0004)

FOREWORD

When measured on its openness to trade, capital flows, exchange of technology and ideas, labour movements and, of course, culture, the UK has one of the most globalized economies in the world. (Ernst & Young, 2013)

Industry and consumers have benefited significantly from this level of globalisation, not least in terms of cost, as supply chains have integrated with businesses throughout Europe, whilst at the same time extending to emerging markets around the world.

Will this position be enhanced or damaged by the decision taken by the British electorate in June 2016?

From conversations with a number of senior industry figures, it is evident that there is no consensus over what Brexit will mean for the UK's supply chains or the logistics companies which serve them. Those people who voted to remain in the EU typically consider that Brexit will create more complexity and regulation in dealing with our largest trading partner. Others who voted for Brexit see an opportunity to increase trade volumes with faster growing markets in North America and parts of the developing world. Their conclusions are largely subjective, an entirely understandable state of affairs given the lack of data with which to make an informed decision.

When addressing the issue of the UK's future role in global supply chains it would be easy to become pre-occupied by trade relations. This would be ill-judged as in many respects supply chains have already left trade policy a long way behind. When supply chain managers make decisions, tariffs and non-tariff barriers are not at the forefront of their minds. Inventory levels, risk, product quality, transport availability and even ethical and environmental factors these days are significantly more important.

Global supply chains operate effectively both within and outside free trade agreements. Having said that, speed and visibility are critical and anything which threatens either would be very costly to UK industry. This could be a major risk if the frictionless trade systems which have been developed within the EU are dismantled.

However such an outcome isn't inevitable or even likely. Around a third of UK trade takes place without a free trade agreement, and consignments from Japan, US, China, Brazil and India have all been successfully integrated within manufacturers' and retailers' eco-systems.

Modern supply chains are flexible and responsive to changing global dynamics. However, in order to enable long term investment decisions to be made by the international business community there is a consensus that the UK Government

now needs to push ahead with the negotiations to create an environment of confidence and certainty.
September 2016

1. FUTURE TRADE SCENARIOS AND SUPPLY CHAIN IMPACT

Trade policy formed an important part of the debate in the run up to the referendum on the UK's membership of the European Union. Many manufacturers based in the UK are deeply integrated within multi-country value chains facilitated by Europe's transport infrastructure and unhindered by barriers to trade.

Many argued that leaving the EU would lead to the unravelling of these regional supply chains, with a subsequent impact on economic growth and investment. However, others argued that such a move would allow the UK to build closer trade partnerships with a range of developed and developing markets. Countries such as India, China and the US are all growing more quickly than their European counterparts and hence could stimulate demand for UK exports.

In an attempt to identify what a future relationship with the EU could look like, it is insightful to examine agreements which a number of non-EU members have been able to negotiate with the European Commission. This can be useful to some extent, but of course the UK is an unique position..

The types of relationship models highlighted below involve a varying level of access to the EU's Single European Market (SEM). An integral aspect of the SEM is a Customs Union to which every EU country (plus Turkey) belongs. As well as setting external tariffs, it also eliminates a range of non-tariff barriers (NTBs) which allow the seamless movement of goods throughout all member countries with a low level of regulation. The EU estimates that European GDP is 2% higher than it would have been had the SEM not been implemented in 1993.

There are four main models of agreement which demonstrate the range of relationships in place.

- Membership of the European Economic Area (so-called 'Norwegian' model)
- Membership of the EU's Customs Union ('Turkish' model)
- Free trade agreements (e.g. Switzerland, Canada and South Korea)
- World Trade Organization rules

1. The Norwegian model

Norway (and also Iceland and Liechtenstein) are members of the European Economic Area but are not full EU members. Norway has significant access to the SEM, but it has to pay for the privilege as well as being bound by a number of EU rules and regulations. For example, it has to accept the free movement of EU citizens. It also has no influence on the development of EU legislation by which, in many instances, it is still bound.

2. The Turkish model

Turkey has been a candidate country to join the EU since 1999 and has been part of the EU's Customs Union since 1995 (although this agreement excludes agricultural goods and services). The EU recognises that there is considerable

'asymmetry' in the agreement as it requires Turkey to align its trade with European policy, although it has no say in its formulation (EC, 2015).

3. Free Trade Agreements

Another alternative would be to agree a deal with the EU which allowed tariff free access to the EU for UK exporters, and likewise, access to the UK for EU exporters. Critics say that this would not wholly address the issue of Non-Tariff Barriers (NTBs) such as consistent product standards or labelling. In Switzerland's case the free movement of people is also one of the conditions. This may not be acceptable to the UK Government.

The trade deal with South Korea could be a better example to follow. Negotiations with South Korea commenced in 2007 and were completed in 2009. The deal was officially signed in 2010 and ratified by the European Parliament in 2011, what many would consider as a very short timescale given the complexity of the negotiations relating to tariffs and NTBs. Any negotiations between the UK and EU would commence from the basis of an already standardised market which may reduce timescales further.

4. WTO scenario

If no agreement between the UK and EU can be brokered, trade relations would default to World Trade Organisation (WTO) rules. The UK is not alone in this, of course, as many major countries trade with the EU using this model. WTO rules work on a 'Most Favoured Nation' (MFN) basis. This means that the best deal on tariffs which is struck by two countries must apply to all others. This would mean, for example, that even if it wanted to, the EU would not be able to unilaterally impose a higher level of tariffs on the UK than it had agreed with any other partner.

However, as will be discussed later in this paper, tariffs are a relatively unimportant trade barrier following years of negotiated reductions.

It should also be noted that about a third of the UK's trade is already conducted under WTO terms. Global trade has grown fast in the last fifty years, largely as a result of WTO agreements. In fact, the EU has few free trade agreements in place with major trading nations (although several are in the process of being negotiated such as the Transatlantic Trade and Investment Partnership (TTIP) with the USA).

2. CHANGES IN TRADE PATTERNS AND THE IMPACT OF TRADE BARRIERS

Trade patterns have changed significantly over the past two decades as, despite membership of the EU, trade with the rest of the world has increased in its relative importance. UK exports to the EU comprised 55% of all exports in 2002; by 2015 this figure had fallen to 44%. The EU's share of imports to the UK fell from 58% in 2002 to 50% in 2011, although it has now increased slightly to 53% in 2015. It seems likely that Brexit will only accelerate this existing long term trend and increase the UK's trade with the rest of the world.

Tariffs and Supply Chains

The issue of any future tariffs which may, or may not, be levied on UK exports to the EU (and vice versa) may not be as serious as some imagine. According to the

World Bank the average tariff levied on goods entering the EU is only 1.5% (World Bank, 2014) although there are higher tariffs on goods such as finished vehicles.

According to some research (Feinberg & Keane, 2005), the influence of tariffs on world trade is less important than ever before. Following the NAFTA deal in 1994, US-Canada trade grew by 100% although tariffs fell by only 3-4 percentage points. Much larger tariff reductions in the 1960s had not resulted in such gains leading to the conclusion by the researchers that cross-border vertical specialisation and multi-stage fragmented manufacturing processes were responsible for the growth in trade rather than tariff reduction. Advanced supply chain management practices were the catalyst, although these practices could only occur within a low tariff environment. Applying this model to the UK and EU, it seems evident that as long as tariffs do not increase significantly (and even under WTO rules this would not happen) extensive fragmentation of production and supply chain integration would continue across the region.

The threat of Non-Tariff Barriers (NTBs)
Non-tariff barriers are measures put in place by individual governments to indirectly reduce the competitiveness of other countries' exporters, thereby protecting their own domestic producers. Largely as a result of the successes of the WTO, tariffs have played an increasingly minor role in protectionism with governments choosing more subtle ways to influence markets. The most important NTBs are addressed below.

One factor which may mitigate the impact of non-tariff barriers is the level of intra-firm trade within domestic and international supply chains. Often multiple movements of components can occur within a single multinational company and in some cases barriers to trade can be completely avoided (Minford, 2016).

The best example of how supply chains have out-paced trade negotiations is in Asia. The development of the 'Factory Asia' concept has brought about integrated, intra-regional cross-border supply chains focused around assembly in China. Often the countries involved have no, or few, official trading agreements although that is now changing with the increasing importance of the Association of South East Asian Nations (ASEAN). It could be concluded, though, that in this case the trade agreement has followed the development of supply chains and not the other way round.

- Rules Of Origin

A significant cost threat to the UK economy is any change to the status of 'Rules of Origin' regulations as applied to UK exporters. Rules of Origin are defined by the WTO as, 'The criteria needed to determine the national source of a product. Their importance is derived from the fact that duties and restrictions depend upon the source of imports.' (WTO, 2016)

If a free trade agreement is concluded between the EU and UK, UK exporters would have to declare to EU customs authorities the proportion of their goods which include sub-components that have been imported from outside the EU. Below a certain threshold and the goods would qualify for preferential treatment; above and they would face the full tariff.

The administration of Rules of Origin can be a complex process and its impact could vary according to the nature of trading agreements between the EU and the UK. The think-tank Open Europe suggests that applying 'rules of origin' could cost around 0.9% of GDP over a 15 year period (Ruparel, 2016). The method of how these rules will be applied will be a major issue to any exporter and importer.

The UK government has estimated that the 'Rules of Origin' provision could costs traders anything from 4-15% of the cost of goods sold. Consequently it is likely that rather pay these internal costs, exporters would choose to pay the EU's external common tariff, especially in cases of low value goods and where tariffs are low.

It should be noted, of course, that EU exporters would be very keen to avoid having to provide 'rules of origin' information to the UK administration. It would therefore become another bargaining chip in the Brexit negotiations.

In fact, as in its agreement with South Korea, EU officials have attempted to make the Rules of Origin administration as simple as possible. (EC, 2011) Major traders can become authorised to make self-declarations as to whether their products have been wholly obtained or sufficiently processed in the EU or South Korea. As an example, products such as machine tools or cars will be classified as of EU origin if they have no more than 45% of their parts by value originating outside of the EU.

- Food hygiene and safety/Labelling and packaging

These two NTBs relate to levels of product standardisation. This is often a critical stumbling block when countries enter into free trade agreement negotiations (as seen in the TTIP process). The UK, however, is already compliant with all the standards required by the EU and the issues in the Brexit negotiation may be the converse: a deal will be dependent on relaxing levels of standardisation rather than increasing them.

- Anti-dumping measures

Another issue which will be addressed in NTB negotiations is 'anti-dumping' (goods exported to a market at a price substantially below their normal value). Most anti-dumping disputes relate to developing markets and commoditised goods and it is difficult to see a material impact on UK-EU supply chains. However, it should be noted that the EU imposed anti-dumping measures on Norway (16% duty on imports of Salmon) in 2005 despite its free trade agreement.

- Producer subsidies

Producer subsidies (including farming) will make it difficult for UK farmers to export to the EU, even if no tariffs are imposed. This will encourage British farmers to push for the continuance of their own support measures.

Currency impact

The fall in the value of sterling by around 10% immediately after the referendum has acted as a stimulus to UK exports as products become more attractive to foreign buyers. More recently, the Bank of England's decision to cut the UK's rate of interest to a record low should depress the value of the pound for some time.

Sterling's weakness will help re-balance air and sea freight import/export volumes in the short term. This may have the effect of increasing rates for the backhaul of containers from the UK to Asia, helping a struggling shipping industry. At the same time import volumes may be negatively impacted as manufacturers and retailers turn to domestic suppliers, thus acting as another stimulus for UK industry and its logistics service providers.

However, for many goods which cannot be sourced in the UK (such as most consumer electronics) input costs may rise which could depress consumer demand and retail sales. The overall picture is likely to remain confused and the consequences for each company will depend individually on its mix of business and customers.

3. IMPACT OF BREXIT ON SUPPLY CHAINS

Supply chains are very sensitive to increases in costs and should Brexit create additional expense and delays in terms of sourcing goods from the EU (and vice versa), then significant changes should be expected. To what extent and the timescale involved relies on whether the supply chains in question are vertically integrated, with owned production facilities across Europe, or whether they are made up of a 'virtual' network of third party suppliers. If the former is the case, the time taken to change supply chain strategy will be longer than if a 'virtual' model is employed.

Although much has been written about the potential impact of Brexit on UK-focused supply chains, it must be noted that the UK already has some of the most globalized supply chains in the world. The country successfully integrates components sourced from non-EU countries into its assembly plants with little problem. As one logistics director commented, 'Look at the ease with which goods from Asia arrive in the UK destined for our retailers and manufacturers. It is seamless with most formalities completed electronically. This includes goods under bond with all the additional complexities that go with that and this will be the same [after Brexit] with Europe.'

Agriculture

The most clearly affected sector, and one that demands extensive logistics services, is that of agricultural products. Although farming accounts for less than 1% of GDP in the UK it makes up 11% of inter-EU exports. It is also the focus of more than 40% of the EU's budget and is protected by an extensive system of tariffs.

Removing such subsidies and tariffs from the UK market will inevitably have an impact. Many basic food commodities such as wheat, beef, and sugar, are available in quantity from world markets at much lower prices. Bearing in mind the UK's long held preference for market driven trade policies it seems likely that in the long term the UK government will seek a change from the protectionism of the Common Agricultural Policy (CAP).

Britain imports around 40% of its food requirements, with the Republic of Ireland and France being the leading beneficiaries of this trade. There are already some indications that UK grocery retailers and their food processor suppliers are

thinking about the structure of their supply chains and here the implications for logistics may be significant.

The appetite for refrigerated services ('reefers') is likely to grow, as will agri-bulk shipping. Air freight may also benefit, with greater opportunities for higher cost fruit and vegetable imports. It would appear logical to assume food warehousing capacity would increase.

The losers may be fewer than might be imagined. Most agricultural products from continental Europe are imported by road, often in a processed form. Cross-Channel road freight therefore may be hit but overall the logistics sector may benefit as a more globalised food supply chain will be more demanding in terms of intensity of logistics services.

Automotive
The automotive industry is of critical importance to the UK's economy representing 10% of the UK's trade in goods. The automotive sector in particular faces a degree of uncertainty. The suggestion is that the assembly plants in Britain will be vulnerable to tariffs imposed by the EU. However, some of the numbers suggest that this might not be such a problem.

According to a 2014 report by consultancy KPMG, around 37% of the total value of spend in the automotive supply chain is sourced from the UK. The report asserts that, 'Depending on the manufacturer, between 20-50% is imported from the EU and the rest from outside the EU.' (KPMG, 2014) This would suggest that the UK's automotive supply chains already work efficiently with perhaps a third of inbound components manufactured outside the EU, with more than a third (UK based) not affected directly by Brexit at all.

There are, of course, strategic concerns over whether non-UK automotive manufacturers would maintain their production locations in the UK. However even here worries may be over-stated as operationally, according to Eurostat, the UK's automotive industry is the most productive in the EU (KPMG, 2014), which suggests there seems little reason for pulling production out of the UK.

The UK runs a £10bn deficit in terms of finished passenger cars. The largest beneficiary of this is Germany, with Poland, Hungary, Sweden, Slovakia, France, and Spain also exporting heavily to Britain. Consequently there are good financial reasons why the major European manufacturers would not want the EU to impose trade barriers on UK imports, if there was a chance that the UK would reciprocate. As a result, the incentive to all concerned to retain the status quo is great.

Possibly there may be changes in the area of finished vehicle imports from outside the EU, with the UK pursuing free-trade agreements with the likes of Japan and the US.

In the specific examples of Japanese manufacturers in the UK, Nissan and Honda, most parts are supplied locally and the second tier suppliers that support the manufacturing plants have long ago established operations in the UK. The parts that come from overseas are as likely to come from the US or Japan as

Europe. These plants manufacture for a global market with Europe being just one region, albeit important.

Retail (non grocery)
With the exception of grocery retailing, which will be influenced by any changes to food production support and protection, the retail sector may be least affected by Brexit in relative terms. Commodities such as clothing, furniture or consumer electronics have long been sourced globally from countries such as China or Japan under WTO rules.

However, even in this sector, there may be changes which support the increased status of non-EU markets. According to research by Barclays, many UK retailers are already reviewing their supply chains as a result of the vote to leave.

- 45% of respondents thought that sourcing from EU would fall
- 32% thought that sourcing goods from the UK would increase
- 50% thought that sourcing from India would increase
- 38% stated that there would be more sourcing from Africa
- 43% said there would be more sourcing from China

Perhaps the biggest threat to the sector would come from a loss of consumer confidence impacting upon the purchase of 'big ticket' items such as cars or a longer term slowdown in the housing market. However, as all recent reports indicate, this has not occurred and a reduction of the interest rate by the Bank of England is likely to stimulate spending further.

Compared to the impact of trends such as e-retailing, it is hard to think that Brexit will have an enormous effect on supply chain geography despite the likelihood of an increase in local sourcing and more imports from non-EU markets, an on-going trend which has already been identified above.

4. CUSTOMS AND TECHNOLOGY

Whilst it is unclear what sort of trading relationship the UK will have with the EU following its decision to leave, it is likely that UK Customs' processes will change significantly. A withdrawal from the European Union Customs Union will involve establishing a new system for classifying imports and exports and the tariffs which would be applicable.

The good news is that the UK appears to have a flexible administration for managing these procedures. Shippers importing goods into the UK operate within a dedicated IT system. Her Majesty's Revenue and Customs (HMRC) has a centralised information network that both manages the authorisation of specific consignments and accepts the payment of any tariffs. Accessing this system requires software which is available to any accredited user. The data demanded by this system is largely available on the bills of lading, waybills or consignment notes. It is widely accepted that the UK has an adaptable system for administering imports into the country and changing such a system ought to be very straightforward to cope with imports from the EU.

Similarly, the nature of data interchange between the UK and the economies of the EU should not be so demanding. The EU 'TRACE' system or 'Excise Movement and Control System' are means of tracking movements of consignments for

purposes of levying taxes or monitoring the routing of goods. Their duplication outside the EU, if needed, would be straightforward using the existing Customs' systems.

5. IMPACT OF BREXIT ON THE LOGISTICS MARKET

Road freight
The UK road freight industry is largely regulated through European legislation, especially in terms of drivers' hours and operator competence. Although it will be possible to amend such legislation when powers are repatriated from Brussels, there would seem little appetite to make major changes especially to health and safety regulations related to trucks or drivers.

However there is potential to unwind some 'pseudo' quantitative regulations such as corporate financial competence which attempt to regulate market entrance (operators have to maintain a certain level of cash in their bank). This could increase market efficiency without impacting on safety.

The UK will also re-gain sovereignty over imposing charges for the use of roads by European freight operators, thereby creating a level playing field of costs. Should the government wish, 'cabotage' (access to the UK's domestic market by European freight operators) in the UK domestic market could also be regulated.

Other macro impacts could include:

- Cross-channel road freight volumes may be negatively impacted as sourcing moves to intercontinental markets
- UK international road freight exports to the EU boosted by weak sterling
- Port-centric road freight services and drayage to increase as sea and air freight volumes rise
- Domestic road haulage industry to benefit from increased local supply chains as EU imports become more expensive
- UK road freight companies benefit from 'level playing field' due to road user charges imposed on foreign hauliers
- Hiring drivers becomes more difficult and expensive as eastern European immigration reduced (especially parcels sector)

International Freight
Brexit will inevitably change the supply chain geographies of many industry vertical sectors, as outlined above. This could have a major impact on the international freight market and the infrastructure needed to facilitate the movement of goods on an inter-continental rather than intra-regional basis. In summary:

- New trade deals will increase inter-continental volumes
- Deep sea shipping services and air cargo will be main beneficiaries
- Inbound European volumes may decrease especially if barriers raised
- Weaker sterling will see boost for export/out-bound volumes
- Reefer services to benefit from increased intercontinental food imports
- Deep sea ports and airport-based distribution to gain
- Cross-channel roll-on roll-off (RORO) to lose out
- Added complexity in terms of documentation processes will increase demand for freight forwarders' services

Warehousing and distribution
There will also be changes to the UK warehousing and distribution markets although overall impact will be negligible in relative terms when compared with other major trends, such as e-commerce.

- Gateway logistics (port-centric) facilities to benefit from increase in sea and air freight volumes
- Challenges to hiring supply chain employees due to limits on immigration
- Increase in warehousing for national distribution if Single European Market rolled back and local supply chains increase
- Migration of pan-European distribution centres to mainland Europe

RECOMMENDATIONS AND CONCLUSION
In order to meet the challenge of the Brexit negotiations, the UK Government should look to the supply chain industry to second experienced and expert opinion. Modern supply chains are complex eco-systems, consisting of sophisticated, evolving and interdependent networks. Trade negotiations must take into account that flows of finished goods and intermediate components are rarely linear or easily understood.

Consequently negotiators should understand the true costs of a supply chain. This may mean less emphasis on tariffs, for example, and more on the trade barriers which have the potential to delay the movement of cross-border shipments. For UK businesses to remain competitive they will need to retain their agile and lean inventory supply chains.

It is likely that throughout the period of negotiation, there will be considerable uncertainty until the final structure of UK-EU trade relations are agreed. It is in the interest of all parties to keep this period to a minimum and there would seem to be little reason why negotiations should be protracted (unless for political aims). After all, a new trade partnership was agreed with South Korea within a relatively short timescale.

Meanwhile, the over-riding message from the UK logistics and supply chain industry is one of 'business as usual'. As one senior executive who voted to remain put it, 'There is no intention for us to sit in a corner and sulk. Now the decision has been made, we need to get on and negotiate the best outcome.'

For UK manufacturers and retailers, the prize will be enhanced links with many of the world's fastest growing economies such as China and India, whilst maintaining their integrated European supply chains.

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Professor John Manners-Bell, Chief Executive, Transport Intelligence Ltd – Written evidence (ETG0004)

Prior to establishing Transport Intelligence in 2002, he worked as an analyst in consultancies specialising in international trade, transport and logistics. He also spent a number of years as a manager of global express and logistics company, UPS, in a strategic marketing and communications role.

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30 September 2016

Lord Price CVO, Minister of State for Trade Policy, Department for International Trade (DIT), and Lord Bridges of Headley MBE, Parliamentary Under-Secretary of State, Department for Exiting the EU (DExEU) – Oral evidence (QQ 40-67)

Transcript to be found under Lord Bridges of Headley MBE, Parliamentary Under-Secretary of State, Department for Exiting the EU (DExEU)

Lord Price CVO, Minister of State for Trade Policy, Department for International Trade (DIT), and Lord Bridges of Headley MBE, Parliamentary Under-Secretary of State, Department for Exiting the EU (DExEU) – Supplementary written evidence (ETG0013)

Transcript to be found under Lord Bridges of Headley MBE, Parliamentary Under-Secretary of State, Department for Exiting the EU (DExEU)

Raoul Ruparel, Co-Director, Open Europe, Dr Markus Gehring, Lecturer, Faculty of Law, Cambridge University , and Luis González García, Associate Member, Matrix Chambers – Oral evidence (QQ 11-19)

Transcript to be found under Dr Markus Gehring, Lecturer, Faculty of Law, Cambridge University

Raoul Ruparel, Co-Director, Open Europe – Supplementary written evidence (ETG0002)

Supplementary questions:

1. To what extent could the UK signing new FTAs with high-growth markets offset the impact of reduced EU market access? What weight should the Government ascribe to signing new FTAs of this kind, relative to securing a preferential trading agreement with the EU?

In our original Brexit report we modelling the potential gains from an extreme free trade scenario – unilateral free trade. This was found to boost UK GDP by 0.75% permanently in the long run (up to 2030). This alone did not offset the impact from leaving the customs union and the single market (between 1% and 2% of GDP in our modelling). Of course, unilateral trade only captures one side of the gains which you would expect from an FTA. We also did some back of the envelope calculations which found that an Australia-like run of FTAs with the major East Asian economies (China, Japan, India and ASEAN), should generate something on the order of a net boost of 0.6% of GDP for the UK." As such, an wider array of new FTAs would offer further gains. It seems unlikely that new FTAs alone would offset the impact of leaving the EU but if combined with securing a good agreement with the EU, keeping the FTAs the UK currently has, maintaining a sensible immigration system and some level of deregulation then it could largely combat the cost, if not offset it entirely.

As we discussed in our liberal, free market guide to Brexit, the UK will need to consider which states to prioritise when it eventually gets round to formally negotiating additional trade agreements. The table below outlines some of the contenders.

	Simple average MFN applied tariff	Simple average MFN applied Agriculture tariff	Simple average MFN applied Non-Agriculture tariff	Share of UK goods export trade	Share of total UK trade in goods	Share of total UK trade in goods and services
Brazil	13.5%	10.2%	14.1%	0.7%	0.6%	0.6%
United States	3.5%	5.1%	3.2%	12.6%	9.2%	13.1%
Australia	2.7%	1.2%	3.0%	1.2%	0.8%	1.2%
China	9.6%	15.2%	8.6%	5.3%	7.4%	5.4%
India	13.5%	33.4%	10.2%	2.2%	2.1%	1.8%
Japan	4.2%	14.3%	2.5%	1.4%	1.6%	1.9%
New Zealand	2.0%	1.4%	2.2%	0.2%	0.2%	0.2%

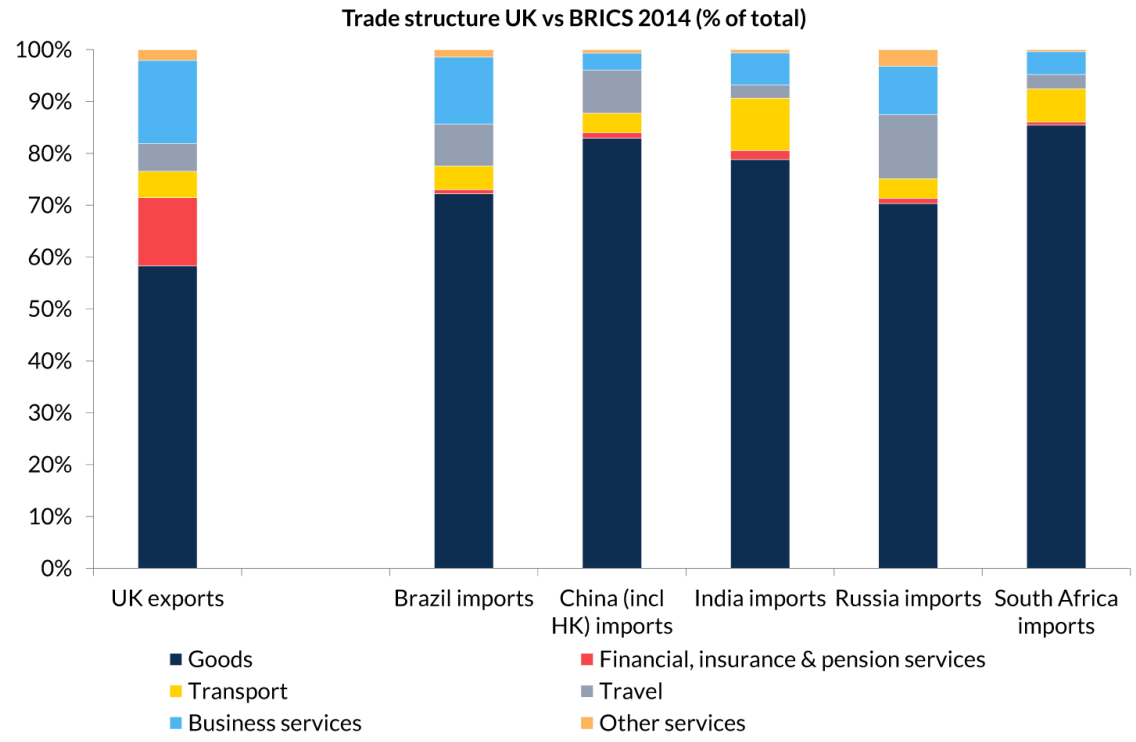
oe Source: WTO Tariff Profiles 2015, and ONS Pink Book 2015

Of those included in the table, the highest average tariff countries that the UK does not yet have FTAs with are India (13.5% MFN), Brazil (13.5%) and China (9.6%). In terms of the UK share of the export of goods that these highest tariff countries make up, China is the largest (9.4%), then India (2.1%) and then Brazil (0.6%). Striking even basic agreements with China, India and Brazil (in reality this would likely be a deal with the South American Mercosur trading bloc) could deliver gains for the UK, not just in terms of reducing the cost of current trade but opening up new avenues.

Needless to say, the longer-term goal for the UK would still be to conclude agreements that provide for the fullest possible liberalisation of trade in services – and financial services in particular. The obvious example where this is true would be the US. While it accounts for 12.6% of UK goods exports, it accounts for 23% of UK services exports. As such, the largest returns from an FTA with the US would come from integration on services by removing regulatory barriers and duplication.

This raises the prospect of an idea which we floated in the same report – multi-stage or separated trade negotiations. When negotiating a free trade agreement, the EU's preferred approach is 'nothing is agreed until everything is agreed'. The inherent risk with this strategy is that a single issue can potentially hold up an entire deal for months or even years. A multi-stage approach could allow the UK to secure duty-free trade in goods with a larger number of countries in a shorter period of time – as scrapping tariffs is usually the easiest bit of a trade deal – while more complex areas would be addressed at a later stage. This is not without risks – the latter talks on services may never get off the ground while it also potentially reduces the UK leverage given services/capital account for a significant part of the UK economy. But it could at least allow a route for the UK to secure basic agreements quickly and help the UK Government to more easily juggle the many priorities with limited resources.

That said, the UK will have to be patient. In many cases, the high growth, developing economies do not yet demand a big part of what UK produces – namely services. This also highlights why the risks of a multi-stage approach may be less than first feared.



oe Source: UNCTAD

As the chart above shows, the UK's export mix and the import mix of the BRICS countries are not that well aligned. 70% - 80% of what they import tends to be goods, while that is less than 60% of what the UK exports. These are often not the same types of goods – they import significant amount of energy related products as well as telecoms equipment, though there is some overlap in cars (a big UK export and a big BRICS import). Furthermore, once goods related services, transport and travel are stripped out, in 2015 the UK alone exported almost as much in services as Brazil, Russia, India, China and South Africa combined imported. In 2015 the value of financial services which the UK exported was six times the value imported by all the BRICS combined. Only in Brazil and Russia do business services, the other big UK services export, come close to accounting for 10% of imports.

This highlights the need to maintain good links with the EU and strike a free trade agreement with the US (two regions which do demand services) whilst also preparing the ground for future expansion into these growth markets and making sure the UK is ready to take advantage of any opportunities. As these countries develop (an uncertain and non-linear path of course) they are likely to demand more of what the UK provides – in particular business and financial services.

2. Please would you give your thoughts on Lord Liddle's question and the responses made by Mr Garcia and Dr Gehring? (Excerpt below)

Lord Liddle: You say that most free trade agreements do not offer full access in services, and that in a lot of sectors, under the existing Single Market, setting up subsidiaries is as important as passporting. That raises the question of free movement. If you have a single company with subsidiaries, are there precedents

for including free movement rights within FTAs? The other thing, I suppose, is that if we want full access to the Single Market, our EU partners might say that we should still be paying into the budget. Is there any precedent within FTAs for budgetary contributions?

Mr Luis González García: On the question of free movement of persons, the short answer is no. Under an FTA you cannot include free movement of people. The EU would not be able to negotiate free movement of people in an FTA. Why? Because it can negotiate only what is included in the Common Commercial Policy (CCP). Not only that, it must take into account the objectives and principles of the EU External Action Service. Free movement of people is not included in the CCP or in the EU External Action Service. That is why it would be outside the scope of an FTA, and there are no precedents; there is no FTA where free movement of people is negotiated. On the budget issue, there is one precedent: for example, the agreements that the EU negotiates with potential members of the EU, countries that are in the process of seeking membership of the EU. A good recent example is Ukraine. It is an FTA within a global political agreement. In the FTA part of the agreement, there is no budget, but in the agreement signed between the EU and Ukraine there is an obligation for Ukraine to contribute to the budget of the EU. Why? It is for two reasons. Ukraine is interested in European funds and in European programmes, so if the UK is interested in continuing, for example, the Erasmus programme, you have to contribute. That is part of the deal. If you want to be part of EU funds, you have to contribute to the budget, but these are different kinds of contributions. It is the same thing with all the other European agencies providing funds and programmes; you have to contribute to those programmes.

Dr Markus Gehring: In an ideal world and with the agreement of European partners, a lot of things would be possible. The WTO GATS agreement itself includes Mode 4, as we said, which includes the physical movement of people. If you liberalise architectural services, you allow an architect to come to the United States and work on a project knowing that once their services are no longer required they go back to the country they came from. Very few countries in the world have liberalised Mode 4. It is normally under a lot of restrictions. I think the most liberal GATS schedule is that of the United States of America, and if you have tried to work in the United States or provide services there, you know what the restrictions are. A lot of thought should be invested in participating in regulatory agencies. There are now quite a few EU regulatory agencies that the UK also benefits from at the moment. Recreating all those agencies in the United Kingdom would easily eat up a chunk of the budget that seems to be overly generously allocated already. There would be precedent to accept not having any governance input into those agencies but just using them for their decision-making power and paying for that kind of service, so that would be another level of contribution.

- While free movement of people may not be explicitly negotiated as part of the FTA it will certainly be a big part of the Brexit negotiations. There is scope to negotiate a bilateral agreement on this issue as Switzerland and the EU have done. There could also be principles agreed regarding the cooperation between the two sides on this. In fact, there is a huge range of what could be included in any bilateral agreement between the two sides on this issue. It could also be tied up with the withdrawal agreement.

- Similarly, on the EU budget both Switzerland and the EEA states make ad-hoc contributions to certain budget programmes. As such, it could be negotiated that the UK would be outside the EU budget framework but could make ad-hoc contributions for programmes which it continued to want to be a part of or to issues which it wanted to contribute.

3. Please would you give your thoughts on Lord Stirrup's question, and the responses made Dr Gehring? (Excerpt below)

Lord Stirrup: Some people have suggested that legally the UK could remain a party to existing EU free trade agreements even after it had left the Union, so they would become agreements between the EU plus one and a third party. Is that a credible path? What would the third parties be likely to think about it, and would it be in the UK's interests to follow that?

Dr Markus Gehring: I think members have seen the blog that I wrote in March. Not much has changed from my point of view since I wrote that. There are four or five aspects that make a simplified version of, "We are a party to these free trade treaties", and some are more complicated. The first aspect is that some FTAs, or some trade agreements, are just concluded by the EU, so there would be no access to the UK. Even some of the mixed agreements specify that the application of the agreement is really restricted to EU Member States, which then makes it very difficult just to partake in those agreements. Of course, if your Article 50 negotiations result in some form of understanding on the 50 or so FTAs that the EU has concluded, everything is fine and you can continue as before. Even if that is not the case, there is the added problem that either the EU or the third-country partner would probably have a right to request some form of renegotiation. I tried to explain that in the sense the EU negotiated as a Customs Union with the internal market at its heart. If the UK can no longer participate in the EU internal market, in my view it can no longer fulfil a good chunk of those free trade obligations, and that triggers the renegotiation. Some partner countries might not have an interest in renegotiation but you still have the EU at the table. The EU could take the very drastic step of either withdrawing or terminating those kinds of agreements, if the partner still lets the UK as a non-EU member state participate in that relationship.

Lord Stirrup: It is an approach that could be pursued under the Article 50 renegotiation.

Dr Markus Gehring: That would be my advice, yes.

- Third country membership of the existing agreements is possible but would require consent of both the EU and the other party. As such, it might be simpler for the UK to seek to sign new bilateral agreements with these states which mirror the current agreements – albeit updated with regards to the UK being outside the single market. This might imply more negotiation but then signing up as a third party as established above is not without its challenges either.

19 September 2016

Dr Ulf Sverdrup, Director, Norwegian Institute of International Affairs, and Dr Peter Holmes, Reader in Economics, University of Sussex – Oral evidence (QQ 20-29)

Transcript to be found under Dr Peter Holmes, Reader in Economics, University of Sussex

Dr Ulf Sverdrup, Director, Norwegian Institute of International Affairs – Written evidence (ETG0010)

Thank you so much for meeting with the Committee a few weeks ago to discuss the EEA Agreement and what the UK's options might be during the Brexit negotiations. Following on from that, there were a few additional questions which it would be helpful to have some clarity on. Your response would be taken as supplementary written evidence to the inquiry.

1) When describing the process through which the UK might adopt the EEA Agreement, your oral evidence noted that:

"There are two options. The first is to remain in the EEA as a contracting party but leave the EU. The second is to leave the EU, remain in the EEA and just switch sides and go into EFTA…The first strategy of moving from the EU, not into EFTA, but remaining an EEA partner, I do not think is feasible."

You go on to say: "The question then is how to switch sides into EFTA."

Could you describe in a bit more detail why the UK would have to join EFTA to participate in the EEA agreement? Does the UK need to join because of the role of the EFTA Court and the EFTA surveillance authority. If so, what role do these two institutions play in relation to Switzerland?

Response Sverdrup

The EEA agreement is constructed as a two pilar system, this means that members of the EEA are supposed to be either members of the EU or members of EFTA. In reality, all EEA members have to be either an EU member or a member of EFTA. If the UK leaves the EU, but wants to remain in the EEA for some time, it follows from this that it should then seek membership in EFTA.

Joining EFTA is partly related to the EFTA court and Surveillance Authority, but it is also important for the other EEA bodies, such as the other EEA institutions, such as the EEA Council and EEA committee. They are the institutions that secure a smooth operation of the agreement and these institutions make decisions, for instance on adding new EU legislation to the EEA agreement.

The EEA institutions play no role in relation to Switzerland. It is a bit confusing for many. You have to separate between EFTA, where Sizerland is a member, and EEA EFTA where Switzwrland is not a member. Switzerland is not a member of the EEA and the EFTA Court and EFTA Surveillance Authority have no role to play in relation to Switzerland. The Efta Court and ESA are just there for the EFTA EEA countries and have no jurisdiction in Switzerland.

(My impression was that EFTA was only a Free Trade Area – and that its role was to negotiate FTAs with third countries and to regulate the trade between EFTA members.))*Response - yes this is partly right - but there is also the EFTA EEA.... It is a bit complicated....(*

2) Open Europe* has said that "EFTA court does not have the same authority at the EU's Court of Justice to issue binding decisions, only recommendations and advisory opinions." Is this accurate? Could you explain in a bit more detail the powers of the EFTA Court?

Response Sverdrup

The EFTA court is modelled on the Europan Court of Justice, and it by intention designed so that it has almost the same procedures. For reasons of formal sovereignty, however, the formal powers of the EFTA Court does not extend quite as far as for the ECJ. But in reality, the difference is not so big. For instance, the EFTA court make binding judgments on infringements proceedings against the member states, such cases are often brought to the court by the EFTA Surveillance authority, in the same way as the Commission bring a case against a member state to the ECJ. The instruments are also slightly weaker, for instance, the EFTA court, can not, however, impose a financial penalty on the countries that have not complied.

As regards preliminary rulings, it is also very much the same procedures as in the EU. The system for making referrals from national courts to Luxembourg is almost the same. As you know, the preliminary judgements from ECJ are binding for national courts, and here there is a slight formal difference. The equivalent in the EFTA Court, is called, advisory opinion. These opinions are not formally binding, however, in effect the differences between ECJ and EFTA court are very small, since it has proved difficult of the national court to go against the advisory opinion of the EFTA court.

I therefore think Open Europe, perhaps exaggerates the significance of the formal differences between the sourts, in reality the differences are quite small.

(*Open Europe, What if? The consequences, challenges and opportunities facing Britain outside the EU, p56 http://2ihmoy1d3v7630ar9h2rsglp.wpengine.netdna-cdn.com/wp-content/uploads/2015/03/150507-Open-Europe-What-If-Report-Final-Digital-Copy.pdf)

3) In relation to invoking Article 112 to limit the free movement of persons, Open Europe* has argued that the EU would also be able to take "retaliatory proportionate rebalancing measures". To your knowledge is this true?

Response Sverdrup

To my knowledge, I would say yes, this is true. Art 112 is the safety clause of the Agreement, and it regulates the possibilities for suspending elements of the agreement. The procedures for managing an Art 112 situation is spelled out in article 113 and article 114, so you should have a look at these paragraphs and perhaps also consult a legal expert.

To my knowledge, the counter measures used by the EU in case a country activates 112, is however, not necessarily retaliatory. The principle is to rebalance the agreement, if one of the parties withdraw from its obligations, and

the rules are designed to prevent any lasting imbalances. The responses by the EU are supposed to be proportional etc, but you have to keep in mind that there are no appeal, or court mechanisms to determine or test if any counter measures are proportional or adequate. In practice, the counter measures can therefore be retaliatory.

(*Open Europe, What if? The consequences, challenges and opportunities facing Britain outside the EU, p56 http://2ihmoy1d3v7630ar9h2rsglp.wpengine.netdna-cdn.com/wp-content/uploads/2015/03/150507-Open-Europe-What-If-Report-Final-Digital-Copy.pdf)

8 October 2016

Dr Christos Tsinopoulos, Senior Lecturer, Durham University, and Professor John Manners-Bell, Chief Executive, Transport Intelligence Ltd – Oral evidence (QQ 30-39)

Transcript to be found under Professor John Manners-Bell, Chief Executive, Transport Intelligence Ltd

Dr Christos Tsinopoulos, Senior Lecturer, Durham University – Written evidence (ETG0008)

1. **In your experience, which we understand relates to the car industry, how sensitive are value chains in Europe to price changes, i.e. how many sourcing decisions are likely to change in the UK with respect to components sourced from the EU, and in the EU with respect to components sourced from the UK, if prices were to rise by 1%, 5% or 10% because of trade barriers between the EU and the UK?**

Thank you for the opportunity for responding to this important question. To answer it I had to conduct some qualitative analysis by asking colleagues and contacts in academia and the automotive sector more generally. Clearly, a complete answer using the three quantitative scenarios you outline above would require the collection so some empirical data. Such an approach would require the inclusion of several assumptions, e.g. on the sensitivity of the pricing on thousands of components. Based on the discussions I have had with representatives of OEMs, tier one suppliers (suppliers of OEMs), and my own understanding of the supply chain decisions, I offer the following thoughts.

Trade barriers and more specifically, tariffs, are often seen as a key issue in the decision making process of location of a part of the supply chain. Such barriers increase costs, and complicate decision making.

High margin models and brands are more likely to be able to sustain an increase in the costs. However, this is less likely to be the case with the models and brands where margins are lower. The degree to which this will be affected will also depend on the type of product that is being produced. In the UK we have examples of both higher and lower margin products.

Therefore, the answer to the above will depend on the type of product that is being sourced and the position in the supply chain. For lower margin models and brands, e.g. small relatively cheap cars, where cost is more important, an increase of 1% would probably lead to a marginal increase of cost. My view is that this would fall within the contingency plan of most companies, e.g. in relation to exchange rate fluctuations. An increase of 5% would probably lead to a significant investment considerations. For higher margin products, e.g. luxury cars where innovation is more important, a 5% increase would probably lead to higher costs but the impact on brand an innovation would probably not lead to significant changes, at least in the short term. In both cases an increase of 10% would probably be prohibitive.

2 October 2016

Peter Ungphakorn, Former Senior Information Officer, World Trade Organization Secretariat, 1996-2015 – Written evidence (ETG0005)

THE QUESTIONS:

Following the first evidence sessions of the inquiry, we have some questions relating specifically to agriculture and the WTO, which we would very much appreciate your assistance with. If you would be willing to answer these questions for the Committees, they would form part of the formal written evidence volume for the inquiry, and would be used as part of the Committees' report into the frameworks for UK trade after Brexit.

REPLY (PREFACE):

For all questions, there is still a considerable amount of uncertainty because we don't know the answer to three underlying questions: (1) **what the UK is going to seek** in the whole Brexit package, including in the WTO,[32] and what its attitude to its counterparts will be; (2) **how the EU will respond**; (3) **how the rest of the world will respond**.

We can only make educated guesses. Other countries' reactions will depend on the content of the UK's position on the WTO, on its diplomatic skills in sustaining their goodwill, and on their own internal pressures and priorities. If the UK, EU and the rest of the world do not cooperate with each other the negotiations are likely to be lengthy and messy.

That said, it's important to note that there are a number of different views on this. Some experts argue that the UK can identify its legal rights as inherited from those of the EU, and then establish its own schedules with little or no negotiation. There might be some limited bargaining over tariff quotas and domestic support. The UK could make its legal claim, leaving it up to other countries to challenge anything they dislike through the WTO's dispute settlement procedures — and the UK would prevail.[33]

Counter-arguments include the view that WTO dispute rulings are unpredictable because of the complexity of WTO and international law and because of adjudicators' individual thinking, meaning the fate of the legal argument would be uncertain. Some also argue that because this position is based largely on law, it overlooks processes, politics and diplomacy in the WTO, including what might happen if other countries claim the right to negotiate with the UK, and the UK replies "see you in court".[34]

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[32] Peter Ungphakorn, "Nothing simple about UK regaining WTO status post-Brexit", https://tradebetablog.wordpress.com/2016/06/07/uk-wto-brexit/

[33] See for example Lorand Bartels, "The UK's Status in the WTO after Brexit", http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2841747, and a two-part article "Understanding the UK's position in the WTO after Brexit", www.ictsd.org/opinion/understanding-the-uk

[34] I discuss some of this in "Second bite — how simple is the UK-WTO relationship post-Brexit?", https://tradebetablog.wordpress.com/2016/08/17/2nd-bite-how-simple-uk-eu-wto/

The questions that we have are as follows:

1. What will be the main issues relating to agriculture in the renegotiation of the UK's WTO schedules following Brexit?

ANSWER:

Potentially most issues covered by two of the three "pillars" of WTO agriculture commitments[35] —**market access** and **domestic support**. How difficult negotiations on these will be will depend on how cooperative with each other the UK, EU and rest of the world are.

FIRST, "**export competition**", the third pillar, which we can quickly get out of the way. It includes **export subsidies** and three areas of policy that may contain hidden subsidies: government involvement in **export credit and insurance**, **food aid**, and **state trading exporting enterprises**. WTO members have agreed to outlaw export subsidies and to discipline the three other components,[36] albeit in a somewhat weaker form than the EU had originally demanded. If the UK accepts the whole package, then this should be implemented without any problems.

SECOND, **market access**. Here the most difficult negotiations will be about **tariff quotas (TRQs)** (*discussed in the next question*).

For **regular "most favoured nation" (MFN) tariffs**, many of the EU's scheduled tariffs can be adopted by the UK with little difficulty and this would probably come under simpler WTO rules on "rectifying" schedules. However, some MFN tariffs may still face negotiations if other countries (such as South Africa) question the UK's need to continue with the EU's complex tariffs protecting certain producers (such as Mediterranean orange producers). UK retailers and consumers might also want lower tariffs and cheaper products. This could lead to a debate within the UK itself, along with a triangle of external negotiations between the UK, EU (on behalf of Spain et al) and non-EU exporting countries.[37]

There might also be some discussion over "**special safeguards (SSGs)**", where import duties can be raised temporarily to deal with import surges or price falls. Some countries might question whether the UK needs to reserve the right to use the safeguards on the EU's entire list of eligible products, particularly if the UK is not a producer.

FINALLY, **domestic support**. Here the key question is about the types that distort trade (by influencing prices or stimulating production, or both), calculated

[35] The WTO's extensive coverage of its work on agriculture is at www.wto.org/agriculture and on its agriculture negotiations at www.wto.org/agnegs
[36] The decision from the 2015 Nairobi Ministerial Conference is at www.wto.org/english/thewto_e/minist_e/mc10_e/l980_e.htm with an explanation at www.wto.org/english/thewto_e/minist_e/mc10_e/briefing_notes_e/brief_agriculture_e.htm#exportcompetition
[37] Peter Ungphakorn, "Oranges: a litmus test of UK post-Brexit tariff negotiations", https://tradebetablog.wordpress.com/2016/09/10/oranges-litmus-test/

in the WTO as **aggregate measurement of support (AMS)**.[38] There is an on-going discussion among legal and trade experts about the appropriate basis for extracting the UK's AMS entitlement from the EU's.[39] But the actual support provided by the EU is much lower than its limit in the WTO — in 2012/2013 only €5.9bn or 8% of its €72.4bn ceiling, according to the EU's latest notification to the WTO. Therefore some "ballpark" calculation for the split ought to be agreed without too much difficulty. If there is a problem, this could well be a sign of ill-will between the UK and the countries concerned.

2. The EU has, as part of its schedule of commitments, established tariff rate quotas (TRQs) on the import of agricultural products from third countries. Other countries have done the same for agricultural imports from the EU. The separation of these quotas between the EU and UK post-Brexit has been named as a major difficulty. Why is that the case? What would be the most contentious issues?

   (*There is a third aspect to consider as well: **the UK's access to the EU's post-Brexit TRQs**, particularly if there is no UK-EU deal that includes free trade in goods. Like the UK, the EU will also have to modify or rectify its TRQs and to negotiate. The UK would want to be part of those talks.*)

   The reasons are both political and technical.[40] TRQs are on the front line in the battle between exporters with offensive interests and import markets with defensive interests. They are on products where exporters fight hardest for market access, and importing countries are under the most intense domestic pressure to protect their producers.

   In summary, the task of extracting UK TRQs from the EU's requires potentially contentious decisions on:

   - how the present EU TRQs should be split to create separate TRQs for the UK and the EU–27
   - how the shares for specific exporting countries should be handled (their proportionate interests in UK and EU markets may vary)
   - how UK-EU trade should be added to the TRQs, and how the sum of the EU–27 and UK TRQs should be expanded for this and other purposes
   - whether these adjustments can still fall under "rectification" of schedules rather than "modification" which is a lengthier process with more specific requirements for negotiations

[38] The WTO's different categories of domestic support (the amber, green and blue "boxes") are explained at www.wto.org/english/tratop_e/agric_e/agboxes_e.htm

[39] See for example, Alan Matthews, "WTO dimensions of a UK 'Brexit' and agricultural trade", http://capreform.eu/wto-dimensions-of-a-uk-brexit-and-agricultural-trade/; and Lorand Bartels' article cited previously, pp.11–12. Conversations I have been privileged to observe include questions such as whether splitting the UK's AMS from the EU's should be based on historical shares from the 1986–94 Uruguay Round negotiations, when the EU's schedule was originally established, or more recent figures, and how a suitable exchange rate might be established for converting commitments in euros to sterling (or even whether to dodge exchange rates completely and keep the UK's commitments in euros)

[40] This is described in detail in Peter Ungphakorn, "The Hilton beef quota: a taste of what post-Brexit UK faces in the WTO", https://tradebetablog.wordpress.com/2016/08/10/hilton-beef-quota/

Each of those questions is both technical and political with real commercial interests involved.

A list of the TRQs on agricultural products is annexed to these replies.

In more detail, dairy, beef, lamb, poultry meat, sugar, fruits and vegetables and many other products all have EU TRQs. Several of these products are contentious in free trade talks (such as TPP across the Pacific and the trans-Atlantic TTIP) and are likely to continue to face the toughest post-Brexit negotiations. How difficult this will be depends on how accommodating the UK, EU and the rest of the world are with each other.

TRQs arose because for many agricultural products, the tariffs that resulted from the 1986–94 Uruguay Round negotiations were so high they would seriously obstruct imports. Exporting countries demanded some market access and the compromise was lower duties on limited quantities, the TRQs.

Technically, as well as politically, TRQs are complex because many of them are also divided up among exporting countries. For example, in the latest available EU schedule (for the old EU–15), the duty-free lamb TRQ is shared out among Argentina, Australia, Chile, New Zealand, Uruguay and nine other countries (several now EU members) with only 200 tonnes out of 283,825 left for "other" countries.[41] And UK-EU trade also needs to be taken into account if the UK does not have free trade in goods with the EU–27 — for obvious reasons, the UK's present imports and exports within the EU do not come under the EU's TRQs.

UK exports to the EU via the EU's TRQs: note that as things stand, if the UK wants to export lamb to the EU through the EU's TRQ, it will have to fight for a share of the 200 tonnes for "other countries". But in 2015 it shipped almost 75,000 tonnes duty-free to the EU.[42] That's why it would want to participate in negotiations over a TRQ for the EU–27 if it doesn't have duty-free access to the EU market. In fact, it may be difficult to separate the negotiations over the UK's and EU's TRQs.

As for other countries' TRQs on exports from the UK and EU, most commentators have only mentioned these in passing.[43] Splitting existing quotas into UK and EU components would be less complex than for their own import quotas. For example the overall current quota size would not need changing, but some negotiation cannot be ruled out.

3. In the negotiations over the division of these TRQs, which countries would have an interest in increasing or decreasing the UK's TRQs, and why?

Most if not all countries that currently use the TRQs have an interest in negotiating the UK's, plus possibly some new players. They will also have an interest in the TRQs left for the post-Brexit EU–27, one reason why it will be

[41] See https://tradebetablog.files.wordpress.com/2016/08/mutton-lamb-trq_eu-151.png, an image used in the previously cited article on the Hilton beef quota
[42] www.uktradeinfo.com
[43] See Alan Matthews' article, previously cited. He says: "in the case of [other countries'] import TRQs there is a more realistic possibility that these might be divided between the UK and the EU27 if there were a will to do this" (my emphasis)

difficult to separate the negotiations over the UK's and EU's schedules. (At this stage we are not discussing increasing or decreasing the UK's TRQs, simply establishing how big they should be.)
Countries that currently have shares of the quotas specifically allocated to them — because of their commercial interests — would have a particular claim. If establishing the UK's and EU's separate TRQs is seen as "modifying" the schedules, then there are WTO rules that state broadly who is eligible to negotiate. They are countries that were originally involved in the negotiations (and any others having a "principal supplying interest") and countries with a "substantial interest".[44]

These are not defined. Excluded countries sometimes argue that they should be involved as well, as China did when the EU modified its schedule on poultry import quotas.[45] It's possible to envisage new players claiming a "substantial interest" for example countries that are starting to become major exporters of cereals or beef but did not previously have shares of the EU's TRQs. The UK and EU could argue that they were not renegotiating the TRQs, simply splitting them. Much would depend on the approach adopted and how other countries responded.

4. Does the fact that the EU's schedule has not been certified complicate the division of TRQs between the EU and the UK?

   It depends. If all the countries concerned are willing to accept the schedules that the EU is applying in practice, then negotiations can proceed on them. But those schedules (assuming they exist in an up-to-date form) are uncertified and are therefore still secret. If other countries wanted to be difficult they might insist on knowing the schedules and negotiating from official versions. This is a hypothetical situation; we don't know how it would turn out.

5. What non-tariff barriers are most pertinent to trade in agricultural products in the absence of any preferential agreement?

   It depends on the product and the supplying country, but the presence or absence of a preferential agreement is probably irrelevant since the preferences only apply to tariffs, not non-tariff measures. (Lower tariffs actually increase exposure to non-tariff barriers.)
   All agricultural products come under the two WTO agreements dealing with product standards and regulation, and over the years, concerns have been raised in the WTO about a wide range of issues.
   The two are the agreements on **Sanitary and Phytosanitary Measures (SPS)** and **Technical Barriers to Trade (TBT)**. SPS deals with food safety (where related to disease or toxins, for example) and animal and plant health; TBT includes other product standards (including some aspects of food and "health", such as nutritional requirements), labelling and other regulations. The

[44] GATT Articles 28 and 28 bis (www.wto.org/english/docs_e/legal_e/gatt47_02_e.htm#articleXXVIII) and subsequent additions (www.wto.org/english/docs_e/legal_e/gatt47_03_e.htm#annexi)
[45] WTO, "China and EU differ in farm committee over right to renegotiate commitments", www.wto.org/english/news_e/news12_e/agcom_20sep12_e.htm

committees dealing with each have a good record of resolving problems and avoiding litigation.[46]

Although all measures under these agreements can be scrutinised in the WTO, most are trouble-free — **non-tariff barriers are often justifiable**, for example to prevent diseases spreading.
Quite a few concerns are raised in question-and-answer sessions. They focus on whether the measures are justified or whether the process of applying them is appropriate, either because they cause problems generally or because individual exporting countries face difficulties.

The most commonly questioned **SPS** measures deal with: **animal diseases** such as BSE, bird flu, foot and mouth disease, and African swine fever; **plant problems** such as fruit flies and other pests, and plant diseases; and **food issues** such as pesticide residues and aflatoxin contamination (associated with fungi). The wide range of concerns raised about agricultural products under **TBT** include **health labelling**, and **controls on the consumption** of tobacco, alcoholic drinks and "junk food".

Issues raised also deal with **mutual recognition** of various controls and whether measures countries take can be considered to provide **equivalent protection** against risk even if the actual measures are not the same. Increasingly discussed are **standards set by the private sector** and whether governments have a responsibility to discipline these under the WTO's inter-governmental agreements.

Developing countries do find it difficult to meet some standards in developed countries, and quite often technical assistance is given to help them upgrade their inspection services and other areas of infrastructure (a topic the UK could consider as it leaves the EU).

In one respect, the UK will avoid a problem that it sometimes faces as an EU member: failure to observe "**regionalisation**". When WTO members restrict problematic products, they are supposed focus only on those from the regions where the problems exit, such as where an animal disease (foot and mouth disease, BSE, etc) has been found, not entire countries or other territories. The EU has frequently complained that products from all its member states have been targeted even though the disease only exists in some areas of some of its members. By leaving the EU, the UK would not suffer bans on products from the whole EU.

Annex: The EU's tariff quotas on agricultural products

Below is an extract from the most recent certified schedule (for the EU–15), WTO document WT/LET/666.

The table below contains agricultural products as defined in the WTO Agriculture Agreement, which excludes fishery and forestry products. Elsewhere, the EU's schedule also has TRQs on these:

[46] WTO information on these two subjects are at www.wto.org/sps and www.wto.org/tbt

- tunas (of the Genus Thunnus) and fish of the Genus Euthunnus (17,250 tonnes at 0% duty)
- herrings (34,000 tonnes at 0%)
- dogfish of the species Squalus acanthias (5,000 tonnes at 6%)
- silver hake (Merluccius bilinearis) (2,000 tonnes at 8%)
- fish of the genus Coregonus (1,000 tonnes at 5.5%)
- cod of the species Gadus morhua (10,000 tonnes at 8%)
- frozen fillets of hake of the genus Merluccius, presented as industrial block, with pin bones (standard), from 1 July to 31 December (5,000 tonnes at 10% subject to compliance with the reference price)
- fish of the species Allocyttus spp. and Pseudocyttus maculatus (200 tonnes at 0%)
- cod of the species Gadus morhua and Gadus ogac. and fish of the species Boreogadus saida (25,000 tonnes at 0%)
- freshwater crayfish, cooked in dill, frozen (3,000 tonnes at 0%)
- shrimps of the species Pandalus borealis, shelled, boiled, frozen, but not further prepared (500 tonnes at 0%)
- some types of coniferous plywood (650,000m^3 at 0%)

For simplicity, some columns in the table have been removed. The first column counting the TRQs, and the lines separating them, have been added:

Schedule CXL - EUROPEAN COMMUNITIES

This schedule is authentic only in the English language

PART I - MOST-FAVOURED-NATION TARIFF

SECTION I - Agricultural Products

SECTION I - B Tariff Quotas

	Description of products	**Tariff item number(s)**	**Final quota quantity and in-quota tariff rate**	**Other terms and conditions**
	1	2	4	7
	Current Access Quotas			
1	Live bovine animals	0102.90.30 Ex	5.000 head 6%	Heifers and cows (other than for slaughter) of the following mountain breeds grey, brown, yellow, spotted Simmental and Pinzgau.
2	Live bovine animals	0102.90.30 Ex	5.000 head 4%	Bulls, cows and heifers (other than for slaughter) of the following mountain breeds : spotted

	Description of products	Tariff item number(s)	Final quota quantity and in-quota tariff rate	Other terms and conditions
				Simmental, Schwyz and Fribourg. Animals must be covered by the following documents:
				- bulls : pedigree certificate
				- cows and heifers : pedigree certificate of herd book entry certificate attesting to the purity of the breed.
3	Live bovine animals	0102.90.20 Ex	169.000 head	Live young male bovine animals weighing 300 kg or less
		0102.90.30 Ex	16% +	intended for fattening.
			582 Euro/t	Qualification for the quota is subject to conditions laid down in the relevant Community provisions.
4	Meat of bovine animals, fresh or chilled	0201 Ex		"High quality" meat, with or without bone, allocated to supplying
	Meat of bovine animals, frozen	0202 Ex		countries as follows :
			37.800 t	Argentina 17.000 t
			(Product	USA / Canada 11.500 t
			weight)	Australia 7.000 t
			20%	Uruguay 2.300 t
	Edible offal			Qualification for the quota is subject to conditions laid down in the
	- Of bovine animals, fresh or chilled			relevant Community provisions.
	-- Thick skirt and thin skirt	0206.10.95 Ex		
	- Of bovine animals, frozen			
	-- Thick skirt and thin skirt	0206.29.91 Ex		

	Description of products	Tariff item number(s)	Final quota quantity and in-quota tariff rate	Other terms and conditions
5	Meat of bovine animals, frozen	0202		
	Edible offal		53.000 t	
	- Of bovine animals, frozen		(Without	
	-- Thick skirt and thin skirt	0206.29.91	bone)	
			20%	
6	Meat of bovine animals, frozen			Supplying country : Australia
	- Boneless			
	-- Buffalo meat	0202.30.90 Ex	2.250 t	Qualification for the quota is subject to conditions laid down
			(Without	in the relevant Community provisions.
			bone)	
			20%	
7	Meat of bovine animals, frozen			
	- Unseparated or separated forequarters	0202.20.30		
	- Boneless	0202.30	50.700 t	The quantity may according to Community provisions be
	Edible offal		(Bone-in)	converted into an equivalent quantity of high quality meat.
	- Of bovine animals. frozen			The meat imported shall be used for processing.
	-- Thick skirt and thin skirt	0206.29.91	(*)	(*) The tariff rate is :
				-20 % ad valorem when the meat is intended for the manufacture of preserved for which does not contain characteristic components other than beef and jelly
				- 20 % ad valorem + 45 % of the specific base rate of duty when the meat is intended for the

	Description of products	Tariff item number(s)	Final quota quantity and in-quota tariff rate	Other terms and conditions
				manufacture of products other than the preserved food referred to in the first indent.
				Qualification for and allocation of the quota is subject to conditions laid down in the relevant Community provisions.
8	Edible offal			Allocated to supplying countries as follows : Argentina 700 t
	- Of bovine animals, frozen			Other 800 t
	-- Thin skirt (whole)	0206.29.91 Ex	1.500 t	Qualification for the quota is subject to conditions laid down in
			4%	the relevant Community provisions.
9	Live sheep and goats, other than pure-bred	0104.10 Ex		Allocated to supplying countries as follows:
	breeding animals		39.310 t	Poland 12.340 t
		0104.20 Ex	10%	Rumania 1.010 t
				Hungary 21.385 t
				Bulgaria 4.255 t
				Former Yugoslav Republic
				of Macedonia 215 t
				Other 105 t
				Qualification for the quota is subject to conditions laid down in the
				relevant Community provisions.
10	Live sheep and goats, other than pure-bred	0104.10 Ex	800 t	Allocated to Czech and Slovak Republic as supplying countries.
	breeding animals	0104.20 Ex	(Carcase	Qualification for the quota is subject to conditions laid down

	Description of products	Tariff item number(s)	Final quota quantity and in-quota tariff rate	Other terms and conditions
	Meat of sheep or goats, fresh, chilled	0204	weight)	in the relevant Community provisions.
	or frozen		10%	
11	Meat of sheep or goats,	0204	283.825 t	Allocated to supplying countries as follows:
	fresh chilled or frozen		(Carcase	Argentina 23.000 t
			weight)	Australia 18.650 t
			0%	Chile 3.000 t
				New Zealand 226.700 t
				Uruguay 5.800 t
				Iceland 600 t
				Poland 200 t
				Rumania 75 t
				Hungary 1.150 t
				Bulgaria 1.250 t
				Bosnia Herzegovina 850 t
				Croatia 450 t
				Slovenia 50 t
				Former Yugoslav Republic
				of Macedonia 1.750 t
				Greenland 100 t
				Other 200 t
				Qualification for the quota is subject to conditions laid down
				in the relevant Community provisions.
12	Butter	0405.10 Ex	76.667 t	Butter of New Zealand origin
				- at least 6 weeks old
			86.88	- with a fat content of not less than 80 % but less than 82 %
			Euro/100 kg	by weight
				- manufactured directly from milk or cream

	Description of products	Tariff item number(s)	Final quota quantity and in-quota tariff rate	Other terms and conditions
				Qualification for the quota is subject to conditions laid down in the
				relevant Community provisions.
13	Cheese for processing	0406.90.11 Ex	4.500 t	Allocated to supplying countries as follows:
				New Zealand 4.000 t
			17.06	Australia 500 t
			Euro/100 kg	Qualification for the quota is subject to conditions laid down in
				the relevant Community provisions.
14	Cheddar	0406.90.21 Ex	10.250 t	Allocated to supplying countries as follows:
				New Zealand 7.000 t
			17.06	Australia 3.250 t
			Euro/100 kg	Whole Cheddar cheeses (of the conventional flat cylindrical shape of a net weight of not less than 33 kg but not more than 44 kg and cheeses of the conventional flat cylindrical shape or cheeses in parallelepiped shape, of a net weight of 10 kg or more) of a minimum fat content of 50 % by weight in the dry matter, matured for at least three months.
				Qualification for the quota is subject to conditions laid down in the relevant Community provisions.
15	Cheddar	0406.90.21 Ex	4.000 t	Allocated to Canada as supplying country.
				Made from unpasteurised milk, of a

	Description of products	Tariff item number(s)	Final quota quantity and in-quota tariff rate	Other terms and conditions
				minimum fat content of 50 %
			13.75	by weight in the dry matter, matured for at least nine months, of a
			Euro/100 kg	free-at-frontier value per 100 kg net, of not less than
				- 334,20 Euro in standard whole sizes
				- 354,83 Euro for cheeses of a net weight of not less than 500 g
				- 368,58 Euro for cheeses of a weight less than 500 g.
				Qualification for the quota is subject to conditions laid down in the relevant Community provisions.
				The expression "standard whole sizes" shall be taken to apply to cheeses of the
				- conventional flat cylindrical shape of a net weight not less than 33 kg but not more than 44 kg
				- conventional flat cylindrical shape or parallelepiped shape, of a net weight of 10 kg or more.
16	Cucumbers, fresh or chilled:			
	- From 1 November to 15 May	0707.00.11	1.100 t	(*) the entry prices (including the specific duties) will apply in the
			2.50%	same way as outside the quota
			(*)	

	Description of products	Tariff item number(s)	Final quota quantity and in-quota tariff rate	Other terms and conditions
17	Manioc (casava)	0714.10	5.500.000 t	Within maximum quantity of 21 million tonnes over each 4 year
			6%	period. Allocated to Thailand as supplying country.
				Qualification for this quota is subject to conditions laid down in the relevant Community provisions.
18	Manioc (casava), other than pellets of flour	0714.10 Ex	1.352.590 t	Allocated to supplying countries as follows:
	and meal		6%	Indonesia 825.000 t
	Arrowroot, salep and similar roots and tubers	0714.90 Ex		Other GATT countries except Thailand 145.590 t
	with high starch content			China 350.000 t
				Other non-GATT countries 32.000 t of which 2.000 t shall be of a kind used for human consumption, in immediate packing of a net content not exceeding 28 kg, either fresh and whole or without skin and frozen, whether or not sliced.
19	Sweet potatoes			Allocated to countries other than China.
	- Other than for human consumption	0714.20.90	5.000 t	
			0%	
20	Sweet potatoes			Allocated to China.
	- Other than for human consumption	0714.20.90	600.000 t	Qualification for the quota is subject to conditions laid down in
			0%	the relevant Community provisions.

	Description of products	Tariff item number(s)	Final quota quantity and in-quota tariff rate	Other terms and conditions
21	Fresh bananas, other than plantains	0803.00.12	2.200.000 t	As indicated in the Annex.
			75 Euro/t	
22	Oranges	0805.10 Ex	20.000 t	High quality sweet oranges during the period 1 February to
	- Sweet oranges, fresh		10%	30 April.
				Qualification for the quota is subject to conditions laid down in the relevant Community provisions.
23	Other citrus hybrids	0805.20 Ex	15.000 t	Citrus hybrids known as "minneolas" during the period 1 February
			2%	to 30 April.
				Qualification for the quota is subject to conditions laid down in the relevant Community provisions.
24	Lemons	0805.30.10	10.000 t	During the period 15 January to 14 June.
			6%	
25	Table grapes, fresh	0806.10.19 Ex	1.500 t	(*) the entry prices (including the specific duties) will apply in the
	- From 21 July to 31 October		9%	same way as outside the quota
			(*)	
26	Apples, fresh:	0808.10.99	600 t	(*) the entry prices (including the specific duties) will apply in the
	- From 1 April to 31 July		0%	same way as outside the quota
			(*)	
27	Pears, fresh, other than peery pears	0808.20.39	1.000 t	(*) the entry prices (including the specific duties) will apply in the
	in bulk:		5%	same way as outside the quota

	Description of products	Tariff item number(s)	Final quota quantity and in-quota tariff rate	Other terms and conditions
	- From 1 August to 31 December		(*)	
28	Apricots, fresh	0809.10.00 Ex	500 t	
	- From 1 August to 31 May		10%	
29	Other	0809.10.00 Ex	2.500 t	(*) the entry prices (including the specific duties) will apply in the
			10%	same way as outside the quota
			(*)	
30	Cherries, fresh, other than sour cherries:			
	- From 21 May to 15 July	0809.20.10 Ex	800 t	(*) the entry prices (including the specific duties) will apply in the
			4%	same way as outside the quota
			(*)	
31	Maize	1005.90.00	2.000.000 t	To be imported into Spain. In addition, the quota Quantity is
			(*)	reduced by quantities of imports into Spain from third countries of
32	Grain sorghum	1007.00.90	300.000 t	maize gluten feed, brewers' grains and citrus pulp
			(*)	(*) The rate shall be fixed by the competent Community authorities
				so as to ensure that the quota will be filled.
33	Broken rice, intended for the production of	1006.40.00	1.000 t	Qualification for this quota is subject to conditions laid down in
	foodstuffs of tariff heading 1901.10		0%	the relevant Community provisions
34	Millet	1008.20.00	1.300 t	
			7 Euro/t	
35	Manioc starch	1108.14.00 Ex	8 000 t	Intended for the manufacture of

	Description of products	Tariff item number(s)	Final quota quantity and in-quota tariff rate	Other terms and conditions
			170.59 Euro/t	- food preparations put up for retail sale and failing within heading No 1901 or
				- tapioca in the form of grains or pearls put up for retail sale falling within heading No 1903
				Qualification for the quota is subject to conditions laid down in the relevant Community provisions.
36	Manioc starch	1108.14.00 Ex	2.000 t	Intended for the manufacture of medicaments failing within
			170.59 Euro/t	heading No 3003 or 3004.
				Qualification for the quota is subject to conditions laid down in the relevant Community provisions.
37	Cane or beet sugar	1701	1.304 700 t	Allocated to supplying countries as follows
			(White sugar	India 10.000 t
			equivalent)	ACP countries 1.294.700 t in accordance with the provisions
			0%	of the Lomé Convention.
38	Raw cane sugar, for refining	1701.11.10	85.463 t	(*) This rate applies to raw sugar with a yield of 92%
			98 Euro/t	Entry under this subheading is subject to conditions laid down
			(*)	in the relevant Community provisions
39	Chemically pure fructose	1702.50.00	4.504 t	
			20%	

	Description of products	Tariff item number(s)	Final quota quantity and in-quota tariff rate	Other terms and conditions
40	Mushrooms, prepared or preserved		62.660 t	Quantity expressed in drained weight.
	otherwise than by vinegar or acetic acid :			
	- Of the species Agaricus:			
	-- Provisionally preserved, completely	2003.10.20	23%	(*) Final quota applicable as from 1996.
	cooked			
	-- Other	2003.10.30	23%	Allocated to supplying countries as follows
	Vegetables provisionally preserved but			1995: Poland 32.480 t
	unsuitable in that state for immediate			Other countries 28.780 t
	consumption :			After 1995 : Poland 33.880 t
	Mushrooms of the species Agaricus	0711.90.40	12%	Other countries 28.780 t
41	Bran, sharps and other residues whether or		475.000 t	Qualification for the quota is subject to conditions laid down
	not in the form of pellets derived from the sifting, milling or other working of cereals:			in the relevant Community provisions.
	- Of wheat :			
41a	-- Of which the starch content does not exceed 28 % by weight, and of which the proportion that passes through a sieve with an aperture of 0,2 mm does not exceed 10 % by	2302.30.10	30,6 Euro/t	

	Description of products	Tariff item number(s)	Final quota quantity and in-quota tariff rate	Other terms and conditions
	weight or alternatively the proportion that passes through the sieve has an ash content, calculated on the dry product, equal to or more than 1,5% by weight			
41b	-- Other	2302.30.90	62,25 Euro/t	
	- Of other cereals (than maize or rice) :			
41c	-- Of which the starch content does not exceed 28 % by weight, and of which the proportion that passes through a sieve with an aperture of 0,2 mm does not exceed 10 % by weight or alternatively the proportion that passes through the sieve has an ash content, calculated on the dry product, equal to or more than 1,5% by weight	2302.40.10	30,6 Euro/t	
41d	-- Other	2302.40. 90	62,25 Euro/t	
42	Preparation consisting of a mixture of malt	2309.90.31 Ex	100.000 t	
	sprouts and of barley screenings		0%	
	before the malting process (possibly			

	Description of products	Tariff item number(s)	Final quota quantity and in-quota tariff rate	Other terms and conditions
	including other seeds) with barley			
	cleanings after the malting process,			
	and containing by weight 15,5 % or			
	more of protein.			
	Preparation consisting of a mixture of	2309.90.41 Ex		
	malt sprouts and of barley screenings			
	before the malting process (possibly			
	including other seeds) with barley			
	cleanings after the malting process,			
	and containing by weight 15,5 % or			
	more of protein and not more than 23 %			
	of starch.			
43	Preparation consisting of a mixture of	2309.90.31 Ex	) 20.000 t	
	malt sprouts and of barley screenings		) 0%	
	before the malting process (possibly			
	including other seeds) with barley			
	cleanings after the malting process,			
	and containing by weight 12,5 % or			
	more of protein.			

	Description of products	Tariff item number(s)	Final quota quantity and in-quota tariff rate	Other terms and conditions
	Preparation consisting of a mixture of	2309.90.41 Ex		
	malt sprouts and of barley screenings			
	before the malting process (possibly			
	including other seeds) with barley			
	cleanings after the malting process,			
	and containing by weight 12,5 % or			
	more of protein and not more than 28 %			
	of starch			
44	Preparation of a kind used in animal feeding:		2.800 t	
	- Other:		7%	
	-----Containing no milk products or			
	containing less than 10% by weight of such			
	products:			
	-----Containing no starch or containing 10%	2309.90.31		
	or less by weight of starch			
	-----Containing more than 10% but not more	2309.90.41		
	than 30% by weight of starch			
	-----Containing more than 30% by weight	2309.90.51		
	of starch			

	Description of products	Tariff item number(s)	Final quota quantity and in-quota tariff rate	Other terms and conditions
	Non-tariffied product quotas			
45	Potatoes, fresh or chilled:			
	--- New:			
	---- From 1 January to 15 May	0701.90.51	4.000 t	
			3%	
46	Carrots and turnips, fresh or chilled	0706.10.00	1.200 t	
			7%	
47	Other vegetables, fresh or chilled:			
	- Fruits of the genus Capsicum or of the			
	genus Pimenta:			
	-- Sweet peppers	0709.60.10	500 t	
			1.5%	
48	Dried onions	0712.20.00	12.000 t	
			10%	
49	Almonds, other than bitter	0802.11 Ex	90.000 t	
		0802.12 Ex	2%	
50	Orange juice		1.500 t	Frozen concentrated orange juice, without added sugar, having a
	- Frozen		13%	degree of concentration of up to 50° Brix, in containers of two litres
	-- Of a density not exceeding			or less, not containing blood orange concentrate.
	1,33 g/cm3 at 20°C			Qualification for this quota is subject to conditions laid down in
	--- Other	2009.11.99 Ex		the relevant Community provisions

	Description of products	Tariff item number(s)	Final quota quantity and in-quota tariff rate	Other terms and conditions
	Minimum Access Quotas			
51	Boneless meat of bovine animals, fresh or	0201.30.00 Ex		"High quality" meat answering the following definition
	chilled		11.000 t	Special or good-quality beef cuts obtained from exclusively
	Edible offal of bovine animals : thick skirt and thin skirt, fresh or chilled	0206.10.95 Ex	20%	pasture-grazed animals, aged between 22 and 24 months, having two permanent incisors and presenting a slaughter liveweight not exceeding 460 kilograms, referred to as "special boxed beef ", cuts of which may bear the letters "cs" (special cuts)'.
				Qualification for the quota is subject to conditions laid down in the relevant Community provisions.
52	Boneless meat of bovine animals,	0201.30.00 Ex		"High quality . meat answering the following definition:
	fresh or chilled			"Beef cuts obtained from steers (novilhos) or heifers (novilhas)
	Boneless meat of bovine animals, frozen			aged between 20 and 24 months, which have been exclusively
	- Other	0202.30.90 Ex	5.000 t	pasture grazed, have lost their central temporary incisors but do
	Edible offal of bovine animals:		20%	not have more than four permanent incisor teeth, which are of a
	Thick skirt and thin skirt, fresh or chilled	0206.10.95 Ex		good maturity and which meet the following beef carcass
	Thick skirt and thin skirt, frozen	0206.29.91 Ex		classification requirements : meat

	Description of products	Tariff item number(s)	Final quota quantity and in-quota tariff rate	Other terms and conditions
				from B or R class carcasses with rounded to straight conformation and a fat-cover class of 2 or 3;
				the cuts bearing the letters "sc" (special cuts) or an "sc" (special cuts) label as a sign of their high quality will be boxed in cartons bearing the words "high quality beef".
				Qualification for the quota is subject to conditions laid down in the relevant Community provisions.
53	Boneless meat of bovine animals, fresh	0201.30.00 Ex		"High quality" meat answering the following definition:
	or chilled			Special or good-quality beef cuts obtained from exclusively
	Boneless meat of bovine animals, frozen	0202.30.90 Ex		Pasture-grazed animals presenting a slaughter liveweight not
	- Other			exceeding 460 kilograms, referred to as "special boxed beef".
	Edible offal of bovine animals	0206.10.95 Ex	4.000 t	These cuts may bear the letters 'sc" (special cuts)'
	- Thick skirt and thin skirt, fresh chilled		20%	Qualification for the quota is subject to conditions laid down
	- Thick skirt and thin skirt, frozen	0206.29.91 Ex		in the relevant Community provisions.
54	Meat of bovine animals, fresh			"High quality" meat answering the following definition:
	or chilled		300 t	"Selected chilled or frozen premium beef cuts derived from
	- Other cuts with bone in, other	0201.20.90 Ex	20%	exclusively pasture-grazed bovine animals

	Description of products	Tariff item number(s)	Final quota quantity and in-quota tariff rate	Other terms and conditions
	- Boneless	0201.30.00 Ex		which do not have more than four permanent incisor teeth in wear, the carcases of which have a dress weight of no more than 325 kilograms, a compact appearance with a good eye of meat of light and uniform colour and adequate but not excessivefat cover. All cuts will be vacuum packaged and referred to as high-quality beef".
	Meat of bovine animals, frozen:			
	- Other cuts with bone in, other	0202.20.90 Ex		
	- Boneless	0202.30 Ex		
	Thick and thin bovine skirt, fresh or chilled	0206.10.95 Ex		Qualification for the quota is subject to conditions laid down
	Thick and thin bovine skirt, frozen	0206.29.91 Ex		in the relevant Community provisions.
55	Meat of swine, fresh, chilled or frozen :			
	- Carcasses and half-Carcasses of domestic	0203.11.10	15.000 t	Import under the Europe Agreements may be taken into account
	swine, fresh, chilled or frozen	0203.21.10	268 Euro/t	when implementing this quota.
56			5.500 t	Import under the Europe Agreements may be taken into account
	- Cuts of domestic swine, fresh,	0203.12.11	389 Euro/ t	when implementing this quota.
	chilled or frozen, with or without	0203.12.19	300 Euro/ t	
	bone, excluding tenderloin presented alone	0203.19.11	300 Euro/ t	
		0203.19.13	434 Euro/ t	
		0203.19.15	233 Euro/ t	
		0203.19.57 Ex	434 Euro/ t	

	Description of products	Tariff item number(s)	Final quota quantity and in-quota tariff rate	Other terms and conditions
		0203.22.11	389 Euro/ t	
		0203.22.19	300 Euro/ t	
		0203.29.11	300 Euro/ t	
		0203.29.13	434 Euro/ t	
		0203.29.15	233 Euro/ t	
		0203.29.57 Ex	434 Euro/ t	
57	Meat of swine, fresh, chilled or frozen :			
	- Fresh or chilled:			
	--- of domestic swine			
	---- loins and cuts thereof, bone-in	0203.19.13	7.000 t	
	- Frozen :		0%	
	--- of domestic swine			
	---- bellies, streaky and cuts thereof	0203.29.15		
58	- Boneless loins and hams, fresh or chilled	0203.19.57 Ex	34.000 t	Import under the Europe Agreements may be taken into
	- Boneless loins and hams, frozen	0203.29.57 Ex	250 Euro/t	account when implementing this quota.
59	- Tenderloins, fresh or chilled	0203.19.57 Ex	5.000 t	Import under the Europe Agreements may be taken into
	- Tenderloins, frozen	0203.29.57 Ex	300 Euro/t	account when implementing this quota.
60			3.000 t	Import under the Europe Agreements may be taken into
	Sausages, dry or for spreading, uncooked	1601.00.91	747 Euro/t	account when implementing this quota.
	Other sausages	1601.00.99	502 Euro/t	

	Description of products	Tariff item number(s)	Final quota quantity and in-quota tariff rate	Other terms and conditions
61			6.100 t	Import under the Europe Agreements may be taken into
	Preserved meat of domestic swine	1602.41.10	784 Euro/t	account when implementing this quota.
		1602.42.10	646 Euro/t	
		1602.49.11	784 Euro/t	
		1602.49.14	646 Euro/t	
		1602.49.19	428 Euro/t	
		1602.49.30	375 Euro/t	
		1602.49.50	271 Euro/t	
62			6.200 t	Import under the Europe Agreements may be taken into
	Chicken carcass, fresh, chilled or frozen	0207.11.10	131 Euro/t	account when implementing this quota.
		0207.11.30	149 Euro/t	
		0207.11.90	162 Euro/t	
		0207.12.10	149 Euro/t	
		0207.12.90	162 Euro/t	
63			4.000 t	Import under the Europe Agreements may be taken into
	Chicken cuts, fresh, chilled or frozen	0207.13.10	512 Euro/t	account when implementing this quota.
		0207.13.20	179 Euro/t	
		0207.13.30	134 Euro/t	
		0207.13.40	93 Euro/t	
		0207.13.50	301 Euro/t	
		0207.13.60	231 Euro/t	
		0207.13.70	504 Euro/t	
		0207.14.20	179 Euro/t	
		0207.14.30	134 Euro/t	

	Description of products	Tariff item number(s)	Final quota quantity and in-quota tariff rate	Other terms and conditions
		0207.14.40	93 Euro/t	
		0207.14.60	231 Euro/t	
64	- Of fowls of the species Gallus domesticus:			
	-- Cuts and offal, frozen:			
	--- Cuts :			
	---- Boneless	0207.14.10	15.500 t	
	---- With bone In		0%	
	----- Breasts and cuts thereof	0207.14.50		
	----- Other (than halves or quarters; whole wings with or without tips; backs, necks, backs with necks attached, rumps and wing tips; legs and cuts thereof)	0207.14.70		
65	- Of fowls of the species Gallus domesticus:		700 t	
	-- Cuts and offal, frozen:		795 Euro/t	
	--- Cuts :			
	---- Boneless	0207.14.10		
66			1.000 t	Import under the Europe Agreements may be taken into account
	Turkey meat, fresh, chilled or frozen	0207.24.10	170 Euro/t	when implementing this quota.
		0207.24.90	186 Euro/t	
		0207.25.10	170 Euro/t	
		0207.25.90	186 Euro/t	
		0207.26.10	425 Euro/t	
		0207.26.20	205 Euro/t	
		0207.26.30	134 Euro/t	
		0207.26.40	93 Euro/t	

	Description of products	Tariff item number(s)	Final quota quantity and in-quota tariff rate	Other terms and conditions
		0207.26.50	339 Euro/t	
		0207.26.60	127 Euro/t	
		0207.26.70	230 Euro/t	
		0207.26.80	415 Euro/t	
		0207.27.30	134 Euro/t	
		0207.27.40	93 Euro/t	
		0207.27.50	339 Euro/t	
		0207.27.60	127 Euro/t	
		0207.27.70	230 Euro/t	
67	- Of turkeys:			
	-- Cuts and offal, frozen :			
	---Cuts:			
	---- Boneless	0207.27.10	2.500 t	
	---- With bone in		0%	
	----- Halves or quarters	0207.27.20		
	----- Other (than whole wings, with or without tips; backs, necks, backs with necks attached, rumps and wing tips, breasts and cuts thereof; legs and cuts thereof)	0207.27.80		
68	Poultry eggs for consumption, in shell	0407.00.30	135.000 t	Import under the Europe Agreements may be taken into account
			152 Euro/t	when implementing this quota.
69			7.000 t	Import under the Europe Agreements may be taken into account
			(shell egg	when implementing this quota.
			equivalent)	
	Eggs yolks	0408.11.80	711 Euro/t	

	Description of products	Tariff item number(s)	Final quota quantity and in-quota tariff rate	Other terms and conditions
		0408.19.81	310 Euro/t	
		0408.19.89	331 Euro/t	
	Bird eggs, not in shell	0408.91.80	687 Euro/t	
		0408.99.80	176 Euro/t	
70			15.500 t	Import under the Europe Agreements may be taken into account
			(shell egg	when implementing this quota.
			equivalent)	
	Egg albumin	3502.11.90	617 Euro/t	
		3502.19.90	83 Euro/t	
71			68.000 t	Import under the Europe Agreements may be taken into account
	Skimmed milk powder	0402.10.19	475 Euro/t	when implementing this quota.
72			10.000 t	Import under the Europe Agreements may be taken into account
			(in butter	when implementing this quota.
			equivalent)	
	Butter	0405.10	948 Euro/t	
		0405.90		
73	Cheese and curd:			Import under the Europe Agreements may be taken into account
			18.400 t	when implementing this quota.
	- Emmental, Including processed	0406.30.10 Ex	719 Euro/t	
	Emmental	0406.90.14 Ex	858 Euro/t	

	Description of products	Tariff item number(s)	Final quota quantity and in-quota tariff rate	Other terms and conditions
74			5.200 t	Import under the Europe Agreements may be taken into account
	- Gruyere, Sbrinz, Including processed	0406.30.10 Ex	719 Euro/t	when implementing this quota.
	Gruyere	0406.90.14 Ex	858 Euro/t	
75			15.000 t	Import under the Europe Agreements may be taken into account
	- Cheddar	0406.90.21	210 Euro/t	when implementing this quota.
76			20.000 t	Entry under this subheading is subject to conditions laid down
	- Cheese for processing	0406.90.11	835 Euro/t	in the relevant Community provisions.
				Import under the Europe Agreements may be taken into account
				when implementing this quota.
77	- Fresh cheese (unripened or uncured),			Import under the Europe Agreements may be taken into account
	including whey cheese and curd :			when implementing this quota.
	-- Pizza cheese, frozen, cut into	0406.10.20 Ex	5.300 t	
	pieces each weighing not more than	0406.10.80 Ex	130 Euro/t	
	1 gram, in containers with a net content of			
	5 kg or more, of a water content, by weight,			
	of 52 % or more, and a fat content by weight			
	in the dry matter of 38% or more.			

	Description of products	Tariff item number(s)	Final quota quantity and in-quota tariff rate	Other terms and conditions
78	Other cheeses		19.500 t	Import under the Europe Agreements may be taken into account
		0406.10.20	926 Euro/t	when implementing this quota.
		0406.10.80	1.064 Euro/t	
		0406.20.90	941 Euro/t	
		0406.30.31	690 Euro/t	
		0406.30.39	719 Euro/t	
		0406.30.90	1.029 Euro/t	
		0406.40.00	704 Euro/t	
		0406.90.14	858 Euro/t	
		0406.90.16	755 Euro/t	
		0406.90.32	755 Euro/t	
		0406.90.50	755 Euro/t	
		0406.90.65	941 Euro/t	
		0406.90.86	755 Euro/t	
		0406.90.92	926 Euro/t	
		0406.90.98	1.064 Euro/t	
79	Wheat	1001.10.50 Ex	300.000 t	"Quality wheat"
		1001.90.95 Ex	0%	Qualification for the quota is subject to conditions laid down in the relevant Community provisions.
80	Durum Wheat	1001.10.50 Ex	50.000 t	Durum wheat with a minimum vitreous kernel content of 73%.

	Description of products	Tariff item number(s)	Final quota quantity and in-quota tariff rate	Other terms and conditions
			0%	Qualification for the quota is subject to conditions laid down in the relevant Community provisions.
81	Oats	1004.00.50	21.000 t	Milling oats having the following specifications:
			89 Euro/t	- a minimum test weight of 55 kg per hectolitre
				- a maximum moisture level of 12 percent
				- a maximum admixture (EG foreign seeds) of 2 percent
				Qualification for the quota is subject to conditions laid down in the relevant Community provisions.
82	Maize	1005.90	500.000 t	To be imported into Portugal.
			Maximum	(*) The rate shall be fixed by the competent Community authorities
			50 Euro/t (*)	so as to ensure that the quota will be filled.
83	Husked (brown) rice	1006.20	20.000 t	
			88 Euro/t	
84	Semi-milled or wholly milled rice	1006.30	63.000 t	
			0%	
85	Worked oats, other than kibbled	1104.22.90	10.000 t	
			0%	
86	Grape juice (including grape must):		14.000 t	Intended for the production of grape juice and/or non-wine sector
	- Of a density exceeding 1.33 g/cm3 at 20°C:			products such as vinegar, non-alcoholic drinks, jams and sauces.
	-- Of a value not exceeding 22	2009.60.11	The initial	

	Description of products	**Tariff item number(s)**	**Final quota quantity and in-quota tariff rate**	**Other terms and conditions**
	Euro/100 kg net weight			
			in-quota	Qualification for the quota is subject to conditions laid down
			tariff rates	in the relevant Community provisions.
	-- Other	2009.60.19	shall be redu-	
			ced as commit-	
	- Of a density not exceeding		ted in Section	
	1.33 g/cm3 at 20°C:		I-A for out-	
	-- Of a value exceeding 18 Euro/100 kg		quota rates.	
	net weight:			
	--- Concentrated	2009.60.51		
	-- Of a value not exceeding			
	18 Euro/100 kg net weight:			
	--- Other	2009.60.90		

3 October 2016