HOUSE OF LORDS

Select Committee on the European Union

Goods Sub-Committee

Corrected oral evidence: Future UK-EU relations: trade in goods

Monday 18 January 2021

10.30 am

Watch the meeting

Members present: Baroness Verma (The Chair); Lord Berkeley; Baroness Chalker of Wallasey; Lord Faulkner of Worcester; Lord Inglewood; Baroness Kramer; Lord Lamont of Lerwick; Lord Lilley; Lord Russell of Liverpool; Lord Shipley; Lord Turnbull; Lord Wood of Anfield.

Evidence Session No. 1 Virtual hearing Questions 1 - 12

Witnesses

I: Christophe Bondy, Partner, Steptoe & Johnson LLP; Nadiya Nychay, Partner, Dentons LLP; David Thorneloe, Legal Director, Pinsent Masons LLP.

Examination of witnesses

Christophe Bondy, Nadiya Nychay and David Thorneloe.

Q1 **The Chair:** Good morning, colleagues. Welcome to our three witnesses to our evidence session on future UK-EU relations: the trade in goods.

Thank you very much for joining us this morning, Christophe Bondy, a partner from Steptoe & Johnson; Nadiya Nychay, a partner at Dentons; and David Thorneloe, legal director at Pinsent Masons. Thank you very much for being here at our evidence session this morning.

As you are aware, it is a public session. I would like to ask you to come back to us with any small alterations or amendments to the transcript if you find that it has not been recorded correctly. Once the session is over you will be asked to exit. I ask colleagues to reconvene afterwards on Teams.

This is an evidence session where you have already seen the questions. As I always say to witnesses, I cannot guarantee that colleagues will ask the questions that have been sent, and they may come back with supplementaries. I will start the session by broadly asking all three of you what your overall impression of the trade provisions in the agreement are. Could we start with you, Christopher?

Christophe Bondy: Thank you, Baroness Verma. It is Christophe, not Christopher.

I view the agreement very much as a divorce agreement. It is a highly unusual situation in international trade, in that most international trade agreements are meant to bring two economic spaces or economies closer together, whereas this one from the start was seeking to take them further apart.

In its substance, it is what one would understand as a basic free trade agreement of the kind that I spent several years working on in negotiations between Canada and the EU, and many of the headings will be the same. As befits a divorce agreement, it also recognises a very long relationship between the UK and the rest of its EU partners, and so had to address through the initial withdrawal agreement things such as the UK's financial responsibilities arising from its membership, treatment of persons, the Irish border and even, within the actual TCA, issues that would not normally be in a trade agreement, such as social security co-operation or co-operation on enforcement of criminal prosecution.

Beyond that within the TCA—perhaps recognising a level of concern or, frankly, mistrust about the direction of travel of the UK—there is what I think is a rather robust level of safeguards that the EU insisted on that are specifically relevant to trade in goods. There are the non-regression provisions, which are robust, but there is also the ability for one or other party to withdraw benefits of the agreement if they feel that the level playing field elements, such as environmental and labour standards or subsidies—state aid—are destroying conditions for competition between the two parties.

That reflects the unique situation of the UK vis-à-vis the EU market. For the UK, the rest of the EU was not a foreign market. It was its home market. It is now stepping back from that, and the EU becomes a foreign market with all the implications that we are beginning to see.

The Chair: Thank you, Christophe. Apologies for my pronunciation. David, may I ask you to come in?

David Thorneloe: Yes, thank you, Baroness Verma. I completely agree with Christophe. The context is really important when looking at this trade agreement. Because we are leaving the EU, it is inevitable that barriers to trade are being raised. The question is to what extent the agreement limits that rise. Certainly, the absence of tariffs and quotas on trade in most goods is a major benefit in avoiding those barriers, but in so many other ways, particularly customs barriers and regulatory barriers, the position we are left in by the agreement is that those barriers are raised to a pretty high level. Of course, with around 50% of all the UK's external trade being with the EU, seeing those barriers imposed is going to be quite a shock to the UK economy when we have become so accustomed to having access to a seamless single market. That impact is not just direct, for businesses operating at the border and across the border, but indirect, in a ripple effect that goes right across the economy to so many businesses.

Nadiya Nychay: My overall impression is perhaps somewhat different from the voice of Christophe and David on this issue. It is my impression that the agreement was negotiated and drafted with a view to making it a dynamic agreement, in the sense of allowing the trade partners to continue to shape the agreement going forward. By its nature, the agreement will have accretion over time, so the way it moves will be important.

The agreement is unique, because it cements a permanent partnership and dialogue between the UK and the EU on matters that relate to the trade relationship and every other matter covered by the agreement. The geography of the new relationship does not change the fact that the UK will continue to be a close ally of the European Union going forward. That said, in the absence of fully-fledged membership of the single market in the European Union and participation in the customs union, and considering the UK's negotiating priorities and the red lines, as we commonly refer to them, I think the overall deal is quite balanced.

There are multiple options for parties, with the scenarios provided for, to further develop the agreement. Importantly for the UK, it leaves a lot of options for working in the policy space, including potentially choosing to create more divergence[1] between the European Union and the UK, or to work independently, and in a sovereign fashion, in areas where it would like to see a distinct approach being developed, as compared to that developed in the European Union. It also provides for multiple options and scenarios for parties to review the trade deal, to address the

[1] Note by witness: corrected to: "convergence"

economic effects of the trade deal, reconsider it, rebalance it and reshape it.

To me, the agreement is dynamic and flexible in what it can offer. More importantly, it is an essential agreement. Considering the reality of the context, to which David referred, I think the agreement was necessary because, in the absence of parties' ability to hash out their differences, trade between the EU and the UK would revert to the MFN tariff in the WTO. That would have been an unhappy scenario, in my opinion. In that respect, the TCA that was concluded is certainly the happiest of the scenarios. The UK is in the process of seeing how the agreement will work going forward, but there is no doubt in my mind that, if we compare this agreement in the stratosphere of regional trade agreements concluded by the EU with other free trade area agreements, it is unique.

The Chair: Thank you very much. That allows us to open up to questions from colleagues.

Q2 **Lord Lamont of Lerwick:** Good morning. If I could, I will turn to Christophe, and then the others can comment if they wish. You referred to your experience with the EU-Canada agreement. Could you tell us what problems arose from that, and whether you would expect similar problems to arise with the UK agreement with the EU, based on your experience with the EU-Canada treaty? Secondly—this is addressed to all three witnesses—if you could influence anything in the agreement now going forward, and there are only certain things that can be influenced, what loose ends would there be?

Christophe Bondy: It is difficult to compare the negotiations between Canada and the EU and between the UK and the EU, because the starting point was so fundamentally different. The political situation was so fundamentally different. The EU and Canada were largely agreed from the start on what they were doing, which is that they were seeking to negotiate a free trade agreement. A free trade agreement, in modern terms, has a certain range of chapters that address things such as public procurement, temporary entry of persons, trade in goods and the whole panoply of things one sees in such agreements.

Within the negotiations relating to specific chapters, there would be particular discussions—perhaps on rules of origin or exceptions to be taken to investment and trade in services rules, or perhaps the scope of elements of public procurement or tariff rate quotas. Usually, in a trade agreement, one ends up with a few issues at the end that become contentious—for example, beef quotas or cheese quotas. Those things get pretty picayune.

In the EU-UK situation, I think there was almost disagreement from the start about what we were doing, with the EU being fairly firm from the start that if we were doing a free trade agreement it was going to be this, and the UK trying to do, as it was commonly called in the UK, a CETA plus or a CETA plus plus. I think that led to a higher degree of disagreement. As I mentioned, the EU wanted a higher degree of

assurances in this agreement with regard to things like the level playing field, which you do not find in the CETA.

I agree with Nadiya. The issue will be the behaviour of the parties going forward, and to what extent the UK seeks to diverge from regulatory standards in the EU, and to what extent the EU, in response to that, evokes the dispute resolution provisions of the agreement, and whether or not that relationship is productive or combative.

What I can be sure of, looking at the agreement and the number of sub-committees and committees it contains, is that it will continue to be a primary occupation for many people in the UK going forward, and rightly so, for the simple reason of proximity and this being your primary market. On the issue of what needs to be fiddled with, I defer to my colleagues for now because I think I have been speaking too much.

David Thorneloe: I am very happy to pick up where Christophe has left off with those loose ends, as you called them, Lord Lamont. I would probably characterise it as a platform in some ways. It is only in specific areas that there is room for hope. We need to be realistic: politically, both sides, after a painful negotiation, will want to step back and take a breath. They are not about to reopen the agreement or have massive new changes or developments that they could not agree on just a few weeks ago. It provides a platform. I would probably single out in particular the trade facilitation measures and customs facilitation, where there is room to co-operate and agree processes that could be quite helpful in years to come.

Another thing I would single out is mutual recognition of professional qualifications. There is no agreement on recognising them in the agreement, but there is a process for discussions to take place about agreeing some mutual recognition. Generally, there is a real lack of mutual recognition, which is a major drawback in the agreement. The more that we can take advantage of and reach agreements on things like that, the better. We need to expect that it will be a gradual process. It will take years, not weeks, to build on the agreement.

Nadiya Nychay: I will briefly comment on Lord Lamont's question. First, on the question about difficulties that may have been experienced in the implementation of the CETA agreement, we may be in the position of trying to compare the results of the agreement negotiations with those that have previously been concluded between the European Union and its partners. It is important to remember that—the position of European and non-European countries vis-à-vis the European Union is very much dictated and informed by the history of those countries with the European Union, on the one hand, and on the other hand by the economic calculus—what is in their best economic interests.

While we all try to look at the specific chapters and see how the other partners of the European Union do in their negotiations and what they have managed to achieve, I think this deal stands on its own footing. It was taking on board the fact that we were trying to disintegrate an

existing regional trade agreement of the European Union and the customs union and create an environment that meets the demands of the United Kingdom's choices on sovereignty and regaining its right to govern and exercise its right to policy-making, removing the jurisdiction of the European Union courts and creating space for independent policy developments in foreign affairs and in different domestic policies.

I think that technical difficulties will continue to emerge. That is why the agreement is going to be a live agreement. How it is implemented going forward is important, but on the specific and very interesting question of the loose ends I agree 100% with David. Another area that is, of course, extremely sensitive and important is conformity assessment. In the area of conformity assessments, very little has been achieved. That may be a genuine complexity and obstacle in the conduct of trade specifically between the European Union and the UK.

Q3 **Baroness Kramer:** Could we spend a few moments looking at rules of origin? I think we all understand that full, bilateral cumulation was negotiated in the TCA, but no diagonal cumulation, even where both parties have a free trade agreement with the potential source country involved.

Do you have any sense, from your discussions with your customers, of what impact that is having on their decisions about how they procure and where they procure? I would also like to hear any comments you have on the complexity of dealing with rules of origin, and whether or not there are ways forward to reduce that complexity?

Nadiya Nychay: In a world without access to the EU single market and customs union, and in a world where originating content determines access to preferential tariffs, the immediate effect of the trade deal is that the rules, as they are currently drafted in the agreement, will cause UK trade flows and supply chains to reorient themselves somewhat along European lines. That is undeniable. It will happen.

As to whether and why the rules of origin have been negotiated to encompass only bilateral cumulation and not diagonal cumulation, from my experience of reviewing trade agreements and, in part, negotiating them as well, rules of origin are always very politically sensitive. It was one of the last issues on the agenda of both the EU and the UK as we were approaching the end of last year. Such negotiations are not easy to handle, particularly when you are negotiating with the European Union, which has done many such deals in the past and has the collective knowledge of everything that its domestic industries are asking for or expecting.

While, at the moment, there is no diagonal cumulation, there are enough options integrated into the agreement to allow parties to reach diagonal cumulation in the future. Because of the political nature of the negotiation, the UK may need to accept additional obligations in consideration of the potential to have diagonal cumulation, but it has not happened yet. At the moment, as a starting point—I insist that it is a

starting point—we have only bilateral cumulation, but that is not to say that that is where things will end. There is a Customs Co-operation and Rules of Origin Committee that will be able to review how the agreement operates. At the top of everything sits the Partnership Council, which may decide to amend the rules of origin in 2027.

I view the agreement and the rules of origin provision as a starting point. There is enough leverage, and there could be more, in ask by the United Kingdom as it works with the agreement and determines what its ultimate priorities are. In order to negotiate more enhanced co-operation and more flexible provisions on the rules of origin, there has to be consensus in society about what we actually want. In December last year, there was no common understanding about how far we needed to go with these provisions, whereas on the EU's part it certainly had that view.

I believe that diagonal cumulation is still possible in the future, when the parties try to work, refresh, rebalance and reshape the agreement.

Christophe Bondy: It is undeniable that the application of rules of origin, in the absence of cross-cumulation, will have an impact on the place of the UK in EU supply chains. It is not quite the same thing, but we have already seen other implications, with the UK no longer being able to act as a distribution hub, or there being an impact on the UK's ability to act as a distribution hub, to EU member states.

There are provisions in the agreement for those issues to be reviewed. The ultimate rules of origin to be applied to products are subject to review on request after four years. From the UK's perspective, it needs to sell any potential enhanced improvements to the rules of origin on the basis of mutual interest with the EU. Frankly, I do not think that simply saying, "We don't like the impact of this on supply chains", will be very successful. The EU will respond by saying, "Then you shouldn't have left the EU". It is what it is.

The automotive business, for example, is a just-in-time business, where production chains have reached a high level of integration, but any business is cost-sensitive and time-sensitive. Once the full impact of the rules is assessed, that will be factored in. We have seen reports in the news recently about four different additional costs that are imposed on smaller businesses because of border issues. That goes beyond rules of origin. Those costs are going to be factored into businesses and, as was said at the beginning, it will mean some smaller businesses deciding not to do business in the EU, which has a knock-on impact on supply chains overall.

Baroness Kramer: Thank you. David, do you have anything to add?

David Thorneloe: Not really. I defer to the expertise of Christophe and Nadiya on rules of origin. I completely agree with everything they have said.

Baroness Kramer: On the other side of the question—the pure

mechanisms of form filling and establishing the levels of origin—clearly the underlying rules cannot be reviewed for four years, by which time supply chains will have adjusted fairly fundamentally, but is there any flexibility to do something about the actual paperwork?

Christophe Bondy: It is a regime of self-certification. One has to determine the origin of the product. Frankly, everyone has to take very considered legal advice to understand how their product fits within the specific rules of origin for that particular product category. There will be some initial need for advice in that regard. The self-certification regime is helpful, but it also means that one has to keep records for four years—there are potential verifications, for example. I think a three-year grace period has been put in, and a one-year grace period for being able to demonstrate that on the part of importers.

There is also a regime for an importer to make a declaration, as opposed to the exporter. There is no doubt that even the regime of self-certification will require a different level of thought process on the part of UK-based businesses—I should say Great Britain-based businesses rather than UK—in relation to what they do when they put a good in a package and send it off to Northern Ireland or to the EU.

Q4 **Baroness Chalker of Wallasey:** In the light of what Nadiya and David said, to what extent does the TCA address issues of conformity assessment, both in general and by specific sectors? I see great problems coming there.

Nadiya Nychay: Getting right to the issue, I have identified that area as one of the loose ends in the agreement for the United Kingdom. That is because there is no real chapter on mutual recognition of conformity assessments in general. From the conformity assessment perspective, the agreement does not offer much by way of an immediate solution. While the EU did not want to address the issue in general, it did, however, engage with the UK on specific sectoral exemptions that would help the UK in the initial impact of exit from the European Union.

What was important for the UK, and what was negotiated, is that UK Type Approval Certification for vehicles will remain recognised in the European Union as long as the UK continues to adhere to the common UNECE set of rules for those vehicles. With that waiver in place, there will still be paperwork; it is a success, but it is not without a price in the burden that the manufacturers will experience.

There was nothing agreed on chemicals that was important for the UK, but the UK has asked for, and managed to secure, the EU's agreement in accepting certification for pharmaceutical plants, compliant with EU rules on good manufacturing practice. That is a success, but it is not a complete success, because some aspects of the safety of products may still need to be reviewed by both the UK and the EU.

Very little has been done on aerospace products. The rules are very complex. They want to move towards mutual recognition of testing and

certification to allow both sides to set up test facilities, but that has not happened yet. The annex at least foresees the possibility of the EU extending their scope to automatic recognition of UK aeronautical products and designs over a period of time.

There are similar commitments in the space for food products and animals. This is a chapter where the two parties need further impetus to work on it. Hopefully, that will happen, but at the moment the UK will be impacted gravely here. Being a member of the European Union, it benefited from the long-established case law of Cassis de Dijon, whereby if your product is legally placed on the market in the member state you do not need anything else to trade anywhere in the European Union. Moving from that type of framework of existence to having each of your products being confirmed in conformity terms in the EU and the UK is a massive burden for businesses in the United Kingdom. Businesses will need to make a lot of adjustment, and it will of course be incredibly costly.

As Christophe mentioned, there are separate provisions for Northern Ireland. That is a very complex regime, and a parallel runs across the agreement. The long and the short of it is that this one chapter is where we need to look at additional solutions for the UK going forward.

Baroness Chalker of Wallasey: Thank you. I very much agree with you. David, do you have anything to add?

David Thorneloe: Nadiya covered the main points really well, so I will just add a couple of things. The technical barriers to trade chapter that deals with conformity assessments is very thin. There is lack of mutual recognition. Looking forward, there are arrangements for co-operation, but essentially they are about transparency of information and discussion, so they are very limited.

As Nadiya said, the real impact of what is not in the deal is shifting from a single seamless system of regulation to two systems. That is doubling compliance for many people. Realistically, Nadiya is quite right: building on the agreement is really where we want to try to find some hope, to see if we could get more co-operation and more recognition of systems. The real challenge here is that the EU's price for that, understandably, is that it would want the UK tied in very tightly to the EU's regulatory system and bound by the EU's laws and the EU's courts. Of course, there was a very clear red line for this UK Government about Brexit meaning extracting the UK from those systems. It is difficult to see how those two competing views of the UK and the EU are compatible and could be a basis for building on the provisions.

Baroness Chalker of Wallasey: Being a dynamic agreement, there is going to be a lot of dynamism going on. Christophe, do you have anything to add?

Christophe Bondy: I have a couple of points. We have to recall that it is not typical for the EU to enter into deep mutual recognition of other

regimes' regulatory standards outside the ecosystem of the EU, as David suggests. What is more typical in free trade agreements is mutual recognition of conformity assessments in relation to the other party's standards. Under the CETA, for example, there could be someone sitting in Alberta double-checking whether a good being sent from Alberta to Germany conforms with Germany's standards. It is a way of smoothing that, and it would not typically exist outside the free trade agreement. Even in that regard, arguably the TCA is CETA or Japan-EU minus in some respects, and something that might be fixed going forward.

That being said, one little ray of sunshine—I have a ray of sunshine coming through the trees of south Dulwich—is the fact that, according to the agreement, where the EU accepted a regime of self-certification of conformity prior to entry into the agreement, the same regimes of self-certification will apply, but they will be as they apply vis-à-vis third-party countries. One is falling to third-party status, as opposed to—this was referred to—the fact that if something is certified to conform within the EU and put on the market, it is assumed that it can be sold everywhere.

Baroness Chalker of Wallasey: I can see that a lot of work needs to be done. Thank you very much, all three of you.

Q5 **Lord Lilley:** Are the level playing field terms of the TCA both reciprocal and symmetrical? In practice, which party is likely to find itself using the arbitration mechanisms to challenge measures which the other side has brought in that it thinks distort trade?

In the past, we have made far less use of opportunities in the European single market to subsidise than the other countries. That is the background to my question.

Christophe Bondy: The obligations on the level playing field are reciprocal. They are obligations of non-regression, and they set out a series of principles rather than adherence to specific EU laws.

As to who is most likely to invoke them, I think there is a balance of power in the sense that the UK is about 65 million people and the EU is 400-odd million people. The threat of withdrawing access to that market is a bigger stick than the threat of withdrawing access to the UK market. That will have to be assessed case by case. My general thinking with regard to these provisions, which go much deeper as disciplines than one would usually see in a classic free trade agreement, is that each party will have to very carefully assess how the measures it proposes to adopt may or may not be caught by the safeguard provisions.

With regard to state aid and subsidies, there is quite a complex regime set out in the agreement for setting parameters for state aid, beyond things that are in the WTO. It is clear that export subsidies, for example, or local content subsidies are illegal, as they are in the WTO. Beyond that, there is a lot of language in the agreement about the purpose, or the legitimate context, of subsidies, and the notion of the impact on the conditions for trade of the traders in the other parties. I think there will have to be a careful assessment on a case-by-case basis. The extent to

which one party or the other invokes those safeguard provisions will depend on economic interest case by case. The fundamental dynamic is that the EU is bigger than the UK, so arguably the UK has more to lose on a high-level basis by not complying.

It is an issue generally. Regardless of the whole issue of sovereignty and the political emotion on that, UK manufacturers are, out of their economic self-interest, going to think, "Do I want to remain in compliance with EU rules in order to be able to continue to sell in that market?" It is not even an issue of safeguards. It is, "Do I allow my product to get into that market?" If the EU deems that the product no longer meets its health and safety standards, for whatever reason, then quite apart from the level playing field, the EU is going to decide that the product cannot be sold in its market.

The Chair: Thank you, Christophe. I am mindful of time, colleagues and witnesses. May I ask for a little brevity? That would be helpful so that we can get all the questions in.

Nadiya Nychay: Thank you, Baroness, and thank you, Lord Lilley, for the important question on the level playing field measures, particularly in the space of subsidies and state aid. I think there is a philosophical decision to be taken by the UK Government. At the moment, the UK system is entirely based on the state aid regime of the European Union. There has to be some logical conclusion to that process.

What should it be? One way to handle it would be to take on board everything that we have learned and done. You pointed out that the UK did not use a lot of subsidies in the past. That said, it was championing legal subsidies in earlier years for urban regeneration projects in the United Kingdom, thanks to which Birmingham and Manchester have become vibrant and modern cities.

Taking on that positive experience of working within the EU general state aid regime, the UK can properly capitalise on it and create a space for an open-door policy with the European Union, discussing plans and what issues of convergence we can find, especially if we are trying to marry projects in science research and development, and bring universities and industry together. I think we can secure a space that will be non-contentious in allowing us to work in a subsidy regime, a newly found autonomous regime, while not stepping on the toes of the European Union.

In contrast, there is one big victory for the UK Government in that they never wanted agricultural subsidies provided by the European Union to be outside the scope of challenge by the United Kingdom. Because the subsidies in the common agricultural policy are so controversial, it is possible that, if the UK feels a severe impact from subsidised products on its market, it could take action against the EU.

David Thorneloe: Perhaps I could add something about reciprocals.[2] As Christophe said, the provisions are reciprocal and apply equally to the

parties, but there is something to be said about the political reality that we are in at the moment. The principles that are set out in the agreement are very much based in their structure on the principles that apply in EU state aid law. Of course, they are principles that we have been long familiar with.

In some ways, when you think about the extent to which these provisions will be invoked by either party, there is an advantage to the UK. This is a system that, within the EU, will police itself, as it always has done. Indeed, over the last 10 or 20 years there have not been huge numbers of occasions when the UK has challenged European Commission decisions about subsidies granted in other parts of the EU. That is because the EU has that enforcement system. There are plenty of other actors within the EU who will challenge those things. They will challenge things that are in the UK's interests. The UK may not need to act except in the most extreme cases where others are not challenging decisions, or where the right outcome for the UK is not reached at the end of a very long process of several years.

Lord Lilley: I did not quite understand Christophe's point. If we are not interested in using lots of subsidies, but we are concerned about subsidies used by the EU, why is the fact that there are 450 million Europeans and 65 million Brits relevant? It is not a question of our suddenly tearing up the whole agreement, is it? We enter a challenge on a specific subsidy, and that subsidy is applying to your exports, of which there are £100 billion more than our exports to them, so it is more likely to occur. I do not see why the difference in size or power enters into it. If it is legal for us to challenge it, why can we not challenge it?

Christophe Bondy: You can absolutely challenge it. My sole point was that the proportionate economic impact of withdrawing benefits of the agreement will be smaller, at a macro level, when the UK invokes it than when the EU invokes it. You are right, if I understand what is behind the question: it will have to be considered in a specific industry. That goes to my point about considering the balance of invoking it in a specific economic context. The UK's withdrawal of benefits vis-à-vis a particular measure by the EU in relation to a specific industry that it is subsidising may hurt and would therefore be effective. That will have to be determined on a case-by-case basis.

David's point is excellent. There are significant disciplines within the EU as a whole as between member states, so the UK, if it does not like a particular subsidy, may be able to let the issue be dealt with as an internal issue to the EU. I hope that is helpful as clarification.

Q6 **Lord Wood of Anfield:** I want to talk about the provisions for customs facilitation in the agreement. How do you assess those provisions? I am particularly interested in those on authorised economic operators. What implications might they have for the way that customs and trade proceeds? Maybe Nadiya and Christophe could lead on this.

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[2] Note by witness: about the reciprocity of the terms of the Agreement.

Nadiya Nychay: In general terms, and briefly due to time, the chapter on customs facilitation is very standard. It includes standard language from the WTO agreement on trade facilitation. In fact, it picks up the parties' commitments undertaken as part of the WTO, but the agreement goes further in setting out provisions that provide possibilities for future co-operation between the parties. They encourage exchange of information relating to customs, transparency and enforcement.

While it may seem watery and not concrete enough, there are some specific projects that are already mentioned and have the potential for burgeoning. One is the initiative mentioned in the TCA: a pilot for developing a mechanism to avoid duplication of customs information. This is similar to what Norway and Sweden enjoy between themselves. If it were to materialise within this year, as the parties envisaged, it would be a fantastic development for the UK and the EU.

As respects the status of the authorised economic operator programmes in both countries, they are reciprocally recognised. It bears saying that there are two types of authorised economic operator status. One relates to customs formalities, the so-called AEOC, and one relates to AEOS, the security provisions. It is the latter status that has been recognised. The practical effect of that status on businesses will be that businesses that enjoy the status will enjoy equal treatment when going through the safety and security formalities in the partner's jurisdiction when they bring in goods for import or export. It does not mean that there will be no controls; they will simply be lighter as compared with the partners that do not enjoy that status.

Maybe one additional flexibility is that there is hope that the status could be granted to small and medium-sized enterprises, but the criteria are quite rigid. It remains to be seen how they can really help smaller businesses on the ground.

Christophe Bondy: That is right. In the interests of time, I want to refer to one experience. It is an analogy between the US and Canada. We have beyond the border initiatives where there is continuous discussion between Canada and the United States about how to facilitate customs arrangements in specific industries such as the automotive industry, and more generally. I foresee that the UK and the EU in their enlightened common self-interest will seek to pursue that dialogue beyond the bare bones that are set out in the agreement.

Lord Wood of Anfield: That is great. Thank you very much.

Q7 **Lord Shipley:** I would like to ask about the sanitary and phytosanitary chapter of the agreement. Nadiya said earlier that it was a dynamic agreement based on a unique permanent dialogue. I am wondering whether this is one of those chapters, because it only has an objective that the parties shall not use SPS measures to create "unnecessary barriers to trade". In the absence of SPS equivalence, to what extent does the agreement minimise trade barriers in that area?

Nadiya Nychay: You are 100% right: there is an objective that SPS measures should not be used to create unjustified barriers to trade, but the parties set out in the agreement specific actions that they think they should take to achieve that objective. Among those measures, from the more general to the more specific, there are commitments in the space of transparency, information exchange between the parties, and on matters related to the development of SPS measures, so they will know what is coming and when it is coming. The parties are committed to holding technical consultations regularly, if there are significant concerns in the space of safety and SPS measures.

Very importantly, and I think it will have a practical effect, the parties recognise the concept of zoning. That means that, if a given region in a partner's territory is affected by a pest or a disease, goods that originate from other parts of the jurisdiction can continue coming in and will not be affected. You can zone it literally within that region.

There is also an approved export establishment based on guarantees provided by the exporting party. That is a mechanism that allows parties to approve establishments that provide guarantees on the safety of goods being exported, without prior inspection by the individual establishments. It is yet to be seen how those will materialise in practice, but the provision exists.

An additional action provided for in the agreement is that the UK and the EU may not introduce authorisation requirements additional to those in existence at the time of the transition period. That is a very important development. There will be some predictability as regards what we are dealing with.

Separately, as you mentioned, there is a specialised committee for SPS measures between the EU and the UK, where many of the issues, obstacles and hurdles can be discussed and, hopefully, ironed out.

Lord Shipley: Thank you. David or Christophe, do you want to add to that?

Christophe Bondy: I have a few points. These provisions are reasonably standard in the context of FTAs with regard to SPS and the fact that there is an ongoing dialogue. As regards WTO law, one would see the notion of necessity and that not creating unnecessary barriers to trade can be a powerful tool for challenging measures that are introduced.

The one caveat I would point to is the issue of precautionary measures. One sees in Europe, including in the UK, a predilection for a precautionary approach with regard to animal and plant safety, on the basis of potential rather than scientifically confirmed threats. This has been a sore point in trade relations between the UK, the EU and the US for a number of years. One can expect that, if there are disputes going forward, and the EU invokes precautionary reasons for adopting certain standards, it will lead to significant disputes. I spent years in the Canadian Government in the Trade Law Bureau looking at, among other

things, proposed measures, and how they related to existing international trade obligations.

In thinking about regulatory change, in the context of WTO law and the likelihood for a dispute arising, the key thing is that it will be no different for the UK in the context of this agreement.

David Thorneloe: I just want to add one point. SPS checks and controls are a major barrier to trade for the food industry. There are limited provisions, which Nadiya has summarised there, and they chip away at that barrier. Yes, there is a process set up for discussions to continue, but realistically we are talking about chipping away. That is not a barrier that will be knocked down any time soon.

Q8 **Lord Inglewood:** Peter Lilley has shot my fox by having hijacked the question I anticipated asking, but I want to follow it up slightly, if I may. Our discussion has been at quite a high theoretical, legal, economic and political level. I would be interested to know our witnesses' views about what they think the actual impact of these changes will be for businesses the length and breadth of the country conducting their commercial activity. Against that background, to what extent would you say we are still in the world of Europe, or are we decoupled from it? What is the likely future dynamic, in your view, of the way this will evolve?

David Thorneloe: Do you mean in relation to the level playing field provisions?

Lord Inglewood: The level playing field position, yes.

David Thorneloe: We have not spoken about the aspects that relate to employment rights and environmental protection, where there are key provisions. The immediate impact for business is quite limited. We have basic minimum standards that will essentially maintain the status quo. In the longer term, it changes the rules of the game for UK Government policy-making. We have regulatory independence, but it is independence with consequences attached. What that means for businesses is ultimately uncertainty. To what extent will the terms of trade with the EU remain stable in the long term, when we have an evolving relationship?

The minimum standards do not mean that our UK laws on employment and the environment are set in stone for ever more, and nor should they be. The UK can think about how it wants to regulate these things. The agreement deals with divergence. From a UK perspective, that might be active divergence, so the UK Government may adopt new legislation, or it might be passive, in the sense that the EU starts to regulate further and the UK decides not to follow what it is doing.

With the so-called rebalancing mechanism, the EU, in that kind of scenario, if there is significant divergence and it has a material impact on trade, can unilaterally impose trade measures on the UK. For future government policy-making, yes, that means much more freedom than when we were tied within the tight framework of EU law; none the less, there will be choices, when making those new regulatory decisions, about

the extent to which the UK wishes to take advantage of that new regulatory independence or try to maintain the benefits of tariff-free trade with the EU.

Lord Inglewood: Do the other witnesses have any thoughts on that, please?

Christophe Bondy: If we are speaking specifically about the level playing field provisions, one would think that on the face of the TCA the commitment to non-regression would give businesses in the UK, at least from that specific point of view, a sense of assurance about regulatory stability going forward. Given that it is acting from a starting point of regulatory alignment with the EU, and with knowledge of the way things work in the EU, the issue is of course, as David points out, that of divergence. I noted with interest this last week that one of the first things that the Government have announced with regard to their policy post signing the TCA is a review of some aspects of labour law in the UK. The proof will be in the pudding. It will depend on the content of that revision. It may fit within the scope of what is allowed with regard to rebalancing, or may not fall foul of rebalancing, but it depends on what exactly the content is. That is why any of the policy choices that the Government make will have to be very carefully reviewed in relation to the issues in the agreement.

As regards the rest of any potential regulatory change in the UK, I understand that the Prime Minister has called on a number of businesses to think about how one might get rid of burdensome substantive regulation, and so on and so forth. There, the issue is more whether products will continue to be acceptable on the EU market in light of those changes.

The Chair: I am very mindful of the time and we have four questions to get through. We will go to Lord Turnbull.

Q9 **Lord Turnbull:** The question I start with is: to what extent does the agreement allow the UK to diverge from the EU's approach to state aid? In other words, how much tolerance and flexibility is there? This does not just apply to state aid; it applies to the level playing field, rules of origin, conformity and so on.

Looking at the agreement, I have a feeling that it is a protectionist's charter. What is to stop a disgruntled business, let us say in France or Germany, raising a complaint? "The UK has moved this and it's no longer in conformity. It has changed that. Its rules of origin claim isn't true". What is very worrying is a comment right at the end of the very good note that David Thorneloe sent to us. He says, "As regards leverage in any trade disputes that do arise, either party retains the right under the agreement to impose some trade measures on the other without waiting for an arbitration ruling in some circumstances". In other words, you shoot first and ask questions later.

How do we prevent disgruntled industries and companies in the EU raising a whole series of vexatious complaints, which we have to deal

with and eventually sort out, but meanwhile the balancing measures have been invoked? They do the damage first and sort it out afterwards. That seems to me a pretty unsatisfactory position to be in.

When the agreement talks about either party, the party in one case is the UK, but who is the party on the other side that can impose a balancing measure? Is it the EU as a whole or a particular country whose industry has complained?

David Thorneloe: There is quite a lot there. I will focus on employment and environment and the rebalancing mechanism. The first thing is that there is a threshold to get over. The general default position under the agreement where there are breaches is that they need to go to arbitration first, a process that will take many years before either side can impose measures on the other.

To answer your question about the EU side, it would need to be the EU collectively; it could not be just a single member state. No doubt there will be lobbying from particular member states or industries, but it would need to be a collective decision at EU level to take that action. When there is a dispute like that, we have to bear in mind that it is not just a legal process but very much a legal and a political process, and one would expect discussions to be going on between the UK and the EU in addition to any legal process.

There is a threshold to get over. The power to issue unilateral trade measures without first going to arbitration is very important for leverage. It applies chiefly in relation to subsidies, employment and environment. With employment and environment measures, it is only if they lead to significant divergence from the EU, in a way that affects trade. It is not a hair-trigger threshold. There is an emphasis on the EU.[3] That leaves considerable room for manoeuvre, which is why, as Christophe mentioned, the UK Government are understandably looking at their regulatory options post Brexit, for those to continue. I will leave it there.

The Chair: If we could have brief comments from Nadiya and Christophe, it would be helpful.

Christophe Bondy: Very briefly, it is a state-to-state mechanism, so a particular company cannot invoke it. It has to be raised at the EU level. There is a consultation process first, but there is a fairly rapid response. I think it is within 60 days according to some elements. Then there has to be an arbitration. That is in relation to the level playing field/state aid element. The UK Government have new flexibility with regard to state aid because they do not have to notify potential state aid to the EU and have it approved, in the kind of process that exists for any EU member state.

The provisions on subsidies in this agreement, and the principles that are applicable to subsidies—the whole framework—is much more elaborate than one would typically find in the context of a free trade agreement. That is again reflective of the EU's concern about the potential direction

[3] Note by witness: "a burden on the EU, as complainer, to overcome this threshold."

of travel by the UK. The proof will very much be in the pudding as to what potential measures the UK, or the EU for that matter, decides to adopt.

The Chair: Apologies, Nadiya, I need to move on.

Q10 **Lord Berkeley:** I want to ask a question about the fifth freedom on the air sector and the equivalent on road transport. At the moment, it limits the ability of UK-registered airlines or road transport to operate within the EU. It is particularly important in the roads sector when there is specialist equipment in vehicles for the arts, television, and orchestras perhaps, and when people want to tour different EU member states. In either case, they will have to get agreement from each member state in turn to operate there. What provision is there for negotiating those issues in future both for the air and for the road transport sector?

Nadiya Nychay: As of January this year, the UK can no longer participate in the fully liberalised EU aviation market, and UK airlines are no longer considered EU carriers. They can no longer enjoy the same level of traffic that they had, and this will have a massive impact on the industry. There will be some flexibility over time, because UK air carriers wishing to fly under the TCA will have to comply with certain conditions, such as holding a valid licence from the UK competent authorities, having their principal place of business in the UK, and being majority UK-owned and controlled, to be able, for instance, to negotiate a certain type of access with EEA parties going forward.[4]

To your question on guarantees that these negotiations will be fruitful, I think there is certainly enough to be able to draw on the experience of the EU, EEA and Switzerland negotiations, but there will not be an easy negotiation to be had.[5] With respect to road transport, indeed, UK companies will no longer hold an EU licence or be able to perform transport services. This will impact especially on logistics companies that operate on both sides of the channel. There will have to be a swap of drivers and other measures foreseen by the parties to address the lack of licences. It is another area to negotiate.

The Chair: Thank you very much. David and Christophe, do you have anything briefly to add?

David Thorneloe: May I add one thing on future co-operation and agreement? Under the TCA, there are specialised committees for both air and road transport. With air transport, there is a bit more scope for optimism. Its purpose is to remove obstacles to trade. I would be less

[4] Note by witness: "Moreover, UK air carriers wishing to fly under the TCA will have to comply with certain conditions, such as holding a valid licence from the UK competent authorities, having their principal place of business in the UK, and being majority UK-owned and controlled. There will be some flexibility overtime, because the UK will be able, for instance, to negotiate bilaterally a certain type of access with EU and EEA parties going forward."

[5] Note by witness: "The UK has already concluded an Agreement relating to Scheduled Air Services with Switzerland."

optimistic about developments in the road transport sector, because that committee seems to be set up around enforcement and ensuring that there is no rowing back from co-operation. There are very strict provisions, because the EU fears that the UK would seek to undercut the EU market with lower regulatory measures. There are much stricter measures there and less cause for optimism.

The Chair: Thank you. I need to move on, if I may.

Q11 **Lord Faulkner of Worcester:** David has answered the question I was going to ask, which is: what scope is there for future co-operation and dialogue? If Christophe would like to add anything to what David has just said about that, it would be great. Is there anything in the TCA that makes future co-operation and dialogue possible? If so, what?

Christophe Bondy: As David pointed out, there are committees on both issues; indeed, there are committees on just about every single issue in the agreement. There is also a general provision in the agreement that any future agreements that fall largely within the scope of the TCA, which is broad, are automatically assumed to be subsumed within the general structure of that agreement. That is a kind of umbrella function that the TCA will achieve going forward.

I really think it will be a question of the UK proceeding on a case-by-case basis, through really quite sustained engagement in those committees. Having identified particular industry issues, which could not be dealt with, frankly, in the very rapid time that this agreement was put in place, it will need to put to the EU, and presumably the EU will do the same to the UK, in their enlightened self-interest, how they might achieve some amelioration of the situation. Sometimes that will involve trade-offs between the economic interests on different points. That is the nature of international treaties.

Lord Faulkner of Worcester: And presumably a fair degree of goodwill on both sides.

Christophe Bondy: Yes, of course. Again, that is why the setting off of the relationship with the EU from the UK's perspective is important. I think there were signals from the Government after the deal was signed saying that they wanted to be the EU's best partner, but the proof will be in the pudding. There is a level of suspicion, starting off, because the impetus for Brexit on the part of many in the leadership of the UK Government was to deregulate. The UK is in a fundamentally different position from Canada or from any other free trade agreement partner of the EU because it is on the EU's doorstep and deeply integrated in the EU economy, and the EU does not want the conditions for competition within the EU undercut by a competitor on its doorstep.

Q12 **Lord Russell of Liverpool:** I have a quick question for each of you. You have covered an awful lot of ground. It seems an irony that in an attempt by people to escape EU bureaucracy we seem to have entered an era where we will have committees left, right and centre.

Given your knowledge of the situation, if we were to anticipate that the UK Government needed to prioritise a particular issue area very quickly, to try to achieve clarification and get on top of it, and you were forced to name one particular issue, what do you think it would be?

Nadiya Nychay: One notable ramification of Brexit is that there is a lot of bureaucracy surrounding movement of goods in the trade space. If I were to prioritise, I would make several key recommendations to the UK Government. Currently, there are three major problems, all requiring separate bureaucracies, when you move goods across the channel.

Every exporter/producer needs to fill in an entry summary declaration. The amount of information in that declaration is staggering. The declaration must be filled in 24 hours before loading. There is a second set of bureaucracies for pre-boarding notification for each export, and there are customs declarations. If you add to that phytosanitary measures, and add to that rules of origin and the need to demonstrate where the product originates from, they all present real challenges. One thing the Government can do is try to provide some smart high-tech solution that simplifies the flow of documents when you move goods across borders. That is one thing.

Secondly, there is a lot to be said about the possibility of firms receiving training on how to handle the procedures. The agreement is incredibly sophisticated, and many businesses find themselves completely unprepared for the impact of the range of requirements, such as needing to identify the tariff code for a product. If you are a firm that has only traded with the Europe Union, you may never have been concerned with the tariff classification or code of a given product. Collectively providing training to businesses would be a massive help to businesses on the ground, to help them feel that they are not left alone to handle the ramifications of Brexit.

Of course, customs co-operation will also be an important factor, because the UK will now have to handle customs procedures not just for extra UK trade but for everything that previously was in the EU realm. That means we need to train more customs agents and customs brokers, and there needs to be a greater quantity of customs agents. I hear that it takes up to three years to train a customs agent. We need to put massive resources into preparing our civil servants for their functions to handle the amount of work and the flow of trade if we want to maintain the same levels of trade.

David Thorneloe: Nadiya gave an excellent answer. I certainly agree that the barriers at the border are a top priority. As a second, I would say let us get to the regulatory barriers behind the borders. We have created two regulatory systems from one, with conformity assessments and product packaging, which affect so many industries. Mutual recognition has gone because we have left the EU, and it is not in the deal, but there could be ways we can chip away by forming agreements to co-operate between different regulatory authorities.

Christophe Bondy: I agree with Nadiya and David. The only other thing I can see as an external observer is sorting out how trade in goods will work with Northern Ireland. That is one part of the agreement that is unique, and seems to be incredibly complex, given that it is sort of in, sort of out, from a variety of points of view. I should think that that will be both an economic sore point and a huge political sore point. I assume that the Government will be focused on trying to sort out how business within the United Kingdom works in light of the agreement.

Lord Russell of Liverpool: Thank you very much.

The Chair: Thank you all very much indeed. We missed one question, question 5, so I request that our three witnesses look at that question and put something in writing, because it is an important part of our evidence session. If you have the question in front of you, that is fine. If not, Sam can send it to you again.

On behalf of the committee, I thank you all very much for your time this morning. It is a very complex area and trying to get very detailed work in a very short period is always difficult. We appreciate you coming this morning. I think the committee will agree that it has been a very informative session for us. As I asked you earlier, if there are any corrections to be made to the transcript, if you could put them in as quickly as possible for us, that would be most helpful. Thank you on behalf of all the committee for coming in this morning and giving us your knowledge about the background of the TCA.