



Select Committee on the European Union

Goods Sub-Committee

Corrected oral evidence: Future UK-EU Relations: Trade in Goods

Monday 25 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. 2

Virtual hearing

Questions 13 - 24

Witnesses

[I](#): Alessandro Marongiu, International Trade Policy Manager, Society of Motor Manufacturers and Traders; Luke Hindlaugh, Senior EU and International Food Trade Executive, Food and Drink Federation; Fergus McReynolds, Director of EU Affairs, Make UK.

Examination of witnesses

Alessandro Marongiu, Luke Hindlaugh and Fergus McReynolds.

Q13 **The Chair:** Good morning and welcome to committee members, and to our three witnesses. This is a public session on future UK-EU relations: the trade in goods.

The witnesses have had sight of our questions. Committee members may come back with supplementaries. In the interest of keeping the session to time, I remind everyone to keep the supplementaries reasonably brief. If, on receiving the transcript after the session, the witnesses see that there are minor corrections to be made, could they let the clerks know as quickly as possible?

Our first witness is Alessandro Marongiu. Apologies if I have said that wrongly, Alessandro; you can correct it when you come to speak. You are the international trade policy manager for the Society of Motor Manufacturers and Traders. Luke Hindlaugh is a senior EU and international trade executive at the Food and Drink Federation. Fergus McReynolds is the director of EU affairs at Make UK.

A very warm welcome to you all. I will get on with the session straightaway because there are many questions, and colleagues will most likely want to come back with supplementaries. I will start with a general question. Within the parameters of the TCA, which industries do you think are or will be the most affected by tariffs, and what do you think can be done to make that impact as little as possible, or the least possible?

Alessandro Marongiu: Thank you very much, Baroness Verma. As regards industries that might be affected, when it comes to manufacturing businesses, in particular the automotive sector, impacts are possible. The SMMT obviously welcomes the conclusion of the trade and co-operation agreement with the European Union. There was a huge sigh of relief from industries facing significant tariff risks from a no-deal WTO outcome. The deal provides the opportunity for tariff and quota-free trade foundations on which the industry can build. However, there is no such thing as a tariff-free deal; tariffs apply, unless you can comply, and demonstrate that you can comply, with the rules of origin requirements. So there is the threat of tariffs for the automotive industry, although the agreement allows us to trade tariff and quota free.

There are risks. Obviously, there is a question about the possibility of complying with rules of origin as set out by the deal. There are risks related to new, potential regulatory biases¹ that could emerge now and in the future. There are the pre-tariff costs of complying with different regulatory requirements. In general, friction at the border and customs issues affect all trade in goods between the two parties, certainly the trade in automotive products.

¹ Note by witness: corrected to "barriers"

I cannot speak for other industries, but those are the main threats that are still there for automotive, despite having a deal in place.

Luke Hindlaugh: I agree. The avoidance of no deal was very much welcomed in our industry. It would have been a disaster for food and drink. The avoiding of tariffs was very welcome.

We produced a two-page summary of the deal, and we are happy to share it with the committee. We very much agree that, on tariffs and tariff-free access, it is very much best in class, but when you go beneath the surface to the rules of origin and the SPS—sanitary and phytosanitary—measures, there are significant barriers to overcome.

To sum it up in a sentence, the headlines are very good, but you need to look beneath the bonnet of the car and realise that you will have to pedal it yourself. For rules of origin, particularly for food and drink, there are particular issues around some of the produce-specific rules that provide worse access than some in the Canada agreement in allowing the value added within those rules. Helping the industry to understand those in particular will ensure that some tariff-free access can continue.

A particular issue is the use of inputs from developing countries, and it is disappointing that it was not addressed in the deal. We were very disappointed that that did not get over the line, because it will impact manufacturers using inputs from developing countries that then go into exports to the EU, or exports that come from the EU to the UK.

The particular challenge in ensuring that people can access the deal—because all tariff-free access is conditional; it is not unconditional—is the late application and notification of the deal. That is causing particular issues for industry. Do people understand what they need for the rules of origin, and have they had time to adequately assess and adapt their supply chains? Over time, there will be adaptation, and people will restructure their supply chains so that they can continue to have tariff-free access to the EU from the UK, and vice versa, but that initial late application is causing the most issues and is where the FDF, over the last few weeks, has had to guide our members through understanding the rules of origin and how they can access them.

Fergus McReynolds: Thank you very much for the opportunity to speak this morning. Like my colleagues, I very much welcome the fact that we ended last year with a deal. It was very important. The ambition of both sides to ensure that the deal would be tariff free and quota free between the two partners was very important. The priority for us, as a sector that is very integrated in the European ecosystem, was an understanding that goods could transit the border in several directions.

Luke and Alessandro have highlighted the issue very well. On the face of it, tariffs are zero rated if you can prove that the goods originate in either of the two parties. That full and bilateral cumulation is welcome, but we would have liked to see more ambition on diagonal cumulation, particularly where we have common free trade agreements.

I think there will be acute effects on certain sectors from the product-specific rules. It is important to remember that we did not see the product-specific rules until 24 December, so the time for them to become understood in the sector has been quite limited.

However, rather than sector by sector, it is more important to understand the profile of the business specifically and the supply chain it is in. If the business is taking a lot of content from outside the EU or the UK, these things will impact it much more. Where a business is trading traditionally, there will also be an impact. It is important to recognise that about 50,000 UK manufacturers have no experience of trading outside the EU, so a lot of the requirements and a lot of the understanding about how to achieve zero-rated trade will be new to them.

The final element is that, while you have the possibility of zero-rated trade, it does not relieve you of any of the responsibilities to prove that. The bureaucracy associated with ensuring that you can trade at a zero rate is the challenge at the moment. Like Luke, most of the questions that we have had in the first three weeks of this year have been on understanding the rules of origin and how they impact a business. We are advising companies to ensure that they can make the best of the agreement.

The Chair: That neatly leads on to the next question, from Lord Turnbull.

Q14 **Lord Turnbull:** My question is deceptively simple. How burdensome are the requirements for demonstrating compliance with the rules of origin? It can be divided into two. There is the burden of understanding the rules, doing the calculation, and documenting that to the satisfaction of anyone who wants to challenge it. Will people find that so difficult that they will just not bother, and will pay the tariff or not export?

It is also burdensome in the sense that, if you want to restructure your supply chain, how difficult is it? If people can do that, instead of importing or producing in the UK or within the rest of the EU, how difficult will it be for them to find alternative suppliers that would bring their numbers up to whatever it is—the 55%?

Alessandro Marongiu: The instruments set by the deal to claim preferential origin are not overburdensome. The agreement allows exporters to self-declare compliance with rules of origin by producing a statement of origin on the invoice or other commercial documents. There is also an innovative solution included that makes it possible for the importer to use their own knowledge of the origin of the goods to claim preferential treatment.

However, putting systems in place or upgrading existing systems to ensure compliance with product-specific rules and associated formalities can be very burdensome, in particular for businesses that have no previous experience of dealing with origin requirements. Given the complexity, deciding to pay the tariff could be an option for smaller businesses, provided that the costs of paying tariffs are smaller than the costs of meeting origin rules.

However, even suppliers that only serve the domestic market, or those that decide to pay the tariffs and are unlikely to meet origin rules, are unlikely to be completely shielded from origin requirements. If customers of suppliers are exporting to the EU and cannot meet origin requirements through their own operations, they will need to know the origin of the components that they incorporate into their products to get zero-tariff treatment. Exporters will ask their suppliers for documents showing the origin of their goods. Clearly, suppliers that are unable or unwilling to show compliance with origin rules risk being at a very serious disadvantage in their customers' future business decisions. I do not know how easy it would be to replace existing suppliers, but it might be part of future considerations.

Lord Turnbull: Can I clarify? If I send something to America, and then they export it to the EU, I then have to tell the people I supply the thing to how much UK-EU content there is.

Alessandro Marongiu: Goods exported to America clearing customs in the US would not have preferential origin in any case. If I reimport the goods into the EU and the UK, and further process them in the EU and the UK, they might comply with origin requirements. In intra-EU-UK trade, there is definitely the possibility of declaring the origin of the good and the value added in the territory of the EU and the UK to facilitate my clients to meet origin requirements on the goods they are trading.

Fergus McReynolds: Alessandro has set out very comprehensively the requirements and some of the challenges that manufacturers will face. What is important to recognise is that, despite the fact that there are some innovative new ways of proving origin, it is still the responsibility of the business to do so. Whether there is easement in place or not, the actual legal responsibility exists, and it may well be challenged retrospectively.

There are probably two issues. There are system issues and structural issues. What do I mean by those two things? The system issues are about coming to understand rules of origin and the processes that are required. Those things are a learning curve, but in time they can be addressed so that they become a day-to-day part of doing business and can be factored into how you trade with your customers or how you bring in supplies.

The structural issues are more challenging. That is where the business model does not fit with the new relationship. A classic example is if you are bringing in product from outside the UK or the EU and are not processing it or having any substantial change in it, and are then supplying it to the EU market. Those businesses and those sorts of operations will, structurally, not be possible in the future relationship.² That is true particularly where we have no free trade agreement with a

² Note by witness: "These operations will be possible, but are likely to face the imposition of tariffs (duties) and may make the operation unviable in the future."

common party, but, because we do not have diagonal cumulation, it is also true where we have continuity agreements with many markets.

There is the system issue, which I think can be addressed in time. Businesses will get used to doing these things. They are resilient. They understand how to take advantage of the new environment they live in, but there are some structural changes which mean that there is the possibility that some companies will choose to do things differently. They will choose to import things into different parts of the two parties, and they may have to look at how their supply chains are structured.

I think that will have an impact. As Alessandro said, for many companies, what is in their best economic interest as a business will be a simple calculation. Is it to ensure that they have all the documentation right for rules of origin, or is it to declare as non-originating and pay the tariff? We have seen evidence of that in other free trade agreements; a manufacturer has just chosen to pay the tariff because it is the least-cost option in comparison to proving origin.

Q15 Baroness Kramer: Could I stay with rules of origin but focus a little more strongly on diagonal cumulation, or its absence? There are two things that I would like you to explore. Do you have a sense, in more practical terms rather than terribly high level terms, of the impact on supply chains? Are we going to see companies shift from sourcing globally to sourcing either within the EU or the UK to any significant degree? Is that going to change?

Secondly, do you see opportunities in the future to renegotiate the characteristics of rules of origin, so that we have an opportunity to include, for example, diagonal cumulation with countries, particularly where both the EU and the UK have free trade agreements, especially ones that are very similar?

Fergus McReynolds: Absolutely. Trying to understand why we did not get to a position of ensuring that we have diagonal cumulation in the agreement is a challenge. That was our preference for the agreement. We did not end up in that space.

As to how that will change people's sourcing and supply chains, as I said, it is important for the individual business to understand whether it makes more economic sense to address some of those challenges. As you have highlighted, some companies might well look to source more locally. They might also simply change the way they operate, so that they bring in components to different parts of the partnership. A company might choose to bring things into Northern Ireland. They might choose to bring things into another EU country in the first instance. Trying to understand how those changes will evolve over time will be a challenge. I do not think we know that today, in the first month of the agreement, but they will start to become evident over the course of the coming months.

I do not see that renegotiation in this area will be possible in the first few months of this agreement. I understand that Michel Barnier spoke to Tony Connelly at the end of last week and made it very clear that he did

not see it as an area for renegotiation. That said, there are specialised committee structures that can address some of the issues. Perhaps there are system issues that could be addressed to try to make some of them easier. There is a particular challenge with international trading rules that do not fit comfortably with the sort of integrated supply chain relationship we have with the EU. That probably needs to be addressed. I am thinking specifically of content that originates in one or other of the markets, undergoes no processing in that market and is then re-exported to the other market.

The simple nature of that issue is that, traditionally, in a free trade agreement you do not bring a product in from a country, do nothing to it and re-export it to that country. You would not bring something in from Canada, do nothing to it and then try to sell it to a customer in Canada, but the way we are set up means that, if you did that under this agreement, you would attract a tariff because you had not converted it to a domestic content.

That is where I would like to see discussion, so that something could be agreed that recognises our unique relationship, and that it is quite common for companies to bring things into one market, into the UK, not to do anything to them and then supply them to the EU market. An example could be tomatoes grown in Spain. They are wholly obtained in the EU. They come to the UK. You do not process them, and then you export them to an EU country, perhaps the Republic of Ireland, or even internally to Northern Ireland. By the nature of not being processed, they lose their wholly obtained content. Reality dictates that they are still Spanish tomatoes, so surely they should be able to be traded without a tariff.

Some of those issues could be addressed, but it will be some time before the two parties get to the long-term issues related to structural negotiations on diagonal cumulation.

Baroness Kramer: That is very helpful. Could Alessandro follow up on that?

Alessandro Marongiu: I fully agree with Fergus. In the short term, the parties are likely to focus on the implementation of the deal. It is possible that either the EU or the UK will seek some amendments in the near future, but those are likely to stem from identification of unintended consequences or from lack of time for proper legal scrubbing rather than from any intention to reopen discussions on very substantial issues at the core of negotiations.

We are in the process of identifying some of those issues. The sector will decide whether it is worth asking for an amendment or not. One area was cited by Fergus: the absence of a clause to allow EU or UK originating content to maintain preferential origin when re-exported unaltered to the country of origin. Another is additional flexibilities for so-called electrified trucks that will not benefit from the very flexible rules of origin that are available for other electrified vehicles.

Extended diagonal cumulation with common trading partners is unlikely to be raised in the near future. An enabling clause in the deal would have paved the way for further discussions, but regrettably that was not agreed by the parties. It is no mystery that the automotive sector would have benefited from extended cumulation of content from common preferential trading partners, in particular for a selected number of commodities.

The industry would look favourably on such an option, but realistically a discussion on that point can happen only if there are fundamental changes in the interests of the parties, and such shifts are likely to take place only in the longer term.

Baroness Kramer: Luke, is the tomato problem at the top of your list for immediate negotiation? Do you have any other comments on that range of issues?

Luke Hindlaugh: The issue Fergus raised about goods coming in that are not processed and get caught under the insufficient processing rules predominantly impacts EU businesses that have set up hubs in the UK to supply both the UK and Ireland. Where the particular issue lies is for goods that move on to the Republic of Ireland. That is where the impact will be felt, because it is the most efficient way to continue serving both the UK and Ireland.

The way that market is set up is that about 95% is in the UK and about 5% is in Ireland. Businesses do that, because it is the most efficient way. If they have to stop doing that, it means either that they stop supplying or that they have to start supplying from the EU to Ireland direct. That is where the impact lies.

On the original points you touched on, diagonal cumulation will push UK businesses to reorientate their supply chains. To take a specific example, in sugar confectionery the lack of diagonal cumulation, or a product-specific rule that allowed for value thresholds—it was only a volume threshold—means that the majority of those manufacturers are probably unlikely to be able to continue sourcing sugar from fair trade sources or non-EU sources. They will be pushed to use UK and EU producers of sugar. Going back to Lord Turnbull's point about how easy it is to do, I think it is easy enough if you have time to do it, but the late notice and lack of grace periods mean that you are very much trying to fix it while you are still riding the bike.

To go back to the points about opportunities to change, as Fergus and Alessandro have touched on, we are unlikely to see the reopening of the rules of origin negotiations. Where there is probably most potential is in streamlining some of the ways to meet the rules of origin requirements. Currently, you have to do certificates of origin. You have grace periods on supplier declarations, but you will have to do that anyway. You can digitise those methods to make it a bit easier for both the exporter and the importer.

There are other avenues outside the rules of origin. Text on the single window in the TCA would be very much welcomed. Currently, exporters and importers have to submit the same information to multiple government agencies, which is quite time-consuming.

I think there is text on creating, and piloting, one single window or customs office to halve the amount of paperwork, rather than having to submit the export safety and security declaration, the export declaration, and then the import declaration and the import safety and security declaration. That system is currently in place, I believe, between Norway and Sweden. Those are the kinds of easy wins that the committees should be prioritising.

The Chair: Thank you very much. I remind colleagues that we are on a timed session.

Q16 **Lord Faulkner of Worcester:** I thank our witnesses for coming to see us this morning. This is a question for Alessandro, but I am very happy to hear from Fergus as well.

I want to ask about the automotive industry and the effect of the TCA on it. Perhaps you could give a general answer about the overall effects, and then say whether the UK will become a less attractive manufacturing base for Asian car manufacturers, say from Japan and Korea.

If there is time, I would like to ask you about batteries and the Sunderland plant. Alessandro, you have written extensively on this. We read what you wrote on your Twitter feed on 29 December. I found that really helpful in framing the question.

Alessandro Marongiu: Thank you very much for the question, Lord Faulkner, and for the kind words about my Twitter activity.

The impacts on the industry will largely depend on the ability of the sector to meet origin requirements and adjust to the new trading environment. However painful it might be to deal with rules of origin now, it is a far less fearsome prospect than facing a non-negotiated outcome that would have meant that tariffs applied, no matter the origin of goods.

To give a fair evaluation of the rules of origin agreed under the TCA for automotive products, it is important that we get the terms of comparison right. Comparing the trading terms under the TCA with the terms offered by the customs union and single market is comparing apples with oranges.

If the benchmark is rules set by similar FTAs, the deal is a mixed bag for the sector. There are some very ambitious rules applicable to automotive products under the TCA. Origin rules are applicable to the vast majority of parts and components, in line with some of the most ambitious deals, but the most significant achievement is the six-year phasing period for batteries; electrified cars, including hybrids; electrified buses and electrified commercial vehicles. The transitional rules applicable until the end of 2023 on electrified vehicles and batteries are, to my knowledge,

unprecedented. Without those facilitations, most electrified vehicles would probably have faced tariffs despite the conclusion of the deal.

Overall, it is a mixed bag, so the impacts will be different depending on what automotive goods you are trading and when. For example, rules of origin on traditional vehicles or combustion engine vehicles are in line with most common precedents. Long-term rules on environmentally friendly vehicles and batteries are some of the toughest ever negotiated by the European Union and will require significant efforts to ensure compliance even in less than 36 months. We are in the early days of application. We will be able to make a proper assessment only at a later stage.

Beyond that, there are impacts that are already very visible today. The tectonic shift from participating in the single market to trading on the basis of an FTA is huge. It is felt by automotive businesses of all kinds, from very small operators to very large industrial groups. To name a handful of issues, UK-based regional distribution centres often face tariffs on exports to EU countries. The process of up-fitting vehicles—for example, to make vehicles wheelchair accessible—might not be enough to avoid tariffs on exports of those products to the European Union.

On remanufactures, they are struggling to import tariff-free cores, which are non-functioning parts to which they give new life through remanufacturing processes, because of difficulties of complying with the rules of origin and other customs requirements. Used cars are at high risk of tariffs, in particular when exported to the Republic of Ireland. There are several cases where, for example, internal combustion engine vehicles cannot meet origin requirements. When these models cannot qualify, tariffs apply already today.

Looking at future investment, following the initial shock, there are new, inbuilt costs that are here to stay and that might affect the competitive advantage gained by UK automotive manufacturers over the last decade. That is unavoidable, but an ambitious industrial strategy, where we could, for example, localise a significant proportion of manufacturing processing for cells and battery packs in the UK, will be essential to maintain tariff-free market access. It should include the production of active cathode materials and the coating of cathodes for electric batteries. A robust, competitive, Anglo-European supply chain for new generation vehicles will be key for future competitiveness, and a key determinant. Complacency with flexible rules is not an option if you want to retain that edge.

Lord Faulkner of Worcester: There was quite a lot of press at the weekend saying that Nissan had announced that it was going to start manufacturing batteries at its Sunderland plant later this year. Judging by what you have just said to us, that would seem to be an incredibly sensible business move. They may not be wrong at Nissan when they claim that it will give them a competitive advantage. Do you agree?

Alessandro Marongiu: First of all, the fact that there was an announcement indicates how positive it is to have a deal. Without the TCA, it would have been far more challenging for automotive businesses to make that kind of investment, so it is welcome news. It goes in the right direction. Obviously, we should not misinterpret an announcement on a single model to mean, for example, that future investment is secure. We will need additional investment, for example in the production of parts that are incorporated in electric power trains. We will need bigger investment in EU³ factories in the future if we want to remain competitive, and, if we want to cope with origin rules, that will be much tougher from the beginning of 2024 until 2027.

Q17 **Lord Inglewood:** I declare an interest as a farmer. I sell milk to Arla.

This question is addressed to Luke. The basic rule is that food imported from third countries to the UK and processed here does not qualify for tariff-free access to the EU market. How wide is the definition of processing? Does it include things like blending?

Secondly, what actual impact is it having now and, for that matter, will it have in the future?

Finally, do you think there is scope to make any easements and loosen up the regime within the framework set by the trade and co-operation agreement?

Luke Hindlaugh: There are quite strict rules, depending on how much processing is done. Simply affixing labels or packaging stuff often does not meet the rules of origin requirements, so if you have that sort of business model you will simply have to change where you source from.

Typically, within the product-specific rules, it will differ; some chapters will be stricter than others. As I mentioned, sugar and confectionery products are quite challenging because there is lack of a value-based rule, whereas in the white chocolate-specific chapter there is a value-based rule that will continue to help. Where they are particularly prohibitive is generally in processed meat. With chapter 16 products, you generally have to use a UK or EU originating source. In some cases, it can be within a change of chapters. I think there was a particular win for the use of certain fish that can be processed and made into things such as breaded fish and fish fingers. That can happen. There is a change of chapter, so you can use non-originating for that.

There are some particular challenges with other sources of meat. With chicken it is much harder to do. Typically, a lot of companies use non-EU chicken in certain products because they can get it at volumes and prices that make economic sense. There is not sufficient capacity within the UK and the EU to do that at the moment. The typical preference of UK and EU consumers is for the breast meat and white meat of the chicken. If you are sourcing that from non-EU counterparts, you can get it at those

³ Note by witness: "and UK"

prices because in those countries they have a whole carcass balance, and they can make it a viable operation.

Lord Inglewood: It will have quite a wide-ranging impact. Do you sense that politically it will be possible to negotiate quite a lot on the margins, or not?

Luke Hindlaugh: The impact will very much vary, depending on what kind of sector you operate in. The PSRs will vary. The opportunity to renegotiate is very limited. Both parties are probably quite hesitant to reopen some of these things. Where perhaps there could be easy wins, using the committees, will be in digitisation and making it more streamlined to prove the origin and get some hands-on support for the traders operating it. I do not think we will see wholesale changes to either diagonal cumulation or product-specific rules. I think they are here to stay. In the next six to nine months, companies will adjust.

Q18 **Lord Russell of Liverpool:** Border controls are being phased in at different times. We have EU controls that already apply as from the beginning of this month, whereas a variety of UK checks are being phased in, typically from the middle of this year onwards. In your view, does that create a risk that supply chains will be reoriented towards the EU and that some UK exporters may face a long-term disadvantage?

Fergus McReynolds: We are very disappointed that we did not see easement on both sides. That was a priority for us, and for our European counterparts. We had a very strong collective message that seeing the text of the deal just over a week before the end of the year, despite perhaps having been able to predict 90% of it, and then having to apply those things from 1 January, has been a considerable challenge, not just for businesses in the UK but for businesses across the continent.

Do I think that it will start to reorient sectors? It is important to address the issue that easement is just that. It does not alleviate the business of any responsibility. While businesses have an opportunity to delay submitting some of the paperwork, they still have the responsibility to have all the calculations and the administration in place, and to know that they are compliant with the rules. It is simply an easement in when they are able to submit some of those forms.

I do not think it will have an impact right now. Most companies are taking time to assess how the relationship will develop over the coming months and years. We are starting to see some issues at the border, but they are a combination of many factors.

I will give some examples, in one, two, three order. The first instance is that there was disruption before Christmas due to the Covid restrictions which many EU countries brought in, but global supply chains are being disrupted generally, which has had a huge impact on businesses. That is one of the key issues. It is becoming less relevant as time passes, but it still has a residual effect.

Many companies chose to stockpile. The PMI data, which was released in the first week of January, clearly showed that in December a lot of businesses had chosen to do so. They tried to avoid the period of the first couple of weeks. We are starting to see those stocks come to an end.

Finally, we are starting to see the real impact of the new measures. While there is easement in place on the UK side, which is entirely welcome, it does not alleviate a business's responsibility. Would we like to see things on the EU side? I think so. There is probably still a conversation to be had, because the real impacts of the changes have not been seen. Levels of trade have not been at their normal levels. Over the coming weeks, and certainly towards the end of this month, we will see that really have an impact.

Luke Hindlaugh: I very much agree with Fergus. I do not think the easements will bring wholesale changes to supply chains that make it much easier to relocate to the EU. The grace periods have been very helpful. It is no coincidence that imports are faring much better than exports. They have had more time to bed in, and that has helped to protect some of the flows.

At the end of the day, disruptions to the immediate imposition of checks and controls impact businesses and consumers. I do not think there is, or was, any sort of appetite to replicate that for UK businesses. EU businesses will face the same challenges come April for SPS, and then in July when the checks and the customs requirements have to be done. Those are coming to EU businesses. I think the hope is that, now that the UK Government have control of their own import regime, they can build that back better and make it more streamlined for importing businesses in the UK to get the critical ingredients they need to continue manufacturing for the UK market.

The Northern Ireland grace period has been very helpful for GB food and drink manufacturers continuing to supply to Northern Ireland. There is hope that GB businesses can continue on that basis after the grace period ends, and that we can find long-term solutions to continue allowing UK businesses to operate across the whole UK.

Q19 **Lord Berkeley:** I would like to follow up Lord Russell's question. How serious will the technical barriers to trade in the TCA provisions be in the long term? We read in the press at the moment stories about pretty horrendous delays and about failures of multiple IT systems. They may be caused by unfamiliarity. I do not want to go over old ground, but there always seem to be quite serious issues particularly with SMEs and their small packages. There was even one story of an SME setting up a distribution centre somewhere in the EU to avoid multiple package documentation, which seems to be a problem.

Do you see these as just teething troubles that will be over when companies get used to things, or do you see a wholesale change in where companies set up parts of their operations, or even just less trade generally?

Fergus McReynolds: The provisions in the agreement that address some of the technical barriers to trade are very welcome. The fact that we have a specialised committee that will look at that is important. We are seeing some issues at the border at the moment. Some of that is system and some is structural. The system issues have the opportunity to become less disruptive and more predictable. It is absolutely true that it will take more time. You will have all the requirements for passing goods across the border, which means that access to the market in both directions will not be as quick as it would have been traditionally, but the system issues should become more predictable in the future. In the future, you could run just-in-time supply chains when predictability was back in the system.

There are acute issues at the border at the moment; we have certainly seen that. Some of them have been system disruptions; some of it is about manufacturers coming to terms with understanding their responsibilities; and some of it is about the weakest-link-in-the-chain issues in groupage that you talked about. We have certainly seen issues where manufacturers have had products returned to site despite their having done everything they needed to do. It was returned, because it was part of a broader shipment, a bigger consignment, and one actor in that supply chain—one of the consignments—did not have their paperwork in order. There are certainly issues on groupage with multiple consignees that will affect SMEs much more. We are starting to see that.

We are starting to see increases in the cost of logistics. Shipping costs have increased significantly since the beginning of the year. Those are system issues that I hope will become easier and more predictable over time. It is true that it will take longer and that it will cost more, but the time and cost implications should become more predictable in the future.

However, there will be some sectors and some businesses where it is structural and it will change their supply chains. It will mean that it is not necessarily economically viable to continue to operate in the way they have done historically. There is a combination of both those things. The role of the specialised committees is to address some of the issues and make sure that we address system issues very quickly, but unfortunately there are some structural issues that cannot be addressed because of the nature of the agreement that was concluded.

Lord Berkeley: Luke, do you think the fish export industry, not the fishing industry itself, will get its act together so that it can continue without the delays that are clearly very serious?

Luke Hindlaugh: For the fishing industry, particularly with groupage, there will inevitably be teething issues with how the paperwork is presented. Have the stamps by the vets been done in the right colour? Are they numbered correctly? It can be done a few hours earlier. A lot of the issues are probably structural.

I do not think that any one partner within that chain is to blame; it is very much the case that everyone is struggling to come to grips with

some of the new processes and they will take longer. There have been issues with all the various people who are putting loads on to a lorry getting the paperwork in order and getting the EHCs signed, which takes time. You have to prove to the vet that you have met the information. There is work involved in navigating all the various IT systems and uploading them. For fish, there are customs, catch certificates and EHCs. All have to be uploaded to separate systems. Even when you get all of them right and the stars are aligned, it takes quite a long time to get through some ports.

Some of it will be teething issues, but some of it is here to stay. SPS in particular will take a long time. It is hard to meet the requirements. You probably will not be able to get an order and ship it on the same day; it will take three or more days to get through. Inevitably, that will be a decision for customers in both the UK and EU to get to grips with. These things will take longer to get through. There is a chance that your lorry or truck will occasionally be pinged for a check, and that will delay it even more. The customer will face a choice. Do they want to take that risk or source from somewhere else?

The Chair: Thank you very much. If the witnesses feel afterwards that they can provide something in written form as a supplementary so that we do not miss out any of the questions, that would be very helpful.

Q20 **Lord Wood of Anfield:** I would like to ask about mutual recognition of conformity assessments, which was pressed for but did not appear. In their absence, what do you estimate is the cost to UK business and trade between the UK and EU of having duplicative certification procedures? Is it something that businesses are getting used to rapidly, or is it proving a big obstacle?

Alessandro Marongiu: The agreement has a general chapter on technical barriers to trade, as well as a specific annexe for motor vehicles and equipment. I will focus specifically on the annexe for the industry. The inclusion of the annexe is an important achievement, taking into account quite divergent initial positions between the negotiating parties. It recognises that the highly regulated and highly integrated automotive sector deserves specific provisions and particular attention.

The automotive industry is lucky enough to benefit from a broad international regulatory framework under the aegis of the United Nations. The annexe mainly consolidates and reiterates provisions held in different United Nations conventions—the so-called UNECE framework. That is particularly important for type approvals of components and subsystems.

However, the annexe falls short on several key industry demands. Essentially, it fails to recognise that the parties followed exactly the same regulations until the end of December. The annexe does not mutually recognise whole vehicle type approvals or approvals of subsystems that are addressed outside the UNECE framework. It also does not mutually recognise respective technical services that would have been instrumental in simplifying the type approval activities for manufacturers

and would have eased the process of mutual acceptance of conformity assessment results. While the annexe is indeed very welcome, it is not as far-reaching as hoped, and it does not include unprecedented provisions.

The SMMT assessed the potential costs of different negotiating outcomes. We have yet to quantify the impacts of the result of the negotiations on regulatory aspects. Costs would have been minimised if the UK had remained an integral part of the EU type approval framework, or if there had been a more comprehensive mutual recognition agreement, but the less ambitious result means that products exported to the EU have to comply fully with EU type approval and testing requirements from day one.

On this side of the channel, there is a UK provisional approval scheme; it is a unilateral measure allowing temporarily EU-approved vehicles to be marketed without further problems, but all UK type approval and testing requirements must also be met when the UK type approval framework will be fully implemented.

In sum, administrative duplication and added costs are unfortunately unavoidable.

Luke Hindlaugh: For food and drink, conformity assessment does not really apply. Where you would see it is in the lack of ability to get sanitary and phytosanitary equivalence. That was really disappointing for the industry. If we had had equivalence, we could have signed off our exports based on UK rules. The fact that they would have been equivalent to the EU rules would effectively have reduced the physical checks. It would have had the benefit of reducing physical checks to about 1%, whereas now for fresh meat it will be about 30% and for others it will be 15%. That means that we have less access to the EU market than New Zealand did with its veterinary agreement, which gave it equivalence.

There are also implications for GB to Northern Ireland trade. At the moment, we have the grace periods. If the grace periods end with full EU rules and compliance, it will mean that GB manufacturers have less access to Northern Ireland than New Zealand producers.

Q21 **Lord Lamont of Lerwick:** I would like to switch back to the motor industry. This is a question to Alessandro. The motor industry is facing huge disruption anyway, quite apart from Brexit, particularly with the advent of electric cars, so supply chains in the future will be completely different from existing supply chains. In fairness, I think you have given a very balanced picture.

Lord Faulkner referred to Nissan. I was very struck by a statement made by Ashwani Gupta, chief operating officer at Sunderland. He said, "Brexit for Nissan is a positive ... We'll redefine ... the auto industry in the UK. In certain conditions, our competitiveness is improved. For some of the cases, it is at par. It depends on which car". He then talked about increasing production to 700,000 vehicles a year. Is that just because of Nissan's position in electric cars? I should add that he went on to talk

about paperwork and cross-border disruption, and was quoted as saying, "For a global manufacturer operating in 150 markets, with 40 plants worldwide, to have additional documentation to fill a form at the border is nothing. People are prepared for it". Why do you think he can take such a strikingly different view?

Alessandro Marongiu: I do not think it is a strikingly different view from mine. Big businesses can handle customs procedures. That does not mean that they do not impact their cost structure. They were able to trade without facing friction in the past, but now they are facing friction and will face it in the future. That said, clearly a global player such as Nissan can address customs requirements, and potentially comply with them, without facing the difficulties that smaller operators face today.

As regards prospects for Japanese investment, the TCA is good news because it lays foundations on which businesses can build and be competitive in the future. Nissan and other manufacturers have built their competitiveness over the years. They want to protect their investment in the UK. I think they can make it work; they appreciate that the TCA can help them to build a successful business in the future, but beyond the immediate announcement, and the welcome news of additional investment for existing models, we need to build a stronger supply chain in the UK to attract investment for future models and for environmentally friendly models to be built here.

Q22 **Baroness Chalker of Wallasey:** My question is for Luke. We witnessed last week a protest in London by Scottish seafood exporters, which highlighted the impact of the existing sanitary and phytosanitary measures on UK business. I understand that it applies also to some meat exporters. How are your members adjusting to the SPS demands of the TCA, and to what extent do the provisions of the TCA minimise the SPS barriers to trade? I think that about sums it up. There is a lot of protest and worry, particularly for very time-sensitive exports.

Luke Hindlaugh: What the deal does in the SPS area is very little compared with no deal. Many of the requirements are still there. You have to comply with the export health certificates that you need to send to the EU or those coming into the UK. The benefits are that it creates trust between both trading parties, which probably helps to manage some of those imports and exports and allows them to flow a bit better. It is too soon to say how traders are adapting, or how trade flows will continue, particularly given the seafood problems they are facing up there. It is not just that sector. A lot of meat exporters using groupage face very much the same issues.

As time goes on, it will get better; businesses will understand some of the requirements, but a lot of them are here to stay. SPS barriers are some of the most cumbersome for trade and some of them are here to stay. Exports will take longer. In particular, it will be difficult for SMEs that rely on groupage. You can get it right as many times as you want, but if someone else gets it wrong, the lorry is held up. One of our members has had orders for about 50 different consignments. Most of them were on

groupage and only about two made it over the EU border; the rest of the 48 were held up. The lorries cannot move; none of the orders in those groupage loads can move. It is very tough to overcome some of those things, and they are very much here to stay.

Baroness Chalker of Wallasey: Thank you for that reply. I am sorry. That is why some of us were really worried about the whole leave movement.

Q23 **Lord Lilley:** To follow on from Baroness Chalker, what leeway is there, either under the trade specialised committee on SPS measures or through arbitration procedures, for us to get a smoother flow of trade without SPS stopping it? The actual agreement says: "The Parties shall not use SPS measures to create unjustified barriers to trade"; that "SPS procedures and approvals" shall be "completed without undue delay"; and that barriers must not be "applied in a manner which would constitute arbitrary or unjustifiable discrimination".

It reaffirms the WTO commitment that "Members shall accept the sanitary and phytosanitary measures of other Members as equivalent, even if these measures differ from their own". The reports we get suggest that that is not how it is being operated on the continent.

Luke Hindlaugh: In some of those challenges, there is also an obligation to meet the requirements that the importing party sets. There might be discrepancies in the paperwork or it might not have met all the requirements. There is little opportunity within the deal to help on some of those issues. Where government can help is with hands-on support for some of those traders to guide them through the processes. Are they getting each of the requirements right? Are they getting the customs paperwork right? Are they getting the sanitary and phytosanitary processes right?

It needs real hands-on support, walking people through it so that they can identify the common mistakes they are making and address them, or find ways to redirect the logistics routes they use. Those are the kinds of things that government should be prioritising, but within the realms of the deal there is not too much that traders can do. It is very much about hands-on support from HMRC and Defra such that a small trader can pick up the phone and say, "I'm having these issues. I want to send a good over to the EU. What should I do? Who should I call?"

Lord Lilley: I agree that that ought to be done and that it ought to be a high priority, but surely the two are not alternatives. We have to help our traders meet any requirements on the continent, however unreasonable they are, but if they are unreasonable we ought also to be proposing changes and objecting to them when they act as clear barriers to trade because they do not recognise our standards as equivalent when they are identical.

Luke Hindlaugh: It is an issue when you leave the single market and there is not that kind of equivalence bridge. Our rules may well be the same, but once you leave you have to prove that you are meeting the

requirements 100% each and every time. Sometimes, there can be tinkering issues when you have to make changes in such a short time.

Lord Lilley: It says that they should make checks based only on risk assessments, which is what they did for New Zealand, is it not?

Luke Hindlaugh: The difference is that New Zealand has a veterinary agreement with the EU, so there is a bridge and equivalence between the New Zealand and the EU rules, whereas we did not get that for the sanitary and phytosanitary measures.

Lord Lilley: But the agreement still commits both sides to follow the WTO. The WTO says that members shall accept the sanitary or phytosanitary measures of other members as equivalent, even if they differ. I cannot understand why we make excuses for them not doing so. Why are we not complaining?

Luke Hindlaugh: It might be for UK and EU officials, when they meet, to address those issues and create common ways of overcoming some of the barriers, but there is not much of an avenue for traders themselves to do that.

Lord Lilley: It is not for the traders. I agree.

Q24 **Lord Shipley:** I would like to ask all three witnesses about government guidance to businesses following signing of the agreement. The Government have issued some guidance, for example on agreed rules of origin, but it is not clear whether it meets the specific needs of UK businesses, generally speaking. There are four chapters and two annexes to the guidance and a disclaimer that states: "Legislation takes precedence over the content of these documents and should always be consulted". How clear is government guidance for businesses on mitigating the impact of non-tariff barriers to trade, and what more should the Government be doing?

Alessandro Marongiu: In principle, the government guidance is quite comprehensive, but businesses face issues on so many different fronts that navigating the guidance becomes overwhelming. Understanding guidance is a very different matter from translating it into actions that make the whole thing work. Business associations such as the SMMT offer as much support as possible to connect the dots or indicate potential solutions, but many businesses need bespoke services. Those are often costly and are an additional strain in an already critical situation where businesses are dealing with depressed demand and a very serious change in trading terms with their biggest trading partner.

The EU put a €5 billion fund in place just to deal with the fallout from Brexit. Dedicated support could have been considered in the UK as well to help businesses get tailor-made advice. I leave it to others to comment.

Fergus McReynolds: I agree with Alessandro about the challenge facing businesses at the moment. Comprehensive guidance is available from government, but it is the scale of change that companies are trying to

deal with. There is also the issue of trying to understand the environment in which we now live.

I do not know what the message has been from 1 January about the different relationship, in both trade and market regulation, in Northern Ireland in comparison with GB. I think more information needs to be provided about recognising that there are three different markets in which goods are being placed. You need to consider different challenges depending on where you are operating. If you are in GB, sending something to Northern Ireland is different from being in Northern Ireland and sending something to GB. Equally, in either of those two markets, sending something to the EU looks different. It is important to make sure that companies are aware of that.

To link this with Lord Wood's question on conformity assessment, I do not know whether enough was made of the difference in market preparation to be ready for those three different markets, and whether companies have their conformity-assessed products, with an EU certificate where necessary, to be able to continue to supply the EU market. I am worried about that as a challenge. I do not know whether enough businesses are ready for that.

From our perspective, what is important, as Alessandro said, is making sure that there are worked examples. That is one area where we could improve the guidance. People could then work through case studies on things that have come up in questions that we have had from companies.

On support from government, as Alessandro said, the EU, as part of its recovery package has a €5 billion fund. Many member states have had voucher schemes to help businesses prepare in the run-up to the changes. It would be good for the Government to explore such schemes.

Finally, it is recognising how businesses operate. It goes back to the issue about conformity assessment. The advantage for a business is to try to make one product for multiple markets, not to make multiple products for multiple markets. While the issues are not there today, they have the potential to be there in future, and how divergence is managed will be a huge part of how the relationship develops over the coming years.

For me, one of the clear issues missing from government guidance is how we will manage that divergence, and how we, either as individual businesses or collectively as business representative organisations, feed into that dialogue and conversation. We want to avoid a separate market in the UK that has a completely different set of requirements, and a completely separate set of rules to comply with, to service the EU market. That is not just an ambition for us; it will also be an issue for our international trading partners. I have spoken to American colleagues about this; they do not want to be in a situation where they have different requirements to supply a customer in continental Europe from those for supplying the UK.

Management of divergence and understanding how we create a mechanism that means that companies can make one product for multiple markets will be a big part of the process. For me, there is a gap in understanding how the Government will hear from businesses on that issue.

Luke Hindlaugh: I very much agree with what Fergus and Alessandro have already said. For food and drink in particular, it is a matter of bringing everything together. There is so much for the food and drinks industry to do and understand, be it customs, sanitary and phytosanitary requirements or VAT. All of it needs to be brought together.

Some hands-on support would really help some of those businesses. In a way, we sort of saw it with the creation of the border and protocol delivery group, which can bring together all the departments that operate across the border. That should be very much followed in the guidance, so that it can provide hands-on support, whether it is understanding what businesses need to do to classify the commodity codes their goods need, or tools whereby they can punch in the ingredients of their goods to understand whether they meet the rules of origin requirements. It is about bringing all of that together and providing some hands-on support for businesses.

The Chair: Thank you very much. Thank you, colleagues, for all your questions and to our witnesses for their very detailed contributions this morning. It would be really helpful to the committee if all three witnesses could reflect on question 9 and give us slightly more information, building on what Fergus said about divergence, about what you want businesses to see from government and what you want the specialised committee to focus on. That would be very helpful to us. I invite all three of you to give us some written information on that from your particular perspective.

On behalf of the committee, I thank you once again for your very detailed input this morning. It will be very useful to us in our report. As I said earlier, if there are any minor corrections that need to be made, please let us know as soon as possible. On behalf of all of us, thank you so much for taking the time to come in today. I think colleagues will agree that it has been an exceptionally good session.