HOUSE OF COMMONS

Committees on Arms Export Controls

Oral evidence: UK arms exports in 2019, HC 224

Tuesday 29 June 2021

Ordered by the House of Commons to be published on 29 June 2021.

Watch the meeting

Members present: Mark Garnier (Chair); Sarah Champion; Tobias Ellwood; Chris Law; Mrs Emma Lewell-Buck; Lloyd Russell-Moyle; Martin Vickers.

Claudia Webbe also attended, pursuant to Standing Order No 137A(1)(e)

Questions 124-149

Witnesses

I: David Lorello, Of Counsel and Vice Chair of International Trade Controls Practice Group, Covington and Burling LLP, Fenella McGerty, Senior Fellow for Defence Economics, International Institute for Strategic Studies and Dr Clara Portela, Professor of Political Science, University of Valencia.

Examination of witnesses

Witnesses: David Lorello, Fenella McGerty and Dr Clara Portela.

Q124 **Chair:** A very good morning to everyone. This is the fourth evidence session in the Committees on Arms Export Controls inquiry on UK arms exports in 2019. Today's session will explore, with expert commentators, the potential impact of the UK's withdrawal from the European Union on strategic export controls and sanctions policies. Before we start the session, I would like each of the witnesses to give a quick introduction. Perhaps I can start with you, David.

David Lorello: Good morning. My name is David Lorello. I am a lawyer in the London office of the international law firm Covington and Burling. I serve as vice-chair of our firm's global export controls and economic sanctions practice. We represent clients across various industries, managing compliance with UK, European and other national trade controls regimes. Lest my New Jersey accent give me away, I should note that I began practising law in the United States but have been living and practising in this country for the last 16 years, with a focus on UK and EU trade controls. It is an honour to be here, and I look forward to the discussion.

Q125 **Chair:** Fantastic. Thank you for coming. Fenella, perhaps we can go to

you next.

Fenella McGerty: Good morning, everybody. Thanks for having me here today. My name is Fenella McGerty. I am a senior fellow for defence economics at the International Institute for Strategic Studies. I am based in London but am speaking from Yorkshire.

I specialise in defence expenditure, defence economics and procurement trends, primarily in Europe and the Middle East, with further experience in wider industry analysis, looking at offset, M&A activity and programme development and opportunities.

Before joining the IISS, I worked at Jane's for over a decade, leading the development of their defence economics portfolio. I am very much focused on the numbers side of the debate.

Q126 **Chair:** Thank you. Clara, over to you—name, rank and serial number.

Dr Portela: My name is Clara Portela. I am a professor at the University of Valencia in Spain; I am originally from Spain. I am an academic specialising in the sanctions policy of the European Union.

Q127 **Chair:** Thank you very much. Fenella, can you give us a brief but wide-reaching overview of the effect of Brexit on EU defence and security exports?

Fenella McGerty: We have statistics that go back to 2016, and they post pretty strong growth for UK defence exports, if you use the DSE—formerly the DSO—data. The UK's share of exports has increased from below 10% in 2016. We are now closer to 16%. There is remarkable growth there, in many ways, but the context is that the figures tend to fluctuate with wider trends. We have estimated that the value of global defence exports fell in 2019 and potentially 2020—we haven't put all the data in yet—so even though there is that increasing share, it is of a slightly smaller market.

The other area of concern is that the primary destination for UK exports is the Middle East—it is around 60%, or even closer to 80%, of UK exports by destination over the last 10 years. In recent years, an increasing amount of accountancy for UK defence exports is in that region. If you consider the impact of Covid-19 on Middle East defence spending, the main issue is the decline in oil prices. It is the third consecutive year of declining defence budgets in the Middle East, with their share of global spending falling. If you consider that that is quite a constrained and increasingly competitive marketplace, it becomes an area of concern for UK defence exports. Beyond that, the other major destination market, which is the US, could turn to favour domestic procurement, further constraining those opportunities for the UK.

On the EU side, the primary countries that are in the top 10 of defence exporters are still there: France, Germany, Italy and Spain tend to be fourth, fifth, sixth and 10th respectively. The defence trade with the EU in terms of exports is fairly small compared with exports to the Middle East or intra-European activity. That is because of a similar level of capability; they tend to be competitors, rather than trading with each other. Europe

as a market has not accounted for such a huge proportion of UK defence exports over the last 10 years—around 10%—so it is not the case that the UK is overly dependent on Europe and vice versa. The main issue is that European competitors to the UK face those same market challenges emerging in export markets such as the Middle East and—but less so—Asia.

Q128 **Chair:** On exports, have we seen a competitive advantage against, say, France and Germany as a result of being outside the EU, or has it not made much of a difference?

Fenella McGerty: I am sure we will talk about the regulations and the changes that have happened since then, but ultimately, in order to continue trading with Europe, the UK has not implemented too drastic a change to its export policy. The easing of restrictions, or at least the ability to export to markets without the restrictions that are put in place by countries with more significant arms export controls, has lessened now. However, I think the UK is still keen to conform as much as possible.

In its 2021 export report, France noted that it is facing a more constrained environment because of wider market dynamics. Brexit was mentioned in the report, but it was more in terms of the regulations that will have to change and perhaps what the UK does not have access to anymore: the ICT regulations and that free transfer of dual use. The main point that was highlighted in terms of Brexit was the change in regulations.

A final point on general exports: what we saw in Germany's recent export reports—this is still with 2019 data; we are waiting for 2020 data from a few countries—was that they had quite a bumpy year for defence exports in 2019, and it was because of intra-European trade. Where France and the UK tend to target the Middle East or Asia Pacific, certainly on the France side, Germany is more focused on home markets, or at least has been in the last few years. That is maybe a result of the nature of their defence exports: the UK is more aerospace focused, but Germany is more land systems and small arms. A bit of an area of concern for the UK, which is noted in the statistics report, is that that aerospace focus is at odds with our competitors, which have a more diversified export portfolio. So yes, that creates wider challenges as well.

Chair: Brilliant, thank you very much.

Q129 **Martin Vickers:** I would like to look at how things have changed in respect of export controls in the post-Brexit environment. David, can I come to you first? What has gone well, and what are the challenges?

David Lorello: It is fair to say that both the UK and the EU did a commendable job of more or less maintaining the status quo in terms of current regulations, from the standpoint of both dual use and military export controls. Of course, the military side is less affected by Brexit to begin with, because military export controls are almost entirely a function of national law, even for EU member states, so very little has changed there, even in terms of the core regulations.

With regard to the dual-use regulatory regime, the general licences that were amended and published by both the EU and the UK have more or less restored the status quo, in the sense that there is not a need to obtain specific licensing for exports of most dual use items.

There are increased administrative burdens on UK companies exporting to the EU; they now have to register for general licences, and have to maintain records and implement a compliance structure around exports to the EU—something they had previously not been required to do. I do not have the impression that that has been a particular concern for exporters in either direction.

Also, companies based both here and in the EU may need multiple licences to do things that previously it was possible to do under a licence issued only by the UK, or only by an EU member state. Again, those issues have been manageable, and were foreseeable. It was clear, leading up to the transition date, that these were things that companies needed to address.

I have not seen or heard significant concerns about where we are. The question really is what happens in the future; that is a harder question to answer with any precision. That is what companies are more focused on, particularly with the dual use recast; as I am sure you are aware, the EU has just published a revision of its dual use regulation. Will the UK follow suit? Over time, will we start to see more significant diversions in the dual use regulatory regimes? That is the key question, rather than the challenges that companies face at the moment.

Q130 **Martin Vickers:** And "How do you anticipate that turning out?".

David Lorello: Yes, that is the ultimate question. What would concern companies the most would be if we started to see fundamental divergences in the lists of items that are controlled for dual-use purposes. If you look at the recast that the EU has published, there are important and notable changes, including with regard to cyber-surveillance technology and some of the definitions in the dual-use regulation, but there are not really radical changes, or changes to the underlying lists.

If the UK were to start to forge an independent path, imposing unilateral export controls on products, and creating a dual-use list in the UK that starts to become fundamentally different from that of the EU, that would be the point at which companies would need to rethink their fundamental approach to complying with European export controls, because they would then have to deal with different lists. The probability of that happening seems low, because for the most part, the items on the dual-use list are a product of international arrangements, such as Wassenaar and the Australia Group, that the UK will of course continue to participate in.

Historically, the EU has been very reticent about departing from Wassenaar and other arrangements. We also see that hesitation in the recast, because there was talk about moving to unilateral export controls in the discussions around the recast, but that ultimately did not happen. I do not think we see clear evidence that the UK intends to depart from

Wassenaar and the other trading arrangements, but if that were to happen, it would impose significant additional compliance obligations on companies in this country.

Q131 **Martin Vickers:** Fenella, do you have any thoughts on this and the challenges? Perhaps we could also touch on whether the Northern Ireland protocol has raised any issues.

Fenella McGerty: Generally, as David mentioned, the changes are relatively mild, and there seems to be a desire to not move away from the export controls that the UK was so instrumental in developing with Europe. The underlying fundamentals of policy goals have not really shifted. Ideally, they would want to continue with broadly similar controls, avoiding costly regulations, new licensing requirements and things like that. One of the biggest challenges is that, following Brexit, the ICT directive no longer applies to transfers of defence-related products. We may touch on dual-use goods later, but certainly there was movement on both sides to avoid too much disruption.

Existing transfers remained in place, which meant that UK and EU companies benefited from as seamless a transition as possible. Those licences that were in place continued, and I think, certainly with Northern Ireland, they also made sure that valid transfer licences remained in place, to avoid an interruption of the flow of goods for technical reasons related to export control. It does create difficulties relating to Northern Ireland. The related transfer of goods will continue to apply under that protocol. There is recognition that we may need a bit more of a transitional period in which there may be a possible extension of these licences until further legislation can be put in place that makes sense of having one policy for Northern Ireland and another for the rest of the UK.

For now, it is a matter of trying to keep things as smooth as possible, but that dual-use issue will always create a major difference between Northern Ireland and the rest of the UK, in terms of defence exports. Again, that would point to the UK not wanting to move too far away from the EU regulations, in order to keep things as in line as they possibly can.

In terms of general co-operation, I think there was some discussion of defence and security in the UK-EU trade agreement. The general consensus was to agree to co-operate, and to continue to counter the proliferation of weapons through full compliance with existing obligations under agreements that were already in place—the multinational treaties. If both agree to continue with those, and indeed to develop their own instruments and effective systems of export controls, the theory is that it will continue to be a collaborative process. There was always regular dialogue to be established on this, and on the transfer of small arms and light weapons. So long as that process continues, it should hopefully start to ease some of the restrictions, issues and frictions that have arisen.

Q132 **Martin Vickers:** Based on what you said earlier, David, the industry's experience has been that, yes, it is a bit more challenging in respect of admin and bureaucracy and so on, but overall there have not really been

any significant difficulties, post Brexit.

David Lorello: That is correct. There have been hiccups here and there around the margins of issues—some of them, frankly, generated more by the EU member states than the UK. For example, I have heard that there are certain documentary and certification requirements that the Italian Government are imposing with regard to the supply of items between the UK and Italy. I think that is largely focused on defence items. However, those are more just a function of getting used to new and emerging documentary requirements around the supply of equipment and services, rather than prohibitions that are really impeding the bottom line. By and large, there have not been any fundamental issues that have come up that have raised major concerns.

Q133 **Chris Law:** David and Fenella, you have talked about some of the changes and the frictions at the edges. What are the risks and advantages of possible UK and EU divergence on export controls, for example, and on the consolidated criteria?

Fenella McGerty: The aim is to not diverge too much, in order to continue partnering with Europe, sharing information, and trying to continue that collaborative effort, which has been pretty successful so far. From my point of view, the feedback from industry is that the concerns primarily extend from transparency, coherence and nuances. If the differences are highlighted, that would help industry, as far as possible. Those differences between any new regulations or controls that were previously in place would really help.

The main concern that came through to me was the loss of access to things like PESCO and EDF. Even though that is quite a small pocket of funding now, if it continues to grow, what then becomes the impetus for UK defence is to invest in R&D and remain competitive, so that you provide that other source for partnerships, and provide an attractive option for those countries that could partner with each other and use PESCO and EDF. If partnering with the UK is the best option, that will override those priorities as well. It is really on the UK now to enhance its competitiveness and invest in R&D.

On harmonisation, I think the driving force behind those export control developments initially was to avoid having too many differences between the UK and European policies to create the perception that one is less strict than the other. That can be exploited by private procurement, or just have the UK being targeted as a lenient market.

We don’t necessarily want that, because if we lose that collaboration and information sharing, procurement agents might exploit those discrepancies between the UK and the EU, with either penalties or customs effectiveness. If that happens, harmonisation starts to become a lot more difficult, because you become such a different market, being targeted by different contracts, and you are moving further away. I don’t think either side would necessarily want that, especially with major programmes such as Tempest, and other European collaborative efforts.

There is such a great European footprint in the defence sector in the UK and vice versa. The UK has a significant presence on the European mainland. The fact that you then have to adhere to certain national regulations anyway would make it in the interests of both to try to harmonise as much as possible, to avoid that discrepancy and targeting from different procurement agents.

Q134 **Chris Law:** Thank you, Fenella. David, are the fears of divergence overstated, given the different application of the consolidated criteria prior to Brexit? For example, some nations banned exports to Saudi Arabia over the situation in Yemen, while others allowed them to continue. What are your thoughts on that?

David Lorello: From the standpoint of the companies that I have been working with, I don't think that the concerns over divergence really arise from how divergences in the application of the consolidated criteria might operate. The concerns are more in relation to more fundamental dynamics in terms of the structure of the underlying regulations. What is controlled? What types of licences are available? How do we define the key restrictions in the underlying trade controls regulations?

From the standpoint of the consolidated criteria, you are right to observe that there always have been differences in how they have been applied. As you know, there are catch-all provisions that allow for fairly wide variance in application. For exporters, to the extent that there were concerns over the UK moving into a very different type of consolidated criteria, it would be the risk that, by creating its own criteria that have not served the test of time, it would lead to a lack of predictability in whether a licence applied for would be granted.

For example, if we start to see new criteria that the agencies struggle to understand the contours of, does that result in a situation where one type of export to Saudi Arabia results in a licence being granted, the other not being granted, and industry unable to determine in advance with reliability what types of licence will be granted and what won't. That would be a concern.

Having said that, I think that concern can be addressed in a number of ways, including through up-front guidance to industry, and perhaps consultation with industry, around what the new criteria, as they are developed, might entail, so that companies are able to predict in advance, when they are negotiating contracts, and understand what might be licensable and what might not be.

Q135 **Chris Law:** Do current EU initiatives on arms controls, for example on dual-use items and the harmonisation of end-user certificates, mark the first stages of divergence between the UK and the EU?

Fenella McGerty: It is my understanding that EU and UK authorities have issued general licences to try to alleviate some of that pressure of the UK not being able to use the ICT and free transfer option. The new general export licence authorises export to the EU for the vast majority of the dual-use items that were not previously eligible for that licence-free

exporting. Even though that will potentially become a more restricted transfer—because it will be classed as an export, rather than a transfer—there have been ways of trying to alleviate that pressure. I think David mentioned that more stringent record-keeping requirement as part of that process.

I have not had any feedback from industry on the effectiveness of this new export licence, but I reiterate the request for transparency and sound policy where the Government work with industry to ensure that minimal disruption. The UK Government did commit to using that full gamut of policy tools that were available in the latest industrial strategy to promote UK exports abroad. That included economic and diplomatic tools, and it must include a coherent approach to UK defence exports and regulations. Part of that support is that clear and coherent export policy.

Q136 **Chris Law:** Lastly, David, what is likely to be the impact of the UK and EU's differing definitions on brokering?

David Lorello: There have been varying definitions around brokering for quite some time. The UK military brokering rules have not been identical to the military brokering standards in EU member states. I do not think that companies see the brokering issue as an issue, at least in the export controls context, that is amplified in some respect as a consequence of Brexit. I think what companies are attentive to is that there are now varying brokering standards within the UK. There is a military brokering standard, there is now a sanctions-related brokering standard—we can talk about sanctions if the Committee would be interested, because there are a number of implications of Brexit with regard to sanctions—which is different from the UK military brokering standard and is also different from the EU sanctions brokering standard.

Brokering is a complicated concept. The last time the UK military brokering rules were significantly revised was in 2010. Guidance was published by the ECJU in 2010 associated with those brokering rules, which to the best of my knowledge has not been updated. I think that Brexit could present an opportunity for the Government to take a look at lessons learned in implementing the brokering rules over the last 12 years, and ideally to find ways to unify, at least in interpretation, how the brokering rules apply in particular contexts.

To give you an example, both industry and, to be fair, the ECJU have struggled at times in understanding and applying standards consistently around a UK national who might be working overseas for an international defence company and is involved in negotiating sales contracts. Is that brokering? Yes, it is. Is that licensable brokering? That depends on a whole array of facts and circumstances. The ECJU has been giving to individual exporters advice on that particular issue that, in some cases, in different contexts, is kind of hard to harmonise.

Similar concerns arise under the sanctions regulations because they also—with regard to the brokering standards, at least—have extraterritorial effect, so if you are a UK national working overseas, you may be subject

to both military and sanctions-related brokering standards. If anything, the implementation of the new sanctions-related brokering rules could present an opportunity really to take stock of where the UK is, from a broad trade controls regulatory standpoint on brokering. Issuing updated guidance in furtherance of the guidance that was issued in 2010 could be an instructive exercise.

Chris Law: Thank you. I know there are questions on sanctions later, so I will leave it there.

Chair: Let us go to Sarah Champion next. I am slightly conscious that we are probably going to run a little over time. Bear in mind that we are a bit time pressed, but do not let that hold you back from a thorough investigation, Sarah.

Q137 **Sarah Champion:** I have heard your warning, Chair, so these will be quickfire questions. Both of you have spoken about the use of dual-use items. Could you speak specifically about how effective the new open general export licence has been in respect of dual-use items from the UK to the EU?

David Lorello: I think it has been very effective. I have not heard of any criticisms or complexities really arising from it. As I mentioned earlier, companies were aware that the open general licence was coming, so they knew that they needed to register for the new UK general licence. There was a widely held expectation that the EU would amend its equivalent general licence, EU001, which it did. I mentioned a moment ago that there are new administrative burdens for some companies that are using that licence. Those are record keeping-type requirements that are well known to exporters. There is nothing new or novel in the nuances and the conditions of that licence. I really have not heard any significant criticisms of the open licence.

Sarah Champion: Thank you. Fenella, do you have anything to add?

Fenella McGerty: I completely agree. I have not had any industry feedback that they are finding more bureaucratic controls or restrictions in general operating. As David said, the fact that it was coming was known, and again, there was that drive on both sides to keep trade flowing as smoothly as possible and to avoid the friction that might cause further issues down the road. I certainly have not seen any feedback that it has become increasingly difficult. I know that there are nuances and differences, but the main thing is that the transparency is there. That is kind of all that industry wants.

Q138 **Sarah Champion:** It is all we all want. David, do you foresee Brexit having any impact on the effectiveness of UK compliance processes and system?

David Lorello: Only in so far as when divergences between the UK and the EU occur, companies in the UK will need to be continually attentive to those changes. That will increase the burden on UK industry to comply. To give you a very pragmatic example, coming back to the brokering point, if

you have been operating for some time under EU definitions of things like brokering and have invested in compliance programme resources, documentation and so on, and the UK now has a separate, slightly different standard, you sort of have to go back to the drawing board. Complexity in and of itself will increase burden and the risk of non-compliance, even for companies that have nothing but the best of intentions. That could apply across military export controls, dual-use export controls, and really any area where there are now multiple standards that companies need to deal with.

Sarah Champion: That is really interesting. Thank you. That is all from me, Chair.

Chair: Thank you, Sarah. That was quick.

Q139 **Mrs Lewell-Buck:** Good morning, everyone. My question is directed to Clara. How effective are sanctions in respect of arms export controls?

Dr Portela: They actually regulate differently. One thing is export controls, and another thing is sanctions. The peculiarity about sanctions regimes is that they normally make it impossible to apply for licences in order to export arms—dual-use items. Basically, they paralyse dual-use trade. I don't have any information that this is not being effective, but in terms of implementation what I can say is that the European Commission has launched an initiative very recently, at the beginning of the year, in order to monitor a bit more closely the implementation of sanctions altogether, precisely because there are big discrepancies between countries in the EU in terms of the capacity that they have to enforce compliance and implementation of embargoes.

This seems to be, to some extent, related to the withdrawal of the UK, precisely because the UK had been the leader of EU sanctions for quite a while. Now that the UK has withdrawn, the EU are in the process of figuring out how they want to manage their own system. To be precise, the Commission has found a role in trying to monitor more closely compliance by individual member states, but this role is actually going to be a bit more important in the field of dual use, because the Commission has competence there, than on the specific aspect of arms embargoes. Because the role of the Commission is very limited, this continues to be mainly in the hands of member states.

To sum up, and to go back to your question, there does not seem to be any major problem with effectiveness, but at the same time, this happens to be one of the aspects in the field of sanctions where the Commission has—well, in general, the ability of Brussels to monitor and to follow what member states are doing is more restricted, so it remains to be seen whether the newly launched initiative or the broader reflection process on how implementation and enforcement of sanctions could be improved will end up having any implications for the transfer of arms. I hope that the other witnesses can complement this if they have specific insights from industry. Thank you.

Q140 **Mrs Lewell-Buck:** Thank you, Clara. Do any of the other witnesses want to come in on the back of that? No. Clara, you said that the UK had been the leader in this, in that the EU are figuring out how to manage their own systems. Will their systems not just replicate what the UK had if we were the leader in it, or is it more complicated than that?

Dr Portela: I was referring more specifically to sanctions, because there is a separate regime for dual use, which is basically managed by the EU trade. Dual-use items have the important participation of the Commission, because this is basically with the EU trade. But then when it comes to sanctions, it is the Council that is in the lead. When the UK was a member of the EU, the UK was often the leader of sanctions regimes, in the sense that it often initiated them and it also contributed the lists of items to be covered. Basically, it played a central role in the design of the sanctions regimes.

When we were talking about the dual-use regime or the export of dual-use items, the UK was one of the participating members. When we were talking about sanctions, the UK was in the lead. As far as the dual-use system is concerned, it remains to be seen whether there will be discrepancies or not, as the other speakers have been saying.

Due to the fact that Northern Ireland will still be covered by the dual-use regulations, both parties—the UK and the EU—have an incentive to ensure that there is a maximum level of convergence; otherwise that might confuse industry and eventually lead to some companies perhaps leaving Northern Ireland legally. They might base themselves in the UK—sorry, in the rest of the UK, elsewhere in Britain—in order to be able to benefit from a less complicated or more interesting environment. That might have negative consequences for the economy of Northern Ireland. Taking into account that the situation in Northern Ireland has improved because of, among other things, growing prosperity, we do not want to do anything to decrease the prosperity of Northern Ireland, because that might also have some consequences for societal harmony.

At the same time, the opposite might also be true. If companies with dual-use items start finding it easier to operate under the dual-use regulations of the EU, they might find it more attractive to move to Northern Ireland. It might even create some complex situations of "shopping". That is not something I can really comment on, because it is dealing with the domestic environment in the UK. As far as dual use is concerned, the incentives for both sides are to co-operate and to keep relations as close and as convergent as possible, on top of the reasons that Fenella and David were mentioning—lack of complexity and making the life of companies easier.

As far as sanctions are concerned, we are operating in a much broader and more complex picture. The UN Security Council has started to decrease its sanctions activity, partly because of the lack of co-operation on the part of Russia and China. Russia and China have become increasingly belligerent in opposition to unilateral sanctions, which is the practice of the US, the EU and the UK. That is having an impact on their

readiness to agree to UN sanctions regimes, in the context of the Security Council.

We are already witnessing a trend towards increased co-operation on sanctions by the US and its allies—first and foremost, the UK, but also Canada and the European Union. That is clearly reflected in the adoption of horizontal sanctions regimes—something that was absent from the practice of the EU recently. Due to precisely the initiative of the UK, the EU adopted the cyber-attack sanctions regime and the chemical weapons sanctions regime, and the human rights sanctions regime was closely linked to the initiative of the UK, even though it was formally launched by the Netherlands.

The thing with the creation of the new frameworks is that they are also in the process of being replicated elsewhere. We already have a human rights sanctions regime in Canada, and in Australia and Japan it is under consideration. That movement is setting the stage for increased co-ordination in sanctions matters between this group of likeminded countries, which is basically the Anglo-Saxon world-plus, EU-plus and Japan. The trend is precisely towards increasing co-ordination, so having any divergence about which countries or targets are under sanctions by the coalition of likeminded countries, or which items are banned and which are not banned, will not benefit the global effort towards, let's say, substituting UN Security Council sanctions. It will not be quite the same because, in terms of the legitimacy and efficacy, it is a completely different scenario. UN sanctions are much more powerful, but the second-best option is to restrict the options of the targets by banning them from basically the western market, including Japan, Australia and New Zealand. From that point view, the trend will be towards enhancing co-ordination irrespective of the specific situation in Northern Ireland.

Mrs Lewell-Buck: Thank you. I will leave it there because of the time, but there is lots to think about. Thank you very much, Clara.

Q141 **Claudia Webbe:** David, can you give us a brief overview of the impact of Brexit on the UK and EU sanctions policies?

David Lorello: The answer is a more complicated one if we verge into the nuances of how the underlying regulations are structured. I can offer some observations on that. From a policy standpoint, what is clear is that we expected there to be differences in approach in terms of which countries and which persons were targeted for sanctions as the UK left the EU, for the simple reason that the UK is no longer subject to the unanimity requirement that exists in the EU with regard to the imposition of sanctions. That was one of the obvious ramifications of Brexit from a trade control standpoint.

There have been instances in which the UK has been more aggressive in adding parties to the sanctions list. In some respects, including very recently in the last couple of weeks with regard to Belarus, the EU has been a little more aggressive than the UK. What Brexit does for the UK from an international law perspective is gives it wider latitude to impose

unilateral sanctions or to choose not to follow suit with regard to the EU, if the EU decides to pursue sanctions.

The subsidiary point, which I can address now or later, is that as sanctions are implemented, how are the details of those regulations implemented? Where there are changes in approach and definitions, how does that affect industry and efforts to comply with the underlying sanctions? That is a slightly different topic from the one you asked about, but we can come to that if it is of interest to you.

Q142 **Claudia Webbe:** As you have indicated, the changes are that the UK can now choose to participate or not, but is it as simple as that? What else specifically has changed?

David Lorello: There are innumerable differences between the UK and the EU in the specifics of the underlying sanctions restrictions, even with regard to sanctions programmes that the UK ostensibly carried over from EU law into UK law. The EU sanctions framework is implemented pursuant to dozens of Council decisions and regulations. Those have almost entirely been transposed into UK legislation in individual legislative instruments, but there are differences in how the UK has addressed definitions and guidance around certain aspects of the sanctions.

I will give you one practical example that I think maybe highlights the point. There are sanctions lists—asset-freezing lists—where, if you end up having a counterparty that is placed on one of those lists under both EU and UK sanctions law, you basically are no longer able to do business with that party. It is a blacklist. A number of Belarusian industrialists were recently added to both the EU and the UK lists. Companies subject to UK and EU jurisdiction now must cease doing business with those parties, except in very limited circumstances.

Under EU sanctions law, there is a standard whereby you are subject to asset-freezing sanctions even if you are not on the list—if you are majority owned or otherwise controlled by someone on the sanctions list. That is a standard that has been reflected in some fairly general EU guidance for a number of years. The UK has now created an ownership and control test that is in some respects a little bit more rigid than the EU test. It includes a number of underlying standards concerning how you define whether someone is owned or controlled by someone else. That results in companies having to take slightly different approaches in evaluating those issues. This is an area where the concept is the same, but the implementation of the concept requires companies in this country to think differently about the type of due diligence that they do with regard to sanctions, as opposed to under the pre-existing EU rules.

That is one example. There are many other concepts and restrictions where the rules are similar, but there are differences that in particular factual circumstances could result in different outcomes.

Claudia Webbe: That is a very interesting example. It gives food for thought on how the UK looks at supply chains, which I guess you are

talking about in a way, and who is connected to whom in that respect. Would you say that there are any outstanding issues or unexpected difficulties?

David Lorello: The difficulties that are surfacing thus far are in the vein of the comments that I have already made, in the sense that companies that are subject to UK sanctions are now having to consider in a very different way questions such as, "Am I engaged in brokering in this particular context?" and, "Do I need to redo due diligence on this Russian counterparty that I did due diligence on under the EU framework?"

What I will say is that the practical difficulty that some companies are experiencing is that they have had some trouble finding guidance, in particular from HM Treasury, although the ECJU also plays a role in licensing certain sanctions matters. It might be useful for both HM Treasury and the ECJU to think about the extent to which they have adopted different standards around the edges of these sanctions regulations and whether they did so with a substantive intention to alter or expand the scope of the prohibitions, and to perhaps issue some guidance that makes clear, "We took a different definition of brokering from the EU. This is why we did it, and these are the things you should be thinking about."

I know that that is hard to do and it requires a lot of consultation, and I don't think guidance from Government is the answer to every question in the trade controls area, but that is one area where additional guidance could be useful. It would be valuable if the Government were to pursue that type of guidance and to have some consultation with industry, because companies are asking a lot of questions, and I am seeing many companies asking the same questions over and over again. It would be useful to have a dialogue with the Government, not to feed the answers to them, but at least so they are aware of the questions and can think about them to the extent that they wish to formulate any guidance along those lines.

Q143 **Claudia Webbe:** Clara, from your perspective, do you see any outstanding issues or unexpected difficulties in terms of the impact of Brexit on UK and EU sanctions policies?

Dr Portela: Thank you for your question. I don't foresee any difficulty—quite the contrary. What I tried to explain earlier was that there are powerful incentives for both parties to continue co-ordinating, even after the UK has stopped being a member of the Council, precisely because, with the general weakening of multilateral sanctions policies, there is now a general desire on the side of the US and the closest allies of the US to put in place restrictions that put pressure on specific targets that can no longer be targeted by the UN Security Council, precisely because the patterns of operation among the big five are weakening.

I don't actually see benefits associated with the EU and the UK going along different paths. I am tracing more benefits in convergence. I think that this is also going to happen naturally, precisely because there is going to

be a number of incentives coming from the North Americans and other members of the group of like-minded countries. The fact that we are now witnessing the trend towards the adoption of Magnitsky-type or human rights sanctions regimes in all those countries is symptomatic that that is already going on.

Q144 **Claudia Webbe:** Presumably, with those types of targeted, focused sanctions, if the EU applied such sanctions, the UK could choose to opt in or opt out. Do you see those kinds of issues or difficulties outstanding in relation to the EU-UK relationship?

Dr Portela: Not at all, because when the UK was a member of the EU, the UK was taking the initiative on most cases. I foresee more difficulty in getting the continental Europeans to follow sanctions in this, rather than the other way round. I can actually foresee very few scenarios, if any, in which the UK chooses not to impose sanctions when the EU does. I actually see that it is going to be rather the other way round—the UK imposing sanctions, often in partnership with the US and probably also Canada, and the EU dragging its feet because there are multiple actors, diversity of interests, and some members might try to water down the sanctions package, or it might take longer to negotiate, because obviously it is a multilateral setting.

I anticipate the UK will be more in the role of contributing to an effort to persuade Brussels to participate in sanctions efforts. Even though the UK is going to be fully autonomous in deciding whether to impose sanctions and which sanctions to impose, there actually seems to be little incentive to do so.

If I still have 20 seconds, there is still something that I would like to point out. That is the fact that the denials information, if I am correctly informed, in the decisions on the denials of licences to export arms to third countries, there is a mechanism within the EU in which member states, when authoring this, inform others in the Commission about decisions to deny an export licence of weapons to any third country. This is an important mechanism because it creates pressure on other member states not to authorise the same request. There is a dimension of social control—say, of prestige—without creating an automatic obligation to deny any request that has been received by any other member state and that has obtained a negative response. At least being informed of who is trying to procure what, and what has not been authorised by other member states, is something that was actually very useful in ensuring some consistency among member states, even in the absence of an obligation.

Now we no longer have this mechanism with the UK. If the UK denies an authorisation to export weapons to a third country, the Commission and the members of the EU are not automatically informed, and the other way around. Perhaps putting in place something that allows for the sharing of certain information would be useful, precisely in order to foster transparency and convergence and to prevent situations in which third parties benefit from discrepancies, or even accentuate such discrepancies, when it comes to the authorisation of weapons exports.

Q145 **Claudia Webbe:** Thank you. That is very useful. Maybe I could just follow up with David on that point. Has the UK lost any access to information sharing on sanction breaches due to Brexit?

David Lorello: It ostensibly has, just by virtue of how those information-sharing mechanisms are constructed. There would need to be an arrangement between the UK and the EU to reconstitute those types of mechanisms. I see no reason why that would be particularly problematic. There could be information sharing with regard to the issue of licence denials, which I agree is a flow of communication that is important and would benefit, frankly, both the EU and the UK in fundamental ways.

There could also be information sharing between the UK and the EU with regard to enforcement. That could be done informally. It could be done through the creation of structures that do not yet exist, or potentially through mutual legal assistance arrangements. It seems obvious, at least from an outside perspective, that it is beneficial to have those frameworks in place. I think in at least some instances it is true that they will not exist unless affirmative action is taken, both by the EU and the UK, to create them.

Q146 **Chris Law:** Clara, do you see possible divergence between UK and EU sanctions reducing the effectiveness of sanctions? Also, can you tell me if there are any particular areas in specific countries where you think that divergence is likely to occur?

Dr Portela: Thank you for the question. I definitely see that having a situation where UK and EU sanctions increasingly diverge is going to weaken their effectiveness, both in terms of the impact that the measures will have on the specific targets and in terms of the force of the message that they deliver. What I was trying to depict earlier, when I was talking about the broader coalition of like-minded countries, is that it does not even suffice if the EU is united in imposing sanctions against a third party. The message has much more force if you also have the UK on board and Canada and the US, and even some partners elsewhere. It is already quite an effort to get the entire collection of EU member states to agree on a sanctions package, but actually the trend is going to be to try to get other actors involved.

Particularly, if we look at financial sanctions or sanctions that have to do with trade and finance and not simply the visa bans that are so often imposed, isolating a target from access to the western markets can have major consequences. So in terms of impact and effectiveness, it makes a big difference whether you are excluded only from the EU market, the Japanese market, or the Canadian market, or if you are excluded, basically, from the west. Then, the options that are left to the target are very limited. From their point of view, there are plenty of reasons and plenty of incentives, or plenty of reasons to believe why the UK and the EU are going to continue to converge and establish co-operation among themselves.

There is very little to gain from having an independent sanctions policy that is not aligned with anybody else's. That simply creates an incentive for the targets, or basically for the non-targets, to trade with you when they cannot trade with anybody else, and that is not good for the reputation of any seller country. Or when you are imposing the sanctions or stopping trade or imposing restrictions and others are not following suit, then you are simply giving the target an incentive to trade with the others.

So, in terms of sanctions policy, the bigger the coalition, the more countries on board, the better. It also enhances the legitimacy of the measures. It enhances effectiveness and it enhances legitimacy. It's basically a win-win situation. It is also the preference of companies that they are not allowed to operate with a third country, with a target, and that nobody else is allowed to do so among the competitors. It is really the win-win situation. So even though there is now going to be full independence when it comes to sanctions decisions, in reality the incentive is to do exactly the contrary: try to converge as much as possible.

Q147 **Chris Law:** I suppose the flip side to that is that it can also be an opportunity for the UK to establish a more effective sanctions regime. David, I wonder whether, as a result of Brexit, there is an opportunity to do that unilaterally without waiting for unanimity from EU states and to align itself with non-EU country's sanctions, such as the US. Is that possible?

David Lorello: It is clearly possible as a function of the UK's departure from the EU. Under the EU framework, if the UK, for example, chose to go in the direction toward the United States on unilateral US sanctions issues, such as US-Iran sanctions, there would have been significant impediments to the UK doing so as part of the EU framework. The same would be true with regard to other emerging sanctions.

I would echo the observation that if the last 15 years of sanctions has taught us much, one thing it has taught us is that multilateral sanctions tend to be more effective than unilateral sanctions. It is widely acknowledged that the joint approach on the part of the United States and the EU, including the UK, toward Iran from 2010 to 2012 was instructive in fostering dialogue with Iran over its nuclear programme. I think it is generally understood and accepted that the joint US and EU approach toward Russia in 2014 did inhibit, to some extent, the actions on the part of the Russian Government in Ukraine. The notion of multilateral approaches to sanctions where the foreign policy stars are aligned between the UK and the EU and others is a principle that has borne itself out in recent sanction policy matters.

Q148 **Chair:** I have one last question for you all but, Clara, why don't we start with you on this? The character of conflict is changing and evolving, particularly with more technology, and I guess even to the point at which software will be quite an important element of conflict. Do you think there is going to be a need for a wholesale revision of export controls and sanctions policies, up to and including new international agreements? How do you think things are going to change in future?

Dr Portela: This is a good question, but I think that it cannot be answered easily. We first have to see what is going to happen with the global arms control export regimes, so I do not think this is something that the EU or the UK will decide single-handedly. We are not sure what is going to happen with these broader regimes.

As far as the EU is concerned, what we are clearly seeing in the adoption of sanctions over the past five years is that the standard arms embargos will also include a prohibition on the delivery of new and used items. Those are increasingly complemented with bans on surveillance equipment, so this has become standard. It used to be completely absent, and now it has been included in every sanctions regime, particularly when it comes to internal repression: there is a specific measure which covers items that can be used for internal repression. This has come to always include surveillance equipment—telecommunications equipment that can be used for surveillance.

This happens to also be one of the most important novelties about the EU's regulation: the fact that these telecommunications items have now been clearly anchored as dual-use goods. This seems to indicate that this is also going to be taken more seriously in the informational, informal technology export control frameworks. In technology export controls, we might actually witness a movement towards increasing regulation at a broader level. I think that is actually quite likely to happen, now that you mention it.

Fenella McGerty: The Institute did some work on this last year, and technology developments and changing innovation patterns do challenge the notion of who needs to be sat around the arms control table and how to bring them together. The traditional arms control community was primarily made up of state and non-state organisations that were primarily focused on defence, but now technologies of concern are stemming from beyond the defence industrial domain, so that military application is not the primary driver of R&D any more; it is the spill-over from commercial technologies, and they have those applications and implications for weapons that are blurring that civil-military divide.

That then changes who needs to be in the discussions. With AI and the emergence of private space launch sectors, neither are primarily focused on military applications, but they do have far-reaching implications for defence and security. The fact that they pose challenges for arms control and, by extension, the control of exports means that those respective sectors need to be engaged earlier. The amount of civil R&D in these technology sectors, and the fact that there is dual use of many of those technologies, means that the effective future arms control architecture has to reach beyond that traditional group of stakeholders.

Q149 **Chair:** That is fantastic. David, in your work you have to analyse some of these agreements in great detail. Are they fit for purpose? Can you give us an idea of how they can be modified to take into account some of those changing dynamics?

David Lorello: The need for regulators to be swift in considering emerging technologies is clearly going to be a crucial issue. If you look at the United States, for example, it has had a very significant initiative towards understanding which emerging technology should be targeted for export controls purposes. Over time, we will see technologies in relation to artificial intelligence, robotics, 3D printing and other emerging areas. I think Fenella is quite right that it is probably not going to be just the defence sector, but increasingly other sectors that will be relevant to those purposes.

The underlying trade controls instruments are more or less sufficient to deal with those issues. It is really more a function of co-ordination between the UK and the United States and between the UK and the EU, because if there is one thing that is clear with regard to controlling those types of technologies, it is that this is an area where multilateral controls again really become crucial. It does not make a lot of sense for there to be splintered approaches on artificial intelligence, for example, with the UK having one standard and other countries having others, because that will reduce the effectiveness of the overall system.

In my judgment, it is less a function of revising the multilateral arrangements as such and more a function of being proactive in the dialogue that leads to changes—for example, the Wassenaar arrangement and other multilateral arrangements.

Chair: Fantastic. That was a very helpful answer. I thank our witnesses, Fenella, David and Clara, for their time—we have gone about 17 minutes over time. I also thank my colleagues from the other Select Committees, who make up this Committee on Arms Export Controls. We are very grateful to all of you for your time.