



Select Committee on the European Union

Goods Sub-Committee

Corrected oral evidence: Beyond tariffs: facilitating UK-EU trade in manufactured goods

Monday 8 June 2020

10.40 am

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

Evidence Session No. 1

Virtual Proceeding

Questions 1 - 10

Witnesses

I: Allie Renison, Head of EU and Trade Policy, Institute of Directors; David Henig, Director, UK Trade Policy Project, European Centre for International Political Economy; Dmitry Grozoubinski, Lead Trainer, ExplainTrade, and Visiting Professor, School of Law, University of Strathclyde.

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Examination of witnesses

Allie Renison, David Henig and Dmitry Grozoubinski.

Q1 The Chair: Thank you very much for joining us. The session will not be broadcast, but there will be a transcript because it is a public session. May I ask each of you to briefly introduce yourselves? We will then go on to the questions that you have had prior notice of. Supplementaries will be added as the session progresses.

Allie Renison: Thank you very much to the House of Lords and the members of the Committee for having us. I head up EU and Trade Policy at the Institute of Directors. That is obviously an increasingly overlapping brief. Prior to that my brief focused on those two separately, but there is a lot of overlap at the moment. We are now trying to push attention foursquare on what business needs to do to prepare for whenever the changes are due to come. I look forward to your questions.

David Henig: Good morning, everybody. I head up the UK Trade Policy Project at the think tank the European Centre for International Political Economy. I have been doing that since March 2018 looking at potential future trade policy. I also look at trade policy globally in terms of big issues such as the US and China. I look forward to answering some questions later.

Dmitry Grozoubinski: It is a pleasure to be here. I run ExplainTrade, which is a consultancy. Prior to that, I was an Australian trade negotiator for a number of years. Probably most relevant to this session is my current work in training negotiators and policymakers for the UK Government and the devolved Administrations, private companies and so on.

Q2 The Chair: Thank you very much and thank you for being brief. The first question is to all three of you. How significant are the non-tariff barriers as a potential obstacle to UK-EU trade in manufactured goods?

Allie Renison: A lot rides on understanding what the impact will be and how disruptive the end of transition will be. That is the one thing that unites every business on this scale, whether they are trading with the EU or not. From the perspective of a chemicals company, regardless of whether it trades with the EU—and in that sector almost every business from small to large trades internationally and with the EU—there needs to be a change to the regulatory competence.

The argument is that REACH, the regulation that governs chemicals if you are part of the single market, will have to be replaced by a UK REACH. Understanding exactly how that will look is an example of what businesses are most worried about, in gauging what the impact will be. For most businesses I speak to, the impact is fundamentally linked to having enough information in advance to adapt to those changes.

David Henig: The measurement of non-tariff barriers and their reduction in trade deals is surprisingly under-researched. We do not know as much

as we would like to know about this. The sector-specific point that Allie makes is right: the barriers are often sector by sector—these regulations are often specific to sectors. There are overall frameworks in place for regulation, such as the way the EU tests for many products, but for chemicals or high-risk products it will have different regulations. This is a complicated picture. Therefore, it would be an inaccurate generalisation to say outright, “It’s this figure”.

We know that some research has said that non-tariff measures can cost, on average, three times more than average tariffs. They can easily add 10% to 20% to costs. Some would put it higher. Very few researchers have put it lower. We know that World Trade Organization rules help little with non-tariff barriers but, equally, the free trade agreements have only just started to tackle them. We have yet to get a really comprehensive free trade agreement that tackles lots of non-tariff barriers where we can see the figures and prove that this works.

Finally, in global trade, there is a differential impact on businesses of different sizes. Large businesses have people whose specialism is overcoming non-tariff barriers in different geographies. Small and medium-sized businesses cannot afford to do that. Anecdotally, we know that, around the world, many businesses do not even try to overcome these barriers where they occur. They just go for easier trade. Therefore, that should be a concern as well. That would be my introductory statement on this.

Dmitry Grozoubski: I do not have a huge amount to add. The only thing I would float for your consideration is that the UK effectively finds itself in open competition for investment and production with the region and, to an extent, the world. There is a question of how much disruption there will be in the week after transition. It is hard to imagine there not being some, and that is problematic and something for you to be aware of.

There is another, far larger, question. A non-tariff barrier does not have to be huge or fatal to make a business consideration change from a factory in Bristol to a factory outside Paris. Often, these fairly minor changes will add up to steer investment, growth and potential export opportunities away from the UK and towards what will be a very large and integrated neighbouring market. The numbers may not tell you the full impact story.

Allie Renison: While, on the one hand, it is helpful to talk in a wider context about the impact of non-tariff barriers, you really have to focus on the Brexit context, for lack of a better term, because it is just so unlike anything else.

In terms of understanding the compliance change requirements that will presumably be imposed on business, it is hard to know for sure. When we talk about alignment and divergence, there are two things to consider from a non-tariff perspective. There is whether you want to align or not align for its own sake, which is relevant in some sectors such as

chemicals. Many businesses in that sector want to align on top of having the market access continuity that comes from being part of REACH, for example, or having mutual recognition with REACH. Many people do not want to duplicate those non-tariff barriers in that setting.

In other settings, though, it is about whether the market access is the most important point or whether it can be obtained through other means. For example, in the Government's opening negotiating text, there is a lot of discussion about equivalence and recognition of non-tariff barriers, be they on SPS—sanitary and phytosanitary standards—that deal predominantly with agri-food, or be they technical barriers to trade. Looking at it from that perspective, if the Government could secure an approach on equivalence for sanitary standards, for example, that would get many businesses the market access that they want. But we do not know that at this point.

If you are a business looking at how to prepare in the agri-food space, it is almost irrelevant at this point what you get out of that. In the absence of being in step with the EU on SPS rules, the assumption has to be, and is for many businesses, that you automatically get a full panoply of third-country controls. That is what one would preferably be looking to work from in preparation.

Those third-country controls can be quite significant. At one point last year, before the UK received what is called third-country listing status in the EU, which should not have been that difficult to obtain, Michael Gove in his ministerial position said that, without that listing, all agri-food exports to the EU market would have just stopped entirely. That is an extreme example. Without wishing to be too sweeping about it, the consensus, inasmuch as there is one, is that tariffs can be unpredictable once they are in place, but businesses know, to some extent, what to plan for at the moment. The impact of non-tariff barriers is potentially greater but, once they are in place, they are less subject to change and unpredictability than the level of tariffs between the UK and EU.

Q3 The Chair: Has adequate consideration been given to this particular matter in the negotiations between the UK and the EU?

Allie Renison: I would go wider than that. The debate generally focuses too much on tariffs simply because they are the easiest quantitative means for understanding what the impact can be. People focus a lot on tariffs because it is easier to extrapolate a number, effectively. Non-tariff barriers are not the same for all sectors, even in a single market. In heavily regulated sectors such as pharmaceuticals or chemicals where you need to have—I cannot remember the exact terminology—a qualified entity on the other side, if we are not aligned and our standards are not deemed equivalent enough to allow for that market access to continue in any form, the upshot of non-tariff barriers, unlike with tariffs, is that many firms will feel that the easiest way of mitigating the impact of disruption is just to have a set-up in another country. The impact of non-tariff barriers is more likely to compel firms to do so, because they know that they may not get the automatic recognition of their certification.

Here in the UK, after these changes come in, as long as we know we are not making the commitment to align with single market rules in any form, we know there is a possibility for those third-country controls. In the absence of clarity on whether the EU will be minded to recognise our regulatory standards as equivalent, most companies in these highly regulated sectors are saying that, because of these non-tariff barriers, it is just easier to make sure that they have an entity set up in the EU already.

Some companies already have that, but many other companies do not. A lot of the legwork in those heavily regulated sectors has been done because of the potential no-deal scenarios over the last 12 months. The impact is greater in some respects because, given the business considerations Dmitry was speaking about, it ends up being easier to have that physical location in another country. That is not the same for every business; small businesses cannot do that. But a lot of that legwork has already been done by companies in heavily regulated sectors where that is a particularly big issue.

Q4 Lord Russell of Liverpool: I do not know whether anybody present has had a chance to look at it, but there is a very sobering and quite long piece in today's *Financial Times* called "Dover-Calais post-Brexit trade plagued by uncertainty". In the context of authorised economic operators, which is part of this question, that article points out that only a little over 1,000 of the estimated 150,000 UK businesses completing customs formalities for the first time after Brexit have AEO status.

Mr Frost, our chief negotiator, often talks about other trade agreements the EU has done as a justification for the UK position. What lessons can be drawn from other trade agreements on how to reduce the impact of non-tariff barriers and facilitate the flow of goods across borders? Could you then talk about your view of the authorised economic operator status and the degree to which that should or could be important?

David Henig: I am afraid it is not a great picture. Free trade agreements have only really started to address non-tariff barriers in the last few years. It was supposed to be part of the TTIP¹ negotiations between the EU and the US, but they did not reach a conclusion. Non-tariff barriers do not, in fact, form a hugely significant part of the EU-Canada agreement. They were addressed to a degree in the EU-Japan agreement, but many of them were outside the agreement. The EU required Japan to remove a number of discriminatory regulations before even starting. We have very little to go on in terms of what should be considered in non-tariff barriers.

Normally in free trade agreements, you have some general language that says, "We should consider each other's regulations broadly equivalent and find ways to co-operate". In reality, this does not take us much further. In the EU-Canada agreement, as I think we will come to later, we have the mutual recognition of conformity assessments. These are the tests that must be done to show that regulations have been met, where

¹ The Transatlantic Trade and Investment Partnership

required. There is a cost saving if you can carry them out in your own market, but we do not know that it makes a huge difference to exporters as yet.

In terms of food and drinks exports, veterinary equivalence, which Allie mentioned earlier, makes a huge difference. We know that that is important. Again, what is in the free trade agreement is the tip of the iceberg. Often, that has to be agreed as part of an annexe or a separate agreement. The free trade agreement is setting the framework for all this. There is a huge amount of further work to be done. We have learned from this that the free trade agreement is just the start and is unlikely to solve all our issues.

In terms of what we should be asking for, which came up in the previous question, we need an agreement as a starting point, but it is far from the end point to addressing these questions. That is what I learned from looking globally. In fact, to be honest, globally they will be looking at the UK-EU agreement to see if we can find a way of taking forward non-tariff barriers. These have not really been fully addressed in trade agreements.

Dmitry Grozoubski: David is right in how he categorises what free trade agreements do on technical barriers to trade. They will establish some basic principles: do not use your technical barriers to trade explicitly to discriminate against us; do not introduce excessively high fees just to keep our goods out of your market; do not have very long processing times; be transparent about how you make regulations and test against regulations.

Some go a little further by listing in an annexe a table of equivalent laws or regulations. For example, the European Union and Canada would say, "This EU regulation on this particular hormone in beef is functionally equivalent to this Act of the Canadian Parliament. While both are in place, we will consider that this hormone is banned enough in both countries that we do not have to test one another's products for it". They go a little further, but it is not a hugely sweeping change.

To go back to the question about the Dover article in the *FT* and authorised economic operators, it is a real challenge. Dover has been built up and designed around the idea that the vast majority of the traffic that passes through it is effectively unscreened for anything except, for example, the immigration status of the drivers. To go from that to treating it as a third-country port is a massive escalation. So far, a lot of the ideas about how that will work are quite high level, conceptual and nebulous. They are an expression that everyone would like it to work better, but they require the Government to make decisions that they have not made yet and the two parties to reach agreement.

On the question of authorised economic operators, the best analogy I can come up with is when I visit the Houses of Parliament in the UK. There is often a very long queue at security screening to check that no one is carrying things they should not be carrying. Addressing the delay that you get at that checkpoint through AEO is like saying, "What if all visitors

to the Houses of Parliament had to join MI6? If you join MI6, you get a badge and you can go through”.

That is the equivalent of expecting companies to join the AEO. It works for very large companies that go through those checkpoints a lot and can undertake the very expensive three to six-month process² of being certified as fundamentally trustworthy and thus capable of receiving extra scrutiny. It is not something that you can just copy, paste and expect the overwhelming majority of transport companies and operators who use that port to take up. It is certainly a useful scheme and a scheme that, in time, it will make a lot of sense to expand and expand access to, but it is not a panacea in any way, shape or form for expanding Dover or coming up with ways to handle what will be a colossal caseload.

Allie Renison: Apologies, I was trying to search for something. I will send it to the Committee once I find it.

We have asked about this question explicitly. It was a few years ago, so I expect interest and awareness to be higher. When we asked about this AEO question, the number of companies in the goods trade that had never heard of it was striking. There is a three-pronged approach here. If Brexit increases the awareness of companies so that they realise why this is important for facilitating international trade generally, that is to be welcomed.

There is an important expectation management piece. Businesses that are not aware of what AEO is, what it does, the procedures for applying, what it offers and what it does not, are interested in it because they see it in the news. That is where most people hear about it. They sometimes see it presented as a panacea, and the perception is that it is a special ticket that means that you are never pulled aside. It definitely lowers your risk profile, but it does not mean that you will not get pulled aside for checks and controls. It is important to understand what it is there for.

I do not want to use the term “side agreement”, but the interesting thing about customs co-operation is that it is not simply within the preserve of the Commission. I would have to triple-check, but I am pretty sure it is at least a mixed competence. Much of the practice of customs co-operation is between the member states. Regardless of that, it is important that we have that if it is going to be part of any mutual recognition. The US and the EU have an MRA in AEO. I do not know to what extent it is relied on.

In terms of the story referenced by Lord Russell, we do not want just to look at the numbers and ask why more companies are not using it, because it is not for every company. I would have to go away and see whether the application procedure has been improved, but as of the last time we discussed this with logistics providers and small companies that were applying, the application times went way beyond three to six months; people were getting it back in 12 months.

² Post-meeting note provided by the witness: Allie Renison’s subsequent correction that the process is now taking far longer than three to six months is almost certainly correct.

That is why it is extremely important to have a balanced narrative on this. There is a reason why a lot of bigger companies tend to have it. It is essential for port operators to have it. It is important for companies that are directly involved in logistics and transport, particularly larger ones. The extent to which it will be useful depends on how much of the heavy lifting one is expecting AEO to do. It will not replace the need to make sure that you are fully compliant. It is important for companies to consider, but it is simply not for everyone.

Having said that, I do not think that people should discount its importance in this context. Understanding how much something like that can do depends on where we get to with the trade agreement, if I am honest. If we got to a point where there was lots of equivalence on regulatory standards, that might help to a certain extent. Norway, for example, is not part of the customs union and does not follow the EU's union customs code wholesale, but post 9/11, when lots of countries were bringing in increased security controls, Norway opted basically to adopt part of the EU's customs code, in order to exempt it from having to worry about safety and security declarations, and to comply with these new controls. In the absence of that, AEO might have had only a limited impact. Therefore, much of understanding what these technical facilitations can do depends on where you get to with the wider agreement first.

Q5 Lord Shipley: Can I ask about rules of origin now? How important is it that the UK and the EU come to an agreement on rules of origin? What explains the differences between the current positions of the two sides?

Dmitry Grozoubinski: If you do not get an agreement on rules of origin, you do not get a free trade agreement. If you are going to lower tariffs between two countries, you need to understand what constitutes a good that comes from either country. It is fundamental. If you are not going to charge a tariff on a European Union good, you need an agreement on rules of origin to determine what a European Union good is. Otherwise, how would you know whether to charge it a tariff? It is vital. There is no way around it; you need an agreement on this in order to move past it.

Rules of origin are not my speciality at all. I know that Dave and Allie have looked into this in more detail. I will defer to my colleagues on the differences in position.

Allie Renison: I will pick up on the relevance of it. As the awareness starts to increase among businesses, so too does the concern about what is needed and question marks over the extent to which a free trade agreement will be useful purely on the basis of rules of origin. I was speaking to one of our members in Northern Ireland before the creation of the protocol, which adds some complexity on top of what we are already talking about. He had done a lot of the legwork. He is in the agri-food space; he works in animal feed. The components of animal feed, such as wheat, come from different parts of the world. He had looked at this from his own business.

It is hard to know exactly where we are going to end up, apart from looking at the opening positions, which I may let David talk about so I can focus more on the business impact. In so far as you can prepare for rules of origin, the best thing, which most auto and agri-food companies are doing, is to look at the requirements for domestic content, such as a certain amount of it being assembled in-country or in various participant countries. Effectively, he said, "You suddenly realise that a free trade agreement is not so free after all, because of the requirements behind it".

It is worth noting that NAFTA, the North American Free Trade Agreement, between Canada, Mexico and the US, has now been renegotiated at the US's behest to try to approach rules of origin in a way that forces more domestic onshoring. At least that is the way people hope to use them. That is usually the intention behind them: to make sure that third-country goods or components are not going into the EU or the UK that are not entitled to have that tariff reduction or tariff preference.

Going back to the AEO question, it is important to realise that, when we talk about customs facilitation and the actual paperwork companies have to do, they do not always speak to the same issue. AEO will be relevant to the movement of goods, but it will not, as was sometimes put about in the media previously, help businesses with rules of origin. There was a lot of discussion last year about avoiding the need for rules of origin checks, but apart from in the context of the Irish land border discussion, checks are not really the issues for business; it is all about the increase in paperwork.

If the tariffs are significant going into the EU or, as an EU business, going into the UK, you will probably see the need to avoid them. However, if the tariff is 2% or 3%, businesses will think about how much they have to uproot their supply chain to fulfil the content requirements based on an EU rule of origin in another trade agreement, which may not be what we agree to as the UK. A lot of people may not want to do that and may end up just paying the tariff. You can argue that that is a business decision but, at the end of the day, rules of origin are probably the biggest part of the text of a trade agreement if we get there, because that is what the negotiators tend to pore over.

From a business impact perspective, it is really important to make this a focus of the negotiation. On customs and tariff, they are the biggest imposition of additional requirements that businesses are not used to. Unlike the NAFTA countries, they are not used to dealing with rules of origin every day for trade with the EU. Companies trading outside the EU are not used to dealing with this either, because the take-up of trade agreements can be so low among businesses, although they are particularly used by the auto sector.

Going back to AEO, customs facilitation and how to prepare, smaller businesses are much further ahead in their ability to manage these things, but many larger companies have concerns about awareness and understanding of non-tariff barriers or rules of origin among companies in the supply chain.

Ultimately, from a business impact perspective, a trade agreement could be negotiated with such complex rules that the businesses do not use them and end up paying the tariffs. From a tariff perspective, that effectively puts you in the same situation as having no deal.

David Henig: Starting with the basics, at the moment the UK can import anything into the UK, construct it into a final product and export it to anywhere in the EU with no issues, no paperwork and no rules of origin. We are talking about the fact that in the future that simply does not apply. For anything made in the UK, it matters where the inputs come from. Under the WTO tariff, it does not matter, but in a preferential arrangement—we sometimes lose sight of the fact that that is what we are negotiating with the EU—it does.

In terms of how the EU handles this, it has two basic models. With the neighbourhood, which is pretty much every country in the region including EU members and non-members, there is something called the pan-Euro-Mediterranean Convention on rules of origin (the PEM Convention). As long as the products have been sourced from within that region, they can be counted towards whatever the percentage may be. To get a reduced tariff on a car, for example, 50% or 60% of its content must have come from one country. The PEM Convention allows that to be sourced anywhere within the region. That is one approach. The more typical approach is simple bilateral cumulation whereby the UK and the EU can count each other's inputs into our trade agreement but not those from anywhere else.

Both of those give certain industries problems. This is where the detail comes in. I would recommend a study carried out for the food and drink industry in 2018, which shows that, under either the rules of origin that were part of CETA or the PEM, certain types of food and drink would not be eligible for a reduced tariff if we were to agree it. Rules of origin are complex. They may hit individual exports and we may find that they are no longer economic to do.

In the negotiations, the UK has come in with quite an ambitious ask. We have asked for what is known as diagonal cumulation, which is the heart of PEM, except that we have not asked for PEM. We have said that, where the UK and the EU have agreements with third countries, we should be allowed to diagonally cumulate with them as well. If we both have agreements with Japan, for example, EU and UK produce would be allowed to contribute to a preferential export to Japan. Similarly, Japanese, UK and EU content could be counted towards an export to the EU. That is very ambitious, and we would not have seen such a sweeping clause in any free trade agreement before. As I understand it, the EU has pretty much all but rejected this approach, saying that it is completely unprecedented, wildly ambitious and not in its interests.

There are big differences between the UK and the EU. Just like the non-tariff barriers, this will hit individual businesses and individual sectors. I am afraid there is no real alternative but to go through it individually, line by line, as to what makes sense for UK business. I fear, with the

timescale we are operating to in this trade agreement, that this is the kind of detail we forget when we say we can do a trade agreement in eight months. Sure, we can agree to have no tariffs in eight months. Whether we can have an agreement that benefits the maximum possible number of UK businesses in eight months, I have my doubts.

Allie Renison: I should make the caveat to the Committee that we are surveying members as we speak to see in the wake of coronavirus if any preferences and priorities have changed in the flexibility versus market access dynamic. We asked this question earlier this year. This is why in the past we have said that the Government should consider aligning at least part of their import tariffs, if they could find a way to avoid rules of origin, in particular but not just for manufacturing, because of the significant number of component parts. We asked that in January and I thought I would briefly summarise for the Committee, with the caveat that we are asking this again.

Some 32% of IOD³ members said that the UK should align all EU import tariffs to avoid rules of origin; 34% said that it should align in part; and 20% said that it should have full flexibility. At that time, two-thirds of members wanted some kind of alignment, if possible—we do not know at this point, because we are not going for the arrangement of having any alignment—to avoid rules of origin. We never discussed whether that was even possible, but I suppose it is redundant because we have now decided that we are going to go for the rules of origin approach. As David said, it is really important to make sure that we have that detail ahead of time.

Q6 Lord Inglewood: David Henig just slightly shot my fox, but you have described a number of approaches to rules of origin. Setting the politics to one side, from a UK commercial perspective which direction of travel should we go in? Should we accede to the PEM Convention or look at it in a different way?

Allie Renison: It depends on the sector, effectively. The Japanese Government wrote a position paper after the referendum, post the Lancaster House speech, setting out their priorities. They were very clear that they wanted to go for diagonal cumulation, given the proliferation of auto parts around the world. PEM may be particularly relevant for textiles and less so for others. It is sector-specific. I cannot give you a firm answer either way at this point across the whole of industry.

David Henig: I should be honest: not enough work has been done by anybody on what our approach should be. This is where I feel we have not had the information from government. To be fair, researchers like me have not always had the time to say, "Let us go through the PEM or what has happened with Canada. How will it affect our individual businesses and sectors? How might they be affected by non-tariff barriers?"

For example, we could spend lots of negotiating capital making sure that we had exactly the right rules for cars, only to find there were so many non-tariff barriers that we could not make cars profitably in the future anyway. I am assuming that food and drink should be a priority, because we have a thriving food and drink manufacturing sector, but we need to look at this in more detail. We cannot do it in five minutes this morning. Sorry if that was not quite the full answer you were looking for.

I am not sure exactly how the PEM Convention numbers are set, but I am sure the EU has a strong influence. I am not sure whether, having just left, we wish to go straight back into that, either politically or commercially.

Allie Renison: From a commercial perspective, until the change in Government last year, all that industry was working to was the proposal for either a facilitated customs arrangement or a new customs partnership. Either way, the aim of the previous Government was to focus not so much on avoiding rules of origin writ large but on avoiding their impact. That is what most of industry was working to. There was no focus on figuring out the best model to use from a rules of origin perspective.

Industry has suddenly had to shift its thinking on what it is trying to contribute to. That is important context. The approach to rules of origin and whether they were an inevitable part of our relationship with the EU was completely different up to the end of last summer.

Lord Inglewood: Am I right in understanding you to say that, whatever we do, there will be some winners and some losers?

Allie Renison: Yes. We have not seen this from our own auto industry, which speaks to how much of the focus and priority in these negotiations has been on continuity and protection of trade. There is an argument, increasingly made in some parts of North America of late, for using rules of origin to try to build up domestic industry. That is a mistaken approach, particularly when you have had that kind of trade integration, whether it is US integration into North American markets or UK integration into European markets. I see no evidence that the Government are trying to push this narrative, but it is a potential consideration.

This is sometimes the EU's approach: to have tough rules, depending on how you define "tough", or fair enough rules, as some people call it, to make sure you keep your own industry built up. Competition over market share will be significantly heightened in the wake of coronavirus. Rules of origin will probably be one area of the negotiations where you have competing interests in Europe. Some industries will want to see rules of origin used, not necessarily to protect trade with the UK but to help, in their minds, to build up domestic industry. I think that is a flawed approach. Once you have had that trade integration, using rules of origin to force manufacturing back to your domestic market is not as straightforward as if you did not have that integration to begin with.

The US Government tried to use rules of origin to increase the content requirements of auto domestic components and domestic manufacturing under NAFTA. It was interesting to note that the auto industry was not necessarily on the same page. It saw this as creating more trade disruption rather than being, on balance, a net benefit to build up domestic industry.

- Q7 **Lord Lamont of Lerwick:** To keep this brief, perhaps I could address this question simply to Mr Henig. You were talking about how difficult it was and how certain questions could not be answered. Does that mean that you cannot give any quantification of the effects of rules of origin as a percentage of transaction costs? One has seen many figures in the past, and it struck me that Switzerland had a very low transactional cost for rules of origin, much below what most trade experts felt was the real cost. Do you think these figures are invalid?

David Henig: There are a number of different figures and, yes, you can provide a quantification. I am saying that I do not think anybody has, as yet, provided a quantification as to how the UK will be affected by different potential schemes for rules of origin. The second form of figures you can have is the utilisation rate for rules of origin, which depends on how it is designed. There are many figures out there for that. You were possibly talking, again, about a slightly different one for Switzerland and the coverage of different types of rules of origin. There are very valid numbers out there. I am just suggesting that we have not yet produced all those numbers for the UK. We hardly have any, so far.

- Q8 **Lord Faulkner of Worcester:** Conformity assessments seem to be a difficult area in the negotiations between Mr Barnier and Mr Frost. Why do you think the EU is refusing at present to accept conformity assessments that are essentially similar to ones they have already agreed to in discussions with other third countries and as part of other free trade agreements?

Dmitry Grozoubski: I am sure there is an element of tactics to it, but it is important to understand what these kinds of conformity assessment commitments in a free trade agreement are. You are essentially saying that the two sides would legally commit themselves to accepting certification by laboratories or third-party bodies in the other country for the duration of the free trade agreement. It is a restriction of policy space. It is essentially binding the hands of legislators like you on both sides of the English Channel, and it is about binding the hands of regulators. The approach especially of the UK in this free trade agreement has been to keep it minimal, to keep it as simple as possible, and to give up as little autonomy or policy space as possible. In a way, you can interpret the EU as simply mirroring that.

There is also a darker side to it. As an inevitable consequence of Brexit, the EU in its decision-making no longer has to consider the interests of the United Kingdom. In considering its policies, its new obligation is to look at the interests of 27 members, to attract investment and business, and to see what works best for them. One way you can interpret the EU's

position as saying is, "We don't know to what extent we'll want to use the levers of regulatory policy to lure business and investment to the 27, either from the UK or coming in afresh to go in one of two directions. We want to reserve the right, from a purely commercial or mercantilist perspective, to make things a little harder for British-based businesses in Europe, to incentivise investment in the EU 27".

They might also be saying, "We don't know in what direction UK policy will go. We don't know what its enforcement regimes will be. We don't want, at this early stage, with a new independent UK exploring all sorts of new avenues, to commit carte blanche to accepting its conformity assessments in perpetuity through this legally binding document". Just because they do not agree to accept a conformity assessment in a trade agreement in perpetuity, it does not mean that on a regulatory level, especially initially after transition, they would not do so. They may, either initially or in time, agree to accept UK conformity assessments in certain areas, but they are not signing away their ability to do so.

Lord Faulkner of Worcester: Yet the EU has agreed to conformity assessments with Canada, Australia, New Zealand and the United States.

Dmitry Grozoubski: Those agreements are fairly specific in that they have taken a number of sectors and, within those sectors, product types. Almost down to the individual regulation, they have said, "On this one, we'll accept third-party conformity assessments. We'll allow an Australian lab to test against the EU's standard in this area but perhaps not this other area".

They have done that through a negotiation. That would have been part of the overall balance of those two deals. It would be an offensive interest for Canada, for example, and a defensive interest for the EU. They would have traded it for something or they would have looked at their industry. But the UK is being reborn as an independent trading nation in a way that Canada was not at the time CETA was negotiated, for example. Canada was a much more known regulatory player than the UK, which is still deciding what kind of trading and regulatory nation it wants to be now that it is in full control of its destiny. That might motivate some of the discrepancy, in addition to good old-fashioned negotiating tactics and perhaps a bit of protectionism.

Lord Faulkner of Worcester: I will finish by reminding you of what you said at the beginning, which is that in your view it was a negotiating tactic. In that case, it should not be a deal-breaker on its own, should it?

Dmitry Grozoubski: That would be up to the UK negotiator. Almost everything in this negotiation, including the incredibly thorny issues, should not be a deal-breaker in and of itself. Both sides, and especially the commentariat, have often turned issues totemic when, in fact, they are distinct, have a distinct commercial impact, and should be considered as a balance of trade-offs. If the deal makes sense, it should still make sense even if they are in there. That is my opinion as an outside technical observer who does not have to go to the ballot box.

Q9 **Baroness Chalker of Wallasey:** What other forms of regulatory co-operation might be agreed to reduce the impact of non-tariff barriers in general?

David Henig: We would expect to see UK regulators talking to their EU counterparts. That is the most basic form of regulatory co-operation such that, when they are considering regulatory changes, they know what each other is doing and can, where it makes sense, mirror each other and therefore reduce the divergence. There are many forms of regulatory co-operation. These have been catalogued quite extensively by the OECD in Paris. Many of them are as informal as that. You can have more formal arrangements where, if you are both regulating in the same areas, you may choose to find ways to do this in common.

Interestingly enough, I do not think the UK has put forward any great suggestions of regulatory co-operation. The EU has put forward an idea that either side should be able to discuss, on request of the other, some individual area of regulatory co-operation. This is generally fine as an idea. There is no great evidence yet that it reduces the costs for individual businesses trading, but it is all part of constructing a new form of relationship and should therefore be encouraged.

All these things take time to negotiate, and we do not have much time left to negotiate. None of this is a given. The EU does not automatically negotiate its regulations on demand with anybody who wants it to, and we would not necessarily want to either.

There is a recently introduced notion in trade agreements called good regulatory practice, whereby both sides sign up for example to producing information in advance on what regulatory changes are planned, and making sure that there are impact assessments and all the things that we traditionally emphasised in the UK in terms of better regulation. But it is quite interesting that those could be turned into a treaty commitment.

With respect to what Dmitry said earlier about how much legislators want their rights to be fettered by international treaties, I find it interesting that that has not been the subject of much discussion yet. There is an awful lot of detail in these trade agreements that really needs to be examined, as much on the regulatory side as any other.

Back to my first point, it is not clear that any of this will definitively reduce the costs of regulation to Allie's members. These are co-operations and we do not really know where they take us.

Baroness Chalker of Wallasey: It is all as clear as mud, because people are not actually getting down to the basics of discussing these individual items.

Q10 **Lord Turnbull:** In the single market, there are a whole host of regulations: flammability of textiles, brightness of lightbulbs, insulation of appliances and so on. We do not regard these as barriers to trade but rather as promoting trade. When we leave, all this gets turned on its head and regulators are seen as a source of barriers. To what extent can

the UK cut through this by certain sectors simply recognising the rulebook, the EU standards, and working with those?

Allie Renison: The best person to answer this is someone from the EU. The question is very interesting and relevant, because in a way it ties back to the previous one. We cannot look at these negotiations as the be-all and end-all. It is important to stress that, as recently as last November and December, after the election when the direction of travel was clear, we are asking businesses, reflecting on the last few years, what was more important to them—substance or speed.

The clear majority, to my surprise, given how much toing and froing there had been over the last three or four years, was that substance was most important. Even if most businesses we speak to would prefer that we get everything into this agreement so that it is all in one fell swoop rather than lots of changes at different points in time, they understand that it has to be a dynamic process. How we co-operate with the EU going forward will be a dynamic process and should be a focus of attention, even if the transition period ends at the end of this year.

Answering the question, it is hard to say from a legal perspective. The presumption, which is the EU's point of view but would be shared worldwide, is that if there is no direct commitment to make that alignment, recognition or co-operation, you will not have that continued access. Governments are constantly co-operating and making small changes to facilitate access all the time. We are doing it in reverse. We could finish the negotiations this year and then spend the next 10 to 20 years negotiating our way back into that access by way of co-operation. Is the point to do it all in one go or to continue? The best answer has to be from the Commission. I do not know what legal basis will allow it, in the absence of an agreement, to say, "Based on your standards, we'll give you this access".

David Henig: There is definitely an argument for unilaterally recognising others' standards and regulations. I am not sure the public will welcome it if, thinking that we are leaving the EU to set our own regulations, we then say, "We'll allow everybody's goods in from certain countries". From a trade point of view, it makes a lot of sense to recognise each other's regulations, but not necessarily from a political point of view. There are an awful lot of political questions behind this regulation. What is more likely to happen, as Allie suggested, is that we spend 20 years talking about the different regulations.

In goods, I can see very little reason, by and large, to move away from EU regulations in areas such as cars and aircraft. Why do we want our own regulations for cars and aircraft? We are a services economy and I can see a much stronger case there. In goods, the EU is our main market and, globally, the main regulator. There is a very strong case. We should certainly be scrutinising very carefully any suggestion of moving away from EU regulations on goods.

Lord Turnbull: Allie referred to coming out and then spending 20 years

negotiating access back. Can we reverse the process so that we largely stay in and spend 20 years negotiating how far we want to come out? It would be much less disruptive in the short term.

Dmitry Grozoubski: I am mindful that one member of the Committee mentioned that we were not starting with the basics, so I might just start there.

On the issue of recognising the EU's regulations, for a business there are basically two questions. First, what does a lightbulb have to be in order to get into the European Union? Secondly, what evidence does the European Union need when that lightbulb arrives at the border to wave it on through and say, "Yes, this lightbulb is safe for a French socket"? Recognising the EU's standards, in a way, solves the first problem. It basically says to UK businesses, "EU lightbulbs are safe here", and encourages them to produce lightbulbs to the EU standard. To maintain that is fine.

However, just recognising their standards comes with no guarantee that the EU, when that lightbulb arrives at the border, will say, "We just automatically accept, because you said that you have our same standard, that it's safe for us". That is where a lot of this friction comes in. It is the burden of proof which the EU will seek from the UK, because UK regulators will no longer be under this umbrella purview of the European Union and the UK will no longer be subject to the jurisdiction of the ECJ. They will have a higher threshold for proof that the UK is indeed living up to their standards, which is where this friction comes from.

As to Lord Turnbull's question about whether it is possible to reverse the process, at this point essentially it is not. At this point, any attempt to maintain the single market and customs union, and then gradually dismantle it over 20 years, would require a complete reversal of basically everything that has happened in the last three years. It would require a complete reimagining of the political declaration and the withdrawal agreement. Frankly, while it may have been a great idea four years ago, at this point that train has well and truly left the station. I would advise dealing with the situation as it is now, not as it could have been.

The Chair: Thank you very much to all three of our guests this morning for coming and giving evidence to us. It has been a very useful session. I am afraid time is not on our side. May I thank Allie, David and Dmitry for coming in and giving us a very candid and frank view of how they see the negotiations going forward? I remind our witnesses that you will be sent a transcript. If any small changes need to be made, please send them back to us as quickly as possible. On that note, thank you very much for coming and being with us this morning.