HOUSE OF LORDS

The Select Committee on the European Union

External Affairs and Internal Market Sub-Committees

Corrected oral evidence: Brexit: future trade between the UK and the EU

Thursday 8 September 2016

10.30 am

[Watch the meeting]

Members present (External Affairs Sub-Committee): Rt Hon the Baroness Armstrong of Hill Top (Chairman)[1]; Lord Balfe; Lord Dubs; Lord Risby; Lord Stirrup KG GCB AFC; Baroness Suttie; Baroness Symons of Vernham Dean; Lord Triesman

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

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

Witnesses

Professor Piet Eeckhout, Professor of EU Law, University College London, and Mr Richard Eglin, Senior Trade Policy Adviser, White and Case LLP.

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

Examination of witnesses

Professor Piet Eeckhout and Mr Richard Eglin.

Lord Whitty took the Chair

Q1 **The Chairman:** We have an array of legislators and a wide range of questions. This is a public session. Therefore, there will be a record, it will be transcribed and you will have sight of it, but we need to bear that in mind in anything we say. We have invited you to contribute your expertise to try to clarify to our two Committees the situation we now face, in dealing both with the WTO and with wider trade organisations. We are focusing in particular on the WTO. I will start with an opening question, but if you wish to elaborate on general points, please use that question so to do.

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

Professor Piet Eeckhout: Seniority?

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

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

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

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

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

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

I noted another couple of points, but they are related as much to the relationship between the European Union and the United Kingdom post-Brexit as to the WTO position. I am uncertain what would happen, for example, with the current antidumping measures that the European

Union applies to imports from other WTO members, which have been the consequence of an EU-wide investigation into dumping. Lots of those currently apply, particularly to China. Whether the United Kingdom could simply continue to apply those or would not apply them may also be an issue that comes up in defining the UK's WTO status.

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

Q2 **Lord Wei:** What do you see as the most contentious points or obstacles to the renegotiation or rectification of WTO membership terms? What elements of that renegotiation would be contingent on the nature of the UK-EU relationship?

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

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

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

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

Mr Richard Eglin: Absolutely.

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

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

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

Professor Piet Eeckhout: Can I add something on what might be contentious and how it relates to the EU-UK relationship? There may be some political dependency as to how the other WTO members look at the UK's position in adopting the EU schedule, in the sense that it makes a massive difference whether the United Kingdom remains in a customs union with the European Union, where you would continue to have one external tariff applying; whether there is a free trade agreement between the United Kingdom and the European Union, in which case there will be rules of origin that determine which goods produced in the United Kingdom have access free of tariffs to the EU internal market; or whether trade will initially be between the European Union and the United Kingdom on WTO terms. Richard has a lot more expertise inside the WTO and can perhaps express a view on that. I am uncertain about the extent to which other WTO members may just take the position: "Before we start looking in the WTO at the UK's schedule, we want to know how UK-EU trade will be conducted and what the terms of trade will be". I guess to the extent that the future may be one of trading between the United Kingdom and the European Union on WTO terms, there will be one party, one member of the WTO, for whom the tariffs in the UK will be new: the European Union, which of course currently exports to the UK in the context of the internal market, and you would have new tariffs. That again would depend on how the negotiations between the EU and the UK run. We have seen, for example, the position paper by the Japanese government on Brexit, which has drawn attention to the fact that Japanese companies have invested in the United Kingdom from the perspective of access to the internal market, and that for a number of companies the terms of trade between the United Kingdom and the EU are terribly important. To what extent that might affect discussions about the new UK schedule in the WTO, I do not know, but it could give rise to problems.

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

Q3 **Lord Green of Hurstpierpoint:** Yes, indeed. I would like to explore, particularly with Mr Eglin, your views on what would happen if there is an objection or a set of objections when we table a new set of market access schedules. I have dealt with the WTO. It works largely by consensus and what happens is all very unclear. Usually it is a matter of the proverbial smoke-filled rooms when there is a disagreement. What is the probability of serious objections to the UK tabling a market access schedule, assuming it is basically cut and paste, and how do you see that being resolved?

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

The important thing in the WTO is that it works from consensus. You are right. There are fine points of law that I am sure one can draw out and say, "Ah, but this means that we do not have this, so you will have to re-accede to the WTO". It does not work like that. The WTO is a commercial contract. It is there for the benefit of all members' businesses. Chaos would break out if anybody were to suggest that the UK does not have a schedule and therefore they will not trade with the UK. It would be absolute pandemonium. It is not going to happen. The reality is that it is a matter of negotiation. It could take years before the schedule is actually certified by consensus, as you say, but in that period we would continue to trade on the terms in which we proposed we should trade, as long as they were reasonable. We cannot come out and slap on restrictions all over the place, put it on the table and then say, "Okay, we are going to restrict all your imports but we expect to be able to access your markets". You cannot do that. As long as it is reasonable, I see no problem whatever.

Lord Green of Hurstpierpoint: That is very helpful.

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

Q4 **Lord Stirrup:** Yes. You started to address the problem, Mr Eglin. Let me postulate the situation where we have triggered Article 50, the two years have expired and they have not been extended, so we are out of the EU but, for some reason or another, we do not have a ratified schedule. If I understand you correctly, you have just said that is okay because we just continue with what we laid on the table and people continue to work at all the issues. First of all, is that a correct interpretation of what you said? Secondly, if I can expand it a little, as the Chairman said, you have made this sound rather straightforward and easy, and you do not foresee any significant road bumps. The press are, I think, sounding a little more cautious. Could I explore a little more deeply what sort of issues could derail the process? You said, "provided that we do not want to change anything", but what if we do want to change things? Are we likely to want to change things, what might they be, what effect would that have and how would that impact on the period between leaving the EU and getting final ratification?

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

Lord Stirrup: Suppose we want to change things.

Mr Richard Eglin: If we want to liberalise, there is no problem whatsoever; we can simply go ahead and do it. Nobody would object in the WTO. The WTO is a commercial contract and it is based on reciprocal concessions. If I want to increase restrictions, and I believe I have a balance at the moment of reciprocal concessions with the EU and the UK splits off, I will look at it and ask whether that balance still holds. If I reach the conclusion that, no, it does not, I will want to talk to you and negotiate with you and find how we can redress the imbalance that I perceive. You may say there is no imbalance. It is a negotiation. It is not a legal matter. A lot of it is in the eye of the beholder. Trade remedies—antidumping—are a different question, but if we intend to introduce greater restrictions in the schedules, we will have to offer to negotiate, under Article XXVIII of the GATT and Article XXI of the GATS, with any other member that says their interests have been damaged by what we have done. We need to think about it carefully, but that does not mean you should not do it. Maybe we should. Maybe we are better off raising a tariff. By the way, the exchange would be that you would have to lower a tariff somewhere else. It is not a question of monetary compensation; it is a question of reciprocal bargaining to establish the basis on which we trade with each other. If we are prepared to raise a tariff here and lower one there, that is the game.

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

Q5 **Lord Aberdare:** I think it probably has been answered. I was going to ask what would happen if we wanted to raise, in particular, or lower tariffs, and you have just answered that. If we wanted to retain the EU's external tariffs, presumably no negotiation would be needed.

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

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

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

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

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

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

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

Mr Richard Eglin: Yes.

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

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

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

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

Q6 **Baroness Randerson:** Professor, in your blog post on Brexit and trade you made the point that radically cutting tariffs would put the UK in a weak position, because the UK would have nothing to offer in relation to future negotiations on FTAs. Given that we already have a relatively open market, what do you see as the UK's main leverage in negotiations?

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

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

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

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

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

More important to me than capacity is joining it all up. If you are going to negotiate, the negotiator needs to be in the WTO armed with a set of instructions that represent government policy. In the WTO you are covering almost every ministry, every department of government. It will need to have been sorted out with agriculture, with the technical regulation people, the veterinary people and customs and so on. It all needs to have been brought together in the first place before instructions can be given to the negotiators. Clear instructions are absolutely paramount to being able to negotiate cleverly or properly. There needs to be a big effort, and with business of course, to find out whether certain parts of business need an increase in a tariff or whether we can live without the tariff rate quotas on this, that or the other. It needs to involve farmers. It all needs to be worked out very carefully beforehand. The capacity is not just people and specialists; the capacity to negotiate is more than that.

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

Q7 **Lord Risby:** If we turn to the services sector, which is so crucial to the economy of this country—almost dominant in many ways—a number of things arise. The first is to preserve the success of the services sector. There was criticism anyway about our ability to protect our full range of service industries in the Single Market as such. Secondly, of course, there is now real concern, at least among people running organisations in the services industry, that parts of it may need to be hived off to protect their bottom line. For us, the whole area of services is absolutely crucial. It would be very helpful for the Committee to understand and have a qualitative assessment of how you think that might work in the context of WTO rules and of the European Union, because this is going to be a very serious matter for us to have to deal with.

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

In financial services—passporting—on the WTO side, there is not much at all on liberalisation and there are, of course, further attempts: the TiSA negotiations are under way and many of the FTA negotiations also cover services, but we would have to see the extent to which the United Kingdom was able to take part in that. It really requires detailed analysis sector by sector as to what the level of access to the EU market currently is and what the baseline of WTO commitments would be. That may be different, but there is definitely a lot more liberalisation within the European internal market than is the case with WTO rules.

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

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

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

Q8 **Lord Dubs:** My question is similar to the previous one but focuses on the UK goods sector and trading with the EU on WTO rules. Are there any differences in the answer you would give as regards the UK goods sector, automotive, food industry, and so on, from the one you have given about services?

Mr Richard Eglin: Yes. In some respects one can be a lot clearer about goods because they are more homogeneous. Even so, you need to separate two parts: agriculture and manufactured goods. We withdraw from the EU and we face the MFN tariffs, which vary enormously. The average for the EU on industrial goods is about 4.5%. For agricultural goods it is about 14.5%, and the agricultural schedule is riddled with quantitative restrictions. We will be taking out a certain part of those quantitative restrictions to put into our own schedule, so it gets quite messy. In food processing, the average tariff in the beverages and confectionery sector, if I remember correctly, is 45% into the EU market, which is very high. That is an average across all sectors. Certain products, sugar and poultry, are very heavily restricted. The ad valorem equivalent tariff on certain kinds of poultry is over 200%. That will be our tariff as well, by the way, if we just take it; that will be what we are applying. There will be much more severe restrictions in certain sectors, primarily agriculture, than we face at the moment as a member of the Single Market. We will need in the negotiations to sort out with the EU whether we get a share of their tariff rate quota for exports of butter from the UK to the EU in the future and how does all that work.

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

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

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

Q9 **Lord Lansley:** Can I follow up on the import of goods? Where the WTO is essentially reciprocal, if we are in a situation where we and the EU separately are applying the same external tariff, on the face of it you might ask what has changed. The answer is that origination has changed, and there will clearly be a difference, from the point of view of people importing goods in a supply chain to the United Kingdom, in their ability to incorporate it in goods that are then freely circulating within the rest of the EU. Viewed not only for investment but for trade purposes, for people outside the EU, dividing the EU and the UK in that way creates an impediment to their trade, so it is not a straightforward shift into a new system. How large is that effect, in your view, potentially, and given the principle of reciprocity, what would our major external trading partners feel about it? What would they look for by way of compensation or reciprocal access in order to reflect the problems that complying with rules of origin might create for them?

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

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

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

Lord Lansley: It is the gateway, in effect.

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

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

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

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

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

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

Q10 **Baroness Donaghy:** At present, UK businesses can go to the European Court of Justice if they feel that the principles of the Single Market have been violated. As you know, under WTO rules, arbitration is only possible under the dispute settlement mechanism, and cases need to be brought forward by government, as opposed to business. What impact would that have on UK businesses, in particular small and medium-sized enterprises? Could you comment on the efficacy of the World Trade Organization arbitration system?

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

I think the question alludes to what would be a matter for UK policy: namely, to decide how actively the United Kingdom wants to make use of dispute settlement, and to what extent it is willing and able to take up at the WTO cases that result from issues in international trade, and with Europe, which are experienced by smaller enterprises as opposed to bigger ones. We see a tendency in the WTO for disputes to be taken to panels in the WTO when larger companies are behind the dispute, although one cannot generalise too much. I see the main difference in the fact that, by definition, in the WTO you need to be somewhat selective with the disputes you bring. The other main difference is that there is no automatic enforcement. It is an international law system. You rely on compliance by the member of the WTO that has been found to violate its commitments. There are ways to exercise pressure by imposing trade sanctions when you have won a dispute, but that takes many years and is of uncertain effect. It does not have the force of domestic law in the way EU internal market law has.

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

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

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

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