Select Committee on the European Union

External Affairs Sub-Committee

Corrected oral evidence: Brexit: Future trade between the UK and the EU in goods

Wednesday 9 November 2016

16.05

Watch the meeting

Members present: Baroness Verma (Chairman); Baroness Armstrong of Hill Top; Lord Balfe; Baroness Brown of Cambridge; Lord Horam; Earl of Oxford and Asquith; Lord Risby; Lord Stirrup; Baroness Suttie; Lord Triesman.

Evidence Session No. 7 Heard in Public Questions 96 - 105

Witnesses

I: H. E. Mr Koji Tsuruoka, Ambassador of Japan to the United Kingdom; Mr Hiroshi Matsuura, Minister (Economic), Embassy of Japan.

Examination of witness

Mr Koji Tsuruoka and Mr Hiroshi Matsuura.

Q96 **The Chairman:** Welcome, your Excellency, Ambassador Tsuruoka. Apologies for my pronunciation. I was dreading saying it and I said it absolutely, terribly wrong. Thank you for coming to this evidence session. We really appreciate you taking the time to be here with us. Just to inform you, this is a public meeting and is broadcast. There will be a transcript, which will be sent to you and we look forward to any corrections you feel should be made. We circulated some of the questions to you prior to your coming here. Really, the Committee wants to draw out your short-term and longer-term view of the implications of those questions. Of course we will try to stick to time. I will start with the first question. What is your overview of the importance of trade and investment with the UK to Japanese businesses?

Mr Koji Tsuruoka: Thank you very much. I am honoured and privileged to be invited to this meeting. I will do my best in presenting you with our findings and thoughts on the issues. Thank you also for your first question. Trade and investment is of course quite important, as it is a means through which two different industries can have a mutually prosperous relationship. I will just say one word about the basic importance of Japan and the UK. These relationships are based on common values: the rule of law, democracy, commitment to a free-market economy, respect for human rights and we are committed to continuing free trade. We have more than 70 years' history of a good track record that all these principles work to the benefit of the Japanese people. It is our understanding that they also work for the British people. We have no problem in Japan with the Government or public officials promoting free trade. Unfortunately, in certain quarters of the world that is becoming more difficult. We think that globalisation, free trade and engaging in a transparent manner across borders is of benefit to both sides, and that is what we would like to continue. That is based on the rule of law, because we value the stability and trade capability, which is very important for people deciding their businesses or investments. I am sure you are all quite aware that Japan is second only to the US as a non-EU partner investing in the UK. We have had many years and many wonderful experiences in the Japanese industry that has come here. We now have more than 1,000 Japanese companies investing all over the UK. They directly generate employment for 140,000 people. If you included indirect employment, that would be multiplied many times. The reason these Japanese companies chose to come to the UK is that this is a stable, predictable and friendly economy. They find the UK very well suited for their investment. That is why you will see that the percentage of Japanese investment in the EU very much leans towards the UK. Despite the size of the UK being about 15% of the EU economy as a whole, more than double that portion is invested by Japanese companies in the UK. That is also linked to the understanding that the UK is the gateway to continental Europe as part of the Single Market. I think it is also important that they value a number of strengths of the UK system, or the traditions of the British system. First, there is language. English is a universal language and the means by which high-quality services can be supplied: legal, accounting and consultancy. This is very important software which makes business profitable. They are available. This is also matched with the possibility of hiring highly skilled people capable of providing these services. Maybe they are not necessarily British but they speak the language. We have difficulty in learning different languages—even English, but that is the first other language of most Japanese so they are capable of working in an English environment. Therefore, through English and through the availability of this highly skilled, high-quality labour and professional expertise, this environment for investment is definitely seen as more suitable for the Japanese companies to come here. I will stop there and ask you to move on.

The Chairman: Thank you, ambassador. That is very helpful as an opening. Of course, as we progress we will see what your own views are on a short and longer-term vision for investment in the UK.

Q97 **Baroness Armstrong of Hill Top:** Your Excellency, I was privileged to meet you at your recent reception. I came to that because I come from the north-east of England and so know Nissan well, and also Hitachi. I want to ask you particularly about the automotive industry. Japan is very important in the UK automotive industry. The top five car-producing companies are Japanese. In Sunderland, my home town, we have Nissan, which has been very important in the local economy and community. Can you comment at all on the agreement made and the determination to build the next model of Qashqai in Sunderland and move production of the X-Trail from Japan to there?

Mr Koji Tsuruoka: Thank you for that question and for identifying Nissan as a great contributor to the UK economy and vital to Sunderland. I understand and have heard directly from the Nissan leadership that it is very happy to operate in Sunderland. Nissan has been successful there for the last 30 years. It wishes and intends to continue its operations as long as the environment for investment continues to be profitable. As I said earlier, the Japanese system is a free-market economy. There are few state-owned enterprises and Nissan is a totally privately owned company. Therefore, it is not for the Government to give any instructions or tell it what to do. It will make its own decisions on the basis of its business interests. The issue of whether Nissan will add new production lines in Sunderland or look for other factories, which it has, in Europe as well, has been very much in the press and high up in the attention of the UK Government. I have been interested in this issue but never had what we might call consultation with Nissan because it is a decision for Nissan to make. I am not in a position to engage myself in the decision-making. Let me say that for the record. Having said that, Nissan also kindly informed us that this was the decision it was to announce, and I received that notification just prior to the actual announcement.

From now on, what I will say is my interpretation of what led it to do this. First and foremost, Nissan is part of Sunderland. In Japanese culture, when you become part of a town or part of the community, you do not abruptly break up. You have created a tradition. It is more than 30 years. Nissan is like family in Sunderland. Nissan knows that what it decides to do will affect in a major way how Sunderland will live. Therefore, it is well aware of the responsibility that it now has vis-à-vis the people in Sunderland. Of course, because it is a company that needs to make profits it has to look to the future effect of this choice of continuing to build and even enhancing the production capacity in Sunderland with two—not just one—new production lines. It has not told me the precise business background for that decision but I can say, based on the more than three decades of good performance and good profits that it has been making, it is a Japanese way of trying to maintain the good will. I do not think that Nissan is willing to cut things off abruptly.

There needs to be further consultation and I think there has been very good consultation between the Government of Prime Minister Theresa May and Nissan. I do not know what conditions or assurances the UK Government might have presented Nissan. Again, this is a business decision. We are not involved. Having the Prime Minister deal with the president of Nissan is in itself a remarkable engagement by the UK Government. Therefore, I interpret this as a strong commitment of good will on the part of the host Government for Nissan. You may have seen in the press that there are certain issues that they discussed, most of them, I believe, to the satisfaction of both sides. That is what led Nissan to maintain the 7,000 employees it directly employs and the manifold indirect employment that it generates.

I am also quite happy that the Nissan decision was welcomed by the British people. That does not mean that it will stay for ever. It is all subject to the profitability of continuing business. It is now up to the Japanese government as well as the UK Government to ensure that Nissan will continue to operate and produce cars out of the UK.

Baroness Armstrong of Hill Top: You have been very clear—thank you—that the environment in which it is working and the environment in which we are trading as a nation will be the indicator for Nissan with regard to future investment decisions—not just Nissan but other automotive industries. Will you say a little more about that?

Mr Koji Tsuruoka: Yes. When we talk about the automotive industry, a car is made of 20,000-plus parts. The Sunderland factory assembles the final product, which starts running after assembly. There are many parts that come to Sunderland that are not produced in Sunderland—they may not be produced in UK territory. This is what we call the global supply chain. There are many parts makers in continental Europe that supply the main factories here. Of course, Nissan is one. There are Toyota and Honda. It is not all made in the UK. They have to assign and order parts from where it is most efficient to do so. There are parts manufacturers across Europe, and it is these parts coming freely through the borders to the factories that makes this efficient car manufacturing possible. The tariffs are often seen as an issue that bars the finished product of the auto being exported elsewhere, but even before that there is this flow of parts, and whether that can be freely and efficiently conducted is very important. With the combination of this two-way street—no tariffs and no obstruction for the free flow of parts that come in—and also bringing the final product back to, for example, the European continental market, if you have tariffs on both sides it means the company suffers very severely, in terms of prices but also procedures. That will be a very costly procedure for the companies, which is not currently in place. It applies to all manufacturing in a way, but automotive companies are really very competitive today so they have allocated those parts manufacturers where they find it most efficient and they have structured all these systems to have no waste in time or resources. It is a very well-structured system that operates most efficiently. If you put in place artificial barriers along the way, by definition it will be costly and inefficient. That is something the car manufacturers operating here in the UK are quite concerned about. Because they are successfully manufacturing cars in the UK under those conditions, they would like to continue being able to do so.

The Chairman: I remind the Committee to speak up. It is difficult for *Hansard* otherwise. Lord Risby.

Q98 **Lord Risby:** Ambassador, in your message that you sent, you referred to the significant relationship between pharmaceutical industries, not least the fact that the European Medicines Agency is located here in London. Of course, that is because you have extremely high standards of manufacture in your own country, as we do. After Brexit, if we did adopt a different set of regulations, how do you think that would impact the investments here from a regulatory and a qualitative point of view, and indeed the activities of Japanese pharmaceutical companies located here trading with the continent of Europe in the European Union?

Mr Koji Tsuruoka: Thank you for raising the pharmaceutical industry. It is one of the most important industries for Japan. It is indeed the driving engine for the future of the Japanese economy, as it is for the UK. It is important not just for business but also for people in general. It is a humanitarian activity at the same time. As you may know, almost all the Japanese pharmaceutical companies have bases in the UK. This is very much based on the presence of the EMA in London. Why is that the case? It is because R&D and all regulatory proceedings take place in London. You can do these face to face and you have the resident expertise in London because there is high demand, which draws these high-skilled researchers as well as the consultants who will help them go through the very complicated regulatory process. If you have a different regulatory regime, it means you have to duplicate that—at least, it will be twice what they need to do.

If they need a different certification or different recognition of their health records and so forth, they could be assessed by the UK authority for sales within the UK. The EMA may move elsewhere, and if it has to go through that different procedure the company will be burdened by doing the same thing twice. Initially, they do it in Japan, in most cases. Today, fortunately, there are not too many countries where you have new drugs being commissioned—very few. It does not even reach 10, around the world.

This is a combination of a number of international co-operative regimes. The aim is to encourage the development of new drugs, because we have new health challenges in this modern age. At the same time, how you allocate resources efficiently to encourage them to do it is a business decision. If the cost of the regulatory regime is too high, companies will not make the investment. This is why regulatory regimes around the world have the common objective of working together to have a fairly harmonised system of recognition. That is what the EMA, the European regulatory agency, is doing with Japan and the US. The pharmaceutical companies will hope that that sort of co-ordinated harmonisation at regulatory agency level continues, and will be enhanced even more.

The timing of the certification and recognition must be as efficient as possible. If the differences in the system prolong clearance timing, that will damage the marketability of the drugs that are in consideration, which reduces their chance of recovering the cost. The current system for Japanese pharmaceutical companies works very well, because they do not have to go anywhere else and can do everything in London. The quality is very high and the conversation is very smooth. Japanese companies have been investing even this year a great deal of money in the structure of stationing the experts and even having a research lab as a supporting mechanism for these regulatory mechanisms. They would really like to continue this as is. That is why you have seen in our message to the UK and the EU the wishes of Japanese pharmaceutical companies to continue operating as they are today. If that is not feasible, because everything is subject to negotiation and agreement, the harmonised system which the pharmaceutical companies need to satisfy and which does not burden anyone with procedural requirements will be further complicated, because if one or the other country needs its own certification mechanism on top of another that may be quite valid. It is an issue of regulatory co-ordination and harmonisation in the end, and it applies not only to pharmaceuticals but to many other products.

Q99 **Baroness Brown of Cambridge:** Your Excellency, you have already spoken very eloquently about the challenges that the car industry would have if there were border tariffs or more complex customs clearance procedures. Are you aware of Japanese business currently looking at what the cost implications might be?

Mr Koji Tsuruoka: I am sure that companies are doing a lot of research. They have to respond to questions from their board presenting different scenarios. But there is not one scenario—there are even two or three, and you can say that it will be one of those three or even one of the five. Everything is totally open right now. They may be doing some research, but none of this I have heard is concrete in any way. I have been advising the Japanese industry to keep calm and not rush to any conclusion—and it is more important to have careful scrutiny and consideration of all possible issues. The message that you have seen is a result of some very hasty work that we did over the summer, but that kind of approach continues to go on on the Japanese side, to identify all the issues before jumping to any conclusion. That is why we believe that the process of consultation over this engagement is important, which is why we have engaged in dialogue between the two Governments, with the support of the industries. So we can assure them and give them comfort that there is not going to be any shock. If they are forced to take action because they never heard any of those decisions were coming, by definition it will be detrimental to their business. But I am trying to tell them that the Japanese government, together with the UK Government, and the EU for that matter, that we are making sure that industry will not be shocked. We need to engage with them—not that we disclose everything, because government-to-government negotiations have to be held in confidence. Otherwise you cannot proceed or make progress in negotiation. At the same time, we need to comfort them and give them assurances that there will be no shocks and their views will be taken into account—maybe not 100%, but their views will be heard. That is what we are trying to do, and I think we have been more or less successful. That is why they do not have to write all the scenarios or contingency plans right now, although they are studying them for sure, because that is what company officials asked us to do. But there is no intention of having any concrete scenario that they see they need to mobilise or deploy any time soon.

Baroness Brown of Cambridge: You talk in your Government's statement about applying the accumulation principle to the rules of origin in trade between the UK and the EU after Brexit. Can you elaborate on what they would mean for Japan's trade with the UK and the EU?

Mr Koji Tsuruoka: The rule of origin comes into play when you have a preferential arrangement with a selected number of trading partners. You have to assign what preferential treatment you provide to which product that comes from where. So let us say that Japan has a free trade agreement with Singapore. If Singapore products come to Japan, we have to make certain that the local content that is Singaporean is at least 40% or 50%, depending on the agreement on each of the products. The EU currently has a number of FTAs with other countries, so the British product today satisfies the requirement of being identified as local content under the definition of the free trade agreement that the EU has with other countries. Let us say that the local content recognition no longer applies to British products—to cars, for example—and the local British content is 50% for a car and the counterpart to the EU FTA insists that it should be a minimum of 60% local content. Today, because the UK is a member, it satisfies that, but if 50% is removed and is no longer recognised as local content of the EU, that product will not be given the preferential tariff treatment.

So the local content requirement, which is the content of the rule of origin, affects the actual manner in which trade is conducted, and this is very important. Many trade agreements are based on the assumption or the understanding that how products are manufactured will be reflected in the rule of origin that has been agreed. By changing the rule, you may inadvertently deprive the existing preferential treatment which has had British content. That is what we want to raise. It is technical, but it affects exports and imports.

Baroness Brown of Cambridge: Are there other agreements outside the EU that are particularly good for these complex integrated supply chains on which we might model our future?

Mr Koji Tsuruoka: There are rules governing trade, of course. The most universal and global rule is the WTO. The WTO rule makes it mandatory for a member of the WTO not to discriminate against other WTO members. That means that if you provide preferential treatment for country A, you have to provide the same treatment for all the others. That is called the Most Favoured Nation clause. But if you have agreed to open up trade comprehensively with a selected partner, then you are not required to apply that preferential treatment to everyone else. Why is that? Because by opening up with selected partners you are stimulating the growth of global trade which will benefit countries that are not part of the preferential treatment. That is how the EU can be compliant with the WTO without applying the tariff-free measures to non-EU countries. It is the same with a number of the FTAs we have seen. NAFTA is one and the bilateral FTAs that we have are another. There are choices around being compliant with the WTO but also having preferential treatment in trade relations with selected countries. The comprehensive nature of those are judged by other WTO members. You will go through the registration process, but so far as I am aware, no FTA has been rejected by the WTO as being worthy of that exception.

The EU market is defined more in terms of the Single Market by EU standards and that satisfies the requirement for a customs union, which is the name provided by the WTO for these free trade agreements, but they do not have to be completely identical. So there are choices to be made after the UK leaves the European Union around what sort of trade arrangements of a preferential nature with selected regions or selected countries you would like to build up.

Baroness Brown of Cambridge: Would a NAFTA-type model be the natural one for us to think about?

Mr Koji Tsuruoka: That is something you have to consider. Japan is not in a position to make suggestions. But I can say that it is quite important to make a thorough survey and assessment of the existing ones. You have a track record of how successful in terms of their effect on the economy these free trade agreements have been. Many have been in force for more than 20 years, so if you are considering which model fits best or what would be good for you, there are a number of cases that you can study.

Baroness Brown of Cambridge: I am sure that is wise advice. Thank you.

Q100 **Lord Stirrup:** Ambassador, so far we have talked mostly about large enterprises, but in your government statement you highlighted the concerns of small and medium-sized Japanese businesses here in the UK. Might a new trading arrangement between the UK and the EU give rise to additional or different concerns and implications for such businesses when compared with their larger cousins? If so, what are the differences and how might we mitigate them?

Mr Koji Tsuruoka: Thank you very much for that question. We believe that it is very important for small and medium-sized companies, which tend to be focused on domestic business, to be open to the possibilities around international activities. Japanese SMEs are quite capable if they are encouraged to do so. It is Japanese policy today to try to encourage Japanese SMEs to engage internationally. Much of the technological expertise and the products they produce are one of a kind, but because the Japanese economy is somewhat large, they are not adventurous enough to travel abroad and introduce them. The reason we have added SMEs as an entry in the Japanese message is geared towards stimulating Japanese SMEs to maintain their interests and expand internationally. In most cases the major companies do not have to bother the Government, or they do not have to ask us about the situation. SMEs may not even ask or be at all interested, so we are trying to promote this. However, it is true that they do not have access to basic information because many may not understand English. We have 1,000-plus outlets of Japanese government agencies that are available for consultation with SMEs and we have heard from them that when Brexit happens—we do not know how it will happen—they will be interested to know whether their businesses or their business opportunities may be affected. That is why we have that entry point. From a Japanese viewpoint, it is important to continue to engage with SMEs because we believe they have great potential if they engage internationally.

Lord Stirrup: Perhaps I may follow that up briefly to be clear. The implication of what you have said seems to be that the SME business you are trying to encourage is essentially with the UK market—business growth which does not exist at the moment. Therefore, it is less about them using the UK as a gateway into the rest of Europe as opposed to them actually seeking new business within the UK market. Is that a fair conclusion?

Mr Koji Tsuruoka: No. Of course the UK market is in itself very important but at the same time they are using the UK as a gateway to Europe. There is no difference in that approach between larger companies and SMEs. Many of the questions that we have seen from the outlets across Japan are around whether access to their products or services would be constrained as a result of Brexit. Of course our answer is that we do not know. It is something that will have to be discussed, considered and decided at a later stage. However, they have expressed their interest in this.

The Chairman: Ambassador, I want to follow up on something you said in your opening remarks when looking at high-end skills, particularly in small and medium-sized businesses. Do you think that small and medium-sized businesses will be risk-averse about coming to the UK and investing in high-end skills here and managing the uncertainty around what Brexit looks like?

Mr Koji Tsuruoka: I cannot speak on their behalf because I have not put that question to them. However, working on the logic that I see in their modus operandi, again, SMEs are quite limited in their capacity—personnel and the resources they can deploy—so they really have to be very careful in choosing where they will invest and be engaged.

They are now asking us for clarity and information so they can make plans as to what economies and which destinations they should prioritise, as they may decide to engage. They are already engaged; the question is whether they will expand further, or whether they will look at other opportunities as a more profitable destination.

For now, I do not think they have made any decisions because nothing has changed, but they are looking at what might happen. Companies will have to make that strategic decision sometime in the future. They cannot withhold a decision for ever. There is a limitation on how many resources they can deploy. If they make a decision to invest in one destination, it means that there will be no possibility of investing in another. That is only natural. The new element they need to take into account is the timing of Brexit and what it will affect, with market access that could or could not be available. It is still very much up in the air right now. They are continuing to keep an interest and following the news. That is what I can fairly say now.

Q101 **Lord Balfe:** Your Excellency, your government mentioned the importance of harmonised standards between the UK and the EU, but there is another way, which is removing some of those harmonised standards if they are impediments to trade. Do you have any idea of EU standards that could beneficially be removed or amended significantly that would, in their turn, help our trading relationship?

Mr Koji Tsuruoka: I am not fully aware of any specific requirements that I could identify as being preferred to be removed. We are currently in the process of negotiating an economic agreement with the EU: the Japan-EU Economic Partnership Agreement. We hope we will have an agreement in principle before the end of the year. We have a team in Brussels negotiating even as I speak. That is one issue they are negotiating.

As I said, harmonising a system of regulatory regimes is mutually beneficial because EU products will come to Japan and they do not have to be verified again. The same works vice versa. If we have higher standards that catch all, we could agree to do that. The question is whether those are overburdensome and based on the hidden intention of blocking trade. I would not be able to identify what they are, but there is always doubt about too cumbersome a procedure and whether it is objectively justifiable. This is very difficult because many of those regulations have been introduced because there are interests and demands for those requirements to be in the system. Deleting them will require a political powerhouse. That is what is happening.

This is consistent with what I said about the British system. I am not aware of any complaint about the British system. Perhaps you do not have that now because of the EU membership, but I do not think it has been a tradition to have complaints raised against the UK on these issues. Transparency, the rule of law and predictability are very important principles, but it is not necessarily the case everywhere. You have a point. When the right time comes I am sure our experts could discuss these issues in detail with yours.

Lord Balfe: But for clarity, you seem to be saying that the approval process is maybe lengthy, but in the end it is simpler just to have a straightforward system where there is common approval.

Mr Koji Tsuruoka: Definitely.

Q102 **Lord Horam:** Ambassador, the Japanese Government said in their statement about Brexit that you would like a transitional arrangement. Could you spell out what you mean by that?

Mr Koji Tsuruoka: The transition that we mentioned indicates no drastic change all of a sudden, which I phrased as 'shock' earlier. The current system is well known and operational. You do not change a system of trade all of a sudden and implement that change from the next day onwards. Companies and firms will not be able to adopt that, if it happens all of a sudden. If there are changes that need to be implemented it is our hope that there will be transparency and an indication as to what will be implemented at some future time, with a time schedule. Companies will therefore be able to adopt a road map that has been made public and known, and they could adjust step by step. If it happens overnight and you say, "The world is now different. Unless you have satisfied A, B and C, your product will not be able to enter the market", that will not be possible for anyone to address.

Lord Horam: I am sure we all agree that that would be absolutely lovely and that that could be achieved in one form, but the truth is that in negotiations of this kind the tradition is that agreements are not made until the very last minute—sometimes past the last minute. If there are to be two years in which this period of negotiation may take place, you may find that you do not know what is happening until the very last minute. Is that not terribly bad from your point of view?

Mr Koji Tsuruoka: Yes. When we know what the package is at the end of the two years it should include the transitional path. It is the same thing when you adopt Bills, for example. You do not enact laws right after you adopt them. You have a public notice period of perhaps half a year or one year to enlighten or inform stakeholders of what they should expect once the law is put into effect: if you have a negotiated agreement with, let us say, the UK that within a few years' time you will reach destination A, the passing point X will happen one or two years from now and this is how it will happen. These are the transitions that need to be made available to those conducting business.

Lord Horam: To be clear, you want a transitional period built into the agreement?

Mr Koji Tsuruoka: Part of the agreement should include the indication of what will happen.

Lord Horam: A transitional period, however long that may last?

Mr Koji Tsuruoka: Yes. That is very important for all the companies to know, otherwise they cannot plan.

Lord Horam: I understand that, but in the interim, while negotiations are going on, you may find reporting on what has happened. Some may be true, some false; you do not know. This itself will cause shocks along the way, will it not? How do we overcome that?

Mr Koji Tsuruoka: You are quite right. I could not agree more. I have conducted negotiations myself. Many rumours are totally unfounded and you learn something suddenly: I have negotiated this deal with another country and without my knowing it is printed in the press. Of course you have to be careful about whether you are led by the press in what you understand to be the case. That is why we need consultation with stakeholders and not to be led by the press in understanding what is really going on.

But it is interesting what may happen when the agreement is reached, because while the negotiation is under way, it is my understanding that the UK's status as an EU member will not be affected. At least, after you trigger the Lisbon Treaty's Article 50, we know about the two-year period that will not change any trade status. It could be extended by agreement by all but those are issues that we will know.

What we will see in the press, and have seen in many of the statements that have already been made public by certain leaders, are just indicators. They are not actual measures that are being implemented. What we are saying is that as an interim or transitional measure, you may not be able to come to the final conclusion of the permanent agreement—because of the time constraint or because of the difficult co-ordination that you need to do—so do not jump to the conclusion that there is no more relationship at all but put something in transition that will allow business to go on, hopefully as usual. If not that, have something that will tell businesses what they need to expect.

Q103 **Lord Triesman:** Good afternoon, your Excellency. I note that in your statement, which I think is very useful guidance for all of us, you request both the United Kingdom and the EU to establish a dialogue with your Government and with Japanese businesses. Has such a consultation taken place yet and, if it has, have these been ad hoc discussions or more formal ones that you would regard as part of an appropriate machinery? Has the EU started that kind of discussion either on an ad hoc or a more formal basis?

Mr Koji Tsuruoka: We have had a consultation between the Japanese Government and the UK Government on a number of occasions. We have not yet set up an agreed, regular, periodic mechanism of consultation but we have had a number of meetings between the relevant officials on the UK side and the Japanese side. I have visited most of the Secretaries of State responsible for Brexit and trade relations, or international trade. My Prime Minister has already had consultation or discussions with Prime Minister Theresa May twice so far. We have an ongoing process of consultation with the UK Government, from the very top to the level of officials.

We are also partly waiting for the UK's system to be set up fully. It is a new challenge; I fully understand that you cannot all of a sudden have expertise that is totally equipped. As we were, it is about running alongside in a spirit of partnership and working together that we are visiting the UK's senior officials. We have had the visits of a number of secretaries of state to Japan. The first message that the UK Government has put to the Japanese public is that the UK is mindful of Japanese interest in Brexit, especially the interest of Japanese industry, and therefore Japanese industry will be heard and there will be consultation. For the time being, it is very important to put to the Japanese industry leaders in Tokyo that there is an engaged process of consultation ongoing between the two Governments.

Beyond that, I think we will have to have more enhanced, detailed and extensive discussion, which be very comprehensive and difficult. We do not want to overburden the British system, as the UK itself has much work to do. But if there is any need or request from the UK Government, we are volunteering to be available to come and work with them on a number of issues. These will not be limited to the issues of Japanese industry's interests but, because we have been negotiating trade deals while the UK has not, there may be certain insights that we can offer to be of help.

On the EU side, to be very frank, it is not providing or allocating resources to engage with Japan on Brexit for the time being because, it says, it has not even received an official notice from the UK and asks, "Why should the EU start discussing Brexit with a third country?". It is difficult to go over that. As you know, we have put the message and we have had consultation in a general way with the senior EU officials but an engaged dialogue is yet to take place between Japan and the EU. It will start, in due course, when the official UK-EU negotiation or consultation starts.

Q104 **Lord Horam:** I want to ask about the proposed European Union-Japan economic partnership, which you hope to conclude. What effect will Brexit have on that?

Mr Koji Tsuruoka: Again, the EU-Japan EPA is currently under negotiation. The two leaders have voiced their hope to have an agreement in principle in place by the end of the year, which means that the most salient points will have been discussed and agreed. That has not been achieved yet and we are in the last stretch of the year for getting that done. This is inclusive of the UK as part of the EU market. In talking of the EU now, it is inclusive of the UK.

Once the Brexit negotiations are over and the UK becomes a separate economic entity that is capable of negotiating and coming to an agreement with another country on the terms of trade, of course we will be willing to engage with it. At the moment, we cannot do that. That is not because Japan does not want to but because the system does not allow us to do that. But having a Japan-EU EPA will be quite useful when we discuss issues with other countries. Because the UK has been part of the EU, I expect that many of the systems will continue to be effective in the UK.

If we agree with the EU on the regulatory mechanisms that we have discussed—for example, harmonisation and how we recognise each other—it is most likely that those will be easily imported into a bilateral trade agreement that we may consider in the future. So I think that a well-thought-through Japan-EU EPA will benefit your trade negotiations with Japan in the future as well. It is not something that is totally irrelevant to the UK.

Lord Horam: So it might be a piece of good fortune both for the UK and for Japan.

Mr Koji Tsuruoka: Yes. We have been receiving strong support from the UK. As I said earlier, the UK and Japan are committed to free trade and therefore there is no sense of protectionism that we need to worry about. We have very much expected and relied on the UK's strong support in bringing the whole of the EU along on those lines.

Q105 **Earl of Oxford and Asquith:** Good afternoon, Ambassador. I am glad to say that in the past I have been quite a frequent visitor to your very efficient embassy, and it is good to see you.

I would like to turn to our last question. Not surprisingly, the Japanese government would like to see euro clearing operations retained in this country. This is a subject under much consideration elsewhere in Parliament and in government. If the euro clearing system had to move to, let us say, Paris or Frankfurt, how would you see that affecting the efficiency of Japanese business, investment and financial transactions in general?

Mr Koji Tsuruoka: As you may know, not just the Japanese but most global financial services providers have concentrated their resources in the City of London. If you look at the past, even from the viewpoint of Japanese financial services providers, those resources have been relocated to the City from elsewhere in the European continent. That is because the concentration of resources is the most efficient way of making the best use of the resources available. Those resources have been multiplying by others concentrating their resources there as well.

The euro clearing mechanism is just one part of the strengths that the financial services providers have brought to London. If they are forced to attend to a clearing mechanism elsewhere, they will have to spend additional resources to do the same thing that they have been doing here most efficiently. Also, the quality and cost of that will of course be a burden and it is not something that businesspeople will welcome.

To be frank, the efficiency of the City of London is very much appreciated and it has been the result of joint work between not just Japanese but UK, American and European banks. They have all decided to do this together in one location. It will be a huge challenge for those companies that have come a long way to establish the most efficient clearing house here in London to be told, "You need to go elsewhere". You can easily imagine that the choice will be difficult to make. There is no comparison and no natural substitute, and then they cannot discuss with other banks where they are going to go. It is nightmarish if you think about the business decisions that they may be forced to make, and it will affect everyone's profitability at the same time. So this is not something that will be welcomed by the financial services providers.

Japanese companies, too, would not like to see that. That is why we raised those points in the message. The smooth, efficient operation of the City of London is one of the most important contributions that the UK has made to the global economy. It not only benefits the UK but is responsible for operating the global economy most efficiently, and that is why these companies are here.

The Chairman: Thank you very much, Ambassador. This has been a very useful and informative evidence session for us all. We all appreciate you coming here and giving us responses that have been as frank and open as possible, given that at the moment there is very little that any of us can say about the negotiations. Thank you very much indeed.

I just remind you, Ambassador, that the transcript will be sent to you. If you feel that there are corrections to be made, please make them and send them back to us. Thank you so much.

Mr Koji Tsuruoka: Thank you all very much. It has been a great honour.

The Chairman: Thank you. This evidence session is closed.