HOUSE OF COMMONS

International Trade Committee

Oral evidence: UK-US Trade Relations, HC481 iii

Wednesday 17 January 2018

Ordered by the House of Commons to be published on 17 January 2018.

Watch the meeting

Members present: Angus Brendan MacNeil (Chair); Mr Nigel Evans; Marcus Fysh; Mr Ranil Jayawardena; Mr Chris Leslie; Emma Little Pengelly; Julia Lopez; Stephanie Peacock; Faisal Rashid; Catherine West; Matt Western.

Questions 160-210

Witnesses

I: Dr Peter Holmes, Reader in Economics, University of Sussex; Julian Jessop, Chief Economist and Head of the Brexit Unit, Institute for Economic Affairs; and Warwick Lightfoot, Director of Research, and Head of the Economics and Social Policy, Policy Exchange.

II: Howard Chase, Director of Government Affairs, Dow Chemical Company; Ian Cranshaw, Head of Business Development and International Trade, Chemical Industries Association; and Saoirse Fitzpatrick, Senior Advocacy Adviser, StopAIDS.

Examination of witnesses

Witnesses: Dr Peter Holmes, Reader in Economics, University of Sussex; Julian Jessop, Chief Economist and Head of the Brexit Unit, Institute for Economic Affairs; and Warwick Lightfoot, Director of Research, and Head of the Economics and Social Policy, Policy Exchange.

Q160 **Chair:** Good morning. May I welcome our panel this morning and ask for your name, rank and serial number just for the record?

Warwick Lightfoot: I am Warwick Lightfoot. I am the Director for Economics and Social Policy at Policy Exchange.

Julian Jessop: I am Julian Jessop. I am Chief Economist at the Institute of Economic Affairs.

Dr Holmes: I am Peter Holmes. I teach economics at the University of Sussex and I belong to the UK Trade Policy Observatory at the university.

Q161 **Chair:** Thank you. The University of Sussex is making quite a name for itself in this period since Brexit. On that, Dr Holmes, some studies have found that free trade agreements have lowered the cost of living, others that they have led to large and long-lasting job losses and others that separate factors such as technical change have much bigger effects on living standards. How do you assess the effects on consumers of trade agreements?

Dr Holmes: Traditionally, we used to look at the effects of trade policy in terms of prices, and it is fairly clear that anything that liberalises trade is likely to lower prices and thus benefit consumers. Increasingly, though, as tariffs have been reduced to very low levels—except in agriculture, which you may want to come back to—the effects of trade agreements on price and thence directly on consumers, are much lower. We have to look really at the regulations—trade agreements are about regulations. I am going to be a typical economist here, but it can go either way. Trade agreements are often sought by developing countries as a way of improving the quality of regulation. For example, the Indians approached the EU for a free trade agreement. One of the motivations for the Indians was that, if they could persuade their businessmen that getting more access into the EU market meant upgrading certain standards and procedures, it would improve their exports. Actually, the Indian Government was partly trying to upgrade the standards infrastructure. So the answer is that it is deeply ambiguous.

If you form an agreement with countries that have very good regulatory standards, you can use those as a way of levering up your standards. If you sign an agreement that involves you being obliged to import stuff made to lower standards than your own, it can go that way. There are two forces at work: what you call a race to the bottom, and a case where in order to get free trade you have to upgrade your standards.

I know I am going on too long here, but my understanding is that within the United States the pollution regulations on cars were effectively dictated by the existence of a single market in the United States. California introduced emissions restrictions, and everybody else wanting to trade into California had to match the California rules, thus upgrading the environmental standards of the whole of the United States to preserve trade within the United States. I am afraid that my answer is that generally on prices they will be favourable, and on standards it depends what regulations and agreements you are looking at.

Q162 **Chair:** You have reminded me of President Truman, who looked for the one-handed economist because of this "on the other hand". You have said a number of interesting things. India wanting regulations and red tape so that it can improve standards is fascinating in the current debate that we have. On the California effect, I remember back to the smogs, and I have just realised that it is cars and that is what happened in the States.

The US's top exports to the UK are aircraft, nuclear energy and precious stones. I notice antiques being quite far up as well—works of art, collectors' pieces and antiques being number four or five. In what sectors do you see US exporters making the greatest gains in the UK, and what impact could this have on UK consumers?

Dr Holmes: Again, it would depend very much on what sort of agreement we had. The US seems to be arguing that agriculture is one of their top priorities: that they want the UK to relax EU standards on food products. I think that is probably not very good for consumers, but food prices might come down—it is very difficult to be absolutely definitive about that. Cars is another area where the standards and enforcement mechanism is different, and they might well be interested in that. It is very difficult to know what the US objectives really are—I can't be more precise than that I'm afraid.

Q163 **Chair:** You mentioned food. The NFU told this Committee that although cheaper food might please some consumers, it might also adversely affect the countryside, supply chains, and the UK's manufacturing sector. Can we say definitively that an FTA with the US would provide a net benefit for the UK? I know that the British Chambers of Commerce is very nervous about an FTA with the US.

Dr Holmes: I think you definitely can't say for sure that it would be beneficial. It very much depends on the terms. Some tariffs are still particularly high in sectors that are relevant for trade. Chemical tariffs are quite high, and I understand that the chemical industry there is looking to see tariffs fall, so even without major regulatory changes that would be a benefit to that industry. For cars, you would get EU tariffs at 10%, US tariffs at 2.5%—they could sell more cars here. Again, it really depends on the terms of the agreement. If it was a very shallow agreement just lowering tariffs, it would have relatively little effect. If it was an agreement affecting regulations primarily, it would really depend on how those regulations were adjusted.

Q164 **Chair:** Before I come to Mr Jayawardena, would any of the rest of the panel like to venture an opinion on this?

Warwick Lightfoot: Policy Exchange's starting point on trade is that trade and commerce is beneficial. That was acknowledged by many of the early practitioners of economics, including the famous Dr Mandeville, David Hume, and Adam Smith. Last year we celebrated the 200th anniversary of the publication of "On the Principles of Political Economy and Taxation", David Ricardo's great book that exposed and set out the argument of comparative advantage. That is the key to all of this. Providing that there is some difference in your relative efficiency, everybody benefits from trade.

Economists disagree on many things—you caught very neatly President Truman's jibe about economists—but oddly enough, one of the things they tend to agree on is the benefits of trade and the principle of comparative advantage. In the way that we look at trade, its advantage is for consumers, and it is the consumers' voice that, if I may say so, Ministers and legislators hear much less of. You will have the NFU, the Chambers of Commerce and the CBI. You will have producer interests that call upon you, but rarely will you get the person in Aldi, in Lidl, in Iceland calling in to ask about the vacuum-packed corned beef that they have just bought. In our perception, this is about putting the consumer, and consumer welfare, at the heart. The advice we would give to the British Government, the EU in future, and the Governments of the United States, Japan and China, is that the principal activity of trade is to expose your own domestic markets to as much competition as possible, so that consumers have as much choice in quality and price as possible.

Q165 **Chair:** What is the risk if only one side does that—if one side opens up its market to consumers and choice, and the other side does not and keeps the protectionist approach? Is there a sort of prisoner's dilemma there?

Warwick Lightfoot: I think it's a mistake to see trade as some kind of complex aspect of game theory, or some kind of mercantilist zero-sum game. The person who expressed that most vividly was a formidable economist, probably the greatest woman economist that Britain has ever produced—the late Joan Robinson. She is mainly known as Keynes's collaborator, and was an important Cambridge economist who developed the whole Keynesian revolution. She said that if your trading partners put rocks in their harbour so your ships cannot enter, you should not make the mistake of doing the same thing on a reciprocal basis. You should ensure that all your markets remain as open to as much trade as is practicable. I was about to say that, of course, we do not want something coming in that is positively dangerous. We don't want something that none of us would want to be using, whether clothing that may pose a fire risk, a product that could damage our wildlife, or whatever. It is very important to have those health and safety rules, but it is important to base that around science. I am sure you will want to pursue this in some of your other questions.

The challenge on trade with the United States will be that the precautionary principle that the EU, and the United Kingdom as part of the EU, has developed, is not entirely consistent with the science-based risk approach that the United States mainly practices. The key question is: is a product safe to use, and would we advise someone—for example a British person going to the United States—with a long list of things not to touch or do because regulation in the United States is defective and you really want to be very careful when you are on holiday there? I think it is about getting the science right, getting the regulation right and recognising the opportunities for trade.

I will say one final thing, it is not about you going halfway around the world and persuading someone over there to buy something they might not otherwise want to have, but giving your own businesses, consumers and economic agents the opportunity to have the full range of international specialisation and to maximise competition in your own domestic market.

Q166 **Mr Jayawardena:** Mr Lightfoot, I am so pleased that you have mentioned not only the precautionary principle—we have heard about how it has been misused to date by the European Union, keeping our prices up and reducing consumer choice for EU consumers—but comparative advantage. In many ways you have answered many of the questions I was going to ask to elicit those sorts of responses already, but—you would be disappointed if there wasn't a "but," Chairman—could I just push you on prices? We have heard from Dr Holmes that there is no clear view on what would happen to prices. You have just talked about the consumers at Aldi, Lidl and—dare I say?—all the way through to Waitrose. I would be interested to hear your view, but I would contend that consumers would benefit from more supply from a wider range of producers, because I believe that that would reduce the cost. Would you agree?

Warwick Lightfoot: I think you are right, but I think that in certain sectors, particularly textiles, food-related products and agricultural products, you would expect prices in a more open and liberal trade environment to actually fall. I would also say that there is an important thing about consumer choice, particularly in relation to textiles. There are certain things available in international markets, available in the United States, that you simply cannot buy in the United Kingdom—certain shoes, for example. This is about not just tariffs, but quotas and rules. May I share a slight domestic irritation with you?

Mr Jayawardena: Please do.

Warwick Lightfoot: My other half—

Chair: It is your domestic?

Warwick Lightfoot: Yes, it is a genuine and for me a potentially embarrassing domestic illustration, but it does it very neatly in a way that I think everyone will understand. My other half has a particular

attachment to a certain form of nightdress of the sort that older, middle-aged people such as myself like. They are comfy, warm, long and fleecy—get the impression? They are manufactured by an Austrian company in China and the United States, and on sale in the United States. They cannot be imported and readily available to my other half here. So she either goes on holiday to the United States and brings them back, and potentially has to go through the red channel, just in case she triggers the tests for duty; or, we have a friend who very kindly allows these things to be sent to his house—when he travels to the United Kingdom, he brings the nightdresses here. In November it was my turn to bring the fleecy nightdresses and go through the red channel. The lady doing the customs said, "You are fine, you are just below the level," and I owned up to what it was all about. But that is about the fundamentals of consumer choice and not just about price.

Q167 **Mr Jayawardena:** You may well have been listening to meetings of this Committee before, because consumer choice is something that has been raised in the past. May I then turn to the United States from a different perspective? I welcome any answers to this. The United States' top goods exports to the UK are aircraft, precious stones, nuclear energy and so on. What, in your view, does that give us from the perspective of bargaining power, in terms of negotiating a trade deal? Those are high-value goods, which arguably we cannot produce readily. We need to be able to import those from the US, but in return we would be able to export different but complementary products. To your point on comparative advantage—I am sure others will have comments—what bargaining power do we have as we negotiate a deal?

Warwick Lightfoot: In terms of going forward with the United States post the EU, the most obvious area is what Dr Holmes touched on—agricultural products. It is worth just pausing and remembering that ever since President Kennedy started the GATT liberalisation trade round, the EU, or the EEC as it was then, and the United States have had an awkward trade relationship and it all turns on agriculture. The first trade row with the United States and Treasury Secretary Dillon was on frozen chicken. It is the food area where I think the United States will say, "Look, this is a very big sector of business. It's one where there has always been a niggle in our trade relationships with the EU and one where we would like to see genuine progress and a more liberal regime." You may have noticed that the US Under-Secretary of Agriculture spoke at the Oxford farming conference about 10 days ago, and he expressly mentioned that in the future that is an area of the trade relationship that he would like to see developed.

Q168 **Mr Jayawardena:** But because the US rules are based on sound science, our countryside is safe, isn't it?

Warwick Lightfoot: Yes. In terms of the safety of the countryside, I would perceive that as mainly to do with the use of things like GM crops in the United States, which are not used here. It is worth collectively reminding ourselves that many people involved in science and the practice of science policy have deep reservations about the way the EU

Commission has taken science advice. As you know, the chief scientific adviser and her team were disbanded precisely because of a controversy surrounding GM crops. The issue was this. The science adviser said, "Look, there may be cultural or political reasons why you don't want those kinds of crops, but I can't tell you for scientific reasons that they are dangerous and you shouldn't have them." Because she would not change the science advice, that set off the controversy, and, for example, Lord May, a former president of the Royal Society, former Chair of the Science and Technology Select Committee in the House of Lords and former chief scientific adviser—I think he was the first scientific adviser to the UK Government, and he was the person who drew my attention to this issue. I am not sufficiently alert to be on top of it because of my own activities, but certainly Bob May was very concerned about it, and it is a very good example of where concerns about safety arise and it doesn't seem to be consistent with the best science advice one can obtain.

Mr Jayawardena: Thank you.

Q169 **Chair:** That wasn't a leading question, was it? Mr Jessop, would you like to come in at this point?

Julian Jessop: Frankly, I would have given quite similar answers to all the questions so far, but I would like to add a few things. In terms of hard evidence of the benefits to consumers from free trade, as far as lowering tariff barriers is concerned, it is widely accepted that consumers are better off. I could point to any number of examples. Interestingly, I have one here from the UK Trade Policy Observatory—the Sussex operation—which suggests that if we were to lower our trade tariffs with the rest of the world, UK households would be £130 a year on average better off after Brexit. I could point to other examples from around the world. One is the downward pressure on prices throughout the west from the opening up of China and cheaper China exports. That part is well established and uncontroversial.

The other things are rather harder to measure. It is not just about price—it is also about choice and more competition—but many studies have shown that increased openness in trade is associated with improvements in productivity, faster economic growth and increases in living standards. And here, for perhaps the first and last time, I am going to refer to the Treasury research on the economic implications of alternatives to EU membership, which did include quite a few studies showing that increased openness of trade is good for the wider economy.

I wouldn't go as far as saying it is good for everybody. This goes to a very important point about Government policy making. I think Warwick was hinting at this. The impact of free trade is asymmetric. There are big benefits, but they are spread among a very large number of people, so the individual benefit to any one person might appear to be quite small, whereas the negative impacts are felt quite hard by a small number of people, who will typically be very vocal. They are the people who have the lobby groups behind them. They are the ones who make the biggest fuss. In practice, as long as the overall economy is better off, it is quite

straightforward to compensate those people in some way. There is overwhelming evidence from economic theory and economic history that trade barriers are a very poor way to protect jobs. There are much better ways to do that. We have a redistributive tax and benefits system, for example. If we want to have lots of farmers who are not very efficient for other reasons, we can subsidise them to be guardians of the environment, for example. We do not have to have consumers doing that through paying higher prices than they have to. I would say that overwhelmingly the evidence is that free trade is good for consumers, but you need some compensation mechanisms to protect those who would initially lose out.

Mr Jayawardena: Or to help them adjust.

Julian Jessop: Exactly. The New Zealand example on agriculture is a good one here. It was extremely painful for New Zealand agriculture, and maybe not enough support was provided through the transition period, but if we look at New Zealand agriculture now, the economy as a whole is unambiguously better off as a result of free trade.

Chair: We must remember to keep our redistributive tax and benefit system afterwards, and not erode it.

Q170 **Matt Western:** Dr Holmes, you were talking about enforcement mechanisms in relation to, I think, US car manufacturers and the US car market. Can you briefly give an example of how they differ between the US and the EU?

Dr Holmes: There is one small example and one broad example. I was at a meeting about TTIP where someone from Ford had said, "Look, we have different types of catches on seatbelts on either side of the Atlantic. No one has ever said that one is better than the other, but you can't use the one on the other side." Subsequently, people came out with studies saying that EU car safety standards are better. That can be argued about. The second point is that the ways in which car safety is assessed are different on the two sides of the Atlantic, if I understand it rightly. In the EU we use something called type approval certification. In the US they have what is called self-certification. There would be a fundamental difference in approach. If the UK were to adopt the US system, as one example, we would not then be able to sell UK cars into the rest of Europe.

Can I just follow up on a couple of points? I absolutely agree with everything my colleagues have said about the general benefits of free trade and lower prices to consumers. I don't think anybody disagrees with that, but a lot of people feel that most of those simple benefits have been obtained already. Tariffs are very low, except, typically, in one or two cases such as cars, chemicals and agriculture. My colleagues at the UKTPO have said there would be a big fall in prices if we adopted zero tariffs for everybody, but if we had a Brexit in which we were obliged to charge WTO MFN tariffs against the EU, there would be a rise in prices. The details of exactly what is going into your agreements determine the outcome.

As I say, the key point is that we are talking very much about regulation. The effects of a UK-US agreement would very much depend on whether,

to support the farmers and keep the Irish border open—I think we will come on to that—we have to have the same prices as the CAP.

Chair: That brings me neatly on to Catherine West, to move this section on a bit.

Q171 **Catherine West:** We would like you to expand on that, because that was our next question. If the UK is to have the flexibility to vary its regulations in pursuit of a new trade agreement with the US, it is suggested, for example, that it needs to sign an agreement with the EU that provides for regulatory equivalence. Could you talk about the likelihood of that?

Dr Holmes: This is very complicated. I was talking yesterday to one of the top people in the DIT, who worked on TTIP. He said that he was working on it for so many years and he still does not grasp it completely. I have been working on this even longer, but there is a caveat—a health warning—on what I say here. My understanding is that the EU is very strict on the conditions under which it allows goods to come in inspection-free from third countries, which we would be after Brexit. EU policy documents have made it very clear that they are reluctant to sign what are called mutual recognition agreements.

The key thing is not the harmonisation of standards and regulations, although that is important, but the circumstances under which testing and certification are recognised—this stuff about type approval certification versus self-certification in the US. That is the crunch point at the border. I think Warwick has a different view on this. My understanding is that the EU would only allow goods to circulate freely between the EU and the UK on what you might call EEA-type lines if the UK adopts, on a very strict basis, all the mandatory regulations on goods and the EU's method of testing specification, and if the UK gives some absolute supranational binding guarantee that those will be enforced.

I was speaking to a senior EU negotiator not long ago who said that there is no problem giving an MRA, but that the UK would have to agree to adhere to all the EU acquis in terms of goods, mandatory standards, and testing specifications to get that agreement. If we did that, we could not have an equivalent agreement with the United States. The EU would require that goods placed on the market in the UK could then sail across the border freely. If it was to accept that, we would have to be applying the same mandatory standards and the same methods of testing them that the US does.

Q172 **Catherine West:** Let us get practical. What actual steps would our Government have to take to reach an agreement on regulation that would satisfy both the EU and the US? You are advising the Government. What would you say if you had to write it down on two sides of A4? What steps do the Government need to take?

Dr Holmes: I am saying that I don't think you could have an agreement that allowed for mutual recognition of testing specification—I am sure you guys know exactly what that means, but most people don't. You could not

have an agreement on mutual recognition of testing specification that would satisfy both the ability to get goods in from the EU, and send stuff to the EU without further testing, and also for the United States. I think you have to choose which of the regimes you are going to adopt.

Q173 **Catherine West:** My next question is about Ireland. How deep would any UK-US agreement be if the avoidance of a hard border on the island of Ireland was achieved only through the full alignment of UK and EU regulations? Obviously for us as practitioners of politics, when you look at what happened just before Christmas, the Irish question looked as though it was going to be very significant in terms of the one-minute-before-midnight negotiation. For us, that really counts, particularly in the context of our current Parliament.

Dr Holmes: It really depends—again, it is a political question. The nuance I should put on what I have just said is that if the EU was willing to accept US-made goods coming in via the UK through Ireland, it is quite straightforward. But I think it will be very difficult, and the question then is: what do you mean by "regulatory alignment"? One thing that people have forgotten is that, in the 1990s when the EU was laying down the conditions for internal market access for the countries of central and eastern Europe, the Community—the EU, not just the Commission but the Council—adopted the principle that goods could come freely without further testing into the EU from the candidate countries, provided that those countries had adopted all EU product standards, although not necessarily the process standards.

For example, if before accession a furniture factory in Poland was doing something with nasty chemicals to its furniture, and those nasty chemicals were staying in a river in Poland and the furniture was free of contamination, it could then go to the EU completely freely as if it was an internal market. Once you become a member, however, you have also to apply the process standards, and those noxious chemicals could not be used if they were banned for use in the EU. That kind of regulatory deviation has been allowed in the past. I think the EU has actually tightened up further, but that is the kind of opening that you could negotiate.

Catherine West: That is helpful—a really good example.

Q174 **Emma Little Pengelly:** On the border between Northern Ireland and the Republic of Ireland, paragraph 49 of the phase one Brexit agreement indicates that the intention of the European Union and the British Government is not to deal with the issue by way of full alignment per se, but that that is the third best option for them. The first option is to deal with it in the context of the EU-UK relationship. So there has been a lot of discussion about full alignment and what that means. I note that it is specified in paragraph 49 in relation to particular areas—north-south co-operation, for example, and the all-island economy—but in relation to alignment, or compatibility, in terms of the UK-EU agreement it is presumably in both the EU's and the UK's interests to ensure that there is still a market. In terms of the industry you are across—we have heard

some of those—the UK will require compatibility, at the very least, because we will still need to sell into the European Union market. Although there has been a discussion about the different standards, presumably there is a pressure on both sides to find a pragmatic solution to what you have indicated around testing, for example, to make sure that that trade can continue at a much wider level than just a Republic of Ireland and Northern Ireland level.

Dr Holmes: One of the issues is that you have to think of it in terms of the border in Calais as well. Anything that would work in Ireland has to be capable of working in Calais. The Republic is not going to set up border checks with France. Obviously, stuff may go through the UK to get to France, but there has to be a degree of compatibility that would apply for the whole of the rest of the EU. The UK is going to be under very strong pressure to maintain alignment.

One of the things is that, as you said, UK firms want to be able to sell into the rest of Europe. There is a purely commercial practice. I was at a meeting in the north-east, where there was a guy from the chemical industry saying that the REACH directive is something that we are going to have to stick to if we want to sell. He said that, in third countries, coming in with the REACH certification gets us into third markets. There is the question of whether we are paying too much attention to producer interests and so on, but I think that there is a real issue there. There is an interest in terms of UK business being able to sell its stuff. Many countries that are outside the EU simply voluntarily adopt EU rules to be able to sell in. That is something that everybody is going to add.

Can I throw in one other thing, which we do not usually talk about in this context: anti-dumping? Tariffs are usually quite low and our standards are quite similar, but if we were to do what we are saying we are going to do, which is to have an independent anti-dumping regime, supposing that the EU puts 100% anti-dumping duties on steel and the UK, for political reasons, puts only 50% on, then we will have a problem at that border. We might just be able to get away with a 2% or 3% tariff difference, or even 10%, but when you have 50%, or if we do not have an anti-dumping duty at all, and they have 100% anti-dumping duty, someone is going to worry about that. That is something for the Committee. Apart from normal tariffs, normal trade and normal regulations, you have to worry about how you are going to deal with those exceptional things. By definition, where anti-dumping is put up, it is a politically sensitive issue.

Q175 **Emma Little Pengelly:** Surely it is also in the European Union's interest. We tend to talk about this issue as a British problem—I do believe that it is an issue much wider than the Republic of Ireland being one of the European countries—but from their perspective there is presumably pressure on the European Union in terms of the same issues that you have referenced around testing and access, because of the reliance on the United Kingdom in relation to the Republic of Ireland's trade.

I am going to make the presumption that the United Kingdom Government will not want anything to be unsafe. They don't dream that

they will not want a very high level of standards. In all of this discussion we have made this presumption about the European Union that, from our point of view in the United Kingdom, their high level of standards will continue beyond that and that there will not need to be that type of testing from the European Union market into the UK. In the context that we will presumably want standards to remain high, is it not in the European Union's interest, particularly from the point of view of Ireland—others who have a high level of trade with the United Kingdom—to find pragmatic solutions. It is not in the EU's interest to say that, ideally, they would not give a mutual recognition. In acknowledgment of the challenges—for example, the Irish border issue for them, as well us—they need to. It is in their power to move and be pragmatic about that, provided that standards are high for both partners.

Dr Holmes: Can I just come in very briefly? I know that others have very important things to say. In some sense it is a mirror image of the US. It will want to get its stuff into the UK and it will be asking the UK to ensure that our testing certification regime matches that of the EU, so they can get their stuff in. Clearly everybody has an interest in making that work. Also, when you say that the EU has a pragmatic interest, they absolutely do, exactly the same as the United States, but the EU—the member states—has a political issue. The integrity of the single market really matters to them in a way which we sometimes do not recognise. That is a matter of principle. German business is not going to tell the German Government to deviate from the principle of the single market for the sake of convenience in getting market access. They will be absolutely determined to get stuff into the UK, but in my view it will more likely take the form of saying that the EU has to press the UK to ensure that it is compatible with EU rules, rather than to modify the way they treat the single market.

Q176 **Emma Little Pengelly:** So in that sense they might be willing to sacrifice to a certain extent some of the economic arguments around, for example, Ireland on the border issue, for the principle of maintaining the single market?

Dr Holmes: I think there is an element of that, yes.

Julian Jessop: May I briefly come in on that?

Chair: Very briefly, time is galloping on.

Julian Jessop: You used the word pragmatism a number of times. I think political will is another way of looking at this. I understand why the European Union is wary of an invisible border between the north and south of Ireland. The risk is that goods cross the border that do not meet standards or bypass the common external tariff and so on. But if you are being pragmatic about this, to what extent is that amount of trade likely to threaten the integrity of the European Union or the single market as a whole? If there are enormous amount of oranges from Florida going across that border, competing with Spanish oranges, somebody would notice. You do not need a border guard there to spot that. That is one point about

pragmatism. The second is that, traditionally, the EU model of regulation has been a standardised, one-size-fits-all project, but in future I suspect they will be more willing to accept forms of mutual recognition where they will say that the thing that matters is the outcome, not exactly how you get there. So if we have similar but different regulatory frameworks that deliver the same outcome, I suspect that in the future they will have to get used to accepting those. This is a very difficult situation for them, because this is not the way that the European Union has developed. It has developed on a rigid one-size-fits-all approach, with no competition in standards. So it does require a mind shift on the part of the rest of the European Union and to some degree for us, as well. If the political will is there—ultimately I would like to think the politics is driven by the economics—I think, hopefully, we will get the right outcome.

Q177 **Mr Evans:** Let's stick with these oranges for a second. The Government do not want a hard border. So these oranges come into Northern Ireland. Let's say they are remarkably cheap—it is difficult in our minds to get around how much cheaper they could be than the Spanish ones, but none the less—and somebody from Dublin buys a load of them and tries to export them to France. I assume that somewhere along the line, all you would say to Ireland is, "There has to be an understanding that you will not export goods into the rest of the European Union that are not eligible," which would include Florida oranges. Could that work, or is that a total no-no?

Julian Jessop: I think so. I think a lot of the problems we have been talking about today can be solved by rules of origin or labelling and so on. If we think about agriculture, for example, if there is no human health reason to ban a certain product, I would be quite happy for it to be labelled. For example, you would have—I dread to say—a chlorinated chicken, and UK consumers could decide whether or not to buy them. Similarly, I would expect any product these days to have some form of labelling about where it is from. That would include oranges. If you have oranges that have no indication of where they come from, you are running into a potential hurdle straightaway about why you are allowed to sell them.

If you have oranges that have no indication of where they come from, you are running into a potential hurdle straightaway about why you are allowed to sell them.

Q178 **Mr Evans:** Yes, but there is a distinction between oranges from South Africa, where they think there is a health problem, and oranges from Florida, where they do not. It is just that there is no trade deal with the United States of America, so there would be a difference there. If they had to be labelled to come in and that label said "USA", could you be in a potential area whereby the European Union could do the odd spot check, or not even check? Let's say they see those oranges on sale in France, and somebody with a clipboard says, "Right, where did they come from? Dublin? Right", and then they fine that firm. Could they possibly do that?

Julian Jessop: I don't see why not. The key thing that we are trying to avoid on the island of Ireland is a hard border with the customs controls on that border, but there is no reason why you could not do spot checks away from the border, or at the point of sale, or at many other points along the chain.

Q179 **Mr Evans:** So that would deal with chlorinated chicken ending up in Paris?

Julian Jessop: Yes. There is a separate issue about chlorinated chicken around animal welfare—that is something else we could bring in—but as far as human safety is concerned, you need to be proportionate. There is no scientific evidence that chlorinated chicken is bad for people. Let people decide whether to buy it.

Q180 **Mr Evans:** I understand that the State Department are very angry about us focusing on chlorinated chicken because they say that the vast majority of their chicken is not chlorinated and it is up to our standards. They would prefer that we did not talk about chlorinated chicken because it is unlikely to end up here.

Chair: So you are upsetting them.

Mr Evans: Yes, I think they are upset actually.

Catherine West: Hormone-boosted beef, then?

Mr Evans: There is a double issue here. If welfare standards in America are lower, clearly the stuff coming into the United Kingdom could compete with the higher standards that British farmers are supposed to maintain, and they could go out of business.

Julian Jessop: There are a number of stakeholders. Obviously there are the British farmers themselves, but thinking about the people directly involved in the product, there are two sets of stakeholders: the people eating it and the animals that produced it. If it were only the people eating it who were at risk, and there was no scientific evidence that a particular product was dangerous, it would simply be a question of labelling. I am sympathetic to the argument, though, that there is what economists call an "externality" here, which is the poor conditions that animals are raised in. Although a consumer from the UK might benefit from lower prices, if the animal is very badly treated, I think that is a legitimate reason for the Government to intervene. But if it is only an issue of human health, and there is no decent scientific evidence that the regulations we currently have are proportionate, I would get rid of those regulations and allow the consumer to decide whether they wanted to buy hormone-boosted beef or whatever else it might be.

Q181 **Mr Evans:** I just want one clarification about this trade deal with the United States of America. I walked around Macy's once with a friend and I said, "Let's see where all the clothes are made". It was anywhere but the United States of America—Bangladesh, Peru, Pakistan, China, but not America. If we do this trade deal with the United States of America and we buy Gap clothes, which are made all over the world, how would that

work if we do not have a trade deal with one of those countries, such as Peru? Would it just come in tariff-free, if that is what the trade deal is?

Julian Jessop: My preference would be to do as many of these things unilaterally. I see no justification at all for us to have import tariffs if there is no health and safety issue, particularly if they are things that we do not produce at home.

Q182 **Mr Evans:** Two points, really. If we are doing a trade deal with America and we are buying Gap clothes—we have Gap stores here—and if we have not got a deal with the country of origin where they are manufactured but we do with America, do they still come in tariff-free? My second question is this: if they are coming in, do they have to come in via America? Or if they are made in Bangladesh, can they come straight from Bangladesh to the United Kingdom without touching America?

Julian Jessop: This is where the issue of rules of origin comes in, so I am happy to pass over to Peter.

Dr Holmes: Very briefly, you have to have a trade agreement with a country. Either you go down Julian's preferred route, which is no tariffs with anybody, or if you do have a positive tariff rate, you are violating WTO rules if you decide to reduce tariffs on some countries and not others. We have to have a trade deal with Bangladesh, Peru and all those other countries to import the stuff. It does not matter whether it comes in directly or indirectly—the FTA with the United States would only cover goods made in the United States. Can I just come back to something you asked earlier? Within the EU, it is a customs union and not a free trade agreement, once things are in they are not subject to any origin requirements. It is unthinkable from the EU's present perspective that goods that have come from a third country into Ireland would not then have free circulation in the rest of the EU. They must. A free trade agreement only applies to the partner countries. With the customs union, once goods have got in they have complete free circulation in the whole of the union. That is one of the principles of the single market that the EU is absolutely determined to preserve.

Warwick Lightfoot: Can I just come in? The question about Ireland and laws of origin goes to the heart of the future trade relationship with the EU as a whole, and also to the heart of the third-party relationships if there is a free trade agreement with the United States of America. It essentially boils down to this: something that is produced inside the United Kingdom can go to America without tariffs and with ease—not just something that has been produced here but something that has had an element of value added. Something that is made outside the UK, dragged in here and sent on with no value added would expect to pay whatever tariffs or obligations there are when it gets to the United States.

In terms of how trade is conducted, I have found the whole Brexit saga fascinating, because we have all been forced to engage with trade more seriously. Economists should know about tax, competition policy and trade, but because there are only 24 hours in the day, we are not as good

as we should be on those things. Now we have all been forced to engage with them, and it has been very interesting. There is what I call the "talking about trade" from trade specialists, civil servants and commentators, and there is trade as it is practised at the big ports.

Policy Exchange has put a lot of work in with the big ports to understand what goes on on the ground. There is no difference in practice between someone bringing something in from continental Europe or externally at a port. Barely 2% or 3% of loads are inspected. It is done on an intelligence basis, normally with a view to unlawful things such as firearms and drugs, or where there is a highly perishable good coming in and you might be worried about its safety—for example certain kinds of medicines or something of that character—where you really need to be on the case.

Very rarely, at Dover, Plymouth, Bristol or any of the ports around the country, are customs checking off every load as it comes in. It is all done on an intelligence basis, and a lot of things are done through the extensive powers customs have once it is inside the country as well. The loads coming in from the EU, funnily enough, are subject to just the same practice as loads coming in from the United States or South Africa, but because it is the same intelligence-base, particular worries are the same. We have to deal with the world as it is.

The other thing worth remembering is that the EU is not a closed world, and we will not be a closed world, and the United States is not a closed world. A huge amount of trade takes place without the assistance of trade specialists. For example, we have a huge amount of trade with the United States, and there is no free trade agreement. There is a huge amount of trade that goes into the EU from China and other countries, and they have developed their trade faster and further than perhaps the United Kingdom has, as a long-standing member, reflecting the underlying dynamics of those economies and the changing character of the fundamentals of comparative advantage involved.

One has to think about how trade is practised. Without wishing to nag you, do bear in mind that you want to have as easy a trade as possible—no tariffs, no restrictions—and a trade agreement where producers can get in there and reshape and reformulate it to their own interests might make things marginally worse, unless you are hyper-alert to what you are doing.

Q183 **Julia Lopez:** I totally agree. This is a question for Dr Holmes: the UKTPO suggests stronger intellectual property rights could encourage knowledge-based industries, while the Cato Institute refers to them as "by definition, protectionism". I wondered if you could explore that idea, outlining your point of view in a bit more detail, and what impact it might have on prices of goods and services for consumers.

Dr Holmes: UKTPO does not necessarily have a collective view. My view is that we need to be very careful about tougher intellectual property rights. There is a misunderstanding in this area, which assumes that a patent applies to a product. Most sophisticated products now are a complex of products, and patenting usually involves just a little bit of a process to

invent a new product. You do not invent a totally new product; you build on a previous one. The effects of tougher intellectual property rights are strictly ambiguous. In the software industry, a proposal to have patents on software was strongly opposed by software specialists in the United States because it meant that if they wanted to develop a product further, they couldn't do so without getting permits from all the other existing copyright holders. At the time, the UK Patent Office was very sceptical about the software patent issue. I have worked in this area but, like regulations, it one of those things where I hesitate to say what is the right answer—you have to be careful because it is very ambiguous.

Tougher intellectual property protection may give an incentive to someone to come up with something completely new, but it makes it harder for someone to develop a new product. All the great breakthroughs in software that took place over the past 30 or 40 years—the existence of a word processor, spreadsheets and so on—were done when there was no patenting on software. Software is patentable in the United States, and not patentable in the EU. The United States has actually rolled back a bit. A very important issue in the UK-US discussion is what we will do about intellectual property rights and data protection. I do not claim to be able to tell you the definitive answer on this, but one can say that it is absolutely not certain that incorporating tougher intellectual property rules into a UK-US agreement would stimulate innovation.

Q184 **Julia Lopez:** What about a UK-China agreement?

Dr Holmes: Well, I think most people would think that the Chinese are more likely to steal people's intellectual property, but what is interesting is that over the years, as China and India have evolved, they have become much more sympathetic to tighter intellectual property rights because they are now generating a lot. They are not just stealing; they are inventing, and they will be coming back to us. Huawei will be coming along and saying that one little bit of that British firm's new invention violates its intellectual property rights, and we will be faced with dealing with that. So be careful what you ask for.

Q185 **Faisal Rashid:** If the UK is unable to secure a significant agreement on goods with the US, perhaps due to the regulatory framework that we discussed earlier, what potential is there for a substantive free trade agreement on services?

Dr Holmes: The US has been quite resistant to including financial services in TTIP, and I do not think that the UK independently would find it much easier. For things like aviation and provision of services at state level, the US is not the easiest customer to get a services deal with.

Q186 **Faisal Rashid:** In 2016, in financial services alone there were £55.5 billion of exports from the UK, and imports were £11.7 billion. There is a surplus of £43 billion, and it is crucial for financial services in the UK to export to the United States. In the same year, the value of total exports of food, feed and grain was £20 billion, and imports were £42 billion. There is a deficit in goods, and it is crucial for us to emphasise services if

the talks on goods do not go the way we want. Is there any leverage in the agreement on services if we cannot get a better agreement on food?

Dr Holmes: What you have to remember is Trump's personal obsession with bilateral trade balances. It is very unlikely that the United States would—we have very little leverage against the United States. I think it's a misleading perspective that they have, but the fact that we appear to be stronger in financial service exports is not going to appeal to the United States as an argument as to why they should open their markets up further, I think.

Q187 **Faisal Rashid:** How does the UK ensure that any UK-US negotiations on trade and services do not become bogged down in questions about protecting the NHS, because that is crucial for us? What is your view on that?

Dr Holmes: My personal view is that we are going to have to follow the recent evolution of debate about this and make sure—actually, I think avoiding the inclusion of investor-state dispute settlement is the way to go. For example, in relation to the CETA agreement, I would say that that makes it very hard for investor-state dispute settlement to interfere with the way the NHS works, but there is a lot of fear. People are going to really object to it. There is no reason to include an investor-state dispute settlement that risks doing that. The problem with investor-state dispute settlement, which is what the debate has been about, is that it is out of control: it is done by private sector lawyers, who may actually be looking over their shoulder to which party is going to give them a future contract. So the simple answer I would give is: keep investor-state dispute settlement out, to avoid the risk of getting into that sort of issue. It's no good saying, "Let's sign an agreement that doesn't cover the health sector," because when it gets to a tribunal, the tribunal have a mind of their own and can say, "Actually, we think that this should not be treated as a public service; it should be treated as something else," and then you're lost. Keep ISDS out would be my simple answer to that.

Q188 **Chair:** Before we bring this section to a close, do the other two panellists have any views they want to share, particularly with regard to the NHS and ISDS?

Warwick Lightfoot: In terms of the NHS, you have to remember that at the moment US healthcare companies can come here and market their services to the private sector. There have been various initiatives. It's always a bit disappointing, because it is a very small sector and they don't have the expensive, rich pickings they have in their own domestic market. They would love to market things to the national health service, but the national health service is a brilliant health provider at containing its costs. The US companies speak with forked tongue: they want to be able to sell things to the national health service and then they complain it never buys anything because they can't actually meet the stringent contracting arrangements that the NHS quite rightly makes for drugs and things like that. So it's one of those markets that I think they would have very little traction over.

I think we have to have balanced tribunals for sorting out disputes that cannot go off to the races on their own. If a tribunal can completely change fundamental policy, there is something wrong with the arrangements. We will have to examine things like the Vienna convention on the interpretation of treaties to find routes to construct an appropriate tribunal.

I will finish with this. This is really about not what we can do for the world on trade, but what trade can do for us. Some people say, as Dr Holmes says, "Well, of course, you do realise that these tariffs are now really very low." I don't want to sound like Cardinal Morton, but if they are so low, why do you want to maintain them?

The other thing I will say is that there has been a very extensive and, in my view, defective literature from the London School of Economics, the National Institute of Economic and Social Research, Her Majesty's Treasury and now the Scottish Government on the impact of leaving the EU. One of the critical assumptions is that the United Kingdom would exit the EU, they would have a bit of a fracas, then the EU would impose tariffs on the UK, and the UK would then impose basic tariffs on the EU. And much of the welfare losses and all the damage that the modellers construct is through imposing those very low tariffs, so my answer to any trade specialist who says, "Darling, don't worry. These are very low tariffs. You can keep them," is, "Okay, if that's the case, why have all those modellers identified those very low tariffs when they were applied to EU trade in the future as the principal source of damage?"

Julian Jessop: On the NHS, often there is a red herring. Whenever we at the IEA propose any reform to the NHS, it is assumed that we want to move to the US model, which I think nobody in practice would want to adopt. As to the risk of having more US contractors bidding for NHS contracts, if those contracts exist, why shouldn't we make them available to as many people as possible who are willing to obey those rules? At the moment, of course, we have to make them open to bidders from the rest of the EU. Why wouldn't we include the US in that list?

As far as investor-state dispute resolution is concerned, I agree with Peter. It is not obvious that you need that arrangement within a free trade agreement, and if you did, why would you necessarily give that opportunity to investors but not to ordinary individuals, to consumers, for example, who might otherwise be affected? Overall I think that that risk is overstated. It is a theoretical risk rather than a real one. If a Government are coming up with a new regulation that is consistent with a free trade agreement or which can be justified as being proportionate to meet a certain aim, it is not obvious to me that an international court of whatever type would decide that it cannot do that. There are many fears that this would give multinational companies free reign to overrule what Governments are doing, but as long what Governments are doing is sensible, I see no reason why courts could not find in favour of the Government concerned.

Chair: Thank you very much, panel. Time, as ever, is up against us.

Thank you for your expertise and willingness to share it this morning.

Examination of witnesses

Witnesses: Howard Chase, Director of Government Affairs, Dow Chemical Company; Ian Cranshaw, Head of Business Development and International Trade, Chemical Industries Association; and Saoirse Fitzpatrick, Senior Advocacy Adviser, StopAIDS.

Chair: Good morning to our second panel. Could you introduce yourselves for the record?

Saoirse Fitzpatrick: I am the senior advocacy adviser from StopAIDS, a network of 70 NGOs working on the international HIV response. I am also representing Universities Allied for Essential Medicines and Just Treatment, a patient activist group.

Howard Chase: I am director of government affairs for the Dow Chemical Company for Europe, the middle east, Africa and India. I am based in Switzerland but I am a UK citizen, as you can tell from my accent.

Ian Cranshaw: I am head of international trade at the Chemical Industries Association.

Q189 **Chair:** Thank you all, it is good to have you here this morning. As an opening question: what is the significance of the US market for the UK chemical and pharmaceutical sectors? Who wants to take that on first?

Ian Cranshaw: I can just offer some brief numbers. The bilateral trade with the US in chemicals and pharmaceuticals in 2016 was £14.3 billion: £10.3 billion from the UK to the US and £4.3 billion the other way. So there was a trade surplus in goods in excess of £6 billion.

Q190 **Chair:** What threats do you see in the future to that? Do you see any threats given the change of status the UK might be experiencing over the next few years?

Ian Cranshaw: There might be threats affecting the UK, but we have seen a complete shift in US production, or rather they are on a journey to changing the nature of production in the US. The introduction of shale gas in 2010 was a game changer for the industry. Since then we have seen in excess of $180 billion worth of investment in the chemical sector. Clearly their capability is increasing. Their competitiveness based on cost will clearly increase. We then have the issues of the US Administration and a strong advocacy for "America First", bringing back some of that overseas manufacture to the US. Those are the things we are starting to watch and advise members on.

Mr Jayawardena: I draw Members' attention to my entry in the Register of Members' Interests. What could the benefits be to consumers from improvements to our relationship with the US? By that I mean: given that R&D spending by US pharmaceutical companies has been on the rise and the Chemical Industries Association has predicted that the UK would receive a boost from liberalisation of tariffs, do you think that could lead

to cheaper drug prices for consumers, and indeed for the NHS? If there was more liberalisation and companies were able to sell more, perhaps their profit margins would not need to be so high, and we might be able to negotiate a better deal from an NHS perspective.

Howard Chase: That reflects the earlier discussion you touched on about tariff and non-tariff barriers. Tariffs are essentially a tax that diverts resources from elsewhere. We could put those resources to better use. With non-tariff barriers you are into the business of standards, as you discussed earlier. I think there is no intent or interest in the chemicals industry in diluting standards in Europe. We can come back to that if it is of interest. Those are the two key points I would make.

Saoirse Fitzpatrick: I think the increase in R&D funding is not that significant if we maintain our current system for researching and developing medicines. We depend on market exclusivity to reward innovation, and that is what leads to higher prices. The way to get around that is to attach conditions to R&D spending. We want to make sure that if it is public money, the public get a return on that investment. At the minute, we had the NHS spending £1 billion last year on three treatments that were largely funded by the UK taxpayer. That is one thing we need to address.

Another issue is that, if a product comes from public funding, we should look at the usefulness of market exclusivity to reward that innovation, if it leads to a higher price. We need to build in some kind of access strategy to those grants for research and development. We also need to improve transparency. We do not know how much it costs to research and develop drugs. It is a very opaque matter and that makes it hard for us to negotiate a price. The list price at the end is also often not publicly accessible. The pharmaceutical industry like it that way, because it means they can charge us a higher price than they are charging other countries in Europe. We need transparency on that as well.

There are already some public interest conditions around R&D, but they are not implemented properly, and that is something we are interested in speaking to the Department of Health about at the moment. Basically, our conclusion is that the situation is not good at the moment, but anything we include in an FTA will be very hard to undo later on, and if we want to do that we will be at the liberty of trade sanctions.

Q191 **Mr Jayawardena:** Before I come back to Mr Cranshaw, can I just push a bit further on these suggestions for how the system could be improved? Do you think that, if your suggestions and those of others were to be taken on board, there would be increased potential for new SMEs to emerge and new ventures to be created because of the ability to either obtain different sources of funding or generate profits in a different way? Do you think that would stimulate new innovation?

Saoirse Fitzpatrick: Definitely. Look at de-linked models that the UK supports at the moment, like the Longitude Prize, which is a prize for a bacterial infection diagnostic. What I mean by de-linkage is that you are

de-linking the incentive of doing R&D from the price at the end. You are basically giving an upfront grant to an organisation rather than saying that they will recoup their R&D costs through a high price at the end. That is open to academic organisations and biotech companies; those kinds of thing open up the playing field for SMEs and other organisations and research institutions to get involved. You are then spreading the risk with those sorts of incentives.

Q192 **Mr Jayawardena:** I just wanted Mr Cranshaw to come back on the point he wanted to make, and perhaps to provide a counterbalance.

Chair: It had better be briefly and quickly, everybody.

Ian Cranshaw: We rightly recognise the US as a great innovator. It always has been and it has led the world in many areas of R&D. I would like to say that the UK chemical and pharmaceutical sector invests £5 billion a year in R&D facilities. That is one of the reasons why we pay such a significant contribution to the UK balance of payments. We export £50 billion a year from the sector, much of it because of the innovation that has been invested at the UK end.

Q193 **Mr Jayawardena:** Surely you would welcome an FTA, then, that allows you to do more?

Ian Cranshaw: Yes, we are a massive supporter of free trade and the removal of tariffs. Anything like that, which encourages business, has been proven to help industry develop—if done in the right way.

Chair: Interesting caveat.

Q194 **Matt Western:** What can we do today, outside of an FTA, to increase the trade in chemicals and pharmaceuticals between the UK and the US? That question is to anyone.

Ian Cranshaw: You have to maintain competitiveness. One of the areas of our concern, and our members' concern, is the differential on energy costs. We are an energy-intensive-user industry. It is a huge percentage of business costs. I was talking to a fertiliser producer this week—the only one in the UK. Forty per cent. of their entire business costs are energy, and we are at a massive energy disadvantage, not just with the US, as I mentioned, because of their shale gas, but with the rest of Europe, due to taxation and other rulings. We have to make sure that the UK is competitive on energy. Otherwise, we will not be competitive in the products that we develop.

Howard Chase: If I may add to that, my company, for example, is the largest chemical company in the United States but has a massive manufacturing footprint in Europe—in Germany, the Netherlands, Spain, and the UK, including a major plant in south Wales. The clear and important point is that it is a highly integrated business in Europe, and is competitive and successful in Europe at the moment because it is an integrated business. Everything that we make, if you track it, criss-crosses borders numerous times on the journey from raw material, to intermediate, to finished products, to final marketing, including branded

products. That is the way it works, and that helps to make Europe competitive, and will continue to make Europe competitive.

We should not speak about the US as different from the EU. We need competitive trade arrangements with both the European Union and the United States, which is the point that I think you all made earlier. How you manage that interface so that you do not damage competitiveness in Europe remains absolutely critical to our industry.

Incidentally, that is also true on energy, where the United States has a natural endowment of shale gas. The crucial thing for the chemical industry is not only the gas, but what are called the gas liquids within the shale gas, which are very good raw materials for chemical manufacture. In Europe, the integration of the European gas market, under the drive of the European Commission and some very distinguished British civil servants, has actually been very successful in making gas more competitive in Europe. If it is not quite as competitively priced as the United States, it is more competitively priced compared to what it would have been. I think the United Kingdom really has to think very hard about the integration of energy markets with Europe, and staying as competitive as you can be in energy going forward.

Q195 **Matt Western:** Just to pick up on the point about the difference between European energy prices, I think BASF in Germany is the largest global chemical producer. How does that compare to the UK?

Howard Chase: Again, I would distinguish between the two key energy sources: natural gas and electricity. In natural gas, it is not quite as competitive as the United States, but it is competitive, again driven by integration of the European market. In electricity, the European electricity markets tend to be balkanised—that is, separated into different markets—partly by renewables policy. You have different renewables policies in different countries, which are fragmenting the European markets. Governments obviously want to protect the subsidies that they have put into the renewable markets.

Over the next 10 years, Europe needs to work very hard on reintegrating its electricity markets. Of course, if you are looking forwards to a lower-carbon future and to a more digital future, all of that is driven by electricity. If you are going to be competitive, you cannot afford to have a broken up and fragmented electricity market.

Q196 **Stephanie Peacock:** How does the EU's approach to regulation of the production and sale of chemicals differ from that of the US, and are the regimes compatible?

Chair: Good question.

Howard Chase: Clearly that is a core question in this industry. The basic point is that they are different—perhaps even more so than is apparent on the surface. The European Union, as you know, through REACH and similar instruments, tries to identify the hazard and risk of products, and to manage them up front, effectively through a permit system. The obligation

is on the producer to provide the information that allows the project to be approved.

The situation in the United States is very different. I do not think that anyone could argue that it is less safe, but it is very different. In the United States, you have the full power of the courts in particular, which can make life very tough for you afterwards if you get something wrong—so actually you are aiming at the same thing, but coming in from very different directions.

Fundamentally we all agree that the idea of harmonising regulation between the EU and the US in the chemicals area is very far-fetched. We are looking for something much more like co-operation than we are at harmonisation.

Q197 **Faisal Rashid:** Mr Cranshaw, in a recent letter to Michael Gove, you wrote that leaving the EU's REACH regulation would "make a mockery of regulatory simplification". What did you mean by that?

Ian Cranshaw: From our perspective, if you were to design a regulatory system as of 2017-2018, you possibly would not design it as REACH is today. It was introduced in 2006. UK companies have had to comply with the sometimes onerous requirements of the REACH rulings. Given how much money has been invested in complying, you certainly would not want to risk diverging in any way from the REACH regulations moving forward. The importance is the size and value to the UK of the EU market. It is our largest single market: 60% of our production goes to the EU and 75% of raw materials come from the EU into the UK. So that relationship is absolutely key. Although we are here today to talk about US-UK opportunities, that always has to be in the bubble of recognising that getting the relationship with the EU correct is absolutely critical before you can even start to really think about the future relationship with the US.

REACH is a tome of huge information and requirements. As an industry we have welcomed those regulations. The industry is far safer now than it was. Incidents are down. Environmental impact is much improved. We have taken huge steps as an industry. In that time we have also pushed down our energy use while still maintaining production levels. As an industry we have got some pride in what has been achieved in the last 10, 12 years since REACH was introduced.

Howard Chase: As a US-headquartered company, I go along with everything Mr Cranshaw has said. REACH is not perfect, but if we are going to sell into European markets we have to be compliant with REACH. That was the origins. Being pragmatic, it then leads on to a couple of points. First, who decides? This is the agency question: the European Chemicals Agency. It is not just a regulation, but who monitors it, who holds the data, who implements it. The United Kingdom will have to sort out its relationship with the relevant agency. Will it be a UK agency? Will it go effectively to ECHA or will it do something similar?

The second point, which maybe echoes the discussion earlier, is that all of our modern legislation that you have passed in the United Kingdom relies heavily on delegated powers. So it is not just the primary legislation. In fact, nowadays, with my team in Brussels, 80% of their work is administrative decision making under delegated powers. You do not necessarily have flexibility on the primary legislation, but the United Kingdom can certainly look at degrees of flexibility in the implementation of legislation under delegated powers: legislation such as the industrial emissions directive, for instance, which governs emissions from factories and installations, where it is the local or national inspectorate that executes it rather than the European inspectorate. So the delegated powers piece needs to figure heavily on the agenda.

Q198 **Faisal Rashid:** What is the significance, if any, of other countries like China and South Korea adopting their own versions of the REACH regulation for future UK FTA negotiations, including with the US?

Howard Chase: I take a pragmatic view if other countries are heading more in the REACH direction. That is clearly very material to the standards you would want to have in the United Kingdom if you are going to be a world exporter.

Ian Cranshaw: As a trade body, we have recently completed some analysis of the regimes in place in the US, Mexico, Brazil and Korea and compared them to REACH. In canvassing all of our members' views, no company has suggested diverging from REACH in any way that helps their business.

Catherine West: I have a very quick question for Ian about production and British science. Many of us have received representations from academics, our own universities and universities in the region that might be affected by the coming arrangements with Europe. Does your industry have a view about how British science will be affected? There is some suggestion—it is not necessarily empirical, but it is a feeling—that Britain is already being dropped off EU grants and so on. Do you have a view on that, formal or informal?

Ian Cranshaw: Over the years, we have witnessed a change in the way that universities are funded and how they work with industry to promote R&D exchanges. One of our key Brexit asks is that we maintain an open border for skilled workers. If you think that 70% of chemical and pharmaceutical production in the UK is by foreign-headquartered companies, it is important that they have the ability to send their R&D staff—their very capable researchers—into the UK to collaborate with UK universities on joint programmes. It is absolutely critical that we maintain that access to talent.

Q199 **Catherine West:** Very quickly—this is my other favourite topic—on the Irish border. We have had a bit of discussion earlier about it, but what is your up-to-date view on the hard border, since the very exciting pre-Christmas negotiations? It looked as though that was a combination of our politics here in Parliament and the actual practical arrangements for

goods and services.

Howard Chase: It was fascinating to listen to the debate earlier, because this is where the rubber hits the road. That came across very clearly. All we can do as a business is point at the obvious points that you have already made, but I would add that the European Union as a customs union is not some sort of added extra or nice-to-have. It is fundamental to the nature of the union—you made that point very well—for the very simple reason that essentially, you control as you cross the border into the customs union and then goods can circulate freely within it, as you know. So it is the fundamental advantageous attribute, in my view, of the European Union.

That control of the border is clearly crucial in Ireland. To echo what Dr Holmes said earlier, you can do a great deal in terms of practical trade facilitation. Most customs checking is not done at the border, as you said, and all companies have computerised systems in place to track origin, transit, movement, payment of tariffs, standards and all the rest of it. You essentially take a pre-clearance approach, which can get you a long way in that direction in a practical sense, but whether you can build the practicalities in enough to give you something that you can rely on politically is not for me to say. I think that might the question.

Q200 **Julia Lopez:** In its opening TTIP position paper on chemicals, the European Commission noted that "neither full harmonisation nor mutual recognition seems feasible on the basis of the existing framework legislations in the US and EU". Is a mutual recognition agreement feasible in the context of a US-UK FTA on chemical and pharmaceutical sectors?

Ian Cranshaw: No sector is unique, so I would never try to suggest that. Howard and I have tried to explain the fundamental differences between our approaches. One puts the responsibility on the producer, while the responsibility in the other—in the US—is on the EPA to consider for themselves which chemicals are being placed on the market and what the impact might be, whether that is environmental or on health. I do not think that a merging or mutual recognition will ever occur, because there can be no meeting of those minds. From the outset, the starting point was very much the mutual acceptance of data and the avoidance of unnecessary duplication in the way that some assessments are carried out. Certainly, if there is data available following an involvement of animal welfare, we would not want to see that replicated. That data has to be held up and accepted as accurate and respected from both sides. There are some United Nations conventions and other global conventions on labelling and on packaging that the chemical sector could move towards. Those are the areas where we think industry ought to be recognising or looking at complying with each other's existing records. That will introduce efficiencies, including environmental efficiencies, and improve competitiveness. If the EU and the US, or the UK and the US, move in that direction, you expect global regulatory regimes to follow. We have seen that in previous questions about which other regimes are looking at REACH, and many of them are. We hold REACH up as a bit of a gold standard on regulation.

Howard Chase: You started with the TTIP work and we will start from the same place—a lot of very good work was done in TTIP preparation in that area. I think we have already echoed the point that harmonisation is a far-fetched question, and co-operation is a real pragmatic question. The paper you are referring to identifies four key areas, including co-operation in prioritising chemicals for assessment, and alignment of classification and labelling. That is particularly important for small and medium-sized enterprises. Big companies have the resources to label whatever, but classification and labelling really matters in the SME sector. Other key areas include co-operation on new and emerging issues, and enhanced information sharing. That is all about not duplicating and reducing testing and so on. Those would be very real gains from a UK-US agreement, which I think would be consistent with the EU relationship if done in the right way.

Saoirse Fitzpatrick: We definitely want to ensure that there is upward regulatory harmonisation if it does occur. For instance, the US patent criteria are slightly weaker than those in the UK and EU, but UK and EU criteria are nowhere near as robust as in India or Brazil, which are the biggest suppliers of generic medicines in the world. We do not include anything that talks about added therapeutic value when scrutinising a patent for a healthcare technology. The drug bulletin Prescrire did a study between 2000 and 2013 of 1,300 drugs. It found that only 7% had a real advantage that added therapeutic value, compared with existing compounds on the market. That is important.

Another issue is exclusivity, and the US patent is one year longer than in the UK. Data exclusivity is a huge barrier to access to generic medicines. We have it already and, as I said before, an FTA with the US would just enshrine that in law and make it harder to undo later on. Something positive that we should introduce since we are leaving the EU is a public health waiver on data exclusivity. At the moment, if something is protected by a patent, countries can use TRIPS flexibilities—they can file for a compulsory licence to get access, or to make or import a generic version of a treatment, but that doesn't include products that are protected by data exclusivity. Basically, there is a misalignment between national law, where compulsory licences exist, and pharmaceutical legislation, where issues of data exclusivity exist.

That is particularly important for biological drugs that cannot be patented because it is a biological process that is hard to do. Those biological drugs can still have market exclusivity under data exclusivity. So, for instance, if there was an outbreak of Ebola in the UK, we would need access to blood from Ebola survivors—that is the treatment, because that blood is full of antibodies. We would not be able to get access to treat everybody in the UK at the moment, because that is protected by data exclusivity and the cost would be too high for us to manage. A public health waiver would basically address the situation, and there is precedent for that—the US talked about it in its new trade policy in 2007 so it does exist. There is currently no mention of it under the EU, but we have an opportunity to introduce it with this FTA.

Q201 **Chair:** Given that the US may prefer more restrictive criteria for data protection and intellectual property rights in the FTAs, how do you envisage a US-UK FTA dealing with pharmaceuticals? I know you have complained about high prices in the past.

Saoirse Fitzpatrick: In a perfect world we would not include anything that was considered TRIPS Plus—that is anything that will extend the patent monopoly. That includes patent extension, which is when, if a patent is held up in the Patent Office because it is under scrutiny and they are wondering whether it should be awarded a patent or not, a drug company could apply for compensation, or extra years of a monopoly, to make up for it. That should not be included. Data exclusivity is something the UK and US already have in national IP law, but as I said, if it goes into this FTA, that's it—we cannot undo it. It is something we should be looking to do, because it is preventing us from getting access to more affordable versions of brand-name drugs. We are shooting ourselves in the foot there.

There is also a real risk with the US Administration, because Trump has been talking a lot about wanting to reduce prices. The thing is, the way he wants to do it is not by looking at drug companies. He either wants to increase the money that insurers would give back to patients for their out-of-pocket expenditure, or extend the monopolies of US pharmaceutical companies in foreign countries—in the UK, for instance, if we entered into this agreement. That is from a leaked trade document available on the Public Citizen site. It is something we need to be wary of.

The US also do not like the way that NICE do pricing. They think it is untransparent and unpredictable, and they also say that NICE should include patient voices when it is deciding on the price of a drug. That sounds great, but those patient activist groups are actually funded by pharmaceutical companies. The pharmaceutical company want the drug to be seen as cost-effective, so they fund those patient activist groups to go to NICE and campaign and say, "This drug is cost-effective," even though it might be at an extortionate price. They also want to get rid of reference pricing—the price that the UK or other countries pay and the final price for a product—because it increases the negotiating power of other countries, which would then get a cheaper price, meaning less profit for a pharmaceutical company.

I will also mention ISDS, which I know you were talking about previously—I am sure you will come on to it. We have already seen how the pharmaceutical industry have used that with Eli Lilly in Canada. They disagreed with Canada's patent law. Eli Lilly had two treatments that they said had new uses, one for schizophrenia and one for ADHD. The Canadian patent law disagreed that there was enough evidence to support the case that the drugs had changed enough to be considered a new product, so doctors were able to use them off-label for those two conditions.

Eli Lilly took Canada to court through the ISDS and wanted £500 million. Late last year, the court case ruled in favour of the Canadian Government and they have now had to pay damages, but it took years and millions and

millions of pounds wasted in a process that was basically Canada trying to protect its country's public health, and Eli Lilly deciding, "No, our profits are more important than that." There should be no inclusion of ISDS in a trade deal.

The US and UK are the biggest opponents of coming out with a new framework for doing research and development. This is something that has been talked about at the UN for 20 years. *The Lancet* talks about it; the WHO and different bodies have talked about it. It is making more and more sense. If we have a situation in the UK where people have to do crowdfunding for breast cancer treatment and people living with hepatitis C cannot get access to the cure because it is rationed on the NHS due to the cost, we have a crisis. The Canadians are saying it, the Netherlands are saying it and other countries in Europe are saying it. We need to catch up and address that issue and, as the biggest funders of R&D, the US and UK should be working toward a new model for R&D.

Howard Chase: Can I just comment on ISDS, not to disagree, but to put forward another aspect? One of my roles is chairman of the industry committee for the energy charter treaty, which was largely a UK-driven treaty regulating international investment in energy in the 1990s and has quite a strong ISDS provision in it. Taking us back to where that started, it is very simple: if I invest £2 billion or £3 billion in an oil production facility in Russia and the Government takes away my right to use it, I have the right to go and claim compensation at the market value. I think everyone would agree that is a fair sort of approach. That was the historical origin of ISDS, and that need remains in large parts of the world—if I am investing in China, for instance.

Q202 **Chair:** Has that original principle been warped?

Howard Chase: Yes. That original principle would rarely go to dispute resolution, because everyone knows what the ground rules are, and that allows you to negotiate with Governments and get to better solutions before you—

Q203 **Chair:** But has the principle subsequently been abused?

Howard Chase: It may well have been. You have given some potential examples, but I am not an expert on that. Originally, ISDS was in TTIP proposals because, among other things, the US and Europe, being such a large part of the world economy, would have set the standards for dispute resolution going forward. There is a need for dispute resolution in major capital investment, but maybe not so much in the areas you are referring to. We may need to find a new balancing point in ISDS. It is not just about the system. It is not really about whether it is a court or a tribunal—or not only about that—but about what you are really trying to achieve through ISDS.

Q204 **Chair:** Thank you. We would like to go further on this, but it is Wednesday morning and we are coming up to Prime Minister's Question Time, and you cannot keep MPs anywhere at midday. Can I thank the panel for coming along this morning? There have been some very

interesting aspects raised and things that we will probably follow up later. I thank the three of you profoundly for your expertise and your help this morning. Thank you.