

# Scottish Affairs Committee

## Oral evidence: [Scotland and Brexit: Trade and Foreign Investment](#), HC 925

Tuesday 5 June 2018

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Members present: Pete Wishart (Chair); Deidre Brock; David Duguid; Hugh Gaffney; Christine Jardine; Ged Killen; John Lamont; Paul Masterton; Danielle Rowley; Tommy Sheppard; Ross Thomson.

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### Witnesses

I: Professor Andrew Scott, Professor of European Union, University of Edinburgh, Professor Graeme Roy, Director, Fraser of Allander Institute, Dr Maria Garcia, Senior Lecturer, University of Bath and Dr Kristen Hopewell, Senior Lecturer in International Political Economy, University of Edinburgh

### Examination of Witnesses

Witnesses: Professor Andrew Scott, Professor Graeme Roy, Dr Maria Garcia and Dr Kristen Hopewell.

Q1 **Chair:** Welcome to the Scottish Affairs Committee to help us out on the first session of Scotland and Brexit: trade and foreign investment. We are hoping to be able to pick your very considerable minds about some of these very complicated and complex issues. We have a series of questions we would like to ask you about the particular circumstances and issues surrounding Scotland.

To help us get started, who you are, who you represent and anything by way of a short introductory statement. I will start with you, Professor Roy.

**Professor Roy:** Good morning, Committee. My name is Graeme Roy. I am Director of the Fraser of Allander Institute at the University of



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Strathclyde. I do not have an opening statement but I am happy to answer any questions as we go.

**Dr Hopewell:** My name is Kristen Hopewell. I am a senior lecturer in international political economy at the University of Edinburgh. My work is focused on the politics of international trade with a focus on the US, China and other emerging powers like India and Brazil. Prior to becoming an academic I worked as a trade official for the Canadian Government where I was involved in trade negotiations, trade disputes and a variety of trade policy issues.

**Professor Scott:** Drew Scott, Edinburgh University, Professor of European Union studies in the School of Law and also Co-Director of the Europa Institute in the University. I should also say I am a part-time secondee to the Scottish Government advising on Brexit and a member of the First Minister's Standing Council on Europe.

**Dr Garcia:** I am Maria Garcia. I am a senior lecturer in international relations at the University of Bath, so I am the only one not coming from Scotland today. My research focuses on the politics of EU trade policy, contestation of trade and those types of issues.

Q2 **Chair:** Thank you. I am very grateful for you being very brief, it gives us more opportunity for questions.

Can I start with a general philosophical and practical question: how is it all going?

**Professor Scott:** It is very difficult from the outside to gauge how it is going but it does not seem to be coming to a conclusion very soon. I think there had been hopes that by June we would be in agreement on the exit settlement. That seems now very unlikely and, of course, the clock is ticking towards the end of March 2019 when the UK will cease to be a member of the EU. In my view there is perhaps growing concern that we have not reached the stage we hoped to have been in. Until we conclude the withdrawal agreement we cannot take forward new relationship discussions. The longer that is delayed the more unlikely it will be that the UK will be fit for leaving the transition period two years after we leave the EU.

**Dr Hopewell:** I concur. This prolonged period of uncertainty is destabilising. Two years after the referendum there still remains no clear plan or indication of what Brexit will look like and what form trade relations between the UK and the EU will take. As the article 50 deadline looms ever closer we are increasingly in danger of a situation where the UK is potentially crashing out of the EU, which is something that would be profoundly damaging to the UK economy.

**Dr Garcia:** I agree entirely with my colleagues. In a way it is not entirely surprising. Normally trade agreements take years and years and years to negotiate so it is not surprising that these things have become so complicated so quickly.



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**Q3 Chair:** I have saved you for last, Professor Roy, because I note you published a report on Brexit and the Scottish economy. Could you talk us through a little bit what your conclusions are, particularly within the exporting sectors of the Scottish economy and where we do most of our exporting?

**Professor Roy:** The first point is about where we are. If you look back to where we were in 2016 you can see the economy—particularly the UK economy—has held up better than potentially the immediate outlook was at the time. However, the concern was always about the long-term implications for this. Looking at the data, we know the EU is Scotland's largest international export market by quite a significant margin, over 40% of Scottish international exports go into the EU. You can then look at what our key export markets are within that, things like manufacturing and agricultural products tend to dominate that. There are some interesting differences between priorities at Scottish level and the UK level in some areas.

What is becoming increasingly clear as we go through the whole Brexit process is that it is not simple to look at what the macroeconomic or sector impacts would be, but that each individual company will be different, depending on how they are integrated into their supply chain, what markets they operate in and who their labour force is. All of these things get really complex very quickly.

**Q4 Chair:** Does anybody have any other views about Scottish export arrangements and concerns, hopes, aspirations and opportunities?

**Professor Scott:** I think Graeme is absolutely right. The point I would make is that this is going to be about regulation. It is not going to be about targets and quotas. The other readiness we have to look to is how ready we are to continue to align ourselves with the regulatory standards. If you take something like food, the regulation of food begins when an animal is born, continues through its slaughter, to the food processing sector, to packaging and to export. It never was simple but it is very, very complex when we come down to the need for regulatory continuity to ensure that producers—food is just one example, of course—have certainty as to what kind of conditions of sale they will have.

It is very true that European Union consumers outside the UK will still want to buy UK products but the question is will we still be allowed to sell them in terms of regulatory compliance. That is a very, very important area we need to dig into very quickly and find out from our regulatory agencies what their views are about our readiness in that regard.

**Q5 Chair:** We want to come onto some of the regulatory issues too because you are right, those are very important. I might be being a little bit cheeky and maybe this is a question more for the end of the session, but what do you believe is going to happen in terms of a trading arrangement with the UK? Looking at where we are just now, what do you think is the



most likely outcome? I am looking to Dr Hopewell to help us with that one.

**Dr Hopewell:** That is an extremely difficult question. At this point we have no indication of what that relationship will look like whatsoever. Part of what is making it extremely difficult for business to do any planning about post-Brexit arrangements is that we have no clarity. We have so many different options on the table right now; whether the UK will ultimately form some kind of a trade agreement with the EU and, if so, what the terms would be, whether it will remain part of the single market through the EEA—the European Economic Area—like Norway, or whether it will potentially remain in the customs union or some customs-like arrangement like the customs partnership or maximum facilitation. All of those would involve a very different set of trade terms with totally different implications for business. One of the challenges for business is how do you make any forward-planning decisions when you have no clear picture of what the terms of trade between the UK and the EU, or between the UK and the rest of the world, will look like. You can imagine how difficult that is for business, especially when now we are looking at a period of potentially 10 months until we will be on some new sort of arrangement.

Q6 **Chair:** At the weekend in *The Sunday Times* there was a particularly frightening headline like queues at Dover on day one and running out of all sorts of things in the supermarket on day two. Is this something we should concern ourselves unduly about, Dr Garcia?

**Dr Garcia:** The stakes are very high on both sides. Clearly the European Union wants Brexit to be as orderly as possible. However, at the moment a customs arrangement, the maximum facilitation option, the UK has put on the table has not been endorsed by the European Union. As my colleagues were saying, there is very little time to come up with something that both parties are willing to accept and that will make life easier for businesses on both sides of the Channel. I think both the UK Government and the EU will try their hardest to avoid that cliff edge and that doomsday scenario.

There is another important point as well, you mentioned opportunities. Yes, in every trade agreement and in every change there will be opportunities. However, as Graeme was saying, it comes down to each individual business. Businesses that only operate within the UK or that are now replacing their external clients with UK clients might fare better than businesses that are still very integrated in supply chains in Europe and beyond. Of course, there is the other issue of the trade agreements to which the UK is party as a member of the EU.

Q7 **Paul Masterton:** Picking up on the customs discussion, is part of the issue that the sort of customs arrangement you need is intrinsically linked and dependent on the future trading relationship precisely because of the question of regulatory equivalence and acceptance within markets? Are we not looking at this back to front by focusing on what we need for



customs before we know what the future trading relationship is like? If there is an agreement on very high levels of alignment on, for example, goods but not on services, then the sort of customs arrangement you need to deal with that is completely different from the sort of customs arrangement you would need where there is not going to be continued alignment with goods. I am wondering whether we are getting ourselves all tied up in knots in customs when the focus should be on the future trading relationship, because until that is set you do not know what customs arrangements you are going to need.

**Professor Scott:** You are going to need customs posts. I suppose the question is what they will do. I take your point that the complexity of the customs process depends entirely on the variables you have set out but there will be a physical customs post at the external frontier of the European Union and, of course, the external frontier of the UK. The question then becomes how serious will be the burden on producers, on firms and companies when they confront that customs barrier, and how will different sizes and orientations of companies deal with the complexities they face.

You are absolutely right, if we are inside a customs union in the single market these complexities become relatively modest. You can talk about the ease of transport there with a formal barrier but nothing particularly onerous. The more we diverge, or the less comprehensive the agreement, then the more these complexities build up. It seems to me we are on a spectrum here. At one end we remain in the single market customs union, which is a no-change option, all the way through to a very crude, basic free trade agreement—if that is to be achieved by the end of 2020—and then build from that into something much more comprehensive over the next decade or two.

Fundamentally we will have a customs post and the question then becomes what burden will be placed on individual traders when they confront that customs post.

**Professor Roy:** I think your point is right. You can look at it in two ways. Thinking about future trading relationships, there is not just a future trading relationship with the EU but also internationally. If one of the opportunities of Brexit is to look at doing wider trade deals with more countries the challenge is that the more you integrate and the more you try to do trade deals with third countries outside the EU then the more significant the customs barrier has to become for trade between the UK and the European Union. Therefore it is a double-edged sword. You get the opportunity of expanding international trade to other markets but at the same time that then means the customs link between ourselves and the EU becomes more significant.

Q8

**John Lamont:** Thank you, Chairman. Before I ask my question, I want to follow up on that last discussion about the impact it was having on business and the need for businesses to have certainty. I spent a large part of last week during our recess meeting my local businesses in the



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Border, some are multinational companies and some are local companies, collectively employing hundreds of people. A few things struck me. One was how busy they are just now, they could not keep up with their orders and they have never known a time like it. I asked them what the biggest challenge was that they foresaw and none of them mentioned Brexit. I found that astonishing. When I challenged them on that and said, "Why are you not saying Brexit because that is what the press is saying and is what our colleagues will say in the Commons?" their response was, "Business is good at adapting. Business is good at dealing with challenges in the marketplace and adapts accordingly."

I accept Brexit is going to be a challenge. However, I wonder from the perspective of business whether this is more of an academic and theoretical challenge, which is perhaps being exaggerated, as opposed to the practical reality the businesses on the ground are facing and how they are approaching it.

**Professor Roy:** It is good news activity in your constituency is doing well, however, there are a few things concerning that. You are entirely right to say that for many businesses this is of secondary importance because they are operating in a domestic market, either locally within Scotland or across the UK as a whole. Therefore many will be insulated, at least directly, from any challenges there.

You can debate whether the scale of the potential challenge to businesses is significant or how significant it is. As much as you might have individual business examples where there are no particular issues, if you look at some of the challenges across the board—in sectors that are really closely integrated into global supply chains, rely on shared regulations for joint research, rely on access to skilled workers or access to migrants to come in and fill areas or rely on EU exports as being a significant source of revenue—it is hard not to see that will be challenging for them. What you potentially start to think about is what you do to try to mitigate that and also, for the businesses you are dealing with, where there are opportunities for them to try to grow into new areas either locally or internationally. A lot of this is about context and scale and for many businesses it will be a significant challenge.

**Dr Garcia:** I completely agree with Graeme's point. I would state that when we talk about "business" there is as an awful lot of diversity within business. I think you mentioned international companies, they are far more likely to have the resources to adapt and will adapt. Some small and medium enterprises will face difficulty in adapting, simply because they do not have the resources. I was at a meeting not with Scottish business associations but with those in my region. Things they were mentioning were SMEs not really preparing or even being fully aware of what is going on, simply because they are concerned with making their product and their day-to-day business. Companies who maybe have their client base within the UK, and are not necessarily aware of what their clients then do with their products as part of broader supply chains, are not fully aware of their exposure to Brexit or to potential problems further





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down the line. Larger businesses will probably be able to adapt and all of their competitors will be in the same boat. It might be costly but they can adapt. It is SMEs that we should probably pay special attention to.

**Q9 John Lamont:** I should point out it was a range of businesses, those that were global and those that were small. I thought it was quite striking that none of them mentioned Brexit as being their main challenge.

My question is about WTO rules and how trade between member countries has to be subject to the most-favoured-nation terms. I wonder if you could explain what that means in practice.

**Dr Hopewell:** Under WTO rules the most-favoured-nation provision requires a country to apply the same tariff rates on a given product to all WTO members. If you, for example, lower the tariff on one particular product you have to extend that tariff concession to all 164 members of the WTO. The idea is that you are not allowed to discriminate against other countries, you have to apply the same tariff to all.

The one deviation or exception from that is if countries enter into a regional trade agreement. If, for example, the UK were to enter into a trade agreement with another country you could unilaterally lower tariffs solely for that country without extending it to the other WTO members. However, the requirement is that that trade agreement has to be comprehensive. Typically the rule of thumb is that it has to include 90% of all trade and deep and meaningful liberalisation.

**Q10 John Lamont:** I guess my next question is also to you as somebody who is a former trade official. When you are negotiating a free trade agreement, what policy tools are available to you as a negotiator to achieve the agreement?

**Dr Hopewell:** The issue with trade negotiations is that they are reciprocal negotiations. In order to gain something in a negotiation your country has to be willing to make a concession to the other country. To gain something you have to be willing to give something. On tariffs you have to agree to lower your tariffs in certain sectors in order to make gains in the other country's market. Therefore it is important that any time you are seeking to make an advantage you have to be willing to cede something in your own market.

**Q11 John Lamont:** Is it quite important then that the negotiators have a good degree of freedom to make those types of decisions and to be able to negotiate freely? You need to have a degree of flexibility, so their political masters have to give them that ability to make those types of calls.

**Dr Hopewell:** Typically the political masters will set the agenda and form the negotiating priorities and objectives. The talks themselves become quite technical in terms of looking at specific provisions and text. There is a clear set of stakeholders domestically that can be business or society actors or subnational levels of Government that are often involved in that



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process of formulating a country's trade position, its stance in the negotiations and the direction that the negotiations go.

- Q12 **Christine Jardine:** Thank you. You were talking about trade-offs. How do Governments manage those trade-offs between wanting to use tariffs to protect domestic industries and negotiating tariff reductions? Is there an advantage in being part of a larger trading group? For example, is there more of an advantage to the UK in being part of the EU, to Scotland in being part of the UK and so forth?

**Dr Hopewell:** There is definitely advantage to size—the bigger the entity negotiating, the greater the gains to the other country. For example, several countries have indicated that if the UK were to try to negotiate agreements independent of the EU they would be willing to give less to the UK than they would to the EU as a whole. That is because the EU as a whole is a larger market and they stand to gain much more. Certainly if you are a smaller entity you have less leverage in trade negotiations. Ultimately trade negotiations are a political process. The more leverage you have, the more you are able to extract in concessions from the other party and the less you have to give yourself.

If we look at the multilateral level of the WTO, for example, in theory the WTO operates by consensus and every country has one vote. In practice, however, it is the most powerful states that dominate the WTO and effectively make the rules of global trade. Discussions take place among a small group of the most powerful countries and then are extended out to the rest of the membership. The EU has been one of the countries in that elite inner circle. The UK, as an independent entity, would not be. It does not have the economic clout or the economic might to be part of that elite inner circle at the high table of decision making. By leaving the EU, the UK would be diminishing its power in multilateral trade negotiations. If we look at Japan, to take one example, its economy is twice the size of the UK's and it is not a part of that elite inner circle so there is no reason to expect the UK would be. It would therefore be substantially diminishing its leverage.

The EU has been a fairly effective negotiating vehicle to date for the UK in international trade negotiations, both at the WTO and also in bilateral regional negotiations. The EU is the world's second largest economy and is a major economic power. Therefore it has been a heavyweight in international trade in a way the UK alone would not be.

- Q13 **Christine Jardine:** To go back to what Dr Garcia was saying in answer to Mr Lamont on the concerns of business, which I hear dearly, and about the implications for them of the UK and Scotland not being part of the EU. Would it be fair to take from that that their concerns are based on the impact on them of the UK no longer being part of that large trading body able to negotiate, particularly in the current climate, favourable or at least strong terms for trade and that they may be individually disadvantaged by the decision to leave the EU?





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**Professor Roy:** At a collective level the economics behind trade integration are clear. There is a lot of evidence that shows that countries coming together to trade boosts growth in the long run. It allows for specialisation and transfer of technological knowledge, it boosts the market size you are operating in, boosts productivity and innovation and allows certain parts of regional trading blocks to take advantage of strength in other areas where it might be at a disadvantage. A classic example in the Scottish case is the ageing population. We have benefited from the ability to have migrants coming to Scotland to address that. Of course, the distribution of these gains is not equal across the board. Collectively you might be better off but there will large distributions of gains and some people will be worse off. That fuels a lot of the concerns people have with globalisation in these trades.

The final point I would make is that there is a reason why countries tend to form trade relationships with their near neighbours, which is simply because it is costly to do trade. That is why the European Union exists successfully. That is why most of the other big trading blocks around the world are within countries that are relatively close to one another. Yes, you can do trade deals with different markets across the world but they would not be as cost effective as having strong relationships with your nearest neighbours.

**Professor Scott:** We are going to encounter this problem quite soon. When the UK leaves the EU in March 2019 it is unclear whether the 40 or so preferential trade agreements the EU has, to which the UK is currently a member, will simply be rolled over and the UK allowed to remain within them until the end of the transition phase at the end of 2020. That is unclear at the moment. That could be a problem very, very soon.

To augment what my colleagues have said, we also have to think about disputes and dispute settlement. As a member of the EU, the UK has a much higher level of protection against aggressive trade policies levelled against it. If there was a dispute over Scottish whisky, for example, then the entire muscle of the EU could be brought to bear on that international dispute. Take the UK out of the EU and you have a much smaller defence mechanism. We should not just think about the gains we make as a consequence of being part of a large trading entity, the EU, we also must think about the protection we get. That protection also can be extended to the behaviour of multinational corporations, for example. Again, the trade vehicle can be used as a way of leveraging behaviour that you find more consistent with your own values.

Q14 **Christine Jardine:** Another question I want to ask is about import quotas as part of trade agreements. First of all, what purpose do quotas serve and what would be the likely impact of the removal of tariffs and quotas on say the Scottish agricultural sector?

**Dr Hopewell:** There are very few actual quotas now in trade. Tariff-rate quotas are the primary instrument. The way that works is that a certain quantity of a given good below the quota level can enter a market at low



or no tariffs, above the quota any imports will face a higher tariff. These are primarily in the agriculture sector. The EU has 100 tariff-rate quotas on a variety of different agricultural products; beef, sheep, cheese, butter—a whole range of goods. Basically these are a mechanism to allow some imports into your market within the context of WTO rules but also to protect those sensitive sectors, which are primarily in agriculture.

**Q15 Christine Jardine:** Would the Scottish agriculture sector be less protected by these quotas?

**Dr Hopewell:** The issue with these tariff-rate quotas is that right now the EU has the tariff-rate quotas. With the UK leaving the EU those tariff-rate quotas will have to be somehow divided between those two entities. The UK and the EU reached agreement on their proposed method for dividing the TRQs. They submitted that proposal to the WTO. Their idea was to divide them based on historical averages, the usage of the quotas between the UK and the EU. They submitted their proposal to do that. The problem is that other countries are objecting to that proposed methodology. They are concerned that way of dividing the quota will effectively diminish its value to other exporters so they are already contesting this proposal. It looks like they are going to try to use this to expand the TRQs to both the UK and Europe. Essentially other countries are using this to try to exert leverage and to try to basically open up greater access to agriculture markets in the UK and the EU. This is an example of the political nature of these negotiations and the fact that other countries are going to be looking to make gains from the UK at every step along the process.

**Q16 Christine Jardine:** Does that go back to what Professor Scott was saying about uncertainty and not quite knowing where we are going come 29 March?

**Professor Scott:** Much will depend on what the UK position is towards farm policy once we leave. I go back far enough to remember the old pre-EU membership policy, which was a deficiency payment system. World market prices then augment the income of farmers by grants from the Treasury. Fast forward to the EU model, which historically was based on price support. Where will the UK find itself in the global trade policy discussions? How will that sit with the WTO partners with whom we are negotiating? This will be a very, very important part, particularly if we are targeting some of the countries that have been mentioned such as South America. These are main agricultural traders. Then we fast forward into the supply chain for food products in Scotland and how that then plays into the European market. This becomes a very complex set of negotiations because if we are generous with imports, from say South America, it will have a huge knock-on effect in terms of the food processing industry looking to mainland Europe as a market. These are highly difficult and complicated areas.

**Dr Garcia:** Beyond the complexities of supply chains there is also the issue of needing coherence between agricultural and industrial policy—all



kinds of policies—and trade policy. Somebody mentioned trade-offs. At the end of the day, when the UK negotiates with third parties they are going to demand something. In the case of the EU, at the moment one of the bargaining chips is agriculture. The EU, and the UK as a member of the EU, is fairly liberal in Government procurement contracts, much more so than other countries around the world. When they demand more access to Government procurement in other countries, other countries might want more access to our agricultural market or something in return. Government are going to have to explicitly think and decide what its negotiating structure is going to be vis-à-vis the EU, also vis-à-vis other countries, and what those bargaining chips are going to be.

A number of the countries that have been identified as future targets of trade agreements—including very friendly countries like Australia and New Zealand—will push very hard on agriculture and are already pushing for more access through the WTO with the tariff-rate quota issue. That is something that needs to be taken into account.

**Q17 Deidre Brock:** I want to ask about free trade agreements. They appear to treat liberalisation of trade in goods differently to those in services. Could someone set out for us why that is?

**Dr Hopewell:** Trading goods is relatively simple in trade negotiations. Typically the primary issue is tariffs, so it is a question of how much you are willing to reduce your tariffs. Services become more complicated. These are not physical items that are traded across borders, therefore services trade liberalisation typically involves granting rights to foreign companies to operate within your territory. It can also involve harmonisation of the regulation of services, and allowing things like recognition of licensing across different territories. For example, this could involve allowing banks or insurance companies to operate in another market or it could involve allowing the licences of professionals, like architects or accountants, to be recognised in another territory.

Another major aspect of services trade is often labour mobility. This is the cutting edge of services trade negotiations. This is a key thing that many countries are demanding in trade negotiations now, access for their workers to foreign markets. This can involve low-skilled labour, for example, farm workers, but it mostly involves high-skilled workers, engineers, software developers and other high-skilled professionals. This is a major demand of many countries now in trade negotiations. If the UK is to be involved in independent trade negotiations this is likely to be one of the key demands that it will be getting from other countries, to open up its market to the temporary movement of labour, and that is obviously a very politically sensitive issue in the UK.

**Deidre Brock:** Indeed.

**Professor Roy:** What is interesting from a Scottish perspective is that our economy is a service economy. The vast majority of our output is in services. Despite that, services account for much less of our export base



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because that is mainly manufacturing. Part of that is the reason that the trade rules around manufacturing are much easier to work through than they are for services, which are very complex and much more into non-tariff barrier elements.

The interesting thing is that the EU is not perfect at all in trade within services but one of the big improvements it has been doing over the last few years, and where it was going in the future, is to try to break down some of these barriers. In terms of the opportunities, close alignment or close access to EU markets provides an opportunity for a country like Scotland, as a service-based economy, to move in there through financial services, professional services and higher education. Things like that will be important for Scotland irrespective of what settlement we get, to have close access to potential integration within services.

**Q18 Deidre Brock:** Are there any other disadvantages or advantages Scotland will see from that particular liberalisation?

**Professor Roy:** In terms of services?

**Deidre Brock:** Yes.

**Professor Roy:** Another really interesting thing as well is that in the global economy the distinction between services and manufacturing is becoming ever more blurred. In the olden days we knew what manufacturing was, Boeing would build an aircraft engine and that was manufacturing. However, all the services that go around that now support the manufacturing of that. It is an additional complexity within potential future trading relationships. It is not just where you might be manufacturing something but where are the services that support that.

**Q19 Chair:** What services are you thinking about?

**Professor Roy:** Financial services. You buy a car; the car is now not just built by a manufacturer, there might be a finance service plan operated by that car manufacturer and you have your service plan to maintain an engine and so on. A large part of Scotland's oil and gas industry is now no longer about producing oil and gas but is about the supply and service chains that support that and go around that whole cluster that exists there.

One of the challenges with this is not just to think about the traditional sense of, "We export a bottle of whisky into the European Union" but the wider services that support that cluster and that network and how we can ensure we also gain advantages with that.

**Professor Scott:** It is legal services, insurance, and transport with lorries and trucks. It is also about how the reorientation might happen. There is an almost implicit assumption that if you lose one market you get another market. Internationalisation is complex and expensive for companies. If they have a market just now in say France, Germany or Italy and for whatever reason part of that market is compromised by



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Brexit, it is not self-evident they will find another market in Argentina or Canada. These are markets that companies have probably worked 20 or 30 years to establish. How they go about refocusing their international activities, if they do, I think will be problematic.

One of the consequences we are seeing, of course, is that service providers are setting up branch factories in mainland Europe. Universities are doing it, research centres are doing it, as well as lawyers, financial services and all the rest of it. We are seeing the beginning of this happening. We are seeing it across the UK generally, of course.

- Q20 **Chair:** On services, we note there are different definitions; the positive list, the negative list and then the hybrid list. What should we understand about this type of approach that the UK will have? The concern I hear from constituents in meetings is that all of a sudden the UK is going to be opened up to American privatisation companies keen to get into the NHS or water services. Would they be reasonably protected from that type of activity or is that something that should concern us?

**Dr Hopewell:** The positive and negative list has to do with the degree of liberalisation that will occur in your services sector. There are ways of indicating what specific sectors you will liberalise and what ones you will continue to protect. The idea of a positive list is a list where you explicitly stipulate the sectors you will liberalise. A negative list is the opposite, where you stipulate the sectors you will not liberalise. It has to do with trying to protect specific services sectors—for example, health or education—where you specifically do not want foreign entities operating in your territory.

That, again, comes down to a process of negotiation, the relative strength of the two parties involved in the negotiation. Certainly if the UK were to be in a bilateral trade negotiation with the US, particularly under the current US administration, we would imagine that would be an extremely difficult negotiation for the UK to try to protect its sensitive areas. It would probably be under considerable pressure to liberalise sectors that could be of commercial interest to US corporations.

- Q21 **David Duguid:** The phrase that keeps going through my mind since this whole session started is “more questions than answers”. We have heard from all of you that it is a very complicated topic.

I would like to go back to something you said near the start, Professor Roy, where you mentioned that 40% of Scottish exports go to the EU. It reminded me of a statistic I heard last week. I was looking at a table here from HMRC on regional trade statistics that lists fish and crustaceans, essentially seafood, as the third biggest export. The statistic I heard last week was that 88% of small pelagic fish landed in Holland is caught in UK waters and 90% of that is further exported to sub-Saharan and western Africa. That is export of primary processed food that then goes forward to secondary processing. Does that factor into that 40% or is that another layer of complexity we have not looked at yet?



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**Professor Roy:** The 40% number relates to the work the Scottish Government does each year to ask companies where they export to, where the destination is that they are selling into.

**David Duguid:** The final destination?

**Professor Roy:** The final destination for the company exporting. It could be part of supply chains, you could be exporting something to another manufacturer who then takes that and uses it somewhere else. It is purely in terms of the exports. The point you are highlighting is an example of complex supply chains that exist, where you might export something to another part of the European Union and that then becomes part of a much bigger supply chain and goes on. It happens the other way as well. Somebody might be importing something from the European Union to then put into a product that is ultimately exported from Scotland. A whisky producer imports sherry casks or something like that, it will be an import but it is to produce something that ultimately comes out as a Scottish export.

Q22 **David Duguid:** Then we get into the whole complication of provenance. The main question I wanted to ask was about non-tariff barriers to trade and I guess this is for the whole panel. How can these be dealt with in free trade agreements?

**Dr Garcia:** It depends on the willingness of the party. Non-tariff barriers are included in, and form a significant part of, free trade agreements. It comes down to this issue of regulatory alignment or independence, whatever you want to call it. You can have wonderful free trade agreements but it does not necessarily mean you have a significant increase in trade. You might remove tariffs but if your product is not able to comply with the requirements of the other market, regarding pesticides or the use of certain products to produce a particular food product, it is still not going to be able to come into the market.

Often what happens in trade negotiations is the parties will evaluate the procedures in the other party and decide whether they are happy to accept them. They might accept the way they produce apples but might not be happy with the way they produce beef for human consumption. They will give certifying bodies in the counterparty a certificate saying, "These apples are fit for market". They will recognise that and maybe not require additional certification but might not do that for beef.

It gets very individual depending on the party with whom you are negotiating, therefore attempts at greater regulatory co-operation or regulatory adherence have been quite challenging. The TTIP negotiations proved the extreme difficulty in terms of that.

**David Duguid:** You mentioned beef, which is a great example. When we had the BSE crisis—and foot and mouth—then certain markets, even within the EU, could say, "We are not going to buy British beef".





**Professor Scott:** It is really helpful to use the EU as a comparator. That case is provided for under the treaty where there is a threat of injury to public health. With the BSE crisis the rest of the EU said, "We believe there is a real threat to public health if we consume the meat coming from the UK" and the Commission agreed they could suspend imports of beef from the UK. We kept eating it ourselves but the rest of the EU availed themselves of that article. There is still an article in the treaty that says you can suspend free movement but you must show just cause. Ultimately it could be for the Court of Justice in the European Union to determine whether you have a just argument or not.

It is useful to compare what we call mutual recognition within the EU with what is sometimes called mutual recognition with free trade agreements. Mutual recognition in the EU simply says if a product complies with minimum regulatory standards agreed at EU level, provided it can be marketed in one country it can be marketed elsewhere in the EU. There is mutual recognition of national standards, subject to minimum essential requirements being harmonised. That does not happen anywhere else in the world in terms of free trade agreements.

What we may have is an agreement that the party to the agreement can have conformity assessment. They can assure the EU, for example, this product meets their regulations but they must meet the EU regulations before they are allowed to be brought to the market. For example, in the Canada agreement there is provision for mutual recognition of conformity assessment but that is not mutual recognition of technical standards. The Canadian standards are the Canadian standards. If they want to get access to the EU market they must meet EU regulations but a Canadian authority is able to validate that these EU regulations have been met. There is not mutual recognition of the technical regulations of the countries concerned, there is mutual recognition of the conformity assessment procedure in both parties.

**Professor Roy:** One interesting thing about non-tariff barriers is that an economy is changing all the time. Tariffs tend to be relatively obvious and relatively fixed over time. You put a tariff on that bottle of water and it does not really change that much over 10 or 15 years. The nature of an economy is always changing and it is the non-tariff barriers that tend to be an issue there. Roaming charges were not thought about 15 or 20 years ago. When the Uruguay round was going on, a lot of the big data IT stuff, which dominates our economies now, was simply not on the register of what we were negotiating back at the time when all these trade deals were there.

One of the things to think about from a UK perspective is not just the nature of the deal when it is done and the UK leaves the EU, but the future ongoing flexibility of that relationship so it can evolve over time to try to ensure that close integration. That is because one thing we know is that in a few years' time it will be out of date and barriers will naturally come up, not for any deliberate reason but because an economy evolves.



You need to have that ongoing dialogue and procedure in place to keep it flexible.

**Q23 David Duguid:** The EU's current position—again, going back to the fishing question—is that it would like a free trade agreement to be dependent on continued and guaranteed access to UK fishing waters post-Brexit. That is clearly not something that is going to go down well with fishermen in Scotland or around the UK. Is there any precedent for that kind of arrangement anywhere else in the world, or with the EU in fact?

**Professor Scott:** There is a general obligation for countries that have fishing waters adjacent to co-ordinate fishing policy. That is a general obligation. It is not a specific detailed outcome but there is an obligation. Norway, for example, discusses fishing policy with the EU. Although both policies are quite different, there is shared water so there is an obligation—I think, I am not an expert on this—under the Law of the Sea for countries who share waters to negotiate appropriate catching.

To go back to the regulation point briefly that Graeme raised, one of the advantages of the single market for countries outside the EU—for example, Norway, Iceland and Liechtenstein—is that they ultimately upgrade their domestic law to make it compliant with EU regulation. Therefore, if there is a change in the regulation coming out of the Brussels legislative system, that automatically is translated into domestic law in the three EFTA countries that are part of the European Economic Area. That is where this question of accountability comes in.

For countries that are not within the European Economic Area there has to be some arrangement made to both ensure compliance is continued, if that is the objective, and to verify compliance and govern any disputes arising from assertions of non-compliance. When the UK exits the EU and to the extent the UK seeks to keep regulations aligned with the EU regulations—we understand there are options on the table for that—it will be very challenging.

**Dr Hopewell:** I want to pick up on the fisheries issue. The issue of securing access to the EU market is a crucial one for Scotland's fishing and seafood industry. The EU applies a relatively high tariff on fish and seafood, the tariffs are as high as 24% on some products. As you mentioned, Scotland's third export to the EU is fish and seafood. About 75% of the UK's catch is exported to the EU. Therefore this is a crucial market for Scotland's fish and seafood industry. It is one where if, for example, we revert to trade-based WTO tariff levels it will face an extremely high tariff that could effectively block its access to the European market for some key products.

We know Norway's fish sector does not have the same kind of tariff-free access to the EU market that Scotland and the UK have. That is part of the reason why Norway moved a lot of its fish processing industry to Scotland. If Scotland all of a sudden faces a very high tariff on its exports



to the EU it could have profoundly negative impacts on the Scottish fish-processing industry. We may see Scotland's fish-processing industry move to places like Poland in order to access the rest of the EU market tariff free. That is why this issue is so crucial for Scotland's industry.

**Q24 David Duguid:** I have heard those concerns before. However, I have also heard fish processors in Scotland express a desire for as free trade an agreement as they possibly can have, but they do not wish that to be at the detriment of the Scottish catching fleet. There is a balance to be made there.

I have a question on the regulatory convergence we talked about. How do we square that with a devolution settlement within Scotland where a lot of the regulatory levers are devolved? What sort of frameworks would we need to ensure that the convergence with third countries does not lead to a divergence within the United Kingdom?

**Professor Scott:** This is a very big question to which nobody has an answer at the moment. You are absolutely right, devolution has assigned to the devolved Administrations in Edinburgh, Belfast and Cardiff certain competencies over regulations. There are many examples where regulatory differences exist within the UK. If the UK is going to sign international agreements that touch on these regulatory questions where there is devolved competence then there has to be a mechanism to reconcile the views of the devolved Administrations, who have the policy competence, with the position of the UK Government in international trade negotiations. That is a challenge that is made more difficult, of course, in the context of Brexit.

**Q25 Deidre Brock:** I will ask a question given we have experts here and this is something that has always puzzled me since hearing about the movement of goods across the border between the Republic and Northern Ireland. If Scotland exports a good into England—Grimsby, for example, to use something fairly topical—that is then processed in some way and exported back to Scotland, how are the export figures determined?

**Professor Roy:** There are two ways to do it. The Scottish Government's approach is to ask firms where they are exporting to, they rely on firms knowing where their export market is. For many firms that could be relatively obvious. For a large whisky company you are exporting so you know ultimately where that market is going to. However, within that you have the so-called Rotterdam effect. A lot of companies will export to a big port that then goes across the world, it might be exporting to an ongoing wholesaler who then takes the product on their behalf and ships it. That will bias the numbers because you are exporting into the Netherlands. The same will happen if you are doing that into the UK as well.

**Deidre Brock:** Exporting into what, sorry?

**Professor Roy:** If you are exporting into the Netherlands. You may be exporting to a wholesaler in the Netherlands who is then shipping your



whisky to different markets. If you are not selling directly to these on-markets, only selling directly to the wholesaler, then it will understandably show up as an export into the Netherlands rather than further afield.

HMRC has a separate approach. It looks at the returns of firms, where they are exporting to for goods, and then allocates that to where essentially the business is located. That is another way of doing it.

What you are also identifying is that increasingly companies—particularly small companies—do not make something themselves and then export it, they are part of a much bigger supply chain. You might be making a tiny widget that ends up going in a BMW car. The complexities of that and how they show up in the export figures are really complex and difficult to find.

**Q26 Deidre Brock:** In a way we do not really know, is that what you are saying on some of these issues?

**Professor Roy:** There is lots of stuff we do not know but we do have decent estimates of firms that definitely know where they are exporting to and those will be accurate. However, there will always be uncertainty.

**Q27 Chair:** For clarity for me, we see these numbers about how much Scotland exports to the UK as opposed to the EU and the rest of the world. If, for example—you were talking about the Rotterdam effect—a Scottish product is on its way to Europe but going through an English port, does that count as an export to the UK or an export to the EU?

**Professor Roy:** I get really quite excited about this, about where the Scottish exports show up. Essentially if a firm knows where the export market is then where it leaves the UK does not matter. If you are exporting a bottle of whisky to India and it leaves through Heathrow it is still—

**Chair:** A Scottish export to the rest of the world.

**Professor Roy:** Exactly, yes. If you are part of a supply chain that is exporting part of a product into the rest of the UK, which then makes up a much bigger product that is then exported internationally, it would show up as a Scottish export to the rest of the UK. Similarly, it could be the other way round. If a UK company was exporting something to Scotland to then make a Scottish product that was exported out, it would show up as a Scottish export.

**Q28 Chair:** I was surprised at just how much the exports are to the UK as opposed to the EU. That would possibly suggest why that number is inflated, if it is part of a supply chain and is labelled as an export to the UK that could push that up quite significantly. Do you have any idea what those figures might be?

**Professor Roy:** It could push it up but it could also push it down because you have the other effect happening as well. A lot of the Scottish



exports to the rest of the UK are services. They are the numbers that dominate and we know that they tend not be onward exported.

It is one of the challenges in measuring statistics that you find—this will be the same for the UK within the EU—you have really complex supply chains of products across the border.

**Q29 Chair:** Could you get these figures? Is there any chance of being able to determine what these figures are, or is it difficult to determine what would be part of a supply chain exported to the UK?

**Professor Roy:** It is exceptionally difficult to do that. What the Scottish Government does, to be fair, is they ask the companies themselves and say, "Where is the ultimate customer of the product you have produced?" They rely on them knowing that ultimately the market is overseas, within the UK or the domestic market.

**Q30 Deidre Brock:** I want to ask about future customs arrangements with the EU. The UK Government have recently proposed two possibilities, one being a highly streamlined customs arrangement and the other a customs partnership. Could you briefly explain the difference between those two proposals?

**Professor Scott:** "Max fac", maximum facilitation, is a proposal that would more or less aim to make trade as frictionless as possible, using sophisticated technologies such that traders could, if you like, register what they were doing without having to have a vehicle or a commodity examined at a border post. It would be using technology—number plate recognition and highly sophisticated IT systems—that would allow traders to plug in the information so when they got to the customs post there was very little, if anything, which had to be done. I understand from hearings in this house that the HMRC thinks that is conceivable over a number of years but the technology does not yet exist. However, this is something that I guess all international trade is working towards. It uses things like economic traders who are authorised—"trusted traders", if you like—and tries to extend that. There are difficulties, of course, for small firms that are involved in direct exports and imports that probably do not have the resources to do it.

This is a way to try to make trade as frictionless as possible. It could never be frictionless because, of course, you are going through an external border. There is an obligation under WTO rules that there has to be a border. The EU has an external border and the UK has an external border. "Max fac" is a way to try to minimise the disruption, minimise the lorry queues and make the passage through the customs post as simple as possible.

The customs partnership is slightly different. That would be, as far as I understand it, the UK acting as the agent of the EU to collect the EU level of tariff on goods arriving in the UK. If the good was destined for consumption in the UK they would then repay the trader the difference



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between the EU rate and the UK rate. That would, again, be a way of saying that anything that comes into the UK passes through the common external tariff of the EU and then payment is made to any domestic agent who keeps the product here.

The difficulty with that of course is it does not get around the problem of regulatory barriers, so if there are technical regulatory differences, a product may come in and the tariff can be paid and then remitted back to the trader if it is destined for the UK. The question then becomes what about the regulatory requirements of the product itself. If it is a vacuum cleaner coming in from outside the EU, does it meet EU noise level regulations and so on, which may be different from the UK? I do not think the customs partnership, in my view, from what I understand it—and I maybe do not understand it fully—answers the question of how you deal with the paperwork when it comes to regulatory divergences on goods moving between the UK and onward transmitted to the EU.

**Dr Hopewell:** I can speak to the max fac option, because the Canada-US border is one of the most technologically sophisticated; it is using cutting-edge technology. That provides a concrete example of how some of this might work in practice. One of the things that they have done on the Canada-US border is they have a pilot customs pre-clearance programme. The idea is that trucks/cargo will be able to be cleared before they reach the border, to facilitate movement across the border, so you do not get massive back-ups of trucks waiting to go through customs there.

The way this works in practice is that they put a customs officer inside a factory in Canada, for example, where a good is produced, and the customs officer will clear the goods in the factory. They use technology to monitor and to track the truck moving to the border to ensure that it does not deviate from its route. They also use an electronic seal on the cargo container to make sure that the goods are not opened or tampered with en route.

The issue with this is that you need the customs officer on the factory floor to do the clearance there if they are not going to do the clearance at the border. This is quite effective as a programme. It does help to pre-clear the goods; they get across the border smoothly and quickly. The problem, as you can imagine, is the costs involved. If you need to place a customs officer in your factory, this is something that is an option for big companies that are exporting a large volume of very high value-added goods to the US. In Canada and the US, it is primarily the auto industry that has been using this option. As you can imagine, for most companies, especially virtually all small and medium-size enterprises, this is not even a possibility.

There are technological solutions to try to facilitate trade, but they add immense cost and inefficiencies. At the Canadian border, this has not solved the problem. The Canada-US border still routinely has massive





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backlogs of trucks lined up for miles waiting to cross the border, so there is no easy technological fix to try to get goods quickly across the border.

- Q31 **Deidre Brock:** Neither of those proposals seems to sound very good at all. Are there any other types of customs unions that you think perhaps should be under consideration by the UK Government?

**Chair:** I think we are thinking of partnerships more than unions here.

**Deidre Brock:** Sorry, yes.

**Dr Garcia:** I do know of one example or at least one idea that was floated in New Zealand. I have not heard it in this context and I do not think it would necessarily be appropriate, but in order to cut down processing times once New Zealand products get to China, what the New Zealand Government suggested to the Chinese was to bring a customs officer to work in New Zealand. I suppose it is similar to what we have, the current arrangement under the Torquay agreement between France and the UK, so hypothetically you could have these products coming into the UK and you could have UK and European Union customs officers located here for those products that are coming in from abroad; some might be staying in the UK market and some might be continuing on to the EU. Again, this is costly. It would depend on both the UK Government and the European Union agreeing to this and of course there are also issues of sovereignty involved in this, which might be politically unpalatable.

- Q32 **Deidre Brock:** Is this still theoretical or this in practice?

**Dr Garcia:** I have not followed up on it. I am very happy to follow up and then send an e-mail on whether they have developed it.

- Q33 **Deidre Brock:** Can someone perhaps spell out for us what impact there will be on Scotland—or the UK generally, I suppose—failing to come to some sort of customs arrangement with the EU? What should we expect?

**Professor Scott:** Empty supermarkets, isn't it? The capacity would have to be increased. Obviously this is about capacity as much as about policy. I am no expert in HMRC and customs, but one imagines that there would have to be a massive increase in capacity very quickly if there were not to be the kinds of delays that could lead to problems of supply for firms. The just-in-time manufacturing sector is very vulnerable to this type of delay, so it would seem at the very least that there would have to be a very rapid increase in the capacity at the key border posts in the UK.

You could have dedicated border posts. There are examples in other customs union arrangements, where you may decide to have a dedicated customs post for a particular type of product and it could be designed to facilitate maximum speed of that particular product, a specialisation, if you like. There are probably tweaks that one could use to try to meet particular blockages, but I think the broad question is one of capacity and whether we have at present, or we plan at present, for the end of March next year or the end of December the following year, to create the kind



of capacity that we are discussing. Eight-mile-long truck queues are not something one imagines could be handled easily at the moment.

**Professor Roy:** Back to the answer I gave to Mr Masterton earlier, there is a direct inverse correlation between the amount of resources we need to go into dealing with our customs and the flexibility you would get to set new trade deals with other countries. That then has big implications for the types of sectors that benefit from that and would be at risk from that. If you want to have maximum flexibility to do quite sophisticated trade deals with third countries then, understandably, the UK and the European Union will want to be very careful about the customs borders that exist to make sure there is no entry through the back door. That will vary by sector, and will vary by the sectors that would maybe gain from accessing international markets outside the EU, whisky being a classic example of that. If you are able to do trade deals with countries that can move you in there, there are opportunities there, but for others, any form of customs border or delay has significant implications for you and that will vary sector by sector.

The other point I would make is it will vary also by size of firm. Kristen was obviously talking about small and large: small changes in costs for small firms will have a disproportionate effect and that gets quite difficult. Even in tariffs, some of the big companies do not even bother to worry about whether they want to avoid not claiming tariffs because it is so small, they can build it into their margins. One of the questions, thinking from a policy perspective and also a devolved perspective, is whether we have the infrastructure ready. If Brexit happens, the way it will turn out, do we have the basic port/airport infrastructure in Scotland to ensure that companies can continue to trade in a smooth way?

Q34 **David Duguid:** I have a very simple question, which may not have a simple answer. It was on the technological potential solutions for cross-border customs control. What—if anything—can we learn from, say, what is already happening at the borders between Norway and Sweden or Switzerland and all the surrounding countries? What could we learn from that that may help with the Northern Ireland question?

**Professor Scott:** Physical design. The Norway-Sweden border is interesting because it is designed in a way that maximises movement. You have colocation of the Swedish and Norwegian customs officials working together. Physical design is quite important. How this thing is designed for ordinary travellers, cars with private citizens in them—presumably that becomes a straight-through drive versus trucks with an entirely different procedure. Funnily enough, I think the physical design of these posts is incredibly important. I cannot talk to any particular example, but I suspect we could learn—and we should learn—from other border areas, such as Norway-Sweden or Canada-US, how they physically designed the real estate to have maximum throughput with maximum speed.



**Dr Hopewell:** It is important to note though that studies have shown that Norwegian firms still complain, even with the best possible conditions for making that border as smooth and as frictionless as possible. Norwegian businesses apparently complain that it is still an encumbrance, it is still a hassle and a delay to try to get through that border and it is impeding their flow of goods, even in the best possible circumstances.

Q35 **Ross Thomson:** The Scottish Government has proposed the idea that the UK leaves the EU, but remains in the single market and customs union, which is essentially staying in the EU. What impact would this have on the ability of the UK to set its own trade policy?

**Chair:** Professor Scott, you are probably best to answer this one.

**Professor Scott:** It would not be staying in the EU, just to clarify. There are three countries that are not in the EU that are in the single market. There are no countries outside the EU that are in both the customs union and the single market. Turkey is in the customs union with the EU, but not in the single market; Norway, Lichtenstein and Iceland are in the single market, but not in the customs union. Also, the customs union does not necessarily implicate certain policies, for example, farming and fishing. I will take them one at a time.

If the UK were to remain in the customs union, of course any product entering the UK from outside the EU and the UK would be charged the duties appropriate, set by the EU.

If the UK was in the single market, in terms of free movement, things would largely continue as they are. The four freedoms would have to be observed, there would certainly be a position for the European Court of Justice, and doubtless there would be a financial contribution as well.

In terms of the consequences of remaining inside the European Economic Area and the single market, we would have to adapt our laws to EU laws. We would no longer have control over setting those laws, which we do at present and so on. In that sense, the presentation of these options as the UK being a rule-taker is, broadly speaking, correct. Although it could influence these rules before they were formulated, it would not have any position in the legislative process.

The other downside of being in the customs union is of course that the UK would lose the ability, as you rightly implied, to negotiate its own trade deals with non-EU countries, and with regard to UK imports by those non-EU countries with which the EU had an agreement, they would not be treated as EU. The UK would find it would not necessarily enjoy the same privileged access to say the Japanese or South Korean market, as opposed to a free trade agreement, as the EU member states have at present. There are downsides to being within the EU customs union, within the single market, as not a member of the EU, which is obviously



why people say, "If you are going to do this, why leave the EU, because at least you retain the right as a rule-maker?"

Against that however, you have to ask the question: what is the alternative scenario. Will the UK be net better off by leaving the single market and leaving the customs union? Certainly all the analysis that I know about—with one exception, of course—implies that there is a cost. The cost can vary depending on the new relationship the UK has with the EU, but there will be a cost. I have not yet seen a study, with one exception, that suggests there are net benefits to be made by this strategy of leaving the single market and leaving the EU. All the studies that I have read, which I think are authoritative, suggest that there are significant costs to both the UK and Scotland. The Scottish Government published a paper at the end of last year setting out what they considered the costs to the Scottish Government would be, which I think struck the same chords as the Fraser of Allander Institute paper published earlier on this.

**Professor Roy:** Following up on that, I cannot stress enough how things will be different by individual sectors and individual companies. Being inside the single market or being outside the single market and in the customs union or being outside of all of that, the actual impact on individual sectors will differ. There has been discussion in the various papers around whisky, for example, because it essentially faces no tariff going into the European Union. Being outside the single market, but locked in the customs union, means that the UK could not try to negotiate new trade deals, which might help support whisky. That may be a sector that might prefer to be completely out of everything if you are going to be out of the single market. That is very much an exception with the individual sector, but obviously important for Scotland. I think understanding the complexities by individual sectors, industries and firms of the outcomes they get will be really important to be able to understand where the opportunities are, but also to be aware of potential risks that we need to try to mitigate.

Q36 **Ross Thomson:** Thank you very much. Both answers have been very helpful and it nicely leads me on to my next question. The Scottish Government produced the "Scotland's Place in Europe" paper, which said ideally they would want the UK to stay within the customs union and the single market, but if that did not happen, there should be a divergence, whereby Scotland could retain membership of the single market and the customs union. Professor Scott, you rightly looked at other examples, where Turkey is in the customs union, but not the single market; Norway is in the single market, but not the customs union. Is there any precedent at all for a sizeable integral part of a country—because it is the UK that is the member state—being part of a single market or a customs union where the rest of that country is not? Is that a route that you are aware of that any other country has gone down?



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**Professor Scott:** There are certainly many examples where parts of a country are a different customs territory for the purposes of the WTO and through that have different trade agreements, for example, Hong Kong and Macau, the Faroe Islands. These are integral parts of bigger countries, but they do have separate trade agreements and are recognised as such under the WTO. There is nothing unprecedented about part of a country being treated as a separate customs territory for the purposes of WTO. Indeed, if Scotland went down the path of seeking to remain within the single market and customs union—but the proposal was to remain within the single market—then it would probably have to be declared a separate customs territory. I suspect the same will be true in Northern Ireland: if Northern Ireland remains within the single market and customs union, almost certainly it will have to be declared a separate customs territory.

That is a technical issue. It is not anything of constitutional significance in the way we usually describe constitutional politics. It is more of a technical issue. There are precedents.

As far as the EU is concerned, there is no precedent for part of a non-member of the EU becoming part of the EU single market. Of course there are precedents for whole countries becoming part of the single market; we have mentioned Norway, Liechtenstein and Iceland before. Yes, this would be an unprecedented development. It was one that the paper you referred to sought to explore in the context of the UK Government.

I should declare an interest: I was part of the team that put that paper together. I do want to make that quite clear. I do not want to convince anybody that I am some independent observer of the paper; I was part of the team that worked on that paper. Yes, it would be unprecedented. It did not propose Scotland being part of the EU customs union; it proposed Scotland remaining part of the UK customs union, obviously with a codicil that the objective would have also been for the UK to remain within the EU customs union. That was the division. The reason for that was to avoid any obstacle to trade within the UK. Northern Ireland is an example where this, in my view at least, will have to happen, that goods and services, particularly goods, of course, traded in Scotland could be coming from either rUK or the EU. Scotland would be a jurisdiction in which regulations in both the EU and the UK would be legally compliant.

I think that is probably going to have to happen in Northern Ireland, because otherwise consumers in Northern Ireland would not be able to buy UK goods, which would be odd. I think that is what we call the Liechtenstein solution, because this happens in Liechtenstein, which is part of a customs union with Switzerland, but part of the single market of the European Union, and Switzerland is not part of the EU single market. Sorry, this gets into great complexity, I know, but some of us have lived with this for so long. This idea of a jurisdiction where regulations that are



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made in one part of the UK and regulations are made in the EU would both be legally compliant in that jurisdiction—I am sorry, it is quite—

- Q37 **Ross Thomson:** That leads me on to my next point, which was, as you have said, if there was to be an arrangement whereby Scotland still retained membership of the single market and therefore had to be compliant in relation to the regulations of the single market, implementing EU law and obviously accepting freedom of movement of people, where the rest of the UK was not, what impact that would have, one on devolution itself, but also with that trade with the rest of the UK, where you would have that divergence. Another aspect of it: you would have across the rest of the UK fishermen free to fish their waters outwith the CFP, and Scotland, part of the single market, tied into the CFP, which would be another interesting dynamic to that, what the impact on our fishing communities would be. What would the impact of such an arrangement be on devolution and also the rest of the UK?

**Professor Scott:** So not fishing. Norway is not part of the CFP or the CAP, so the proposals that were put forward in that paper, the December 2016 paper, fishing is not part of the single European market as far as the EEA is concerned, so fishing would not be implicated. The UK would retain control over fishing policy the way that Norway does under the proposal that came out in December 2016. The same with farming: farming would not be implicated, because Norway is not in the CAP. There are a number of other policy areas that are not implicated because they are not part of the single market programme or the European Economic Area programme.

The point I would make is in a sense is echoing a point that Graeme made earlier, that Scotland's needs from single market membership extend beyond trade. They include free movement, in my view. Free movement of people has been an essential bulwark of the Scottish economy, and indeed probably Scottish society over the period since we joined. Scotland's demographic challenges are significant and I am sure Graeme can speak to those as well. The population growth we anticipate going forward will more or less only come from inward migration and inward migration of employed people. We are not going to become the Sun Belt.

- Q38 **Ross Thomson:** That very issue about freedom of movement, you are absolutely right about the demographic needs. If you look at the polling though, Scottish public opinion is no different on the issue of immigration from the rest of the UK. I think where there is an appetite, it is not so much for freedom of movement of people, but freedom of movement of labour, whereby they know that people coming to the UK are coming with the certainty of a job and then to a conduit to public services, not to come to the UK without a job to use public services. What would the issue be if Scotland was part of a system whereby you had freedom of movement of people and the rest of the UK was not, in terms of that





issue between the border between the UK and Scotland? What questions does that bring up, if you have two different structures of immigration?

**Professor Scott:** There are two things I would say. First of all, freedom of movement is not without qualification. People do not have freedom of movement to seek social welfare. There is a three-month limit. If you do not find a job within three months, you can be asked to leave. There is no general right to move without employment. Freedom of movement of people is circumscribed by the law and European law is quite clear: there is no absolute right. You must move in the likelihood of getting a job. If you do not get a job, you can be asked to leave. The fact that perhaps the UK has not enforced that particular rule is for the UK.

The second thing I would say is that a number of countries operate—I am sure Canada and Australia are examples—policies where regional differences in immigration are permitted. Of course it is controlled through work permits. If you are availing yourself of free movement of labour to Scotland, then you would not be able to then go and work in England. It would be against criminal law.

We need to think about the legal system as a way to manage a complex environment such as the one that was being proposed in the December paper. The fear of labour moving to Scotland—if this were to happen under the rules of a single market—and that it would then drip into the rest of the UK and upset the immigration figures, I cannot say that would not happen, but the criminal justice system is there to ensure it does not. There are other checks. You have to demonstrate an ability to work, social security numbers and all the rest of it, so I think there are ways of constraining leakage.

**Chair:** These are some of the issues that we have been looking at in our immigration inquiry, so we are very keen to see your views on that when it is eventually published, which hopefully will not be too long.

Q39 **Tommy Sheppard:** I want to ask the same question, but from a slightly different perspective. It is a big hypothetical, but let's assume that there was a political consensus in London, Edinburgh and Brussels that it is desirable that Scotland should be able to stay in the single market. What technical changes would need to take place in order for that to happen? In particular, what further devolution of legislation to the Scottish Government would be required?

**Professor Scott:** I am sorry, I do not want to hog this, but we were quite clear in the paper that was published in December 2016 that this would imply a significant extension of devolved competencies. There is no question about that; there would have to be devolved competence to ensure the regulation of the single market was managed in Scotland. Already there are a number of agencies who manage the compliance of the single market—CETA, with environment protection, would be an example—but of course that would have to ramp up and the regulatory capacity in Scotland would have to increase dramatically in order to



assure the EU that we were complying with European regulations, food safety, pharmaceuticals, medicines and so on and so forth.

The extent to which that would be required would be dependent on the new relationship the UK formed with the EU, because we already know that there are many claims that the UK should stay within the European Medical Agency, aerospace and air transport and so on. It is the delta, it is the difference: where would the UK be in terms of compliance after Brexit and what would be the difference between where they are and the single market? Certainly we would have to increase the number of devolved competencies extensively—no question—in order to meet the obligations of single market membership.

**Q40 Tommy Sheppard:** In your view, if that were to happen, is there anything in that package that would prevent the United Kingdom entering into free trade agreements with other parties not in the EU?

**Professor Scott:** No, it would not prevent the UK entering into those agreements. There would have to be an agreement within the UK as to how their international agreements could be managed within the UK. For example, if the UK entered into an agreement that brought into the UK products that were not compliant with the single market, they could still be sold in Scotland. What they could not be is then onward shipped from Scotland to the rest of the single market. Scotland would be in the Liechtenstein position, where the regulations governing the sale of products in rUK would be valid in Scotland, as would the regulations governing the sale of products in the single market be valid in Scotland.

What could not happen, however—and this is where the administrative burden would lie—is segmenting those UK markets from the EU market, so that Scotland could not become a conduit, the same as Northern Ireland. This is exactly the issue that is going to arise in the context of Northern Ireland if the UK signs deals that bring in imports that do not comply regulatorily with the EU obligations, but Northern Ireland is part of a regulatory structure that is with Ireland, which is EU-driven, then there has to be a way of ensuring that Northern Ireland does not become a conduit.

**Q41 Tommy Sheppard:** People who are against the position of the Scottish Government would argue that it is not possible, because it would jeopardise the possibility of the United Kingdom making its own independent trade arrangements and any regional or sub-national decentralisation of the regulatory framework puts that at risk. Personally I do not understand it, because I think you can sign a contract with the United States saying, “Yes, you can bring all the chlorinated chicken you want, but if you want to bring it to Scotland, you will have to talk to these guys” because it is a different thing. You can build codicils into any agreement about what would happen. Am I right in thinking that—that it is possible to square this circle between having a decentralisation of regulatory activity within the UK, but that being acknowledged and recognised in any international free trade agreement?



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**Professor Scott:** You have raised a very profound question. The UK is a unitary market, but not a uniform market. In other words, the UK is a single market, there is no question it is an internal market, but it is not a uniform market. You can look at things like the minimum pricing of alcohol. It is now illegal to sell alcohol in Scotland at prices you could sell alcohol for in the rest of the UK, so we are a unitary market, but we are not a uniform market.

The question you raise about trade will emerge quickly, I suspect, because we can imagine GM foods, we can imagine fracking, we can imagine your chlorinated chicken example, we can imagine many circumstances where perhaps—and I am not saying this will be the case—differences across these islands will emerge between regulatory objectives. Regulatory objectives can differ for a whole raft of reasons. There can be differences in size; there can be differences in social policy objectives; there can be differences in value of human life. There are lots of reasons why countries regulate the same products in a different way. Within the UK that exists.

There is provision within the devolved agreements, as they stand, for diverging regulation. As I said before, we have seen it in a number of cases already. There is a very important question out there as to how differences between the devolved Administrations and the UK Government will be reconciled, should they appear, in the UK's international negotiations, for example with the US, when it comes to importing products. That problem already exists. It is not a problem that would be raised by the proposals set out in 2016. That problem is a problem and it is back to the legislative consent motion, it is back to the devolved powers of the Parliament, it is back to the structures that one suspects will need to be created to buttress the devolved settlements when the UK begins to negotiate internationally.

**Professor Roy:** I cannot comment with much authority on the policy aspects. The only point I would make is the importance of recognising what we were discussing earlier about integration with your close neighbours. Again, whatever constitutional settlement Scotland have in the future, its key trading market is the rest of the UK and its exports into the rest of the UK, about 60% of our exports go into the rest of the UK and companies operate very complex supply chains and many do not see a border between Scotland and the rest of the UK. Whatever relationship we have, whatever complexities about regulations et cetera, we just need to bear in mind the importance ultimately of economics at the end of the day and the jobs that are dependent upon not just trade with the rest of the UK, but trade with Europe and trade with other countries and the importance of ensuring that you can ultimately get demand, the benefits we talked about from innovation, from productivity, from training, because ultimately those are the things that improve prosperity.



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**Q42 Tommy Sheppard:** Do you see any problems for having good trading relationships between Scotland and the rest of the UK that might arise from having a divergent regulatory system in Scotland and to allow Scotland to have a different relationship with the single European market?

**Professor Roy:** The point I am making is just that anything where you have differences that potentially mean that businesses have to take different actions, whether positive or negative, will have economic consequences. You could have a situation where, if Scotland was in the single market, companies in the rest of the UK might find it more attractive to be in Scotland to access the single market, but equally, many other companies might also find that, "We are having to comply and ensure two different regulations" and it might be more costly. The point I am making is that anything where you have different divergence, as we will see with Brexit, as we start to go through that, means that you will have individual companies and firms taking different decisions and that will have economic consequences.

**Q43 Paul Masterton:** Some issues that Mr Thomson and Mr Sheppard picked up on: international trade negotiations and implementation of international trade agreements are reserved under the devolution settlement, are they not? Just so it is on the record, can someone say yes?

**Professor Scott:** Yes.

**Q44 Paul Masterton:** The key thing is that even though there are areas of regulatory divergence and devolution, the Scotland Act, since 1998, since the settlement and implementation of devolution, has contained a very clear provision that the UK Government retain the right to legislate any areas that are otherwise devolved competencies to ensure that the UK can uphold its international obligations. Presumably if you were in a situation where you did have this complexity of differing regulatory regimes, you had the UK trying to enter into new international trade agreements on a UK-wide basis, where there were elements conflicting with the new UK regulatory regime and the Scottish regime, fundamentally the devolution settlement, as it exists just now, would still allow for the UK Government effectively to legislate in devolved areas. It gets incredibly messy, very messy, but I suppose in terms of talking about the future upcoming Trade Bill, where the Scottish Government have clearly objected to certain powers being proposed by UK Ministers in relation to trade relationships, those powers already exist within the devolution framework as it stands. Is that not the case?

**Professor Scott:** Yes, absolutely. Both the 1998 and the subsequent legislation does not compromise the supremacy of the UK Parliament, but it also builds in the LCM process, where the UK is to legislate on issues that are devolved and they would normally seek an LCM from the Scottish Parliament, in our case. But you are absolutely right, there is nothing in the legislation that in any way annuls or compromises the ability of the



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UK Parliament to legislate anything for the UK as a whole. Sorry, I have lost my train of thought. I was going to come back to your second question.

- Q45 **Paul Masterton:** No, that was it. I was just trying to understand that although, yes, in theory you could have the UK entering into the USA as an easy example—whether or not it is an easy agreement is another question—but I do not think it is very likely that the USA is going to accept any kind of deal with the UK that eliminates Scotland from the market. I do not think that it is realistic to expect that any third country will enter into anything on that basis. But you then get drawn into, if Scotland was in the single market, a very complex system where could the UK Government then legislate on areas of devolved competence that then change the Scottish law from being aligned with the EU to what it needs to be to meet its new agreement and how does that pull together?

**Professor Scott:** Two things. If we go back to the December 2016 paper, the idea was not that Scotland would become a haven only for single European market rules; Scotland would be a jurisdiction in which either UK or EU regulations would be legally possible. If you were a producer in England and you wanted to sell your product in the Scottish market, provided you met the UK regulations, then it would be mutual recognition; it would be sellable, it would be tradeable in Scotland and ditto, single market could be tradeable in Scotland. What could not happen is Scotland acting as a conduit from which UK products that did not comply with single market rules could enter the EU and vice versa. It is not an either/or.

- Q46 **Paul Masterton:** I suppose the point I am trying to make is while you are suggesting it would not be an either/or, are there circumstances where it could be an either/or, where the level of divergence with the post-Brexit UK regulatory regime is so different from what the EU single market is doing that the two simply would not be compatible? I appreciate we are talking in hypotheticals all around.

**Professor Scott:** The answer to that question, directly based on our paper in 2016, is no, that circumstance has not been foreseen within the context of the paper. I would just like to go back to what we will face. There will be disruption, there will be cost. We know that. The question is where the balance is and how do we minimise the cost. In my view, Brexit will be costly. The question is how do we minimise in Scotland the cost that Brexit is going to encounter to the Scottish economy? My view then, and my view now, is that remaining within the single market is a way of minimising those costs, but that is contestable, I quite agree.

The important point that I was trying to struggle towards is that if the UK Government seek to conclude international trade agreements with third countries—and the EU will be a third country in those terms, post-Brexit—there is a question, a kind of constitutional question: how do they get the agreement of the devolved Administrations where their competencies are in play. If it is about the environment, do they seek the



agreement of the devolved Administrations to say, "Look, this is what we are proposing to agree with America. Are you happy with that? Will you give us the authority through an LCM to negotiate this?" or do the UK Government say, "This is reserved. We will negotiate"? I have no view on that; that is something the future will tell us.

The point I was going to make is that international trade is increasingly challengeable. We saw the TTIP collapse because the public were anxious about it. The public were anxious in this country about the National Health Service. Because the National Health Service has been opened up to competitive tendering, under WTO rules on public procurement, if you open it up, you may fall into that band. You do not have to open it up, but if you do, you may be subject to that kind of rule. What we saw—and I look to Kristen here—with the Canada deal with the EU is that the EU, I think it was, said, "We need to be sure you have a consensus in your country for this trade deal, because we cannot afford another TTIP round where people, anti-globalisation or whatever, are going to cause a political difficulty when we come to ratify this agreement".

- Q47 **Chair:** This is important, because I think we were talking about devolved institutions when it comes to these sorts of arrangements, but I remember the example of Wallonia, which seemed to almost get in the way of any sort of arrangement and agreement with the TTIP process. Scotland does not have anything like that sort of clout or authority when it comes to ratifying these arrangements and we would very much be expected to go along with what the UK says. Is my understanding of that correct?

**Professor Scott:** Yes, we saw this settlement almost come unstuck because of public opinion and some behaviour in Belgium.

- Q48 **Christine Jardine:** Going back to the chlorinated chicken, I take your point absolutely about the UK being a unitary market, but not a uniform one. It never has been. Even before devolution, we had different licensing laws, for example, in Scotland than England, so that would not be a problem.

I would like to pick up on a point you made about the business conditions that would affect companies. You might have a major supermarket chain that has a bulk-buying deal with somewhere in America for chlorinated chicken, for example—although I would not recommend it, but there you go—which was not sellable in Scotland. Can we face the situation where there were certain foodstuffs that were more expensive because Scottish supermarkets, as part of that chain, did not have access to a product and that their product lines were no longer available, several of them, in Scotland? Consumers could lose out in lots of areas, not just supermarkets, but cars etc, where there were different customs agreements and you would get into a very complicated situation that would not be to anyone's benefit.





**Professor Scott:** I think I have confused the issue here. If we are talking about the Scottish Government paper in December 2016, that problem would not arise because you would be allowed to sell in Scotland products that conformed to UK standards and products that conformed to EU standards, full stop, so it would be that Liechtenstein. Northern Ireland will be an example of that in the future. It would not be that chlorinated chicken could not be sold in Scotland for that reason.

Q49 **Christine Jardine:** So there is no protection against chlorinated chicken?

**Professor Scott:** That brings me to the second question, which is quite detached from all of the proposals and discussions so far, which is what if there is an objection in the Scottish Parliament to the sale of chlorinated chicken. How does that play out in terms of the UK's external trade agreements? I have no idea of the answer to that, but I do not think it is an inconceivable scenario as we look to the future.

**Christine Jardine:** Is that not Mr Masterton's question?

Q50 **Paul Masterton:** I was going to say that my understanding is that the Scotland Act 1998 contains an express provision that effectively enables UK Ministers to force change in the Scottish legislation.

**Professor Scott:** Yes, of course. Absolutely.

**Paul Masterton:** That is a position that has existed since day one.

**Chair:** The new assertion of sovereignty would allow it to do whatever it wants anyway.

**Professor Scott:** You are absolutely right. Constitutionally the UK Government could do that. I am just surmising the possibility—

**Paul Masterton:** Yes, but the political question is a different—

**Christine Jardine:** Yes, the political question.

**Paul Masterton:** —question, but the strength of the legal position is that there is nothing new being proposed here in terms of the Trade Bill, for example.

**Professor Scott:** Absolutely.

**Christine Jardine:** Yes, so potentially in that scenario you would have a similar situation to Northern Ireland in political terms, in that you would have an agreement that potentially could become unworkable.

**Chair:** Can we leave hypotheticals? I think we have exhausted this one. We have given it a good kick-around and we have managed to exhaust Professor Scott on some of these things, so we will move on.

Q51 **Hugh Gaffney:** Following up on the implementation period, the UK Government have said they intend to replicate the free trade agreements the EU has with other nations. How feasible is this?



**Dr Garcia:** My understanding is that the UK Government have already started discussions with the 50-plus free trade agreement partners that we have as a member of the European Union. It is going to be up to them whether they want those agreements to continue applying to the United Kingdom post the end of March next year. You might have access to more up-to-date information than I have. I do recall seeing some small report in the press about a country like Chile using the opportunity to ask the UK for some more access for its lamb to the UK market in exchange for agreeing that that free trade agreement will continue to apply to the UK. To a large extent, this will depend on the goodwill of third parties, on their individual dependence or interest in the UK market. The UK market is an important market, so all of the free trade agreement partners have—at least in principle—told the UK Government that they are willing to talk about so-called grandfathering of these agreements and continuing to apply them, but it will depend on them.

I have read some work by legal scholars in Belgium, arguing that maybe an exchange of letters might be more appropriate than copying and pasting those agreements, not least because of the timescales involved. We are not that far away from March, and if these are new agreements, even if it is just deleting “EU” for “UK”, they will have to go through parliamentary procedures and ratification processes in other countries, which can cause delays.

Again, other countries might not see it as a temporary measure and they might want to renegotiate certain things. The UK is an important market, but it is not the size or the importance of the European Union.

**Dr Hopewell:** I would add that it looks increasingly like most countries will want to renegotiate, that they will not be willing to let the UK just replicate, copy and paste agreements. Another example is Japan, which has already come out and clearly stated they will not be willing to just replicate the EU-Japan free trade agreement. They are going to demand more from the UK on labour mobility. They want more flexibility in terms of getting visas for their workers in the UK. They also are going to want a reduction in the UK’s auto tariffs and they are going to be willing to do less in their own domestic market on agriculture liberalisation. Another country, South Korea, has also indicated this as well. It is highly unlikely that the UK will be able to just replicate the deals it has now. It is going to wind up with lower quality access to foreign markets and have to give more in its own market.

Q52 **Hugh Gaffney:** That brings me on to my supplemental. Other countries may use this as an opportunity to renegotiate the terms of such agreements in their favour. How will the Government manage that risk? You mentioned that they are talking already to the 50-plus. Is that why they are doing this, to look at this risk? The EU could still block it, so it might be feasible and it might not be feasible.

**Dr Hopewell:** Another issue is that there has been a lot of emphasis on the UK regaining its independent trade policy and the ability to negotiate



its own trade agreements. There are reasons to question the value of that to the UK, ultimately. The reality is that the EU is the most valuable market to the UK. There is no way that you can ink free trade agreements with other countries that are going to compensate for loss in free trade with the EU. The EU is the second-largest economy in the world, the second-largest consumer market. It is right next door. That geographic proximity is a major factor in driving trade flows. There is no other free trade agreement that the UK could sign that would compensate for a lack of free trade with the EU.

**Hugh Gaffney:** If there is no deal, if there is no agreement, then the UK can be bullied by the EU.

Q53 **Ged Killen:** Turning to intergovernmental relations in the UK, which we touched on earlier, how have the devolved Governments been involved in setting the UK's negotiating position on trade issues so far in the Brexit process?

**Professor Scott:** I cannot speak for the Government. I feel I have a conflict of interest in answering that question. I think intergovernmental relations are moving forward, but I could not really answer the question in any detail at all, I am afraid.

**Ged Killen:** Does anyone else want to put forward a—

**Professor Roy:** I would not know how much the Government has been involved and how they have been influencing it. The bit we have touched on today that I think is really important is trying to understand the subtleties and where particular issues for Scotland might be more or less important within that context. We have spoken a bit about sectors, and sectors that are more important in Scotland than the rest of the UK, fish being a classic example, No. 3 in terms of Scottish goods exports to the European Union, but does not appear anywhere in the top 20 of UK-backed exports into the European Union. Whisky is again massively important in the Scottish context, but from a UK context, it is automotive that is a much more dominant factor there. There is something about sectors.

We also spoke a bit about migration as well and population challenges that are particularly important in Scotland there as well. I do not know how much the specific Scottish angle is being used or being influenced or being captured in the negotiating process, but I think that it is important, that the differences across the UK will be really quite important. That will be a key part of the negotiating strategy, to identify just how different the impacts will be across different regions.

Q54 **Ged Killen:** A Scottish Parliament Committee had recommended a Joint Ministerial Sub-Committee on international trade. Are there any views on the panel about whether a formal mechanism such as that is needed to incorporate the views of devolved Governments?



**Professor Scott:** There is no question that these intergovernmental forums are essential, all the more so because we are entering into totally uncharted waters. Of course, traditionally there has been a Joint Ministerial Committee on EU Affairs and there is now a Joint Ministerial Committee (European Negotiations), but we are now entering into a world we have never been in since 1973, if you like, and way before devolution. Institutional circumstances have changed so profoundly, even since the original Scotland Act was entered into force. These arrangements have changed so profoundly that there has to be now a complete refreshment and re-examination of how intergovernmental relations work if we are to proceed in a smooth and consensual manner. That is my own personal view.

**Professor Roy:** I think the one point that will be really important in that is the nature of that inter-government relationship. Is it just essentially a relationship, with the UK Government coming to Scotland, coming to Edinburgh and saying, "This is what is happening. How does it feel for you?" or is it a genuine, meaningful engagement where the Scottish Government or any devolved Administration have an opportunity to shape and influence the policy and the strategy, if that is in their interests? It is not just the design of having an institution. Is the institution going to work effectively, capture, and give the devolved Administrations an opportunity to genuinely influence policy?

Q55 **Paul Masterton:** Professor Hopewell, building on this theme about discussions between Westminster and Holyrood, could you briefly explain how Canada engages with its provinces when looking at their trade policy and whether or not there are lessons, perhaps both positive and negative, that we could consider from their experience?

**Dr Hopewell:** Canada is a federal state with the division of power between the federal Government and the provinces, with some matters of jurisdiction at the authority of the federal Government, some at the provinces and some split between the two. The federal Government have authority for negotiating and signing trade agreements, but they involve the provinces very heavily in that process. Their approach for incorporating the provinces had been ad hoc rather than formalised in nature and it has also been evolving over a period of several decades. Part of the rationale for involving the provinces in the process of trade negotiations is because increasingly these trade agreements involve, as we have been talking about, not just tariff rate actions, but these sorts of regulatory issues that can often be the responsibility of sub-national levels of government, such as the provinces. Those include issues such as government procurement, agricultural, environment, health, energy and labour investment.

In Canada now, most provinces have a trade team that has a chief negotiator that interfaces with federal Government to ensure that the interests of provinces are represented. Mechanisms are in place to consult with the provinces in real time, to discuss the progress of talks



and to see their inputs and their technical expertise. The primary mechanism for this in Canada is the Permanent Federal Provincial Territorial Trade Committee, known as the C-Trade Committee. I think this would be something similar to the Joint Ministerial Sub-Committee that you were mentioning. This Committee meets up to four times a year in face-to-face meetings. They also have supplementary teleconference calls as well.

There are similar consultative committees that exist on issue-specific areas. For example, there is a committee that deals specifically with agricultural trade issues and similar specialised committees for other trade issues. The idea is that discussions within these committees involve updates on progress in trade negotiations, trade disputes and other trade policy issues. This is supposed to provide a forum for ongoing dialogue that provides an important and permanent source of information on regional and sectoral interests and also ensures that the national negotiating position is one that is acceptable to all of the provinces as well as the federal Government.

In the case of the CETA negotiations, in that negotiation, the provinces played a particularly large role. They were involved in crafting the mandate for the negotiations; they provided inputs on their issues of interest and expertise; they had access to the confidential negotiating documents and they were extensively consulted throughout the negotiations. The provinces nominated their own chief negotiators to join the Canadian delegation. The C-Trade Committee that I mentioned, they met before every stage in the negotiations, every round of negotiations, and they provided the key forum for agreeing on Canada's negotiating position. The provinces were an integral part of deciding Canada's negotiating position.

**Chair:** It looks like very extensive engagement and relationships.

Q56 **Paul Masterton:** I do not understand quite the split of powers between the different levels in Canada, but in terms of pulling that over to the UK, obviously we are focused, as the Scottish Committee, on the Scottish Government. Would you maybe be envisaging, if you had something similar in the UK, that would also include, for example, the Mayor of London and some of the regional mayors, as and when there is more delegation of power in terms of England, from here out into the regions or are they another level down in terms of their equivalents with the Canadian provinces?

**Dr Hopewell:** They would be a different level. The Canadian provinces would be equivalent to the devolved Administrations in the UK, yes. In the case of CETA, the provinces had a seat at the negotiating table in the negotiation, so there was a very high degree of involvement by the provinces. Even in all other trade negotiations, the provinces have been extensively consulted.



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Q57 **Paul Masterton:** Could they veto or block it or were they there effectively more very actively engaged, but fundamentally as observers, rather than in terms of yea-ing or nay-ing the final outcome?

**Dr Hopewell:** The way the constitutional division of powers operates in Canada, the provinces would have the authority. The way a trade agreement comes to be implemented in Canada, the provinces have to approve in legislation any aspects that relate to provincial regulations, so if the province were not to enact those new regulations in their provincial legislatures, then it would not come into effect in the province.

Q58 **Paul Masterton:** So it is an effective veto?

**Dr Hopewell:** Effectively, yes. That is part of why it is so essential that the provinces are so actively incorporated into the negotiations in Canada and they agree to that common negotiating position.

Q59 **Chair:** There is no reason why that could not happen in the UK with our structure of devolved Administrations and Parliaments?

**Dr Hopewell:** I am not a constitutional expert on the UK, so I would have to research it.

Q60 **Chair:** Professor Scott is perhaps a little bit more of a constitutional expert, but there would not be a good reason why that could not happen, if that was—

**Professor Scott:** Other than the Scotland Act, which says it does not have to happen, but yes. It would seem to be a very sensible way to proceed, but of course the Scottish Parliament could not ultimately block an agreement.

**Chair:** Yes. I do not think there would be a desire to do that, but there does not seem to be any sort of conversation about the possibility of this happening as we go forward. Maybe that is something we could do, as we go through this inquiry—have a look at a more structured role for the Scottish Parliament and other devolved Administrations in all this. If there is anything that you could do, Professor Scott, to help us with that, it would be gratefully received.

Q61 **Paul Masterton:** Obviously in the UK Government you have the Scotland Office, the Wales Office, the Northern Ireland Office and then the Cabinet Office, which effectively then has overarching responsibility for the devolved areas. Is there an equivalent in the top level of Canadian Government of where the provinces have basically a seat around the Cabinet table or the equivalent of the Cabinet table? A lot of people would argue that Scotland's representation, Northern Ireland's representation, Wales's representation at the trading negotiation table is through their representation in the UK Government Cabinet.

**Dr Hopewell:** As far as I know, no. The provinces would be primarily represented through their provincial representatives in these joint federal provincial committees.





**Professor Scott:** It would also come down to who has the knowledge. If you are going to have serious negotiations, the people around the table, regardless of their constitutional complexion, must be the ones that have the knowledge. I would imagine in the case of Scotland, the Scottish Government and Parliament probably at this point in time have more knowledge than perhaps the Secretary of State has because of the sheer scale of the different offices, but that is a personal view.

**Dr Hopewell:** Yes. This is the key issue. The sub-national governments tend to be closer to their sectors and industries and they have a better sense of how potential trade provisions will affect their industries. In Canada, the auto industry is concentrated in Ontario, so it is essential the Ontario Government understands the effect of a trade agreement on the auto industry. The beef industry in Alberta, it is the Alberta Government that will understand that best and have that expertise. Bringing in sub-national levels of government can enhance the UK's position in trade negotiations because they will have a better understanding of the national interest.

Q62 **Chair:** I do not know how much you will be able to help us with this, but the geographical indicators, which are obviously part of the EU, I think we have all been quite surprised about the interest in this inquiry about the branding-related issues. We have seen the evidence that several of you provided about Scotland food and produce, the share of the exports that we have, particularly to the rest of the world. What is likely to happen to our geographical indicators? There are 15 products on the EU protected food name scheme. Have you any views about what might happen beyond Brexit, how these brands will be protected?

**Dr Garcia:** My understanding is that through the EU (Withdrawal) Bill, the UK will be putting into UK law everything, all the EU-derived legislation that we currently have, which would include the way in which we protect GIs. The European GI register has GIs that are not European; through free trade agreements, the EU has incorporated Korean GIs and they are in the register and they are protected within the European Union territory. In a sense, provided the UK continues to have that system, it would not change anything on the ground, it would not change anything or the protection within the European Union market.

In terms of what happens outside of the European Union, through its free trade agreements, the EU got partners to recognise some EU GIs. The number of GIs that are recognised in CETA or in the Korea agreement differs from country to country, so it can go from around 50 to 100 and something. There are well over 3,000 GIs in the European register. From a Scottish perspective, obviously Scotch whisky is the main one. I made a list of the other GIs earlier.

**Chair:** We had that list last week, so you are okay.

**Dr Garcia:** Wool etc, but they are not considered as sensitive; they are less likely to be imitated elsewhere.



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**Q63 Chair:** The key point with the bilateral third-party conversations, we are hearing, is that a lot of these third-party initiatives are not all that keen on GIs and would like to renegotiate. Given that our biggest export is Scotch whisky, is it a risk that we have to be aware of here? What would we be looking to the UK Government to do to ensure that something as important to the Scottish economy and the UK economy as Scotch whisky could be protected?

**Dr Garcia:** I think it will depend on whether the UK Government into the future, post-Brexit, decides to continue with the existing system. They will probably have to create their own register to re-register everything, because within the EU GI register, you can only be protected if you already have a GI registration in your country of origin. I suppose the simplest thing would be to replicate that and to create a UK register and just transpose all the existing ones into that and notify the EU that we would like them to continue being within the EU register. I am not the Government or future Government, so I do not know whether they will change their mind on that in the future. I am assuming that given the history, that we have adopted this particular system of GI protection and not the US trademark-based one, we will continue with this.

**Chair:** That is some reassurance, I think.

**Dr Garcia:** It might get complicated if we then have a trade agreement with the US and the US pushes for—

**Chair:** For a trademark?

**Dr Garcia:** —for their trademark mechanism to also be recognised within the UK. My understanding of CETA and other agreements is that you do not necessarily override the existing system, but you create a situation where trademarks and GIs can co-exist in a market.

**Dr Hopewell:** The EU has really been a crusader on the GI issue. They have been the key actor in the trading system, pushing for international recognition and protection of GIs. The issue is the UK, as a single entity, will have a lot less leverage in negotiations at the WTO, but also in bilateral and regional agreements, to try to get that recognition of its GIs abroad. Recognition of Scottish whisky and protection of that GI in trade negotiations will be much more difficult for the UK acting alone. It will have much less success, probably, in getting its demands met, than it would as part of the EU.

**Chair:** Thank you ever so much, you have been very helpful in helping us wade our way through the trade and Brexit minefield. If there is anything that you feel that we have missed, anything that you feel that you could help us with further—I think we asked Professor Scott to have a look at some of these issues—we would be grateful. We will probably be hearing from you again at some point, but thank you for this session this morning and for getting us started so well.