

ADS Group - Aerospace, Defence, Security & Space-

Written evidence FUU0015

SUMMARY

- 1.1 ADS is the trade association for the UK's aerospace, defence, security, and space industries. ADS has more than 1,100 member companies across all four sectors, with over 95% of these companies identified as Small and Medium Size Enterprises (SMEs). The UK is a world leader in the supply of aerospace, defence, security and space products and services. From technology and exports to apprenticeships and investment, our sectors are vital to the UK's growth – generating £79 billion turnover a year in the UK, including £46 billion in exports, and supporting over one million jobs.
- 1.2 The UK Aerospace sector is amongst the worst affected by the pandemic with over 15,000 job losses in UK aerospace manufacturing. Tens of thousands more remain at risk in the wider aviation sector, as well as companies in the interdependent defence, security and space sectors. Many of our member companies face continued threats to their future, given the ongoing impacts and restrictions. Even before any new measures at the border are put in place this month UK flight volumes have fallen to over 80 per cent lower than comparable figures from 2019 due to the pandemic¹.
- 1.3 ADS therefore welcomed the last-minute agreement between the UK and EU to ensure tariff-free trade from 1st January and regulatory cooperation in key areas such as aviation safety. The Trade a Cooperation Agreement (TCA) does not achieve everything ADS members were looking for, for example it does not go as far as it could have on aviation safety, the chemicals annex does not include access to the EU Chemicals Agency data, and it does not include a comprehensive defence and security partnership. However, when compared to a non-negotiated outcome, the TCA does achieve some positive outcomes and provides the basis for a deeper and more comprehensive relationship in the future.
- 1.4 The UK Government's decision to leave the EU's Customs Union, Single Market, and its agencies and institutions means that significant non-tariff barriers are unavoidable. However, the agreement could have gone further to minimise these barriers. For ADS members, this is particularly apparent in the areas of aviation safety, rules of origin, and chemicals. Further disruption could come

¹ [Daily Traffic Variation - States \(eurocontrol.int\)](https://www.eurocontrol.int/en/traffic-operations/traffic-variation-states)

in six months if the UK is not deemed data adequate by the EU, and when the UK starts implementing full import controls at the GB-EU border.

- 1.5 It is vital that the UK and EU continue to work together to overcome obstacles presented by the change in trading arrangements. For businesses in Northern Ireland in particular, the issue of goods defined as 'at risk' of moving into the EU is causing a significant degree of confusion and uncertainty. This submission outlines the key 'wins', issues and priorities for ADS sectors that have come to light in recent weeks in relation to trade in goods. The reality is that the EU is the UK's largest trading partner, therefore both sides must work together to deepen the relationship and strengthen regulatory cooperation in the medium to long-term.

2 AS OPPOSED TO OTHER POSSIBLE OUTCOMES, WHAT DOES THE PRESENCE OF AN EU-UK FREE TRADE AGREEMENT MEAN FOR TRADE IN GOODS?

2.1 Non-tariff barriers to trade

- 2.1.1 ADS civil aerospace members are not hugely exposed to rules of origin requirements as the sector benefits from the WTO Plurilateral Agreement on Trade in Civil Aircraft (it's worth noting that ADS is challenging the acceptance of a military equivalent airworthiness certificate). Where it does impact them is when importing raw materials from non-EU countries, which they would then export to Northern Ireland or EU Member States. ADS is still assessing the extent to which its aerospace members are exposed, but it appears that this may be a particular issue for members in Northern Ireland importing from Great Britain. Furthermore, ADS members operating in the defence/military goods sector are now grappling with rules of origin for the first time. It is likely that the agreement on bilateral cumulation, but not diagonal cumulation, within the requirements will lead many companies to simply decide to pay the necessary tariffs instead of relocating their supply chain. More information on the challenges this presents can be found in sections 3.1.2, 4.1.1, and 4.1.2.

- 2.1.2 When compared with a non-negotiated outcome, the presence of the TCA does reduce regulatory barriers. This is particularly important again for the aerospace sector where the UK's departure from the European Union Aviation Safety Agency (EASA) has the potential to cause significant disruption in the sector. The agreement on aviation safety and airworthiness annex provides for a level of recognition of each side's aerospace designs and products. It also provides the basis for greater levels of recognition and

cooperation going forward. Without this agreement both sides had put mitigating measures in place to avoid short-term disruption, but there was no certainty about the medium to long-term arrangements, which had the potential to do significant and lasting damage to the competitiveness of the UK's world-leading aerospace sector.

2.1.3 The other regulatory aspect of major interest for ADS members, particularly in the aerospace and defence sectors, is that of chemicals regulation, more specifically REACH. The TCA has not achieved much in this area as the chemicals annex does not include an arrangement for the Health and Safety Executive (HSE) to access data held on the European Chemicals Agency's (ECHA) database. Businesses producing and importing chemicals in the UK will need to register those chemicals on the new UK REACH system, while they will need to be registered on the EU REACH system for export to Northern Ireland or the EU. In order to re-register chemicals on the UK REACH system, companies will need to negotiate access to the data held by ECHA with the companies that hold those registrations in the EU. This is likely to be extremely costly and could lead to a reduction in chemicals production and supply in the UK. This does not differ from what would have been the case in a non-negotiated scenario.

2.1.4 The longer-term risk to industry is the level of regulatory divergence that the UK may undertake in the future away from EU standards. For example, in the UK's security and resilience sector a range of companies are active in the field of aviation security, which the UK was previously influential in shaping standards and regulations for at the EU level. The TCA sets out a shared ambition for the two sides to continue to cooperate in this area going forwards, but future regulatory divergence would pose a risk to future UK access to the EU aviation security market. This will incentivise UK companies to adhere to EU and international standards, not UK ones, and potentially encourage the basing of future investment in the EU. However, it is worth noting that the TCA's commitment towards cooperation and consultation minimises any immediate disruption arising from regulatory divergence as compared to a non-negotiated outcome.

2.1.5 While the issue of data sharing has been handled separately to the TCA, it is welcome that the UK and EU agreed to a 'bridging' mechanism for personal data flows for an initial four-month period. A wide array of UK companies doing business in the EU use personal data in their daily operations and it remains highly important for the UK to secure a data adequacy decision, so as avoid any interruption to the free flow of EU to UK personal data. Alternative transfer

mechanisms are available to UK businesses to safeguard against this, including standard contractual clauses, but these will generate additional administrative costs for UK businesses seeking to continue to do business in the EU.

2.2 Customs and trade facilitation

2.2.1 When compared to a non-negotiated outcome, the TCA does achieve some positive outcomes in the mutual recognition of Authorised Economic Operator (AEO) schemes. UK companies with AEO status will benefit from simplified customs declarations and paperwork when trading with the EU. The agreement does not remove the need for administration and customs documentation for goods moving between the UK and EU.

2.2.2 The agreement has established a framework for administrative collaboration and measures to combat VAT fraud. The Protocol builds on existing international agreements, including the OECD Convention on Mutual Administrative Assistance in Tax Matters. Without this the changes of VAT fraud taking place would be increased given the previous interconnectedness of the UK with member states. The agreement allows for the exchange of information that may help to affect a correct assessment of VAT, monitor the correct application of VAT, and combat VAT fraud.

2.2.3 The arrangement also allows for either Party to make a request of the other to recover taxes and unpaid customs duties, excise or VAT on its behalf. This is another example of the agreement enabling UK and member state authorities to assist each other in ensuring compliance and in protecting revenue.

2.3 Transport

2.3.1 A strong UK aerospace sector relies on a strong UK aviation sector. The inclusion of a comprehensive air services agreement that allows flights to continue between the UK and EU without quantitative restrictions on passengers or cargo is a positive outcome for UK aviation and aerospace. Again, the UK and EU had implemented mitigating measures to prevent immediate significant disruption in the event of a non-negotiated outcome, however the sector faced uncertainty about air services arrangements in the medium to long-term.

2.4 Public Procurement

2.4.1 When compared to a non-negotiated outcome, having the TCA in place provides a solid basis for UK companies to continue to tender for EU work, in so far as having an agreed, stable framework for

cooperation. The TCA provides for reciprocal access of EU and UK suppliers to each other's public procurement opportunities. More broadly, it will allow the UK to drive forwards with its proposed reforms to its public procurement regime as outlined in the *Transforming Public Procurement* Green Paper, following the replacement of the UK's use of the Official Journal of the European Union with the UK's new Find a Tender system. In comparison, a non-negotiated outcome would have still seen the UK become party to the WTO Government Procurement Agreement (GPA), which the TCA itself serves to incorporate. By being party to the GPA this limited the extent of divergence that the UK can undertake from EU public procurement rules in any case. The greater challenge for UK suppliers is primarily not their ability to bid for EU contracts under the TCA, but instead their relative competitiveness as compared to EU suppliers given the other trade barriers now facing UK suppliers.

3 WHAT IS YOUR ASSESSMENT OF THE RELEVANT PROVISIONS IN THE TCA AND THEIR IMPACT ON YOUR BUSINESS OR POLICY AREA? AND WHAT DO THOSE PROVISIONS ACHIEVE?

3.1 Non-tariff barriers to trade

3.1.1 Broadly speaking, the working capital demands that non-tariff barriers bring, as a result of the additional processing they necessitate, is a barrier to trade in and of itself. Companies have had to invest in new systems to deal with new customs formalities, employ the services of customs intermediaries, upgrade systems to deal with the new regulatory landscape, and undergo complex analysis of their supply chains in order to calculate the origin of the parts they import. Furthermore, companies are finding that the time it takes to move goods has increased significantly. One member has reported that a transit movement that took three days prior to the end of the transition period now takes seven days as a result of increased processes and procedures.

3.1.2 The rules of origin provisions in the TCA present a new challenge for many ADS members, particularly those that have no experience trading outside of the EU. As mentioned in section 2.1.1, ADS currently sees this having a particular impact on members in Northern Ireland – where they are importing parts and raw materials originating in non-EU countries for processing from Great Britain – and for companies in the defence/military good sector that are not covered by the WTO civil aerospace agreement. The requirements of supplying origin information are lengthy and difficult for some deeper supply chains. We are also aware that the agreement in place doesn't ensure that the customs officer in the country of import considers documentation to be sufficient which is often a risk the businesses cannot account for.

- 3.1.3 The TCA erects new barriers to trade in aerospace goods. While a member of the EU, the UK enjoyed the benefits of EASA membership. Aerospace companies in the UK had their designs, products and maintenance work regulated and certified by EASA, and then had access to not just the whole EU market, but also to markets with which EASA has bilateral agreements and working arrangements in place.
- 3.1.4 The TCA does achieve mutual recognition of each other's products meaning that UK companies producing aerospace parts can continue to sell into the EU with just an approval from the UK CAA.
- 3.1.5 In the area of design certification however, the agreement is asymmetrical in favour of the EU. This is reflective of the reality that the CAA is rebuilding competence and capability in this area as EASA has been responsible since its inception (while the UK was a member of EASA, responsibility for UK production and maintenance approvals was delegated to the UK CAA). The TCA facilitates mutual recognition of minor changes and repairs in relation to design certification, however each side will need to validate the other's type certificates and significant supplemental type certificates for the design of aerospace products. The asymmetry applies in relation to non-significant type certificates, non-significant major changes or repairs and technical standard order approvals. The UK CAA will automatically accept these issued by EASA, whereas EASA will validate those issued by the UK CAA. In the long-term, the agreement provides the potential for further levels of automatic acceptance in this area, which could remove the asymmetry from the agreement.
- 3.1.6 UK aerospace companies are experiencing challenges in having CAA forms accepted by non-EU countries with which the UK does not have a bilateral agreement or working arrangements on aviation safety. The UK no longer benefits from the bilateral agreements EASA has in place with countries around the world. While the CAA has ensured agreements are in place with key markets, such as the USA, Brazil and Canada, members are reporting issues when shipping to customers in other countries where there is no agreement in place, such as Russia, Australia and China.
- 3.1.7 Finally, a Specialised Committee for Aviation Safety will be established under the terms of the TCA. ADS has been told to expect this committee to focus on ensuring the agreement is applied consistently across the UK and EU, and that it will be responsible for agreeing further annexes in the future. An immediate priority for the UK aerospace sector will be a

maintenance annex as this is currently not included in the TCA. One ADS member with four repair and overhaul sites in the UK has reported that third-country maintenance organisation approvals with EASA (essential in the absence of a maintenance annex) will cost them €150k in 2021. A maintenance annex to this agreement would not remove the cost entirely, but it is fair to assume the cost would not be as significant as €150k.

3.1.8 As set out in section 2.1.3 the TCA does not provide a satisfactory outcome for REACH, which was the highest priority for industry in relation to chemicals regulation. The greatest burden is on access to testing data held on the ECHA database which will now need to be negotiated commercially and is likely to be highly costly.

3.2 Customs and trade facilitation

3.2.1 As set out in section 2.2.1, the TCA facilitates mutual recognition of AEO status. This is welcomed by industry as it will simplify the new customs declarations and paperwork that companies are exposed to following the UK's departure from the EU's Customs Union. However, it will, not remove the need for customs declarations and paperwork entirely. Furthermore, to successfully apply for and be granted AEO status is a complex, costly and time-consuming process. It is not easily achievable for SMEs, which make up 95% of ADS members, particularly given many smaller companies have no experience of dealing with customs formalities and would therefore find it challenging to pass the initial auditing process. For example, it took a major UK aerospace OEM six years to comply and successfully achieve AEO status.

3.3 Transport

3.3.1 As set out in section 2.3.1, the air services agreement is a positive outcome for the aviation sector, and in turn the aerospace sector.

3.4 Public procurement

3.4.1 The provisions of the TCA importantly provide for UK suppliers to continue to have access to EU public procurement markets (and vice versa). It widens the level of access that UK and EU businesses will have in each other's markets as compared to a non-negotiated outcome. While the TCA is narrower in scope than the EU procurement regime itself, the primary challenge that will face UK suppliers is their relative competitiveness as compared to EU suppliers. For that reason, this will place an increasing importance on the Government's export support activities for industry via UK Defence and Security Exports to ensure that UK defence and

security companies can continue to secure export opportunities in the EU.

4 WHAT, IF ANY, CHALLENGES ARISE BECAUSE OF THOSE PROVISIONS? HOW SHOULD THESE CHALLENGED BE ADDRESSED AND WHAT SUPPORT IS NEEDED, IF ANY?

4.1 Non-tariff barriers

- 4.1.1 For rules of origin, the main challenge for ADS members is that they have not previously had to comply with rules of origin requirements, and it is notoriously complex. Members have reported confusion within their own business as to which department is responsible for proving origin or providing the information related to origin. For the aerospace sector, the previously mentioned WTO Agreement on Trade in Civil Aircraft negates the need to utilise the origin provisions in the TCA, but this doesn't apply to raw materials and certain components far down the supply chain. Military goods are not covered by the WTO plurilateral and therefore members operating in the defence sector are now encountering rules of origin requirements for the first time. Many do not have the required sophisticated systems and software to calculate 10-digit level codes, or the information on the previous origin of goods that are needed in order to calculate content.
- 4.1.2 There is also a unique challenge for companies based in Northern Ireland importing non-originating goods from Great Britain. ADS has spoken to members that currently import raw material from Great Britain for processing into airworthy parts, which would then not be subject to tariffs if they moved into the EU due to the WTO agreement previously mentioned. Because the raw materials are being moved into Northern Ireland for processing, they would be defined as 'at risk' of moving into the EU and would therefore attract the EU tariff. This puts aerospace companies in Northern Ireland at a competitive disadvantage when compared to their counterparts in Great Britain and undermines the intention of the Internal Market Act "to ensure there are no harmful new barriers to trade between all parts of the UK." An example of this would be titanium bolts imported to Great Britain from the USA and then moved into Northern Ireland for processing. HMRC has suggested a number of actions businesses can take to avoid the tariff, however all of these options come with a cost of their own, be it direct or indirect.
- 4.1.3 ADS has a proposed solution on the Northern Ireland issue specifically. The UK Government should, through the UK-EU Joint Committee, seek to agree an exemption for Northern Irish aerospace companies importing parts and materials for processing into Northern Ireland from Great Britain. Aerospace companies in Northern Ireland should be able to use their CAA approval to apply

for a 'trusted trader' type status which would allow them to import parts and materials from Great Britain without having to pay a tariff. This could even be added as an additional criterion for approval through the UK Trader Scheme. This would avoid having to set up a separate scheme entirely. HMRC can audit these companies in much the same way as they would for other businesses authorised under the UK Trader Scheme and, given the aerospace sector is already highly regulated, this would not add a significant burden on the sector.

4.1.4 As previously mentioned, the aviation safety agreement within the TCA erects new barriers to the EU market for UK aerospace companies. The principle issue here is in relation to design certification and the new validation processes that will apply. Furthermore, the agreement on aviation safety isn't yet complete. The UK CAA and EASA need to negotiate the Technical Implementing Procedures (TIP) to support the airworthiness annex. The UK CAA has told ADS it expects this to take a number of months but is unable to put a precise timescale on the work. This is already having an impact on UK-based aerospace design organisations. Some have reported losing contracts as a result of the ambiguity surrounding the deal while the TIP is yet to be agreed, and others have reported being unable to fulfil contracted services for EU operators as they are now unable to self-approve major repairs outside of the EASA framework. The lack of a TIP means there is currently no route to securing these approvals. The solution here is fairly simple – the UK CAA and EASA must urgently agree the TIP, and in the meantime both sides should work to incorporate temporary working agreements or instructions that will assist industry in continuing to deliver certified products, rather than stopping work.

4.1.5 As mentioned in sections 2.1.3 and 3.1.8, the lack of a data sharing arrangement between the UK and EU REACH systems will add significant cost to companies looking to register chemicals on the UK REACH system. ADS has been told by DEFRA that the EU could not agree to the UK's data sharing proposals as it viewed access to the data as a right that should only be enjoyed by members of the EU's single market.

4.2 Customs and trade facilitation

4.2.1 The introduction of customs controls between the UK and EU will be disruptive for ADS members. To date, no significant disruption has been reported from ADS members, but with COVID suppressing demand and unusually low overall flow of goods between the UK and EU throughout January, it's difficult to know exactly how disruptive this might be in the short, medium and long-term. As

mentioned in section 3.2.1, mutual recognition of AEO status is positive for the businesses that are able to secure AEO status but securing that status in the first place is a challenge in and of itself.

4.3 Transport

4.3.1 The Agreement sets out continued market access rights for UK and EU road haulage operators. However, the physical process and coming to terms with new system and form filling requirements means this isn't as operationally easy as the agreement sets out. Members have reported increased transit times as a result of being held at customs borders for goods in transit where the interpretation of requirements by customs officials in the UK is different to the destination or transit member state. Understanding this and overcoming the challenges has been a priority for members and HMRC in recent weeks. Without an agreement or without commitment to discuss these issues, the problems would likely remain without resolution and create more significant long-term disruption to trade.

5 WHAT DO YOU IDENTIFY AS THE MOST IMPORTANT ISSUES THAT THE TCA LEAVES FOR FURTHER NEGOTIATION? WHAT WOULD REPRESENT A BEST-CASE RESOLUTION OF THESE ISSUES?

5.1 Non-tariff barriers

5.1.1 As touched on in sections 3.1.3 – 3.1.6, the UK and EU need to prioritise negotiations of the TIP to support the airworthiness annex of the TCA. Without this, there is no detailed outline of what should be automatically accepted, what qualifies for streamlined validation, what requires full technical validation, and how those validation processes should work. The ambiguity is already having a direct impact on UK aerospace companies. A best-case resolution would be temporary working arrangements to be implemented immediately that ensures companies are able to fulfil contracted obligations that existed before the end of the transition period while the more detailed and long-term arrangements are quickly put in place through the negotiation of the TIP. Ultimately the industry creates wealth by designing and building new products. The ability to get them certified needs to be a priority.

5.1.2 Once the TIP has been finalised and implemented, the Specialised Committee on Aviation Safety should work with industry to agree a comprehensive maintenance annex to the TCA. This is a significant gap in the agreement and given the highly integrated nature of the European aviation and aerospace sectors, it should be a high priority for future negotiations. Section 3.1.7 provides an example

of the kind of costs companies are currently exposed to while this gap remains.

6 WITHIN THE PARAMETERS OF THE TCA, WHAT SHOULD THE UK SEEK TO ACCOMPLISH WITH THE EU IN RELATION TO YOUR INDUSTRY OR POLICY AREA IN THE SHORT, MEDIUM AND LONG TERM?

6.1 Aerospace

6.1.1 The UK aerospace sector does not see the benefit of divergence from the EU's aviation safety framework. As we seek to overcome the shared challenge of climate change it is right that the UK should look to show global leadership. It should use the TCA as a basis for continued cooperation with the EU to develop, certify, and manufacture the next generation technology that is essential for combatting emissions from aviation.

6.2 Defence and security

6.2.1 The absence of an accompanying defence, security and foreign policy agreement between the EU and UK will pose challenges towards industrial cooperation in defence and other areas of national security. While this sits outside of the TCA's provisions, the failure to agree structures for industrial cooperation in defence and security, for instance via initiatives such as the European Defence Fund, will have a detrimental long-term impact on the trade in defence and security goods and the ability to partner on future research and development (R&D) and capability programmes of work.

6.2.2 The current participation requirements for the European Defence Fund (EDF) and Permanent Structured Cooperation (PESCO) activities do not currently provide good benefits for UK Government and UK entity engagement. The restrictions on ownership of the intellectual property developed and user rights with regard to export are too restrictive for Third Countries, the category under which the UK now falls. UK industry is very keen to explore with UK Government how the UK may continue to work with European partners in an international landscape where these challenges exist.

6.2.3 The UK's defence and security sectors hope that now a free trade agreement has been reached between the two sides, greater attention will be given to wider security and foreign policy issues, leading to future institutionalised arrangements for UK-EU defence and security industrial co-operation.