

***UK Trade Negotiations*** International Trade Committee

Note from Sheila Lawlor, Politeia, following Zoom session, 17 June 2020

***Which FTA matters - that with the EU or that with the US?***

1. The US economic model is based on the same broad principles as the UK's – a competitive economy based on free markets competing under the rule of law, both countries having the common law tradition. It is an open system, permissive, in that all activities are permitted other than those prohibited by law. The UK is therefore knocking at a door of an economic and trade system which is based on the same principles as the UK's.
2. The EU economic model by contrast is based on the centrally controlled model, perfected by France since the 17<sup>th</sup> century and underwritten by civil (Roman) law. A prescriptive, codified system determines what is and is not permissible. For historic reasons that model served the aims of the French state and its rulers, political and military. When what became the EU was founded as a French initiated, Franco-German project, that model was adopted, and with it the system of protection and controls, which has since further developed in the EU. Therefore, there are differences in the EU's approach to its economic model - controlled, regulated and protected - which will bring difficulties to the UK.

***The UK's overall trade strategy - the respective importance to the UK of a US or EU trade deal***

3. For a FTA with the US or the EU, the UK approach should be on the basis of seeking the same sort of trade-off. Each of these parties wants to sell us goods. We offer a big market of c. 66.6 million people, and (at least until the lockdown), the UK was the 5<sup>th</sup> largest economy in the world.
4. We should insist from the start on a quid pro quo for services. Services account for 81 per cent of our economy, goods for less than 20 per cent. And financial services (estimated as c. 7 per cent) offer both sides great opportunities for cross border trade and investment. In the case of a US deal, the two sides give the world its two leading global hubs: New York as a world financial centre is rivalled only by London. Already the US and the UK are each other's biggest services trading partners. And, with the EU, we have already developed proven systems for services trading.

***The gains? US, EU, Japan – How realistic are the assessments by HMG (or by others)?***

5. Projections do not and cannot take account of all the relevant data, known and unknown. Most economists, like generals of the past, are fighting the last war, future trade policy often being considered in terms of keeping the status quo ante 2016.
6. I don't accept that the Whitehall figures used by HMG, or those of many other economists in UK universities or institutions, reliably indicate what is likely to be the case. First, estimating and forecasting economic relationships is inherently difficult and there is no reason for assuming that

such relationships will stay stable over time. Second, in economics, as in every other discipline, we should recognize that there is political bias in what evidence is selected, sifted and used to make a case. Economists refer this as 'data mining' when large numbers of statistical relationships are estimated, but only those that fit prior beliefs are used.

7. Selecting subject, focus and evidence in most disciplines reflects a personal or group mindset, or bias. Like historians, political scientists and other academics, economists are not free of user bias, and government economists are no different. This should be born in mind in assessing any data, especially on one of the most polarizing subjects of a generation, Brexit and the UK-EU future relationship, where economists on both sides of the Brexit debate have reached very different conclusions on outcomes.
8. It would be unusual for the UK Civil Service led by the Treasury, to be other than notoriously conservative in approaching change, fearing the worst: the case it makes to ministers and the public tends to reflect that of the established consensus, and cannot take account of the unknowns.

***Do We Need an FTA for Services? Overall Strategy of HMG's UK-US FTA approach?***

9. The UK proposes better regulatory cooperation but not, it would appear, a significant, legally binding agreement for services trade (UK outline proposal, *UK-US Free Trade Agreement*, DIT, 2/3/20). It seems merely to aim for a general agreement on services - to increase market access and fair competition and to improve regulatory co-operation. This is less than ambitious.
10. For financial services trade there should be a binding legal agreement (i.e. as a separate chapter) in an FTA with mutually agreed dispute regulation procedures. The UK should propose a specific, legally binding 'equivalence' agreement to cover financial services trade, enhanced to give businesses greater security in planning and providing services. It would be based on the principle proposed to the EU of enhanced equivalence, under which each party would recognise that the other's laws lead to the same outcomes or standards. In practice a UK company would trade in the US without the need to set up a subsidiary, the US recognising that the UK laws under which the UK company does business are equivalent to its own, with UK court resolution and UK regulatory supervision. The problem with the envisaged basis is that we already have regulatory cooperation and, even if enhanced, where a matter is disputed or unclear, then US lawyers will judge on the basis of US law, not UK law. A change in the US legislative framework and permitting the US regulators to rely on the UK regulators to a degree more significant than is possible through mere regulatory cooperation would be needed.
11. The UK would thereby follow the same overall approach to the US for UK-US financial services trade as already proposed for the EU (and set out in Barnabas Reynolds' *Template for Enhanced Equivalence*, Politeia 2017). In the event of a dispute or regulatory matter the US courts and regulators would stand back, not having jurisdiction, and the customer would be protected solely by the remedies and protections available in the UK. Firms could be required to notify customers in advance of such an arrangement. This would amount to a caveat emptor approach, where US purchasers could obtain the benefits of UK services and products, but on the basis solely of UK protections, so the US buyer would be allowed to opt out of the US regime and into the UK one, with all the consequences (and benefits) that brings. Given the sophistication and fairness of the UK regulators and court system the result should be seen as favourable to the customer, but this would need to be explained. The same position would be true in reverse for UK purchasers from US sellers. Furthermore, a separate consumer protection arrangement could be considered,

allowing for local protections to apply in sensitive areas of consumer welfare.

12. Such a formal agreement would make for clarity and greater legal certainty. It would give businesses the security they need to trade, under laws they understand. This should be particularly possible and attractive given that the UK and US share the same overall approach to the law. While a change of US law would be needed to allow for the recognition of UK standards and supervision, it should be a priority for UK trade policy to propose this by proposing a specific equivalence agreement as part of an overarching UK-US FTA.

(SL, Politeia, 19<sup>th</sup> June, 2020)

Written submission from Sheila Lawlor (UKT0007)