

The Society of Motor Manufacturers and Traders (SMMT) – Written evidence (FFT0023)

Background

The Society of Motor Manufacturers and Traders (SMMT) is one of the largest and most influential trade associations in the UK. It supports the interests of the UK automotive industry at home and abroad, promoting a united position to government, stakeholders and the media.

The automotive industry is a vital part of the UK economy accounting for £82 billion turnover and £18.6 billion value added. With some 168,000 people employed directly in manufacturing and 823,000 across the wider automotive industry, it accounts for 14.4% of total UK export of goods and invests £3.75 billion each year in automotive R&D. More than 30 manufacturers build some 70 models of vehicle in the UK supported by 2,500 component providers and some of the world's most skilled engineers.

Overview

UK automotive is a highly competitive, export-led industry, with complex supply chains that are fully integrated with the rest of the European Union. The sector's competitiveness is built upon free and frictionless trade with the EU, and a manufacturer's ability to not only sell finished vehicles tariff free, but to source components from all 27 EU member states.

The successful conclusion of a UK-EU Free Trade Agreement (FTA) will not be sufficient to ensure continued tariff-free trade unless the accompanying provisions on rules of origin do not enable all UK automotive manufacturers and suppliers to trade tariff-free in the short, medium and long-term. The parties should agree on more liberal rules of origin for finished vehicles and ensure workable rules of origin are agreed for automotive parts and components. The implementation of a phase-in period for new rules of origin requirements is highly significant.

Regulatory convergence, and the consequent removal of "behind the border" barriers to trade within the Single Market, has played an essential role in promoting the industry's international competitiveness. SMMT believes that the UK and EU should base their future trading relationship on a new framework for regulatory cooperation and dialogue in relation to automotive. This should start from a position of complete alignment, recognising that the UK and EU currently share the same rules, and be supported by a robust governance framework. In addition, while a future FTA will not curtail the UK's sovereignty on regulatory matters, the automotive industry believes the significant cost of additional testing and certification should be avoided by the UK choosing to align with EU technical regulations and seeking mutual recognition for its type approval framework

Questions

1. What are likely to be the key non-tariff barriers affecting future UK-EU trade in goods and how could these affect the operations of UK businesses?

Basing the new UK-EU trading relationship on the provisions permissible in a free trade agreement will significantly change the administrative processes related to the movement of goods between the UK and the EU. The trade agreement between the UK and the EU will result in increased friction at the border. The industry operates a just-in-time, just-in-sequence manufacturing model. Delays to the arrival of components at manufacturing plants are measured in minutes. Every minute of delay could cost approximately £50,000 in gross value added to the industry, totalling over £70 million per day. For automotive manufacturers, border delays are unacceptably disruptive, and if the sector in the UK is to remain competitive, these must be minimised.

Should the parties achieve a tariff-free deal, this would mean that all automotive goods exchanged between the EU and the UK will be *eligible* for tariff free treatment, but not that zero-tariff will automatically apply. Zero tariff will apply exclusively to products that *originate* in the territory of the parties according to the FTA's rules of origin. Products failing to comply with these rules will be subject to tariffs on a most-favoured-nation basis. For imports into the UK, this means the new UK Global Tariff (UKGT); for exports to the EU, the Common External Tariff (CET) will apply to non-originating products. Both UKGT and CET set a 10% tariff applicable on non-originating passenger cars. CET duties applicable on non-originating accessories and heavy-duty vehicles would be higher than those recently established by the UKGT.

The introduction of regulatory divergence between the UK and the EU on product regulations (for example, those in relation to type approval) where such divergence does not currently exist, would create technical barriers to trade (TBTs), increase the cost of doing business, and potentially limit market access for UK exports to the EU and vice versa. In addition, this would almost certainly result in a reduction in product choice for the consumer in the UK.

2. What are likely to be the most important technical barriers to UK trade with the EU? How could these be addressed in the future UK-EU trade agreement and what precedents exist in other trade agreements?

Regulatory alignment with the EU and the removal of TBTs in automotive goods has played a critical role in providing UK manufacturers with unrestricted access to the EU market, which in turn has led to improved competitiveness for the UK sector. Should the automotive regulations in the UK differ to those in the EU, regulatory divergence would not benefit the sector, customer or the UK economy. There would be a significant increase in

the cost of doing business for UK-based manufacturers, particularly if it resulted in the development of a unique UK testing regime.

In addition, the UK risks diverging where regulations are not kept up-to-date and aligned with regulatory advances in the EU. This would create technical barriers which would disadvantage UK manufacturers, since market access would be reduced. The emergence of divergent technical regulations in the short, medium or long-term would increase design, testing and manufacturing costs, making the production of some models for the UK market unprofitable, leading to reduced consumer choice, while others would become more expensive for UK consumers.

A dedicated Automotive Annex would be the industry's preferred choice as the legal basis to address sectoral regulatory barriers in a future UK-EU FTA. Automotive-specific annexes have regularly been included in EU trade agreements since the conclusion of the EU-Korea FTA in 2011, including in FTAs with Canada, Japan, Singapore, the newly approved deal with Vietnam and the agreement in principle with MERCOSUR. However, to deliver on the industry's priorities, an Automotive Annex between the UK and the EU should go beyond the recognition of mutually applied international standards.

3. What form of regulatory cooperation should there be between the UK and EU, including cooperation with EU agencies?

To address the issues referred to under question 2, an UK-EU trade deal should address the need to create a new framework for regulatory cooperation and dialogue between the UK and the EU. This should be supported by robust governance that obliges both sides to notify the other in advance of regulatory changes and provides mechanisms for the potential impact of divergence on market access and the cost of doing business to be assessed in advance of new regulations coming into force. The UK and the EU should also commit to continue to work together to shape future regulations at the international UNECE level.

Cooperation with EU agencies is necessary for areas such as REACH and type approval. With regards to chemicals, the introduction of new and potentially conflicting chemicals regulations in the UK will have significant and negative impacts on the UK automotive sector, including disruption to the supply chain and increased costs for manufacturers and ultimately consumers. The UK should aim to secure, as part of the future trading relationship with the EU, provision for UK representatives to participate in relevant expert groups related to chemicals regulations.

4. How could the UK and EU minimise the costs and disruption associated with any testing and compliance processes that will be required, including conformity assessments? How effective would mutual recognition be in keeping these to a minimum?

Through a dedicated Automotive Annex, a UK-EU trade agreement should recognise that the UK and EU currently share all the same regulations, and so both parties should mutually recognise all technical regulations related to automotive applied by the parties at the date of entry into force of the agreement, including those outside of type approval related to emissions and environmental regulations, such as end-of-life vehicle regulation, waste management and product specific recycling requirements.

At a minimum, mutual recognition of approvals and test reports for systems, components or separate technical units in compliance with the applicable legislation is required.

The recognition of technical services of the UK and the EU by each party to the future FTA, would be instrumental for simplifying the type approval activities for manufacturers and would greatly ease the process of mutual acceptance of conformity assessment results. This would also maintain the current level of resource within the technical services, expediting the approval process for both UK and EU manufacturers.

Mutual recognition of whole vehicle type approvals between the EU and the UK would be the optimal situation but relies upon the willingness of the parties to ensure ongoing alignment of all relevant regulations.

5. What arrangements on rules of origin should there be between the UK and the EU? What precedents are there for bespoke arrangements in other trade agreements?

Provisions on rules of origin are required to enable all UK manufacturers and suppliers to trade tariff-free in the short, medium and long-term. As such, the UK and EU must negotiate a standalone rules of origin chapter and protocol that takes into account the uniquely integrated nature of UK/EU trade. Except for agreements with the parties to the the Regional Convention on pan-Euro-Mediterranean preferential rules of origin (PEM Convention), bespoke protocols on rules of origin have been regularly negotiated and agreed in existing EU preferential trade agreements.

The UK and EU should agree on alternative rules of origin for all relevant automotive products. In principle, these rules should set lower regional value content thresholds compared to applicable product-specific rules agreed in most EU trade agreements, allow a broader use of change of tariff heading or tariff sub-heading provisions and include simple product-specific processing rules when needed.

For passenger cars, commercial vehicles and buses, most EU FTAs demand a minimum regional value content between 55% and 60% to qualify for preferential treatment. The EU and UK automotive industry advocate for more liberal rules of origin to apply in future trade of finished vehicles. At present, the lowest value threshold agreed in EU FTAs demand 50% of the

value of a finished vehicle to be added in the territory of the parties to qualify for preferential treatment.

With regard to parts and components, liberal rules of origin would be beneficial for both the UK and the EU given the highly integrated nature of European supply chains and the accelerated shift in the industry to move towards electrified vehicles, components and materials which are typically sourced from outside the territory of both the parties.

In this regard, much more liberal rules of origin need to be applied on the trade in batteries for electrified vehicles. Product-specific precedents are greatly varied, ranging from very liberal rules applicable under the EU-Canada agreement to virtually unworkable rules under the current PEM convention. Given the high value of a battery as a proportion of the total value of an electric vehicle, unattainable rules of origin on batteries would result in the application of tariffs to new-generation vehicles at a time when both the UK and the EU are trying to accelerate the uptake of such vehicles.

In line with all existing EU FTAs, the future agreement must allow the cumulation of content originating in the territory of the EU and in the UK to meet future rules of origin criteria.

However, a simple bilateral cumulation would be largely insufficient to mitigate disruptions to bilateral trade. In light of the highly integrated UK-EU value chain, the parties must also agree on full cumulation provisions allowing for all inputs or operations carried out in either the EU or the UK to be taken into account, including value added on non-originating materials. Full cumulation provisions are already provided for in trade agreements like EU-Japan and EU-Canada.

As a means to preserve modern international value chains in both the UK and EU automotive sectors, the parties should also agree on provisions allowing cumulation with common preferential trading partners. The scope of these provisions should be limited to tariff lines which are relevant for automotive production. In doing so, the parties should ensure that rules of origin and preferential duty rates applicable by the EU and the UK on imports from common preferential trading partners are compatible in order to maintain a level playing field. The parties could build upon existing provisions related to extended cumulation included in EU agreements with Japan, Canada and the new FTA with Vietnam.

To reduce the administrative burden and facilitate compliance with rules of origin, modern origin provisions and related formalities, should be agreed by the parties. Examples of facilitative measures can be found in existing EU trade agreements, and these include increased tolerance thresholds for non-originating materials as well as precedents allowing duty drawbacks, gradual origin achievement, split shipments and self-certification mechanisms for origin declarations.

A significant facilitation the industry has long called for regards the possibility to meet value threshold by averaging across component or vehicle model ranges instead of calculating origin for each unique component type or individual vehicle model.

Finally, there must also be the inclusion of a phase-in period in the application of rules of origin to allow manufacturers and suppliers with sufficient time to complete model cycles, adapt their systems, process and contracts to a new trading relationship that will necessitate the provision of rules of preferential origin declarations. Rules of origin applicable during the phase-in period should be significantly less demanding compared with end-rules. Phase-in periods have also been agreed in a number of FTAs, including those with Canada and Japan.

6. How could customs processes and documentation be simplified to support UK-EU trade? What role could new technology play in this regard?

The free trade area envisaged by the UK and EU should make provision for:

- a) Simplified customs procedures to facilitate trade between the UK and the EU with a view to minimising costs and burdens for importers and exporters. This could be achieved through the development of a fully interconnected and interoperable single window system to facilitate trade by, among other things, converging import and export data and documentation requirements and establishing a single location for documentary and physical verification of consignments;
- b) A shared trusted trader scheme that allows as many automotive companies as possible to have goods cleared at the point of destination or before shipment, and avoid the need to stop at the border;
- c) Information and data sharing between customs authorities so as to facilitate the smooth movement of automotive goods through points of entry into the UK and the EU;
- d) Cooperation between customs authorities in the UK and EU member states.

In addition to seeking these provisions in the trade deal, the UK should fully implement the Union Customs Code. It should also aspire to become a global leader in trade logistics and make the necessary investment at all points of entry and exit to promote the rapid movement of goods to and from all global trading partners.

7. What improvements should be made to existing customs facilitations, such as trusted trader schemes, particularly for the benefit of small and newly-established businesses?

We recognise that HMRC are going to be stretched to grant authorisations to companies in time for the end of the transition period. HMRC should consider pre-authorising companies based on their submission of documented procedures. This could reduce the pressure on both HMRC and companies. HMRC have previously run the process in this way where they visit a company pre authorisation and then conduct the full audit after 6 months of the company running the live operation. This has the added benefit of giving the trader time to bed in their processes.

Trust in traders must be a central pillar in any government vision for the UK border. Moreover where government provides facilitations such as AEO, the benefits must be worth the time taken to apply for them. If a company has AEO status it should mean that government trusts that company, providing them substantial benefits for moving goods in and out of the UK. Government should consider a 'gold' standard for AEO holders where they are automatically allowed to operate other procedures e.g. simplified declaration procedures if they have AEOC. This should not exclude companies from obtaining simplified or special procedures without AEO but it would avoid the need for duplication of applications.

8. What impact would the absence of a UK-EU trade agreement at the end of the transition period have on non-tariff barriers and, consequently, UK businesses? How prepared are UK businesses for this situation and what should they be doing to get ready?

Regardless of a trade agreement government must ensure that sufficient time is given to businesses to implement any change so as to not negatively impact existing automotive supply chains and purchasing/sourcing decisions.

Substantial guidance and supporting documents are needed alongside government announcements and engagement opportunities to allow companies to fully evaluate the process changes that will be coming into force, understand how it impacts them and develop internal solutions. Guidance for both moving goods into and out of the EU27 would also be welcomed.

While the specifics of the UK's future trading relationship with the EU will not be known until the end of the year, it is already clear that the new relationship will fundamentally change the way that businesses trade with the EU.

Government should continue to work with the automotive industry to ensure that those companies that make-up the UK's largest goods exporting sector are fully prepared for the changes that will come into force next year.

We believe that joint industry and government efforts should focus on three broad areas:

- a. **Raising Awareness** – ensuring that vehicle manufacturers and suppliers of all sizes understand that from 1 January 2021 there will be changes in the areas of customs, trade, regulation and immigration.
- b. **Training** – provide business representatives with the knowledge and skills required to understand the impact of the new trading landscape, including through the provision of comprehensive customs training for automotive SMEs that have previously only traded with the EU, and will be importing and exporting for the first time following the agreement of a UK/EU trade deal
- c. **Action** – taking the learnings from training sessions back into the business and making the necessary changes to operations at the earliest opportunity with the option for further assistance where it is required.

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