

PLAN A+

Creating a prosperous
post-Brexit U.K.

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IEA Discussion Paper 95

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Acknowledgements

The authors are grateful for the contributions and advice of the many people who have contributed to this document. We would especially like to thank Catherine McBride, Victoria Hewson, Julian Jessop, Jamie Whyte, Mark Littlewood, Kate Andrews, Darren Grimes, among others at the IEA, Prof David Collins at City University, as well as the members of our Advisory Council: Sir Lockwood Smith, Eduardo Perez Motta, John Cooke, Srin Rangan, Alan Oxley, Razeen Sally, John Weekes, Peter Allgeier, and Stuart Harbinson.

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Glossary

ACITA: Association for International Trade
ACMD: Anti-Competitive Market Distortion
AEO: Authorised Economic Operator
AMS: Aggregate Measure of Support
AVMSD: Audiovisual Media Services Directive
BEIS: Department for Business, Energy and Industrial Strategy
BIP: Border Inspection Post
CAP: Common Agricultural Policy
CET: Common External Tariff
CETA: EU-Canada Comprehensive Economic and Trade Agreement
CEN: European Committee for Standardisation
CENELEC: European Committee for Electrotechnical Standardisation
CFP: Common Fisheries Policy
CFSP: Customs Freight Simplified Procedures
CMA: Competition and Markets Authority
COREPER: Committee of Permanent Representatives of the European Union
CPTPP: Comprehensive and Progressive Agreement for Trans-Pacific Partnership
CSA: Customs Self-Assessment
CTA: Common Travel Area
DEFRA: Department for Environment, Food and Rural Affairs
DIT: Department for International Trade
EBA: Everything But Arms
EEA: European Economic Area
EEZ: Exclusive Economic Zone
EFTA: European Free Trade Association
ETSI: European Telecommunications Standards Institute
FCA: Facilitated Customs Agreement
FTA: Free Trade Agreement
G7: Group of Seven
GATS: General Agreement on Trade in Services

GATT: General Agreement on Tariffs and Trade
GDPR: General Data Protection Regulation
GPA: Agreement on Government Procurement
GRP: Good Regulatory Practice
GSP: Generalised System of Preferences
HMRC: Her Majesty's Revenue and Customs
ICES: International Council for the Exploration of the Sea
ICJ: International Court of Justice
ICN: International Competition Network
ILO: International Labour Organisation
IMF: International Monetary Fund
ITRP: Independent Trade and Regulatory Policy
MiFID II: Markets in Financial Instruments Directive II
MFP: Multilateral Framework on Procedures
MFN: Most Favoured Nation
MRA: Mutual Recognition Agreement
NAFTA: North American Free Trade Agreement
NATO: North Atlantic Treaty Organisation
NCP: New Customs Partnership
NEAFC: North East Atlantic Fisheries Commission
NTB: Non-Tariff Barrier
OECD: Organisation for Economic Co-operation and Development
PESCO: Permanent Structured Cooperation
QMV: Qualified Majority Voting
REACH: Registration, Evaluation, Authorisation and Restriction of Chemicals
REX: Registered Exporter System
RFMO: Regional Fisheries Management Organisation
SEM: Single Electricity Market
SFPA: Sustainable Fisheries Partnership Agreements
SOE: State-Owned Enterprise
SPS: Sanitary and Phytosanitary
TAC: Total Allowable Catch
TBT: Technical Barriers to Trade
TiSA: Trade in Services Agreement
TRQ: Tariff-Rate Quota
TTIP: Transatlantic Trade and Investment Partnership
UCC: Union Customs Code
UKFP: United Kingdom Fisheries Policy

UNCITRAL: United Nations Commission on International Trade Law

UNCLOS: United Nations Convention on the Law of the Sea

UNFSA: United Nations Fish Stocks Agreement

USTR: United States Trade Representative

VIES: VAT Information Exchange System

Preface

The United Kingdom's relationship with the European Union has been a divisive issue in political and economic debate for many years, but particularly so in the referendum of 2016 and in the two years thereafter.

Divisions in opinion have gone far beyond the wisdom of us staying in the EU or leaving it and now encompass a whole raft of issues about what a sensible departure might look like, whether a temporary or transitional arrangement would be open to rapid revision or would effectively be an end state and even the circumstances in which the decision to exit the EU could be revisited.

The debate has not merely divided public opinion in the country at the large, but has also been the principal focus of contemporary debate between politicians and policy makers both within political parties and between them.

The Institute of Economic Affairs is an educational charity which seeks to improve the understanding of the positive role free markets can play. It takes no corporate view on any specific policy matter, including the merits or the precise nature of the UK's departure from the European Union.

Similarly, the IEA takes no view of the politics involved in determining the Brexit process. It may be that one particular course of action has political or electoral implications for a specific politician or political party, but this is a matter of indifference for the Institute.

However, what is undeniable is that the nature and form of the UK's departure from the European Union – as well as our future relationship with the EU and the rest of the world – are likely to have substantial implications for the UK's economy, its ability to trade as freely as possible across the globe and its domestic regulatory environment.

These are all matters of considerable interest to the Institute and our hope is that this document provides an informative and educational template of the steps the United Kingdom could take and the strategy it should implement if the benefits of a more market-orientated economy are to be realised.

Mark Littlewood, Director General & Ralph Harris Fellow, Institute of Economic Affairs

Executive Summary

Delivering the Brexit Prize

The opportunity before the UK as a result of Brexit is huge: but if we squander it, the “new normal” of limited economic growth will prevail, with an EU system that is failing to respond to the challenges of the modern economy.

In her Mansion House speech, the Prime Minister stated that the UK’s regulations need not be identical to the EU’s, even if they would achieve the same outcomes. But the Government White Paper (The future relationship between the United Kingdom and the European Union) proposes that the UK would have substantively harmonised regulations with the EU, which, with the customs arrangement it outlined, would make an independent trade policy all but impossible. It also described a swathe of other infringements to independence.

The UK running its own economy will not render a deal with the EU impossible. It will bring back real growth, let the UK do other trade deals, and create leverage to get positive results from EU negotiations. Political, trade, and regulatory independence is therefore not just an ideological position, but what makes the gains possible.

This proposal will set these out, and demonstrate what will be lost if the UK Government maintains a model similar to the approach adopted at the Chequers cabinet meeting in July 2018, further elaborated in the White Paper, or one even more closely aligned to the EU. The economic scale of the prize shows the opportunity to unleash prosperity when we liberate ourselves from a system with such serious distortions. This is a framework outlining how the UK can still attain the Brexit Prize.

Four pillars

The governing principle of this alternative approach is the pursuit of a competitive and thriving UK economy. We have based the approach on four fundamental 'pillars' of prosperity, to create a joined up trade and regulatory policy. It is a central tenet of this paper that the UK's bifurcation of EU policy and rest of the world policy has damaged its ability to use the interactions between these pillars to its advantage. The pillars are:

a. Unilateral

The UK should make unilateral moves in domestic policy and trade policy terms. Many EU regulations are bad for growth: the UK needs the freedom to do better, this includes:

- Improving the way regulations are made to better support competitive markets: in particular to ensure a pro-competitive environment in digital, financial services, and other areas that are crucial to the UK's economic success, but where **continued adherence to EU norms would hold us back**
- In **agricultural policy, eliminating tariffs and quotas** on all products the UK does not produce; methods to rebalance prices of imports of products whose costs are reduced by distortions in other markets
- In **fisheries policy**, restoring sovereignty over UK waters and sustainably addressing barriers to entry for new fishermen.

In **other non-trade areas**:

- **Defence and Security**: cooperate with EU allies – but not in the direction envisaged in the White Paper of participation in PESCO.
- **Immigration**: replace free movement of workers and EU citizenship with an efficient and balanced framework for movement of workers from the EU and the rest of the world that recognises the economic and social benefits and costs of immigration.

b. Bilateral

The UK must undertake bilateral agreements with others concurrently during the EU negotiation. It should seek to replicate the EU's agreements with third countries to cover the UK bilaterally, and focus on major trading partners with whom the EU does not yet have agreements. Negotiating regulatory recognition with the EU will be challenging, but is too important to abandon, with EU regulation damaging to growth. Tying the UK to future EU regulation is a major threat to the UK economy.

Options

As the negotiations pursuant to Article 50 stand, most of the legal drafting of the agreement that will include any negotiated arrangements (the Withdrawal Agreement) has been provisionally agreed. The most fundamental outstanding elements are the framework for the future relationship and the so-called backstop arrangement for the Irish border ("Irish Backstop"). It was the desire to avoid the Irish Backstop being invoked that informed the design of the White Paper – a way of preserving free circulation of goods without either leaving Northern Ireland in the EU's customs union and single market, or having the whole of the UK stay in the single market and a customs union.

The UK government has options available to it that would deliver varying levels of autonomy, negotiability and associated risk. At one end of the spectrum, terminating the negotiations in order to focus on 'no deal' preparations, including protecting the positions of EEA citizens by unilateral measures, could deliver the most independence in the shortest time frame. This option would not mean no exit arrangements at all, as the UK could propose self-contained agreements with the EU in areas like aviation and nuclear safety, enabling the Council to issue the necessary mandates to the Commission to negotiate such matters, and refer the question of the financial settlement to independent arbitration.

At the opposite end of the spectrum, the UK could request an extension of the negotiating period to enable the outstanding provisions of the Withdrawal Agreement to be completed, and to advance no deal preparations. Against this option are the likely domestic political consequences, the possibility that the extension would be declined and the protracted uncertainty for businesses and individuals.

The option being pursued by the Government is being resisted by the EU,

due to the legal and practical challenges of the FCA and the disaggregation of goods from other components of the single market. It may also be voted down by the UK Parliament.

An option is therefore required to maximise the progress already made on the terms of the Withdrawal Agreement but unblock the impasse over the Irish border and future framework. The government should seek to retain all of the agreed elements (the financial settlement, citizens' rights, the transition period of 21 months (the Transition Period) and withdrawal terms) and propose a new backstop and framework for a future relationship. The new backstop would comprise a basic free trade agreement between the UK and the EU for goods, and a commitment by the parties to undertake all necessary investment and cooperation mechanisms to enable formalities on trade between Northern Ireland and Ireland to be overseen away from the border. This would enable the completion of the Withdrawal Agreement and incentivise the parties to agree a better FTA during the Transition Period. It would also enable the UK to negotiate more effectively with rest-of-world trading partners during the transition, with a baseline element of the relationship with the EU known at the outset.

A UK-EU Free Trade Plus deal:

- Fully activating all of the pillars listed now will start to put the UK on a stronger negotiating footing. Requests for more time will make the UK look weak and cause more delays before the UK activates the strategy outlined here.
- For an FTA with maximum regulatory recognition, the UK should put text on the table in the form of best in class chapters in all these areas: Zero tariffs in goods and agriculture; customs and trade facilitation chapter and Irish border protocol; government procurement; regulatory coherence including specific sectoral annexes (e.g. pharmaceuticals); competition policy and state aids; open services chapter with maximum liberalisation; no restrictions in all four modes of service supply in market access or national treatment; mutual recognition of occupation licensing; specific sectoral annexes in key areas including telecoms, data and financial services; investment; dispute settlement.

FTAs with the US, India, China, and other partners:

Simultaneous discussions should include with partners for more difficult FTAs in the longer term.

Bilateral deals with countries where an EU FTA should be rolled over:

- Negotiations should be accelerated to roll over existing agreements and agree a new FTA with EFTA. the Department for International Trade (“DIT”) should seek to conclude these negotiations provisionally, so they can come into effect on 30 March 2019 in case of no Withdrawal Agreement and no Transition Period.

Alternative model of bilateral relationships for developing countries:

- The UK has an historic opportunity to create genuine Economic Partnership Agreements that do not hinder growth, unlike the EU’s Generalised System of Preferences model. But better models require the UK having tariff and regulatory control.

c. Plurilateral

- The UK should seek membership of major arrangements which involve a number of countries, including the Comprehensive and Progressive Trans-Pacific Partnership (CPTPP) and North American Free Trade Agreement (NAFTA). Tariff and regulatory control would also be needed to accede to CPTPP.

d. Multilateral

- There are two aspects to multilateral strategy: using the WTO transition to reinforce the other pillars; and using a fully-fledged WTO membership to promote wealth creation for the UK economy and the world.

At the WTO

The UK can use its Aggregate Measure of Support (“AMS”) offer to signal its free trade intent, seeking no or de minimis AMS to show it will not pursue production subsidies in agriculture beyond what it has now, and limit direct payments to allowed green box payments. In **bilateral negotiations with TRQ (Tariff-Rate Quota) partners, and parties with whom it has negotiations through the EU, **it is critical the UK negotiates with partners by itself.****

The UK should also join numerous WTO groups as soon as possible, showing the UK is a committed liberaliser of trade & committed to open domestic settings, for instance:

- **The Cairns Group** of agricultural exporters (the UK is not a major agricultural exporter but is locked into EU supply chains).
- **The Manchester Group.** Just as Australia launched the Cairns Group, as the world's second-largest services exporter, the UK should launch the 'Manchester Group of Services Exporters', named for the city's role in the Victorian free trade movement.
- **The UK can join the e-commerce plurilateral initiative & take a leadership role in services liberalisation.**

Strategic shifts

It is not possible to lay out all the required steps, but an effective strategy is only possible once the customs union or any variant of it (such as the Facilitated Customs Arrangement (FCA) set out in the White Paper or its predecessor the New Customs Partnership (NCP)) is off the table.

- If the EU does not cooperate with serious UK proposals, the UK should move to a more aggressive footing; if the EU refuses to recognise UK regulations on day one of Brexit, the UK should be prepared to take action in the WTO for violations of the General Agreement on Tariffs and Trade (the GATT) and the Agreements on Technical Barriers to Trade (TBT Agreement) and Sanitary and Phytosanitary Measures (SPS Agreement).
- In the event of no agreement, the UK could elect not to impose checks on goods trade at the Irish border, and apply zero tariffs on agri-food, on an MFN basis for all imports, and selectively reduce and eliminate tariffs on other goods.

Fundamentally, progress in one pillar reinforces the others. The UK should be playing chess on multiple chess boards, maintaining freedom to pursue all areas simultaneously.

This alternative approach aims to be a framework for the adoption of a UK independent trade and regulatory policy, including in its relationship with the EU. As a framework, many of the areas should be developed further, and represent ongoing work streams.

We seek a UK economy which employs people in good jobs, where they are able to succeed based on the merits of their ideas and their hard work. An economic system based on competition as opposed to cronyism will maximise wealth creation and lead to more money in the pockets of UK consumers, and more money for essential services.

No plan can predict every possible future move that our trading partners may or may not engage in. No plan can definitely say what final or intermediate states in our relationship will look like. This alternative approach sets out what the overall objectives of the UK government should be (the four pillared trade policy which we outline below). It then makes recommendations about what initial moves the UK could make to realise the benefits of leaving the EU.

Introduction

Membership of the European Union stifles prosperity just as it prevents the UK governing itself. It saddles the UK with regulations that protect large incumbent businesses from competition, harming innovation and reducing efficiency. And it prevents the UK from entering into its own free trade agreements (FTAs) with countries outside the EU. This increases the prices paid by consumers and diverts capital and labour away from their most productive uses. In short, it makes us poorer.

Brexit thus presents the UK with a rare opportunity to radically change this: but the opportunity is a brief one. To take that opportunity, the UK's regulations and trade relations must become truly independent of the EU. Until recently, the Prime Minister, Theresa May, seemed to envisage such a Brexit. In her speech at Lancaster House last year, she said that Brexit would set the UK free to have an independent trade policy, with the ability to strike agreements outside the EU and the customs union's Common External Tariff. In her Mansion House speech in March this year, she clarified that the UK's regulations need not be identical to the EU's, even if they would achieve the same outcomes.

This summer, however, the Government's White Paper proposed substantially harmonising UK regulations with those of the EU after Brexit. Combined with the customs arrangement it also outlined, this would make an independent trade policy all but impossible. Keen to avoid potential disruption in our trading relationship with the EU, the Prime Minister is now set to throw away the potential gains of Brexit. Given that the latter are greater than the former, this is a profound mistake.

This paper therefore proposes an alternative to the Chequers plan, one through which the UK has genuine independence after Brexit – which must include regulatory freedom and trade independence.

Many of the actions we recommend can be taken unilaterally: that is, the UK government can act without needing to win the agreement of other governments, inside or outside the EU. Regulatory reforms, import tariffs and border controls (on the UK side) are obvious examples. Then there are measures that will need agreement with individual foreign governments (bilateral arrangements), such as the Brexit deal with the EU and, ideally, an EU-UK FTA. Other recommended measures are plurilateral, such as joining NAFTA, while yet others, pursued through the WTO, are multilateral. We call these different ways of pursuing improved regulation and trading relations – unilateral, bilateral, plurilateral and multilateral – the four “pillars” of our alternative plan.

We begin by explaining the gains to be had by taking advantage of independence from EU rule-making to improve the UK’s regulatory and trading arrangements. From this, we show in Chapter 3, that the White Paper would forgo these gains. Having made our general case, we use Chapter 4 to look more closely at each of our four pillars; Chapter 5 considers strategic questions associated with the UK’s negotiations with the EU, and Chapter 6 domestic reforms.

Brexit is an historic opportunity for the UK of the highest order. To benefit, the UK must once again become a self-governing, free-trading nation.

Chapter One

Keeping Our Eyes on the Prize

A major G7 economy has the chance to embrace independent trade and regulatory policy for the first time in forty years. This is unprecedented and could lead to huge opportunities for the UK and the world. The Prime Minister spoke about a Brexit Prize in the Lancaster House speech and clearly that prize takes many dimensions. **A free people exercising their sovereign rights is a prize in and of itself; we will focus on the economic dimensions of the prize.** Its scale depends on three contextual points. First, the direction of travel of the global trading system. Second, the direction of travel of the European regulatory system. Third, the direction of travel of the global regulatory system. If the prize is large, then pursuit of this prize should drive the UK's strategy. If it is small, then minimising the disruptions of leaving the EU's institutions would instead drive the strategy.

The Global Trading System is in crisis

It is uncontroversial to note that the global trading system is in crisis. Since the Uruguay Round of 1994, no significant global round has been negotiated. This is one third of the lifetime of the entire GATT/WTO system: it is unprecedented. In 1997, when the Basic Telecoms Agreement was signed, the outlook for further world trade liberalisation looked bright. Financial services and then energy services were next on the agenda. In services, countries were expected to open their services markets for further negotiation. But as the backlash against liberalisation and globalisation gathered steam in the 1990s, none of this agenda was realised. It has been said that trade negotiations are like riding a bike. You need to keep doing it or you fall off. As a result, key indicators are showing the weakness of the global system. Measures of global industrial output have been stalled since before the financial crisis.¹ Global trade as a percentage of global GDP also dipped, and global trade growth stalled in 2015 in an unprecedented fashion.² Christine Lagarde at the IMF has

¹ International Monetary Fund, *Global Industrial Output Growth*, Data from 1980-2017. See (Singham, S., "How the World can benefit from the Network Effects of the Commonwealth", Institute of Economic Affairs, April 20189) for analysis.

² Speech by Christine Lagarde at the ECB Forum on Central Banking, "Monetary Policy in a Changing Financial Landscape", May 25, 2014.

Available at: <https://www.imf.org/en/News/Articles/2015/09/28/04/53/sp052514>

called this a new normal³ where we can expect low growth in developed markets for the foreseeable future. WTO Director General Azevedo has noted that in terms of trade liberalisation we are not only going in the wrong direction but doing so with increased rapidity.⁴

Opening the report, DG Azevedo said:

“The message of the Report before us today is serious. We are heading in the wrong direction, and we seem to be speeding up. Growth, jobs and recovery are at stake. I call on members to recognise the gravity of this report and its findings. We need to see immediate steps which de-escalate the situation. I will continue working with all members to this end.”

Most recently, the US administration has made its own threats to the global system, in particular to the WTO's dispute settlement mechanism (and appellate body), once the crown jewels of the international trading system. The lack of countries willing to support the global system allows more and more pernicious activities to develop.

But this means a vital opportunity for the UK. The re-emergence of a G7 country and the world's second-largest services exporter on the trade policy stage should mean that the UK can act to lower market distortions around the world and start to help reverse these damaging trends, if it maintains its traditional open and free market orientation.

The EU regulatory system is moving in the wrong direction

The direction of travel of the EU economy from which the UK is emerging is crucial to this analysis. If the EU was moving in a pro-competitive and liberalising direction, then this analysis would be very different. We believe that the EU is moving in an ever more prescriptive and anti-competitive direction.

The following brief examples outline various major EU-originated anti-competitive regulations in the UK.⁵ The point is not that 'deregulation' is needed, but regulation that is pro-competitive, increasing consumer

3 Speech by Christine Lagarde at the ECB Forum on Central Banking, "Monetary Policy in a Changing Financial Landscape", May 25, 2014.

Available at: <https://www.imf.org/en/News/Articles/2015/09/28/04/53/sp052514>

4 Roberto Azevedo presenting the WTO's "2018 Trade Monitoring Report", July 25, 2018. Available at: https://www.wto.org/english/news_e/news18_e/trdev_25jul18_e.htm

5 Singham, S. A., Tylecote, R. & Hewson, V., 2018. "Freedom to Flourish - UK regulatory autonomy, recognition, and a productive economy", IEA Discussion Paper No.91, London, 2018.

welfare. Anti-competitive regulations can raise costs for businesses or, unlike tariffs, actually prevent products and services being created at all.

Digital

- **General Data Protection Regulation (GDPR) (Regulation (EU) 2016/679)**

GDPR has extra-territorial reach wherever the EU citizens' personal data is processed. It is suspicious of innovation, and its complex requirements mean small entrants find it harder to comply. Fines can range from €10m or 2 per cent of global turnover to up to €20m, or 4 per cent. Smaller firms lack the resources to monitor compliance, and may risk sanction to avoid the compliance costs, making GDPR self-defeating. Firms exiting the market because of GDPR means an anti-competitive outcome.

Chemicals

- **Registration, Evaluation, Authorisation & Restriction of Chemicals (2006) (REACH) (Regulation (EC) No 1907/2006 Jun-07)**

REACH is a framework for chemicals manufacture and use in the EU. Its stated aim is to ensure chemicals produced, imported, sold, and used in the EU are safe. It obliges manufacturers to gather information on new and existing chemicals they use, submitting the information to the European Chemicals Agency (ECHA) for review and inclusion in a central database; the UK has the second highest number of registrations.

The regulation reduces third country exports to the EU by increasing cost and, in some cases, barring products from the single market. In the National Trade Estimate Report on

Foreign Trade Barriers (2017), the US Trade Representative stated:

“REACH impacts virtually every industrial sector... It imposes extensive registration, testing and data requirements on tens of thousands of chemicals. REACH also subjects certain identified hazardous chemicals to an authorisation process that would prohibit them from being placed on the EU market unless a manufacturer or user has obtained permission from the Commission... REACH appears to impose requirements that are either more onerous on foreign producers than EU producers or simply unnecessary.” Its report added: “WTO Members have emphasised [the] problems producers have in understanding and complying with REACH’s extensive registration and safety data information requirements”.

The Commission itself admits this is: “one of the most difficult pieces of legislation for industry to deal with — in particular SMEs”. Some businesses have moved production overseas to avoid it, or exited the market completely, while testing costs are often high, harming profitability and cutting smaller firms out of the market. The result has been to drive some production out of the EU to avoid the regulations or for companies to leave the market altogether, thereby lowering competition and eventually pushing up consumer prices.

Transport

- **Port Services Regulation (EU 2017/352)**

The EU’s Port Services Regulation (EU 2017/352) was designed to improve competition and financial transparency between continental EU ports, 80% of which are state owned. The regulation seeks to achieve fair competition in the sector, especially between the larger container ports. Few doubt that the use of public infrastructure funding has distorted

competition in EU ports. For instance:

- Dutch ports are exempt from corporation tax
- Antwerp, Bremerhaven, and Hamburg's infrastructure costs are covered by the state
- French and Belgian ports receive tax breaks

All these are contrary to EU state aid rules and create a competitive advantage over ports in other member states.

The UK's much smaller and almost all privately-owned port operators are already extremely competitive; there are over 80 ports in the UK. This EU regulation however would add to cost pressures on UK operators, while eroding their ability to control prices. UK port operators believe that the new rules are unnecessary as they are already competitively managed.

The Ports services regulation is a good example of EU "one size fits all" regulation: while the rules will ensure improved competition in continental EU container ports, the additional compliance costs the regulation imposes will make UK ports less competitive against their continental counterparts, forcing them to pass on costs to the consumer.

The EU is also pushing its regulatory system on the rest of the world. GDPR is one example of this. Another example includes the sector-specific Agreement on Conformity Assessment and Acceptance (ACAA) with Israel for pharmaceuticals: this requires full alignment with EU rules. Through the EU-Switzerland relationship in market integration, Switzerland applies EU product standards to its own market.⁶

⁶ European Scrutiny Committee, 2018

Available at: <https://publications.parliament.uk/pa/cm201719/cmselect/cmeuleg/301-xxvi/30104.htm> p. 1.44

Finance

- **The Solvency II Directive (Directive 2009/138/EC Jan-16)**

Solvency II is the EU's prescriptive prudential regime for insurance. The Directive puts considerable emphasis on unreliable data for infrequent events, thus increasing capital required, which in turn excludes new entrants from the market and has forced operators out of some product lines. Higher capital requirements create higher operating costs, which become higher premiums for consumers.

- **The Markets in Financial Instruments Directive (MiFID II) (Directive on Markets in Financial Instruments, repealing Directive 2004/39/EC of the European Parliament and of the Council)**

MiFID II took effect in the UK in January 2018. Its stated aim was increased transparency across EU financial markets, and standardised regulatory disclosures. It covers almost all trading, including bonds and securities, reporting requirements, large transaction limits, brokers, exchanges, and retail clients. It has created a major compliance burden for the industry, increasing the transaction data-gathering requirement by 270%, as well as adding best execution policies and onerous private client regulations. MiFID II has made off-exchange trading in volume more difficult for large clients and forced investors to pay for company research reports. All this has increased compliance costs and complexity, reduced the number of firms willing to provide private client services and decreased end-user choice but it has not improved liquidity in the markets which most participants believe is the major problem. The requirement to pay for research has encouraged analysts to move their coverage to larger companies, cutting investment in small and medium-sized companies.

Furthermore, the regulation requires transaction reports containing 65 data fields to be stored for every investment and

every client, and by buying agent, selling agent and market, which is particularly onerous for firms dealing for private clients. This will mean, for example, that a private client wealth manager with 2,700 clients will create 175,500 data fields (65×2700) every time they invest in a company. Trades are timestamped to 100 microseconds and transaction data must be stored for at least five years; under the best execution requirements, banks and brokers must be able to show customers that their orders were filled at the best available price. This is expensive for brokers: some orders cannot be filled at this best price, while the broker must make up the shortfall.

These examples illustrate that it will be increasingly important for the UK to have the ability to diverge from EU regulation in order to capture the Brexit Prize, and that any locking in to the EU regulatory system will prevent these gains from being realised. It should also be noted that the direction of travel of EU regulation is likely to accelerate as a result of the UK not having a significant say in these regulations. The move to Qualified Majority Voting in 2009⁷ has meant that the UK has been finding it increasingly difficult to win regulatory battles in COREPER (the Committee of Permanent Representatives to the European Union responsible for preparing the work of the Council of Ministers). This does not include the many occasions when the UK has chosen not to fight, knowing that they would likely lose a vote under QMV. Therefore, any harmonisation to the EU rule-book would be harmonisation to the rule book now, and as it will be in the future.

In this context, the UK government must think carefully not just about the next five or ten years, but the next several decades, and not make decisions now, that lock the UK into a permanent arrangement from which it will be difficult to depart.

The global regulatory system is moving in the wrong direction

There has been a marked increase in the volume of global regulatory barriers and distortions since the Global Financial Crisis.⁸ While the EU is moving in the wrong direction, and imposing its regulatory system on the

⁷ European Parliament (2018). *Fact Sheets on the European Union 2018: The Treaty of Lisbon*. Retrieved on 17th September 2018

Available at http://www.europarl.europa.eu/ftu/pdf/en/FTU_1.1.5.pdf

⁸ Evenett, S., and Fritz, J., "*The Tide Turns? Trade, Protectionism, and Slowing Global Growth*", Global Trade Alert, Centre for Economic Policy Research, London, 2015.

Available at: <https://www.globaltradealert.org/reports/21>

rest of the world, other countries, like China, are in this case adding Chinese characteristics to global standards and pushing these on the rest of the world. The net effect is an increase in prescriptive regulation, which leads to wealth destruction, pushing people into poverty. In this environment, the UK has the opportunity to advocate pro-competitive regulatory policies, and so reverse the tide of anti-competitive regulation that is sweeping the world. If the UK can execute its independent trade and regulatory policy in such a way as to lower these market distortions both at home and in other countries, there could be a significant gain for the world and for the UK.

Trade policy is not only about commercial considerations, but forms a vital part of a nation's geo-strategic and geopolitical approach. Here, also, there are significant gains. There is a battle going on in the world between a system of competition-based capitalism, such as is found in the US, UK, Hong Kong, Singapore, New Zealand and others, and more cronyist systems of capitalism, which we have seen in the former Soviet Union and China, for instance. At the heart of competition-based economies is the market structure – where competition on the merits is the organising economic principle. Cronyism is carried by a network of anti-competitive regulation – on the basis that such regulations are used to damage competitors. But there is also movement between the two. Latin America for the most part (with the spectacular exceptions of Venezuela, Cuba and Bolivia) has been moving away from a fundamentally anti-competitive system towards more competitive systems (especially the CPTPP members, Colombia, Peru and Chile). India is moving slowly away from its anti-competitive past. China initially moved away from its cronyist past after its WTO accession in 2001, only to seem to re-embrace anti-competitive and prescriptive regulation now. The UK can play a major part in this battle, where wealth creation is at stake and where either the new normal will continue, or growth and economic opportunity for all can be created. If it follows the increasingly anti-competitive EU direction in a host of areas, then those countries which do embrace competitive regulatory frameworks will become increasingly isolated, and global firms will increasingly accept the burdens of anti-competitive regulation. The result will be wealth destruction.. Innovation will stall, and those voices who claim that the era of innovation is over will be proved correct.⁹

9 Gordon, R.J., CEPR Policy Insight No 63: *Is US economic growth over? Faltering innovation confronts the six headwinds*. London: Northwestern University and CEPR, 2012.

What is the Role of Business?

Ensuring as positive outcome from Brexit as possible is not just the job of government, it is the job of all of us. This includes the private sector. Business consists of many different categories – global supply chain managers, small businesses, businesses of the future, and new and innovative, entrepreneurial firms. The Brexit narrative seems to have been captured by one part of one of these groups – managers of EU-UK supply chains. Naturally these entities will always wish to preserve the status quo. Many of the gains we have described are not part of their jurisdiction, but are still the concern of the global firms they are part of, and perhaps most critically of the shareholders of those firms. All firms should ask not what the EU-UK supply chain needs, but what do they want the world to look like. If there is, as we describe, an opportunity to unblock stalled trade agendas, and unlock wealth by making global supply chains more competitive, then global firms and their shareholders' interests are best served by recognising these opportunities. It is business that should be most concerned about the rise of anti-competitive regulatory frameworks as this will ultimately mean a market of ever decreasing size. Incumbent businesses may prefer to have an increasing share of a declining market, but this is a small corner of the total private sector. All businesses are also consumers of something, and lowering their costs by greater competition is a benefit for all. Shifting the discussion to one focused on consumers and consumer welfare will be very important.

Determining the Scale of the Prize

The prize is determined by the operation of the UK's independent trade and regulatory policy. While the gains from tariff reductions can be modelled relatively easily, the gains from a reduction of behind the border barriers – the new barriers in trade – are more difficult to model.

Governments usually massively underestimate the gains of international trade agreements. In New Zealand, for example, the authorities underestimated the benefits of the New Zealand-China FTA by some 500% (including estimating a level of exports for twenty years after the deal, which was in fact reached in just twenty months)¹⁰. The US ITC noted the difficulties they encountered in modelling the TPP.

Meanwhile, it has become possible over the last twenty years to model the costs of the 'anti-competitive market distortions' that burden otherwise prosperous nations when they are encumbered by the needlessly

¹⁰ New Zealand Ministry of Foreign Affairs and Trade (2008), *National Interest Analysis: New Zealand – China Free Trade Agreement*, Wellington.

burdensome and growth restricting regulations that issue forth from political systems like the EU in particular, and, conversely, the opportunities to realise prosperity that can be realised by leaving such a system. To take just one example, the OECD has shown that the ability to reform regulations – in essence, a country's economic ecosystem – in the direction of pro-competitive reform, adds as much as 10-12% to the GDP of developing countries. Similarly, analysis by the Australian Productivity Commission has found that pro-competitive reform of regulation could boost Australian GDP by between 2.5% and 5.5%. This does not necessarily mean deregulation, but to the contrary and as we will describe, means reform that improves consumer welfare and releases growth.

There is significant evidence that a reduction of distortions can lead to very large economic gains.^{13 14 15 16 17 18} Of course, there are many cases where government intervention is needed, where failure to act would indeed increase distortions in the economy, including such precautions as ensuring clean air and water. But no modern economy can thrive if groups of firms are given unfair advantages over others by government action instead of their innate advantages.

Modelling the Brexit Prize

Beware the consensus

The consensus on modelling Brexit, including assessments by the OECD, IMF, LSE and NIESR, as well as the government's own published analysis, is that the long-term economic impact will be negative. However, this observation is not as persuasive as it may first appear.

For a start, these studies make similar assumptions and judgements about what Brexit will mean in practice, and apply these inputs using similar methodologies to similar models. There is clearly a risk of "group think" here. If these inputs and tools are wrong, or simply incomplete, the conclusions are likely to be wrong too.

What's more, the upfront costs of Brexit (notably any increase in barriers

13 Shanker A. Singham and Alden F. Abbott, "Enhancing Welfare by Attacking Anticompetitive Market Distortions", *Revue Concurrences*, No. 4–2011 (November 2011).

14 Shanker A. Singham, U. Srinivasa Rangan, and Robert Bradley, "The Effect of Anticompetitive Market Distortions (ACMDs) on Global Markets", *Revue Concurrences*, No. 4–2014 (October 2014).

15 Shanker A. Singham, A. Molly Kiniry, Dr U. Srinivasa Rangan and Robert Bradley, "Introduction to Anti-Competitive Market Distortions and the Distortions Index", Legatum Institute, London, 2016

16 Bhagwati, J. *Weltwirtschaftliches Archiv* (1989) 125: 17. <https://doi.org/10.1007/BF02707517>. This thinking builds on a body of work on domestic distortions in the 1980s by Bhagwati and Krugman.

17 Krugman, P., "A 'reciprocal dumping' model of international trade", *Journal of International Economics*, Volume 15, Issues 3–4, November 1983, Pages 313-321

18 Bhagwati, J., "Shifting Comparative Advantage, Protectionist Demands, and Policy Response", in "Import Competition and Response", University of Chicago (1982), 151-196.

to trade with the EU) are easier to identify and quantify than the benefits (gains from lowering barriers to trade with the rest of the world and regulatory optimisation at home), which, although potentially larger, may also take longer to materialise. On top of this, the potential costs may be concentrated among a relatively small number of losers, who are better able to mobilise in lobby groups. In contrast, the potential benefits are spread across a much more diverse range of people, usually consumers rather than producers, without such a strong voice. This reinforces the unfortunate tendency to regard the UK's departure from the EU as an exercise in 'damage limitation', rather than a set of opportunities to be maximised.

The debate many years ago about whether the UK should join the euro illustrates both these points. It's easy to forget, but there was a strong consensus both among academic economists¹⁹ and business leaders²⁰ that the UK should adopt the single currency. The CBI²¹ and auto sector lobbied particularly hard in favour, prompting headlines such as "Britain must join euro, says car industry".²² Most people surely now accept that what was then conventional wisdom has proved to be wrong.

Now, many of the same voices are arguing that it is essential to keep trade with the EU as 'frictionless' as possible, by retaining membership of the single market and/or customs union. But if frictionless trade were indeed the overriding concern, the UK should also still adopt the euro, which would reduce transactions costs, eliminate currency fluctuations against the euro area, and improve price transparency. These would all be relatively tangible benefits.

But again, most people surely still accept that these benefits of euro membership would be outweighed by the costs, even though these costs are harder to quantify. The costs of euro membership include the loss of independence on monetary policy, lack of flexibility against non-euro currencies, and a raft of additional obligations to other members of monetary union. There is a simple parallel here with the loss of independence on trade policy and regulatory autonomy that comes with membership of the EU.

Finally, it is important to keep a sense of perspective. People like specific numbers (all the better to paint on the side of a bus). But these need to be

19 The Economist (1999). Economists for EMU. Available at <https://www.economist.com/britain/1999/04/15/economists-for-emu>

20 Morgan, O. "CBI survey shows strong support for euro", The Observer (1999). Available at <https://www.theguardian.com/business/1999/jul/18/observerbusiness.theobserver>

21 Trefgame, G. "CBI tells Blair to get off the fence and back euro", The Telegraph (2000). Available at <https://www.telegraph.co.uk/news/uknews/1347701/CBI-tells-Blair-to-get-off-the-fence-and-back-euro.html>

22 White, M. "Britain must join euro, says car industry", The Guardian (2001). Available at <https://www.theguardian.com/business/2001/jan/15/emu.carindustry>

put in context. For example, let's suppose that conventional modelling of all the easier-to-quantify costs and benefits of Brexit suggests that the level of GDP would be 5% lower than otherwise over a 15-year period.

However, this would be relative to a baseline where GDP might be 25% higher (if trend growth is assumed to be 1.5% per annum), or 30% higher (1.75%). In other words, GDP would still increase by between 20% and 25% over this period, even without allowing for the harder-to-quantify gains, both economic and non-economic, that the departure from the EU would bring.

Weaknesses in the Whitehall analysis

Turning to the modelling of Brexit itself, it makes sense to start with the government's own analysis.

The latest official analysis of the long-term economic implications of Brexit is the Whitehall briefing²³ of January 2018. This is actually no more than a set of PowerPoint slides and the briefing itself acknowledges that this work is preliminary and incomplete (every page is stamped 'draft provisional results'). Nonetheless, this has not stopped the results from being taken by some as definitive proof that GDP will be lower in all scenarios.

In short, the report modelled three arrangements for future trade between the UK and the EU, each based on existing precedents:

1. A European Economic Area (EEA) scenario (similar to the 'Norway option'), where the UK keeps most of the rights and obligations of the single market, but leaves the customs union;
2. An FTA, where the UK leaves both the single market and customs union and settles for a standard 'low access' free trade agreement (similar to, but not necessarily as good as, the EU-Canada deal);
3. A 'no deal' WTO scenario, where the UK and EU simply trade on World Trade Organisation rules, without an FTA.

The results are presented in terms of the impact on cumulative GDP over a 15-year horizon, relative to a baseline scenario (the 'status quo') where the UK effectively remains in the EU. The central estimates are that GDP

23 Exiting the European Union Committee, "EU Exit Analysis – Cross Whitehall Briefing", House of Commons, January 2018.
Available at: <https://www.parliament.uk/documents/commons-committees/Exiting-the-European-Union/17-19/Cross-Whitehall-briefing/EU-Exit-Analysis-Cross-Whitehall-Briefing.pdf>

would be 1.6% lower than otherwise in the EEA scenario, 4.8% lower in the FTA scenario, and 7.7% lower in the WTO scenario (the range on the last of these being -5.0% to -10.3%).

There are, however, many weaknesses in the analysis. Some of these are not necessarily critical. For example, the Whitehall Briefing does not model actual government policy (whether this was the Canada plus model favoured at the time, or the new Chequers Plan). But it is not unreasonable to argue that, if the report's assumptions and methodology are correct, the UK would land somewhere in the range of the three scenarios that it does quantify.

There are six more serious problems. First, the Whitehall Briefing assumes that there will be a large increase in non-tariff barriers (NTBs) between the UK and the EU, especially in a 'no deal' WTO scenario, and that these will have a large negative impact on trade and productivity. Indeed, this is a key assumption in most such studies.

This can be challenged in many ways. Technology is continually reducing the costs of customs NTBs, so it is wrong to assume that the costs in future would be the same as they would be now. This is a good example of the risks in extrapolating current thinking to make forecasts over a period as long as 15 years. The UK and EU will also have the same regulations and standards at the point of departure. This should mitigate the impact even in a 'no deal' WTO scenario, where the EU would treat the UK in the same way as any other third country with whom it does not have an FTA. Finally, estimates of the costs of erecting new trade barriers are typically based on the assumption that most, if not all, of the benefits of previous reductions in trade barriers and closer integration would be lost, even where these have been locked in.

Second, the results of the FTA and (especially) the WTO scenarios in the Whitehall Briefing are made worse by the assumption that the UK would choose to impose tariffs on imports from the EU, rather than maintain the level playing field required under WTO rules by lowering tariffs on imports from the rest of the world. This assumption, again common to most of these studies, turns a potential opportunity for gain into a loss.

Third, the results of these two scenarios are also made worse by the assumption that the UK government would restrict EU migration (with no offsetting increase in migration from the rest of the world) in ways that exacerbate skills shortages and undermine productivity. Like the decision on tariffs, that's a mistake that the government can avoid.

Fourth, the Whitehall Briefing is skimpy on its assessment of the benefits of new free trade deals. The headline numbers only include the boost to GDP from a deal with the US, itself estimated at a low 0.2% of GDP. It does mention that the inclusion of other deals would provide a total long-term increase of up to 0.7%, but again this seems small. Many previous studies have underestimated the benefits of liberalisation, especially when extended to NTBs that the Whitehall Briefing assumes will remain high.

Fifth, the Whitehall Briefing makes little allowance for gains from regulatory optimisation. To be clear, the UK is already one of the more liberalised economies in the OECD, let alone the EU. But this does not mean it cannot do better still.

Sixth, the savings on contributions to the EU budget are excluded from the headline analysis (presumably because they may not translate 1-to-1 to an increase in GDP). Instead they are considered separately in a section on fiscal implications, which concludes they would be dwarfed by the fiscal costs. But these costs mainly follow from the finding that the economy would be a lot weaker. If that is wrong, the fiscal numbers are wrong too. It certainly seems odd not to allow any credit for savings which might amount to 0.5% of GDP each year, or a cumulative 7.5% of GDP over a 15-year period.

A brief comparison with other studies

The Whitehall Briefing also cites studies by other organisations which arrive at a wide range of estimates. Some of these suggest that the long-run impact of Brexit would be a much smaller negative than the official figures, or that it would be positive:

- Oxford Economics²⁴ estimated the loss in GDP at between 0.1% and 3.9%;
- PWC²⁵ estimated the loss at between 1.2% to 3.5%;
- Open Europe²⁶ estimated the loss at 2.2% in a worst-case scenario, but with a potential gain of 1.6% in a best-case scenario;
- Economists for Free Trade²⁷ have estimated a gain of 7% even in a WTO scenario (comprising a 4% gain from a net reduction in trade barriers, 2% from regulatory optimisation, and a further 1% from fiscal savings).

24 Oxford Economics, "Assessing the Economic Implications of Brexit", 2016.

Available at: <https://www.oxfordeconomics.com/brexit>

25 <https://www.pwc.co.uk/economic-services/assets/leaving-the-eu-implications-for-the-uk-economy.pdf>

26 Open Europe, "Where next? A liberal, free-market guide to Brexit", 2016.

Available at: <https://openeurope.org.uk/intelligence/britain-and-the-eu/guide-to-brexit/>

27 Economists for Free Trade, *A World Trade Deal: The Complete Guide*, 2018

Available at: <https://www.economistsforfreetrade.com/wp-content/uploads/2018/09/A-World-Trade-Deal-The-Complete-Guide-Final-Upload.pdf>

The IEA's own modelling work²⁸ is focusing on the benefits of regulatory optimisation and the reduction of anti-competitive market distortions. (This does not mean abandoning safety or quality standards that are proportionate and science-based, and which apply equally to domestically-produced goods and services.) Preliminary results suggest that a 30% reduction in these sorts of distortions between key trading partners by 2034 could increase the GDP of the US, CPTPP-11 plus UK by up to 7.25%, compared to where it would otherwise have been.²⁹

There are four key points to take away.

First, modelling the economic impact of Brexit is inherently difficult, partly because the longer-term benefits are harder to quantify than the initial costs. This reinforces the danger that policy-makers focus too much on keeping as close as possible to the status quo, rather than seeking an outcome that makes the most of the opportunities created by the UK's departure from the EU.

Second, the conventional wisdom has often been wrong (for example, on the case for joining the euro, and even the immediate economic impact of a vote to leave the EU, which, although negative has been much less than many feared³⁰). This does not mean, of course, that the consensus is wrong this time too, but it should be taken with large pinch of salt.

Third, estimates for the impact need to be put in their proper context – recognising the uncertainties and kept in perspective, especially when they represent relatively small changes in the level of GDP compared to the growth that might otherwise be expected over long periods.

Finally, it is important not to pin too much on any number. As the Whitehall Briefing itself notes, “*excessive weight should not be given to single-point estimates, given uncertainties, ranges of opinion on assumptions, global and sector trends and a variety of potential end states*”. Instead, it should be recognised that alternative modelling of the economic impact of Brexit can produce very different results – both positive as well as negative.

Given that all the major contexts in which the Brexit process sits are moving in a negative direction, the UK may be able to make significant gains if it adopts an aggressive independent trade and regulatory policy designed to knock down barriers at home and abroad. This, then, points us to the prize that the Prime Minister once spoke of: an economy typified once more by high growth, a world of global trade with barriers being reduced

28 Singham, S. A., Tylecote, R. & Hewson, V., 2018. "Freedom to Flourish - UK regulatory autonomy, recognition, and a productive economy", Institute of Economic Affairs, London, 2018.

Available at: https://iea.org.uk/wp-content/uploads/2018/07/DP91_Freedom-to-flourish_web-002.pdf

Singham, S.A., Kiriya, M., Rangan, S.U., and Bradley, R. "Introduction to Anti-Competitive Market Distortions and the Distortions Index" (September 2016). Available at:

<https://www.li.com/activities/publications/introduction-to-anti-competitive-market-distortions-and-the-distortions-index>

29 Note that the gains would not be shared equally across all parties but this gives a sense of the scale of reduction in distortions and behind the border barriers.

30 Jessop, J., "GDP already hit 2.1% - And it will only get worse", Institute of Economic Affairs, 2018.

Available at: <https://iea.org.uk/publications/gdp-already-hit-2-1-and-it-will-only-get-worse/>

not rebuilt, developing countries able to export with increasing freedom to our country and to others, and the barriers to trade behind national borders that discriminate against our imports being reduced, so that our service-oriented economy is supercharged by access to new markets and sources of growth.

Given that there is ample evidence that the potential gains to the world are significant, it is the UK's independent trade and regulatory policy that must be preserved, while at the same time mitigating the damage caused by leaving the EU's institutions.

The disruptions caused by leaving the EU's customs union and single market can be mitigated, as we demonstrate in chapters 2, 4 and 5. What is crucial, however, is that the UK has the ability to realise the opportunities that can be set before it, which will mean that any disruption costs will be strongly outweighed, bearing in mind that EU regulation is not static but evolving.

Chapter Two

How Independent Trade and Regulatory Policy Delivers the Brexit Prize

It is the capacity to apply an independent trade and regulatory policy that gives rise to the economic gains of the Brexit Prize. To make the most of this exercise, the UK should follow an integrated trade policy strategy based on **four fundamental pillars**.

All independent countries have some variant of a four pillared trade policy. This includes autonomy over their domestic regulatory settings. To have a credible and executable **independent trade policy**, the UK must have **control over its tariff schedules**, and **domestic regulatory autonomy**. Without both of these, it will not be a **credible trade partner**, and this precludes being a member of the customs union and the single market or either of them. The nature of the UK's economy also determines how it should proceed. If the UK economy was dependent, in trade policy terms, on securing agriculture or industrial goods tariff reductions, then some of these might be secured even with industrial goods regulatory harmonisation with the EU. It is because the UK is a heavily services-based economy, and the barriers to exports of services are predominantly related to regulatory issues, that it must have maximum leverage to secure reductions in these barriers around the world by having flexibility over its own regulatory system. As we briefly outline the different pillars here, it is crucial to have a combined and coherent approach to all of them, and not, as the UK government has done so far, to bifurcate the EU process from the rest of the UK's independent trade and regulatory policy.

We discuss these pillars in greater detail in Chapter 4, but a summary is necessary in order to then discuss how the pillars interact with each other. The UK is playing chess on multiple chessboards, and one of the most troubling aspects of the negotiations so far has been the propensity of the UK to lose sight of the non-EU chessboards so that the negative impact across these other pillars of concessions made to the EU are not fully understood in real time. This is the where we have been led in negotiation by the EU.

Unilateral

These are the things that the UK can do unilaterally, **both in trade policy terms (e.g. its own tariff settings) as well as domestic regulatory choices**. Unilateral regulatory change does not mean massive deregulation, but better, pro-competitive regulation (which is also in line with accepted best practice as set out in the OECD's regulatory toolkit³¹ and competition assessment toolkit,³² and the work of the International Competition Network).³³

Bilateral

The UK can undertake negotiations of a **number of bilateral agreements simultaneously**. The **EU agreement itself is one part of this bilateral agenda**. While this has occupied most of the bandwidth in Whitehall for understandable reasons, it is critical that independent trade and regulatory policy is conducted holistically, and we do not bifurcate the EU piece from independent trade and regulatory policy generally.

The major markets with whom the UK has trade agreements through the EU – the EU-X agreements can be replicated between the UK alone and the partner country if the partner country agrees. EU cooperation is necessary to the extent that both parties would want to have regional cumulation of origin so that supply chains involving both UK and EU content can enter the third country party at the preferential rate. It is unlikely that any such third country would resist this as it would be the price for continued access to the UK market, and can be accomplished as long as the EU's and UK's agreements with the same country have the same rules of origin. Fortunately, EU rules of origin are relatively liberal at the moment, and there would be no particular reason for the UK to diverge from these.

Additional bilaterals can be negotiated where the EU currently has none, and the UK should focus on major trading partners such as the US, Australia, New Zealand, the Gulf countries, India and China.

Plurilateral

The major plurilateral arrangements which the UK could accede to at the moment include the CPTPP, NAFTA, and the Pacific Alliance. The CPTPP is one of the most advanced trade agreements in the world, and can

31 OECD, *Regulatory Toolkit*, accessed 09/2018.

Available at: <https://www.oecd.org/cleangovbiz/toolkit/regulatorypolicy.htm>

32 OECD, *Competition Assessment Toolkit*, accessed 09/2018.

Available at: <http://www.oecd.org/daf/competition/assessment-toolkit.htm>

33 International Competition Network, 2009. *RECOMMENDED PRACTICE ON COMPETITION ASSESSMENT*. [Online] Available at: <http://www.internationalcompetitionnetwork.org/uploads/library/doc978.pdf>

become a trade policy centre of gravity as countries around the world seek to join.³⁴ This enables the UK to increase its access to the fastest growing markets in the world.

Multilateral

The multilateral pillar relates to what we can do **through our WTO transition** and afterwards. Full flexibility here is very important as the UK will need to be able to offer further liberalisation in the future, i.e. soon.

An Integrated Trade and Regulatory Policy and the need to exploit positive interactions and minimise negative interactions between pillars

Very little attention has been paid to how the different processes the UK is embarked on impact each other, and how the UK can use these interaction effects to its own advantage. Given that managing this process can be the difference between a good result and a bad one, understanding and using these interactions is a very high priority. Progress in some of these different pillars or areas will have an impact on other negotiations and other pillars, especially the EU negotiations. Some of these interaction effects are positive for the UK, while others are negative. For example, if the UK is able to progress its US FTA and CPTPP accession, it is much more likely to have a better negotiation with the EU. Similarly, if it looks to tariff-rate quota (TRQ) partners that it will not have enough control over its tariff schedules and sufficient regulatory autonomy, then they may seek to get as much access as they can in the TRQ process, as opposed to gaining that further access in a subsequent FTA, because they will no longer think such an FTA is possible.

It is not possible to list all of the interaction effects between the four pillars in a single document, but it is useful to consider some examples which demonstrate the need for a coherent strategy.

34 Recently South Korea formally applied to join CPTPP: "S. Korea Decides To Join CPTPP | WTO And International Trade Policies". 2018. Wtocenter.Vn. <http://wtocenter.vn/tpp/s-korea-decides-join-cptpp>.

Consider the UK's application to accede to the Government Procurement Agreement, one of the WTO agreements to which the UK has to accede. The EU requested that they have a role in that accession process, and agreed to assist the UK in that process. When the EU reneged on that offer, the UK's accession process was temporarily off track. Here the decision to follow the EU's lead stemmed from an interpretation of the duty of sincere cooperation required by article 4 of the Treaty on European Union "to assist each other [the EU and Member States] in carrying out the tasks which flow from the Treaties"³⁵ which, when followed to its logical conclusion, requires the UK to accede to many EU suggestions where a different approach would lead to gains in the other, non-EU pillars. The result of this, if the UK emerges from the EU without being a member of the GPA would be damaging to many UK industries. This is an example where the UK should conduct its own GPA negotiations on a bilateral basis with its trading partners without EU participation even if this has an impact on the dynamics of the UK-EU negotiation.

Consider the proposition in the draft Withdrawal Agreement that the duty of sincere cooperation and common commercial policy apply during the Transition Period. Viewed through a purely EU lens, one might be forgiven for thinking that this is a reasonable EU request. However, the application of these two principles could have serious consequences for any attempt to negotiate seriously with other countries and thus activate the other non-EU pillars of UK trade policy in a timeframe that will help the EU negotiation. These negotiations are intended to be carved out of the application of the duty of sincere cooperation by article 124(4). However in practical trade policy terms, if a member state is unhappy with the UK's negotiating approach with other countries, it can pressure the other country on the basis that the UK is still bound by the common commercial policy. The UK will have to demonstrate a much more robust approach to the duty of sincere cooperation, common commercial policy and the carve-out, than it has so far demonstrated. There is little evidence that this is about to change.

35 Elsuwege, P., "The duty of sincere cooperation and its impact for the national interest of EU Member States in the field of external relations", Working Paper, UCAES, 2018.

Consider the UK's acceptance of the position in the Joint Report of December 2017 on the Irish Backstop. Viewed through the lens of the EU only, the backstop seems reasonable enough. It is an insurance policy just in case no FTA is concluded. However, from the perspective of the rest of the world, the backstop removes the EU's incentive to negotiate with the UK at all. The backstop then becomes an indefinite state and the UK will have either ceded sovereignty over a part of its territory or submitted to remaining in a form of customs union and single market.

Consider the Facilitated Customs Arrangement and its predecessor, the New Customs Partnership. If one ignores the impact of these arrangements on the rest of the world, they appear to mitigate the increased customs clearance costs brought about through leaving the customs union, and moving to a free trade relationship. However, from a rest of the world perspective, these options would damage the ability to execute the other pillars of trade policy, because they nullify the potential gains which can arise from customs concessions which the UK might give to another trading partner.^{36 37}

There are also positive interaction effects which would be lost if the UK continues to separate trade policy between the EU and rest of the world. Consider the WTO transition and TRQ³⁸ negotiations and Aggregate Measure of Support³⁹ (AMS) offers. The EU has sought to negotiate the transition of TRQs jointly with the UK or on the UK's behalf. Viewed through the lens of the EU only, this might seem a reasonable request. Viewed through the lens of the whole of independent trade

36 Victoria Hewson, "*Under Control*", Institute of Economic Affairs, London, 2018.

Available at: <https://iea.org.uk/publications/under-control/>

37 European Foundation, 2018. "*The New Customs Partnership*".

Available at: <https://europeanfoundation.org/wp-content/uploads/2018/05/Customs-Partnership-Briefing.pdf>

38 The tariff rate quota is the agricultural import quota which the UK offers the rest of the world. It has to be separated from the combined EU-28 TRQ, and this has to be agreed by WTO members as part of the laying of the UK's good schedules before the WTO.

39 AMS is the amount of agricultural so-called Amber Box production subsidies WTO members are allowed to claim.

and regulatory policy, the UK's favoured approach would be to negotiate these bilaterally with the countries involved. The UK could then maintain that these TRQ partners should be reasonable with it on the TRQs (agreeing to the UK's idea of splitting the TRQ based on historic market shares between the UK and EU) in exchange for the UK offering further liberalisation in these products relatively quickly, and being a positive force in the WTO. But the TRQ partners would have to be able to convince their agricultural lobbies that this was indeed possible, and that it would happen quickly. Hence the length of time of any interim period (the transitional period) after the UK leaves the EU and the time at which actual FTA negotiations with TRQ partners might start is very important. If the UK can negotiate TRQs bilaterally, it might be able to secure a better deal for itself than otherwise.⁴⁰

Because it is so important to manage these interaction effects which often happen in real time and cannot wait for the standard Whitehall write-round process, it is critical that there is **coordination over all of the policy**. Read-across to other agreements is also critical. For example, if the UK proposes language for financial services regulatory recognition, this can be read across to other agreements such as the UK-US FTA. If this language is then agreed in the UK-US FTA, the EU is more likely to agree to it themselves. Unless there is a single mind over all of this policy, errors may continue to be made that have wide-reaching consequences for the UK's ability to capture the Brexit Prize.

⁴⁰ The UK has sought a technical rectification as part of its WTO transition which is sensible – however technical rectification does not require an agreed position with the EU; in any event the EU has moved itself to a modification of its schedules, which the UK may or may not follow. The important point is that whatever process is followed, the UK has the capacity to have direct and credible conversations with its trading partners about the benefits they may secure as a result of the UK's WTO transition.

Chapter Three

Why the Chequers Proposal Removes Independent Trade and Regulatory Policy

In Chapter 1, we described the Brexit Prize and why an Independent Trade and Regulatory Policy is so critical to achieving it. In Chapter 2, we outlined how coordination over all independent trade and regulatory policy is at the heart of that policy. We reviewed examples of how the bifurcation of trade policy into an EU and Rest of World approach has caused problems and will cause problems in the future. We briefly explained what an independent trade and regulatory policy could be expected to achieve.

We now review how the Government's various proposals impact its own ability to execute that policy. The Government, in the Lancaster House speech, expressed an approach that enabled all four pillars of the independent trade and regulatory policy to be meaningfully realised, because the UK would maintain control over tariff schedules and regulatory policy. Indeed this was a critical aspect of the speech itself and its reference to a Brexit Prize.

However, it is our view that the Government White Paper takes that independent trade and regulatory policy off the table, and puts the Brexit Prize out of reach. Despite the White Paper's statements that an independent trade and regulatory policy is still possible, we find that despite the creative attempts by the Government to preserve independent trade policy and also retain sufficient harmonisation to the EU to retain key aspects of free circulation, the White Paper does not achieve this goal for the reasons we set out below.

In addition, there is not, and in fact has never been, any indication as to how its policy positions can be delivered. This is at the heart of our concern about the process. By bifurcating the EU and the rest of the UK's independent trade and regulatory policy, the UK has allowed itself to be trapped on the EU's battlefield, so that it is unlikely to achieve any

optimal results. It has also been very difficult to make any progress with the EU without putting negotiating text on the table, which is another core recommendation of this paper.

The White Paper broadly outlines a free trade area between the EU and UK, with a common rule-book on agri-food and goods in respect of regulations that affect checks at the border. If the “common rule book” was genuinely a result of a shared negotiation of equal partners, then it would not necessarily constrain the UK’s independent trade policy. A comprehensive FTA with a management of differences mechanism could also lead to what could be described as a “common rule book”. However the problems are in the detail of precisely what the “common rule book” is and the limitations in UK deviation from it (see below). The services, investment, government procurement and mutual recognition of occupation licensing provisions are broadly sensible proposals from which negotiating text could be drawn. One of the major issues which troubles trading partners outside of the EU, however, is that arrangements with the EU prevent the UK from being as open as it needs to be, especially in goods and agri-food regulation, in order to secure economic gains. Simply having the ability to negotiate on services does not mean that trade deals can be done in these areas.

The White Paper provides for a common rule-book in goods and agri-food⁴¹, which is by treaty harmonisation with the EU’s rule book with a commitment to harmonise to future EU rules in these areas.⁴² The carve-outs for CAP and CFP, and for marketing and labelling rules do not recognise that most of the trade complaints about EU agricultural policy lie precisely in the SPS area. We have given some examples of these in Chapter 1. Especially given the direction of travel of EU regulation in this area, it is difficult to see how having no flexibility in these SPS areas can lead to trade agreements with others. Not only is the division between services and goods essentially artificial, but any change that the UK might seek would have to go through a complex process involving a joint committee where the EU would ultimately adjudicate on whether the UK was in fact

41 See 1.2.3 & 1.2.4 of Department for Exiting the European Union, 2018. *Policy paper: The future relationship between the United Kingdom and the European Union*.

Available at: <https://www.gov.uk/government/publications/the-future-relationship-between-the-united-kingdom-and-the-european-union/the-future-relationship-between-the-united-kingdom-and-the-european-union-html-version#goods>

42 The language of the White Paper suggests that the rules which will be harmonised in goods and agri-food relate only to their trade across borders, but the SPS and some TBT measures that are caught by these provisions are precisely those that necessitate border inspections for these products. It is true that certain marketing and labelling rules would not be caught by these provisions and a mutual recognition approach such as the White Paper highlights would be appropriate (para 37 at p23) as part of an FTA’s mutual recognition provisions.

harmonised to the EU rule.⁴³ From a trading partner perspective, this means that the UK is severely constrained in its ability to change rules in the area of goods and agri-food, as well as in certain horizontal areas such as labour, and the environment, where non-regression clauses require the UK to maintain all current levels of standards in this area, because it would ultimately be up to the CJEU to decide whether the UK had diverged in an unacceptable manner.⁴⁴ A determination about whether the UK had fallen below the benchmarked level of standards would be determined by the EU with the possible imposition of fines or other “rebalancing mechanisms”.⁴⁵ Under these principles, if the EU and UK could not agree a particular measure, the UK could be fined if it did not include the EU measure into its rule book. Thus any change from the EU’s standards as at the moment of leaving the EU would be liable to be met by the allegation that the UK was violating the agreement on harmonisation to the EU rule book or the non-regression clauses and would lead to protracted debate and litigation, making it very difficult for the UK to improve regulations. A trading partner seeking changes in these areas would also assume that the UK could not, in fact, concede anything, or that the path to a concession was through Brussels not London. This also creates the perverse situation whereby if the UK brings its SPS rules into line with WTO decisions, it could violate the UK-EU non-regression clauses in environmental rules, or could violate the treaty commitment to a common rulebook. Given the direction of travel of those rules, and the EU’s increasing position as an outlier in the world in these areas, the separation between the EU rule book and the position taken by the UK’s other key trading partners is likely to widen even further.

USTR’s National Trade Estimate (the US’ inventory of foreign country trade barriers)⁴⁶ shows that the vast majority of US complaints against the EU relate to rules in goods and agri-food, and so taking these off the table will mean the UK will have no leverage to obtain the changes from the US it needs which would be primarily be in the services area where the barriers are difficult to remove anyway. The same is true of other big agricultural exporters like Australia, New Zealand and many of the CPTPP countries. Acceding to CPTPP, for example, would be very difficult, if not impossible, for a country to do, without control over its regulatory rulebook. If the UK was in practice unable to diverge from the EU, it is doubtful that the large agricultural exporters in the CPTPP would welcome its entry.

43 White Paper, 4.5.144

44 The proposal expressly recognises that the CJEU will be the ultimate interpreter of EU law, not just for the EU but as regards its application in the UK.

45 White Paper, 4.4.1. para 30

46 Office of the United States Trade Representatives, 2018. National Trade Estimate Report on Foreign Trade Barriers. Available at: <https://ustr.gov/sites/default/files/files/Press/Reports/2018%20National%20Trade%20Estimate%20Report.pdf>

It would also be very difficult to improve domestic regulations in line with the recommendations of the OECD^{47 48}, if the UK remained tied to the EU regulatory system in particular and failed to meet CPTPP members' approaches to good regulatory practice. As pointed out in chapter two, the EU appears to be moving away from those standards, not approaching them.

Facilitated Customs Arrangement

The Facilitated Customs Arrangement is drawn from the earlier New Customs Partnership, and contains most of its key elements. These measures have been discussed at length elsewhere,⁴⁹ highlighting the WTO violations in the NCP which have tracked through to the FCA, and the specific reasons why they make an independent trade and regulatory policy very difficult. Others have also noted the WTO illegality of the FCA arrangements. The track and rebate system is likely to be a violation of GATT Art III (National Treatment) as it treats imported products differently from like domestic products.⁵⁰ The FCA could also violate WTO rules on transparency (GATT Article X). WTO members could additionally argue that any negotiated benefits with the UK would be nullified or impaired by this system. In the case of an anti-dumping duty, where the UK might not apply a dumping duty which the EU has in place, the duty recoverable could be quite large, and the cash flow issues for importers significant. Any consumer benefits which the UK could seek to derive from having a more open, liberal anti-dumping policy than the EU would be vitiated by this mechanism. In any event, the EU would have considerable problems if products covered by EU anti-dumping orders were to leak into the EU from the UK.

All that said, the fundamental problem with the FCA is not that it may violate the WTO but rather the impact that it will have on the UK's negotiating flexibility with other countries. In customs, the FCA will have significant impacts on the ability to negotiate with trading partners.⁵¹ Outside the EU, this will have a similar *de facto* effect on trading partners as a customs union, and make it impossible for other countries to fully rely on the tariff

47 International Competition Network, 2009. *RECOMMENDED PRACTICE ON COMPETITION ASSESSMENT*. [Online] Available at: <http://www.internationalcompetitionnetwork.org/uploads/library/doc978.pdf>

48 OECD (2018), OECD Regulatory Enforcement and Inspections Toolkit, OECD Publishing, Paris, <https://doi.org/10.1787/9789264303959-en>.

49 European Foundation, 2018. The New Customs Partnership. [Online] Available at: <https://europeanfoundation.org/wp-content/uploads/2018/05/Customs-Partnership-Briefing.pdf>

50 Lawyers for Britain, "Chequers White Paper Briefing No. 2: Does the Facilitated Customs Arrangement comply with WTO law?", 2018.

Available at: <https://lawyersforbritain.org/chequers-cowhite-paper-briefing-no-2-does-the-facilitated-customs-arrangement-comply-with-wto-law>

51 European Foundation, 2018. The New Customs Partnership. [Online] Available at: <https://europeanfoundation.org/wp-content/uploads/2018/05/Customs-Partnership-Briefing.pdf>

concessions they may nominally obtain as against the EU's common external tariff. Our soundings suggest that no trading partner will take the FCA (or NCP, or similar variant) seriously. From their perspective, they will act as if they were dealing with a member of a customs union.

The White Paper thus limits the UK's control of tariff schedules and regulatory policy through the FCA and harmonised rulebook. This is also the view of leading trade negotiators. Former New Zealand trade minister, Sir Lockwood Smith notes: "if Brexit results in the Chequers approach, with the regulations dictated from Brussels, it's difficult to see how the UK could meet these important [for joining CPTPP] requirements."⁵² Former Deputy USTR, Peter Allgeier notes that "if the UK is merely a smaller version of the EU, then it is unlikely to be a particularly interesting trade negotiations partner. It is precisely the UK's ability to diverge from EU regulation that makes it interesting."⁵³ Former GATT Council Chairman, Alan Oxley noted that under Chequers, "the UK would find itself bound to EU regulations over which, as a partial outsider, it would have no control."⁵⁴

In any trade negotiation, countries need to know that their trading partner genuinely has the ability to grant "concessions" in other areas, so that trade-offs can be made. The more critical an area where trade-offs can be made is to the trading partner, the less likely they will be to give concessions to the UK in areas the UK deems important. The UK needs services barriers removed, which are some of the most difficult areas in which to make progress. The countries with which the UK would most benefit from striking trade deals will need concessions in goods and agri-food for instance, precisely the area where the White Paper limits the UK's ability to make concessions.

The EU as a regulatory outlier

The government seems to assume in its analysis that the EU regulatory system is regarded by the world as a gold standard system. This is not the case. Indeed most of the world regards the EU as the outlier especially in terms of its regulations of goods and agriculture. In goods,

52 Smith, S. L. "*Britain has a golden chance to join the biggest free trade agreement in history*", Conservative Home 2018

Available at: <https://www.conservativehome.com/platform/2018/08/lockwood-smith-britain-has-a-golden-chance-to-join-the-biggest-free-trade-agreement-in-history-but-chequers-is-likely-to-wreck-it.html> [Accessed 11 09 2018].

53 Allgeier, P. F., "*The Chequers proposal would prevent the UK regaining an independent trade policy*", Conservative Home, 2018, Available at: <https://www.conservativehome.com/platform/2018/08/peter-f-allgeier-the-chequers-proposal-would-prevent-the-uk-regaining-an-independent-trade-policy.html> [Accessed 11 09 2018].

54 Oxley, A., "*My reading of the Brexit White Paper suggests the Government doesn't really get what is at stake*", Brexit Central, September 18th, 2018.

Available at: <https://brexitcentral.com/reading-brexit-white-paper-suggests-government-doesnt-really-get-stake/>

the EU's top down approach to standards and the recent imposition of its approach to data protection on the rest of the world is considered deeply problematic.⁵⁵

The White Paper says that the UK and EU set the highest global standards in the SPS area for agri-foods, but here again most of the world has a different view, and considers many of these protectionist and artificially restrictive trade barriers. Indeed, the EU has been found in violation of WTO rules in a number of agricultural sectors, for instance on measures affecting poultry meat from the United States,⁵⁶ and hormone treated meat from Canada⁵⁷ and the US.⁵⁸

In this context, harmonisation to EU rules will be regarded by the world as moving the UK further away from good regulatory practice, and therefore a much less credible and valuable trading partner.

Intellectual Property

The White Paper also states that the UK will seek to remain in the European Patents System and the European Patents Court. While UK intellectual property (IP) law may be similar to EU law substantively, the UK will need to ensure that its courts determine the scope of IP law and policy. Implementation of IP law is a very important aspect of a country's economic policy. A clear statement that property rights will be protected is a strong signal to innovators and investors alike. When countries improve their IP rights, their economic development improves, and venture capital and other financing opportunities are created.⁵⁹ The statement in the White Paper limits the UK's authority over the application of its own intellectual property laws, adopting a unitary approach to patent registration and litigation. If the CJEU decides to adopt a more interventionist approach which erodes patent protection along a similar economic rationale to its approach to competition policy, this may make negotiating agreements with demanders, such as the US, who seek high levels of IP protection, more difficult, and may weaken the UK's domestic environment.

There are also concerns with the non-regression clauses in a number of areas.

55 Office of the United States Trade Representatives, 2018. National Trade Estimate Report on Foreign Trade Barriers. Available at: <https://ustr.gov/sites/default/files/files/Press/Reports/2018%20National%20Trade%20Estimate%20Report.pdf> [Accessed 17 09 2018].

56 EC-Poultry (US), WTO Dispute Settlement DS389, online:

https://www.wto.org/english/tratop_e/dispu_e/cases_e/DS389_e.htm

57 EC-Hormones (Canada), WTO Dispute Settlement DS48, online:

https://www.wto.org/english/tratop_e/dispu_e/cases_e/DS48_e.htm

58 EC-Hormones, WTO Dispute Settlement DS26, online:

https://www.wto.org/english/tratop_e/dispu_e/cases_e/ds26_e.htm

59 See Singham, A General Theory of Trade and Competition: Trade Liberalisation and Competitive Markets, Cameron May 2007 at pp319 et ff

Horizontal Measures in Competition and State Aids

The UK and EU have broadly similar approaches to the implementation of competition law and policy. However, there are significant and substantive areas where differences do arise, and it is likely that the UK will want to have the flexibility to depart from the EU's substantive interpretation of competition law, as well as retain its own procedural rules. It will also want to negotiate global agreements on procedure that the EU may not wish to negotiate, for example the Multilateral Framework on Procedures in Competition Law Investigation and Enforcement (MFP) which has recently been proposed by the US and other leading antitrust agencies.⁶⁰ The UK has an opportunity to be a charter member in a groundbreaking global agreement which will ensure better procedures that protect the rule of law and economic freedom, and ensure that antitrust is administered fairly. The White Paper itself notes that there are aspects of procedural enforcement where the UK is ahead of the EU. The EU is objecting to the MFP, and requiring member states to join it in its objections.⁶¹

With regard to substance, the EU applies a collective dominance approach to single firm conduct which we believe harms consumer welfare in the economic sense. A better approach is to include in a competition chapter in an FTA a framework for cooperation in these areas recognising that the UK may enforce competition law, both in terms of procedure and substance differently than the EU. A sample competition chapter of the FTA is forthcoming. This sort of approach recognises and builds on section 60 of the Competition Act which recognises that there are differences between UK competition law and European law.

The UK should be prepared to carry over and agree state aids disciplines in the UK-EU agreement and a chapter on state-aids should be relatively easy to conclude. It is certainly in both parties' interests that the other is not able to confer aid on an undertaking and thus distort market competition.

Horizontal Measures in Labour and Environment. With regard to horizontal measures, there are provisions of the Government's position in the White Paper that would have a serious impact on the ability of the UK to have a competitive economy. Although the provisions in these areas in the White Paper are non-regression clauses (rather than outright harmonisation), and therefore not obliging the UK to keep up with the EU's changes, any change the UK does make may be regarded by the EU as a lessening of standards.

60 *Fresh Thinking on Procedural Fairness: A Multilateral Framework on Procedures in Antitrust Enforcement*, United States Department of Justice, Washington, 2018.

61 The impasse on the MFP is but one example of likely future clashes between what the UK will seek to do in global standard setting and rule-making bodies and what the EU will allow it to do if alignment is too tight.

The European Union has recently been moving in an anti-competitive direction in these areas, as evidenced by changes in EU labour rules,⁶² the working time directive,⁶³ application of the EU's own interpretation of the precautionary principle,^{64 65} and REACH,⁶⁶ among others.⁶⁷ Under the White Paper proposal, if the UK chooses to move away from the EU in any of these areas it is likely to be treated as a reduction in standards, the ultimate arbiter of whether the UK has violated the provisions is the CJEU. This is likely to prevent the UK implementing pro-competitive regulation in these areas, even if such reforms preserve or improve existing standards of protection.

Exemption from the EU social chapter had previously been a core element of UK policy since its accession to the Common Market itself. This was to ensure that the UK could set its own labour market policies and thus to ensure a more flexibility – one more conducive to job creation, and a dynamic economy. The UK has since embraced a number of labour policies which go well beyond what can be seen to be reasonable protections of workers. Indeed some of these policies make it much harder to hire new workers. The opportunity presented by Brexit should not be lost by locking the UK into EU labour policies and practices which have been demonstrated to have slowed the European economy.⁶⁸ In many areas, UK organisations have called the Working Time Directive, and the Posted Workers Directives examples of overly prescriptive regulation that goes beyond what are necessary for worker protection.⁶⁹

62 The Agency Workers Regulations (AWR) 2010 (Directive 2008/104/ EC Oct-11)

63 The Working Time Regulations 1998 and Working Time (Amendment) Regulations 2003 (Directive 2003/88/EC Oct-98/ Aug- 03)

64 Parsons, D. and Garnett, K., "Multi-Case Review of the Application of the Precautionary Principle in European Union Law and Case Law", Risk Analysis, 37:3, pp 502-516, 2017.

65 Woolcock, S., "The Precautionary Principle in the EU and Its Impact on International Trade Relations", CEPS, Working Document 186, 2002.

Available at: <https://www.ceps.eu/publications/precautionary-principle-eu-and-its-impact-international-trade-relations>

66 Registration, Evaluation, Authorisation & Restriction of Chemicals (2006) (REACH) (Regulation (EC) No 1907/2006 Jun-07)

67 Singham, S. A., Tylecote, R. & Hewson, V., 2018. "Freedom to Flourish - UK regulatory autonomy, recognition, and a productive economy", IEA Discussion Paper No.91, Chapter 5. [Online]

Available at: https://iea.org.uk/wp-content/uploads/2018/07/DP91_Freedom-to-flourish_web-002.pdf

68 Woolcock, S., "The Precautionary Principle in the EU and Its Impact on International Trade Relations", CEPS, Working Document 186, 2002.

Available at: <https://www.ceps.eu/publications/precautionary-principle-eu-and-its-impact-international-trade-relations>

69 See Chapters 3.27 - 3.35 of HM Government, Summer 2014. "Review of the Balance of Competences between the United Kingdom and the European Union: Social and Employment Policy." [Online]

Available at: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/332524/review-of-the-balance-of-competences-between-the-united-kingdom-and-the-european-union-social-and-employment-policy.pdf

This is also true of EU environmental protection rules, which is one of the areas where EU regulation is moving in an anti-competitive direction. We are supportive of environmental protection, but it should be noted that European environmental rules apply to many different product categories, and lead to increases in costs for many companies – sometimes they are valid attempts to deal with real environmental problems, but frequently they are disguised methods of protectionism, for instance the EU’s restrictions on citrus imports and certification requirements for Specified Risk Materials.⁷⁰ So agreeing with the EU not to lessen current environmental standards will have wide ranging impacts.

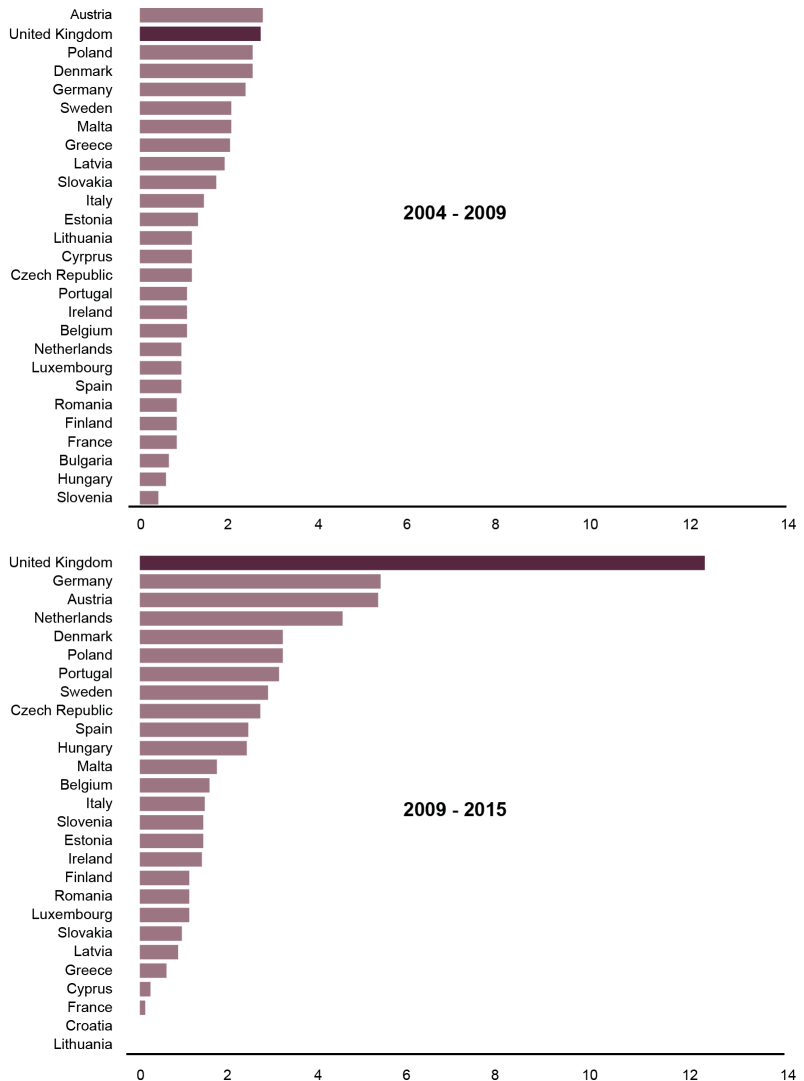
Furthermore, the UK has a history of opposing EU rules in this area. The move to Qualified Majority Voting (QMV) which we discussed earlier has meant that no member state has a veto, and we have seen an increase in the volume of regulation whose prescriptive and anti-competitive nature goes against the grain of how the UK has historically chosen to regulate. Since its introduction in 2009 the UK has lost three times as many of the Council votes it has participated in by proportion as during the previous five years, and more than twice the percentage of the next nearest member nation, see fig 1 below.⁷¹

70 United States Trade Representative, 2017, *National Trade Estimate Report on Foreign Trade Barriers*, pp152-154

Available at: <https://ustr.gov/sites/default/files/files/reports/2017/NTE/2017%20NTE.pdf>

71 *Does the UK win or lose in the Council of Ministers?* Hix and Hageman, UK in a Changing Europe. Available at: ukandeu.ac.uk/explainers/does-the-uk-win-or-lose-in-the-council-of-ministers/

Figure 1: Percentage of times each EU government has been in a losing “minority” in Council votes, as a proportion of all votes it took part in during the 2004-2009 and 2009-2015 periods⁷²



⁷² Figures from: Singham, S., Tylecote, R., and Hewson, V., “*Brexit Inflection Point*”, Legatum, 2017, pp 30. Source of data is reference 78 above.

Numerous UK entities seek mutual recognition, rather than harmonisation, and many have pointed out the damaging consequences of harmonisation. As noted in chapter 1, the goal of the regulatory provisions in any trade agreement are to ensure that both parties satisfy Good Regulatory Practice (“GRP”) and that as much regulatory recognition as possible is achieved in this area.

There is no reason why the UK should accept the position that market access to the EU market should be constrained by differences across the broad horizontal areas like labour and environment. This is not how modern trade arrangements work. Generally other countries provide a level of standards that both sides would agree, as part of their trade agreements. Since the UK and EU-27 consist of advanced economies, agreeing base minimal levels of compliance (such as core ILO standards, and core environmental standards) should be relatively straightforward, but cannot require the UK to follow the EU’s *acquis* in these areas as a precondition to market access.

Remaining in EU Agencies

The White Paper states that there would be three agencies of the European Union that the UK would seek to remain part of, and also seek to have some sort of role in EU rule-making. These are:

1. The ECAA. The European Civil Aviation Authority is the EU regulator for aviation, air safety and related matters.
2. ECA. The European Chemical Agency regulates the chemicals industry especially REACH.
3. EMA. The European Medicines Agency regulates the pharmaceutical industry among other areas.

ECAA

In terms of the UK regulatory rule-book, the ECAA has replaced the Civil Aviation Agency (CAA). There is value in ensuring minimal disruption of air travel, so we are not concerned about this offer. We also do not find that the direction of travel of EU regulation in this area is especially troubling, but it should be noted that under this arrangement, the UK would need assurance that its voice would be heard – which is more likely here than in other areas because the UK includes the world’s third largest aviation area.

ECA

It is understandable that managers of UK-EU supply chains would want the rules that cover their sector not to be affected. However in the chemicals area, we already know the overall direction of travel of EU regulation as exemplified by REACH which has had a serious impact on the chemicals industry in Europe, not to mention increasing costs for consumers of those products, such as the plastics and other related industries. There is a serious risk here that this sort of burdensome and restrictive regulation expands, and that firms around the world regard this as a global standard. This will certainly have a negative impact on innovation.

EMA

What is true of the chemicals industry is doubly true in the case of pharmaceutical and biotech where the UK has a competitive advantage. Already, the global pharmaceutical industry has had difficulty with EU clinical trials directives. In particular, the rules on disclosure of clinical trials data, including disclosure of confidential information released to the EMA has been a problem for pharmaceutical companies. Many member states maintain market access barriers to pharmaceutical products⁷³ as well as taxes that impact various levels of production.⁷⁴ The global pharmaceutical industry in which the UK has a leadership role needs to ensure that the overall climate on pharmaceutical related issues such as patent protection, and patent term extension are as strong as possible and clinical trials and pharmaco-vigilance is as pro-competitive and least distortive as possible. The EU has not taken especially helpful positions in the TRIPs council in the WTO on issues like compulsory licensing. It is not in the interests of the pharmaceutical and biotech industries to become an effective rule taker (it is hard to see how the EU will allow the UK to sit on relevant regulatory promulgation bodies in the European Council for only this sector) for the foreseeable future.

An Alternative Approach

An Alternative Approach, as we note in the following chapter is to offer an advanced free trade agreement with detailed chapters which support the provisions set out in this chapter and ensure that the UK's ability to operate on the global stage (and thus capture the benefits of the Brexit Prize outlined in Chapter 1) is not compromised. A competition and state aids chapter should give confidence to the EU that it is not the UK's intention to use government subsidy and tolerance of cartels and anti-competitive mergers

73 Office of the United States Trade Representatives, 2018. National Trade Estimate Report on Foreign Trade Barriers. [Online]

Available at: <https://ustr.gov/sites/default/files/files/Press/Reports/2018%20National%20Trade%20Estimate%20Report.pdf>

74 Ibid. pp. 195

to drive UK competitiveness. Issues like labour and the environment should be treated as they are in all other trade agreements, with commitments that countries make to enforce their own laws and abide by international rules.

Chapter Four

A Deeper Dive into the Four Pillars of Independent Trade and Regulatory Policy

A. Unilateral

Domestic tariff and regulatory improvements

The UK should **lower tariffs** where it can, especially on food, clothes and shoes. These tariffs keep the price of basic goods and staples higher, which harms the poorest in society the most. The UK should lower tariffs to zero on a unilateral basis for intermediate goods, so that its domestic manufacturing competitiveness can increase.

It should **lower tariffs to zero** for agricultural products that it does not produce, increasing the supply of these goods into the UK market. These products include products like bananas, oranges, rice and avocados.

- In the event that no free trade agreement with the EU can be concluded before the UK's departure from the customs union and single market (because the parties are unable to agree on a withdrawal agreement that is duly ratified, or they do, but no FTA emerges during the Transition Period), then to combat potential food price inflation that could otherwise be caused by the application of UK tariffs set at the Common External Tariff rate (CET) to the imports of European agri-food the UK will need to either:
 - lower agricultural duties on agri-food to zero on a most favoured nation (MFN) basis
 - not apply its bound rate (to all parties), which will be the CET at the point of exit, effectively lowering the applied rate to zero.

- Recognising that this would subject UK farmers to competition from highly subsidised agri-food from continental Europe and elsewhere, the UK would have to develop a mechanism which would let UK farmers challenge such distortions through countervailing duties, or through a mechanism to deal with Anti-Competitive Market Distortions (ACMDs).^{75 76 77} This would provide a mechanism through which a level playing field could be achieved (a level playing field does not exist now however: UK farmers must compete head on with heavily subsidised continental European farmers).

At the heart of the **domestic competitiveness agenda** is ensuring that markets are truly free and competitive. This refers to domestic anti-competitive barriers, and foreign trade and competition barriers, which affect the global supply chain and impact the UK economy. International trade has moved on to a world of competing supply chains, but governments sometimes operate as if companies simply produce a product in one country, then sell it in another. A selection of actions follows.

Creation of UK Competitiveness Czar

The UK's competitiveness relies on a reduction of barriers abroad, but also critically a reduction of barriers at home. This goes beyond the current activities of the Competition and Markets Authority (CMA), although it is consistent with the competition advocacy mandate of the CMA.

This process can be led by a Competitiveness Czar based in the Prime Minister's Office, but whose remit covers barriers faced by UK firms, at home or abroad, and who will liaise with all relevant Government Departments and agencies, including the Department of Business Enterprise, Innovation and Skills (BEIS), the CMA, the Bank of England, the Department of International Trade (DIT), HM Treasury ("HMT") and the Department of the Environment, Food and Rural Affairs ("DEFRA").

Free trade, and free and competitive markets, have done more to lift people out of poverty than any other policy or practice: but there are many

75 Singham, S. A., Kiniry, M., Dr Rangan, U. S., and Bradley, R., "Introduction to Anti-Competitive Market Distortions and the Distortions Index", Legatum Institute, London, 2016 Available at: <https://www.li.com/activities/publications/introduction-to-anti-competitive-market-distortions-and-the-distortions-index>

76 Singham, S. A. and Abbott, A. F., "Enhancing welfare by attacking anticompetitive market distortions", *Concurrences* No. 4, 2011 Available at: <https://www.ftc.gov/sites/default/files/attachments/key-speeches-presentations/ssrn-id1977517.pdf>

77 Abbott, A. F. and Singham, S. A., "*Competition Policy and International Trade Distortions*", in *European Yearbook of International Law* 2013, Springer, 2013 Available at: http://thf_media.s3.amazonaws.com/2015/pdf/9783642339165-c1.pdf

areas where the UK economy is uncompetitive, because the market does not work properly. These can be divided into horizontal anti-competitive practices, laws and regulations; and sector-specific vertical ones. The UK should also develop a pro-competitive regulatory promulgation mechanism, which helps avoid new regulations damaging ordinary market processes along OECD-recommended lines.⁷⁸

Building a more competitive market in the UK

We will discuss the need for a competition chapter in a UK-EU FTA below; the UK must have flexibility in these areas because this is crucial to ensuring a competitive and thriving economy. The recommendations demonstrate the need for divergence from the EU regulatory system: some, indeed, go beyond what the EU has required in the *acquis*. There are anti-competitive distortions in key UK markets in a number of sectors, especially questions of the lifeblood of the UK economy, such as inputs into major manufacturing, services and agricultural industries (examples would include energy, retail banking, transport (including rail) and property). The Government, as part of its Brexit strategy, should be considering how to make improvements in all these sectors. The following represent examples of priorities.

UK Agricultural Policy

- The EU's Common Agricultural Policy (CAP) is a system of tariff protection, subsidy, and regulatory control that unfairly restricts imports from the developing world, raises prices for the British consumer, and has led to the state of European agriculture being described as a "museum of world farming".⁷⁹
- The Government's White Paper would keep the United Kingdom locked into EU agri-food regulation, without a say on how it is made.

As a member of the EU, the UK's agricultural production and trade have been regulated by the CAP and CET. Domestic agriculture gives Britain around 60% of its food, with 1.6% of its labour force, constituting 0.6% of its GDP. In 2015, gross agricultural output was £23.9 billion, and total

78 OECD (2018), OECD Regulatory Enforcement and Inspections Toolkit, OECD Publishing, Paris, <https://doi.org/10.1787/9789264303959-en>.

79 Owen Paterson MP quoted in "Once wedded to the EU, some British farmers think it's time to quit", Euractiv with Reuters, 2016.

Available at: <https://www.euractiv.com/section/agriculture-food/news/once-wedded-to-the-eu-some-british-farmers-think-it-s-time-to-quit/>

income from farming in the UK was £3.8 billion.^{80 81} But subsidy payments from the CAP make up 50-60% of UK farming income.

The United Kingdom now has the opportunity for a new approach to farming and agricultural trade. Without control over agricultural policy, the promised benefits of leaving the EU would be nullified, just as if the UK merely replicated the tariff, quota and sanitary and phytosanitary (SPS) and technical barriers to trade (TBT) measures currently in place. Instead, we should bring down tariffs, expand trade abroad, and make our food cheaper.

The Common Agricultural Policy

Subsidies are used to incentivise (and occasionally disincentivise) agricultural production across the EU: these are most often tied to land, but also production (e.g. head of cattle). The CAP also mandates a regime of tariffs and quotas which control the flow of agri-food products in and out of the EU.

Exiting the CAP presents significant dividends of the Brexit process, providing British policymakers with their first opportunity in over forty years to decide an economically and ecologically sensible set of policies for consumers and farmers. It will also open free trade negotiations with third countries, growing not only the agricultural sector but the whole of the British economy. Agriculture represents a 'threshold issue' in negotiations with most countries, especially the ones which the UK is most likely to strike initial deals with: these domestic reforms should be addressed early. The UK has relatively few defensive interests in agriculture, making potential trade partners more likely to agree to liberalisation in difficult areas which are more important to the British economy, like services. **The EU's refusal to seriously negotiate on agriculture has made negotiation with third countries on services, investment and behind the border barriers such as anti-competitive market distortions more difficult.**

An Open Agricultural Policy that works for the UK's Farmers

The new agricultural regime that we propose is based on openness. The goal is to gradually liberalise tariffs in agriculture so that over time. However, tariffs are only one side of agricultural trade barriers. Most

80 see page 12, DEFRA Agriculture in the UK 2015 : https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/535996/AUK-2015-07jul16.pdf

81 DEFRA, Agriculture in the United Kingdom 2015, https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/535996/AUK-2015-07jul16.pdf, page 1. (accessed 27 September 2016).

of the UK's trading partners are just as concerned with SPS and TBT barriers. Here the White Paper would prevent the UK from ensuring that these barriers are WTO compliant and **based on sound science (not the EU's interpretation of the precautionary principle which is bringing it into conflict with other WTO members)**, and a countervailing duty and **mechanism to protect British producers from anti-competitive market distortions** from abroad (including from the EU-27) Once the UK leaves the EU, it will repatriate trade remedy measures, **including traditional anti-dumping and countervailing duties laws.**

Many WTO-compatible mechanisms could be used to provide relief to British farmers who might suffer from highly subsidised or otherwise distorted imports. The UK could also develop a **safeguard mechanism** to increase the tariff to the rate of the CET if the applied rate is lower (e.g. as a result of the application of lower tariffs in certain areas as a result of a policy of gradual liberalisation).

These measures will satisfy those farmers who are legitimately concerned with import competition from products benefiting from distortions, and satisfy those countries who want broader access to the UK market. We set out below areas and programmes which would be affected by an exit from the CAP regime, to demonstrate how British farming can not only survive, but be much better off, post-Brexit.

Tariffs and Quotas

- Eliminate quotas and tariffs on all products that the UK does not produce, such as bananas, rice, and oranges.
- After binding at the CET rate through technical rectification or modification of our WTO schedules, gradually convert quotas and tariff-rate quotas (TRQs) to tariffs for all products that the UK does produce, recognising that the country is not self-sufficient in most agricultural products.
- Create a tariffication mechanism to rebalance prices of products whose costs are reduced by distortions in their own markets, or use the difference between the CET and the applied rate to re-apply the CET in the event of proof of an illegal subsidy or anti-competitive market distortion as a countervailing measure.

Subsidies and Supports

- Phase out production- or land-based subsidies, moving towards direct transfer payments by 2021.
- Redirect funding to support individual, active farmers via direct transfer payments to prevent a shock to the United Kingdom's farming families and communities, and increase transparency.
- Re-engineer greening payments towards environmental remediation schemes on an as-needed basis, funded by an insurance scheme covering events out of the ordinary and out of farmers' control (e.g. flooding).
- Maintain animal disease compensation funds.
- Maintain R&D funding for farming techniques and equipment.
- Allow bridging funds to flow to farmers who diversify holdings with other services (e.g. tourism).

Regulation

- Regulate on the basis of sound science, and in compliance with the letter and the spirit of WTO SPS and TBT Agreements, not the EU's anti-innovation application of the precautionary principle.

UK Fisheries Policy

The EU's Common Fisheries Policy (CFP) has denied the UK control of its own waters, depleted its fish stocks and caused severe ecological degradation. CFP rules have also disproportionately subsidised non-UK EU fishermen, helping cause chronic unemployment among our fishing communities. The White Paper, however, promises that we will leave the CFP, but states that we will continue to regulate our waters jointly with the EU.

The UK has the opportunity to develop its own UK Fisheries Policy (UKFP), once it withdraws from the EU and the CFP. As a net fish importer (we

tend to import what we eat, and export what we catch) we have a unique opportunity to support consumer and producer interests simultaneously.

- The primary objective of a UK fisheries policy should be the restoration of sovereignty over UK waters, then balancing the goals of commercial fishing in UK waters, sustainability, and cheaper fish for UK consumers.
- To limit unnecessary costs for producers and consumers, policy should be the least trade-distortive possible, consistent with regulatory goals.
- For cheaper food and more choice, policy should also be the least anti-competitive possible, consistent with regulatory goals.
- It will need to be in the context of the international framework for fisheries, in particular UNCLOS and UNFSA.
- For continuity, some elements of the CFP could be retained for the immediate future, like specific technical measures. Others, like access to waters and SPS/TBT questions, should be altered immediately.
- The UK should also enhance its scientific advisory body, actively engaging in ICES.

Access to waters and management of quotas

- For sustainability internationally, the UK should join the NEAFC, and consider other RFMOs, participating in international negotiations on Total Allowable Catches (TACs) for different fish stocks.
- Negotiating bilateral agreements with the EU, Norway, Iceland, and the Faroe Islands, on access to respective Exclusive Economic Zones (EEZs) and management of fish stocks, should be a priority. Negotiations should be in conjunction with those on process and methodology for determining TACs for shared and straddling fish stocks.

- The UK's relatively limited need for access to others' EEZs strengthens its position in negotiating TACs. This leverage must be put to use.
- The UK should consider which Sustainable Fisheries Partnership Agreements (SFPAs) to replicate, to support developing countries and to allow our fishermen access to more fish stocks.

Fisheries management

- The UKFP should address barriers to entry for new fishermen created by the FQA system, which favours incumbents. Instead, our system should maximise competition, while considering development of a fair and transparent allocation mechanism for fishing rights, e.g. through auctions.
- The UKFP should have mechanisms to avoid discards, such as introduction of risk pools or quota bundles, for quick transfers of quotas as needed.
- Policymakers may trial "days at sea" to prevent overfishing.

Funding and government support

Subsidies to fishermen should be phased out: these may support inefficient production and limit competition and incentives for better productivity. However the Government may need to provide interim support, such as for transitional costs in fitting new monitoring systems.

- A mechanism should enable fishermen to seek remedies against imports that have benefitted from government distortion, to level the playing field and enable effective competition.
- The UK should investigate creating markets for insurance products, to guard against the impact of fluctuating stocks.

Trade in fisheries products

EU tariffs on imports are currently relatively high. Lower tariffs for seafood consumed but not commonly caught in the UK would benefit consumers, with little impact on domestic fishing.

- The UK should set regulatory barriers at the level consistent with the goals of human and animal health, but still the least trade- and market-distortive, based on scientific evidence.
- A UK-EU FTA should include a comprehensive fisheries chapter. This needs to include provisions including on mutual recognition of standards and application of import conditions, with a mechanism to manage divergence in standards after the UK leaves.
- The UK should join the WTO Friends of Fish group and actively advocate in Geneva for a WTO fisheries schedule and the successful conclusion of fisheries subsidies negotiations.

Aquaculture

Aquaculture has the potential to support employment in fisheries, guard against price shocks for UK consumers, and help the UK more responsibly steward its marine resources.

- The Government can support the industry through streamlining planning processes, ensuring efficiency in licence allocation, and incentivising innovation.

Fisheries and devolution

Further distribution of powers to devolved governments should be considered. Areas such as trade and negotiations of TACs, and access to the UK's EEZ, would remain with the UK Government, however.

UK Finance: An Alternative Plan for the City

Protect and enhance the integrity of the UK Financial System

- **Reduce the application of the EU's Capital requirement to only internationally active banks**

The objectives of Basel III were to avoid systemic risk, market fragmentation and regulatory arbitrage for 'internationally active banks', but the EU applies these regulations to all EU banks and investment firms via the Capital Requirement Regulation and Directive (CRR and CRD IV)

regardless of whether they are internationally active or pose a systemic threat to the market. This increases the amount of capital EU financial service companies must hold, reducing the amount they can lend to, underwrite or invest in the wider economy. In January 2019, all UK banks will need to ring-fence their retail banking from their investment banking activities so there will be no reason for the UK to continue to follow the EU's capital requirements for domestic UK banks. Instead after Brexit the UK financial authorities should reduce the application of CRR/CRD IV to cover only globally active financial institutions as originally intended by Basel III. Lowering the capital requirements for domestically focused UK financial services will increase the amount of capital available for domestic consumers and businesses, providing a boost to the economy.

- **Retain London's position as the centre of wholesale finance in Europe by allowing EU-headquartered financial institutions to remain operating in the UK**

The Bank of England will allow any EU financial institution operating in the UK to continue if there is a cooperative agreement with their home state regulator. The Bank will also grant temporary permission if there is no transition period post-Brexit to allow EEA firms using a UK passport to continue to operate and fulfill existing contracts while they seek full UK authorisation. This will allow the UK to retain its position as the world's financial supermarket. Also, EU firms could set up a small UK subsidiary with legal substance to be the recipient of any financial service business. EU-based companies will still be able to raise money in the UK, just as companies from all over the world raise money in London's efficient capital pools and its liquid secondary markets. Clients from the EU27 will still be able to trade with UK banks by using relationship-based, reverse solicitation exclusion, just as non-EU clients do.⁸²

Promote effective Competition for both large and small consumers

- **Improve Large Fund trade facilitation rather than adopting the EU's double volume caps**

After Brexit, the UK financial authorities should abandon the double volume cap or at least increase it to the 11% and 17% recommended by the FCA to ESMA. The present 4% and 8% caps hurt the heavily traded, UK markets, making it more difficult for large investors to trade in large sizes without moving the market price against them. The UK has a comparative advantage in Asset Management and trading, and should not

82 Barnabas Reynolds, Blue Print for Brexit, Politeia. Jul 2016, page 18

risk losing this market due to a trading limit set for smaller and low volume EU markets. According to Efama, UK is the largest asset manager in the EEA with 36% of the market.

- **Review the definition of trade incentives such as unbundled research**

The EU regulations that require company research to be purchased by asset managers should be dropped post-Brexit. Reading research reports is not an inducement to trade; it requires effort and may not convince an investor to follow its recommendation or even to trade at all. The previous system worked, and there was no requirement for the FCA to waste resources monitoring research fees. Purchasing research is reducing the research available on smaller, less traded and new companies, as financial analysts move their coverage to larger companies that offer the greatest return for their reports.

- **Encourage new market entrants with proportional regulations and taxation**

It is important to encourage innovation and new market entrants, however much of the EU's existing regulation favours the large incumbent companies either by explicitly protecting them from competition or by increasing regulation so that compliance costs become crippling for smaller competitors or new market entrants.

- **Regulation**

When we leave the EU, the UK should extend the *de minimis* **exemptions in regulations** and increase the financial threshold so that start-up and disruptor companies can get more than just a foothold in the UK market. Reducing the burdens of MiFID II regulations on small firms, especially excessive data collections, the “suitability and appropriateness” assessments, as well as the “complex” investment determinations for retail clients, would all help to expand private client investments and improve the capital-raising process for new companies, which predominately rely on private client investors.

Expanding the FCA's very successful sandbox for financial innovation to other areas and industries could be a major boost to the economy. Taking part in the sandbox program has enabled new companies to assure investors that their inventions/services will get approval from the regulators

when complete. The program has attracted fintech companies from around the world applying to work alongside the FCA.

London is also leading the world in **Green Finance**, having raised more than \$24bn for green bonds. The Green Finance Taskforce can be expanded by working with industry to accelerate the growth of green finance as well as with the British Standards Institute to develop a set of green standards to provide clarity to financial institutions over the credentials of green financial products. The taskforce will also work with mortgage lenders to develop green mortgage products that reflect the lower financial risks associated with the reduced outgoings for owners of energy efficient properties.

- **Taxation**

HMRC needs to plan for a post-Brexit tax system that encourages investment, promotes start-up and scale-up businesses, and reduces the complexity of the UK tax code. Every new tax makes the UK a harder place to do business and discourages inward investment. Post-Brexit the UK's competition for innovators will especially be economies like Singapore, where new firms are given tax incentives to incorporate there (although Singapore's corporate tax rates are already lower than the UK, at only 17%).

HMRC should remove the 8% bank surcharge which pushes profitable UK banks into a tax rate that is much higher than the US, where federal corporation tax has been cut to 21%. For many UK financial service providers, the US offers a very viable alternative to London: indeed, in the most recent Global Financial Centre Index, New York has overtaken London to top place. Even many EU countries, including Luxembourg, the Netherlands and Ireland have lower corporate taxes for financial services than London.

Secure an appropriate degree of protection for consumers without lowering market liquidity

A large part of any financial regulatory regime is to protect consumers of and investors in financial products. This is important because financial markets rely on consumers and investors who in turn rely on the knowledge that their assets and investments will be safe. Having a liquid secondary market that lets investors cash out or change their investments whenever they wish is also a key element of efficient financial markets. So, any regulation to protect consumers should also be careful not to drive liquidity out of the market.

The UK regulators could improve market liquidity post Brexit by reviewing some of the MiFID II requirements that hinder competition in the market without providing any real consumer protection.

- **Data requirements**

MiFID II now requires 65 data points for every transaction by both buyer and seller, but it is beyond the ability of regulators to monitor this amount of information in any meaningful way. Under the first MiFID directive, implemented in 2007, only 24 data points were required, and even this was considered excessive by most market participants (even major banks with large compliance departments were fined for mistakes in their data). The excessive data requirement disproportionately effects an investment firm with a large number of small clients or clients who trade frequently.

- **Retail investors**

The determination of what is a “suitable” and also “appropriate” investment for a private client greatly increases administration costs, making it too expensive for investment banks to focus their business models on individual wealth management and share ownership.

This regulation is reducing the number of retail investors in the market which is reducing the ability of SMEs to raise funds in the equity markets, as well as reducing the liquidity of the secondary markets. SMEs rely on private client share ownership as they are too small to appeal to large investment firms, who must buy larger tranches of shares to make an effective return for their much larger funds. Ironically, larger financial services firms who can afford the additional regulatory costs of dealing with private clients don’t generally do so, because the potential returns are too small.

- **Short selling**

Similarly post-Brexit, UK regulators should also drop the EU’s preoccupation with short selling. The idea that short selling is riskier than buying is partly a symptom of a 9-year long bull market; in a bear market the reverse will be true. In the futures market, both long and short transactions may be uncovered by the underlying physical commodity and yet the futures market functions well, with margins required from both sides (many market observers believe that the recent sell off in the Crypto Currency bubble was due to the CME introducing a futures contract that enabled investors to short the market).

- **CFDs and fintech trading**

Unacceptable conduct such as insider trading, price manipulation and financial fraud must be prevented and prosecuted after the fact. But introducing more and more hurdles for private client advisors to jump is only lowering the overall market liquidity by driving investors towards unregulated, offshore platforms. It is better for the whole economy if a retail investor trades in shares listed on a regulated market.

Regulators need to spend their time and money keeping the whole system afloat, and ensuring that systemic market risk is minimised or avoided completely. Regulators watching for potential threats to small investors will never be as effective as those investors watching out for themselves.

Sectoral regulatory reform opportunities and regulatory promulgation

Anti-competitive regulations can raise costs for businesses or create actual blockages to trade. The acquis includes numerous anti-competitive and over-prescriptive regulations. The UK should prioritise to determine which to remove to make our overall economy more pro-competitive. The CMA and other government departments should be heavily involved in reviewing the acquis as it is ported over, to remove the anti-competitive regulations that damage consumers, especially the poorest.

The following brief examples illustrate EU-originated anti-competitive regulations in the UK.⁸³ The point is not that 'deregulation' is needed, but regulation that is pro-competitive, increasing consumer welfare.

Digital

The UK has a competitive advantage in the digital economy. Many of its innovative firms rely on data flow, so it is imperative that the regulatory environment accounts for this and allows these companies to flourish.

- **General Data Protection Regulation (GDPR) (Regulation (EU) 2016/679)**

GDPR has extra-territorial reach wherever EU citizens' personal data is processed. It is suspicious of innovation however, and its complex requirements mean small entrants find compliance harder. Fines can go up to €20m, or 4 per cent of worldwide turnover. Smaller firms lack the resources to monitor compliance, and may risk sanction to avoid the

83 Singham, S. A., Tylecote, R. & Hewson, V., 2018. "Freedom to Flourish - UK regulatory autonomy, recognition, and a productive economy", IEA Discussion Paper No.91, Chapter 5. [Online] Available at: https://iea.org.uk/wp-content/uploads/2018/07/DP91_Freedom-to-flourish_web-002.pdf

compliance costs, making GDPR self-defeating; firms exiting the market because of GDPR also means an anti-competitive outcome.

Moving away from the strictures of the GDPR, the UK should work with other like-minded WTO members (such as the US and members of the Plurilateral Working Group on E-Commerce in the WTO). It should ally with these countries in seeking provisions in the UK-EU FTA that allow adequacy in cases where data rules are objectively achieving the same data protection goals, but are not identical. This is one of many examples where the EU is an outlier.

The UK will need to regulate in ways that differ from the EU's approach to data flow in order to promote this sector. At the same time, cross-border flow of data into the EU is important, so a solution must be found where the EU allows data to flow even if technical regulation differs, provided the overall goals of data protection are being met.

Outside of the EU's regulatory structure, the UK would not be bound by some of the aspects of the Digital Single Market initiative which have caused concern. Such as the copyright directive currently making its way through the EU law-making process

Audiovisual

- **Audiovisual Media Services Directive (AVMSD)
(Directive 2010/13/EU)**

AVMSD requires member states comply with content requirements in exchange for being able to distribute their country's content to other EU Member States, which includes a requirement to reserve a certain amount of airtime for 'European works'. The test for where a media business is established under the AVMSD has also been criticised by Member States for being difficult to assess and enforce. Works produced in third countries are subject to the airtime allocation requirements for European works and may find it difficult to access the European market. The imposition of local content requirements is a classic example of an ACMD: these rules hamper content producers' ability to make investment and production decisions.

The UK has a very strong offering in the entertainment sector and should not be hampered by local content rules which it does not need in order to be successful.

Chemicals

This sector is an example of advanced manufacturing where the UK should seek the most pro-competitive regulation possible, for a vibrant, dynamic sector. EU regulation in this area is highly restrictive.

- **Registration, Evaluation, Authorisation & Restriction of Chemicals (2006) (REACH) (Regulation (EC) No 1907/2006 Jun-07)**

REACH is a framework for chemicals manufacture and use in the EU, whose stated aim is to ensure chemicals produced, imported, sold, and used in the EU are safe. It obliges manufacturers to gather information on new and existing chemicals they use, submitting the information to the European Chemicals Agency (ECHA) for review and inclusion in a central database; the UK has the second highest number of registrations.

The regulation reduces third country exports to the EU, however, by increasing cost and, in some cases, barring products from the single market. In the National Trade Estimate Report on Foreign Trade Barriers (2017), the US Trade Representative stated:

“REACH impacts virtually every industrial sector... It imposes extensive registration, testing and data requirements on tens of thousands of chemicals. REACH also subjects certain identified hazardous chemicals to an authorisation process that would prohibit them from being placed on the EU market unless a manufacturer or user has obtained permission from the Commission... REACH appears to impose requirements that are either more onerous on foreign producers than EU producers or simply unnecessary.” Its report added: “WTO Members have emphasised [the] problems producers have in understanding and complying with REACH’s extensive registration and safety data information requirements”.

The Commission itself admits this is: “one of the most difficult pieces of legislation for industry to deal with — in particular SMEs”. Some businesses have moved production overseas to avoid it, or exited the market completely. Testing costs are often high, harming profitability.

Pharmaceutical and Biotech

The biotech and pharmaceutical sector is one where the UK is and should remain a global leader. Global pharmaceutical companies have expressed concern about European approaches to clinical trials including the potential

for confidential test data and confidential commercial information submitted to the EMA to be disclosed. If the sector is subject to EU rules as the White Paper calls for, it is unlikely the UK would be able to properly oppose the direction of travel of EU regulation in this area. Given that approaches to these issues are global and require global solutions, the UK is better off negotiating them in an FTA and working with allies around the world for a less trade restrictive and anti-competitive approach from the EU.

Far from locking into to the EU's regulatory system and intellectual property approach, the UK should agree a set of approaches and disciplines with more like-minded parties, such as the US and to some extent Japan.

B. Bilateral

EU – A Free Trade Plus deal

“Work must be accelerated with a view to preparing a political declaration on the framework for the future relationship...” June 29, 2018, Article 50 Conclusions, European Council.

So far, the UK has spent a lot of time negotiating with itself, not with the EU. For instance, the UK has gone as far as to consult with the EU on how negotiable its proposals might be (see Olly Robbins's testimony at the European Scrutiny Committee on how critical negotiating documents were shared with the EU to assess negotiability, even before releasing to the members of the Cabinet).⁸⁴

But negotiability in trade is only really tested in the heat of actual negotiation. Negotiability is also a dynamic concept. UK proposals will receive better treatment from the EU if the latter is under greater pressure, from without and within, to accept them (we discuss the strategy for this below). **A paradigm shift is therefore required.**

The EU meanwhile has taken the White Paper as the UK's opening bid, with respect to the crucial trade aspects of an agreement, meaning it will likely seek further concessions. This could include the UK being a member of the European Economic Area (EEA).⁸⁵ However, **EEA members who are not EU members do not sit on the essential rule-making and comitology committees, and have no say in EU rule-making.**

“In particular, like the EFTA Convention, the EEA Agreement incorporates

⁸⁴ Oliver Robbins witnessing before the Exiting the European Union Committee, 24th July 2018. (remarks at around 15:15) Video: <https://www.parliamentlive.tv/Event/Index/5342afbc-c9d3-4a2c-8bb4-c0ab9214db68#player-tabs>

⁸⁵ Whose precise rules were discussed in Singh, S. A., Tylecote, R., and Hewson V., “*Brexit Inflection Point*”, Legatum, London, 2017.

all EU measures on technical barriers to trade, but goes further than EFTA, also incorporating SPS measures. Given that the EEA Agreement applies to all EU and EFTA states except Switzerland, and any others which in theory could join the Agreement, as the EFTA secretariat describes, this means:

“The EEA Agreement extends the Union’s internal market rules to the three EEA EFTA States. This comprises the entire body of technical regulations determining the requirements products need to fulfil concerning safety, consumer protection, health and the environment, as well as the procedures for testing conformity with such requirements. The Convention incorporates the rules established under the bilateral agreement between Switzerland and the EU in this area, as well as the corresponding provisions of the EEA Agreement.”⁸⁶

The EFTA states are not part of the customs union or subject to the common commercial policy and enter into FTAs with other countries either in their own right or as a bloc. However, once again, the FTAs are very limited in scope and focus mainly on goods and tariffs. With respect to non-tariff barriers and services, they generally do not go beyond affirming the parties’ existing WTO commitments and some hortatory language on co-operation.

Compare, for example, EFTA’s agreement with Canada and the EU’s comprehensive FTA with Canada (the Comprehensive Economic and Trade Agreement “CETA”⁸⁷). CETA covers services, investment and goods, and includes provisions on technical barriers to trade and SPS measures, which EFTA states would not be able to agree to as they are not in control of their regulations in these areas, which are passed to them from the EU. The four freedoms are indivisible and regulations that implement them must be complied with. The history of the EEA Agreement has shown that the EFTA states that are parties to the agreement are rule-takers, and must take on the single market acquis, but have no vote on legislation and only consultative input on its formulation. The potential for EFTA countries to use the EEA Agreement’s provisions to block regulation has never been carried out, for good reason: the EFTA parties to the EEA Agreement have

86 Short Overview of the EFTA Convention www.efta.int/legal-texts/eftaconvention/detailed-overview-of-the-efta-convention#tbt 25 Free Trade Agreement Between Canada and the States of the European Free Trade Association (Iceland, Liechtenstein, Norway And Switzerland), signed January 2008 available at www.efta.int/free-trade/free-trade-agreements/canada

87 Available at ec.europa.eu/trade/policy/in-focus/ceta/index_en.htm 27 See for example the testimony of Dr Johanna Jonsdottir, Policy Officer in the EFTA Secretariat, on 25th April, 2012 the House of Commons Foreign Affairs Committee, available at www.publications.parliament.uk/pa/cm201314/cmselect/cmfa/87/87we02.htm

no formal access to the Council or Commission, and only limited access to the Commission's relevant groups.

Many have claimed that Section 102 of the EEA Agreement allows EFTA members to avoid taking on EEA rules they do not like. However, since the EEA Agreement is the agreement providing preferential access to the single market, and since market access issues are linked, triggering Article 102 gives the EU the right to take retaliatory measures to reflect the non-compliance of an EFTA member who declines a measure. This is why the EFTA countries have never used this power.

For the UK, this would mean whenever it wanted to change its baseline legislation (as it stood at Brexit), the consent of the EEA Joint Committee would be needed. If it did not agree (which, when diverging from the *acquis*, is inevitable) the EU could trigger retaliation against UK trade.

The EEA Agreement also established the EFTA Surveillance Authority, of which the EFTA Secretariat itself states: "the EFTA Surveillance Authority and the EFTA Court [respectively] mirror the surveillance functions of the European Commission and the Competences of the Court of Justice of the European Union". (The Commission has also recommended strengthening the EFTA Surveillance Authority and Court, to function as a mirror to EU authorities.) This is harmonisation of regulation, not divergence, and demonstrates that the EU would be able to enact a swathe of regulations which the UK has blocked before, and would effectively lock the UK out of trade negotiations with other countries.

Instead of continuing with the White Paper proposals, or pursuing the EEA option, we advise that the UK now make a different bid (with relevant text), **a UK Offer based on the following concepts**, which are broadly similar to Council President Donald Tusk's offer of an advanced Free Trade Agreement (made on March 7th, 2018.⁸⁸

- (i) Market Access and National Treatment for Goods. All tariff lines to be zero. These are currently zero tariffs in goods, and this should be replicated.

⁸⁸ "Statement by President Donald Tusk on the draft guidelines on the framework for the future relationship with the UK", European Council, March 7th 2018.

Available at: <http://www.consilium.europa.eu/en/press/press-releases/2018/03/07/statement-by-president-donald-tusk-on-the-draft-guidelines-on-the-framework-for-the-future-relationship-with-the-uk/>

- (ii) Draft, and agree, chapters that are relatively uncontroversial, such as baseline intellectual property protection,⁸⁹ government procurement, and investment rules.
- (iii) Start negotiating other chapters which will require more time.⁹⁰
- (iv) A competition policy chapter would deal not only with cooperation between competition agencies but also with ACMDs, i.e. typically state-created distortions that damage competition in the market, unfairly increasing the costs of some (especially smaller firms) and relatively lowering the costs of others (especially large incumbents). Here, as elsewhere, putting sample text on the table assuages concerns about what our future policy choices might be: where we can, we should give that comfort. As the UK can point out to the EU, it is not the intention to erode normative competition principles, such as to allow cartels or abuses of monopoly power. (We suggest a sample competition policy and state aids chapter which we do not include in this paper, but which we will submit shortly.)
- (v) Maximum regulatory recognition for both goods and services and a mechanism to manage differences that arise because the UK or EU diverge.
- (vi) The regulatory coherence chapter included in the Annex to this alternative approach starts from an assumption that the Parties will agree maximal mutual regulatory recognition on day one. The chapter will include a section on GRP, setting out the obligations of both parties to commit to the core principles, such as promulgating laws and regulations that are the least trade restrictive and least anti-competitive possible, consistent with a clearly stated and legitimate regulatory goal.

89 Substantively, the UK and EU will have similar though not identical approaches to IP (for example the UK may seek fewer geographical Indications (GIs) than the EU) in the areas of patent, copyright, trademark and trade dress, and industrial design. However, procedurally, there may be great differences (UK courts should determine the scope of IP rights). The UK therefore cannot be within the jurisdiction of the United Patent Court, which the White Paper proposes; this body would interpret law in accordance with the CJEU. It would also inevitably become more anti-competitive over time.

90 The chapters of a UK-EU agreements beyond those listed here include: 1) Market Access for Goods and related schedules; 2) Rules of Origin and Origin Procedures; 3) Customs and Trade Facilitation; 4) Trade Remedies; 5) Sanitary and Phytosanitary measures; 6) Technical Barriers to Trade; 7) Investment; 8) Government Procurement; 9) Competition Policy; 10) Regulatory Coherence; 11) Intellectual Property; 12) Cross Border Trade in Services; 13) Sectoral Annexes in services including financial services, telecoms, e-commerce and others; 14) Labour; 15) Environment; 16) Dispute Settlement.

Given the starting point of regulatory recognition (see below), a management of differences mechanism will be needed to broadly ensure recognition will not be unreasonably withheld. The starting point is that as long as the parties are implementing GRP, consistent with the overall WTO framework and its spirit, the regulatory goals are objectively achieved even by different regulation, recognition should not be unreasonably withheld. This means that while it remains open to either party to exercise its legal sovereignty and withhold or withdraw recognition, if doing so contravenes the commitment to recognition in the FTA, this would be subject to trade consequences, within the dispute settlement system of the UK-EU agreement. As we note in Chapter 5, the UK's bid may be rejected here, but negotiating this is still crucial to the UK's interests. Other WTO Members can also be marshalled in support for this best in class agreement, which is in their interests to emulate.

If these terms are not met, recognition may be withdrawn with trade consequences within the dispute settlement system of the UK-EU agreement. As we note in Chapter 5, the UK's bid may be rejected here, but negotiating this is still crucial to the UK's interests. Other WTO Members can also be marshalled in support for this best in class agreement, which is in their interests to emulate.

We include text in the Annex of this document for regulatory coherence, where the drafting of negotiating text should begin immediately. Drafts of financial services and other chapters should be tabled. One key area will be customs and trade facilitation with an Irish border protocol. These should also be tabled in the negotiation towards agreeing a framework for the future relationship, based on these concepts:

Customs

Ordinarily, customs chapters in trade agreements are quite simple and not a source of contention between the parties. **What makes the UK-EU arrangements different is that the starting point is the low friction and absence of customs clearance costs**, as the UK is within the EU customs union and single market. **The opportunity therefore exists to craft more ambitious customs arrangements between the two, and better develop customs systems** for a new era of trade. UK customs clearance processes must accommodate a potentially five-fold increase in customs documentation between the UK and EU on the day of Brexit.⁹¹ The key element of the arrangements will be to separate movement of goods from processing of forms (electronically or otherwise) for as many traders as possible.

The agreement will provide for many of the things that already appear in advanced trade agreements but a best in class customs and trade facilitation agreement by itself will not solve all the disruptions caused by leaving the customs union and single market. The UK and EU will need other solutions. In particular the UK will need to use technology and process improvements to upgrade its own customs systems. Some solutions have been described by Hewson.⁹² Others include using newer technology such as smart ledgers, which, it has been estimated⁹³ could add at least \$35bn and as much as \$140bn to global trade in goods each year. Former Director of Swedish Customs Lars Karlsson has also described some of these technologies and processes.⁹⁴ Hans Maessen former chairman of the customs brokers association in the Netherlands has noted that:

“This situation provides a unique starting point to formulate new and efficient customs procedures. [The transaction based approach] can be taken over by a system-based approach, based on trusted traders and repetitive transactions.”⁹⁵

A customs chapter in an FTA between the UK and the EU should comprise the following commitments, to reduce the burden of formalities on traders, and avoid pressure and congestion at ports and airports:

- General inter-agency and authority cooperation and information sharing
- Use of simplified procedures and data processing at points of departure and destination, to cover the import, export and transit of goods.
- Maintenance of procedures for the prompt release of goods, and for release prior to final determination and payment of duties, taxes and fees, supported by procedures for post-release audit, to be conducted in a risk-based manner. Expedited procedures to be made available to qualifying operators and mutual recognition of AEO programmes.
- Operation of self- assessment for importers to declare imports periodically and account for any duties payable, and support to encourage its uptake by traders.
- Agreement that physical inspection of goods is to be carried by means of random checks, except in duly justified circumstances.

95 Maessen, H., “Drive Through Borders”, SGS, 2018, pp. 1.

- Ensuring that any necessary formalities and inspections are carried out with the minimum of delay and, to the maximum extent possible, away from the border.
- Commitment to apply agreed security measures with respect to third country trade, recognition of equivalence of security-related risk management systems and cooperation information exchange and risk management.
- Recognition of inspections and documents of the other party for certification of conformity with country or import or export, as applicable,
- Where a party requires veterinary inspections of meat or animal products, and such requirements are not waived for the other party, commitment to maintain veterinary inspection facilities at all border crossings where meat and animals may be imported
- Adherence to international standards of the WTO, WCO and other appropriate bodies.
- Operation of juxtaposed inspection offices where possible.
- Operation of suitable de minimis exemptions from submitting formal entry documents for low value consignments.
- Efficient and effective management of transshipment operations.
- Special rules and facilitations for specific sectors such as automotive, agriculture, pharmaceuticals.

At functional and operational levels, HMRC, DEFRA and other relevant authorities will need to continue cooperating with the counterparts in bordering member states. HMRC and HM Treasury will also need to invest in improvements to systems and resources, and legislative reforms to reduce the burdens on businesses and reduce the distortions that currently operate against rest of world trade.⁹⁶ This should include improving trusted trader schemes like AEO and CFSP, and making them available to the most traders possible, an ensuring that intermediaries like customs brokers and freight forwarders have a clear legal framework that will enable them to provide competitive, scalable solutions.

⁹⁶ See Under Control - What HMRC can do to prepare and optimise customs processes for all outcomes IEA and ACITA, April 2018

Much has been made of the need for free circulation to preserve just in time supply chains. The mitigants suggested in this customs section will ensure that there is minimal friction for supply chain managers; indeed, these suggestions make it clear that there is also no logistical justification for the White Paper model. In addition, the customs and trade facilitation chapter could include an auto pact to include further mitigants. This could also apply for other sectors if it can be genuinely shown that the mitigants in this section do not sufficiently mitigate frictions. It is important however to note that it would make little sense to take the UK's independent trade and regulatory policy off the table for maintaining the position in an area where the costs are going down over time anyway due to technological advances.

Additional measures for the border between Ireland and Northern Ireland are set out, however in due course they could be extended to all of the UK's trade with EU member states.

Key elements on the Irish border issue.

One of the most pivotal issues with respect to progress is negotiating even the outline of the future UK-EU relationship is the Irish border. The way forward considers the existing trade patterns between Northern Ireland, Ireland and Great Britain and the systems and operations in place at present to operate current border operations in respect of VAT, excise duties and regulatory differences.⁹⁷ We, therefore make the following proposals.

In order to progress matters in the negotiation of the Withdrawal Agreement from the current position, it will be necessary to agree binding commitments as to what measures will pertain in respect of the Irish border if no full free trade agreement is agreed at the end of the transitional period. It will be necessary to achieve a border with no physical infrastructure, respecting the position of the parties in the Joint Report in December 2017.

The solution must respect the sovereignty of Ireland and the EU's control of its borders and the consequences of the UK being a third country. It must recognise that for some goods, border controls on imports from third countries are more sensitive than others in particular agriculture and animals. The UK should therefore commit to aligning trade relevant aspects of SPS regime in Northern Ireland with that of the EU, with suitable powers devolved to the government of Northern Ireland to enable them to fully cooperate and coordinate with the Irish authorities, in accordance with the Belfast Agreement. It is recognised that this may entail border inspections

⁹⁷ For a full examination See Singham, Morgan, Hewson And Brooks, Legatum Institute Technical Note *Mutual Interest - How The UK And EU Can Resolve The Irish Border For Brexit* and Morgan and Hewson *A Hard Question – managing the Irish border through Brexit*, Irish Journal of European Law 2017

at designated posts at ports for imports of meat and animal products to Northern Ireland from mainland Great Britain, but also that this is already the case under existing arrangements as there is an all-island regime in operation at present, and that veterinary inspections are a key component of the EU's protection of its internal market. Other regulatory matters can be enforced away from the border and in the market, as they are at present in respect of goods which are regulated differently in member states (of which there are many, including for example medicines). Such oversight should also be part of the close coordination between authorities north and south of the border, and underpinned by arrangements both in the back-stop and in an Ireland/Northern Ireland specific chapter of the final free trade agreement.

In respect of movement of people, both the UK and Ireland wish to retain the Common Travel Area, the well-established arrangement that allows British and Irish people to travel to, live in and work in each other's territories.

This will facilitate not just travel across the border with only the current levels of checks to control movement of people who do not have the right to be in either country, but also the continued provision of healthcare and education services and ability for Irish and Northern Irish people to work on either side of the border (third country immigration is a national competence so it will remain the right of Ireland to accord this preference to the UK, as are matters such as access to welfare, healthcare and education).

By using best practice and existing technologies, the customs and regulatory border can be managed without infrastructure or routine interventions at the land border. In general the solutions are measures that would be equally applicable for other UK/EU borders, with the exception of the establishment of a single zone for SP and animal health matters:

- Inland clearance should be made available to all traders. This would mean electronic export and import declarations being made and, if required, inspections by HMRC or the Irish Revenue Commissioners (as applicable) being made at the importer's premises.
- Exports of goods between Northern Ireland and Ireland must already be shown in VAT returns, in order to qualify for the VAT exemption for exports. If a trader is not duly submitting an export declaration, matched on the other side of the border by an import declaration, they will not be able to support their VAT accounting. This means there is a strong incentive to compliance on the traders themselves.

- Smugglers would be breaking the law not just in respect of customs duties but also VAT. As duties are generally low, and items where higher duties apply (such as cars, and agriculture) are difficult to smuggle at any scale (and easily monitored in the market and in the supply chains, which are highly regulated), the incentive to evade duties and mis-declare or fail to declare trade will be very low.
- Intermediaries will play a key role in facilitating this trade and taking the burden of compliance away from the traders. The sector needs clarity on the legal framework that will operate, to be able to design competitive, scalable solutions for small and medium sized businesses.
- Certification of origin is being simplified globally and by the EU with the introduction of self-certification by the exporter through the REX (registered exporter) system. It will not be necessary for traders to incur cost or inconvenience in having goods independently certified.
- The UK and Irish governments should both make self-assessment and periodic declarations available as widely as possible.
- All deliverable under UCC and UK's mirroring version of UCC brought into domestic law through European Union (Withdrawal) Act if the UK had to manage with no other negotiated solutions. These elements are summarised in the table below.

On a negotiated basis, it would be possible to permit waivers from import and export declarations for originating goods where only VAT will need to be accounted for (as no import duties will be due – it can be reasonably expected, given trade patterns in Ireland and Northern Ireland, that this will be the great majority of transactions as few third country goods are traded across the Irish border). Free zones or free ports could also be established, both for cross-border island trade and for global trade, to benefit Irish and Northern Irish businesses.

| | Fiscal | Regulatory |
|------------------------|--|--|
| Backstop | <p>Zero tariffs – whole UK/EU; limited FTA to include standard provisions on state aid and competition</p> <p>UK to maintain same external tariff as EU for time limited period</p> <p>Intensive supervision of imports into UK of goods where EU quotas and trade remedies are in operation</p> <p>Maximum deployment of all facilitations under UCC to enable 100% inland clearance.</p> <p>Investment in systems, and resources for mobile inspections and audits, training for businesses and expansion of intermediary sectors (customs brokers, fiscal representatives).</p> <p>Continuation of VIES</p> | <p>UK to pass law against knowingly exporting or carrying non-compliant goods into Irish market.</p> <p>SPS and animal health</p> <p>Northern Ireland to retain all existing SPS regulations and UK to commit to updating them, for Northern Ireland only in accordance with EU law.</p> <p>Checks on consignments of meat and animal products from GB or rest of world (ex EU) to take place at Northern Irish ports, in accordance with current processes in line with all-island animal health regime.</p> <p>Other goods</p> <p>Dispersed checks – ad hoc in border vicinity and in market, by Irish authorities/their agents in farms/processing facilities in NI</p> |
| Negotiating objectives | <p>Zero tariffs – whole UK; full FTA including regulatory coherence, services and investment.</p> <p>Move from transaction- to system-based approach to formalities Integrate information systems and waivers for originating goods where only VAT payable</p> <p>Special Economic Zones/Free Zones</p> | <p>SPS and animal health</p> <p>Northern Ireland to assume autonomy over SPS and animal health and determine whether the remain harmonised to EU requirements or diverge if and when UK government changes regulations applicable in mainland GB.</p> <p>Agreements on equivalence and formalised certification/inspection regimes.</p> <p>Other goods</p> <p>Dispersed checks – ad hoc in border vicinity and in market, by Irish authorities/their agents in farms/processing facilities in NI</p> |

Regulatory Autonomy and Mutual Recognition

Industrial Goods

In her speech at the Mansion House in March 2018, the Prime Minister was right to state that UK regulations would ‘achieve the same outcomes’ as EU law, but need not be identical.⁹⁸ **For pro-competitive regulation, ‘regulatory autonomy’, the capacity to diverge in regulation, is vital.**

The regulatory system the UK needs involves three components: **regulations** (rules made by an authority, in particular for products and services); **standards** (which show a product or service has met regulations, or are marks of quality) and **conformity assessment** (the system of bodies such as laboratories and professional bodies that assess conformity to standards, providing certification).

Domestic regulatory autonomy does not mean divergence in all areas, immediately, because capacity to diverge does not mean either side will; however, the mandatory harmonisation of regulation via alignment of regulations themselves (as opposed to alignment of their goals) would fail to deliver the benefits of leaving. **The UK may choose to retain EU regulations at times in some sectors, but must be able to choose not to.**

The UK should put forward an open and constructive offer of mutual recognition with the EU. **Autonomy would be followed by recognition by the UK of EU regulation, standards, and conformity assessment, meaning institutional competition for the UK, commercial competition from EU imports, and avoidance of unnecessary trade barriers on imports.** It is then to be expected that recognition by the EU will vary by sector, but for the EU not to grant recognition would constitute creating new trade barriers, because on Brexit day the EU and UK have full harmonisation or mutual recognition. This creates a unique opportunity to achieve maximal recognition.

Withdrawal must therefore deliver the following five points:

- 1) **Autonomy for the UK to make its own regulation** (for both goods and services)
- 2) **Autonomy for the UK to set its own standards** (for both goods and services), which can include using global standards

⁹⁸ May, T., 2018. PM speech on our future economic partnership with the European Union [Speech] (2 March 2018). Available at: <https://www.gov.uk/government/speeches/pm-speech-on-our-future-economic-partnership-with-the-european-union>

3) **Autonomy for a UK system of conformity assessment**
(able to assess conformity to UK and EU standards and regulations)

4) **Unilateral recognition by the UK of EU regulations, standards, and its conformity assessment system**
(able to assess conformity to EU and UK standards and regulations)

5) **Seek recognition by the EU of the UK's regulations, standards, and its conformity assessment system.**

EU regulation is growing more damaging to growth, and the concept that the government would decide, in advance, to tie the UK to future EU regulations, without representation, would both be very unusual, and threaten our democracy and competitiveness. On Brexit day, UK and EU regulations will be harmonised and recognised. Subsequently, **in the absence of a bilateral trade deal, the UK can also unilaterally recognise the EU's framework**, for which procedures must be put in place now. New Zealand former trade minister Sir Lockwood Smith has noted that **this starting point is precisely why the EU and UK should agree the most advanced trade agreement** in history.⁹⁹ To achieve this, the UK should agree with the EU a **regulatory coherence chapter** in which both sides are committed to more pro-competitive regulation. This is, again, **best practice** in all recently negotiated trade agreements, as well as the clear approach of all OECD countries¹⁰⁰ and we would expect the UK and EU to be no different.

The **Regulatory Coherence chapter** (see Annex) is drawn from the regulatory coherence chapters of the CPTPP, the EU and US offers in the TTIP negotiations, and relevant WTO provisions in these areas. The sample chapter represents the type of arrangement the EU and UK could agree. The key elements are:

(i) **Strong commitment by both sides to GRP**, including transparency in how regulations are promulgated, effective cost-benefit analysis including taking into account both

99 Sir Lockwood Smith, (2018), "*Britain has a golden chance to join the biggest free trade agreement in history.*" Conservative Home.

Available at: <https://www.conservativehome.com/platform/2018/08/lockwood-smith-britain-has-a-golden-chance-to-join-the-biggest-free-trade-agreement-in-history-but-chequers-is-likely-to-wreck-it.html>

100 OECD (2018), OECD Regulatory Enforcement and Inspections Toolkit, OECD Publishing, Paris, <https://doi.org/10.1787/9789264303959-en>

the trade effects and competition effects of regulation, and enshrining into the agreement the best aspects of regulatory promulgation, as found in the OECD's Regulatory Toolkit¹⁰¹ and Competition Assessment,¹⁰² and WTO principles and the work of the Competition Advocacy Group of the International Competition Network (ICN).¹⁰³

(ii) **Commitment by both sides to the idea of promulgating regulation which is the least trade restrictive** and least market restrictive from a competition perspective consistent with a clearly stated, legitimate regulatory goal.

The parties would negotiate the precise mechanics of these in different sectors, but as the draft regulatory coherence chapter notes, **these provisions are likely to involve a Joint Committee and a Conciliation Process prior to full dispute settlement.**

Services liberalisation and regulatory issues

The UK-EU agreement would be based on a negative list covering all services unless specifically exempted.

The opening bid would be maximal openness across all four modes of supply, plus strong disciplines in a horizontal regulatory coherence chapter, and vertical subject matter annexes.

- **Key elements on regulatory issues in services**

As with manufactured goods, the UK needs to **ensure disciplines that make it more likely that both parties move in pro-competitive ways**, both by agreeing GRP, and by pushing for pro-competitive regulation. Every country that negotiates with the EU, for example the US in the TTIP, seeks this kind of discipline. **The second objective is to ensure that there is the maximum regulatory recognition for services sectors.** We have given an example in the case of financial services.

- **The key elements of GRP** for services are broadly as noted for industrial goods: commitment by both sides to GRP, including transparency, taking into account the right inputs when deciding to regulate, such as impact on trade and impact on the market, and broadly speaking,

101 OECD, *Regulatory Toolkit*, accessed 09/2018.

Available at: <https://www.oecd.org/cleangovbiz/toolkit/regulatorypolicy.htm>

102 OECD, *Competition Assessment Toolkit*, accessed 09/2018.

Available at: <http://www.oecd.org/daf/competition/assessment-toolkit.htm>

103 International Competition Network, 2009. *RECOMMENDED PRACTICE ON COMPETITION ASSESSMENT*. [Online] Available at: <http://www.internationalcompetitionnetwork.org/uploads/library/doc978.pdf>

regulating in ways that are the least trade distortive and the least damaging to market competition consistent with clearly stated and legitimate regulatory goals. Violation of these elements would result in violation of the agreement, leading to dispute resolution.

- **Key elements on financial services**

The UK and EU will **seek maximum trade liberalisation in financial services with deference between home state regulators**. They already have harmonised regulation in many important areas and many key areas of financial regulation are based on international standards set by the Basel Committee of Banking Supervision in order to avoid systemic risk, regulatory arbitrage, market fragmentation and protectionism. Many countries whose regulations have similar principles and outcomes have formed cooperative regulatory alliances that allow cross border financial service transactions.

Principle and outcome based regulatory cooperation allows greater divergence than seeking line-by-line adherence to a prescriptive rulebook and facilitates better customer outcomes.¹⁰⁴

Cooperating countries focused on the same regulatory principles and outcomes should permit deference to the relevant foreign regulator in matters of host state supervision. If international standards are robust and comprehensive the home state regulators should be confident that adherence to them by host state countries would address their supervisory concerns.

The EU and the UK should continue to operate with a consensually established set of regulations based on international standards, mutual transparency and cooperation between home state regulators, provided that such cooperation does not prevent either party from diverging nor allowing such divergence to act as a hair trigger causing loss of recognition. At present both the EU and the UK grant access to third country providers through their system of equivalence which is granted unilaterally. However, the system of equivalence does not cover the full spectrum of financial services and equivalence is not granted on purely economic concerns.¹⁰⁵

When the UK itself becomes a third country to the EU, it will have regulations that the EU already recognises and considers to be adequate, which means both should start by granting each other

¹⁰⁴ This has been dealt with in more detail in the IEA's publication *Improving Global Financial Services Regulation*: Singham and McBride, *Improving Global Financial Service Regulation*, IEA, May 2018

¹⁰⁵ Barnabas Reynolds, *A Template for Enhanced Equivalence*, Politeia, 2017
the process required to enhance the equivalence regime has been covered extensively by Barnabas Reynolds for Politeia

equivalence in all available financial sectors, as well as allowing divergence provided that the regulation is still achieving the same prudential goals. The nations that presently have EU equivalence do not have identical regulations to the EU. The EU and UK agreement must include a mechanism designed for managing divergence anchored by one or more forms of dispute resolution. Such mechanisms may include a specific approach that is unique to financial services as has been included in the EU's CETA with Canada, or they may be more broadly applied across the whole of a mutual access regime.

The agreement should prohibit practices which distort competition and trade such as cartels, abusive behavior by dominant market players or anti-competitive mergers. Adding provisions to ensure they act fairly and transparently when applying their competition laws or investigating transgressions will require continued cooperation between the UK and EU competition authorities.

The agreement should be subject to independent arbitration as in a normal trading arrangement so that neither party is subject to interpretation by the other. Maintaining the UK's overseas persons exclusion and the EU's reverse solicitation exclusion will enable cross-border wholesale financial services between regulated institutions and professional investors in the other jurisdiction without even triggering the equivalence regime.

This should be understood within the context of an advanced FTA being the UK's first offer to the EU, with the EU invited to respond, as the negotiating field is altered by action taken in the other pillars and pressure applied to the EU.

- **Dispute settlement mechanism**

All modern FTAs have dispute settlement mechanisms and the UK-EU FTA will be no different. The UK's offer on the dispute settlement mechanism should be **an arbitration-based mechanism following generally accepted good practice** in this area.

UK-US FTA: the renewal of the Special Relationship

- **A UK-US FTA is one of the great opportunities of Brexit in the immediate future, and a UK Government should greet the prospect of such a bilateral deal with our greatest ally with genuine enthusiasm.**

The UK-US FTA we seek must encourage trade and economic liberalisation, reduce domestic protectionism, and help create a more competitive economy for both parties, to the improvement of consumer welfare.

At the centre of trade agreements, and a US-UK FTA, will be improved market access for goods, services, and investment. This means the **elimination of tariffs to the lowest possible levels on the greatest number of goods, with services markets open to competition from the other party's providers**, while government procurement markets to both goods and services providers from each party should also be open (while preserving our NHS, for example). The FTA will **also cover digital trade, with data flows essential components of goods and services**, albeit with reasonable levels of privacy protection that are not unduly burdensome.

Meanwhile, when businesses are made to meet two sets of regulations to sell in different markets, this hinders efficiency and limits exports. This FTA, again, should **also therefore include a mutual recognition agreement (MRA)**, which would allow companies from each party, in as many sectors as possible, to export according to their own country's regulations and standards, which would then be recognised by the other country. Of course, the FTA's rules will need to be enforceable, with binding, enforceable dispute settlement to ensure the agreement is followed.

The evidence also shows that the British people are increasingly enthusiastic about a UK-US FTA, with over 60% in favour according to recent polling.¹⁰⁶ The UK must therefore now accelerate its negotiations with the US. The US administration has indicated that it wants a free trade agreement with the UK. There is a very high level of support on both sides of the aisle in the US congress also. Recently, Republican Senator Portman has set up the US-UK FTA caucus in the Senate with Democrat Chris Coons;¹⁰⁷ the Trump administration is now frequently on the record as strongly supporting an FTA with the UK.¹⁰⁸ US industry is increasingly vocally supportive, and the Office of the US Trade Representative (USTR) has recently launched a stakeholder engagement process for an FTA with the UK. A key feature of that process is the input of small businesses who face regulatory barriers in the UK.

A coalition of UK and US think tanks have produced a proposed draft of

106 Heffernan, S. "BREXIT: UK wants US Deal", Live Trading News (2018). Available at: https://www.livetradingnews.com/brexit-uk-want-us-deal-98466.html#W6DQ_-hKg2w

107 Senator Portman (2018). "Portman, Coons Launch Senate UK Trade Caucus to Build Support for Bilateral Trade Agreement". Available at <https://www.portman.senate.gov/public/index.cfm/2018/5/portman-coons-launch-senate-uk-trade-caucus-to-build-support-for-bilateral-trade-agreement>

108 US Trade Representative, 2015. *GUIDELINES FOR CONSULTATION AND ENGAGEMENT OFFICE OF THE UNITED STATES TRADE REPRESENTATIVE*. [Online] Available at: <https://ustr.gov/sites/default/files/USTR%20Guidelines%20for%20Consultation%20and%20Engagement.pdf> [Accessed 18 09 2018].

109 Document to be made available at 14:30 BST, on Tuesday September 18th: http://ifreetrade.org/publication/us_uk_shadow_trade_talks_an_ideal_fta

an FTA between the US and UK, published on September 18, 2018.¹⁰⁹ The UK should use the opportunity of the UK-US negotiation to craft its own model FTA.

As the world's number two exporter of services, the UK will need to use access to its own market in goods and agriculture to secure services concessions from the US. The US will be concerned about underlying product regulation that may discriminate against its goods, for instance. It is also a critical part of the UK-US FTA discussion that solutions to the most pressing problems in international trade today are agreed by the UK and US. These two countries could agree a very high standard agreement that delivers both free trade and free markets between them, setting up the conditions in which future agreements with other countries can yield benefits. For instance, even though the US and UK do not have many state-owned enterprises in commercial sectors, the two could agree a free trade agreement with strong provisions to discipline state-owned enterprises, anti-competitive market distortions by the state, and other subsidies (see link to potential UK-US FTA). Since we envisage that this agreement would be an open accession agreement, others could accede, provided they could meet the terms.

Many commentators have rightly noted the impact of the Trump administration trade policy on the global trading system, and argued that therefore no trade deal with the UK will be possible or it will be very much on the US's terms and be detrimental to UK interests. This misunderstands the support for the UK at all levels, and also the fact that the Trump administration would need to do a deal with a country that is a significant economy, where there is no trade deficit, and where there would be no race to the bottom on labour costs. The UK is the ideal candidate for this US agenda, and concluding a comprehensive trade agreement with the UK would enable the US administration to demonstrate to the Congress that it did in fact have a trade agenda that is not solely about renegotiating or pulling out of existing agreements.

The UK-US FTA would therefore need to address the major concerns of the US administration with respect to 21st century trade. The US administration is seeking a solution to the problem of global market distortions and the UK-US FTA could be an important step. Similar rules apply in the CPTPP and so this would also act as a platform to gain further disciplines over those countries that distort their markets.

While there have been concerns about the implications of a US deal for

109 Document to be made available at 14:30 BST, on Tuesday September 18th: http://ifretrade.org/publication/us_uk_shadow_trade_talks_an_ideal_fta

the NHS, the NHS may simply be reserved from the provisions of the agreement. However, the NHS does purchase drugs and other products from global suppliers and it would be in the interests of the NHS (and the British taxpayer) to ensure that procurements are as pro-competitive as possible. US firms have not complained about the NHS, and it has not featured in recent National Trade Estimates (the US' inventory of foreign country trade barriers). It is extremely unlikely that the US would be interested in raising any issue with the UK in a trade negotiation which has not featured in the NTE in some way. In any negotiation with the US, it is open for the UK to rely on high standards of consumer protection which are generally not opposed, except when they are a form of disguised protectionism.

Provided that the UK is able to have control over its own regulatory structure, it will be able to agree terms with the US that the EU would not be able to reach because of the difference in regulatory approaches between the EU and US in many areas. As the UK negotiates with the US, it is critical that we explain why a trade deal with the UK is strongly in the US interest for strategic reasons. The UK has made itself a regulatory battleground in a world that is being rapidly divided into pro-competitive regulatory systems, and prescriptive and anti-competitive ones. The US understands that the value of a UK-US trade agreement is to pull a major G-7, European economy into a pro-competitive regulatory setting.

A UK-India Trade Deal is Feasible

A deal between the UK and India is an example of one which could take longer to negotiate, due in part to the many distortions in the Indian economy. However, this is a deal DIT must begin preparing for, and which represents a great opportunity for the UK.

A trade deal with India stands to be of substantial benefit to the UK. India is one of the fastest-growing big emerging markets in the world. The contours of a deal between the UK and India are visible because of the narrowly-focused offensive interests of the UK, and of India, and because of the UK's limited defensive concerns.

Negotiations will herald opportunities to discuss helping to modernise areas of India's economy and lower the barriers that limit competition for various Indian sectors. Trade barriers apply in legal and financial services, as well as high taxes on Scotch Whiskey, for instance. Similarly, India has significant difficulties with the EU's regulatory bans on its foods.¹¹⁰

The EU has struggled to conclude a deal with India for a number of reasons. Major obstacles have been the EU's regulatory system in agriculture, and its aversion to allowing India Mode 4 services access (ironically led by the UK). Furthermore, the offensive interests of the EU were not equally shared by all the member states. The UK has very particular focused interests, especially in legal and financial services (especially insurance) and, in agri-food, barriers for its Scotch Whiskey exports. In a purely UK-India context, the UK might change its overall approach to Mode 4 precisely if those focused offensive interests look like they may be accommodated. Singham, Rangan, and Bradley analyse the barriers between India and the UK comprehensively in.¹¹⁰ The key elements of a potential deal are as follows:

- India would provide **better legal and financial services** access for the UK, especially allowing UK law firms to establish and practice law in India, and to allow foreign ownership in the insurance sector to increase.
- The UK would provide **Mode 4 services access**¹¹² for India. India's trade negotiating objectives prioritise the access of their citizens to the UK market as part of the delivery of services. Indian high-tech companies in particular need trading conditions such that some personnel can move to the UK; however, the UK's interest will naturally be in selected numbers of highly skilled workers, and the numbers involved would be very small
- The UK will need to provide much **greater market access to India's agricultural produce**. This means reducing tariffs, but critically means reducing the regulatory barriers derived from the SPS and TBT rules in the European acquis. Thus the UK will need regulatory autonomy over these rules in order to do a deal with India. This will benefit Indian producers as well as British consumers through cheaper products.
- The India-UK working groups have concluded that

110 For example, the EU ban on Indian basmati rice: Bodkin, H. "Rice to become more expensive due to 'disastrous' EU import rules". The Telegraph (2017). Available at <https://www.telegraph.co.uk/news/2017/10/14/rice-become-expensive-due-disastrous-eu-import-rules/>

111 Singham, S., Rangan, U., Bradley, R., and Kiniry, M., "Anti-Competitive Market Distortions and Their Impact: A Case Study of India", Legatum 2016.

112 As noted earlier, the WTO provides that services are delivered across four critical modes of supply – cross border supply (mode 1), consumption abroad (mode 2), commercial presence (Mode 3) and movement of natural persons (mode 4). India has always prioritised the ability of its services personnel especially in the IT Sector to be able to move freely from India to other countries where their investments are located.

improvement of the regulatory barriers between them is very significant.¹¹³ In particular, India will want to see a more open UK agricultural sector, both in terms of tariffs and in terms of regulatory barriers such as the EU's environmental and other regulatory barriers in the agricultural sector.

Exploring a UK-China deal

The UK should initiate discussions with China, but be clear that its requirements for a UK-China deal are likely to be difficult for China to meet in the short term. This is a longer-term discussion aimed at moving China towards liberalising aspects of its economic behaviour, with a view to a future trade deal.

A future UK-China deal is important, but cannot be rushed, requiring mature acknowledgement that the UK would need progress in many areas of China's approach to trade. This does not imply protectionism on the UK's part; the approach should be to encourage less distortive and protectionist behaviour by China, for the benefit of the United Kingdom and China, and for global growth. The two countries will naturally maintain friendly relations as we work towards a deal.

China's actions have a huge impact on global trade. Ensuring that its rise does not destroy wealth, or lead to an increase in cronyism, is a critical challenge for the world's major economies, including the UK. It must therefore proceed carefully, bearing in mind the network of China's State-Owned Enterprises ("SOEs") (which often receive free land and water, for example) and other anti-competitive market distortions, which make fair competition for British firms difficult.

Countries that attempt bilateral trade arrangements with China have not generally been successful in concluding deeply liberalising agreements that deal meaningfully with Chinese behind the border barriers (the Switzerland-China FTA and the Iceland-China FTAs are examples of relatively one-sided deals that do not make a meaningful impact on China's behind the border barriers and its regulatory protectionism).

In addition, the UK should approach China's Belt and Road initiative as a way to promote pro-competitive regulation. It is crucial that the Special Economic Zones that may arise as a result of Belt and Road do not become playgrounds for China SOEs to the exclusion of other competitive, private

¹¹³ Business and Enterprise Committee, "*Waking up to India: Developments in UK-India economic relations*", House of Commons, 2008.

Available at: <https://publications.parliament.uk/pa/cm200708/cmselect/cmberr/209/209.pdf>

businesses. What happens will depend on the regulatory framework which underpins these zones, and the UK can play an extensive role. At a time of rising hostilities, a strong but pragmatic UK-China relationship will be very important to ensuring a better climate for the global trading system.

Bilateral deals with countries where an EU FTA should be rolled over

Negotiations should be accelerated with these countries on the basis that the UK will need to roll over existing agreements, and agree a new FTA in the case of EFTA. Here, DIT should be tasked to conclude these negotiations on a provisional basis, in case there is no Withdrawal Agreement and therefore no Transition Period. The UK should negotiate directly with these countries on a bilateral basis (just as in the case of British Tariff Rate Quotas (TRQs (see below))). The problem has been that the UK has been relying on the principle of continuity of third country FTAs in the transition period, without certainty as to whether there would be one. As noted in chapter 5, there are considerable risks to this continuity approach as it requires application of the common commercial policy in the Transition Period, negatively impacting the UK's ability to negotiate properly.

EU cooperation will be required to ensure that both sides have the same rules of origin with respect to the relevant country, so that content in the UK and EU-27 can be cumulated to satisfy that country's rules of origin (rules of origin refer to how customs authorities determine where an export has come from). Without this however, it will still be possible to have market access between both that country and the UK and EU separately (even if the efficiency of pan-European supply chains is partially lost). Of course, it is in both the EU and UK interest to agree rules of origin that allow cumulation with the third country, and this should be possible if the UK and EU retain the same rules of origin.

Typically the EU's rules of origin are relatively liberal. The direction of travel of US rules of origin is towards more restrictions, and thus the UK should seek maximum diagonal cumulation with countries with whom it has trade agreements. This will be challenging with the current US administration, but the UK should seek to negotiate as liberal rules of origin as possible with cumulation with as many countries as possible, and take steps to reinvigorate a crucial discussion in the WTO on the increasingly damaging effect on global trade of diverging and restrictive rules of origin.¹¹⁴

¹¹⁴ As noted in the WTO Section, the UK should reinvigorate the stalled effort begun in the WTO Rules of Origin Committee to ensure harmonisation of rules of origin based as much on substantial transformation as possible (with as little supplemental local content requirements).

An alternative model of bilateral relationships for developing countries and emerging markets

The UK will have to replicate the current EU structure of preference programmes with developing countries and emerging markets. However, in doing this it has an historic opportunity to transform previous EU arrangements into genuine Economic Partnership Agreements that are reciprocal in nature and do not discourage or hinder developing countries growth, unlike current EU development models.

The current model is based around the concept of the Generalised System of Preferences (GSP and the special programme GSP+).¹¹⁵ Many developing countries are unhappy with these, however because the preferences can be lost if a country graduates out of the programme or a particular product exceeds a specified share of trade.¹¹⁶ The EU's Everything But Arms (EBA) initiative was a positive development as it was unconditional, but does give a preference to producers in the poorest countries in the world. Very poor producers in other countries that are not EBA beneficiaries must compete against these preferences, and often lose out.

Problems also occur because of the lack of predictability of how exemptions occur, and the circumstances in which they will be removed; and in which types of products developed countries allow the exemptions to apply to. For example, many cocoa producers have had their tariffs lowered on exports to the EU through the GSP programme. Without GSP benefits, these exports would be subject to tariff escalation, charging a lower tariff on the basic raw material, but a higher tariff on the processed good. This means firms in developed countries are more likely to reap the value-add from processing.

115 The Generalised System of Preferences (and GSP +) and the Everything But Arms initiative are the primary trade development tools that the EU uses in its trade policy. EBA covers only the poorest countries in the world (LDC's as defined by the UN) and is unconditional. All other programmes are conditional. Countries may graduate out of them, or the preference may be lost for other reasons, such as support for terrorism or failing to support Intellectual Property laws.

116 The GSP programme is highly managed trade where a particular product from a particular country can graduate out of the programme if its share of GSP trade exceeds specific percentages which differ from product to product sometimes by quite wide margins. This damages incentives for producers in those product categories to be successful.

117 For example, as from 1 January 2017 certain products no longer benefited from GSP preferences before formal review in January, 2019. The tariff preferences for the products/product groups originating in the countries mentioned below are suspended (see Regulation (EU) 2016/330) because the average value of EU imports of these goods from the GSP beneficiary country over three consecutive years exceeds the thresholds listed in Annex VI of Regulation (EU) 978/2012. Origin and product groups ceasing to benefit from GSP India ĩ S-14: Pearls and precious metals ĩ S-15a: Iron, steel and articles of iron and steel ĩ S-15b: Base metals (excl. iron and steel), articles of base metals (excl. articles of iron and steel).

Furthermore, a developing country currently benefiting from a preferential rate may still graduate out of the GSP programme if their economy grows above a certain level (one example of this is India for many products¹¹⁷). **Perversely, countries therefore lose their preferences if they succeed, discouraging investment**, locking in existing supply chains (as GSP can be lost for a variety of reasons, producers are less willing to go up the value chain and invest in the necessary equipment, because they might lose the preference and be subject to higher tariffs). So developing countries remain stuck in a poverty trap.

Currently, gains are captured by developed country producers who use the raw material inputs at low tariff rates to lower their input costs (although this also distorts developed country economies). In our example, cocoa producers in Ghana might be able to invest in partnering with dairy and sugar producers to produce chocolate on a commercial scale. Under the current arrangements they would not be advised to do so, as if the GSP benefits were withdrawn, the chocolate tariff would significantly increase (crippling potential new business).

The UK can be more open and not penalise developing country exporters for success, and be more open to the products of developing countries without strings and conditionality. **A better development model for poor countries is therefore a true economic partnership: but this requires the UK having tariff and regulatory control.**

If the UK is more open on the products that developing countries produce – and those higher up the value chain, but which they could produce under more favourable trade conditions – their producers will be better able to make the necessary capital investments to upgrade, which they would not be if the preference could easily be withdrawn.

To successfully make this transition, the UK will have to find a solution to the preference erosion problem: this is a dynamic whereby developing country beneficiaries of the preference in fact lobby to keep the developed countries' tariff rate (or Most Favoured Nation rate) high, so that they continue to benefit from the preference. This harms poor consumers in the developed country (meanwhile, countries that are too developed to benefit from GSP but still have large numbers of poor people, like India, see fewer benefits from the system).

The UK could provide, as part of its suite of trade remedies, an option for developing countries which face competition from other countries

whose producers have their costs artificially lowered by ACMDs to complain about the distortion and point out the damage it does to their own exports to the UK. This distortion could be tarifficated for the offending country, to correct the unfair trade that the GSP/GSP+ beneficiary was competing with.

C. Plurilateral

Accession to the CPTPP

The CPTPP (Comprehensive and Progressive Agreement for Trans-Pacific Partnership) replaces the Trans-Pacific Partnership (TPP), following the withdrawal of the US. This plurilateral agreement consists of eleven countries – Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore and Vietnam.

CPTPP is an open agreement and its signatories indicate they would welcome the UK seeking to be a member. Indeed, the Government is to be commended for successfully getting major CPTPP partners to offer CPTPP Membership to the UK.^{118 119} The UK has also officially launched its consultation process for the CPTPP (along with the US, Australia and New Zealand agreements¹²⁰), and should officially apply to join the CPTPP as soon as it can.

CPTPP accession for the UK is also a central geo-strategic move. This is an important platform agreement of some of the fastest growing countries in the world.¹²¹ Not only does the CPTPP consist with the UK of 17% of global GDP (40% if the US re-joins), but the CPTPP is also an open accession agreement which other countries can join; most recently, South Korea indicated that they wish to join the CPTPP.

The e-commerce and SME chapters of CPTPP go further than any other trade agreement (with prohibition on data localisation, non-discrimination, as well as privacy protection. The UK is an e-commerce champion, and

118 Department for International Trade (2018). “Japan will “spare no effort to support the UK” in joining the CPTPP, Available at: <https://www.gov.uk/government/news/japan-will-spare-no-effort-to-support-the-uk-in-joining-the-cptpp>

119 Sydney Morning Herald, “Australia will pursue one-on-one deal even if UK joins revived TPP trade bloc”, January 25th, 2018. Available at: <https://www.smh.com.au/world/australia-will-pursue-oneonone-deal-even-if-uk-joins-revived-tpp-trade-bloc-20180125-h0nxzl.html>

120 Department for International Trade (2018). “Liam Fox launches consultations on UK’s trading future outside of EU”. Available at: <https://www.gov.uk/government/news/liam-fox-launches-consultations-on-uks-trading-future-outside-of-eu>

121 Department for International Trade (2018). “New public consultations announced for future trade agreements”. Available at: <https://www.gov.uk/government/news/new-public-consultations-announced-for-future-trade-agreements>

the CPTPP would only strengthen this position, helping spread digital trade around the world at a time when its liberalisation is badly needed. This is the most liberalising of regional platform agreements (China has its own version of a regional agreement involving the ASEAN countries, the Regional Cooperation and Economic Partnership (“RCEP”), but this is limited to eliminating border measures, and does not deal significantly with behind the border barriers and regulatory issues, partly because China has taken the position that these issues are internal issues for China and not relevant to trade policy. This is becoming a less tenable position).

As noted in Chapter 5, the UK should, as soon as its stakeholder process is complete (even if this is before actual leaving of the EU on March 29, 2019), formally apply to join the CPTPP and go through the relevant CPTPP mandated mechanisms to avail itself of the open accession clause. **The UK cannot join unless we have control over our regulatory system.** This has been made clear by a number of commentators.¹²² Many of the latter do not meet CPTPP standards, such as in agriculture, where they violate the WTO SPS rules on sound science-based animal, human and plant health protections.^{123 124 125 126 127 128}

Tariff and regulatory control, and changes, would be needed for the UK to accede to CPTPP. Accepting the European *acquis* would violate the CPTPP provisions in SPS and TBT measures. If the UK accedes to the European Patents Court, and the enforcement of patents in the UK differed from CPTPP practice and requirements, then it would also be hard for the UK to join.

122 Smith, L. “*Britain has a golden chance to join the biggest free trade agreement in history. But Chequers is likely to wreck it.*”, Conservative Home (2018) Available at: <https://www.conservativehome.com/platform/2018/08/lockwood-smith-britain-has-a-golden-chance-to-join-the-biggest-free-trade-agreement-in-history-but-chequers-is-likely-to-wreck-it.html>

123 DS337: European Communities — Anti-Dumping Measure on Farmed Salmon from Norway https://www.wto.org/english/tratop_e/dispu_e/cases_e/ds337_e.htm

124 DS137: European Communities — Measures Affecting Imports of Wood of Conifers from Canada https://www.wto.org/english/tratop_e/dispu_e/cases_e/ds137_e.htm

125 DS48: European Communities — Measures Concerning Meat and Meat Products (Hormones) https://www.wto.org/english/tratop_e/dispu_e/cases_e/ds48_e.htm

126 DS26: European Communities — Measures Concerning Meat and Meat Products (Hormones) https://www.wto.org/english/tratop_e/dispu_e/cases_e/ds26_e.htm

127 DS293: European Communities — Measures Affecting the Approval and Marketing of Biotech Products https://www.wto.org/english/tratop_e/dispu_e/cases_e/ds293_e.htm

128 DS389: European Communities — Certain Measures Affecting Poultry Meat and Poultry Meat Products from the United States

Evaluating NAFTA accession

Many US members of Congress over the last two decades have called publicly for the UK to accede to NAFTA. The Trump administration has sought to pull the US out of NAFTA,¹²⁹ and renegotiation is ongoing. The US is seeking to do this by two bilateral conversations with Mexico and then Canada. The UK would be in a better position to accede to whatever form of NAFTA prevails (whether or not Canada is ultimately included), because the UK will not have hold-outs regarding the protected dairy sector (as Canada does). There is nothing inconsistent with the UK seeking a trade deal on a bilateral basis with the US and also evaluating NAFTA accession (since NAFTA has an open accession clause).

The UK in the Commonwealth

The Commonwealth is an alignment of nations gathered especially around concepts such as rule of law. It is an unusual network in that it contains some of the most developed countries in the world, as well as the smallest micro-states. Far from being a weakness, as it is often perceived to be, this diversity is the source of its strength. One of the most important things the Commonwealth can bring to the debate is to help facilitate an unblocking of the global economic architecture by enabling its members to discuss issues prior to interacting with their various affinity groups in international organisations.

By surfacing and discussing international issues, Commonwealth countries, while not necessarily agreeing as a bloc to a particular approach, may nevertheless subscribe to similar philosophies and broad positions. Ministers from these countries, if they meet in advance of global meetings, will, in effect get two bites at the apple when it comes to forging coalitions in support of a more liberalising approach. In the case of trade, many Commonwealth countries belong to affinity groups with others who have historically been opposed to efforts to liberalise trade. A Commonwealth trade pre-meeting could be used to broker solutions in the WTO ministerial meeting which follows it. It could also be used to discuss how non-Commonwealth members might react to proposals that members might be making. In the trade context we have seen countries emerge to salvage aspects of trade ministerials, such as when Australia's trade minister Steven Ciobo led an effort to develop a plurilateral agreement on e-commerce, when the multilateral work appeared to be foundering.

129 United States Trade Representative, "USTR Releases Updated NAFTA Negotiating Objectives", November 2017.

<https://ustr.gov/about-us/policy-offices/press-office/press-releases/2017/november/ustr-releases-updated-nafta>

Often in WTO ministerial meetings, trade ministers do not have much time to break through logjams (typically 48 – 72 hours maximum), and so unless there is a degree of alignment prior to the meeting, it is extremely unlikely that big differences can be papered over sufficiently to allow for a Ministerial Declaration that all can live with. We are entering into a particularly dangerous time now, as the US apparently withdraws from playing the brokering role it has historically played. Many of the countries the UK would be seeking to negotiate free trade agreements with as it executes its independent trade policy (such as Australia, New Zealand, Canada, and others) are Commonwealth countries. These countries are like-minded in terms of a shared commitment to trade liberalisation and competitive markets, and have worked together in other contexts to deepen liberalisation, such as through the Trans Pacific Partnership (TPP). They are discussing the kinds of concepts which should ultimately be multilateralised and could play a significant role in pushing them proactively in WTO councils.

Commonwealth Network Effects

The Commonwealth has significant network effects which could be exploited. It is important that these are used to ensure pro-competitive and liberalised trade, so that the overall levels of market distortions around the world are lowered, and consequently wealth is created in the global economy. The Commonwealth could also play a role in helping its members engage in the structural reform that is so necessary to improve their own economies. Such structural reform would also make members better trading partners, as they would then be able to negotiate both tariff reductions and regulatory improvements. Another potential use of the Commonwealth network is to bring together businesses that can integrate into global supply chains which feature Commonwealth countries. There are a number of Commonwealth groups, including the Commonwealth Enterprise and Investment Council (CWEIC) that can play a role in bringing Commonwealth businesses together. Finally, the Commonwealth can be used as a vehicle for members to identify trade barriers faced by their members which are imposed by other members. This could be a **Commonwealth Trade Barrier Mechanism (CTBM)**, and could be used to identify trade and regulatory barriers in all Commonwealth countries.

D. Multilateral

There are two aspects of our multilateral strategy: first, how to use our WTO transition to reinforce work in the other pillars; and second, how we can use our fully-fledged WTO membership to promote trade liberalisation and wealth creation, for our own economy and the world.

At the WTO

- **Use TRQ negotiations as a springboard for FTA negotiations with major TRQ partners**

The government has conceded that its TRQ proposals should be jointly presented with the EU. It has therefore lost the opportunity to make direct, bilateral presentations of its TRQ proposals to TRQ partners, preventing it from making the argument that it is able to offer greater liberalisation in (the near) future.

If the UK cannot do this, TRQ partners will seek to extract as many concessions from both UK and EU as possible during the TRQ process. New Zealand, for instance, has refused to accept the UK's schedules as placed before the WTO.¹³⁰ The UK should immediately move to a bilateral discussion with TRQ partners, where it is clear it will be able to gradually liberalise tariffs in agriculture to zero over time (depending to an extent on the benefits we can secure for our industries in this process), even if the EU claims this is a violation of the duty of sincere cooperation.

Customs union or similar language remaining on the table also prevents the UK conducting the process above; TRQ partners will be unwilling to negotiate given a risk that the UK will remain in the customs union.

- In the event of **no trade deal with the EU**, the UK could choose not to have a TRQ for TRQ partners that were also CPTPP members, and could discuss gradual liberalisation schedules now.
- **Use the WTO transition process to send important signals to our partners: e.g. the example of Aggregate Measure of Support (AMS).**

The UK can use its Aggregate Measure of Support (AMS)¹³² offer to signal free trade intent; we should seek no or *de minimis* AMS as an indication that we will not pursue production subsidies in agriculture beyond what it has now, and will limit direct payments to allowed green box payments.

¹³⁰ Global Meat News, "New Zealand opposes UK's WTO quota plan", July 27th, 2018. Available at: <https://www.globalmeatnews.com/Article/2018/07/27/New-Zealand-opposes-EU-and-UK-s-quota-split-proposal>

¹³¹ The EU is one of the few WTO members that has a country specific TRQ; the UK could have a global TRQ or simply move to gradual liberalisation.

¹³² Aggregate Measure of Support (AMS) is the amount of Amber Box (i.e. allowed) production subsidies that countries can adopt. The EU has a very high level of AMS set at €70bn (WTO, G/AG/N/EU/26 (2 November 2015) Notification of domestic support by the European Union for the 2012/2013 marketing year.) but it only uses €5bn as an insurance policy just in case some of its direct payments are included in the amber box and not the green box as they presently are.

The UK currently has two small production subsidy programmes, for beef and lamb in Scotland amounting to £39m, a very low amount, especially compared to the EU AMS level.

For too long, farmers have been subject to financial compliance burdens, instead of prioritising farming, and have been prevented from using technology to improve productivity, due to the EU's application of the precautionary principle. By integrating global supply chains, and linking British farmers with supply chains they have been outside for forty years, British farming can have a bright future without the need for subsidies, which ultimately destroy wealth for all. The current government position of a share of the very large European AMS will cause trading partners to question the UK's intentions, and whether a future government might engage in larger production subsidies to the detriment of producers around the world.¹³³

In bilateral negotiations with TRQ partners, and parties with whom the UK has have negotiations through the EU, it is critical the UK negotiates with partners by itself, to discuss the flexibility it has regarding the potential for further trade liberalisation in an FTA.

In the case of no deal, the UK should consider a global, as opposed to a country specific, TRQ¹³⁴, or even dispense with a TRQ altogether and initiate gradual tariff liberalisation.

- **The UK's relationships at the WTO in general**

The UK can play an active, leading role, supporting the rules-based international order in its own interest, and bring a strongly pro-trade, pro-development message to the table. This also means contributing significantly to badly needed reforms of a system in crisis. But to influence WTO discussions, the UK needs to demonstrate that it is an independent player.

133 Domestic Policy Settings are the domestic regulatory approach the UK will maintain in agriculture and other related areas. Settings may tend towards being more open if the UK does not maintain subsidies and regulatory barriers, or more closed if the UK pursues more subsidy and regulatory barriers.

134 Unlike a country-specific TRQ, a global TRQ operates on a first-come-first-served basis, where the UK would have a global quota for a particular product that countries would seek to fill.

There has recently been another challenge to the global trading system, namely the US approach - for example to the dispute settlement mechanism and the appellate body. While the dispute settlement mechanism is not perfect, it has often been referred to as the “crown jewels” of the WTO system itself.

It is very important that the US, as a major bulwark of the global trading system, acts as a constructive reformer. Given the US approach, this is clearly calling for other leadership from a nation that is committed to free trade principles. Here the UK can play a vital role, using its negotiations with the US to help ensure that the US attempts to deal with the problems it faces in international trade by helping strengthen, not weaken, the system. **One example is the recently agreed joint group (US, EU, Japan) set up to deal with market distortions in third countries.**¹³⁵ The UK should join this. If the US sees progress here, it is less likely to subvert the system, because it will see the WTO framework as one capable of dealing with major global challenges such as distortions in China, for example.

Looking ahead, in terms of the United Kingdom’s future role in the WTO, there are many WTO groups the UK should join as soon as possible. This would signal intent to Friends of the WTO System¹³⁶ that the UK has a liberalising vision of itself, and is committed to open domestic settings.

(i) The UK could join the Cairns Group of agricultural exporters. The founder nations have sought the reduction of agricultural trade barriers, and while the UK is not currently a major agricultural exporter, it is locked into EU supply chains. Embracing new technologies like synthetic biology stand to make the UK a net exporter of agricultural products.

(ii) The Manchester Group. Just as Australia launched the Cairns Group of agricultural exporters, as the world’s second-largest services exporter, the UK should launch the Manchester Group of Services Exporters. As the Cairns Group was named for the city of its founding, the Manchester Group would pay tribute both to the North’s transition from a manufacturing- to service-based economy, and of the central role of that city in the Victorian free trade movement.

¹³⁵ It is ironic that DG Trade in the EU supported the creation of this group, but that member states were concerned about it as it could apply equally to the increasing number of market distortions in the EU.

¹³⁶ Friends of the WTO System is a term of art and means the coalition of around 44 countries who seek progress and greater liberalisation at the WTO.

(iii) **The UK could join the e-commerce plurilateral initiative**, which is already fragmenting between the US, which wants a more extensive approach including dealing with local content regulation and other localisation rules, and the EU, with a more limited attitude, partly because of its commitment to spreading its regulatory approach on data protection (e.g. the General Data Protection Regulation (GDPR)). It is likely the US will lead a smaller group, which the UK could join, provided it is more open on data flows than the EU would be.

(iv) **The UK can take a leadership role in the Trade in Services Agreement (TiSA)**, in which the EU has been unable to include new services because of its approach to data flow. To play a meaningful role, the UK will need to separate itself from the EU data flow approach, while seeking to ensure adequacy with the EU's data regime. The group has been languishing partly as a result of disagreements between the US and the EU, and is in need of revival. There would be no better agent of revival than the world's second largest exporter of services.

(v) **The UK could also table services liberalisation offers to revive the GATS built-in agenda on services**, a much-neglected area. When the GATS was launched in 1996, it was anticipated that countries would submit a series of services offers, as the GATS is a positive list agreement where only services that are affirmatively put on the table for liberalisation are included. But the **GATS has lacked a services' champion**, an economy that will be an effective advocate for bilateral and plurilateral arrangements for liberalisation. **The UK can take a leading role in the Services Working Group** to expand services coverage, and as a **services and digital trade champion** can take a leading role in both working groups. The UK can also support multilateral recognition initiatives in certain professions rather than a series of bilateral ones through FTAs (currently there is only a multilateral recognition discipline for accounting).

(vi) **The UK can also help with WTO dispute settlement reform**, but as with digital and services, the UK needs

to take these steps now, demonstrating to WTO Friends of the System and others that the UK will be a force for liberalisation.

(vii) **The UK could revive the stalled work in the WTO Rules of Origin committee**, recognising that increasingly restrictive rules of origin have become tools of trade policy, and that the original GATT provisions, which left it to members to decide their rules of origin, were not developed at a time of so many preferential arrangements, and are unfit for purpose. The UK should, over the long-term, ensure liberal rules of origin apply; this would unlock considerable supply chain efficiency across the world. This is another example of a WTO group covering an increasingly important area that has stalled.

(viii) Geneva is a much better context for the UK's global aspirations than Brussels. **The government should seek to notify (even if not officially) its intent to negotiate an FTA with the EU in the WTO and encourage WTO partners to pressure the EU to behave in a constructive fashion**, and negotiate based on commercial logic instead of political considerations. These countries have a stake in ensuring that this is indeed the EU approach. Anything that increases the cost of global supply chains (imposing tariffs and unnecessary friction between the UK and EU) will be bad for the managers of big global supply chains that flow through them, like the US, Japan, and others.

At the OECD

The UK should step up activities at the Organisation for Economic Co-operation and Development (OECD), where it has its own seat. **The UK should increase its work in the OECD Trade Committee and re-launch and lead the OECD Joint Group on Trade and Competition**, which would cover much of the interface of trade, competition and regulation.

The UK and standard setting bodies

The UK should play a leadership role in all standard-setting bodies, using the historic credibility of the British Standards Institute

(an example of soft power) to move these bodies in a more pro-competitive direction. Instead of the top-down regulation favoured by the EU through its standards setting bodies CEN, CENELEC and ETSI, the UK should promote a more voluntary standard setting mechanism, subject to a requirement to ensure standards do not exclude new entrants. This can be **supplemented by the competition advocacy of the CMA and other competition agencies through the International Competition Network (ICN).**

The UK should also spearhead an agreement between the main financial centres to include Singapore, New York, Tokyo and others, to promote a shared approach to global financial services standards, but which also allows UK sovereignty, while addressing barriers to services trade and agreeing a common pro-competitive position in international bodies.

Planning for the UK and EU not agreeing a Free Trade Agreement (FTA)

A 'no deal' scenario, as defined by the government,¹³⁷ is one where the UK leaves the EU and becomes a third country at 11pm GMT on 29th March 2019 without a Withdrawal Agreement and framework for a future relationship in place between the UK and the EU. This result would clearly be far from ideal and it is one that very few people would favour. Nonetheless, it is right to prepare for it seriously, for three reasons:

1. The UK's bargaining position in the negotiations with the EU would be fatally undermined if there is no credible alternative to doing a deal;
2. It is always possible that the two sides fail to reach an agreement despite their best efforts, for example because time simply runs out, or because domestic political conditions change;
3. Many of the steps that need to be taken to prepare for 'no deal' will be necessary anyway in other Brexit scenarios, depending on the degree of disengagement from the EU's single market and customs union.

In preparing for and assessing the impact of 'no deal', however, it is important to recognise that this term could cover a range of outcomes. The media headlines have tended to focus on a chaotic no-deal Brexit,

¹³⁷ <https://www.gov.uk/government/publications/uk-governments-preparations-for-a-no-deal-scenario/uk-governments-preparations-for-a-no-deal-scenario>

where there are no agreements at all, on anything, and where both sides allow relations to break down more or less completely, despite their own economic interests and legal obligations. This is a very literal interpretation of 'no deal', and potentially just a straw man.

Nonetheless, the fact that actions can still be taken to mitigate any additional costs of 'no deal' does not mean that the risk can be dismissed lightly. For example, if the UK simply becomes a third country, planes would indeed be unable to fly.¹³⁸ Air traffic rights are not covered by WTO rules and only exist between the UK and EU (and between the UK and much of the rest of the world) as a consequence of the UK's current membership of the EU's Single Aviation Market. There would also be problems with the certification of UK aircraft, components and personnel.

There are some straightforward solutions to these problems, typically revolving around some combination of retaining UK membership of the European Common Aviation Area (ECAA) and/or negotiating new air services agreements. The key question for the EU is whether the necessity of keeping planes flying outweighs any threats to the integrity of the single market or the risks of giving the UK special treatment. The answer to this must surely be 'yes'.

But this still requires flexibility on both sides. On the UK's part, the government may need to recognise some continued role for the CJEU in supervising the aviation sector. And to avoid a temporary hiatus after Brexit, the EU would need to be willing to negotiate a new agreement on aviation with the UK before it becomes a third country, and separately from the Article 50 process.

The upshot is that there are a number of crucial elements in 'no deal' planning.

First, it will be important to maintain goodwill as far as possible. 'No deal' does not necessarily have to be acrimonious, but this may also require concessions on both sides. On the UK's part, this is likely to mean **unilaterally agreeing the rights of EU citizens already in the UK and reaffirming commitments made on the free movement of people across the Irish border**. These are things that the UK would, or should, be doing anyway.

More controversially, the UK might still have to pay some, if not all, of the estimated £39 billion financial settlement. This is discussed further below,

¹³⁸ <https://iea.org.uk/publications/planes-wont-fly/>

but even the full £39 billion could be a small price to pay to help avoid a chaotic Brexit.

Second, it will be important to ensure that the UK strengthens its own institutions. Some opponents of Brexit appear to believe that we would be lost without EU institutions to set rules and regulate our lives. In practice, most EU rules are implemented by national regulators. The UK therefore already has a Civil Aviation Authority, Food Standards Agency, medicines regulator, and so on. But they may end up with more work to do, and need to be properly resourced. The same applies, of course, to UK border and customs agencies.

Third, and perhaps most importantly, the UK should be ready to act unilaterally and in ways that best serve the long-term interests of the economy as a whole. Again, some opponents of Brexit assume that the UK can't fix problems on its own, or even that the government would act in ways that make problems worse.

One example here is the common assumption that the government would choose to maintain the level playing field required under the WTO's MFN rules by imposing tariffs on imports from the EU, rather than by lowering them on imports from the rest of the world. Another is the fear that the government would impose restrictions on migration that compound skills shortages in key sectors.

These principles can be applied to many of the challenges that a no-deal Brexit would present, for which responses are being prepared. For example:

1. There are many areas where the UK could simply recognise EU standards, unilaterally, as just as good as its own. This has already been proposed¹³⁹ and accepted¹⁴⁰ for many medicines and medical devices. Crucially, this pragmatic approach would still allow the UK to recognise different standards applied elsewhere in the world, and would not require all UK producers to follow a Common UK/EU Rule Book;
2. There are other areas where the problems are grossly overstated and can be dealt with easily, ranging from maintaining the Single Electricity Market (SEM)¹⁴¹ on the island of Ireland to continuing the Tripartite Agreement governing the movement of racehorses¹⁴²;

139 <https://iea.org.uk/publications/medical-provisions-post-brexit/>

140 <https://www.gov.uk/government/publications/how-medicines-medical-devices-and-clinical-trials-would-be-regulated-if-theres-no-brexit-deal/how-medicines-medical-devices-and-clinical-trials-would-be-regulated-if-theres-no-brexit-deal>

3. There will be areas where the UK government should step aside and allow market forces to do their job, rather than replicate market-distorting intervention previously undertaken by the EU. This includes regulations to set mobile roaming charges¹⁴³, where the interests of consumers are already well served by strong competition and new technologies.

Encouragingly, these principles already seem to run through most of the government's own papers¹⁴⁴ on preparations for a 'no deal' scenario. But there is still a need for a shift in mindset so that all parties recognise that a 'no deal' is a credible alternative.

Finally, customs preparedness is also a central part of no deal planning. Here, Government should implement self-assessment for customs declarations, reducing the burden of more returns on the HMRC system and resources; train and support businesses to achieve authorisations for the full extent of available facilitations; use the private sector to carry out training and audits, alleviating resourcing pressures on HMRC; relax or repeal requirements for comprehensive customs guarantees, alleviating the burden on businesses; and extend postponed accounting for all imports, negating the cash flow impact from ending acquisition VAT and boosting the competitiveness of supply chains that import from the rest of the world.

141 <https://iea.org.uk/publications/generators-on-barges-in-the-irish-sea/>

142 <https://iea.org.uk/publications/grand-national-would-be-hit-by-a-no-deal-brexite/>

143 <https://iea.org.uk/publications/mobile-phone-bills-will-soar/>

144 <https://www.gov.uk/government/collections/how-to-prepare-if-the-uk-leaves-the-eu-with-no-deal#overview>

Chapter Five

Strategic Approach

This chapter makes recommendations about what immediate steps can be taken to ensure that the goals set out in this alternative approach can be achieved.

From the outset, it should be the UK Government's objective to use the different pillars outlined here to apply pressure on the EU. It is not possible, or indeed advisable, to lay out all the required strategic thinking of a party to a trade negotiation in a public setting, so these areas must by definition be limited. We therefore set out central non-exhaustive areas.

First, it is vital that the **negotiating dynamics** with the EU are carefully handled. These relate to the following areas:

- **Pressure to isolate the EU** by agreements with other countries, demonstrating that on issues like good regulatory practice and regulatory recognition, **the EU is an outlier** in recognising regulations only when they are identical, or in limited circumstances.
- **Pressure internally on EU member states** where there would likely be significant losses in the event of no EU trade deal. These include Bavaria (cars and dairy), Ireland (beef and dairy), Catalonia (cars and dairy), and Northern Italy (textiles and dairy) (see Figure 2 below).

Figure 2: Estimated impacts of applying the Common External Tariff on selected industries^{145 146}

| Country | Sector | Change in annual exports to UK in 2019 (Euro m) | Changes in annual exports to UK in 2019 (%) | Net annual impact on overall sector exports (%) | Net impact on annual producer revenues (Euro m) | Estimated impact on jobs | Regions potentially impacted |
|---------|-------------|---|---|---|---|--------------------------|---|
| EU27 | Automobiles | (4,180) - (14,675) | (10%) - (36%) | (1%) - (5%) | (4,013) - (12,820) | (15,552) - (49,688) | - |
| EU27 | Dairy | (1,584) - (2,812) | (56%) - (100%) | (4%) - (8%) | (1,171) - (1,726) | (6,875) - (10,136) | - |
| Germany | Automobiles | (2,245) - (7,880) | (10%) - (36%) | (2%) - (6%) | (2,218) - (7,586) | (8,597) - (29,403) | Baden-Württemberg, Bavaria, North Rhine-Westphalia |
| Germany | Dairy | (247) - (378) | (66%) - (100%) | (3%) - (5%) | (214) - (299) | (1,259) - (1,756) | Bavaria, Lower Saxony, North Rhine-Westphalia |
| France | Dairy | (335) - (591) | (57%) - (100%) | (6%) - (10%) | (294) - (466) | (1,147) - (1,814) | Bretagne, Pays de la Loire, Basse-Normandie |
| France | Beverages | (114) - (413) | (8%) - (24%) | (1%) - (3%) | (138) - (402) | (537) - (1,566) | île de France, Champagne-Ardenne, Rhône-Alpes, Provence-Alpes-Côte d'Azur |
| Ireland | Beef | (656) - (971) | (68%) - (100%) | (34%) - (50%) | (579) - (802) | (3,397) - (4,711) | West (Mayo, Roscommon, Galway and Galway City) and Border (Cavan, Donegal, Leitrim, Louth, Monaghan, Sligo) regions |
| Ireland | Dairy | (409) - (732) | (56%) - (100%) | (23%) - (42%) | (209) - (255) | (1,224) - (1,495) | West (Mayo, Roscommon, Galway and Galway City) and Border (Cavan, Donegal, Leitrim, Louth, Monaghan, Sligo) regions |
| Italy | Clothing | (145) - (529) | (12%) - (43%) | (1%) - (3%) | (136) - (371) | (1,222) - (3,336) | Lombardia, Veneto, Toscana |
| Italy | Dairy | (106) - (204) | (52%) - (100%) | (4%) - (8%) | (93) - (176) | (545) - (1,034) | Lombardia, Emilia, Romagna, Veneto, Piemonte, Campania |
| Spain | Automobiles | (390) - (1,371) | (10%) - (36%) | (1%) - (5%) | (368) - (1,053) | (1,426) - (4,080) | Cataluña, Castilla y León, Comunidad Valenciana |
| Spain | Clothing | (68) - (251) | (12%) - (43%) | (1%) - (2%) | (63) - (170) | (565) - (1,531) | Cataluña, Galicia |

¹⁴⁵ Singham, S., "If EU intransigence results in tariffs, it could cost continental exporters dear in revenues and jobs", Brexit Central, October 16th, 2017.

Available at: <https://brexitcentral.com/eu-intransigence-tariffs-cost-continental-exporters-dear-revenues-jobs/>

¹⁴⁶ The above does not include the increased cost of capital if no trade deal leads to a fragmentation of the single capital pool in the City of London.

Any such attempts can only be initiated once the customs union or any variant of it (such as the FCA, NCP or other similar arrangements) has been taken off the table. Indeed if it proves necessary to unilaterally apply a zero tariff rate in some sectors, even with a view to re-applying the bound rate in a fixed period after stabilisation, this could cause many EU producers to have different agendas, allowing the divergence the UK would benefit from to emerge.¹⁴⁷

Dealing with EU Non-Cooperation

It may well be that the EU does not cooperate with UK Government proposals. In this case, the Government will need to move to a more proactive footing in response to EU obstructionism, not accepting the EU's negotiating mandate and demands.

The operating assumption seems to have been that supplicatory behaviour will lead to a desirable outcome. This fails to understand how the EU works. Indeed, the EU has obstructed the UK in a number of ways, such as reneging on an undertaking to assist the UK's application to accede to the Government Procurement Agreement. The EU has published a number of position papers suggesting a lack of cooperation with the UK that violates the duty of sincere cooperation (which flows in both directions), and the principle of good neighbourliness in Article 8, of the Treaty on European Union.^{148 149} The UK should be prepared to inventory these violations and if necessary litigate these issues as part of a signaling mechanism. Many other countries have similar difficulties dealing with the EU. This approach will confirm their views and strengthen the UK's hand.

- **In this vein, if the EU refuses to recognise UK regulations on day one of Brexit, the UK should be prepared to take action in the WTO under the GATT and the SPS and TBT Agreements .** It is true that such claims can take years to resolve, but the UK should use threats of trade litigation to help support its negotiating objectives, as is normal practice around the world.

The purpose of these actions is not because we expect them to cause an immediate change in EU behaviour, but because this is one of the ways we can highlight that **the EU is in fact an outlier in its behaviour.**

The UK's right to negotiate and the Duty of Sincere Cooperation. The UK has the right to negotiate with third parties now, and does not have to

¹⁴⁷ When the US government imposed the steel and aluminum tariff under section 232 (US Customs and Border Protection, 2018, Section 232 Tariffs on Aluminum and Steel), France and Germany took significantly opposing views on what the approach should be. If one tariff line can cause such division, this carefully calibrated strategy should yield significant divergence which the UK could then exploit.

¹⁴⁸ Articles 8 and 50 (13 December 2007)

¹⁴⁹ European Union (Notification of Withdrawal) Act 2017, Chapter 9.

wait until it exits the EU. This makes sense given that the UK is currently negotiating its WTO transition: it cannot be limited in that regard until the moment it leaves the EU, as WTO partners need to know what their trading terms will be on the UK's exit. However the UK should negotiate across all pillars simultaneously. The duty of sincere cooperation flows both ways, and the UK is entitled to cooperation from the EU, as the UK as a current member state. The UK should be robust in its approach to the duty of sincere cooperation and not accept the EU's interpretation. The UK should also include in its outreach to other countries a clear explanation of its own interpretation of the duty of sincere cooperation, and why it believes that it has right to negotiate agreements ready to come into effect at the end of the Transition Period or as soon as possible in the event that no Withdrawal Agreement is reached.

- **Transitional Period**

The UK cannot accept a Transition Period that includes the EU's interpretation of the Duty of Sincere Cooperation and the Common Commercial Policy continuing to apply, nor can it accept the principle of continuity that appears to be the current government view, because this will impede the exercise of this plan and push the UK further onto the EU's chosen field.

While the Transition Period is necessary, and its terms as set out in the Withdrawal Agreement should, for pragmatic reasons, not be re-opened at this stage, the provision specifically acknowledging the UK's right to negotiate and sign agreements with third countries and bodies¹⁵¹ is critical. The present interpretation of the duty of sincere cooperation, if continued, will limit the usefulness of these important and hard-won provisions. Similarly the Common Commercial Policy also can be used by other member states to impede the UK's ability to negotiate properly.

EU complaints about a particular UK negotiation, both to the UK and the other party, are liable to render the UK unable to be a credible negotiating partner. The presence of the Common Commercial Policy means there is no incentive for the UK to negotiate properly with the countries it has agreements with through the EU, except in the most general of ways. By allowing the EU to negotiate these arrangements on behalf of the UK, the UK will lose the ability to convey to these countries that it is capable of greater liberalisation in the future (which needs to mean very soon). The UK has allowed itself to be trapped on the EU's playing field. If the UK does continue with the Transition Period, then it must take a far more robust approach to

151 Her Majesties Government, "Draft Withdrawal Agreement – 19th March 2018", Article 124:4.

Available at: <https://www.gov.uk/government/publications/draft-withdrawal-agreement-19-m>

the duty of sincere cooperation, and seek assurance to safeguard the right of the UK to progress its own negotiations during the Transition Period. We suggest amending article 124(4) of the Withdrawal Agreement by adding “neither the principle of the duty of sincere cooperation, nor the common commercial policy will be relied on by the Union or any Member State to disadvantage in any way the UK or third party’s negotiations. Violation of this provision shall be, itself a violation of the duty of sincere cooperation by the Union.”

Simultaneous Non-EU Approach

In these contexts, the UK Government should proceed as follows

UK-US FTA

1. Make the case to the US why it is strongly in the US interest to have an FTA with the UK, on the basis that the US needs allies in its advocacy of good regulatory practice and a reduction of anti-competitive barriers and distortions, and that the UK would be a major ally in this process.
2. Galvanise the support of US firms and global supply chains to understand the value of a major G-7 nation diverging from the EU regulatory system.
3. Accelerate US negotiations by moving to chapter-by-chapter negotiations of an FTA, closing chapters and agreeing a time-line.

CPTPP

1. Formally apply to join CPTPP as soon as possible
2. Work with CPTPP members to keep pushing for UK accession to CPTPP.

WTO

1. Negotiate TRQs bilaterally, having proposed to the EU an FTA+ deal.

2. Informally notify WTO Membership of FTA+ intent with the EU, unilaterally if necessary.
3. Offer a de minimis AMS amount as a signal of UK commitment to liberalisation.
4. Indicate which groups the UK seeks to join on transition, thus showing coalitions like the Friends of the System the immediate value of UK independence.
5. Be prepared to offer a package deal on TRQs/AMS and further liberalisation for key TRQ partners and potential trade partners.
6. Prepare a default option of unilateral liberalisation in key sectors (at least at the applied rate for a temporary period) and announce these to WTO members as a fixed two or three year applied rate of zero, on the basis that the UK will apply the bound rate to all members with whom it does not have a deal in March 2022.

The Approach to the UK-EU FTA and Withdrawal Agreement

- **UK-EU FTA**

1. The government should present a UK offer along the lines suggested in this document, with negotiating text on the table (for example the draft chapter in the Annex), recognising that closing text improves the negotiating environment and makes a final deal more likely (this has occurred even in the NAFTA re-negotiation process, where chapters, including relatively controversial ones such as Regulatory Coherence, have been closed already). Even if the EU maintains that the time is not ripe for a trade negotiation, preliminary soundings of Task Force 50 suggest that the EU would welcome text, from which to agree the future framework for the trade relationship.
2. The core elements of the offer will be comprised in an FTA to include the following:
 - a. Zero tariffs in goods and agriculture including

liberal rules of origin allowing both parties to cumulate across other FTAs;

b. Customs and trade facilitation chapter and Irish border protocol;

c. Government procurement

d. Regulatory coherence including specific sectoral annexes (e.g. pharmaceutical, etc.)

e. Competition

f. State aids

g. Services with maximum liberalisation based on a negative list approach (all sectors to be included); no restrictions in all four modes of service supply in either market access or national treatment columns.

h. Mutual recognition of occupation licensing;

i. Specific sectoral annexes in key areas including telecoms, data and financial services;

j. Investment;

k. Dispute settlement.

If the advanced FTA concept outlined above cannot be agreed as the framework for the purposes of the Withdrawal Agreement, or if a Withdrawal Agreement cannot be agreed at all, the EU will need to justify to its citizens and trading partners why it has been able to agree advanced measures in its existing FTAs like CETA, and its existing MRAs, such as the agreement with New Zealand on sanitary measures in meat and animal products and the suite of MRAs in place with the US, but is not able to agree similar arrangements with its closest neighbour and key trading partner.

The UK would be seeking to negotiate the ceiling, but be prepared to fall back onto the reserve parachute.

In negotiations, the EU has successfully used time against the UK in the hope that it would be forced to concede to the EU's terms. Given that this was a specific strategy of the EU, it would be an error now to say that the negotiations out of time and must accept the EU's terms. Many negotiations are resolved in the final period of negotiation; however, the most important thing the UK can do is reset the process, retake control of the agenda, and move forward rapidly **across all the pillars simultaneously as a matter of urgency.**

Options

As the negotiations pursuant to Article 50 stand, most of the legal drafting of the Withdrawal Agreement has been provisionally agreed. The most fundamental outstanding elements are the framework for the future relationship and the so-called backstop arrangement for the Irish border ("Irish Backstop"). It was the desire to avoid the Irish Backstop being invoked that informed the design of the White Paper – a way of preserving free circulation of goods without either leaving Northern Ireland in the EU's customs union and single market, or having the whole of the UK stay in the single market and a customs union.

The UK government has options available to it that would deliver varying levels of autonomy, negotiability and associated risk. At one end of the spectrum, terminating the negotiations in order to focus on 'no deal' preparations, including protecting the positions of EEA citizens by unilateral measures, could deliver the most independence in the shortest time frame. This option would not mean no exit arrangements at all, as the UK could propose self-contained agreements with the EU in areas like aviation and nuclear safety, enabling the Council to issue the necessary mandates to the Commission to negotiate such matters, and refer the question of the financial settlement to independent arbitration.

At the opposite end of the spectrum, the UK could request an extension of the negotiating period to enable the outstanding provisions of the Withdrawal Agreement to be completed, and to advance no deal preparations. Against this option are the likely domestic political consequences, the possibility that the extension would be declined and the protracted uncertainty for businesses and individuals.

The option being pursued by the Government is being resisted by the EU, due to the legal and practical challenges of the FCA and the disaggregation of goods from other components of the single market. It may also be voted down by the UK Parliament.

An option is therefore required to maximise the progress already made on the terms of the Withdrawal Agreement but unblock the impasse over the Irish border and future framework. The government should seek to retain all of the agreed elements (the financial settlement, citizens' rights, the transition period and withdrawal terms) and propose a new backstop and framework for a future relationship. The new backstop would comprise a basic free trade agreement between the UK and the EU for goods, and a commitment by the parties to undertake all necessary investment and cooperation mechanisms to enable formalities on trade between Northern Ireland and Ireland to be overseen away from the border. This would enable the completion of the Withdrawal Agreement and incentivise the parties to agree a better FTA during the transition period. It would also enable the UK to negotiate more effectively with rest-of-world trading partners during the transition, with a baseline element of the relationship with the EU known at the outset.

Position on the Joint Report

If the UK determines that the EU's position makes a backstop impossible without jeopardising the integrity of the UK single market and the Union itself, then it should state that clearly as a non-negotiable item that it does not agree with the EU's interpretation of the Joint Report.¹⁵²

It can then make an offer to the EU on the basis that it no longer agrees with the EU's changing interpretation (for example, even though there are currently different VAT regimes on the island of Ireland, the EU is suggesting that there should be no difference; as well as the notion that alignment of regulation consistent with the all-island economy in the Joint Report has been interpreted by the EU and UK to now mean regulatory identity over all of the economy).

This would not need to have the effect of re-opening other questions such as payments of money, citizens and the Transition Period, which were settled in principle in the Joint Report and have legal drafting agreed in the draft Withdrawal Agreement. However, given that the Irish Backstop issue is holding up progress on the Withdrawal Agreement, we think a new approach is more likely to lead to a conclusion of this part of the negotiation.

However, the UK must recognise that the difficulty with the EU approach is much deeper, in the negotiating mandate of the EU itself which was accepted by the UK government. It is not logical to seek

¹⁵² Commission to the European Union, "Joint report from the negotiators of the European Union and the United Kingdom Government on progress during phase 1 of negotiations under Article 50 TEU on the United Kingdom's orderly withdrawal from the European Union.", Presented jointly by the negotiators of the European Union and the United Kingdom Government, December 8th, 2017.

Available at: https://ec.europa.eu/commission/sites/beta-political/files/joint_report.

to negotiate a future framework for the trade relationship without at least commencing negotiations on what that framework could be, for example on the basis of an advanced FTA. **From these initial discussions, a framework consistent with the Article 50 negotiating mandate can be agreed, and the transition period can be preserved, provided the UK acts now.**

The UK could present the EU with its own vision of what an FTA looks like, with an Irish border protocol in the FTA (as part of the customs and trade facilitation chapter), and a version of what arrangements the UK would seek to have in place in the event of no trade deal.

Strategic Actions Across Other Pillars

The UK would action the other pillars described in this document immediately, so that negotiations with the US, application to join the CPTPP, and the final stages of WTO transition run concurrently with the EU negotiation.

The government would seek to ensure that TRQ partners were reasonable in the WTO transition and accepted the UK's bilateral offer of historic market shares plus,¹⁵³ in exchange for initiating negotiations to gradually liberalise immediately, and to play a role in arguing for greater liberalisation in the WTO.

If no Withdrawal Agreement can be reached with the EU or if the Withdrawal Agreement is rejected by a vote in the UK Parliament or via the EU's own processes

If the UK and EU are unable to come to terms, the UK will leave without a Withdrawal Agreement and Transitional Period. This would result in the UK falling back onto the Common External Tariff as an independent WTO member. It would mean a considerably more limited financial arrangement. Both the UK and EU need to plan for this eventuality.

- **Financial settlement**

The UK's stated willingness to pay a large 'divorce bill' as part of the Withdrawal Agreement from the EU still rankles with many – and understandably so. It is not immediately obvious why the UK should continue

¹⁵³ The current UK and EU offer in the TRQ negotiation is for a split based on historic market shares. The UK could offer historic market shares plus a small amount to improve its offer.

to contribute to the EU budget long after Brexit, especially when the EU appears reluctant to offer the UK better terms on the future relationship than it would to any other country. This concern would, of course, be all the stronger in a ‘no-deal’ scenario.

Nonetheless, the UK should be guided by the principle that it will honour commitments made to the EU in the past. The Prime Minister pledged in her Florence speech¹⁵⁴ in September 2017 that ‘the UK will honour commitments we have made during the period of our membership’.

It is therefore wrong for some to claim that the divorce bill is an additional ‘cost’ of Brexit. In reality it is simply money that the UK would have had to pay anyway had it still been a member. But nor is it necessarily anything to do with the future relationship, or meant to be a down payment for a comprehensive free trade deal or streamlined customs arrangements. Indeed, the UK shouldn’t be expected to pay extra for these benefits anyway, since they would help both sides.

One could argue that the UK’s willingness to continue to contribute to the EU’s annual budget until the end of 2020 should be seen as a quid pro quo for the EU’s offer of a standstill transition period over this timeframe. But that’s not strictly what it’s supposed to be either. In any event, these annual payments account for less than half of the estimated £35-39 billion total cost of the financial settlement, as detailed by the NAO¹⁵⁵.

It is true that many (including a House of Lords committee¹⁵⁶) have argued that the UK would be on strong legal ground if we decided to walk away with paying a penny. And even though the UK and the EU have signed up to a methodology¹⁵⁷ for the financial settlement, ‘nothing is agreed until everything is agreed’.

But the threat of refusing to pay would not be costless. Whatever the legal technicalities, refusing to settle up could be seen as bad faith – and not just in the rest of Europe. Some third countries looking to do trade deals with the UK might not be impressed if we appear to go back on promises to our former partners in the EU.

154 <https://www.gov.uk/government/speeches/pms-florence-speech-a-new-era-of-cooperation-and-partnership-between-the-uk-and-the-eu>

155 National Audit Office, “*Exiting the EU: The financial settlement*”, Her Majesty’s Treasury, April 20th, 2018. Available at: <https://www.nao.org.uk/report/exiting-the-v-settlement/>

156 European Union Committee, “*Brexit and the EU budget*”, House of Lords, March 4th, 2017. Available at: <https://publications.parliament.uk/pa/ld201617/ldselect/ldeucom/125/125.pdf>

157 Commission to the European Union, “*Joint report ...*” Presented by the negotiators of the European Union and the United Kingdom Government, December 8th, 2017. Available at: https://ec.europa.eu/commission/sites/beta-political/files/joint_report.

Finally, even £39bn would be less than 2% of one year's UK GDP, spread over many years, and just a few tenths of a percent of the GDP of the rest of the EU. It would be difficult for the other countries of the EU to have to fill the gap, but these sums are simply not large enough to be game-changers. Overall, then, the divorce bill probably isn't as powerful a bargaining chip as many seem to think. But it remains part of the UK's hand. If the negotiations do stall, the money should surely come back into play. Indeed, it still seems perfectly reasonable for the UK to attach conditions to the financial settlement, even at this late stage.

For example, the UK could agree now to pay the annual net contributions up until the end of 2020 (perhaps £16bn), regardless of the progress of the talks. This would go a long way towards meeting the Prime Minister's Florence pledge, which was that the UK's partners shouldn't fear 'they will need to pay more or receive less over the remainder of the current budget plan as a result of our decision to leave'. Other interested parties elsewhere in the world would probably also regard it as a fair offer.

In summary, even in the absence of a comprehensive withdrawal agreement, paying at least some of the financial settlement could be a relatively small price to pay for maintaining goodwill. However, if the UK and the EU can't agree a satisfactory long-term deal (or, of course, if the UK withdraws from the EU with no deal) we could retain some or all of the remainder of the settlement that relates to payments beyond 2020.

- **Irish Border in the event of no Withdrawal Agreement**

In the event of no agreement, the UK (and the EU if it so chose) could choose not to impose any checks on goods trade at the Irish border, using legal and technical solutions to manage the trade away from the border. It would also be possible to seek a WTO waiver (allowed under Article IX:3), available when the precise application of WTO obligations would conflict with some other overarching principle of international law, or if there is an emergency situation in a WTO member. While waivers are narrowly drawn, the potential for conflict in Northern Ireland and a return to the troubles would appear to be fully justify any request for a WTO waiver. For example, the waiver process has been used with respect to the Kimberley Certification Scheme for Rough Diamonds, and for the TRIPs Access to Essential Medicines agreement. Under the WTO's waiver power, a contracting party can request the General Council or the Ministerial Conference to waive a WTO obligation by consensus (the GATT rule required three quarters

of the membership to approve). The time period for a response from the General Council is ninety days. Such a waiver could be granted until the next WTO Ministerial Conference at which it could be renewed depending on the circumstances. Additionally or in the alternative, a national security exemption under Article XXI would be possible on the basis that it is necessary to take this action in order to protect the UK's national security interests in time of war or other emergency in international relations (Article XXI(b)(iii)) or under Article XXI(c)'s provisions which allow parties to act to maintain United Nations Charter obligations to maintain international peace and security.

It is extremely unlikely that any WTO member will complain, given the question of the security of Northern Ireland. It is open to the EU to do the same, and if it does not, it would need to explain this to the Republic of Ireland. The Waiver or National Security exemption could be for a limited (say two-year period) as the systems referred to above are brought on-line. In any event, the UK should activate the measures set out in this document, and should have started to prepare for them much in advance of the date of this plan.

- **Economic Relationship**

In a no trade deal scenario, the UK could apply zero tariffs in agri-food (to control food price inflation)¹⁵⁸, but would have to do so on an MFN basis for the world. It could selectively apply other tariffs at the zero level also. EU member states are more likely to diverge at this point from each other if some tariffs are retained at the Common External Tariff level (the bound rate) while others are reduced to zero for the world. For example, French farmers and German car manufacturers would have very different interests and might react differently to unilateral tariff reduction on an MFN basis, especially in agriculture, if the UK were also to use a mechanism to protect its farmers from subsidies or other anti-competitive practices, as described in this document. It is at this point that member state harmony might be disrupted.

If the UK chose to apply tariffs at the zero rate, while maintaining its binding at the CET rate, it could reapply the bound rate within two years of leaving the EU, creating an incentive for all parties to negotiate trade deals with it.

¹⁵⁸ The UK would bind its tariffs to the CET in the WTO, but apply lower tariffs for a time-limited period.

Chapter Six

Domestic Reforms for the UK

Domestic Aspects of Autonomy for the UK

There are a number of areas which, while outside the scope of trade and regulatory policy, are serious concerns arising from the White Paper, and will need to be addressed as the UK leaves the EU. It is not the intent of this paper to discuss these issues in great detail, but they are flagged up to the extent that they have a trade implication or spill-over effect.

The main questions here are as follows:

- **Defence and Security**

The UK should remain open to cooperating on an ad hoc basis with EU allies, but not to the detriment of its Five Eyes relationships. This is an area of particular concern. The EU is moving in the direction of a European army, according to the President of the European Commission, and a common defence policy, with severe implications for the Article 50 negotiations and UK sovereignty. It is crucial that major UK security partnerships, such as NATO, and the US-UK relationship, remain the focus, and nothing is done with the EU to imperil this.

It will be especially important for the UK to avoid the White Paper's proposals of "coordination on foreign policy [and] defence". The White Paper makes a range of hazardous commitments to UK-EU defence integration, including the implication that the EU itself will be able to use "civilian and military assets and capabilities", and pursue "commitments to support a collaborative and inclusive approach to European capability development and planning". This also covers a UK offer to "host an Operational Headquarters (OHQ) and consider future contributions to EU Battlegroups as part of the enhanced future partnership", with the ambition that "the EU [make] best use of UK assets". White Paper "collaboration" would also include collaboration with Permanent Structured Cooperation

(PESCO), but in which the UK should not be an official, or de facto, member. It is also important to note that in the defence area, there is a spill-over into UK trade relationships because defence cooperation in the trade area with the US is so important. The UK's defence and procurement commitments with respect to the EU should not risk cooperation with the US in this area.

- **Immigration**

Free movement of workers and the associated rights of EU citizenship cannot continue after the UK has left the EU. The UK will therefore need a comprehensive and sensible immigration policy. This policy needs to enable dynamic recruitment of skills and talent where the market requires.

Government functioning

Constitutional adjustments will be needed once the UK leaves the EU, because with full regulatory autonomy the UK will need to operate on the global stage in a different way from how it has operated since joining the EU. If appropriate attention is not paid to this area, the UK will not have the institutional machinery to be able to operate in an effective manner on the global stage. Central changes should include the following:

(i) Greater devolution of powers to local government and devolved administrations, where feasible.

(ii) Injection of more specific long-term subject matter expertise into the Civil Service through the use of political appointments at senior levels with the understanding that the civil service should do less, and elected officials more.

(iii) Upgrading of parliamentary capacity to scrutinise foreign trade and other policy decisions of the government. The relevant parliamentary committees will become more important over time, and it is important for them to be treated with the seriousness they deserve. In other countries which operate their own independent policies, these committee chairs are very important political figures in their own right, and remain in these positions for significant periods of time which enables their offices to build up expertise.

They are often selected for Cabinet positions as they have developed relevant expertise and experience over long periods of time, and so these positions become sought after, and committee chairs (and ranking members) remain in place for long periods of time.

Annex

REGULATORY COHERENCE

1. Definitions

For the purposes of this Chapter:

- (a) “Competition Agency” means:
 - (i) in the case of the United Kingdom, the Competition and Markets Authority; and
 - (ii) in the case of the European Union, the European Commission Directorate-General for Competition;

- (b) “Covered Action” means any of the following actions to the extent they are material:
 - (i) legally binding substantive rules including subordinate regulations;
 - (ii) interpretation of rules that have a binding effect on agencies or private parties;
 - (iii) adjudications that have a binding effect on one or more parties;
 - (iv) procedural rules that bind agencies or the public; and
 - (v) decisions to grant, revoke, extend, or modify a License;

- (c) “International Instruments” means any document adopted by international bodies or fora in which both Parties’ Regulatory Agencies participate, including as observers, and which provide requirements or related procedures, recommendations or guidelines on the supply or use of a service, such as, for example authorisation, licensing, qualification or on characteristics or related production

methods, presentation or use of a product;

(d) “Joint Committee” means the committee formed by the Parties pursuant to Article 1.

(e) “License” means any license, permit, grant, approval, registration, charter, statutory exemption or other form of government permission or approval required for a person to engage in a regulated activity;

(f) “Regulation” means:

(i) in the case of the European Union:

(A) Directives;

(B) Regulations; and

(C) any delegated directives, regulations, regulatory technical standards, implementing technical standards, orders or guidance promulgated under either of the foregoing;

(ii) in the case of the United Kingdom:

(A) Acts of Parliament;

(B) Statutory instruments; and

(C) any rules, regulations, codes, orders, requirements or guidance promulgated under either of the foregoing, including any rules, guidance, examples, practice documents and handbooks of regulators including the Financial Conduct Authority, Prudential Regulation Authority, Competition and Markets Authority and Bank of England;

(g) “Regulatory Agency” means a governmental department or commission of a Party that engages in any Covered Action.

2. General Provisions

2.1. For the purposes of this Chapter, regulatory coherence refers to the use of good regulatory practices in the process of planning, designing, issuing, implementing and reviewing legal and regulatory measures in order to facilitate achievement of domestic policy objectives, and in efforts by the Parties to enhance regulatory cooperation and to minimise regulatory divergence provided that the ultimate goal is to promote international trade and investment, markets characterised by competition, economic growth and employment.

2.2. The Parties affirm the importance of:

(a) sustaining and enhancing the benefits of this Agreement through regulatory coherence in terms of facilitating increased trade in goods and services and increased investment between the Parties;

(b) promoting an effective, pro-competitive regulatory environment which is transparent for citizens and economic operators;

(c) furthering the development of international instruments, and their timely implementation and application, as a means to work together more effectively with each other and with third countries to strive towards consistent regulatory outcomes;

(d) aligning with international standards (including, without limitation, those developed by the International Organization of Securities Commissions, the Financial Stability Board, the Basel Committee on Banking Supervision and the Financial Action Task Force) and conforming with related international obligations;

(e) each Party's sovereign right to identify its regulatory priorities and establish and implement legal and regulatory measures to address these priorities, at the levels that the Party considers appropriate;

(f) the role that law and regulation plays in achieving public policy objectives;

(g) taking into account input from interested persons in the development of legal and regulatory measures;

(h) developing legal and regulatory cooperation and capacity building between the Parties; and

(i) developing mechanisms to ensure that unnecessarily burdensome, duplicative or divergent regulatory requirements do not emerge over time, consistent with the Parties' efforts to stimulate economic growth and jobs, and with their commitments to protect the environment, consumer welfare, innovation, working conditions, human, animal and plant health, and other prudential objectives.

2.3. The Parties affirm their shared commitment to good regulatory principles and practices, as laid down in the OECD Recommendation of 22 March 2012 on Regulatory Policy and Governance, and the OECD Competition Assessment Toolkit, based on the OECD Recommendation of 22 October 2009.

3. Establishment of Joint Committee

3.1. The Parties have agreed to establish a joint committee for the purposes of assisting and monitoring the regulatory coherence relationship established under this Chapter (the "Joint Committee").

3.2. The Joint Committee's roles shall consist of:

(a) [•];

3.3. The Joint Committee shall consist of [3] permanent members appointed by the United Kingdom and [3] permanent members appointed by the European Union.

3.4. The Joint Committee's permanent members shall elect a seventh member to carry out the functions of the chairperson of the Joint Committee, at its first meeting by mutual consent of the permanent members, and

thereafter in accordance with any relevant internal procedures established by the Joint Committee.

3.5. The Joint Committee shall conduct itself by majority vote, and in the event of a tied vote, the chairperson shall cast the final binding vote.

3.6. The Joint Committee shall adopt its internal procedures initially by mutual consent of the permanent members, and subsequently in accordance with Article 1.1

3.7. The Joint Committee's chairperson, permanent members and any other ancillary staff shall be chosen on the basis of appropriate technical or regulatory expertise, practice or other relevant experience.

3.8. The Joint Committee shall meet [at least every [•]] / [in accordance with its established procedures, as necessary] to carry out its duties.

3.9. The Joint Committee shall be able to request specialist technical, legal or other advice and employ ancillary additional staff if it considers necessary.

3.10. The costs of the Joint Committee shall be shared equally by the Parties.

4. Scope of Covered Action

Each Party shall promptly, and no later than one year after the date of entry into force of this Agreement, determine and make publicly available the scope of its Covered Actions. In determining the scope of its Covered Actions, each Party should aim to achieve significant coverage.

5. Coordination and Review Processes

5.1. The Parties recognise that regulatory coherence can be facilitated through domestic mechanisms that increase inter-agency consultation and coordination associated with processes for developing regulatory measures. Accordingly, each Party shall endeavour to ensure that it has processes or mechanisms to facilitate the effective inter-agency coordination and review of proposed Covered Actions. Each Party should

consider establishing and maintaining a central coordinating body for this purpose.

5.2. The Parties recognise that while the processes or mechanisms referred to in Article 1.1 may vary between the Parties depending on their respective circumstances (including differences in levels of development and political and institutional structures), they should generally have as overarching characteristics the ability to:

(a) review proposed Covered Actions to determine the extent to which the development of such measures adheres to good regulatory practices, which may include but are not limited to those set out in Article 17 (Implementation of Core Good Regulatory Practices), and make recommendations based on that review;

(b) strengthen consultation and coordination among domestic agencies so as to identify potential overlap and duplication and to prevent the creation of inconsistent requirements across agencies;

(c) make recommendations for systemic regulatory improvements; and

(d) publicly report on regulatory measures reviewed, any proposals for systemic regulatory improvements, and any updates on changes to the processes and mechanisms referred to in Article 1.1.

5.3. Each Party should generally produce documents that include descriptions of those processes or mechanisms and that can be made available to the public.

6. Legitimate Regulatory Objectives

6.1. The Parties will promulgate regulation which is the least trade restrictive, and anticompetitive consistent with a legitimate, publicly stated regulatory goal.

6.2. A legitimate regulatory goal means a regulatory goal that is either prudential, protective of animal, plant or human health, or to protect national security.

6.3. Legitimate regulatory goals cannot be so detailed, prescriptive or specific as to require a specific regulatory solution, and cannot be to ban products, or prescribe a particular technological process without an adequate explanation as to why it is necessary for the ban to have such broad coverage.

7. Trade Effects

When developing a Regulation, a Regulatory Agency of a Party shall give notice to, give opportunity for submissions by and consider any information provided in comments by, the other Party or a Regulatory Agency of the other Party [or private party established in or authorised by the Other Party that would be affected by such a Regulation] regarding the potential trade effects of the Regulation that it receives during the comment period and provide its views on substantive issues raised.

8. Competitive Effects

8.1. When developing a Regulation, a Regulatory Agency of a Party shall give notice to, and give opportunity for submissions by and consider any information provided in comments by the other Party or a Regulatory Agency of the other Party [or private party established in or authorised by the Other Party that would be affected by such a Regulation] regarding the potential competitive effects of the Regulation that it receives during the comment period and provide its views on substantive issues raised.

8.2. The Party's Competition Agency shall be given notice, at the earliest practicable stage in the regulatory promulgation process of the competitive effect of Regulations.

8.3. The Party shall ensure the relevant national regulator makes itself available to the Competition Agency, as well as making sure that any data, studies, market surveys or other preparatory work is shared with the Competition Agency in as expeditious a manner as possible.

8.4. In making its decisions, the Parties agree that the Competition Agency will utilise the following methodology:

(a) The analysis must take into account the issues addressed in Article 1.1.

(b) Such analysis must include:

- (i) a treatment on the impact on related industries, consumers and competitiveness, including whether the Covered Action will erect entry barriers that might reduce innovation by impeding new entrants into the market; and
- (ii) whether the Covered Action has any other effects on competition.

9. Statement of Cost-Benefit Methodology

9.1. The Parties agree that a Regulatory Agency proposing a Covered Action will produce a statement of cost-benefit methodology to describe the methodology employed by the Regulatory Agency, including a description of its assumptions in calculating a base-line scenario (the scenario without the Covered Action) and the policy scenario (the scenario with the Covered Action).

9.2. The statement shall include the results of the analysis using the cost-benefit methodology, including separate and itemised lists of the costs and benefits identified, as well as descriptions of costs and benefits that cannot be monetised.

9.3. If a Regulatory Agency proceeds to engage in a Covered Action even though the analysis using the cost-benefit methodology shows that the costs outweigh the benefits, that Party must include reasons why it is overriding the analysis either in the original statement or in a subsequent statement referring to the original statement.

9.4. In cases where the governing statutes or other authorities would expressly prohibit the use of the cost-benefit methodology or any other form of cost-benefit analysis or impact analysis or any aspect hereof in respect of a Covered Action, the Regulatory Agency engaging in the Covered Action shall include in its statement an explanation of why it is unable to perform a cost-benefit analysis (or ignore the result) as otherwise required by this Chapter.

10. Access to Government Documents

10.1. Each Party shall make publicly available the following:

(a) a description of each of its Regulatory Agencies' functions and organisation, including the appropriate offices, through which the public can obtain information, make submissions or requests, or obtain submissions; and

(b) any rules of procedure or forms utilised or promulgated by any of its Regulatory Agencies as well as any associated fees.

10.2. Each Party shall adopt or maintain laws or procedures that allow for persons to request access to documents from a Regulatory Agency of a Party. Such laws or procedures that allow for persons to request access to documents from a Regulatory Agency of a Party shall provide no less favourable treatment to persons of the other Party than it provides to persons of the Party.

11. Description of Regulatory Processes

Each Party shall make publicly available a detailed description of the processes and mechanisms employed by its regulatory agencies to develop Regulations. The description shall identify:

(a) the applicable guidelines or rules for providing the public with opportunities to participate in the development of Regulations;

(b) the procedures for ensuring that regulatory agencies have considered public input;

(c) the judicial or administrative procedures available to challenge Regulations or the procedures by which they were developed; and

(d) the processes or mechanisms referred to in Article 1.

12. Regulatory Collection

12.1. Each Party shall ensure that all of its Regulations that are currently in effect are published in a designated collection. The collection shall be

organised logically to promote easy access to relevant Regulations. To that end, the collection should be clearly organised by topic.

12.2. Each Party shall make its respective collection of Regulations available on a single, freely accessible public internet website that is capable of performing searches for Regulations by citation or by word search.

12.3. Each Party shall make sure that its collection is updated when Regulations are amended, repealed or replaced.

13. Decision-Making Based on Evidence

13.1. Each Party recognises the need for Regulations to be based upon information that is reliable and of high quality. To that end, each Party should adopt or maintain publicly available guidance or mechanisms that encourage a Regulatory Agency when it is developing a Regulation to:

(a) seek the best reasonably obtainable information, including scientific, economic, technical, or other information relevant to the Regulation it is developing; and

(b) rely on information that is of high quality (including with respect to utility, objectivity, integrity, clarity and accuracy).

13.2. When publishing any final administrative decision with respect to a Regulation, the Party shall make publicly available an explanation of:

(a) the Regulation, including its policy objectives, how the Regulation achieves those objectives, and the rationale for and an explanation of the material features of the Regulation; and

(b) the relationship between the Regulation and the key evidence, data, cost-benefit analysis and other information the Regulatory Agency considered in preparing the final administrative decision.

Such explanation should also identify any major alternatives that the Regulatory Agency considered in developing the Regulation and provide an explanation supporting the alternative that is selected for the final administrative decision.

13.3. Each Party shall prepare, on an annual basis, a public report setting forth:

- (a) an estimate, to the extent feasible, regarding the total annual costs and benefits of major final Regulations issued in that period by its respective regulatory agencies;
- (b) any proposals for systemic regulatory improvements; and
- (c) any updates on changes to relevant processes and mechanisms.

14. Petitions

Each Party shall provide for any interested person to petition any Regulatory Agency of the Party for the issuance, amendment, or repeal of a Regulation. The basis for such petition may include, for example, that in the view of the person submitting the petition, the Regulation has become more burdensome, trade restrictive or damaging to competition than necessary to achieve its objective, as well as technical or legal commentary. For the purposes of this Article, an “interested person” means any person in the jurisdiction of either of the Parties who is directly or indirectly affected by a Regulation.

15. Retrospective Review of Regulation and Management of Differences

15.1. Each Party shall maintain procedures or mechanisms to promote periodic reviews of Regulations that are in effect in order to determine whether they are in need of revision or repeal, including on a Regulatory Agency’s own initiative or in response to a petition filed pursuant to Article 1.

15.2. Each Party shall make publicly available the results of any such retrospective reviews or analyses conducted by its regulatory agencies, including any supporting data whenever practicable.

15.3. Each Party shall include in procedures or mechanisms adopted pursuant to Article 1.1 provisions addressing Regulations that it considers to have a significant impact on a substantial number of small entities.

15.4. Acknowledging that on the effective date of this Agreement, both Parties' regulatory systems are closely aligned and subject to either harmonisation or mutual recognition, the Parties agree to recognise each other's laws and regulations in respect of goods and will accept certification of conformity to applicable laws and regulations by duly authorised conformity assessment bodies of the other Party to the fullest extent allowable by law

15.5. Each Party agrees that it will not withdraw this recognition provided that the other Party has adhered to the provisions of this Chapter, and the respective laws and regulations of each Party in the relevant field achieve the respective policy objectives.

15.6. The Parties agree that it is the intention of the Parties to include detailed agreements in the following sectors [sectoral annexes]

15.7. Any disputes concerning this will be submitted to the Joint Committee for resolution in the manner described in this Chapter. [Linked to Dispute Settlement Mechanism].

16. Reducing Information Collection Burdens Associated with Regulation

Each Party shall provide that, to the extent regulatory agencies use surveys to request or compel information from the public in developing a Regulation, these regulatory agencies should endeavour to do so in a manner that minimises unnecessary burdens and avoids duplication.

17. Implementation of Core Good Regulatory Practices

17.1. The Parties agree that the optimal way of avoiding unnecessary differences in laws and regulations is to agree similar core good regulatory practices.

17.2. The Parties agree that in achieving the legitimate and publicly stated goal(s) of any Covered Action, Covered Action taken or to be taken by a Party to achieve such goal(s) should be the least anti-competitive and least restrictive on trade while being consistent with the relevant objective(s) for the Covered Action.

17.3. To assist in designing a measure to best achieve the Party's objectives, each Party should generally encourage relevant regulatory agencies, consistent with its laws and regulations, to conduct regulatory impact assessments when developing proposed Covered Actions that exceed a threshold of economic impact, or other regulatory impact, where appropriate, as established by the Party. Regulatory impact assessments may encompass a range of procedures to determine possible impacts.

17.4. Regulatory impact assessments conducted by a Party should, among other things:

(a) assess the need for a regulatory proposal, including a description of the nature and significance of the problem;

(b) examine feasible alternatives, including, to the extent feasible and consistent with laws and regulations, their costs and benefits, such as damage to international trade or to competition, recognising that some costs and benefits are difficult to quantify and monetise;

(c) when highlighting the costs and benefits of new laws and regulations, the Parties agree to separate the costs analysis from the benefits analysis, in particular recognising that benefits are often difficult to quantify and monetise, but the costs side can be more objectively analysed if it is limited to business compliance costs, impact on international trade, and impact on competition;

(d) explain the grounds for concluding that the selected alternative achieves the policy objectives in an efficient manner, including, if appropriate, reference to the costs and benefits and the potential for managing risks; and

(e) rely on the best reasonably obtainable existing information including relevant scientific, technical, economic or other information, within the boundaries of the authorities, mandates and resources of the particular Regulatory Agency.

17.5 When conducting regulatory impact assessments, a Party may take into consideration the potential impact of the proposed Regulation on SMEs, and shall apply principles of proportionality in determining the level of regulation required.

17.6 Each Party should ensure that new Covered Actions are plainly written and are clear, concise, well organised and easy to understand, recognising that some measures address technical issues and that relevant expertise may be needed to understand and apply them.

17.7 A Regulatory Agency of either Party, when considering a Covered Action, shall propose such Covered Action to the public and will provide for a public notice-and-comment period. This notice and comment period shall be of reasonable duration, having regard to the nature, scope and complexity of the Covered Action. The Notice shall include a statement of cost benefit analysis as expressed in Article 1. This publication requirement shall apply to all statements of policy and all interpretations issued by a Regulatory Agency in its official capacity that are not solely internal and related to the internal management structure of the Regulatory Agency.

17.8 The Parties agree that Regulatory Agency decisions on License applications will be made in a reasonable period of time. Apart from voluntary or requested Licence cancellations, suspensions or modifications, a Regulatory Agency may not revoke or modify Licenses without prior written notice, and it must afford the affected person a reasonable opportunity to demonstrate compliance with the law. Parties must provide written reasons for license rejections or modifications. Parties may not revoke or modify licenses without prior written notice, and must afford the affected person a reasonable opportunity to demonstrate compliance with the law.

17.9 Subject to its laws and regulations, each Party should ensure that relevant Regulatory Agencies provide public access to information on new Covered Actions and, where practicable, make this information available online.

17.10 If a Party submits a request for information to a Regulatory Agency of the other Party, the Regulatory Agency of the responding Party should, in a manner it deems appropriate, and consistent with its Regulations, provide

the requesting Party with notice of any Covered Action that it reasonably expects to issue within the following 12-month period from the date that the request made by the requesting Party is received.

17.11. To the extent appropriate and consistent with its law, each Party should encourage its relevant Regulatory Agencies to consider Regulations of the other Party, as well as relevant developments in international, regional and other fora when planning Covered Actions.

18. Cooperation

18.1. The Parties shall cooperate in order to facilitate the implementation of this Chapter and to maximise the benefits arising from it. Cooperation activities shall take into consideration each Party's needs, and may include:

- (a) information exchanges, dialogues or meetings with the other Party;
- (b) information exchanges, dialogues or meetings with interested persons, including with SMEs, of the other Party;
- (c) strengthening cooperation and other relevant activities between regulatory agencies; and
- (d) other activities that the Parties may agree.

18.2. The Parties further recognise that cooperation between Parties on regulatory matters can be enhanced through, among other things, ensuring that each Party's Regulations are centrally available.

19. Notification of Implementation

19.1. For the purposes of transparency, and to serve as a basis for cooperation and capacity building activities under this Chapter, each Party shall submit a notification of implementation to the Joint Committee through the contact points designated pursuant to Article 1. (Contact Points) within two years of the date of entry into force of this Agreement and at least once every four years thereafter.

19.2. In its initial notification, each Party shall describe the steps that it has taken since the date of entry into force of this Agreement, and the steps that it plans to take to implement this Chapter, including those to:

(a) establish processes or mechanisms to facilitate effective inter-agency coordination and review of proposed Covered Actions in accordance with Article 1 (Coordination and Review Processes);

(b) encourage relevant regulatory agencies to conduct regulatory impact assessments in accordance with Article 1 (Implementation of Core Good Regulatory Practices);

(c) ensure that Covered Actions are written and made available in accordance with Article 1 (Implementation of Core Good Regulatory Practices);

(d) review its Covered Actions in accordance with Article 1 (Implementation of Core Good Regulatory Practices); and

(e) provide information to the public in its annual notice of prospective Covered Actions in accordance with Article 1 (Implementation of Core Good Regulatory Practices).

19.3. In subsequent notifications, each Party shall describe the steps, including those set out in Article 1.1, that it has taken since the previous notification, and those that it plans to take to implement this Chapter, and to improve its adherence to it.

19.4. In its consideration of issues associated with the implementation and operation of this Chapter, the Joint Committee may review notifications made by a Party pursuant to Article 1.1. During that review, Parties may ask questions or discuss specific aspects of that Party's notification. The Joint Committee may use its review and discussion of a notification as a basis for identifying opportunities for assistance and cooperative activities to provide assistance in accordance with Article 1 (Cooperation).

20. Relation to Other Chapters

In the event of any inconsistency between this Chapter and another

Chapter of this Agreement, this Chapter shall prevail to the extent of the inconsistency, except where there is a sectoral annex for specific services areas in which case that sectoral annex shall apply.

21. Non-Application of Dispute Settlement

No Party shall have recourse to dispute settlement under Chapter [•] (Dispute Settlement) for any matter arising under this Chapter. Instead, the specific dispute settlement provisions of this chapter [and its sectoral annexes] shall apply.

22. Dispute Settlement Mechanism

22.1. If one Party withdraws recognition from the other, and the other Party considers there to have been a violation of the agreement, it shall bring a complaint to the Joint Committee.

22.2. If a Party considers that a valid petition has been made under Article 1 and believes that this petition has not been validly dealt with by the other Party, the other Party shall bring a Complaint to the Joint Committee.

22.3. The Joint Committee shall conduct a consultation mechanism for 30 days, and if the Parties have not resolved the issue the complaining Party can suspend concessions made under this [Chapter] [Agreement] [or impose fines].

23. Contact Points

23.1. The contact points for each Party in relation to submissions to the Committee under this Chapter shall be as follows:

(a) For the United Kingdom: [•]; and

(b) For the European Union: [•].

The Institute of Economic Affairs
2 Lord North Street
London SW1P 3LB
Tel 020 7799 8900
Email iea@iea.org.uk


Institute of
Economic Affairs