

# Connecting our Econ Teams

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**Attachments** Ciuriak et al. Brexit Trade Impacts Alternative Scenarios (2017).pdf (916.83 kB); CRS : US UK FTA.PDF (916.46 kB); Singham Hewson and Tylecote 2017.pdf (4.24 MB)

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Richard/Catherine – Nice talking with you and your colleagues this afternoon (EST). (b) (1) (A), (b) (1) (B)

Attached are the academic studies we have found thus far on a U.S.-UK FTA, as well as a link below to an ITC analysis from 2000 looking at the UK joining NAFTA.

<https://www.usitc.gov/publications/332/pub3339.pdf>

Let us know if you have any questions.

Best,

Bill

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# Brexit Trade Impacts: Alternative Scenarios

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**Abstract:** This note develops four alternative estimates of the trade-related impacts of the United Kingdom seceding from the European Union. We contrast two basic scenarios: an exit that re-sets the UK's relationship with the rest of the EU to a WTO-rules most favoured nation basis ("Brexit"), versus a negotiated change in the UK's status that largely preserves the UK's integration with the rest of the EU at a level similar to that of the European Free Trade Association ("Brefta"). A third scenario introduces a "single market" effect that reflects EU27 "home bias" (EU27 preference for EU27 products). A fourth scenario introduces a UK-US free trade agreement in a context in which the TTIP not going ahead due to the widening gulf between EU and US positions on social and environmental issues under the Trump Administration.

**Keywords:** United Kingdom, European Union, Brexit, Brefta, TTIP, single market, exit, CGE

**JEL Codes:** F13, F14



# 1. Introduction

The United Kingdom's withdrawal from the European Union was set in motion by the triggering of Article 50 by UK Prime Minister Theresa May on 29 March 2017, setting the clock ticking towards a formal UK exit in 2019. The terms of exit are very much up in the air. Both sides have indicated they are seeking a mutually beneficial economic partnership, with the rights of EU citizens living in Britain protected and vice versa, and soft land borders in contiguous regions. The latter include the border between Northern Ireland and the Republic of Ireland, between Gibraltar and Spain (and possibly between Scotland and England if the Brexit shoe falls pursuant to a referendum that Scottish First Minister Nicola Sturgeon says will be held once the terms of Brexit become clear).

In this study, we evaluate the trade-related impacts of an exit by the UK from the EU under alternative scenarios regarding what would replace the current single-market relationship, and weigh the costs against the potential benefits available to the UK from obtaining a free trade agreement with the United States in a context where the Transatlantic Trade and Investment Partnership (TTIP) does not go ahead due to the widening gulf between EU and US positions on social and environmental issues.

We consider two basic alternative exit outcomes: one that resets UK relations with the remaining 27 members ("EU27") on a default World Trade Organization (WTO)-rules basis ("Brexit") and a negotiated exit, which preserves a level of integration equivalent to that under the EU's arrangements with the European Free Trade Association (EFTA) (i.e., a "Brefta"). These scenarios build on the Ciuriak et al. (2015) study for Open Europe, and take into account the impact of Brexit on uncertainty of services market access, following Lysenko and Ciuriak (2016), who develop composite non-tariff barrier estimates for services market access that reflect changes to both applied measures and changes to the gap between applied and bound positions under the General Agreement on Trade in Services (GATS) – i.e., "water in the GATS" (Miroudot and Pertel, 2015). Under the Brefta scenario, this "unbinding" effect of a Brexit is not present.

A third scenario introduces a "single market" effect that takes into account EU27 preference for EU27 products. As a consequence of modelling Brexit and Brefta with the EU27 disaggregated, trade between the EU27 regions substitutes against third party trade at the higher Armington elasticity in the Global Trade Analysis Project (GTAP) database, which does not capture any "home bias" within the EU27 for production in other EU Member States based on, for example, confidence in the EU regulatory framework. By aggregating the EU27 into one region and assigning all intra-EU27 trade to domestic sales, we mimic an effect where there is home bias within the EU27.

Finally, a fourth scenario introduces a UK free trade agreement with the United States in the context of the TTIP not going ahead. This reflects the emerging political economy of trans-Atlantic trade relations where US policy under the Trump Administration is diverging sharply from positions that would be tenable for the EU, but which the UK might accept to offset the trade losses implied by Brexit.

We consider the following factors in the quantification of the impacts of the Brexit and Brefta scenarios:

- The emergence of a tariff wall between the UK and the EU27 under Brexit;
- The emergence of a new hard border for trade between the UK and the EU27, under alternative assumptions concerning the nature of that border under Brexit versus under Brefta;
- The introduction of new administrative requirements to track rules of origin (ROOs) for purposes of UK-EU27 trade under a preferential trade agreement in the Brefta scenario;
- The emergence of new non-tariff barriers (NTBs) to goods trade, reflecting the "drift" of UK regulations away from the EU's absent the requirement to implement Commission directives; and

- The emergence of new barriers to cross-border services trade and foreign direct investment (FDI), under alternative assumptions concerning the terms of the UK's exit from the single market; in the Brexit scenarios, this includes the removal of the binding effect EU policies on UK policies relative to WTO commitments.

The major caveats concern the many factors that cannot be quantified in the current analytical setting:

- The one-time costs of establishing the new border between the UK and the EU27, including potentially the construction of a customs border between Northern Ireland and the Republic of Ireland, between Gibraltar and Spain (and possibly between Scotland and England in a post-Scexit scenario, although the early discussion of new hard borders indicates all efforts would be made to avoid these.
- The implications for cross-channel value chains – particularly in cases where UK suppliers provide a relatively small share of the overall value-added in EU27 products (and vice versa), given that the value-added content in bilateral exports would bear the full weight of the additional border costs;
- Sector-specific impacts, in particular the City of London's access to EU27 internal financial market transactions, and UK-based air carriers' ability to offer intra-EU flight services;
- Interim frictions for the UK firms in terms of access to international certification which currently runs through EU participation in international agreements.
- The extent to which (and with what effect) exit from the single market would open domestic economic policy options to the UK (and to the EU27) that are not available to either under the single market;
- The economic implications of the cessation of UK net contributions to the EU budget and of EU funding of activities in the UK;
- The implications for multinational firms' investment decisions due to the new uncertainty about future market access in bilateral UK-EU27 trade (e.g., a range of contingent-protection measures would be deployable in bilateral UK-EU27 trade outside the single market framework, including anti-dumping and countervailing duties and border carbon offsets for climate change-related measures);
- Labour market effects such as skill mis-matches due to reduced labour movement (press reports indicate that employers in the UK are facing difficulty in filling vacancies after a drop for more in the number of available candidates; Allen, 2017).
- The impact of financial market reactions on the dynamic path that the UK and EU27 would take to reach the new equilibrium implied by the policy changes under UK withdrawal;
- The implications for investment decisions (including both of establishing commercial presence and incurring sunk costs to establish an export market presence) of UK withdrawal from the EU single market and institutions on the parties' political risk profile; and
- The economic consequences of possible knock-on political contingencies, including Scotland seceding from the UK in order to remain within the single market or Ireland withdrawing from the single market to avoid the costs of a hard border with Northern Ireland, etc.

This note is organized as follows. Section 2 sets out the empirical approach to generating the quantitative assessments in the present study. Section 3 sets out the results of the simulations. Section 4 concludes. Annex 1 describes the construction of the various policy shocks and the supporting evidence for the assumptions made.

## 2. Empirical Approach

### 2.1. Model

We use a recursive dynamic version of the GTAP computable general equilibrium (CGE) model that incorporates FDI by building in a foreign-invested representative firm in each GTAP region-sector, as described in Ciuriak and Xiao (2014) with an extension to the goods sector. In our model, labour responds to changes in the wage rate with a long-run elasticity of unity and capital supply responds to changes in the rate of return on capital; the investment response is based on the Monash capital model (Dixon and Rimmer, 1998).

Labour and capital are mobile across all sectors within a country. Capital is also mobile internationally in our model, which incorporates a foreign-owned representative firm in each GTAP sector; FDI flows respond to changes in restrictions on FDI, which are modelled as “phantom taxes” that influence behaviour, but do not generate government tax revenue. Labour is not, however, mobile internationally and we cannot directly take into account Brexit-induced changes to the labour supply through existing mechanisms in the model.

### 2.2. Implementation

We use the 57-product group level of disaggregation permitted by the GTAP database and a regional aggregation featuring 28 economies, including, inter alia, the UK and 16 EU27 countries/regions. We aggregate several of the smaller EU economies into groups: Bellux (Belgium and Luxembourg), Baltics (Estonia, Latvia, and Lithuania), Iberia (Spain and Portugal), Adriatics (Croatia and Slovenia), Central and Eastern European Countries or CEECs (Bulgaria, Czech Republic, Hungary, Romania, and Slovakia), and Mediterraneans (Cyprus, Greece, and Malta). Other economies represented include the non-EU G8 economies and China.

To simulate our various scenarios, we first develop a simulation of the GTAP database to 2030, using GTAP dynamic database tools, which draw on available macroeconomic data (Fouré et al., 2012). According to this macroeconomic projection for the world economy, global growth averages about 3.06% per annum over the period 2016-2030. The UK grows at 2.12% over this period, the EU27 by 1.56%, and the US by 1.53%. China’s growth slows to 5.38% over this period; accordingly, it is a fairly conservative view of global growth prospects.

For convenience, we assume the UK’s exit occurs as of 1 January 2020. For convenience in comparing options, we adopt the same date for the hard Brexit and the soft Brefta exits, and for the UK’s independent entry into a TTIP-type FTA with the US. The individual elements of the shocks are simulated sequentially in order to show the relative contributions of each element.

### 2.3. Model Closures

For microeconomic closures, modellers have an option of fixing the quantity of labour and capital available for production and allowing wages and returns to capital to adjust; or fixing the returns to capital or to labour and allowing the quantity of the production factors to adjust. Each of these closure rules makes an extreme assumption about the supply of labour and/or capital: it is either perfectly elastic or perfectly inelastic. The reality is likely to be somewhere in between. In the GTAP-FDI model, investment adjusts to changes in the rate of return; similarly, we allow labour supply to adjust to changes in wages. As a result, the policy shocks that we simulate generate “endowment” effects: that is, the amount of labour and capital in an economy changes based on changes in returns to labour and capital.

As regards macroeconomic closures, two approaches are available. First, the current account can be fixed. This assumes that the external balance is determined entirely by domestic investment-savings dynamics. When trade policy shocks result in unbalanced changes in imports and exports, the original trade balance is restored by implicit

exchange rate adjustments. Alternatively, the current account can be allowed to adjust to the trade shock. The change in the current account then must be offset by equivalent changes in capital flows. In reality, unbalanced trade impacts are likely to have both effects: induce subsequent exchange rate adjustments and offset capital flows. Given the active role of FDI in our model, we necessarily adopt the closure where the current account adjusts.

## 2.4. Scenario Design

We focus on changes to the bilateral UK-EU27 trade regime. However, Brexit affects trade relationships with third parties. We assume that the UK and EU27 maintain EU28 WTO and existing FTA commitments vis-à-vis third parties. This limits the impacts to those that arise from changes to bilateral UK-EU27 trade. This outcome could be achieved by all parties agreeing to maintain status-quo market access on a provisional basis, pending formal restructuring of the EU28 commitments into separate UK and EU27 commitments. This obviously slides over some potentially thorny issues such as access to quotas.

Honouring outstanding commitments by third parties includes continuing to allow cross-cumulation of UK and EU27 value-added for access to preferences available to UK and EU27 exporters under the rules of origin (ROOs) in the EU's existing FTAs. There are precedents for this – for example, the Euro-Med origin regime allows for cumulation with two or more free trade partners of the EU, provided that they have concluded FTAs with one another and apply the Euro-Med origin protocol. There are additional costs: in addition to the existing proofs of origin (MC EUR.1 and invoice declaration), in certain cases, additional certification is required. The need for such cross-cumulation when FTAs are struck with partners that have deep integration with third parties (e.g., Canada and the United States) has been recognized in EU negotiations of trans-Atlantic agreements – e.g., the ROOs derogations under the Canada-EU Comprehensive Economic and Trade Partnership (CETA) for the auto sector, which contemplate allowing auto parts originating in the United States to count as originating for a vehicle produced in the EU or in Canada. Again, the assumption that suitable regimes would be put in place seamlessly slides over a potentially complex and thorny set of issues (consider for example areas where ROOs are typically restrictive such as the EU's “fabric forward” rules for apparel trade).

A ROOs issue would also arise under the WTO's General System of Preferences (GSP): currently, the bilateral cumulation provisions under the EU's GSP regime provide for diagonal cumulation, under which UK content exported for processing to some 150 developing countries is eligible for GSP preferences when these goods are exported back to other EU Member States (and vice versa). Under the EU's post-Cotonou Economic Partnership Agreements (EPAs) with African, Caribbean, and Pacific (ACP) countries, diagonal cumulation could continue under regionalized ROOs. We assume such a device would be used to cover this to avoid additional tightening of market access for ACP countries to both the EU27 and UK markets. In simulations not reported here, we estimate that abrogation of the UK's FTAs with third parties upon a hard Brexit would result in a significant negative impact on the UK of about -0.2% in terms of lowered real GDP and a welfare reduction of about USD 6.5 billion.

We also do not factor in the one-time costs of erecting a customs border control between Ireland and Northern Ireland, nor the one-time administrative costs on British and EU27 firms. For example, VAT would no longer be charged on UK-EU27 shipments, so firms would have to put in place the paperwork to modify their VAT collection and reporting systems. Membership of UK firms in EU internal organizations would lapse, requiring repatriation of representatives, etc. Websites, letterheads, advertising, etc. would all have to be modified. We could not find a basis to calibrate these latter costs and so do not include them, although they are likely to be non-negligible when cumulated across businesses.<sup>1</sup>

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<sup>1</sup> For example, a study conducted by the Centre for International Economics Canberra & Sydney (2008) estimated that the cost of one-off label changes was around 1.1% of product costs.

Finally, one issue which is important for cross-border flows which we do not incorporate is the cessation of the net fiscal transfer from the UK to the EU27. For the EU28, the welfare calculation of the cessation of the transfer would be essentially neutral, as the EU27 would suffer a net loss equivalent to the UK's net gain. The extent of the impact on the EU27 and the UK depends on the basis of measurement.<sup>2</sup>

### 2.4.1. Brexit

The Brexit scenario incorporates the following effects:

- UK-EU27 trade shifts to an MFN tariff basis. We build an MFN tariff wall between the UK and the EU27. The construction of the Brexit tariff shock is described in the Technical Annex.
- Brexit would raise issues regarding the managed agricultural trade regime under the EU's Common Agricultural Policy (CAP). Over the years and the course of numerous General Agreement on Tariffs and Trade (GATT)/WTO negotiations, the EU has accommodated the agricultural export interests of third parties with tariff rate quotas on sensitive products. But no such agreements have been put in place for UK exports to the EU27 – or, conversely, for EU27 exporters in the UK. Following Ciuriak et al. (2015), where a move to MFN tariffs would shut down trade entirely in some agricultural sectors, we assume that the UK and the EU27 pragmatically limit the increase in bilateral protection to enable market access at levels between the EU and the United States.
- We introduce customs clearance costs for UK-EU27 trade. These are based on estimates drawn from the literature on the increased time costs for customs clearance and additional paperwork.
- We assume that UK economic regulation would be identical to EU27 regulation out of the exit gate. Nonetheless, NTBs would gradually emerge as UK and EU27 rules drift apart under independent reforms and differing legal determinations by their respective courts. We phase in NTB costs equivalent to those faced by EU firms in Canada, which we consider to be a good proxy for a liberal, efficient trade environment tailored for access to both EU and US markets.
- We evaluate the Brexit shock based on changes to the UK and EU27 scores on the OECD's Services Trade Restrictiveness Index (STRI) and Foreign Direct Investment Restrictiveness (FDIR) index. Since the OECD has not calculated the level of intra-EU STRI and FDIR values, we estimate Community internal standards as equivalent to the least restrictive regime maintained by any EU Member State. Further, we assume that the EU membership effectively binds such market access at the applied level, meaning there was no "water" in the bilateral services and investment market access commitments under the EU single market. Brexit will not only revert applied practice to the EU's MFN applied level, but will also remove the certainty of market access generated by EU membership as the EU and UK would be free to revert to bound levels of market access. We incorporate estimates of the effective trade costs of higher uncertainty from the creation of water in the EU27 and UK services commitments. The construction of the new

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<sup>2</sup> There are alternative estimates for the UK fiscal offset. On the basis of the Operating Budgetary Balance, the UK average net contribution over the 2007-2013 budget cycle was GBP 3.8 billion, or 0.25% of UK GDP (see European Commission in the UK, 3 November 2014). The UK government provides a calculation of the net transfer for the same period of GBP 6.66 billion, or 0.44% of UK GDP (HM Treasury, 2013 and 2014, Tables 3.A). Ottaviano et al. (2014) incorporate an offset of 0.53% of GDP, based on the HM Treasury figure for the 2013 outturn. The HM Treasury estimates for the 2014-2019 period, compared to our forward projections of UK GDP, average out at about 0.45% of GDP. Caution should be used in combining such a figure, where the fiscal transfer is expressed as a percent of GDP, with estimated impacts of other policy changes on GDP, as these are not directly comparable calculations. To put the fiscal offset into a directly comparable form, one would have to model the fiscal shock in the UK (in the form of reduced taxes or increased expenditure or some combination of the two) which would have tax and fiscal multiplier effects, as well as the fiscal shock to the EU27 of a similar amount, compounded by corresponding tax and fiscal multipliers. The UK would experience a positive fiscal shock and a negative external demand shock; the effect on UK GDP would be the net of these effects; how close this would be to offset as calculated above is an empirical question not addressed here.

composite non-tariff barrier that integrates the increase in applied market access restrictions and increased uncertainty is described in the Technical Annex.

- Finally, we assume that Mode 4 (commercial presence) services trade is grandfathered for expatriates currently employed, and Brexit only impacts on future workers, or those without jobs. This implies no initial discontinuous rise in labour costs due to labour market disruptions.

#### **2.4.2. Brefta**

This scenario evaluates the less disruptive outcome under a negotiated exit that grandfathers existing bilateral trade positions and erects only the minimum of new barriers implied by the shift from a single market environment to one in which a border re-appears. In particular, NTBs in goods markets do not emerge since we assume an EFTA-type relationship agreement requires the UK to largely implement EU rules and standards. By the same token, the UK shares in future deepening of the EU single market and, thus, does not face the costs of drift hypothesized in Ottaviano et al. (2014) and reflected in the Brexit scenario.

While the Brefta is as close to being inside the single market as can be obtained for a party that does not assume the obligations of the single market, it still might have sufficient impact to disrupt particular sectors such as the City of London. We do not take into account the risk of additional NTBs emerging that might affect the ability of UK firms to access EU services markets on a cross-border basis in specific sectors (e.g., the City of London).

Similarly, we do not take into account the possibility of the unravelling of value chains in which the UK provides a relatively small share of the value added, which would bear the full cost of the additional border frictions as goods enter and exit within the value chain. Finally, introducing ROOs into UK-EU27 trade generates issues with third-party FTAs. We assume these would be managed by regionalizing the respective FTAs by providing for regional cumulation of value added, thus preserving the current EU FTAs undisturbed in this regard.

On this basis, the Brefta features the following shocks:

- While no new tariffs are imposed on UK-EU27 trade, a ROOs compliance cost would emerge. We assume this to be equal to 1% of the value of trade (we effectively assume 100% utilization of the EFTA-type preferences), which is at the bottom end of the range of ROOs cost estimates in the literature, and reflects the likely desire of both parties to implement a low-cost border regime.
- We introduce new border costs. For the Brefta border, we retain the estimates of the administrative costs of the Brexit border, but assume that a negotiated exit would feature a state-of-the-art border in terms of minimizing time costs to minimize the disruption to UK-EU27 bilateral trade. Where the Brexit border resembles the Canada-US border in terms of costs, the Brefta border resembles the EU-Swiss border.
- We assume a modest increase in barriers to cross-border services trade and FDI based on less flexible provisions for movement of personnel. The OECD's STRI, which we use to code the services and FDI shocks, has a line for "other" restrictions related to movement of persons. We shock this element to increase services trade restrictions under a Brefta, with the interpretation that it would reflect measures related to the issue of "benefit tourism", which was a point of friction for the UK.

#### **2.4.3. Brexit with Single Market Effects**

This scenario uses the same shock files and assumptions as the first Brexit scenario but modifies substitution elasticities from CES to CRESH for intra-EU27 trade to capture the effect of the single market in generating home bias in favour of goods subject to full EU regulation and of EU-brand loyalty of EU27 consumers.

#### **2.4.4. UK-US FTA**

One of the issues raised in the Brexit debate concerns the possibility that the UK could pursue a more effective trade policy by negotiating FTAs more quickly and reaching deeper liberalization commitments alone, rather than as part of the EU. We simulate the implications of the UK securing an FTA with the United States while the TTIP lapses due to widening gaps between the EU and US positions on social and environmental issues.



### 3. Results

This section reports the results of the four scenarios described above. We report the impacts for the UK, the EU27 as a whole, the larger individual EU Member States, regional aggregations of the small EU Member States, the US, other major global economies, and the rest of the world. We report the value figures in USD at 2011 prices, the base year for the GTAP 9.0 database. The reported values can be converted to current USD by factoring in the approximately 10% of inflation in the US (as measured by the GDP deflator) between 2011 and 2017. For a European readership, the figures in USD at 2011 prices can be read as equivalent to 2017 EUR (since the 1.10 anticipated USD/EUR exchange rate offsets the approximately 10% inflation in the USD between 2011 and 2017).

#### 3.1. Brexit Impacts

Table 1 summarizes the macroeconomic impacts of the Brexit scenario on the UK, the EU27 and other parties. The EU member states are ranked by % change in real GDP in 2030.

**Table 1: GDP and Welfare Impacts of Brexit, Relative to Baseline, by Region**

	Real GDP (% change)		Welfare (USD billions)	
	2020	2030	2020	2030
<b>EU28</b>	<b>-0.308</b>	<b>-0.649</b>	<b>-78.58</b>	<b>-173.46</b>
<b>UK</b>	<b>-1.349</b>	<b>-2.540</b>	<b>-50.09</b>	<b>-101.63</b>
<b>EU27</b>	<b>-0.126</b>	<b>-0.237</b>	<b>-28.49</b>	<b>-71.83</b>
Ireland	-1.042	-2.760	-3.00	-8.95
Bellux	-0.420	-0.881	-3.90	-7.56
Netherlands	-0.191	-0.388	-2.67	-5.92
Baltics	-0.095	-0.354	-0.23	-0.98
Denmark	-0.159	-0.344	-0.94	-2.07
Mediterranean	-0.129	-0.319	-0.69	-1.91
Iberia	-0.110	-0.251	-3.28	-8.34
Germany	-0.097	-0.253	-4.79	-11.77
Poland	-0.094	-0.236	-1.02	-3.15
CEECs	-0.084	-0.230	-1.07	-3.63
Sweden	-0.121	-0.245	-0.74	-1.95
France	-0.106	-0.210	-4.05	-9.85
Italy	-0.051	-0.146	-1.58	-4.09
Finland	-0.077	-0.157	-0.26	-0.66
Austria	-0.041	-0.118	-0.19	-0.76
Adriatic	-0.054	-0.121	-0.08	-0.23
<b>G8 &amp; China</b>				
Canada	0.010	0.035	0.56	1.86
Japan	0.009	0.036	1.49	4.76
Russia	0.014	0.033	1.27	3.74
USA	0.006	0.023	3.05	8.32
China	0.011	0.027	2.82	15.94
<b>World Total</b>	<b>-0.059</b>	<b>-0.091</b>	<b>-58.75</b>	<b>-90.74</b>

Source: Calculations by the authors.

Exit by the UK from the EU under the Brexit assumptions generates significant negative impacts for the UK, the EU27 and the global economy as a whole:

- UK real GDP declines by -2.54%, and economic welfare declines by just over USD 100 billion in 2030, measured at 2011 prices;
- The decline in real GDP for the EU27 is much smaller at only -0.24%, however, the decline in economic welfare of USD 72 billion is closer to the impact observed for the UK;
- For the EU28, these impacts add up to -0.65% decline in real GDP and just over USD 173 billion reduction in economic welfare;
- For the global economy as a whole, the corresponding figures are -0.09% and USD 91 billion.

There are, however, beneficiaries from Brexit as the erosion of mutual preferences in the UK and EU27 markets provides windfall gains to third parties in terms of market share gains in both the UK and EU27 markets, notwithstanding negative income effects. Brexit also generates relative competitiveness gains for third parties. For the major G8 economies and China, the net effect is positive, both in terms of real GDP and economic welfare. China is the biggest beneficiary in aggregate economic welfare terms, gaining almost USD 16 billion, as it supplants the UK and the EU27 in each of these region's trade. Japan is the biggest beneficiary in terms of real GDP growth. Thus, as the EU27 and UK lose preferences in each other's markets, third parties gain a competitive edge against both.

Within the EU27, the impacts differ based on the intensity of exposure to bilateral trade with the UK. The average real GDP decline across EU27 Member States is -0.44%. Ireland is the biggest loser from a Brexit, as its GDP declines by -2.8% and economic welfare falls by USD 9 billion by 2030. The Bellux group, along with the Netherlands, are the next most affected with real GDP declines of -0.88% and -0.39% respectively. The impact to Ireland and the Bellux group is such that they are the only Member States with above average declines. Excluding these two regions, the average decline in real GDP for the balance of the Member States is about -0.24%, just over half the overall average rate. The least affected are Austria and the Adriatic states (Croatia and Slovenia) with real GDP declines of -0.118, and -0.121 respectively. The Adriatic states also had the smallest decline in economic welfare at USD 0.23 billion. Geography and trade exposure are, thus, key factors in Brexit's impact on the EU27 Member States. By the same token, most EU member states will feel comparatively little pressure to accommodate UK interests in the Brexit negotiations.

The effects build up over time due to two factors: the gradual build-up of NTBs between the UK and the EU27 and the gradual response of investment to the changes in rates of return induced by the Brexit shock. This latter effect reflects the lead-time for investment decisions. On average, the long-run impacts are roughly two and a half times the size of the initial first-year impacts, although the extent of build up varies somewhat across individual regions. In this regard, it is important to distinguish the build-up in the equilibrium impact and short-term dynamics. The initial impact of Brexit could be much greater than portrayed here because of market reactions that are then dampened over time. However, while the market sensitivities are likely to die out over time, the equilibrium impact will continue to build.

While the EU's applied MFN tariffs are generally low, the combination of the insertion of a tariff wall between the UK and the EU27 and the imposition of the new time and out-of-pocket costs of cross-border trade results in a non-negligible impact on bilateral trade, with commensurate consequences for GDP and welfare.

For both the UK and EU27, border costs have the largest impact on GDP followed by tariffs, goods NTBs, services NTBs and lastly FDI NTBs. Border costs also constitute the largest source of changes in real GDP for most other markets, with the exception of Ireland, Bellux, Netherlands, Baltics, Denmark and Japan, for which tariffs have the bigger impact.

As regards impacts on individual third parties, with the exception of FDI NTBs, Ireland's declines in GDP resulting from Brexit's tariffs, border costs and both goods and services NTBs are the largest in the EU27 for each source of impact. Denmark has the largest decline in real GDP attributable to rising NTBs on FDI.

**Table 2: Source of Impacts on Real GDP and Welfare, 2030**

	Tariffs	Border Costs	Goods NTBs	Services NTBs	FDI NTBs	Tariffs	Border Costs	Goods NTBs	Services NTBs	FDI NTBs
	Real GDP (% change)					Welfare (USD billions)				
<b>EU28</b>	<b>-0.223</b>	<b>-0.289</b>	<b>-0.122</b>	<b>-0.011</b>	<b>-0.004</b>	<b>-56.25</b>	<b>-78.85</b>	<b>-34.73</b>	<b>-2.85</b>	<b>-0.79</b>
<b>UK</b>	<b>-0.899</b>	<b>-1.160</b>	<b>-0.437</b>	<b>-0.043</b>	<b>-0.001</b>	<b>-30.09</b>	<b>-49.93</b>	<b>-19.80</b>	<b>-1.80</b>	<b>-0.01</b>
<b>EU27</b>	<b>-0.098</b>	<b>-0.128</b>	<b>-0.064</b>	<b>-0.005</b>	<b>-0.004</b>	<b>-26.15</b>	<b>-28.92</b>	<b>-14.93</b>	<b>-1.05</b>	<b>-0.78</b>
Ireland	-1.071	-1.060	-0.569	-0.058	-0.002	-3.61	-3.34	-1.81	-0.17	-0.01
Bellux	-0.356	-0.329	-0.184	-0.007	-0.004	-3.43	-2.64	-1.41	-0.05	-0.03
Netherlands	-0.163	-0.142	-0.070	-0.012	-0.001	-2.68	-1.90	-1.21	-0.13	-0.01
Baltics	-0.142	-0.140	-0.069	-0.001	-0.002	-0.44	-0.36	-0.18	0.00	0.00
Denmark	-0.121	-0.116	-0.044	-0.008	-0.056	-0.83	-0.63	-0.33	-0.03	-0.25
Mediterranean	-0.079	-0.154	-0.079	-0.007	0.000	-0.50	-0.90	-0.47	-0.05	0.01
Iberia	-0.085	-0.109	-0.049	-0.004	-0.003	-3.28	-3.30	-1.57	-0.12	-0.07
Germany	-0.061	-0.119	-0.067	-0.003	-0.002	-3.32	-5.26	-2.96	-0.14	-0.09
Poland	-0.073	-0.116	-0.045	-0.002	0.000	-1.16	-1.37	-0.60	-0.02	0.00
CEECs	-0.084	-0.104	-0.039	-0.002	-0.001	-1.52	-1.47	-0.61	-0.02	-0.01
Sweden	-0.057	-0.120	-0.047	-0.005	-0.016	-0.45	-1.01	-0.38	-0.03	-0.07
France	-0.062	-0.095	-0.047	-0.003	-0.001	-3.24	-4.29	-2.15	-0.12	-0.05
Italy	-0.047	-0.063	-0.028	-0.005	-0.002	-1.42	-1.66	-0.83	-0.13	-0.05
Finland	-0.025	-0.081	-0.040	-0.009	-0.003	-0.09	-0.35	-0.18	-0.03	-0.01
Austria	-0.024	-0.049	-0.021	-0.001	-0.023	-0.17	-0.31	-0.15	0.00	-0.12
Adriatic	-0.012	-0.065	-0.040	-0.003	-0.001	-0.03	-0.12	-0.08	0.00	0.00
G8 & China										
Canada	0.012	0.018	0.004	0.001	-0.001	0.39	1.06	0.40	0.04	-0.03
Japan	0.023	0.014	-0.001	0.000	-0.001	3.07	1.95	-0.26	0.06	-0.05
Russia	0.012	0.014	0.006	0.002	-0.001	0.24	2.01	1.46	0.09	-0.05
USA	0.011	0.012	0.000	0.000	0.000	3.74	4.23	0.31	0.14	-0.09
China	0.014	0.015	-0.002	0.000	-0.001	8.29	8.28	-0.56	0.15	-0.22
World Total	-0.026	-0.040	-0.022	-0.001	-0.001	-20.77	-40.31	-26.36	-1.52	-1.78

Source: Calculations by the authors.

### 3.2. Brefta Impacts

The main factor under Brefta is the imposition of the new time and out-of-pocket costs of cross-border trade through the imposition of a new hard border. Because of the need to enforce the EFTA-type FTA between the UK and the EU27, which characterizes the Brefta, there is an additional cost of demonstrating ROOs compliance. Thus, while Brefta is tariff-free, it is not cost-free in this sense. Our assumption that the four freedoms of movement remain in place for the most part results in only a modest increment to NTBs between the UK and EU27.

Table 3 summarizes the macroeconomic impacts of the Brefta scenario on the UK, the EU27 and other parties. Under the less disruptive exit assumed in the Brefta scenario, the UK's exit from the EU results in a decline in real GDP for the UK of about -1.0% and a loss of economic welfare of about USD 42 billion. For the EU27, the corresponding figures are about -0.1% and USD 24 billion. As in the Brexit scenario, Ireland takes by far the largest hit among the other individual Member States at -0.95%, with the Bellux group also absorbing a larger-than-EU27-average decline in GDP. Just as with the Brexit scenario, excluding these two regions results in a much smaller average decline in real GDP (-0.09%) for the balance of the Member States compared to the average rate (-0.16%) under Brexit. As in the Brexit scenario, Austria and the Adriatic states are the least affected in terms of GDP impacts. There are a few shifts in ranking under the Brefta scenario vs Brexit – the Mediterranean economies move into 3<sup>rd</sup> place from 6<sup>th</sup>, the Baltics move from 4<sup>th</sup> to 6<sup>th</sup> place and Sweden moves from 9<sup>th</sup> to 7<sup>th</sup> place in terms of the most significant.

For third parties, the Brefta generates similar patterns of both positive trade diversion and negative income effects; however, just as for the UK and EU27 the effects are much more muted. There are some changes in the ranking of the third parties; Canada now makes the biggest gain in terms of real GDP at 0.015% – vs Japan in the Brexit scenario. China, at USD 7 billion, continues to make the largest aggregate gain in economic welfare. The global economy as a whole is worse off, with real GDP 0.03% lower than the baseline – but this compares favourably to the 0.09% reduction in the Brexit scenario.

Because of the dynamic nature of the model, the full impact of the Brefta shock is realized only gradually and the effects, thus, build up over time. Brefta features less of build-up of impacts over time since there is no regulatory drift to widen the negative impact on bilateral trade over time. The effects in 2030 on real GDP are on average about half again as high as in 2020, compared to the approximate doubling of impacts under Brexit.

**Table 3: GDP and Welfare Impacts of Brefta, Relative to Baseline, by Region**

	Real GDP (% change)		Welfare (USD billions)	
	2020	2030	2020	2030
<b>EU28</b>	<b>-0.153</b>	<b>-0.243</b>	<b>-39.06</b>	<b>-65.87</b>
<b>UK</b>	<b>-0.646</b>	<b>-0.967</b>	<b>-25.56</b>	<b>-41.60</b>
<b>EU27</b>	<b>-0.067</b>	<b>-0.109</b>	<b>-13.50</b>	<b>-24.27</b>
Ireland	-0.510	-0.945	-1.29	-2.94
Bellux	-0.204	-0.298	-1.57	-2.36
Netherlands	-0.088	-0.125	-0.98	-1.62
Baltics	-0.058	-0.113	-0.12	-0.29
Denmark	-0.082	-0.120	-0.37	-0.61
Mediterranean	-0.081	-0.135	-0.43	-0.80
Iberia	-0.058	-0.094	-1.48	-2.86
Germany	-0.057	-0.095	-2.56	-4.16
Poland	-0.051	-0.093	-0.49	-1.09
CEECs	-0.047	-0.087	-0.52	-1.21
Sweden	-0.068	-0.096	-0.45	-0.79
France	-0.057	-0.077	-2.05	-3.44
Italy	-0.031	-0.056	-0.86	-1.45
Finland	-0.046	-0.066	-0.17	-0.28
Austria	-0.026	-0.043	-0.13	-0.27
Adriatic	-0.039	-0.052	-0.06	-0.09
G8 & China				
Canada	0.005	0.015	0.37	0.87
Japan	0.002	0.012	0.29	1.62
Russia	0.007	0.013	0.84	1.57
USA	0.002	0.010	1.27	3.75
China	0.004	0.012	0.89	6.81
World Total	-0.030	-0.033	-30.34	-33.21

Source: Calculations by the authors.

Across the board, border costs have the largest impact on GDP followed by ROOs, and services NTBs. The, FDI NTBs were generally fourth in terms of impact – with the exception of Austria where the FDI NTBs ranked third, followed by services NTBs.

With the exception of FDI NTBs, Ireland's declines in GDP resulting from Brexit's ROOs, border costs and services NTBs were the largest in the EU27 for each source. Denmark had the largest decline in real GDP attributable to FDI NTBs.

**Table 4: Source of Impacts on Real GDP and Welfare, 2030**

	ROOs	Border Costs	Goods NTBs	Services NTBs	FDI NTBs	ROOs	Border Costs	Goods NTBs	Services NTBs	FDI NTBs
	Real GDP (% change)					Welfare (USD billions)				
<b>EU28</b>	<b>-0.097</b>	<b>-0.123</b>	<b>0.000</b>	<b>-0.022</b>	<b>-0.001</b>	<b>-26.35</b>	<b>-33.58</b>	<b>0.00</b>	<b>-5.78</b>	<b>-0.16</b>
<b>UK</b>	<b>-0.390</b>	<b>-0.497</b>	<b>0.000</b>	<b>-0.079</b>	<b>-0.001</b>	<b>-16.81</b>	<b>-21.35</b>	<b>0.00</b>	<b>-3.40</b>	<b>-0.04</b>
<b>EU27</b>	<b>-0.042</b>	<b>-0.054</b>	<b>0.000</b>	<b>-0.012</b>	<b>-0.001</b>	<b>-9.54</b>	<b>-12.22</b>	<b>0.00</b>	<b>-2.39</b>	<b>-0.12</b>
Ireland	-0.356	-0.459	0.000	-0.130	-0.001	-1.12	-1.45	0.00	-0.37	0.00
Bellux	-0.112	-0.142	0.000	-0.042	-0.002	-0.90	-1.15	0.00	-0.29	-0.01
Netherlands	-0.048	-0.061	0.000	-0.016	0.000	-0.64	-0.82	0.00	-0.16	0.00
Baltics	-0.047	-0.060	0.000	-0.005	0.000	-0.12	-0.15	0.00	-0.01	0.00
Denmark	-0.039	-0.050	0.000	-0.022	-0.009	-0.22	-0.27	0.00	-0.08	-0.04
Mediterranean	-0.051	-0.065	0.000	-0.019	0.000	-0.30	-0.38	0.00	-0.13	0.00
Iberia	-0.036	-0.046	0.000	-0.012	0.000	-1.09	-1.40	0.00	-0.37	0.00
Germany	-0.038	-0.049	0.000	-0.007	0.000	-1.69	-2.16	0.00	-0.30	-0.01
Poland	-0.038	-0.049	0.000	-0.006	0.000	-0.45	-0.58	0.00	-0.06	0.00
CEECs	-0.035	-0.045	0.000	-0.007	0.000	-0.50	-0.64	0.00	-0.07	0.00
Sweden	-0.039	-0.050	0.000	-0.006	-0.001	-0.32	-0.42	0.00	-0.04	-0.01
France	-0.031	-0.040	0.000	-0.006	0.000	-1.39	-1.78	0.00	-0.25	-0.02
Italy	-0.021	-0.027	0.000	-0.008	0.000	-0.55	-0.71	0.00	-0.19	0.00
Finland	-0.026	-0.033	0.000	-0.006	0.000	-0.11	-0.15	0.00	-0.02	0.00
Austria	-0.016	-0.020	0.000	-0.003	-0.004	-0.10	-0.13	0.00	-0.02	-0.02
Adriatic	-0.021	-0.027	0.000	-0.005	0.000	-0.04	-0.05	0.00	-0.01	0.00
G8 & China										
Canada	0.006	0.008	0.000	0.001	0.000	0.35	0.45	0.00	0.07	0.00
Japan	0.005	0.006	0.000	0.001	0.000	0.67	0.86	0.00	0.09	0.00
Russia	0.005	0.006	0.000	0.003	0.000	0.65	0.83	0.00	0.10	-0.01
USA	0.004	0.005	0.000	0.001	0.000	1.45	1.84	0.00	0.47	-0.01
China	0.005	0.007	0.000	0.000	0.000	2.93	3.72	0.00	0.19	-0.02
World Total	-0.013	-0.017	0.000	-0.003	0.000	-13.17	-16.80	0.00	-2.97	-0.27

Source: Calculations by the authors.

### 3.3. Brexit with Single Market Effect

One issue with modelling trade scenarios involving the EU consists of the treatment for the single market. In this simulation, we treat intra-EU trade as enjoying a home bias. To do this, for each EU27 Member State, we treat imports from other EU Member States as domestic sales – that is, we set the substitution elasticity between imports from EU Member States and non-EU parties (including the UK in the Brexit scenario) at the level that applies for substitution between domestic production and imports. This has several implications. Most importantly, just as trade diversion effects reduce the gains from trade in a liberalization scenario, so they intensify losses in a scenario in which trade barriers are erected. Reducing the amount of trade diversion from intra-EU trade due to Brexit amplifies the costs for the EU27. This may also be considered as capturing the variety effect: as shown by Ossa (2012), applying the model developed by Arkolakis et al. (2012), as the substitution elasticity falls, the welfare gains from trade rise (and conversely, the welfare losses from reduction of trade increase). Tables 5 and 6 report the results.

Under this modelling approach, the UK figures are little changed: real GDP declines by 2.49% (vs -2.54% without the single market effect), and economic welfare loss is USD 99 billion vs a USD 101 billion loss under Brexit. For the EU27 Member States, however, the impact is significantly larger. The GDP decline is -0.32% vs -0.24%. The welfare effect for this scenario is a decline of USD 108 billion which is a 50% increase over the decline of USD 72 billion under the Brexit scenario. Treating the EU as a single market increases the negative impact of Brexit on the global economy as a whole, from USD 91 billion to USD 96 billion.

**Table 5: GDP and Welfare Impacts of Brexit with Single Market Effect, Relative to Baseline, by Region**

	Real GDP (% change)		Welfare (USD billions)	
	2020	2030	2020	2030
<b>EU28</b>	<b>-0.340</b>	<b>-0.723</b>	<b>-97.16</b>	<b>-206.86</b>
<b>UK</b>	<b>-1.325</b>	<b>-2.495</b>	<b>-48.79</b>	<b>-99.10</b>
<b>EU27</b>	<b>-0.169</b>	<b>-0.318</b>	<b>-48.36</b>	<b>-107.76</b>
Ireland	-1.163	-3.167	-3.89	-10.72
Bellux	-0.592	-1.171	-6.74	-11.43
Netherlands	-0.262	-0.529	-4.34	-8.77
Baltics	-0.154	-0.588	-0.47	-1.76
Denmark	-0.218	-0.434	-1.52	-2.95
Mediterranean	-0.150	-0.380	-0.98	-2.47
Iberia	-0.151	-0.347	-5.41	-12.70
Germany	-0.125	-0.314	-8.08	-17.14
Poland	-0.142	-0.389	-2.00	-5.59
CEECs	-0.140	-0.388	-2.54	-7.01
Sweden	-0.168	-0.338	-1.50	-3.29
France	-0.142	-0.274	-6.73	-14.64
Italy	-0.067	-0.186	-2.79	-6.15
Finland	-0.110	-0.216	-0.50	-1.08
Austria	-0.080	-0.197	-0.67	-1.59
Adriatic	-0.093	-0.197	-0.20	-0.47
G8 & China				
Canada	0.014	0.051	0.67	2.50
Japan	0.012	0.054	1.97	6.59
Russia	0.022	0.061	1.53	5.01
USA	0.009	0.035	4.25	11.39
China	0.015	0.043	3.61	21.13
World Total	-0.063	-0.089	-71.40	-96.01

Source: Calculations by the authors.

**Table 6: Source of Impacts on Real GDP and Welfare, 2030**

	Real GDP (% change)					Welfare (USD billions)				
	ROOs	Border Costs	Goods NTBs	Services NTBs	FDI NTBs	ROOs	Border Costs	Goods NTBs	Services NTBs	FDI NTBs
<b>EU28</b>	<b>-0.262</b>	<b>-0.314</b>	<b>-0.131</b>	<b>-0.013</b>	<b>-0.004</b>	<b>-73.22</b>	<b>-89.97</b>	<b>-39.49</b>	<b>-3.44</b>	<b>-0.73</b>
<b>UK</b>	<b>-0.882</b>	<b>-1.139</b>	<b>-0.431</b>	<b>-0.043</b>	<b>-0.001</b>	<b>-29.09</b>	<b>-48.75</b>	<b>-19.45</b>	<b>-1.79</b>	<b>-0.01</b>
<b>EU27</b>	<b>-0.147</b>	<b>-0.162</b>	<b>-0.075</b>	<b>-0.007</b>	<b>-0.004</b>	<b>-44.13</b>	<b>-41.22</b>	<b>-20.04</b>	<b>-1.66</b>	<b>-0.71</b>
Ireland	-1.280	-1.183	-0.630	-0.072	-0.002	-4.50	-3.88	-2.11	-0.23	-0.01
Bellux	-0.511	-0.425	-0.220	-0.011	-0.004	-5.44	-3.86	-2.01	-0.10	-0.02
Netherlands	-0.239	-0.184	-0.090	-0.016	-0.001	-4.19	-2.72	-1.66	-0.19	-0.01
Baltics	-0.280	-0.206	-0.099	-0.003	-0.001	-0.90	-0.57	-0.28	-0.01	0.00
Denmark	-0.176	-0.145	-0.050	-0.010	-0.053	-1.27	-0.92	-0.48	-0.05	-0.23
Mediterranean	-0.107	-0.178	-0.085	-0.010	0.000	-0.75	-1.10	-0.55	-0.08	0.01
Iberia	-0.136	-0.141	-0.060	-0.006	-0.003	-5.56	-4.72	-2.15	-0.19	-0.07
Germany	-0.091	-0.142	-0.074	-0.005	-0.002	-5.93	-7.23	-3.68	-0.22	-0.08
Poland	-0.150	-0.173	-0.061	-0.004	-0.001	-2.39	-2.26	-0.90	-0.05	0.00
CEECs	-0.166	-0.163	-0.054	-0.004	-0.001	-3.25	-2.70	-1.00	-0.06	-0.01
Sweden	-0.096	-0.159	-0.061	-0.006	-0.015	-1.01	-1.55	-0.61	-0.05	-0.06
France	-0.093	-0.119	-0.057	-0.004	-0.001	-5.50	-6.01	-2.89	-0.19	-0.05
Italy	-0.068	-0.076	-0.033	-0.007	-0.002	-2.47	-2.35	-1.10	-0.18	-0.05
Finland	-0.049	-0.107	-0.048	-0.010	-0.003	-0.26	-0.53	-0.24	-0.04	-0.01
Austria	-0.064	-0.080	-0.030	-0.002	-0.022	-0.58	-0.63	-0.25	-0.02	-0.11
Adriatic	-0.047	-0.095	-0.049	-0.005	-0.001	-0.13	-0.21	-0.11	-0.01	0.00

	ROOs	Border Costs	Goods NTBs	Services NTBs	FDI NTBs	ROOs	Border Costs	Goods NTBs	Services NTBs	FDI NTBs
	Real GDP (% change)					Welfare (USD billions)				
G8 & China										
Canada	0.021	0.024	0.006	0.001	-0.001	0.72	1.29	0.46	0.06	-0.03
Japan	0.033	0.021	0.000	0.001	-0.001	4.06	2.59	-0.09	0.08	-0.05
Russia	0.027	0.024	0.009	0.003	-0.001	0.87	2.47	1.61	0.12	-0.06
USA	0.018	0.016	0.001	0.001	0.000	5.23	5.37	0.67	0.20	-0.09
China	0.022	0.021	0.000	0.001	-0.001	10.98	10.23	-0.08	0.23	-0.23
World Total	-0.025	-0.039	-0.022	-0.001	-0.001	-23.14	-41.35	-28.17	-1.56	-1.78

Source: Calculations by the authors.

### 3.4. Brexit with a UK-US FTA

One possible offset for the UK to the costs of withdrawal from the single market is an opportunity to pursue a more aggressive FTA agenda, in particular with the United States. With the radical turn of events in the United States on social and environmental fronts, an EU-US TTIP might be difficult to conclude in the politically relevant coming decade, given the sustainability hurdles that an EU FTA must pass to obtain ratification. The UK would seem to face lower hurdles to proceed with an FTA with the United States, although it must be acknowledged that political signals are open to multiple interpretations. We simulate Brexit with an add-on of a UK-US FTA, provisionally implemented in 2020 to avoid the question of how long such an agreement might actually take to negotiate. This FTA is modelled on CETA-level tariff and NTB commitments for the UK and TPP-level tariff and NTB commitments for the United States. The simulation is run with the model incorporating the single market effect for the EU. Tables 7 and 8 provide the results.

Under this scenario, the negative impact to the UK is about 6% smaller than in the Brexit scenario. Real GDP declines by 2.39% (vs by about 2.5% for Brexit without a UK-US FTA add-on) and the economic welfare loss falls to USD 95 billion from USD 101 billion. For the EU27 Member States, the UK-US FTA raises the cost of Brexit: significantly in terms of real GDP, the negative impact rises 70% from -0.237% to -0.403%; and in terms of welfare there is a 50% increase from USD 72 billion to USD 110 billion.

Ireland continues to take the largest hit, followed by the Bellux group. As in the Brexit with Single Market Effect scenario, Italy has the smallest change in GDP, followed by Austria and the Adriatic states. A few countries shift in the rankings, with the biggest shift being for Poland, Germany and CEECs, which move from 7<sup>th</sup>, 10<sup>th</sup> and 11<sup>th</sup> rank under Brexit to 11<sup>th</sup>, 6<sup>th</sup> and 7<sup>th</sup> in this scenario, respectively. For third parties, Russia retains its first place ranking in terms of real GDP gain as in the Brexit with Single Market Effect scenario and as with all the other scenarios China continues to have largest aggregate gain in economic welfare. The global economy as a whole remains worse off – the UK-US FTA does not compensate for Brexit. The offset is relatively small, lowering the real GDP loss to 0.087% from about 0.091% in the Brexit scenarios and the welfare loss to USD 96 billion from USD 100 billion in the Brexit scenario. ROOs and border costs account for the largest impact on GDP both in the EU27 and outside the EU28.

The figures that really jump off the page in this scenario, however, are the impacts of the UK-US FTA for the United States. For the United States, the bilateral trade agreement with the UK generates very small gains of 0.056% in real GDP with USD 18 billion in welfare gains. In the three earlier scenarios, the US welfare gain was about half that generated for China. In this scenario, the welfare gain is about 90% of China's welfare gain. One of the major issues for the UK will be to get policy attention in foreign capitals mobilized to address the impacts of the Trump Administration policies on the global trading order as well as the policy attention of the Trump Administration itself.

**Table 7: GDP and Welfare Impacts of Brexit + UK-US FTA, Relative to Baseline, by Region**

	Real GDP (% change)		Welfare (USD billions)	
	2020	2030	2020	2030
<b>EU28</b>	<b>-0.334</b>	<b>-0.713</b>	<b>-96.17</b>	<b>-205.13</b>
<b>UK</b>	<b>-1.261</b>	<b>-2.387</b>	<b>-46.26</b>	<b>-94.86</b>
<b>EU27</b>	<b>-0.172</b>	<b>-0.403</b>	<b>-49.91</b>	<b>-110.28</b>
Ireland	-1.179	-3.218	-4.01	-10.96
Bellux	-0.605	-1.190	-6.93	-11.65
Netherlands	-0.268	-0.541	-4.48	-8.97
Baltics	-0.156	-0.594	-0.47	-1.78
Denmark	-0.223	-0.442	-1.56	-3.01
Mediterranean	-0.152	-0.383	-0.99	-2.50
Iberia	-0.154	-0.352	-5.53	-12.92
Germany	-0.129	-0.321	-8.42	-17.61
Poland	-0.145	-0.399	-2.07	-5.75
CEECs	-0.142	-0.393	-2.59	-7.13
Sweden	-0.171	-0.345	-1.55	-3.38
France	-0.145	-0.281	-6.97	-15.07
Italy	-0.069	-0.192	-2.91	-6.32
Finland	-0.112	-0.220	-0.52	-1.10
Austria	-0.082	-0.203	-0.70	-1.63
Adriatic	-0.096	-0.201	-0.21	-0.48
G8 & China				
Canada	0.007	0.036	0.27	1.77
Japan	0.011	0.050	1.76	6.02
Russia	0.021	0.057	1.49	4.71
USA	0.018	0.056	7.61	18.27
China	0.014	0.041	3.36	19.72
World Total	-0.060	-0.087	-69.26	-95.82

Source: Calculations by the authors.

**Table 8: Source of Impacts on Real GDP and Welfare, 2030**

	ROOs+ Border costs	Goods NTBs	Services NTBs	FDI NTBs	ROOs+ border costs	Goods NTBs	Services NTBs	FDI NTBs
	Real GDP (% change)				Welfare (USD billions)			
<b>EU28</b>	<b>-0.716</b>	<b>0.002</b>	<b>0.000</b>	<b>0.000</b>	<b>-205.94</b>	<b>0.71</b>	<b>0.10</b>	<b>0.00</b>
<b>UK</b>	<b>-2.413</b>	<b>0.024</b>	<b>0.003</b>	<b>0.000</b>	<b>-96.17</b>	<b>1.16</b>	<b>0.15</b>	<b>0.00</b>
<b>EU27</b>	<b>-0.401</b>	<b>-0.002</b>	<b>0.000</b>	<b>0.000</b>	<b>-109.77</b>	<b>-0.45</b>	<b>-0.06</b>	<b>0.00</b>
Ireland	-3.198	-0.019	-0.001	0.000	-10.87	-0.08	-0.01	0.00
Bellux	-1.186	-0.004	0.000	0.000	-11.60	-0.05	0.00	0.00
Netherlands	-0.538	-0.002	0.000	0.000	-8.93	-0.04	0.00	0.00
Baltics	-0.593	-0.001	0.000	0.000	-1.77	0.00	0.00	0.00
Denmark	-0.441	-0.001	0.000	0.000	-3.00	-0.01	0.00	0.00
Mediterranean	-0.383	0.000	0.000	0.000	-2.50	0.00	0.00	0.00
Iberia	-0.351	-0.001	0.000	0.000	-12.88	-0.03	-0.01	0.00
Germany	-0.320	-0.001	0.000	0.000	-17.51	-0.09	-0.01	0.00
Poland	-0.397	-0.001	0.000	0.000	-5.73	-0.02	0.00	0.00
CEECs	-0.392	-0.001	0.000	0.000	-7.12	-0.01	0.00	0.00
Sweden	-0.343	-0.001	0.000	0.000	-3.36	-0.02	0.00	0.00
France	-0.280	-0.001	0.000	0.000	-15.00	-0.07	-0.01	0.00
Italy	-0.191	-0.001	0.000	0.000	-6.29	-0.02	-0.01	0.00
Finland	-0.219	-0.001	0.000	0.000	-1.10	0.00	0.00	0.00
Austria	-0.202	-0.001	0.000	0.000	-1.63	-0.01	0.00	0.00
Adriatic	-0.200	-0.001	0.000	0.000	-0.48	0.00	0.00	0.00



	ROOs+ Border costs	Goods NTBs	Services NTBs	FDI NTBs	ROOs+ border costs	Goods NTBs	Services NTBs	FDI NTBs
	Real GDP (% change)				Welfare (USD billions)			
G8 & China								
Canada	0.039	-0.003	0.000	0.000	1.90	-0.12	-0.01	0.01
Japan	0.051	-0.001	0.000	0.000	6.12	-0.10	-0.01	0.00
Russia	0.058	0.000	0.000	0.000	4.74	-0.03	-0.01	0.01
USA	0.051	0.004	0.001	0.001	17.01	0.95	0.10	0.21
China	0.042	0.000	0.000	0.000	19.99	-0.27	-0.02	0.02
World Total	-0.088	0.001	0.000	0.000	-96.58	0.37	0.05	0.34

Source: Calculations by the authors.

### 3.5. Macro Impacts on the UK and the EU27

Tables 9 and 10 summarize the main indicators under the four scenarios for the UK and the EU27 respectively in 2030 when all the impacts of the scenarios will have worked their way through the economy.

**Table 9: Summary of Macroeconomic Impacts on the UK, 2030**

	Brexit	Brefita	Brexit – Single Market	Brexit - Single Market + UK-US FTA
Major aggregates				
Economic Welfare USD billions	-101.6	-41.6	-99.1	-94.9
Economic Welfare % change	-2.75	-1.08	-2.69	-2.58
GDP value USD billions	-114.0	-53.6	-89.7	-85.9
GDP value USD billions % change	-2.89	-1.36	-2.80	-2.68
GDP volume % change	-2.54	-0.97	-2.50	-2.39
GDP deflator % change	-0.35	-0.39	-0.30	-0.29
CPI % change	0.08	-0.24	0.10	0.10
National Accounts Aggregates (real terms)				
Consumption	-3.00	-1.15	-2.93	-2.81
Government Expenditure	-1.93	-0.84	-1.88	-1.80
Investment	-4.38	-1.63	-4.28	-4.06
Total Exports of Goods & Services	-6.75	-1.72	-6.63	-6.24
Total Imports of Goods & Services	-7.53	-2.20	-7.34	-6.93
Trade Impacts (value terms)				
Bilateral exports UK to EU27 USD billions	-100.3	-31.4	-98.2	-98.5
Bilateral Exports % change	-22.86	-6.98	-22.48	-22.57
Bilateral Imports UK from EU27 USD billions	-144.4	-40.0	-141.7	-143.9
Bilateral Imports % change	-31.79	-9.01	-31.42	-31.89
Total Exports USD billions	-81.0	-22.6	-79.1	-74.9
Total Exports % change	-6.75	-1.72	-6.63	-6.24
Total Imports USD billions	-97.1	-28.5	-94.8	-89.8
Total Imports % change	-7.53	-2.20	-7.34	-6.93
Trade balance USD billions	16.1	5.9	15.7	14.9
Terms of Trade % change	-0.50	-0.29	-0.45	-0.43
Factor Markets				
Capital Stock % change	-1.84	-0.75	-1.80	-1.70
Real wage of Unskilled labour % change	-1.70	-0.58	-1.66	-1.58
Real wage of skilled labour % change	-1.80	-0.60	-1.76	-1.68
Real GDP / Total Real Trade	0.36	0.49	0.36	0.36
Labour Productivity / Real Wage	1.45	1.64	1.46	1.46

Source: Calculations by the authors.

**Table 10: Summary of Macroeconomic Impacts on the EU27, 2030**

	Brexit	Brefta	Brexit – Single Market	Brexit – Single Market + UK-US FTA
<b>Major aggregates</b>				
Economic Welfare USD billions	-71.8	-24.3	-107.8	-110.3
Economic Welfare % change	-0.35	-0.12	-0.52	-0.53
GDP value USD billions	-107.4	-32.3	-122.5	-127.2
GDP value USD billions % change	-0.50	-0.15	-0.67	-0.69
GDP volume % change	-0.30	-0.11	-0.39	-0.40
GDP deflator % change	-0.20	-0.04	-0.28	-0.30
CPI % change	-0.13	-0.03	-0.17	-0.19
<b>National Accounts Aggregates (real terms)</b>				
Consumption	-0.38	-0.13	-0.56	-0.57
Government Expenditure	-0.25	-0.09	-0.37	-0.37
Investment	-0.49	-0.16	-0.68	-0.70
Total Exports of Goods & Services	-0.40	-0.11	-0.59	-0.60
Total Imports of Goods & Services	-0.59	-0.16	-0.97	-0.99
<b>Trade Impacts (value terms)</b>				
Bilateral exports EU27 to UK USD billions	-144.4	-40.0	-141.7	-143.9
Bilateral Exports % change	-31.79	-9.01	-31.42	-31.89
Bilateral Imports EU27 from UK USD billions	-100.3	-31.4	-98.2	-98.5
Bilateral Imports % change	-22.86	-6.98	-22.48	-22.57
Total Exports USD billions	-55.1	-14.2	-79.5	-82.2
Total Exports % change	-0.40	-0.11	-0.59	-0.60
Total Imports USD billions	-56.3	-14.6	-93.0	-95.8
Total Imports % change	-0.59	-0.16	-0.97	-0.99
Trade balance USD billions	1.3	0.4	13.5	13.6
Terms of Trade % change	-0.08	-0.01	-0.11	-0.12
<b>Factor Markets</b>				
Capital Stock % change	-0.19	-0.07	-0.27	-0.27
Real wage of Unskilled labour % change	-0.20	-0.07	-0.29	-0.29
Real wage of skilled labour % change	-0.21	-0.07	-0.30	-0.31
Real GDP / Total Real Trade	0.60	0.81	0.50	0.50
Labour Productivity / Real Wage	1.47	1.66	1.32	1.33

Source: Calculations by the authors.

## 4. Conclusions

In terms of numbers, Brexit is an expensive proposition for both the UK and the EU27. We evaluate the cost to the UK as equivalent to a permanent reduction of GDP by about 2.54% by 2030. The welfare cost to UK households is equivalent to a loss of about USD 100 billion in total household income. The hypothetical border that we construct for this scenario using available data for the cost of trading across borders for the UK and the EU is the single biggest element of the increased costs. In terms of its costs, our constructed border resembles the Canada-US border based on a range of studies of the cost of the latter.

Under Brefta, where the UK exits the EU with an EFTA-style agreement in place, the cost is substantially reduced. For this scenario, which assumes a carefully negotiated exit that minimizes bilateral trade costs between the UK and the EU27, we reduce the cost of the border to one comparable to the current EU-Swiss border. We do not factor in the one-time costs of constructing the border. Since there is no legacy border to deal with, the UK and the EU27 would be free to construct an optimal border, drawing on state-of-the-art customs procedures, information technology, risk management, and so forth, to largely retain the seamless experience under the single market. However, whereas Brexit does not impose additional ROOs costs on UK-EU27 trade (which is conducted on an MFN basis), Brefta does. We assume a low-cost ROOs regime that minimizes costs for small and medium-sized enterprises.

We consider the implications of Brexit given the existence of a single market effect, which creates lower substitutability of internal EU27 trade for external trade. In this scenario, the welfare costs rise, particularly for the EU27 as lower trade elasticities imply higher welfare losses from the disruption of trade by Brexit.

A UK FTA with the United States softens the blow of Brexit but only compensates for about one-fifth of the welfare losses to the UK from Brexit. The preference erosion for the EU27 in the UK and US markets adds on additional welfare losses for the EU27 although these are relatively modest in the big picture.

Table 11 summarizes the main results across the four scenarios.

The least disruptive scenario is Brefta. Brexit with Single Market Effect generates the best outcome for third parties with the exception of the United States which has the best outcome under the Brexit with a UK-US FTA scenario.

**Table 11: Summary of Real GDP and Welfare 2030 – 4 Scenarios**

	Real GDP (% change) 2030				Welfare (USD billions) 2030			
	Brexit	Brefta	Brexit with Single Market Effect	Brexit with a UK-US FTA	Brexit	Brefta	Brexit with Single Market Effect	Brexit with a UK-US FTA
UK	-2.54	-0.97	-2.50	-2.39	-101.6	-41.6	-99.1	-94.9
EU27	-0.30	-0.11	-0.40	-0.40	-71.8	-24.3	-107.8	-110.3
Canada	0.03	0.02	0.05	0.04	1.9	0.9	2.5	1.8
Japan	0.04	0.01	0.05	0.05	4.8	1.6	6.6	6.0
Russia	0.03	0.01	0.06	0.06	3.7	1.6	5.0	4.7
USA	0.02	0.01	0.04	0.06	8.3	3.8	11.4	18.3
China	0.03	0.01	0.04	0.04	15.9	6.8	21.1	19.7
World Total	-0.09	-0.03	-0.09	-0.09	-90.7	-33.2	-96.0	-95.8

Source: Calculations by the authors.

Several conclusions can be derived from these results.

First, the economic disruption of a full Brexit generates significant economic costs for both parties – the UK and the EU27. These costs substantially exceed those associated with the UK exiting the EU with an EFTA-like free trade arrangement.

Second, for the UK, an FTA with the United States reduces the negative impact on welfare marginally – with only a USD 6 billion improvement in economic welfare. This reflects the heavy toll that distance exacts on trade: although the United States is larger than the EU27, the distance across the Atlantic is sufficiently greater than that across the English Channel that the trade gains under a UK-US FTA are a steep discount to those available under the Single Market. This reality is compounded by the necessarily shallower degree of liberalization possible with the United States. The incremental USD 10 billion in welfare that is generated from a bilateral UK-US FTA post Brexit may complicate matters for the UK since there is no mistaking the position of US trade policy as considering America first – and an overall gain of USD 18 billion for America may affect the UK's ranking in the US's FTA queue.

Third, from a technical modelling perspective, the welfare loss to the EU27 is greater if we treat all internal EU27 trade as equivalent to domestic shipments. This is consistent with theoretical treatments of the welfare gains from trade as depending on the trade elasticity and also consistent with the increase in economic gains for the EU from trade liberalization when its internal market is treated as a Single Market.

Fourth, the main external beneficiaries of Brexit are geopolitical rivals – USA and China.

The bottom line is that Brexit scenarios put the UK and the EU27 onto lower-output tracks due to economic inefficiencies that persist year-in, year-out. There are many caveats to this conclusion based on factors that are not explicitly incorporated in the modelling: one set is based on potential economic gains that Brexit might afford; the second is based on dynamic effects that could amplify the losses.

A major premise of support for Brexit is that EU regulation impedes UK growth. This can be neither substantiated nor dismissed out of hand since: (a) EU regulation by definition has a “one size fits all” within the Union; and (b) given there are thousands of regulations, it is not possible to parse through these and identify those where the purpose of the regulation is not served by its application in the UK but the cost of compliance is nonetheless borne by UK firms.

Looking first at regulations that address product quality and are required for market access (e.g., documentation of chemical content of products), Brexit is not a solution – the better option to modify regulations is to remain in the Union and influence their making.

Looking next at regulations that address over-riding social or environmental objectives (e.g., labour market or climate change), de-regulation in these areas by the UK might generate cost savings to the UK economy. An Open Europe assessment (conducted pre-Brexit in Spring 2015) suggested GBP 12.8 billion of savings were possible (about USD 20 billion 2011 USD). This, if realizable, would represent a modest offset to the Brexit costs, if it flowed entirely into UK household incomes. If the benefits flowed primarily to multinational firms' bottom lines, UK welfare might be minimally improved, if at all. At the same time, the UK would face constraints from potential anti-dumping/countervailing duty actions if new regulations were construed as generating either social or environmental dumping.

The second set of caveats concerns factors that could worsen outcomes. As we have not attempted to explicitly quantify these, the most that can be said is that the majority of these represent negative impacts for the UK and the EU27 because of additional transactions costs and heightened uncertainty.

In this regard, it is important to distinguish the build-up over time in the equilibrium impact reported in this study and short-term dynamics. The initial impact of Brexit could be much greater in a negative sense than portrayed here because of market reactions that are then dampened over time. Table 12 sets out the present value of the foregone income from Brexit on an equilibrium path. They are large. If the economy takes a low road – i.e., greater short-term disruption than would be felt in the long-run outcome – the present value of the foregone income would be considerably higher. The chances of a high road seem to be small since the reaction of business to the announcement of Brexit is already to make adjustments rather than wait for the actual change in trade relations.

**Table 12: Impacts of Brexit Scenario in Present Value Terms**

	Brexit	Brefta	Brexit with Single Market Effect	Brexit plus UK-US FTA
<b>EU28</b>	<b>-832</b>	<b>-357</b>	<b>-1007</b>	<b>-998</b>
<b>UK</b>	<b>-503</b>	<b>-229</b>	<b>-491</b>	<b>-468</b>
<b>EU27</b>	<b>-329</b>	<b>-128</b>	<b>-516</b>	<b>-530</b>
Ireland	-38	-14	-47	-48
Bellux	-38	-14	-61	-63
Netherlands	-29	-9	-44	-45
Baltics	-4	-1	-7	-7
Denmark	-11	-3	-16	-16
Mediterraneans	-8	-4	-11	-11
Iberia	-38	-14	-59	-60
Germany	-55	-23	-85	-88
Poland	-13	-5	-24	-25
CEECs	-15	-6	-31	-31
Sweden	-9	-4	-16	-16
France	-45	-19	-71	-73
Italy	-19	-8	-30	-31
Finland	-3	-2	-5	-5
Austria	-3	-1	-8	-8
Adriatics	-1	-1	-2	-2
<b>G8 &amp; China</b>				
Canada	8	4	10	7
Japan	21	7	29	27
Russia	17	8	22	21
USA	38	17	52	87
China	60	25	79	74
<b>World Total</b>	<b>-504</b>	<b>-220</b>	<b>-570</b>	<b>-560</b>

Source: Calculations by the authors.

Finally, there is a general caveat to be noted. The scenarios described here explicitly assume the global trading environment remains as it was in the base year of the GTAP dataset – 2011. That world is now long gone and Brexit and the election of Donald Trump have injected a major dollop of uncertainty into international commerce. A basic premise underpinning Brexit was that there were trade opportunities available to the UK on a timelier or deeper basis than as part of the EU. The most important trade partner for the UK in this regard is the United States. The Trump election casts doubt on what the UK can achieve one-on-one with the United States, especially in light of the uncertainty as to what the United States will ultimately sign on to.

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# Technical Annex

## 1. Construction of the Brexit Tariff Shock

The Brexit tariff shock consists of the imposition of WTO MFN levels of protection between the UK and the EU27. To construct this policy shock, we build up weighted average protection levels from the 10-digit tariff-line level to the GTAP product group level. This tariff profile is then imposed upon UK-EU27 trade at the disaggregated EU Member State level.

Since trade within the EU is not distorted by tariffs, we have the unusual luxury of not having to worry about endogeneity bias in applying the tariff shock.<sup>3</sup> Accordingly, we use the weighted average MFN rates that emerge from our calculations. Constructed in this fashion, the tariffs vary by EU27 Member State/region. Notably, while the EU MFN tariff is the same at the tariff-line level, the different composition of imports and exports means that the UK faces a different level of tariffs in the EU27 than the EU27 faces in the UK. Further, as can be seen from Table A1, the changing composition of trade from year to year means that there is no definitive tariff shock for Brexit. The actual tariff shock under Brexit would depend on what trade would have been in the counterfactual where the UK remained in the EU.

For a handful of agricultural products that feature very high MFN tariffs (in all cases, agricultural products are subject to managed trade regimes with tariff rate quotas limiting the extent of market access), we adopt pragmatic “halfway house” assumptions since the Brexit shock would otherwise be excessive; for this purpose, we use US-EU levels of bilateral protection in agriculture to establish the tariff shock. The specific areas where we intervene are the following:

- Beef: UK imports from Ireland, where we lower the effective tariff increase from 75% to 23%;
- Dairy: UK imports from Ireland, where we lower the effective tariff increase from 50% to 30%; and
- Sugar: UK imports from France, where we lower the effective tariff increase from 63% to 8%.

The full set of initial tariffs by GTAP sector is included in the “Brexit Tariff Shock” tab of the Excel data file accompanying this report. We describe the detailed methodology below.

The Brexit tariff shock is based on the EU 2014 MFN schedule and is weighted by imports of the following 17 EU regions: Adriatics (Croatia and Slovenia), Austria, Baltics, Bellux (Belgium and Luxembourg), CEECs (Bulgaria, Czech Republic, Hungary, Romania, and Slovakia), Denmark, Finland, France, Germany, Iberia (Portugal and Spain), Ireland, Italy, Mediterraneans (Cyprus, Greece, and Malta), Netherlands, Poland, Sweden, and the UK.

We construct four separate datasets by weighting the 2014 MFN schedule by 2010, 2011, 2012, and 2013 imports.<sup>4</sup> This provides the basis for assessment of whether any specific year is an outlier. The procedure involves the following steps:

- 1) The MFN schedule is obtained from the International Trade Centre’s (ITC) Market Access Map database.<sup>5</sup> An advantage of using ITC data is that specific tariffs (which are not expressed as a percentage of the value of the dutiable products) in the national tariff schedules are converted by ITC to ad valorem equivalents (i.e., the tariffs are expressed as a percentage of the value of the dutiable products).

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<sup>3</sup> See Boumellassa et al. (2009) for a discussion of the endogeneity issue in constructing tariff protection.

<sup>4</sup> 2014 imports were not yet available at the time of construction of the data.

<sup>5</sup> International Trade Centre (2014).



- 2) The MFN tariffs, which are suspended by the EU, are replaced with MFN tariffs.<sup>6</sup> In some cases, tariffs are suspended only partially and a specific suspended tariff is applied. In these cases, we use ITC data to convert specific suspended tariffs into ad valorem equivalents.<sup>7</sup>
- 3) Because the 2014 EU tariff schedule follows a classification based on HS2012 and import data for 2010 and 2011 follow HS2007, the tariff lines are matched to corresponding HS2007 6-digit codes. This is required for subsequent aggregation of the tariffs. A conversion table from HS2012 to HS2007 is sourced from the United Nations Statistics Division (2010).
- 4) Aggregate tariffs at 10-digit tariff-line level up to HS 6-digit level as a simple average. Weighting cannot be performed at this detailed level, because the most disaggregated level at which the appropriate import data is available is HS 6-digit level.<sup>8</sup>
- 5) We then match 2010 and 2011 HS2007 6-digit imports of a region (by region-source) to 2014 tariffs (converted to HS2007, 6-digit level, at step 3). Similarly, we match 2012 and 2013 HS2012 6-digit imports to 2014 tariffs that also follow HS2012 classification.
- 6) We then aggregate the import and tariff data to GTAP codes. The mappings between GTAP and HS classifications are provided within the World Integrated Trade Solutions software package developed by the World Bank and the United Nations Conference on Trade and Development (UNCTD).<sup>9</sup> The mapping between GTAP and HS2007 is readily available. In order to create HS2012-GTAP mapping, an HS2012-HS2007 conversion table produced by the United Nations Statistics Division (2010) is used.
- 7) Aggregate tariffs at the HS 6-digit level up to GTAP code as weighted averages using actual imports as weights.
- 8) For the UK tariffs facing EU27 member states and the EU27 tariffs facing UK, we take the average MFN rates from 2010 to 2013 as the final protection level. However, for the agricultural products that feature very high MFN tariffs, we adopt the pragmatic "halfway house" assumptions discussed previously.

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<sup>6</sup> Tariff suspensions are total or partial waiver of tariffs that are in force over a specific period of time. See European Commission (2015a) for more information. There are more than 2,000 tariff lines for which tariffs are suspended, out of the almost 15,000 tariff lines in the MFN schedule. Suspensions are extracted from the TARIC database European Commission (2015b).

<sup>7</sup> We do not take into account the airworthiness tariff suspension (suspensions of duties for import of parts and other goods used for aircraft), because they are conditional on the use of product. As a product may have many uses besides aircraft (and the tariff is waived only if the product is used for aircraft), taking into account these suspensions would underestimate the level of protection.

<sup>8</sup> EUROSTAT provides data at Combined Nomenclature 8-digit level, but these data cannot be used for our purposes, because the nomenclature is changed every year and, for practical purposes, it is not possible to match CN8 codes for different years to 2014 tariff lines. In the 2010 and 2011 datasets, tariffs are aggregated up to HS2007 6-digit level and, in the 2012 and 2013 datasets, tariffs are aggregated up to HS2012 6-digit level. A shortcoming of calculating simple average tariffs is that they may be biased, because an equal weight is given to products that are imported in different volumes or even not imported at all. This bias is somewhat mitigated, because we use simple average tariffs to move only between 10-digit tariff line and the still-very-detailed HS 6-digit level. The bias, however, may be somewhat larger in some sectors in the 2010 and 2011 datasets, because in some cases tariff lines are aggregated within a broader HS 6-digit category than in the 2012 and 2013 datasets. This happens, because a 2014-10-digit tariff line necessarily corresponds to a single 6-digit HS2012 code, but it may correspond to several 6-digit HS2007 codes (because a single 6-digit HS2012 code may correspond to several 6-digit HS2007 codes). This is likely to be an issue only for those sectors that experienced substantial revision in HS2012. This also can make comparison of tariffs of a GTAP sector between 2010/2011 and 2012/2013 problematic.

<sup>9</sup> See WITS (n.d.). The mapping excludes GTAP 11 (raw milk) and corresponding 6-digit HS code(s) are matched to GTAP 22 (dairy products).

**Table A1: GTAP-level aggregation of Implied MFN tariffs, UK and EU27, 2010-2013**

		Tariffs that EU27 faces in UK				Tariffs that UK faces in EU27			
		2010	2011	2012	2013	2010	2011	2012	2013
1	PDR - Paddy rice	12.47	13.50	12.87	12.22	16.14	21.89	25.90	22.48
2	WHT - Wheat	20.04	19.37	19.87	20.49	20.67	20.94	20.04	20.26
3	GRO - Cereal grains n.e.c.	5.72	7.21	8.37	7.40	38.73	39.46	35.51	34.72
4	V_F - Vegetables, fruit, nuts	14.22	13.98	13.71	13.39	10.49	10.23	10.68	10.29
5	OSD - Oil seeds	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
6	C_B - Sugar cane, sugar beet	50.31	50.31	50.31	50.31	50.31	50.31	50.31	50.31
7	PFB - Plant-based fibers	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
8	OCR - Crops n.e.c.	6.90	6.81	6.90	6.89	3.61	4.00	3.84	3.89
9	CTL - Bovine cattle, sheep and goats, horses	4.97	5.10	8.18	5.30	2.06	3.19	3.97	4.18
10	OAP - Animal products n.e.c.	12.93	12.29	13.55	11.92	6.16	5.77	6.68	7.39
12	WOL - Wool, silk-worm cocoons	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
13	FRS - Forestry	1.09	0.71	0.90	0.89	0.25	0.28	0.14	0.11
14	FSH - Fishing	7.33	6.96	8.76	7.08	8.56	8.16	8.15	7.95
15	COA - Coal	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
16	OIL - Oil	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
17	GAS - Gas	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
18	OMN - Minerals n.e.c.	0.05	0.04	0.05	0.04	0.01	0.01	0.01	0.01
19	CMT - Bovine meat prods	74.12	72.99	72.88	73.26	57.57	58.18	56.72	58.86
20	OMT - Meat products n.e.c.	29.94	31.02	31.45	31.68	32.34	32.80	34.33	35.07
21	VOL - Vegetable oils and fats	12.50	12.92	11.24	11.19	9.05	8.03	7.74	7.61
22	MIL - Dairy products	50.04	50.36	50.76	50.96	51.24	52.96	54.42	55.38
23	PCR - Processed rice	26.01	26.31	26.35	26.38	25.87	26.86	26.49	26.83
24	SGR - Sugar	62.49	62.20	65.12	62.01	67.84	67.98	66.96	64.11
25	OFD - Food products n.e.c.	15.73	15.76	15.51	15.52	14.61	14.86	15.05	14.95
26	B_T - Beverages and tobacco products	10.96	13.42	10.34	9.07	8.22	8.03	7.18	6.60
27	TEX - Textiles	7.85	7.87	7.92	7.99	7.25	7.21	7.26	7.16
28	WAP - Wearing apparel	11.26	11.22	11.20	11.17	11.10	11.10	11.08	11.11
29	LEA - Leather products	8.24	8.28	8.60	8.33	8.26	8.09	8.23	8.18
30	LUM - Wood products	1.65	1.68	1.59	1.58	1.85	2.04	2.18	2.31
31	PPP - Paper products, publishing	0.12	0.15	0.23	0.28	0.12	0.12	0.13	0.09
32	P_C - Petroleum, coal products	2.14	2.01	2.11	2.24	2.06	2.02	2.29	2.28
33	CRP - Chemical, rubber, plastic products	1.97	2.08	1.95	1.88	1.73	1.82	1.83	1.76
34	NMM - Mineral products n.e.c.	3.12	3.09	3.18	3.33	2.55	2.54	2.55	2.54
35	I_S - Ferrous metals	0.22	0.20	0.19	0.22	0.27	0.26	0.32	0.24
36	NFM - Metals n.e.c.	2.03	1.72	1.34	1.60	1.63	1.45	1.43	1.44
37	FMP - Metal products	2.09	2.13	2.13	2.13	2.13	2.06	2.10	2.09
38	MVH - Motor vehicles and parts	8.23	8.24	8.17	8.33	7.86	7.87	7.94	8.09
39	OTN - Transport equipment n.e.c.	1.66	2.03	2.05	2.22	0.88	0.92	0.87	0.90
40	ELE - Electronic equipment	2.04	1.59	1.49	1.38	0.58	0.72	0.66	0.62
41	OME - Machinery and equipment n.e.c.	1.29	1.30	1.30	1.30	1.22	1.25	1.25	1.26
42	OMF - Manufactures n.e.c.	1.35	1.23	1.41	1.52	1.57	1.56	1.74	1.87

Source: Calculations by the authors. Note: MFN tariffs that are suspended by the EU are accordingly replaced with suspended tariffs sourced from the TARIC database.

A recent exercise in constructing a tariff shock for Brexit by Ottaviano et al. (2014) produced similar figures for most sectors, although the HS-based aggregates used in this study are not directly comparable to the GTAP sectors in the present study. In two sectors, the data diverged. This may reflect the different sources of data used (we use ITC Trade Map data, whereas Ottaviano et al., 2014 use WTO data).

**Table A2: Comparison of Constructed Tariffs**

	Ottaviano et al (2014)		Present Study	
	Tariff in UK	Tariff in EU27	Tariff in UK	Tariff in EU27
Food, Beverages, and Tobacco	7.26%	4.96%	23.38	22.40
Agriculture, Hunting, Forestry, and Fishing	5.90%	5.63%	11.27	8.26

## 2. Calibrating the Brexit and Brefta Border Costs

To construct the Brexit border, we draw on the time and out-of-pocket cost of border transit in the World Bank’s Doing Business surveys for the UK and the EU. The introduction of a customs barrier to UK-EU27 trade would occur in a generally low-cost environment. Doing Business indicates one day to exit and one day to enter, which we assume would be additional time, compared to the relatively seamless procedure under the single market. This is valued at an ad valorem tariff equivalent of 1.3% per day, which is the midpoint of the range identified by Hummels and Schaur (2012) that each day in transit is worth between 0.6% and 2% of the value of the goods being shipped.

In addition, we impose an additional administrative cost equal to US\$100 per container to reflect the new requirement of an additional document, the Single Administration Document (SAD) that now accompanies extra-EU exports. Currently, to export a container requires three documents, which cost US\$175 to prepare, and to import requires two documents, which cost US\$180. We assume the SAD takes up a modestly disproportionate share of the export total and further assume that the additional document preparation time does not add to the time costs of UK-EU27 trade, as such preparation can be done in anticipation of actual transit.

We transform this into an ad valorem equivalent cost by applying it to an estimate of the average value of goods shipped in a standard container (twenty-foot equivalent unit or TEU) between the US and Europe and in the reverse direction. This figure is about 0.33%, which is derived as follows. We rely on a Swiss Re estimate of the value of a container load going in these two directions in 2007 (average value of US\$27,452), which we raise to US\$30,606 based on the estimated increase in the US GDP deflator between 2007 and 2014. We assume a \$100 cost of the SAD, loosely based on the Doing Business documentation costs, which were valid for 2014. This works out to an ad valorem equivalent (AVE) of 0.33%. The combined costs generate a total border cost as an AVE on imports of 3.26%.

Examining the literature, this figure is comparable to estimates for the Canada-US border, cited by Moens and Gabler (2012) and Moens and Cust (2008), albeit at the high end of the range. Several other observations are salient:

- Notably, notwithstanding the very high degree of trust between Canada and the US, the costs of border security have not decreased over time – if anything, the reverse is true.<sup>10</sup> Our assumed costs do not directly take into account additional behind-the-border costs of trading companies to obtaining and maintaining certification under Authorized Economic Operator (AEO) schemes, which are not required for intra-EU trade. These costs are not insignificant: for example, Australia declined, in 2005, to enter into AEO schemes, because the costs were deemed too high for the value, although this position changed under the Abbott government.<sup>11</sup> For the UK, estimates of the cost of AEO certification range from £14,000 for medium-sized firms to £40,000 for larger companies with multiple facilities.<sup>12</sup>

<sup>10</sup> See the report on the latest effort to streamline the Canada-US border by Sinoski (2015).

<sup>11</sup> See Centre for Customs and Excise Studies (2014).

<sup>12</sup> HM Revenue and Customs (2009).

- Even for e-commerce transactions, based on eBay data, when a country joins a single market like the EU, the positive impact on e-commerce surpasses that of FTAs, pointing to the existence of border effects even for this generally micro level of trade (Ciuriak and Melin, 2014; Ciuriak et al., 2015).
- Small businesses, which have been free of borders in the EU environment, will bear the additional costs disproportionately since larger companies are already geared up for extra-EU trade.

Accordingly, the relatively costly Brexit border may be characterized as reflecting a world in which implementation lags vision, where well-intentioned schemes to create efficiencies nonetheless create red tape and inefficiency (the cost of which falls disproportionately on small business), where security trumps trade, and so forth. It is not unrealistic; many such borders exist, even between friendly regimes like Canada and the US – in the latter case despite the fact that more than one border initiative has been launched to streamline processes.

However, the UK and the EU27 are not necessarily condemned to experience such a border in the event of the UK's withdrawal from the single market. Under Brefta, we maintain our assumptions about documentation costs, but reduce our time costs by a quarter, calibrating our overall border costs to what has been estimated prevails for the EU-Swiss border (Minsch and Moser, 2006). Under a Brefta scenario, both the UK and the EU27 would have it in their mutual interest to minimize the disruption of bilateral trade, which would hand the advantage to third parties. The UK and the EU27, moreover, would have the unusual advantage of having no legacy border regime for trade in place. The trade border could be designed *de novo*, based on state-of-the-art information technology, risk management methods, and so forth. By incorporating features to minimize the costs of the new border to smaller businesses, it would also have a chance to preserve a high share of the existing cross-border integration that has evolved under the single market (see, e.g., the proposal to recast ROOs provisions to facilitate small business utilization of preferences, such as would obtain under Brefta, in Ciuriak and Bienen, 2014).

On this basis we assume the following: one-quarter of the time for customs clearance, the same documentation costs as under Brexit, and a 1% ROOs cost, which is at the lower bound of the range of estimates. This adds up to a total border cost as an AVE on imports of 2.31%.

### **3. Calibrating Goods NTBs under Brexit**

In the Brexit scenario, we assume that the UK starts with the EU regulatory regime and, thus, there is no shock to NTBs for goods trade immediately upon Brexit. However, over time, we assume some drift between the UK and the continent, in part based on the philosophical differences concerning regulation, which constitute one of the factors giving rise to consideration of Brexit in the first place.

As regards the manner in which the NTBs are introduced into the model, there are two options: an increase in rents or an increase in costs. As we work in a perfect competition modelling framework, which does not include cost mark-ups, we make a virtue of necessity in choosing the increased cost mode of NTBs, on grounds that the main elements of NTBs that would creep into UK-EU27 trade would likely take the form of additional marketing costs, including certification, as UK standards start to drift from continental standards. We use scores for Canadian NTBs of 0.080 for agriculture and 0.013 for manufactures to capture this effect (Petri et al., 2011; 66).

### **4. Constructing the Services and FDI NTBs**

To quantify the services NTBs, this study takes into account both actual reductions of barriers to cross-border services trade and the impact of binding existing market access. The methodology involves combining the reduction in actual barriers and the reduction of “water” (the difference between bound and applied market

access) into a composite NTB (following Ciuriak and Lysenko, 2016). The Brexit impacts on this composite NTB represent a percentage reduction in services market access barriers that reflects both applied restrictions and uncertainty. This percentage reduction in barriers is then applied to estimates of ad valorem trade cost equivalents developed for cross-border trade by Fontagne, Guillin and Mitaritonna (2011).<sup>13</sup>

It is well established that a reduction in uncertainty about market access stimulates trade (see, e.g., Handley and Limão, 2012). It follows that econometric estimates of the height of barriers to services trade (ad valorem equivalents or AVEs) reflect both the effect of actual restrictions and of policy uncertainty.

Ciuriak and Lysenko (2016) use a gravity modelling approach to identify the separate effects on services trade access from applied restrictions and water. They find that services trade responds positively but in-elastically to reductions in services trade barriers, as measured by the STRI, and that the response to actual restrictions is about twice as strong as the response to comparable reductions in “water.”

We note that both the STRI and “water” are measured on the basis of the same index and have approximately equal mean values in the Ciuriak and Lysenko dataset. This allows us to combine the effects into a single aggregate NTB, on the basis of the following aggregation formula:

$$\text{Total NTB} = \alpha(\text{STRI} + 0.5*\text{Water})$$

Where  $\alpha$  is a coefficient that scales the index-based measure to the measured AVEs. Alternative sets of AVEs have been measured by Jafari & Tarr (2014) for 103 countries and 11 sectors, on the basis of price wedges across countries; and by Fontagné et al. (2011) for 65 countries and 9 sectors, on the basis of gravity modelling which infers the height of barriers by the differences in actual trade versus expected levels, given gravity model relationships.

The STRI database covers the 34 OECD member countries plus Brazil, China, Colombia, India, Indonesia, Latvia, Russia and South Africa – 42 countries in all.

The STRI categorizes each sector under five policy areas:

- Restrictions on foreign ownership and other market entry conditions;
- Restrictions on the movement of people;
- Other discriminatory measures and international standards;
- Barriers to competition and public ownership; and
- Regulatory transparency and administrative requirements.

These individual policy areas are then broken down much more finely to capture the various issues confronted in each sector.

The calculation of Brexit impacts on UK’s services restrictions was coded for 18 sectors. These sectors and the mapping to the GTAP study sectors are listed in the table below:

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<sup>13</sup> [http://www.cepii.fr/PDF\\_PUB/wp/2011/wp2011-24.pdf](http://www.cepii.fr/PDF_PUB/wp/2011/wp2011-24.pdf)

**Table A3: Services sector mapping to GTAP sectors**

STRI Sector	GTAP	GTAP Sector No.
Construction	Construction	46
Distribution	Trade	47
Air Transport	Air transport	50
Maritime Transport	Sea transport	49
Rail freight transport	Transport nec	48
Road Transport	Transport nec	48
Courier	Transport nec	48
Telecommunications	Communication	51
Commercial Banking	Financial services nec	52
Insurance	Insurance	53
Accounting	Business services nec	54
Architecture	Business services nec	54
Computer	Business services nec	54
Engineering	Business services nec	54
Legal	Business services nec	54

**a) Calculating the liberalization shock for UK-US FTA**

The reduction to barriers to cross-border services trade is based on the impact of the binding measures in the Korea US FTA (KORUS) as a proxy for UK-US FTA. The approach is straightforward. First, we create a template based on the UK-US FTA's commitments. In developing the template, each article of the UK-US FTA is mapped to a measure in the STRI. Second, to calculate the policy shock for UK and US, the template is applied in light of their Schedule of commitments for cross border supply of services and establishment. For UK, we have taken into account the traditional reservations, most of which are mentioned in CETA.

If the template changes the answer to “not restrictive”, the contribution of that measure to the restrictiveness of the regime, which is based on its index weight, is removed. The Simulator recalculates the final score of the specific sector for the US or UK as the case may be. The percentage difference is taken as the degree of reduction of the existing barriers to services trade.

This methodology covers both horizontal and sector-specific commitments. The horizontal commitments stipulate conditions and restrictions that apply to all sectors of the economy. These measures include investment screening, limitations on board members and managers of firms, impediments on acquiring land and real estate, and so forth.

The specific commitments apply to a specific sector as indicated in the schedule. For instance, interest rate regulations pertain only to financial services. Some restrictions tend to impact some sectors more than other; for example, restrictions in public procurement have a particularly large impact on the construction sector in light of the importance of government demand for these services.

To measure the liberalization potential under the UK-US for cross-border services trade, we isolate those measures that affect Mode 1 (cross-border) specifically and those that affect all modes. These measures constitute a sub-index that can be referred to as the Cross-Border Services Restrictiveness Index (CBS-RI in our terminology). The corresponding sub-index for bindings is the GATS Cross-Border Services Restrictiveness Index or G-CBS-RI.

**b) Calculating the bindings shock**

To evaluate the impact of improved bindings under the UK-US, we compare the STRI as calculated based on GATS commitments (GATS Trade Restrictiveness Index or GTRI) and the STRI as bound under the UK-US FTA. The calculation of the binding shock is straightforward: the difference between the GTRI and the STRI

represents “water” in the bindings. The difference between “water” pre- and post- UK-US FTA constitutes the binding shock.

The table below sets out the detailed results of the coding of the impacts of the UK-US FTA on US and US’ STRI/GTRI.

**Table A4: UK Cross-border Services Shock for the UK-US FTA**

UK – Cross-border	Pre-UK-US FTA		Post- UK-US FTA		NTB Shock	GTAP	GTAP Sector Name
	CBS-RI	G-CBS-RI	CBS-RI	G-CBS-RI			
Construction	0.017	0.034	0.017	0.034	0.000	46	Construction
Distribution	0.000	0.009	0.000	0.009	0.000	47	Trade
Courier	0.061	0.072	0.061	0.072	0.000	48	Transport nec
Rail freight transport	0.000	0.096	0.000	0.096	0.000	48	Transport nec
Road Transport	0.053	0.070	0.053	0.070	0.000	48	Transport nec
Maritime Transport	0.056	0.151	0.056	0.133	0.009	49	Sea transport
Air Transport	0.140	0.309	0.140	0.309	0.000	50	Air Transport
Broadcasting	0.000	0.025	0.000	0.025	0.000	51	Communication
Motion Picture	0.013	0.101	0.013	0.101	0.000	51	Communication
Sound Recording	0.020	0.096	0.020	0.096	0.000	51	Communication
Telecommunications	0.052	0.052	0.036	0.036	0.024	51	Communication
Commercial banking	0.041	0.041	0.041	0.041	0.000	52	Financial services nec
Accounting	0.059	0.193	0.059	0.161	0.016	54	Business services nec
Architecture	0.012	0.162	0.012	0.114	0.024	54	Business services nec
Computer	0.120	0.199	0.120	0.199	0.000	54	Business services nec
Engineering	0.011	0.142	0.011	0.105	0.018	54	Business services nec
Legal	0.067	0.239	0.067	0.239	0.000	54	Business services nec

**Table A5: US Cross-border Services Shock for the UK-US FTA**

US – Cross-border	Pre-UK-US FTA		Post- UK-US FTA		NTB Shock	GTAP	GTAP Sector Name
	CBS-RI	G-CBS-RI	CBS-RI	G-CBS-RI			
Construction	0.073	0.089	0.060	0.076	0.019	46	Construction
Distribution	0.030	0.039	0.030	0.039	0.000	47	Trade
Courier	0.135	0.144	0.135	0.144	0.000	48	Transport nec
Rail freight transport	0.015	0.025	0.015	0.025	0.000	48	Transport nec
Road Transport	0.060	0.077	0.060	0.077	0.000	48	Transport nec
Maritime Transport	0.154	0.178	0.154	0.178	0.000	49	Sea transport
Air Transport	0.166	0.309	0.166	0.309	0.000	50	Air Transport
Broadcasting	0.019	0.019	0.019	0.019	0.000	51	Communication
Motion Picture	0.013	0.039	0.013	0.039	0.000	51	Communication
Sound Recording	0.020	0.060	0.020	0.060	0.000	51	Communication
Telecommunications	0.041	0.041	0.041	0.041	0.000	51	Communication
Commercial banking	0.037	0.037	0.037	0.037	0.000	52	Financial services nec
Accounting	0.066	0.183	0.066	0.152	0.016	54	Business services nec
Architecture	0.078	0.210	0.078	0.144	0.033	54	Business services nec
Computer	0.117	0.217	0.117	0.217	0.000	54	Business services nec
Engineering	0.094	0.189	0.058	0.134	0.064	54	Business services nec
Legal	0.039	0.183	0.039	0.145	0.019	54	Business services nec

**Table A6: UK Cross-border FDI Shock for the UK-US FTA**

UK – FDI	Pre-UK-US FTA		Post- UK-US FTA		NTB Shock	GTAP	GTAP Sector Name
	FDI-RI	G-FDI-RI	FDI-RI	G-FDI-RI			
Construction	0.000	0.034	0.000	0.000	0.017	46	Construction
Distribution	0.038	0.038	0.022	0.022	0.024	47	Trade
Courier	0.057	0.416	0.057	0.287	0.064	48	Transport nec
Rail freight transport	0.032	0.423	0.032	0.223	0.100	48	Transport nec
Road Transport	0.025	0.025	0.025	0.025	0.000	48	Transport nec
Maritime Transport	0.007	0.490	0.007	0.312	0.089	49	Sea transport
Air Transport	0.222	0.634	0.222	0.634	0.000	50	Air Transport
Broadcasting	0.095	0.718	0.095	0.718	0.000	51	Communication
Motion Picture	0.045	0.502	0.045	0.502	0.000	51	Communication
Sound Recording	0.000	0.301	0.000	0.301	0.000	51	Communication
Telecommunications	0.024	0.028	0.024	0.028	0.000	51	Communication
Commercial banking	0.036	0.063	0.036	0.063	0.000	52	Financial services nec
Accounting	0.036	0.036	0.036	0.036	0.000	54	Business services nec
Architecture	0.013	0.013	0.013	0.013	0.000	54	Business services nec
Computer	0.000	0.000	0.000	0.000	0.000	54	Business services nec
Engineering	0.000	0.000	0.000	0.000	0.000	54	Business services nec
Legal	0.000	0.387	0.000	0.387	0.000	54	Business services nec

**Table A7: US Cross-border FDI Shock for the UK-US FTA**

US – FDI	Pre-UK-US FTA		Post- UK-US FTA		NTB Shock	GTAP	GTAP Sector Name
	FDI-RI	G-FDI-RI	FDI-RI	G-FDI-RI			
Construction	0.034	0.067	0.034	0.067	0.000	46	Construction
Distribution	0.032	0.063	0.032	0.047	0.008	47	Trade
Courier	0.194	0.194	0.194	0.194	0.000	48	Transport nec
Rail freight transport	0.082	0.082	0.082	0.082	0.000	48	Transport nec
Road Transport	0.049	0.074	0.049	0.049	0.012	48	Transport nec
Maritime Transport	0.178	0.490	0.178	0.490	0.000	49	Sea transport
Air Transport	0.359	0.634	0.359	0.634	0.000	50	Air Transport
Broadcasting	0.263	0.288	0.263	0.288	0.000	51	Communication
Motion Picture	0.018	0.055	0.018	0.055	0.000	51	Communication
Sound Recording	0.000	0.000	0.000	0.000	0.000	51	Communication
Telecommunications	0.068	0.177	0.068	0.110	0.034	51	Communication
Commercial banking	0.081	0.081	0.081	0.081	0.000	52	Financial services nec
Accounting	0.018	0.054	0.018	0.018	0.018	54	Business services nec
Architecture	0.013	0.026	0.013	0.026	0.000	54	Business services nec
Computer	0.034	0.034	0.034	0.034	0.000	54	Business services nec
Engineering	0.013	0.027	0.013	0.027	0.000	54	Business services nec
Legal	0.024	0.024	0.024	0.024	0.000	54	Business services nec





LEGATUM  
INSTITUTE

SPECIAL TRADE  
COMMISSION



JUNE 2017

# Developing a True Transatlantic Partnership

—a High Standard Trade Agreement  
to Propel the Global Economy

by Shanker A. Singham, Victoria Hewson,  
and Radomir Tylecote

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## 1. EXECUTIVE SUMMARY

### THE BACKDROP

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- 1.1 Global growth has been stalling for several years, with measures of industrial output falling since before the 2008 financial crisis. Deep trade liberalisation can be a catalyst to economic growth again, such as through a UK-US free trade agreement ("FTA"). Such an agreement has been mooted since the early 1990s. There is a Trans-Atlantic Trade and Investment Partnership ("TTIP") between the US and the EU currently under negotiation (although not actively at present), which the UK would no longer be a part of once it leaves the EU. Without the restrictions associated with EU membership, the UK has an opportunity to negotiate a deep and effective trade agreement with the US, including in areas that previously have been too politically difficult for negotiation.
- 1.2 The UK and the US already have relatively free trade in terms of market access for goods, with relatively low levels of tariffs generally. However, the terms of an agreement could go further and seek to reduce non-tariff barriers and address behind the border barriers and regulatory distortions (which we have classified as anti-competitive market distortions ("ACMDs")), which would promote greater economic growth.
- 1.3 Such an agreement will have a number of challenges. UK consumers have already professed concerns about lower regulatory standards in agricultural products and privatisation of the National Health Service ("NHS") under an UK-US FTA, and the UK will have to manage such interest groups carefully. The US administration and president on the other hand, have expressed a mercantilist approach to trade, accompanied by "Buy American" rhetoric. Further, in previous negotiations, such as in TTIP, the US has shown an unwillingness to negotiate on certain areas that would be priorities for the UK, such as financial services. While such matters present challenges, a shared commitment to open trade and removal of distortions to drive competitive markets will be a strong starting point for negotiations. Negotiations on a free trade agreement can begin immediately as a matter of law; there are no impediments from Article 50 as long as the UK is following the principle of sincere cooperation with the EU. UK ministers should start engaging with US counterparts immediately to discuss the opportunities for collaboration, and prioritising areas for negotiation and agreement.

### A UK-US AGREEMENT CAN ACHIEVE MORE BARRIER REDUCTION THAN TTIP

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- 1.4 **Regulatory promulgation.** In a UK-US agreement, there is an opportunity for both parties to agree regulatory promulgation mechanisms, which ensure that new regulations are pro-competitive. This should move away from the precautionary principle adopted by the EU, which, when applied, requires

1. Shanker A. Singham, *Freeing the Global Market: How to Boost the Economy by Curbing Regulatory Distortions* <http://www.cfr.org/world/freeing-global-market-boost-economy-curbing-regulatory-distortions/p29123>
2. Nothing in Article 3(1) of the Treaty for the Functioning of the European Union or Article 50 of the Treaty on European Union ("TEU") prevent a member state in the process of exiting the EU from engaging in trade negotiations with third countries as long as no legal commitment enters into force prior to the exit and the duty of sincere cooperation under Article 4 TEU is respected.

the producer / importer to prove absence of danger. As part of this process, the US and the UK could undertake joint analysis of current domestic markets to review and remove existing barriers to trade and investment. This could work in parallel to the review by US federal agencies of regulations for repeal, replacement or modification required under the recent executive order signed by President Trump.

- 1.5 **Food and Agriculture.** As part of any negotiation, the US will inevitably seek greater openness on agricultural products. The UK will have to commit this to an extent and should seek greater commitments in other areas, particularly services, in return. The US has also expressed concerns with the so-called Meursing table, which is the EU's special tariff rate for imported products containing milk protein, milk fat, starch and sugar content. The UK could offer to reform or eliminate this. The US, on the other hand, has domestic distortions through subsidies and similar programmes, alongside tariffs, that the UK would seek to address in an FTA.
- 1.6 **Regulatory barriers.** There needs to be agreement on labelling standards, noting that in many areas, the EU, and therefore current UK, standards exceed those of the Codex Alimentarius General Standards, e.g. in fishing and aquaculture, as well as agreement on use of geographical indications. The most difficult area will be agreement on application of standards. The agreement should specify use of appropriate, proportionate standards for agricultural products, based on sound scientific evidence, and remove unnecessary Sanitary and Phytosanitary ("SPS") and Technical Barriers to Trade ("TBT") measures, and agree on eligibility, authorisation and assessment processes. This in particular can be politically challenging, and the UK will have to manage concerns from interest groups.
- 1.7 **Government Procurement.** The US has barriers in government procurement, through the Buy American Act ("BAA"), which applies to federal government procurement of supplies and construction materials. This has recently been reinforced through President Trump's "Buy American, Hire American" executive order which requires a review of current compliance and use of waivers. This will make an agreement in this area potentially challenging, and the UK will potentially have to seek special arrangements in relation to government procurement.
- 1.8 **Financial Services.** The UK and the US are relatively open on financial services in terms of market access. Greater regulatory co-ordination and recognition of home state regulation could deliver significant gains to both parties. In the TTIP negotiations the US expressed an unwillingness to include regulatory co-ordination in financial services in trade negotiations and so this may be an area of difficulty. However, the US has, for example, previously signed a mutual recognition agreement with Australian regulators in 2008 for mutual recognition in certain areas of financial services and deferred compliance measures are in place with the EU, so there is precedent for such an approach.

- 1.9 **Standards.** Standard setting currently is very different between the UK and the US, and was a major stumbling block in the TTIP negotiations, but this is largely because of the EU process. The challenge here will be for the UK to develop a new conformity assessment system for standards that can support the creation of mutual recognition agreements in new trading arrangements, including with the US and the EU. This could be the development of a private-led ecosystem with lighter state oversight, starting with mutual recognition agreements across different sectors that had been initially discussed between the US and the EU, including information technology, telecommunications products attached to public networks, medical devices, electrical safety, electromagnetic interference, pharmaceuticals, amongst others.
- 1.10 **Other Areas.** There are several other areas where the UK and US have common goals and will have to work to align regulations going forward, which for the UK, will potentially mean a move away from current EU rules. For example, both the UK and the US are committed to strong intellectual property protection, but would have to address areas such as use of geographical indications. There are public concerns about an agreement with the US leading to the privatisation of the NHS. It is unlikely that large or significant parts of the NHS would be opened up to provision by foreign companies. Where there is private provision, US providers have already invested in the area, and there is scope for the US to invest in the private healthcare market. However, the substantial barriers posed by the socialised healthcare system are unlikely to change, and the UK could easily reserve this area in services negotiations.

#### UK-US FTA AS PART OF A WIDER UK TRADE POLICY

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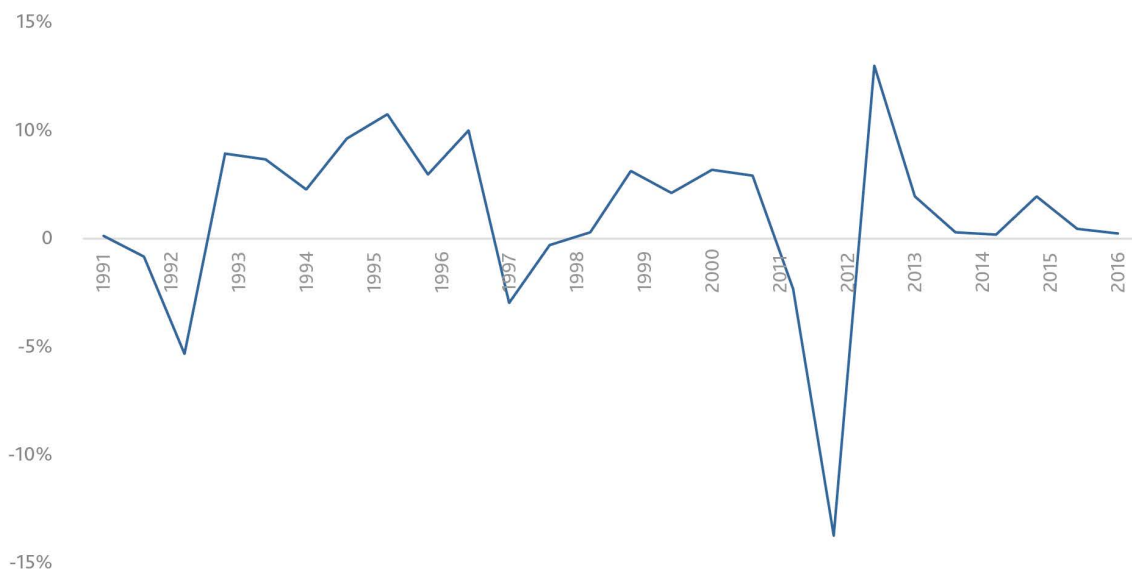
- 1.11 The concurrent negotiations with the US and the EU will present both opportunities and challenges. The UK sits between the US and the EU in many areas of law and regulation, and concurrent negotiations mean that the UK can act as a bridge in certain key areas. The challenges are primarily in areas where the EU and US regulate in very different ways, and it may not be possible in certain cases to have an agreement that works for both parties and enables a single supply chain across the US-UK-EU region. In financial services, for example, to ensure that the UK can continue to transact business in the EU without being locally licensed and supervised, there will have to be some mutual recognition and ongoing co-ordination of regulation, especially prudential regulation. The question is whether this can also be extended to include the US and other countries. The key will be to agree arrangements that are enabled by MRAs across the UK, US and EU while the parties are also working to ensure global standards develop in a more consumer welfare-enhancing direction.
- 1.12 This agreement can be a stepping-stone to working with other like-minded countries to make progress on ACMDs and behind-the-border barriers. We have separately proposed a “Prosperity Zone”, a plurilateral agreement amongst countries with similar goals of open trade, competition on the merits as an organising principle, and property rights protection. This could be a starting point to addressing the global economic growth challenges.
- 1.13 The UK-US FTA is also important because it will ensure that the UK does not become by default “locked in” to EU standards and product regulation such that it cannot be flexible in negotiating FTAs with other countries.

## 2. THE ECONOMIC CONTEXT FOR BREXIT

Below: Figure 1: Index  
of Industrial Production  
—Advanced Economies  
(growth rate)

Source: IMF (2017)

- 2.1 The global economy has been stalled for over a decade. Growth in measures of economic output and wealth creation such as industrial output has fallen significantly since before the global financial crisis. As illustrated below, there was relatively strong growth in the IMF's index of industrial production for advanced economies in the mid-late 1990s. Output fell with the 2001 recession, following which there was more subdued rates of growth. This has worsened since the financial crisis, with little to no growth in industrial output in recent years. In the five years preceding the crisis, the average annual growth rate for advanced economies in the IMF's index of industrial production was 2.4%, compared to an average annual growth rate of 0.9% after 2010.<sup>3</sup>
- 2.2 In GDP terms, the OECD noted in 2016<sup>4</sup> that growth was flat in advanced economies and slowing in emerging economies that had been the 'global locomotive' since the global financial crisis. Secretary General Angel Gurría called for "comprehensive policy action... to ensure that we get off this disappointing growth path and propel our economies to levels that will safeguard living standards for all".



3. IMF (2017), "Prices, Production, Labor and Population", available at <http://data.imf.org/?sk=6AC22EA7-E792-4687-B7F8-C2DF114D9FDC&sid=1439776194766>, accessed on 30 March 2017.
4. OECD Global Interim Economic Outlook, March 2017 <http://www.oecd.org/economy/economicoutlook.htm>

- 2.3 While the reasons for this slump are myriad, it is notable in this context that with the exception of the recently concluded trade facilitation agreement, no multilateral trade agreement round has been concluded for twenty-two years, a longer period than at any other time in the history of the World Trade Organization (“WTO”) or its predecessor, the General Agreement on Tariffs and Trade (“GATT”). Indeed, an argument can be made that the consensus in support of deeper trade liberalisation was in deep trouble as early as prior to the 1999 WTO Seattle meeting protests.
- 2.4 The early and enduring success of the GATT means that tariffs have come down but behind the border barriers and anti-competitive market distortions (“ACMDs”) have become the major obstacles to free trade and competitive markets, pre-requisites for economic growth. ACMDs can only be dealt with through deeper, more liberalizing agreements among nations, either at a multilateral or regional/bilateral level. These ACMDs particularly affect services exports, which are disproportionately affected by regulatory barriers. We argue that addressing these matters will be key to the success of policies that seek to promote growth and wealth creation.
- 2.5 What are the blockages in the trade agenda? The attempt to deepen trade liberalisation through the so-called Singapore Issues failed in the late 1990s, and the attempt to launch a new trade round in 1999 met with disaster in Seattle when the US raised the issue of trade sanctions for labour violations, a position which was anathema for developing countries. An argument can certainly be made that the only reason the Doha Round was launched was because the launch meeting in Doha, Qatar followed the terrorist attacks on September 11th, 2001. Little progress was made and it is widely (though not universally) considered that the Doha Development Agenda (“DDA”) was effectively killed off at the Nairobi Ministerial Conference in December 2015 and the WTO needs to move on. Worse, the DDA distracted WTO members from developing the built-in agenda on services towards deeper liberalisation.
- 2.6 Other agreements which were attempts to introduce more trade liberalising measures, such as the Trans-Pacific Partnership (“TPP”) and Trans-Atlantic Trade and Investment Partnership (“TTIP”) have proved impossible either to progress, or to ultimately ratify, whether due to adverse domestic politics or substantive negotiation differences. Protectionist and populist impulses have made traditional trade liberalisation very difficult to accomplish.
- 2.7 There is a need for a deeply liberalising agreement between countries that agree on the fundamental pre-requisites for a growing economy. There are very few such countries in the world, but we have suggested in our paper Trade Tools for the 21st Century<sup>5</sup> which countries are broadly in this category.<sup>6</sup> Of these countries the US has made it clear that it wishes to have a trade agreement with the UK, and the purpose of this paper is to evaluate what that deal might look like and what benefits it might confer on people in both countries.
- 2.8 A trade agreement between the UK and the US has been mooted for a considerable period,<sup>7</sup> but has not been possible because of the UK’s membership of the EU which has precluded it from negotiating an agreement with another customs territory. Now that the UK is about to leave the EU, trade agreements with other countries are possible. The UK is able to do a considerable amount of preparation prior to actually leaving the EU. This work can and should begin in earnest for a deal with the US.

5. <http://www.li.com/activities/publications/trade-tools-for-the-21st-century>

6. They are US, Australia, Canada, Singapore, New Zealand, and possibly Switzerland.

7. See for example calls in 2000 by Senator Phil Gramm for the UK to join NAFTA <http://www.economist.com/node/302480>



- 2.9 Negotiating a deal with the US at the same time that the deal is being negotiated with the EU will present both opportunities and challenges. A UK-US trade agreement could be a comprehensive agreement, committing the parties to high standards of openness and competition, which makes progress on behind the border barriers which particularly afflict UK and US service providers and spur the progress on these matters more widely.
- 2.10 This can be accomplished by:
- 2.10.1 greater border measure reduction;
  - 2.10.2 improving competitive markets by eliminating ACMDs; and
  - 2.10.3 improving property rights protection.
- 2.11 This paper aims to address how the US and the UK should seek to reduce behind the border barriers and domestic anti-competitive market distortions generally, followed by brief analysis of existing barriers in the US and UK markets and how such barriers might be reduced or removed entirely in a free trade agreement between the two parties, focusing in particular on the structural matters of product standards and mutual recognition. Finally, we consider how this process between the UK and the US fits into both sides' wider trade policy and political considerations—in the case of the US, NAFTA and the Trump administration's trade policy goals, and in the case of the UK, establishing an independent trade policy, including a deep and special trade relationship with the EU (we have described a four-pillar approach to building the UK's trade policy in our paper "A Blueprint for UK Trade Policy").<sup>8</sup>
- 2.12 A non-exhaustive list of examples of the existing UK/EU and US barriers is contained in Appendix 1.

8. <https://lif.blob.core.windows.net/lif/docs/default-source/default-library/170427-final-trade-blueprintweb.pdf?sfvrsn=0>

### 3. UK AND US TRADE RELATIONSHIPS

- 3.1 The US and UK have historically enjoyed close economic and diplomatic relations. These ties were strengthened during the First and Second World Wars and the post-war period. The relationship goes beyond economics and politics. They are ties of shared values, shared culture and a commitment to free trade, free markets, competition as an organising principle for the economy, and free and open liberal democracy. No matter who the leaders of the UK and US are, these ideas are so embedded that they cannot easily be removed.
- 3.2 Today, the US is Britain's largest single export market, and its second-largest import supplier (behind Germany).<sup>9</sup> The US is also the single largest source of, and destination for, foreign direct investment for Britain.<sup>10</sup> Both countries were founding entities in the GATT system itself which did more to reduce border barriers than any other single venture.
- 3.3 Since the 1980s, the special relationship between the UK and US has incorporated a desire to have closer economic ties between the two countries. The UK acceded to the European Economic Community in 1973, at some considerable cost to the Commonwealth countries, and the preferences that they had enjoyed. As part of the European customs union, the UK has not been able to consider even the most basic agreement with the US to reduce border barriers except through the EU. That said, as noted above, many US members of Congress have called for a UK-US agreement of some sort. Some have called for the UK to accede to NAFTA, some for a bilateral agreement (even though the UK cannot enter one, or accede to any other agreement as long as it is part of the customs union).
- 3.4 A Transatlantic Free Trade Area or Agreement ("TAFTA") has been floated since the early 1990s by proponents of free trade on both sides of the Atlantic. TTIP is the current proposed US-EU trade deal. The High Level Group on Jobs and Growth formally recommended that the US begin negotiations with the EU in February 2013.<sup>11</sup> The Council of the European Union issued Directives for the Negotiation on the Transatlantic Trade and Investment Partnership between the European Union and the United States of America in June 2013; negotiations were formally commenced in July 2013.<sup>12</sup> After fifteen rounds of negotiation (from July 2014 to October 2016), talks have stalled. The US and EU have been unable to come to agreement on any of the 27 proposed chapters. Agriculture, standards, regulatory coherence and public procurement are areas of particular difficulty. If TTIP is revived,<sup>13</sup> the same issues that prevented progress will still be present.
- 3.5 There have been objections to the TTIP in the EU. Sigmar Gabriel, German Minister for Economic Affairs and Vice Chancellor, gave an interview in late August 2016 in which he proclaimed the TTIP negotiations to be "de facto failed", adding that "nothing is moving" because the "Europeans did not want to subject ourselves to American demands".<sup>14</sup> His comments came

9. <https://www.ons.gov.uk/economy/nationalaccounts/balanceofpayments/articles/ktradeandinvestmentrelationshipwiththeunitedstatesofamerica/2016>

10. <https://www.ons.gov.uk/economy/nationalaccounts/balanceofpayments/articles/theuktradeandinvestmentrelationshipwiththeunitedstatesofamerica/2016>

11. [http://trade.ec.europa.eu/doclib/docs/2013/february/tradoc\\_150519.pdf](http://trade.ec.europa.eu/doclib/docs/2013/february/tradoc_150519.pdf)

12. <http://data.consilium.europa.eu/doc/document/ST-11103-2013-DCL-1/en/pdf>

13. See Paul Ryan's speech on 19 April 2017 as recited at <https://www.theguardian.com/us-news/2017/apr/19/paul-ryan-london-visit-us-uk-trade-agreement-brexit>

14. <http://www.dw.com/en/germanys-vice-chancellor-gabriel-us-eu-trade-talks-have-failed/a-19509401>

on the heels of a series of large protests in Germany against TTIP, and the Comprehensive Economic and Trade Agreement (“CETA”) with Canada. On the American side, Senate Leader Mitch McConnell (R-Ky.) and other prominent Republicans have criticised European treatment of agriculture. It is thought that one major advantage of a US-UK FTA would likely be more relaxed dynamics on the regulation and trade of agricultural products.<sup>15</sup>

- 3.6 Key House and Senate Republicans, as well as President Trump, have indicated that they support and expect a forthcoming free trade agreement between the UK and US. Then-candidate Trump said on the 24th of June 2016 that Britain “will always be at the front of the line”, in reference to President Obama’s warning that a post-Brexit Britain would be “at the back of the queue” for future US trade deals.<sup>16</sup> The political climate in Washington is such that President Obama’s opposition to Brexit and a subsequent US-UK trade deal is likely to generate support for such a deal amongst congressional Republicans at least through the end of the 115th Congress. Senators Cotton (R-Al.), Isakson (R-Ga.), Hatch (R-Ut.), Corker (R-Tn.), and Lee (R-Ut.) have all publicly expressed support for a US-UK FTA; Senators Cruz (R-Tx.), Lee (R-Ut.) and Sessions (R-Al., US Attorney General) issued a letter of condemnation to President Obama before the UK Brexit referendum vote for interfering in British sovereignty.<sup>17,18</sup>
- 3.7 President Trump has delivered top line messages on trade that are hostile to countries that distort their markets in anti-competitive ways. For example, he is highly critical of China’s domestic practices which distort markets and artificially lower the cost of certain Chinese producers in markets around the world. He rightly identifies that global trade rules have not done a good enough job of penalising these distortions. Trump’s America First rhetoric is an attack on trade policies he finds unfair to American businesses, and American workers. This is not especially unlike the policies adopted by other American presidents even if the rhetoric is more strident. He has also vowed to punish those companies who choose to move jobs outside of the United States; in one high-profile case, he convinced Indiana-based Carrier to keep 800 jobs in the US, rather than moving them to Mexico. However, on trade measures one can start to see the beginnings of how President Trump’s high level messages will be interpreted by a Republican House of Representatives and Senate. In the case of the border tax proposal, one of the reasons that large US exporters support the Ryan proposal is that many countries impose a value added tax (“VAT”) on imports, whereas the US does not (although the US does impose varying state-local sales taxes). Hence US exporters face a cost increase in external markets which their competitors do not face in the US. In this context the VAT which can be quite high (20% and above in many EU member states, as high as 27%, in Hungary for example) represents a significant distortion. As we have discussed in our approach to ACMDs and potential policy responses, a border tax may be a way of correcting this distortion.<sup>19</sup>
- 3.8 President Trump has initiated renegotiation of NAFTA.<sup>20</sup> Such a re-negotiation could incorporate elements of an anti-distortion model (like the Prosperity Zone described below). This would deliver solutions satisfactory to US, Canadian, and Mexican consumers, businesses, and workers. A simple imposition of tariffs on all goods coming from Mexico (including from American companies with production bases in Mexico) would be highly distortive and unproductive, and

15. <http://www.politico.com/tipsheets/morning-trade/2016/02/major-tpp-political-players-talking-warren-hits-tpp-ahead-of-signing-spring-showers-bring-ttip-flowers-212510>

16. See Paul Ryan’s speech on 19 April 2017 as recited at <https://www.theguardian.com/us-news/2017/apr/19/paul-ryan-london-visit-us-uk-trade-agreement-brexit>

17. <http://www.politico.eu/article/the-bright-side-of-brexit-us-uk-bilateral-bliss/>

18. [http://www.cruz.senate.gov/files/documents/Letters/20160620\\_BrexitLetter.pdf](http://www.cruz.senate.gov/files/documents/Letters/20160620_BrexitLetter.pdf)

19. <http://www.li.com/activities/publications/trade-tools-for-the-21st-century>

20. <http://www.nbcnews.com/news/us-news/white-house-trump-says-u-s-will-not-withdraw-nafta-n751731>

likely lead to the loss of American jobs, but measures to deal properly with distortions would have an entirely different effect.

- 3.9 President Trump has talked publicly about a free trade agreement with the UK, and has shown an aversion to multilateral and regional agreements. This is based on a concern that these agreements are based on a lowest common denominator, and are with countries with considerably different labour and environmental standards. However, it is feasible that an agreement with a like-minded group of countries would be met with support by the Trump administration. Initially any US agreement will likely be on a bilateral basis with other countries, and the UK will be no exemption. However, the ultimate destination of the agreement could still be a broader, platform agreement such as the Prosperity Zone set out below.

## 4. HOW CAN THE US AND THE UK MAKE PROGRESS ON BEHIND THE BORDER BARRIERS AND ACMDs?

- 4.1 Progress can be made on behind-the-border-barriers and ACMDs by gathering like-minded countries who believe in competition on the merits as an organising economic principle.
- 4.2 Ensuring that those countries that believe in these concepts come together to pursue these ends would be a positive step forwards. We believe these like-minded countries can come together to form a prosperity zone (the "Prosperity Zone"). The concept of a Prosperity Zone was first floated during Gov. Mitt Romney's 2008 presidential campaign.<sup>21</sup> The Prosperity Zone recognises that the nations of the world are not all equally committed to open trade, competition on the merits as an organising principle, and property rights protection. The ultimate goal of the Prosperity Zone is to effect a global reduction in ACMDs. As described in *Trade Tools for the 21st Century*, ACMDs exist to

"limit the number and range of competitors; to restrict the ability of individual companies to compete by artificially increasing their costs or artificially lowering competitors' costs; and to favour state-owned enterprises",

and are proliferated through the use of:

"exclusive distribution rights, licencing regimes, corrupt public procurement practices, geographical/labour limitations, scientifically unsound standard-setting, limitations on direct-to-consumer advertising, forced production shifting, exemptions from onerous regulations for 'favoured' corporations, and outright subsidies".<sup>22</sup>

- 4.3 While the GATT has successfully eliminated many at-the-border tariff barriers, many behind-the-border barriers still exist as ACMDs. The examples of ACMDs listed above are often the most difficult areas to negotiate in trade negotiations. The General Agreement on Trade in Services ("GATS") agenda initiated after the Uruguay Round in 1994 has not materially progressed barriers in services trade, as was one of the goals of the so-called Built-In Agenda. The services offers made by countries as part of the Built-in Agenda are very weak and minimally cover the sectors. Only one sector has been properly dealt with—telecommunications, through the GATS Telecommunications Annex and the related Reference Paper on Competition Safeguards. After the 1997 Annex on Telecommunications, the members intended that financial services and other sectors would follow.
- 4.4 We have previously laid out in *Trade Tools for the 21st Century* the gains which would be achievable under a full reduction of tariff and non-tariff barriers in a Prosperity Zone which included the UK, US, Switzerland, Canada, Hong Kong SAR, Singapore, New Zealand and Australia. Our calculations showed that roughly 2-3% year-on-year growth in gross world product ("GWP") would be possible under this framework. These gains are based on our

21. Referred to as the Reagan Economic Zone <http://www.politifact.com/truth-o-meter/statements/2012/may/17/mitt-romney/mitt-romney-once-distanced-himself-ronald-reagan-n/>

22. <https://lif.blob.core.windows.net/lif/docs/default-source/publications/trade-tools-for-the-21st-century-pdf.pdf?sfvrsn=4>

methodology for measuring ACMDs.<sup>23</sup> We assume that the Prosperity Zone leads to a 30% reduction in ACMDs over a fifteen-year period in these countries.

- 4.5 As the US, Canada and Switzerland retain significant agricultural distortions, it would be best to begin negotiations with those countries who carry the least defensive baggage in agriculture: the UK (subject to jettisoning the Common Agricultural Policy ("CAP")), Australia, New Zealand and Singapore. As the TPP has been abandoned by the US, these nations will be eager to re-engage in a more promising round of negotiations. Once the Prosperity Zone had been ratified by those four nations, the process to accede the US, Canada, and perhaps Switzerland, could begin, with an eye to the further accession of several like-minded Pacific Alliance countries, including Chile, Colombia, Peru and Mexico. Another relatively expeditious action would be the UK acceding to and then building on the P-4 agreement. In this case, Chile would already be a member (along with New Zealand, Singapore and Brunei) and accessions of the Pacific Alliance countries would be possible.
- 4.6 A bilateral UK-US agreement should be deeply liberalising and a stepping-stone to a Prosperity Zone. As soon as possible, the UK should agree a memorandum of understanding with the US regarding intent to sign a high-standards free trade agreement after the UK has formally exited the European Union. Discussions in relation to this FTA could begin immediately; there is no legal reason to wait for the Article 50 process to be concluded before commencing negotiations.<sup>24</sup> The issue is more of a political matter. The US will have to determine whether it is worthwhile negotiating towards an agreement with the UK, based on how much they believe that the UK will emerge at the end of the Article 50 process (i.e. by April 1, 2019) fully outside of the Customs Union and no longer a member of the EEA (which at the time of writing is the stated expectation of both the British government and the EU institutions). In this case, the UK will simply be a third country negotiating an FTA with the EU as is the case for many countries that it is negotiating FTAs with.

23. See Shanker A Singham and Molly Kiniry *Introduction to Anti-Competitive Market Distortions and the Distortions Index* (September 2016)

24. As acknowledged in paragraph V of the Council of the European Union's European Council (Art. 50) guidelines following the United Kingdom's notification under Article 50 TEU issued on 29 April 2017 and see also Francis Hoar, *The United Kingdom's Right to Negotiate Free Trade Agreements before leaving the European Union* <http://www.lawyersforbritain.org/files/uk-right-to-negotiate-free-trade-agreements-before-leaving-eu.pdf>

## 5. SCOPING AN FTA BETWEEN THE US AND UK

- 5.1 In general terms, except in agriculture, tariffs between the US and UK are low. The major impediments are in the regulatory and behind the border areas. It is here where a US-UK agreement can be most effective.
- 5.2 Appendix 1 contains an inventory of barriers in both the US and UK which each party's businesses face in the other's market. Trade in services faces barriers on both sides of the Atlantic and regulatory differences cause significant costs and distortions in goods and services trade. More particularly, the US barriers of most interest are in the following broad categories:
- Agricultural subsidisation
  - 'Buy America' and public/defence procurement
  - Financial services
- 5.3 The major UK barriers are broadly in the following categories
- Food standards and SPS
  - Product standards and regulation
  - Data protection
- 5.4 We have set out below an analysis of these barriers and how they could begin to be addressed within the scope of an FTA between the UK and the US.

## 6. IMPROVING REGULATORY PROMULGATION TO DELIVER CONSUMER WELFARE

- 6.1 While an agreement on tariffs in industrial goods between the US and UK should be relatively straightforward, there will be more issues in the regulatory area. The UK is currently bound by EU regulation. As this will be the starting point post-Brexit (because the Great Repeal Bill will transpose substantially all of EU regulation into UK law),<sup>25</sup> any discussion of a regulatory agreement between the US and the UK must start with EU regulation. The regulatory promulgation in the EU includes the precautionary principle. Although not formally defined and used in the Treaty for the Functioning of the European Union (“TFEU”) only in the context of environmental regulation, the precautionary principle is an important influence on the regulations in the EU through case law and practice. As noted in a Commission Communication in 2000,<sup>26</sup> it may be invoked “when a phenomenon, product or process may have a dangerous effect, identified by a scientific and objective evaluation, if this evaluation does not allow the risk to be determined with sufficient certainty”, and while it is not to be extended generally to all products and processes placed on the market, where action is taken under the precautionary principle (which will be determined by authorities on a risk basis), a producer or importer may be required to prove absence of danger. The principle is applied to not just environment (as provided in the TFEU), but to conservation policy, food legislation and human, animal and plant health. While the precautionary principle is recognised in the WTO Agreement on the Application of Sanitary and Phytosanitary Measures (“SPS Agreement”), the approach in the EU goes far beyond what is required and recognised under the WTO.
- 6.2 The precautionary principle is not widely deployed in regulatory promulgation in the US and this is part of the reason for wide regulation divergence between the UK/EU and the US. The guidance given to US regulatory authorities in Circular A-4 from the Office of Management and Budget<sup>27</sup> states that cost-benefit analysis is a primary tool for regulatory analysis and states a number of considerations and presumptions that should form part of such analysis. It specifically counsels against “conservative assumptions and defaults (whether motivated by science policy or precautionary instincts) [which] will be incompatible with benefit analysis as they will result in benefit estimates that exceed the expected value”. This is in line with the SPS Agreement, which states that any sanitary and phytosanitary (“SPS”) measures implemented must be based on a risk assessment. Where there is no sufficient scientific evidence available, only provisional measures are permitted, accompanied by an obligation to seek to obtain additional information necessary for a risk assessment, and to review the provisional measure within a reasonable period of time.<sup>28</sup>
- 6.3 In the US-UK agreement, there is an opportunity for both parties to agree a regulatory promulgation mechanism that ensures that new regulations are pro-competitive by setting up a system that builds on the process outlined in Circular A-4 and the UK’s domestic equivalent

25. The United Kingdom’s exit from and new partnership with the European Union White Paper <https://www.gov.uk/government/publications/the-united-kingdoms-exit-from-and-new-partnership-with-the-european-union-white-paper>

26. Commission Communication (COM (2000)1)

27. <https://obamawhitehouse.archives.gov/sites/default/files/omb/assets/omb/circulars/a004/a-4.pdf>

28. [https://www.foodwatch.org/fileadmin/Themen/TTIP\\_Freihandel/Dokumente/2016-06-21\\_foodwatch-study\\_precautionary-principle.pdf](https://www.foodwatch.org/fileadmin/Themen/TTIP_Freihandel/Dokumente/2016-06-21_foodwatch-study_precautionary-principle.pdf)



cost benefit analysis process undertaken in carrying out impact assessment of legislation, set out in the Green Book, and moves away from the precautionary principle where appropriate. The UK Competition and Markets Authority (“CMA”) is already in the forefront of doing market studies that look at regulations that have anti-competitive effects, but we would argue that on both sides of the Atlantic many of these reports and analysis do not go far enough in terms of specific analysis of regulations and their consumer welfare effects. For example, the CMA’s analysis of the banking sector in the UK does recognise that capital adequacy rules can have negative competitive effects, it also says that these are prudential matters related to the sectoral regulator which the competition agency should not deal with. These sectoral studies can be converted into specific regulatory analyses. The problem is not that regulations are too many or even that costs of compliance for businesses are too great, but rather that their effect is anti-competitive, and this depends on the nature of specific regulations.

- 6.4 New Zealand and Australia have historically collaborated together via a productivity commission to analyse their existing domestic markets with the ultimate aim of proposing recommendations for a package of measures to enhance cooperation between Australia and New Zealand in relation to their competition and consumer protection regimes.<sup>29</sup> A similar joint analysis conducted by the UK and the US could lead to the removal of existing barriers and obstacles to trade and investment. On 24 February 2017, President Trump signed an executive order<sup>30</sup> that requires federal agencies to designate a Regulatory Reform Officer and set up a Regulatory Reform Task Force to improve implementation of regulatory reform initiatives and identify regulations for repeal, replacement or modification that impact on jobs, are outdated, unnecessary or ineffective, impose costs greater than benefits. This could be done in collaboration with the UK’s Regulatory Policy Committee’s work in this field.<sup>31</sup>

29. *Australian and New Zealand Competition and Consumer Protection Regimes*, Productivity Commission Research Report (December 2016)

30. <https://www.whitehouse.gov/the-press-office/2017/02/24/presidential-executive-order-enforcing-regulatory-reform-agenda>

31. <https://www.gov.uk/government/organisations/regulatory-policy-committee>

## 7. FOOD AND AGRICULTURE

### TARIFFS AND QUOTAS

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- 7.1 To the extent that part of what the US will need is access to the UK's agriculture market, the UK will have to be committed to more open trade in agricultural products. There are many products that the UK does not produce, or produce products that are directly competitive or substitutable with them. In these cases, the UK could simply reduce or eliminate its tariffs and quotas unilaterally. To do so would not affect UK farming interests but would immediately serve to lower any food price inflation that affects the UK on exit from the EU, and send a strong message to trading partners that the UK is serious in its commitment to becoming a leader in the global trade agenda. Some examples of such products which the UK does not produce are set out in section 7.4.
- 7.2 The US has also expressed its concern with the so-called Meursing table, which is the EU's special tariff rate for imported products containing milk protein, milk fat, starch and sugar content. The UK could offer to eliminate the Meursing Table in total and simply categorise products, rather than their recipes.
- 7.3 There are also many distortions in the US agriculture sector, through subsidies and similar programmes, and the US operates TRQs on 44 lines of agricultural products, that could usefully be addressed in a US/UK FTA.
- 7.4 The UK can lower agricultural tariffs on a number of products without affecting domestic producers for example:
- 7.4.1 **Rice:** The UK does not produce rice but does have processing facilities. It is therefore very much in the UK's interest to lower or eliminate the rice tariff. The US has previously requested that the EU lower its tariffs on brown rice in the TTIP agreement. This is something the UK could offer immediately.
- 7.4.2 **Peaches, Citrus Fruits and Olives:** The US has complained about EU hidden subsidies for these industries. The UK can eliminate any TRQs for all these products, as well as remove any provision for payments to producers of these products (which are not produced in the UK).
- 7.5 The US operates TRQs in 44 lines of agricultural products including products that the UK produces such as dairy, beef and animal feed, which the UK would wish to have reduced or eliminated entirely for UK exports to the US. The UK would likely seek to follow the NAFTA model for its agricultural products, which provided for duty-free and unlimited access for beef amongst US, Canada and Mexico.<sup>32</sup>

<sup>32</sup> <https://www.fas.usda.gov/data/review-us-tariff-rate-quotas-beef-imports>

- 7.6 The US also subsidises agricultural production extensively, distorting the market in favour of domestic producers and certain crops. For example, the US provides a Federal Crop Insurance program to American farmers, which has been criticised for encouraging farmers to gamble on risky plantings and marginal acres at a significant cost to the US government and taxpayers. American farmers receive a financial incentive to buy the insurance coverage from existing insurers, with the US government ultimately covering any losses incurred in excess of predetermined limits under the insurance policy. Farm subsidies are also accused of being the reason behind high consumer pricing for agricultural products, due to there being a lack of incentive for farmers to price products competitively.<sup>33</sup>

## ENSURING TECHNICAL REGULATION AND LABELLING IS NOT A BARTO TRADE

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- 7.7 There is a range of technical barriers to trade where progress can be made if the UK is out of the EU. We have set out some of them in the following sections.
- 7.8 There are many areas of food labelling where EU standards exceed those of the Codex Alimentarius General Standards (for example in fisheries labelling and aquaculture). As the EU and the US legislation relating to mandatory food labelling are both based on international Codex standards, they share similarities. The EU and the US both require detailed labelling on food packaging, to communicate to the customer key facts about the product, including nutritional and allergen information. However, there are some differences between the two regimes, for example (i) how nutrition information is communicated (in the US calories must be stated by reference to servings; in the EU all nutrition listings must be displayed per 100g but may also be given per portion;<sup>34</sup> and (ii) the US lists sodium content (measured in milligrams) on nutrition labels, while the EU lists salt content (measured in grams).<sup>35</sup>
- 7.9 The US will also likely seek to challenge the European Geographical Indications, including the expansion of country of origin standards to place of farming. The Codex does not require place of origin designation. Traditional terms that are restricted such as tawny, ruby and chateau which the Codex also does not include are problematic. The World Wine Trade Group, consisting of Australia, Canada, Chile, Georgia, New Zealand, South Africa, and the US have campaigned on various aspects of wine designation and will be anxious to secure more openness from the UK than from Europe.<sup>36</sup>
- 7.10 The US-UK agreement can be used to agree appropriate, proportionate standards for such agricultural products, based on sound scientific evidence. In addition, the agreement should seek to eliminate unnecessary SPS measures and import controls that act as barriers to trade, where there is no proven risk to human, animal or plant health. It should be noted that this discussion might not be straightforward, as there is likely to be some resistance from producers and consumer groups in the UK, particularly with regard to hormone-treated beef products.

33. [https://www.researchgate.net/publication/264887771\\_Farm\\_Subsidies\\_and\\_Obesity\\_in\\_the\\_United\\_States](https://www.researchgate.net/publication/264887771_Farm_Subsidies_and_Obesity_in_the_United_States)

34. See The Federal Food, Drug, and Cosmetic Act and the Fair Packaging and Labeling Act (US) and Regulation (EU) No 1169/2011 Food information to consumers (EU)

35. Regulation (EU) 1169/2011

36. <http://www.wwtg-gmcc.org/p/achievements.html>

- 7.11 There are a number of EU bans in the area of TBT/SPS measures. These include bans on growth hormones in beef and beta agonists. In particular, there is an EU ban on ractopamine which promotes leanness in meat. Codex has suggested that ractopamine at specific residual levels (10 parts per billion (ppb) in comparison to limits set by the US Food and Drug Administration at 30 ppb for beef and 50 ppb for pork) has no effect on human health.<sup>37</sup> The WTO has already found the EU ban in violation of WTO rules. As a result of the ongoing dispute, grain-fed, High Quality Beef (“HQB”) was allowed a special TRQ. Since other countries complained about this, the quota was opened up to Argentina, Australia, Canada, New Zealand and Uruguay, and the US now controls only 45% of the HQB quota. The beneficiaries of the HQB quota will likely seek to replicate the quota in its entirety for the UK market but the UK and US can look at it in a more holistic way if the UK signals more general openness with respect to US meat imports under an FTA.
- 7.12 The EU has rules against food products as a result of animal cloning. Such food products are categorised as “novel foods” under EU law, and require authorisation from the Commission to be placed on the EU market.<sup>38</sup> The Commission released guidelines to state that novel food will only be approved for use in the EU if they do not present a risk to public health, are not nutritionally disadvantageous when replacing a similar food and are not misleading to the consumer. They must undergo a scientific assessment prior to authorisation to ensure their safety.<sup>39</sup> Similarly, authorisation must be obtained for use of genetically modified organisms (“GMO”) in cultivation and the marketing of food and feed and derived products. All applications for GMO authorisation must be submitted with a dossier with experimental data and a risk assessment. In March 2015, the EU allowed member states to ban GMO for non-science based reasons, a clear WTO violation, and pathogen reduction treatments. In the last case, the purpose of these anti-microbial washes is to kill pathogens and make the products safer for human consumption. There is no evidence of a danger to human health—indeed not using effective disinfectants presents a danger to human health.
- 7.13 EU certification requirements limit US agricultural exports such as meat, dairy, and eggs. In general, health certificates are required for all products of animal origin imported in the EU and phytosanitary certificates are needed for all plant products that could introduce pests into the EU. Import requirements for animals and animal products are harmonised across the EU in a three-part process. First, the EU must recognise a country as eligible to export a particular animal or animal products. In the absence of an approved US residue plan for horsemeat, the US has effectively been restricted from exporting horsemeat to the EU since 2011. Secondly, the EU requires lists of approved establishments based on submissions from US government agencies. Only those products processed at approved establishments may enter the EU. In the US, such establishments include the Food Safety and Inspection Service, the Animal and Plant Health Inspection Service, the Food and Drug Administration, and the Agricultural Marketing Service. Lastly, animal or public health certificates based on the model certificates published by the EU and signed by US officials must accompany all imports.<sup>40</sup>
- 7.14 Under the European Regulation (EC) No 1907/2006 on the Registration, Evaluation, Authorisation and Restriction of Chemicals (“REACH”), manufacturers and users of chemicals,

37. <http://www.foodsafetynews.com/2012/07/codex-votes-69-67-to-advance-ractopamine-limits-for-beef-and-pork/#.WNut5o-cE2w>

38. <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32015R2283&from=EN> Regulation (EU) 2015/2283 of 25 November 2015 on novel foods

39. [http://europa.eu/rapid/press-release\\_MEMO-15-5875\\_en.htm](http://europa.eu/rapid/press-release_MEMO-15-5875_en.htm)

40. [https://gain.fas.usda.gov/Recent%20GAIN%20Publications/Food%20and%20Agricultural%20Import%20Regulations%20and%20Standards%20-%20Certification\\_Brussels%20USEU\\_EU-28\\_2-13-2017.pdf](https://gain.fas.usda.gov/Recent%20GAIN%20Publications/Food%20and%20Agricultural%20Import%20Regulations%20and%20Standards%20-%20Certification_Brussels%20USEU_EU-28_2-13-2017.pdf)



such as pesticides, must prove they are safe before they are released into the EU market. Of particular interest, endocrine disruptors are considered of similar regulatory concern as substances of very high concern under REACH. However, endocrine disruptors are difficult to distinguish from endocrine active substances (substances that can interact or interfere with normal hormonal action, but without adverse effects). The Commission is currently working with Member States, the European Chemicals Agency and the European Food Safety Authority to produce full guidance to identify substances with endocrine-disrupting properties in pesticides and biocides, to be opened to public consultation in Summer 2017.<sup>41</sup>

- 7.15 Milk is barred if the somatic cell count ("SCC") (white blood cells) is above 750,000 ml even though this has no effect on the actual milk quality or its capacity to harm humans. In comparison, the EU SCC requirement is 400,000 cells per ml. Since milk and dairy products for export can't be easily segregated, many farms in the US have been forced to meet the 400,000 EU standard.<sup>42</sup>

41. <https://echa.europa.eu/-/endocrine-disruptors-efsa-and-echa-outline-guidance-plans>

42. <http://www.progressivedairy.com/news/industry-news/scc-limit-in-the-us-remains-at-750000>

*Above:* Parade of prize-winning cattle at the Royal Cornwall Show. Wadebridge, June 2016.

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Shutterstock.com

- 7.16 The EU's citrus canker rules keep citrus from Florida out of the territory of the EU, because it states that where there is one infected plant, produce from the whole grove is banned.
- 7.17 There are also bans at the member state level (such as the French ban on bisphenol A). The US would want all of these issues to be corrected but to the extent they are member state issues that do not apply in the UK, this is an advantage to the UK.
- 7.18 With regard to Animal Welfare Certificates, the EU's process is in excess of what is required in SPS certification procedures from the Codes, OIE and the International Plant Protection Convention.
- 7.19 The US imposes certain SPS measures and import controls on certain meat products and eggs, which the UK is likely to seek to have eliminated for imports from the UK. In 1997 the US closed its market to a number of EU animals and animal products (including beef and goats) on the basis that such products posed a risk of carrying bovine spongiform encephalopathy ("BSE"). In March 2014, the US aligned its import requirements to that of the World Organisation for Animal Health ("OIE"), through introduction of the 'comprehensive rule'. The OIE standards call for countries to base their trade policies on the actual risk of cattle and cattle products harbouring BSE. In light of this, the comprehensive rule incorporates a risk-based approach aligned to international animal health guidelines and scientific understanding, and in particular permit the export of all boneless beef to the US, regardless of the risk category of the country of origin.<sup>43</sup>
- 7.20 However, before trade is able to resume between the EU and the US, EU establishments must be approved and member states re-instated by the Food Safety and Inspection Service ("FSIS"), which the Commission describes as an "ongoing" process.<sup>44</sup> In order to be certified for FSIS equivalence, it must be determined that the member state has maintained an equivalent beef slaughter and/or processing system (to include providing supporting documentation of appropriate government oversight and an onsite audit).<sup>45</sup> The UK is in the process of applying for equivalence for meat products, and is currently at 'stage 2' of the process, which involves submission of a self-reporting tool and supporting documentation.<sup>46</sup>
- 7.21 The most recent export eligibility list published by the United States Department of Agriculture provides that the UK is only eligible to export pork to the US. Exports of beef and veal are conditional on the UK obtaining verification of FSIS equivalence. The UK will want to obtain a similar eligibility standard to that of Canada, which is considered eligible to export beef and veal, lamb and mutton, goat, pork, poultry and ratites and egg products freely to the US.
- 7.22 The US also requires that formal authorisation and pest risk assessment must be carried out for all food crops, including edible fruit and vegetables before it is permitted for import. For those products that are not approved pending risk assessment, authorisation can take several years to be granted.<sup>47</sup> Assessment is carried out by the Animal and Plant Health Inspection Service under the umbrella of the US Department of Agriculture. The UK is likely to seek recognition of its food crops under the FTA to avoid the assessment and authorisation process entirely, or at a minimum, seek to agree that UK applications will be expedited beyond the existing timeframes.

43. [http://www.aphis.usda.gov/publications/animal\\_health/2013/faq\\_bse\\_rule\\_final.pdf](http://www.aphis.usda.gov/publications/animal_health/2013/faq_bse_rule_final.pdf)

44. [http://madb.europa.eu/madb/sps\\_barriers\\_details.htm?isSps=true&barrier\\_id=10784](http://madb.europa.eu/madb/sps_barriers_details.htm?isSps=true&barrier_id=10784)

45. [https://www.fsis.usda.gov/wps/wcm/connect/4872809d-90c6-4fa6-a2a8-baa77f48e9af/Countries\\_Products\\_Eligible\\_for\\_Export.pdf?MOD=AJPERES](https://www.fsis.usda.gov/wps/wcm/connect/4872809d-90c6-4fa6-a2a8-baa77f48e9af/Countries_Products_Eligible_for_Export.pdf?MOD=AJPERES)

46. <https://www.fsis.usda.gov/wps/wcm/connect/2514b05f-82b2-4c1a-a7f2-fdf4610d4d8e/Equivalence-Status-Chart.pdf?MOD=AJPERES>

47. [http://madb.europa.eu/madb/sps\\_barriers\\_details.htm?isSps=true&barrier\\_id=10783](http://madb.europa.eu/madb/sps_barriers_details.htm?isSps=true&barrier_id=10783)

## 8. IMPROVING ACCESS TO GOVERNMENT BUSINESS OPPORTUNITIES

- 8.1 Various laws enacted by the United States Congress require that the federal government favour US suppliers in making purchases. These laws are rather complex in their application and are subject to a variety of exceptions. 'Buy American' provisions are a condition of US federal government grants to state, municipal or other organisations, including transit authorities. Current federal policy, enunciated by President Trump, directs US Government agencies to seek to favour domestic suppliers to the full extent allowed by law.<sup>48</sup>
- 8.2 The core US statute in this regard is the Buy American Act of 1933 ("BAA"), which has been amended over time. The BAA applies to procurement of supplies and construction materials by the US Government. (Thus, for example, if the US government issues a solicitation for construction of an infrastructure project, the BAA would apply to the procurement).
- 8.3 Concerns about controlling the cost of federal procurements lie at the heart of BAA exceptions. For instance, the BAA requirement to purchase US-made steel may be waived by the government if the domestic cost is 25% or more expensive than if foreign-sourced, if the product is not available domestically in sufficient quantity or quality, or "if doing so is in the public interest," an inherently malleable term that has been invoked on many occasions to allow the substitution of foreign for domestic supplies.
- 8.4 Agency-specific regulations govern the extent of BAA preferences. The US Department of Transportation ("DOT") requires that, to justify turning to foreign sources, the cost of the American component must be so high as to increase an entire project's contract cost by 25%, not just the cost of the specific item. Regulations applicable to non-DOT purchases, however, require adding a 6% cost differential in comparing bids, "[u]nless the head of the agency specifies a higher percentage".
- 8.5 The Trade Agreements Act of 1979 gives the President certain latitude to waive Buy American provisions. Moreover, under this Act, imports from "designated countries" (including most notably nations with which the U.S. has free trade agreements such as Canada, Mexico, Australia, and New Zealand) generally are not subject to BAA restrictions.
- 8.6 The American Recovery and Reinvestment Act of 2009 ("Recovery Act") expanded Buy American preferences by including strict domestic requirements for iron, steel, and manufactured goods for contracts for public buildings and public works awarded by federal agencies using stimulus funds available pursuant to the Recovery Act. The Recovery Act included an exemption for projects valued at \$7,804,000 or more with respect to products from specified countries that have entered into free trade agreements with the United States. The Recovery Act repeated the earlier requirement for the US Commerce Department to grant waivers with respect to covered

<sup>48</sup> Presidential Executive Order on Buy American and Hire American signed on 18 April 2017 <https://www.whitehouse.gov/the-press-office/2017/04/18/presidential-executive-order-buy-american-and-hire-american>

products (1) that are not produced in the U.S. in sufficient and reasonably available quantities, or (2) where domestic purchases would raise the overall project cost by over 25%, or (3) where application of the Recovery Act's preference "would be inconsistent with the public interest."

- 8.7 The Recovery Act was shortly followed by guidance from the Office of Management and Budget ("OMB") as to how the Buy American restrictions should be implemented, which ultimately resulted in a reduction in the use of waivers post-2009 as they became harder to justify. For example, the waiver relating to unreasonable cost was only available if a domestic purchase would raise the cost of the *entire project* (not just the item in question) by 25%, which would be relatively rare. In addition, if a product met the availability and cost criteria, it would be unlikely that an agency could put forward a compelling public interest exemption to satisfy the waiver provisions. The OMB guidelines also included a requirement on any agency granting a waiver to publish a detailed written justification in the Federal Register.
- 8.8 On 18 April, President Trump signed a new 'Buy American, Hire American' executive order<sup>49</sup> that sets the policy of the executive branch to maximise the use of domestically produced goods, and to rigorously enforce and administer immigration laws, with development of reforms to the H-1B skilled worker visa program to counter fraud and abuse of the program. The executive order requires agencies to monitor, enforce and comply with Buy American laws, and minimise the use of waivers, with an assessment of current compliance and development of policy proposals to maximise procurement of domestically produced goods. The executive order also requires that before granting a public interest waiver, the relevant agency will have to take appropriate account of whether a significant proportion of the cost advantage of a foreign-sourced product is the result of use of dumped steel, iron or manufactured goods, or the use of injuriously subsidised steel, iron or manufactured goods. Further, the Secretary of Commerce and the USTR will also have to assess the impacts of all US FTAs, including the WTO Agreement on Government Procurement, on the operation of Buy American laws and implementation of domestic procurement preferences. The executive order states that "it shall be the policy of the executive branch to maximise, consistent with law, through terms and conditions of Federal financial assistance awards and Federal procurements, the use of goods, products, and materials produced in the United States." The order cautions that it "shall be implemented consistent with applicable law", which means that it does not expand the scope of Buy American preferences beyond the ambit of what the existing Buy American statutes provide. It remains to be seen whether the Trump administration's direction of travel is to extend the restrictions which the Obama administration implemented, or whether they may be reined in.
- 8.9 This executive order may make an agreement on government procurement more difficult. The requirement for consideration of distortions before the application of the public interest waiver is consistent with our proposals on addressing ACMDs. However, the executive order also potentially creates uncertainty with the review of FTAs, and the outcomes of this would provide useful guidance on implications for a US-UK agreement. The UK should try and negotiate a special arrangement with relation to government procurement.

49. <https://www.whitehouse.gov/the-press-office/2017/04/18/presidential-executive-order-buy-american-and-hire-american>





- 8.10 Finally, several US states have introduced “Buy America” proposals with the intention of limiting state contracts to companies that manufacture products made with a certain percentage of domestic content, sometimes as high as 100%. Various municipalities have sought to adopt similar restrictive procurement policies.
- 8.11 The US is signatory to the WTO Government Procurement Agreement (“GPA”) which contains obligations on its signatories to open their procurement markets to international competition. However, the US’s obligations under the GPA are limited. Only 37 states and the federal government are signatories to the GPA. This means that any municipal contracts are not subject to the GPA, even where such municipal projects are funded by the federal government. The relevant municipality will be considered the “owner” of the project for the purposes of the GPA and such federal funding will be considered “assistance” under the GPA and expressly carved out of its scope. Under the GPA, parties may agree thresholds for the provisions to apply on a reciprocal basis through free trade agreements.

*Above: Tappan Zee Bridge under construction in Tarrytown, New York, Westchester County, USA. November, 2016,*

*©Sean Wandzilak  
Shutterstock*

## 9. IMPROVING DEFENCE COOPERATION

- 9.1 The US and the UK already work closely together in the fields of defence and security, and have significant investment in defence industries in each other's territories. There are a number of measures that could be taken to improve trade in this sector, which would deliver both economic benefits and more competition and innovation. It has been suggested that the process under Section 811 of the Fiscal Year 2018 National Defense Authorization Act ("NDAA"), which mandates a Defense Department study of ways to improve the integration of the US defence industrial base, including Britain and Australia should be initiated, to find ways to collaborate with allies and build on trade in this area.<sup>50</sup>
- 9.2 The Committee on Foreign Investment in the United States ("CFIUS") is an inter-agency committee authorised to review transactions that could result in control of a US business by a foreign person ("covered transactions"), in order to determine the effect of such transactions on the national security of the US. CFIUS has powers to investigate and approve any such covered transaction, including powers to impose conditions to mitigate a threat to US national security (addressed below), or it may refer the matter to the President for final action. The President holds ultimate authority to prohibit or unwind a transaction where there is credible evidence that the transaction threatens to impair US national security and the threat cannot be adequately mitigated.<sup>51</sup>
- 9.3 The CFIUS review process is regulated by a statutory-mandated timeline and ranges from 30 to 90 days, depend on whether CFIUS requires a full investigation period of up to 45 days and presidential review. The confidential review process includes consideration of certain statutorily enumerated factors that CFIUS considers when reviewing a covered transaction. These include, for example, ensuring the domestic capability and capacity necessary to fulfil national defence requirements, the impact of a transaction on US technological leadership in an area affecting national security, the potential effects on US critical infrastructure, effects on critical technologies, long-term US energy needs, whether the transaction involves an acquirer that is controlled by a foreign government, and whether the home country of the acquirer adheres to US policy on non-proliferation and export control requirements.<sup>52</sup>
- 9.4 CFIUS assesses transactions by way of a three-part "national security analysis". First, CFIUS evaluates the foreign person to determine whether it has the ability or intent to exploit or cause harm. Second, it considers the US business being acquired, including any relationship to weakness or shortcoming in the US national defence or any susceptibility to impairment of US national security. Finally, it evaluates the risk of potential threat or vulnerability caused as to US national security as a result of the intended transaction. If CFIUS concludes there is a potential threat to national security, it may require the parties to the transaction to

50. Nile Gardiner and Ted Bromund *The Trump–May White House Meeting: Five Key Recommendations for Advancing the Special Relationship* (January 2017) <http://origin.heritage.org/research/reports/2017/01/the-trumpmay-white-house-meeting-five-key-recommendations-for-advancing-the-special-relationship>

51. [http://www.ofii.org/sites/default/files/OFII\\_CFIUS\\_Primer.pdf](http://www.ofii.org/sites/default/files/OFII_CFIUS_Primer.pdf)

52. *Ibid.*



enter into a mitigation agreement which might include a governance measures, security requirements, and monitoring/verification mechanisms, among other conditions.<sup>53</sup> Not all transactions are subject to CFIUS review. The parties may choose to submit their transaction to CFIUS review, but there is considerable discretion in the process which makes outcomes unpredictable.

- 9.5 The US and UK might seek to agree a more streamlined review process for UK-based businesses. This could come in the form of a light-touch review process through mutual recognition of any transaction involving a business that can demonstrate it has been legally incorporated in the UK (e.g. a presumption that all UK businesses will not offer a threat to US national security), or through an expedited review process (e.g. where any review by CFIUS of a transaction involving a UK business is prioritised and processed faster than the current statutory timescales).<sup>54</sup>

Above: US Air Force F-16 fighter jet at the International Aerospace Exhibition ILA, Berlin, 2014.

©VanderWolf Images / Shutterstock.com

<sup>53</sup> *Ibid.*

<sup>54</sup> The presence of Chinese products in the UK supply chains will complicate any attempt to agree CFIUS review.

## 10. IMPROVING PROPERTY RIGHTS PROTECTION— INTELLECTUAL PROPERTY

- 10.1 The UK and US share a commitment to protection of intellectual property protection (“IPR”). The EU has extended IPR into areas such as the EU’s broad interpretation of Geographical Indications (“GIs”) which have harmed UK and US interests alike (especially in areas like wine and champagne production).<sup>55</sup> Apart from Scotch Whiskey, the UK’s interests in GIs are limited and opportunistic. For example, simply because they are available, incumbent producers often take advantage of them.<sup>55a</sup>
- 10.2 Other like-minded countries in the Prosperity Zone would welcome the elimination of GIs as they are all negatively impacted by them. As mentioned above, the World Wine Trade Group, consisting of Australia, Canada, Chile, Georgia, New Zealand, South Africa, and the US have campaigned on various aspects of wine designation and will be anxious to secure more openness from the UK than from the EU.
- 10.3 Apart from this area, UK and US IP law align well in terms of overall objectives. By contrast, some EU countries are still on the intellectual property watch-lists maintained by the US government such as Bulgaria, Greece and Romania.<sup>56</sup> The UK was not mentioned in the National Trade Estimate of 2017 indicating its approach to IPR and their protection is better than other EU member states.
- 10.4 Although the US and the UK both maintain a high level of IPR protection, it should be noted that the IPR chapter of the TTIP was one of the most contentious in negotiations between the US and the EU. Problematic discussions arose relating to internet service provider liability, finding commonalities between EU and US privacy, copyright policies and patent term extensions, protection of test data and patent linkage.<sup>57</sup>

55. <https://www.agra-net.com/agra/agra-europe/policy-and-legislation/trade-policy/us-report-identifies-eu-s-agricultural-barriers-to-trade-547308.htm>

55a. See for example the award of protected status to Welsh laver bread <http://www.bbc.co.uk/news/uk-wales-39949753>

56. <https://ustr.gov/sites/default/files/USTR-2016-Special-301-Report.pdf>

57. [http://www.europarl.europa.eu/RegData/bibliotheque/briefing/2014/140760/LDM\\_BRI\(2014\)140760\\_REV1\\_EN.pdf](http://www.europarl.europa.eu/RegData/bibliotheque/briefing/2014/140760/LDM_BRI(2014)140760_REV1_EN.pdf)

## 11. THE POSSIBILITIES FOR FINANCIAL SERVICES LIBERALISATION

- 11.1 There is an opportunity for the UK and US to cooperate on financial services with a view to establishing more pro-competitive regulation around the world. Indeed, some of the major financial centres around the world, such as Hong Kong, Tokyo, New York, London and Zurich might be interested in working together on such an endeavour. In this context the UK-US FTA is a vital part of the process.
- 11.2 The UK is relatively open in financial services. Greater co-ordination and recognition of home state regulation could deliver significant gains to the US and the UK, and to the global economy if it results in greater innovation and consumer welfare enhancing financial products. Our paper *A New UK/EU Relationship in Financial Services—a Bilateral Regulatory Partnership* sets out a model for how this could be achieved.<sup>58</sup>
- 11.3 In mutual recognition for financial services, there is already precedent for the US adopting mutual recognition, such as the mutual recognition arrangement signed by the US Securities and Exchange Commission (“SEC”) and the Australian Securities and Investment Commission (“ASIC”) in 2008. This provided the framework for the authorities to consider regulatory exemptions that would permit US and eligible Australian stock exchanges and broker-dealers to operate in both jurisdictions, without requiring them to be separately regulated in each country. An Enhanced Enforcement MOU and a new Supervisory MOU allowed for greater regulatory cooperation and coordination between the SEC and ASIC. The intention was to provide US and Australian investors and businesses easier and more competitive access to each other’s markets. The US also has accords in place for mutual recognition and substituted compliance in some fields, such as central counterparties. The US and the UK should be able to build on this bilaterally and working in global fora.
- 11.4 In the US, the fragmentation of insurance regulation on a state basis is a significant barrier that could be addressed. The International Monetary Fund reported that the existing complexity and fragmentation bring risks of a lack of consistency and of failure to act on gaps or weaknesses in regulation with sector or system-wide implications.<sup>59</sup> The size of each insured population and how insurance risk is shared also has an impact on consumer pricing. Small employers, groups and individuals often find insurance coverage more expensive than larger groups such as government programmes and large employers, due to providers finding it more difficult to cross-subsidise with a smaller risk pool. There is also generally a lack of supervision of the insurance providers from a federal level, and rules vary from state to state. Ideally, the US should look to introduce a single insurance regulation, recognised on a state-wide basis, with a centralised supervisory body to enforce compliance by insurance providers. This might have the ancillary benefit of helping the US healthcare insurance market become more competitive.

58. <http://www.li.com/activities/publications>

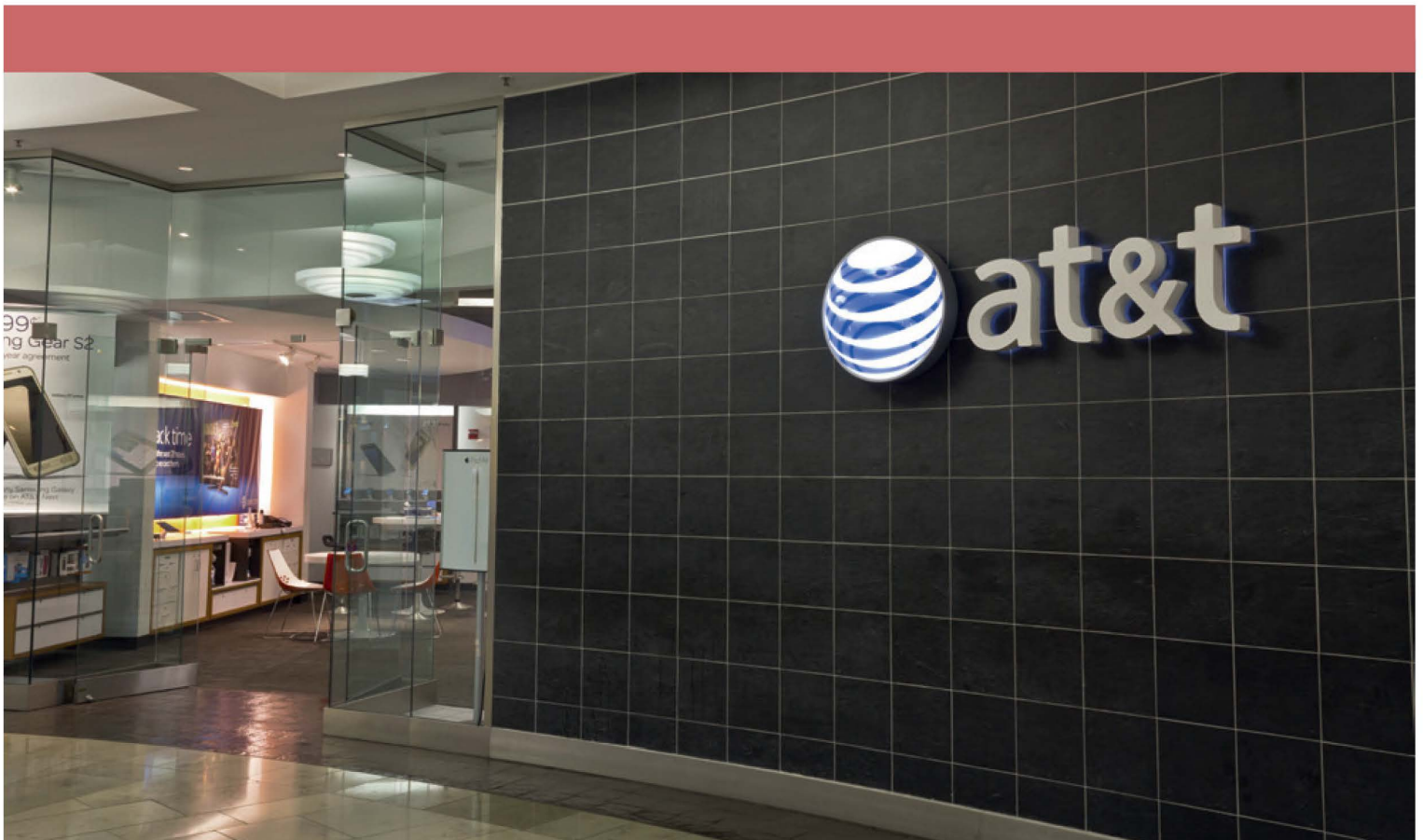
59. IMF Country Report No. 15/90 *United States: Detailed Assessment of Observance of Insurance Core Principles* (April 2015)

## 12. TELECOMMUNICATIONS

- 12.1 The US has complained about a perceived two tier structure on costs of termination of international traffic in the EU. If the UK is outside the EU, it may be subject to this as well. In any event the parties should seek to include a reciprocal requirement to enforce cost-oriented interconnection in any FTA between them.

*Below:* AT&T (American Telecommunications Corporation) Retail Store. Indianapolis 2016.

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## 13. DIGITAL SINGLE MARKET

- 13.1 The Audio Visual Media Services Directive (“AVMS”) requires minimum local content in television broadcasting in all member states, and will be updated as part of the EU’s Digital Single Market Programme to include ‘on-demand’ content through on-line channels. The UK will have to retain local content rules for broadcast media when it is outside the EU, as this is governed by a separate international convention (the Council of Europe Convention on Transfrontier Television) that the UK will still be a member of. This will be necessary for UK operators to benefit from continued access to the European television markets. The UK will in any event be carrying all EU laws and regulations into national law, so this will include the AVMS. The UK will in any event be carrying all EU laws and regulations into national law, so this will include the AVMS. However, there are provisions of this directive that the UK should review in due course, potentially as part of the trade agenda with the US. AVMS may therefore represent a soft base-line for the regulatory part of the negotiations.
- 13.2 TPP was the first agreement of its type to contain provisions relating to digital trade and the digital market and promotion of electronic commerce.<sup>60</sup> TPP sought to remove existing barriers to transfer of data by preventing the localisation of data and prohibiting digital customs duties. In addition, the TPP encourages governments to cooperate on matters of cyber security and banning parties from implementing certain arbitrary policies banning the use of technologies such as encryption or VPN on the basis that they threaten security. The agreement between the US and the UK will provide the opportunity to build on this shared ideal, to ensure that both parties benefit from a free and competitive flow of digital services.

60. <https://ustr.gov/sites/default/files/TPP-Promoting-Digital-Trade-Fact-Sheet.pdf>

## 14. DATA PROTECTION—THE TENSION BETWEEN DATA FLOW AND DATA PRIVACY

- 14.1 There is a philosophical difference in the approach of the US and the EU to data. The US's businesses have loudly advocated for data flow. Many US firms are at the forefront of the "big data" and "Internet of Things" revolutions. In order for this "Fourth Industrial Revolution" to deliver its potential, data will have to easily flow across businesses and geographies. In Europe, by contrast citizens, concerned about the use of their private data appear to have won the battle with business and the EU is much more protective of privacy with the resulting restrictions on data flow. This is an area where there will either be a way that data can flow across the US-UK-EU supply chain, or it cannot. UK-US FTA negotiations must seek to find this path.
- 14.2 The EU General Data Protection Regulation ("GDPR") will be in place with effect from May 2018. The GDPR contains very stringent protections for data (how it is held, who holds it and what it can be used for), and purports to extra territorial reach wherever personal data of EU citizens is processed. It also includes specific controls on the transfer of personal data to non-EEA countries who are not officially recognised by the Commission as providing for an adequate level of protection of personal data (so-called 'white-listing'). This will make it difficult for data to flow to the US without satisfying a number of safeguards. This, in turn, will create significant issues with the US, for whom data flow is a very important deliverable in any trade agreement, but the UK will not be in a position to relax these requirements without losing its own white listing (which it will hope to have in place as at the date of Brexit).
- 14.3 The US is not whitelisted, due to a number of issues in its approach to data protection (or lack of it) that do not satisfy Commission requirements. The alternative solution in operation is the Privacy Shield (which replaces the Safe Harbor scheme), under which businesses can operate certain measures to protect personal data and can therefore receive personal data from the EEA without further safeguards. The Privacy Shield is designed to allow companies in the EEA and Switzerland to transfer data from their home jurisdictions to the US without putting further safeguards in place. As a minimum, it can be expected that the UK will replicate the Privacy Shield determination.



## 15. HEALTH SERVICES

- 15.1 The socialised healthcare system operated through the British National Health Service (“NHS”) means that there are substantial barriers to the healthcare market in the UK. Some services are provided by private contractors under contract to the NHS, and US providers have invested in such business, mainly through acquisition. For example, US-based Acadia owns the Priory Group, whilst the Hospital Corporation of America owns several private hospitals in Britain. However, it is unlikely that large or significant parts of the NHS would be opened up to provision by foreign companies, although government procurement rules could be opened up to allow US firms to bid for NHS contracts in the same way as European firms. In reality, the structure and financing of the NHS mean there is little appetite to invest in this market,<sup>61</sup> and the political imperative to protect, and be seen to protect, the NHS mean that for a trade deal to progress expeditiously, it would be preferable not to include NHS services. As in all services areas, the UK could simply reserve the sector. Progress could be made in the private healthcare market, however, it should be noted that the private healthcare sector in the UK is less attractive because it has to compete with a state-supported entity.

<sup>61</sup> <http://www.economist.com/news/britain/21716662-question-what-firm-would-invest-national-health-service-american-trade-deal>

## 16. CHEMICALS: AN EXAMPLE OF THE PRECAUTIONARY PRINCIPLE

- 16.1 Regulation of the chemicals sector in the EU is perhaps subject to more complaints by non-EU businesses than any other sector. EU chemicals regulation, which is led by Regulation (No 1907/2006) regarding the Registration, Evaluation, Authorisation and Restriction of Chemicals (“REACH”), which applies the precautionary principle to this sector.
- 16.2 REACH is a framework for chemicals manufacture and use in Europe with its stated aim to ensure that chemicals produced, imported, sold and used in the EU are safe.<sup>62</sup> There is a registration/data generation requirement within REACH which obliges manufacturers to gather information relating to new and existing chemicals used within their business and submit such information to the European Chemicals Agency (ECHA) for review and for inclusion within a ‘central chemicals database’ to be administered by the ECHA. Behind Germany, the UK has the second highest number of REACH registrations at 5,488.<sup>63</sup> REACH reduces third country exports to the EU by increasing cost and, in some cases, barring products from entering the single market, prompting concerns that such actions are not always necessary and/or proportionate to the potential risk posed.
- 16.3 For example, in 2013, Germany started campaigning for beryllium, a metal that is used in defence and commercial applications to be included on the REACH list of substances of very high concern for authorisation. Such inclusion would have placed onerous obligations on imports of products including use of such metal into the EU and effectively created a barrier to imports of the metal from the US which, according to the Office of the United States Trade Representative (“USTR”), accounted for 40% of the US’s sale of the metal. Of particular issue for the USTR was that beryllium was difficult to replace with any other substitute (it has definitive properties such as strength, low weight, and resistance to chemical deterioration). It was submitted by the USTR that although it recognised the health risks from exposure to beryllium, it believed that the appropriate way to manage that risk was by controlling human exposure rather than effectively banning the substance from import into the EU.<sup>64</sup>
- 16.4 In light of this, it is key for the UK to be able to sensibly assess the risks of imported products on a case-by-case basis and have the option to create practical solutions when dealing with such products, so as not to lose the benefit of products with no substitutional equivalent. The UK’s position on REACH should align to its position on standards (as outlined in section 18 below).
- 16.5 The UK and US will have to agree some science-based approach to product risk that would enable product MRAs with the EU for both parties.

62. <http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=URISERV%3A121282>

63. <https://echa.europa.eu/regulations/reach/registration/registration-statistics/overview-all-countries>

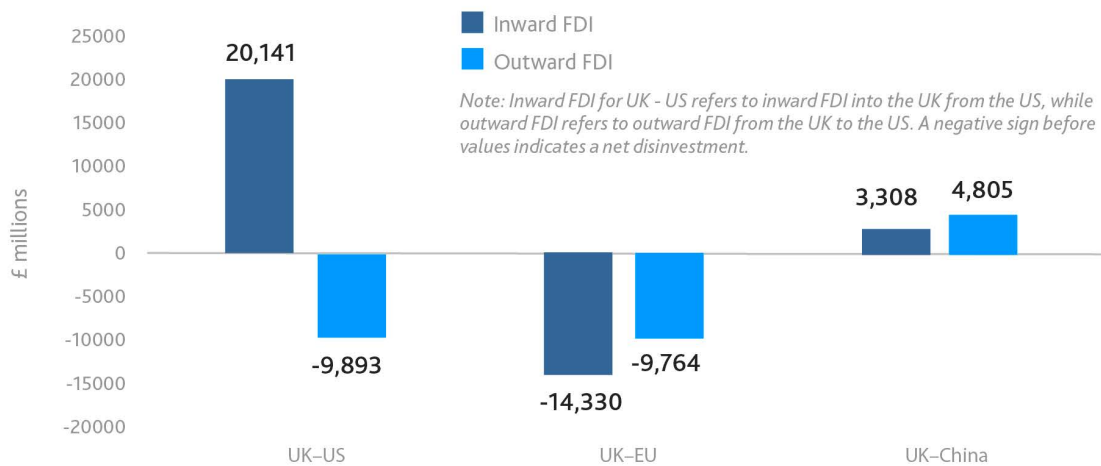
64. <https://ustr.gov/about-us/policy-offices/press-office/factsheets/2016/march/ustr-successes-reducing-technical>

## 17. MANAGING TALENT

Below: Figure 2: FDI flows, 2015

Source: UK data from ONS, Inward Foreign Direct Investment involving UK Companies, 2015, ONS, Outward Foreign Direct Investment involving UK companies, 2015, US data from OECD, FDI Financial Flows. US data converted from USD to GBP using the OECD exchange rate for 2015.<sup>66</sup>

- 17.1 One of the major issues that the UK and US should agree is how to ensure the best talent is available to firms in both jurisdictions. There is such a shared set of values, language and laws between the UK and the US that it should be possible to ensure a situation where British and American people can live and work much more easily in each other's countries. In particular, given that the UK-US investment relationship is the strongest in the world (as shown in figure 2 below) it should be possible to agree "mode 4 services" arrangements between these two countries. Mode 4 services means the presence of persons of one WTO member in the territory of another for the purpose of providing a service.<sup>65</sup>
- 17.2 The US and the UK should seek to agree reciprocal rights for movement of people between the two countries. Following its exit from the EU, the UK may seek to establish a needs-based immigration policy, which might seek in part to replicate a similar mechanism to the existing US H1-B visa. The H1-B visa permits US employers to recruit foreign workers in speciality occupations on a temporary basis. Workers under the H1-B visa programme are authorised to remain in the US for 3 years, extendable to 6 years. However, in the event that the relevant occupation ceases, holders are required to apply for an alternative status,



<sup>65</sup> [https://www.wto.org/english/tratop\\_e/serv\\_e/mouvement\\_persons\\_e/mouvement\\_persons\\_e.htm](https://www.wto.org/english/tratop_e/serv_e/mouvement_persons_e/mouvement_persons_e.htm)

<sup>66</sup> Notes: Inward FDI for UK—US refers to inward FDI into the UK from the US, while outward FDI refers to outward FDI from the UK to the US. A negative sign before values indicates a net disinvestment.

find another employer or leave the US. Such speciality occupations particularly include skilled and professional work such as architecture, engineering, mathematics, law and accountancy. With the recent reforms instructed to the H1-B visa procedure by virtue of the “Buy American, Hire American” Executive Order, signed by the president on 18 April 2017, a discussion between the US and UK on this issue should be sought as soon as possible.

- 17.3 Special provisions for the H-1B program for the UK could be agreed, where there would be a mechanism for especially skilled and professional workers. We could also make it easier for our university students from the other country to stay on after their degrees to work in the host country. An automatic right to remain (or green card, in US parlance) should be in place for advanced degrees in certain courses (for example, science, technology, engineering and mathematics, or “STEM”).

## 18. IMPROVING THE STANDARDS SETTING ENVIRONMENT BETWEEN BOTH COUNTRIES

- 18.1 This is a key area for the UK to get right in the context of its other agreements, and one where there is a very significant America interest. It would not be in either the UK or US's long term interests for the UK to simply agree to be locked in to the EU standards and product regulation. If this occurs, the UK will become a propagator of EU standards and product regulation all over the world. It will significantly imperil the ability of the UK to come to agreements with other countries and will threaten the UK's independent trade policy (as described in *A Blueprint for UK Trade Policy*.<sup>67</sup> Instead the best approach is to strengthen the networks of MRAs between the US and UK, and separately between the UK and EU. This also recognises the process which has already occurred (the six MRAs between the US and EU were first negotiated in 1997 (see section 17.46 below)).
- 18.2 Standard setting and the interaction between standards and mandatory legal product requirements are materially different between the UK (under harmonised EU regulations and processes) and the US, and was a major stumbling block in TTIP negotiations.
- 18.3 The overall approach to standard setting and regulation differs quite considerably between the US and a UK which has had its regulatory system decided in Brussels over forty years. The EU approach to standard setting is much more centralised. The US and EU already have a framework agreement in the areas of conformity assessment and mutual recognition in a number of sectors. Appendix 2 contains an analysis of Mutual Recognition Agreements ("MRAs") between the US and EU.

### RATIONALE FOR MRAS AND THEIR RELATIONSHIP TO CONFORMITY ASSESSMENTS

- 18.4 MRAs refer to negotiations to achieve the mutual acceptance of conformity assessment procedures: or the testing, certification, accreditation, and quality system registration of products and processes, which are intended to reduce barriers to trade.<sup>68</sup> MRAs can prevent new barriers appearing as nations develop more complex infrastructure for testing and approving goods and services, including in emerging technological fields. Therefore, understanding and improving these processes is one of the most important areas in creating new trade deals, including for developed economies.
- 18.5 While tariffs have been cut globally, there has been an increase in other mechanisms to prevent access of goods to national markets. The costs of traditional types of protection are much discussed, but less attention has been paid to analysing such non-tariff barriers to trade ("NTBs"). With the decrease in transatlantic tariff barriers between the US and EU, firms became more concerned with what they termed duplicative regulatory compliance costs, pressing for their removal. As a result of the MRA between the two, private testing bodies often test products in the manufacturer's place of production on one side of the Atlantic in accordance with standards set

<sup>67</sup> <https://lif.blob.core.windows.net/lif/docs/default-source/default-library/170427-final-trade-blueprintweb.pdf?sfvrsn=0>

<sup>68</sup> Conformity assessment is defined by the International Organization for Standardization/International Electrotechnical Commission Guide 2: 1996 as: 'any activity concerned with determining directly or indirectly that relevant requirements are fulfilled.' Typical examples of conformity assessment activities are sampling, testing and inspection, evaluation, verification and assurance of conformity (supplier's declaration), certification, registration, accreditation, and approval as well as their combinations. Conformity assessment may also be the process by which it is determined that a product's design meets a specification or standard (NIST, 2000).

on the other, under a sub-contracting arrangement with the responsible certification body in the importing jurisdiction.

- 18.6 MRAs and efficient international standards regimes accomplish several important goals, including facilitating the diffusion of innovative technologies and production techniques and helping create global economies of scale. Conformity to standards is understood to be where exporters' costs are likely to grow in the future, and this pressure can be expected to appear again in the context of a UK-US trade deal. However, such MRAs allowing the recognition of respective domestic conformity assessment procedures as valid for export can become both more comprehensive in terms of products—and more effective—with a new UK conformity assessment system presumably to be constructed following the UK departure from the European Union.
- 18.7 The following discussion will attempt to understand the US and EU conformity assessment structures, opportunities for MRAs, and their competition implications beyond a UK-US MRA itself.
- 18.8 Through establishing an MRA, each party has the ability to test, then certify, products against the regulatory requirements of the other party in the agreement, within its own territory and prior to export.<sup>69</sup> This occurs where countries need third-party certification for particular products, so is typically useful for products presenting possible risks to the public, or whose technical or chemical capacities and risks are unknown, and which must be submitted to stringent technical control.
- 18.9 A product being evaluated in its country of production is believed to improve efficiency and competition: it reduces time, expense, and/or the unpredictability involved in obtaining approval. These savings can be important, especially where a market is distant; where rejection of products by destination country agencies would mean delay or increased shipping costs; where a sector is highly regulated; where testing is done prior to and after export, or where early marketing may be vital for competitiveness.<sup>70</sup> These are understood to be especially useful for small and medium sized enterprises ("SMEs") lacking the resources to understand or access the regulatory system of a third country, as MRAs enable testing and certification to be done locally (the benefits to SMEs also imply helping create a more competitive business ecosystem). In addition, MRAs can create longer-term regulatory benefits, including reducing the risk of conformity assessment being used to protect domestic manufacturers (e.g. where testing and certification is carried out in conjunction with research for domestic industrial interests).<sup>71</sup>
- 18.10 MRAs do not themselves require harmonisation of regulatory procedures, or of technical standards, although they highlight the differences between regulatory systems of the parties involved, and therefore point to areas where their improvement or harmonisation could be beneficial. MRAs can thus be used as statements that lead to improved regulatory agreements for larger trade zones, and can be gradually revised in this manner. Thus in most instances, MRAs will operate where parties' underlying rules remain different, but can be used as an opportunity to improve conformity assessment. Thus in general, the greatest gains are to be made where mutual recognition is achieved against a background of harmonised or equivalent rules, deepening competition.
- 18.11 Meanwhile, in some sectors with shorter life cycles (such as ICT products), the benefits of gradual harmonisation of conformity assessment by removing the costs to industry of national differences in standards or technical regulation may be more important than MRAs themselves. Here mutual recognition may be seen as a useful step towards regulatory convergence.<sup>72</sup>

69. Park, C.H. (2001). *Economic Analysis of Conformity Assessment*. Korea Information Society Development Institute, Report.

70. Schmidt, S.K. (2007). 'Mutual Recognition as a New Mode of Governance.' *Journal of European Public Policy*, 14: 5, pp.668-687.

71. Park, C.H. (2001). *Economic Analysis of Conformity Assessment*. Korea Information Society Development Institute, Report.

72. The welfare implications of MRAs are discussed in p.32-36 of Park, C.H. (2001). *Economic Analysis of Conformity Assessment*.

18.12 The following sections outline the US and EU standards and conformity assessment systems as they currently exist, the challenges in MRA negotiations between them, and begins to establish how the development of a new UK conformity assessment system for standards can ease the creation of MRAs in new trading arrangements with the US in particular, with a view to longer-term conformity assessment harmonisation.

## THE US AND EU STANDARDS AND CONFORMITY ASSESSMENT SYSTEMS:

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### US system—Overview of the decentralised rationale of the system

- 18.13 In the US standards development system many US voluntary consensus standards organisations are coordinated by the private, nonprofit American National Standards Institute (“ANSI”). ANSI sets guidelines for groups to follow in managing the consensus-seeking process for establishing standards in a ‘fair and open manner’, accrediting many standards-setting organisations for compliance with these guidelines. It also approves many of the standards these organisations produce, designating them American National Standards.
- 18.14 ANSI has a decentralised organisational structure, its intent being for standards developers and users by industry to manage standards development themselves. ANSI members in the IT industry emphasise international standardisation, and are free to pursue its coordination, while consumer and workplace safety and health standards are developed by organisations with a focus on national standards.
- 18.15 ANSI is a nonprofit organisation, and membership includes approximately 1,300 firms, 35 government agencies, and over 260 technical, trade, labour and consumer groups. ANSI arose from the American Engineering Standards Committee, formed in 1918 as a federation of Standards Developing Organizations (“SDOs”), and was renamed the American National Standards Institute in the 1960s, its principal missions being to coordinate the voluntary consensus standards development system, promote awareness and use of voluntary standards, and represent US interests in international standardisation bodies. ANSI does not need to approve government-set standards.

### Standards Developing Organisations (“SDOs”) under ANSI

- 18.16 SDOs can be divided into membership organisations; professional societies (including academic); and industry associations (by sector) (while ANSI itself can be called an SDO). For instance, the 20 leading nongovernment standards developers by number of standards produced cover a range of sectors: electronics; aerospace; automotive and mechanical engineering; chemicals; and cosmetics. Most formal standards used in the US private sector are developed by private SDOs.
- 18.17 Compared to most systems, the institutional structure of the US standards system is very decentralised, with over 400 private standards developers. Most SDOs are organised around a given industry, profession, or discipline, and around 275 engage in ‘ongoing’ standards-setting; the others have developed standards before, sometimes updating these.

Table 1: Examples of SDOs

<b>FEDERAL GOVERNMENT</b>
<b>Department of Defense</b>
General Services Administration (nondefense procurement)
<b>Other federal (primarily regulatory)</b>
Examples: Environmental Protection Agency, Occupational Safety and Health Administration, Federal Communications Commission
<b>PRIVATE SECTOR*</b>
<b>Scientific and Professional Societies</b>
Examples: American Society of Mechanical Engineers (ASME), Institute of Electrical and Electronics Engineers (IEEE)
<b>Trade Associations</b>
Examples: National Electrical Manufacturers Association (NEMA) Computer and Business Equipment Manufacturers Association (CBEMA)
<b>Standard-Developing Membership Organisations</b>
Examples: American Society for Testing and Materials (ASTM), National Fire Protection Association (NFPA)

\*not including de facto industry standards

(Source: National Research Council, 1995)

18.18 After review, comment, and approval by an SDO's oversight board and membership at large, the organisation may publish a standard. If the SDO uses ANSI-accredited procedures, it may choose to have the standard approved and distributed by ANSI as an American National Standard. ANSI does not review the standard for technical merit but, rather, certifies it was developed in an open, consensus-oriented manner and does not seriously conflict with or duplicate current standards. The standard's usefulness to interested parties in the relevant market sector—manufacturers, purchasers, regulators, testing laboratories, certifiers, and others—largely determines whether it gains widespread acceptance. A technologically obsolete, commercially unviable standard will be neglected and will be discontinued by the SDO.<sup>73</sup>

18.19 The following table defines the three principal types of standards by development process.

73. National Research Council. (1995). *Standards, Conformity Assessment and Trade into the 21st Century*. Washington, DC.



Table 2: Types of US standard

<b>DE FACTO STANDARD</b>	A standard arising from uncoordinated processes in the competitive marketplace. When a particular set of product or process specifications gains market share such that it acquires authority or influence, the set of specifications is then considered a de facto standard. <b>Example: IBM-compatible personal computer architecture</b>
<b>VOLUNTARY CONSENSUS STANDARD</b>	A standard arising from a formal, coordinated process in which key participants in a market seek consensus. Use of the resulting standard is voluntary. Key participants may include not only designers and producers, but also consumers, corporate and government purchasing officials, and regulatory authorities. <b>Example: photographic film speed--ISO 100, 200, 400, etc., set by International Organization for Standardization (ISO)</b>
<b>MANDATORY STANDARD</b>	A standard set by government. A procurement standard specifies requirements that must be met by suppliers to government. A regulatory standard may set safety, health, environmental, or related criteria. Voluntary standards developed for private use often become mandatory when referenced within government regulation or procurement. <b>Example: automobile crash protection—air bag and/or passive seat restraint mandated by National Highway and Traffic Safety Administration</b>

(Source: National Research Council, 1995)

18.20 The largest proportion are developed within the second type, comprising consensus-building activities among private firms, technical experts, customers, and other interested parties (these groups write standards through formal discussion, drafting and review process, members forming consensus on the best specifications for industry and public need, with standards published for voluntary use throughout industry). Standards arising from these processes are termed 'voluntary consensus' standards. Examples range from dimensions of valve fittings in household plumbing to performance characteristics of automotive structural materials. Various private organisations produce voluntary consensus standards, including nonprofit, standards-setting membership organisations and industry and trade associations.

18.21 The public sector also plays a major role in the US standards system. Federal, state, and local government agencies are active in developing standards. Those written by federal agencies for regulatory and procurement purposes comprise more than half the total national standards. These are 'mandatory standards', reflecting imposition through legislation/regulation or via contractual arrangements for government procurement<sup>74</sup> (although these are developed outside the ANSI-coordinated voluntary consensus system, the mandatory and voluntary standards overlap. Many government standards refer to voluntary standards, which then become mandatory).

18.22 The Department of Defense and the General Services Administration, respectively constitute the bulk of federal standards, the remaining standards—mainly technical regulations—being produced by a range of departments and agencies (see Table 3, below). Regulatory standards centre on protecting public health and safety, and examples include the Food and Drug Administration ("FDA"), Occupational Safety and Health Administration ("OSHA"), and the Environmental Protection Agency. Increasingly however, government agencies meet their obligations not by participating in (and adopting) the results of voluntary consensus standards development.

74. National Bureau of Standards (NBS) Special Publication 681. (1984). *Standards Activities of Organizations in the United States* (R.B Toth, Ed.)

Table 3: US government standards developers

<p><b>Agriculture, Department of</b></p> <ul style="list-style-type: none"> <li>Agricultural Marketing Service</li> <li>Federal Grain Inspection Service</li> <li>Field Management Division</li> <li>Standards and Procedures Branch</li> <li>Food Safety and Inspection Service</li> <li>Foreign Agricultural Service</li> <li>Forest Service</li> <li>Engineering Staff</li> <li>Information Resources Management Planning, Review, and Standards Division</li> <li>Packers and Stockyards Administration</li> <li>Livestock Marketing Division</li> <li>Rural Electrification Administration</li> </ul> <p><b>Commerce, Department of</b></p> <ul style="list-style-type: none"> <li>Bureau of the Census</li> <li>Federal Coordinator for Meteorology</li> <li>National Institute of Standards and Technology</li> <li>National Computer Systems Laboratory</li> <li>National Engineering Laboratory and Law Enforcement Standards Laboratory</li> <li>Technology Services—Voluntary Product Standards</li> <li>National Oceanic and Atmospheric Administration</li> <li>National Marine Fisheries Service</li> <li>National Environmental Satellite, Data, and Information Service</li> <li>National Weather Service</li> <li>National Telecommunications and Information Administration</li> <li>Institute for Telecommunications Sciences</li> <li>U.S. Patent and Trademark Office</li> <li>Assistant Commissioner for Information Systems</li> <li>Assistant Commissioner for Patents</li> <li>International Patent Documentation</li> <li>Trademark Examining Operation</li> </ul>	<p><b>Consumer Product Safety Commission</b></p> <ul style="list-style-type: none"> <li>Directorate for Engineering Sciences</li> <li>Directorate for Health Sciences</li> </ul> <p><b>Defense, Department of</b></p> <ul style="list-style-type: none"> <li>Office of the Assistant Secretary of Defense, Acquisition</li> <li>Defense Industrial Supply Center</li> </ul> <p><b>Energy, Department of</b></p> <ul style="list-style-type: none"> <li>Assistant Secretary for Defense Programs</li> <li>Building Technologies</li> <li>Building Systems and Materials Division</li> <li>Building Equipment Division</li> <li>Energy Information Administration</li> <li>Statistical Standards</li> <li>Environment, Safety, and Health Safety and Quality Assurance</li> </ul> <p><b>Environmental Protection Agency</b></p> <p><b>Federal Communications Commission</b></p> <ul style="list-style-type: none"> <li>Office of Engineering and Technology</li> </ul> <p><b>General Services Administration</b></p> <ul style="list-style-type: none"> <li>Information Resources Management</li> <li>Federal Supply Service Commodity Management</li> <li>Public Building Service</li> </ul> <p><b>Health and Human Services, Department of</b></p> <ul style="list-style-type: none"> <li>Centers for Disease Control</li> <li>National Institute for Occupational Safety and Health</li> <li>Food and Drug Administration</li> <li>Regulatory Affairs</li> <li>Health Care Financing Administration</li> </ul> <p><b>Housing and Urban Development, Department of</b></p> <ul style="list-style-type: none"> <li>Assistant Secretary for Housing—Federal Housing Commissioner</li> <li>Manufactured Housing and Construction Standards Division</li> </ul>
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**Interior, Department of the**

Minerals Management Service Rules, Orders, and Standards  
U.S. Geological Survey  
Information Systems Division  
National Mapping Division  
Water Resources Division

**Labor, Department of**

Mine Safety and Health Administration Standards, Regulations and Variances  
Occupational Safety and Health Administration  
Directorate of Safety Standards Programs

**National Aeronautics and Space Administration**

Occupational Health  
Safety, Reliability, Maintainability, and Quality  
Assurance Division

**National Archives and Records Administration**

Archival Research and Evaluation Staff

**Nuclear Regulatory Commission**

Nuclear Regulatory Research

**State, Department of**

U.S. National Committee for the International Telecommunications Union-Telecommunication Standardization Sector

**Transportation, Department of**

Federal Aviation Administration  
Federal Highway Administration  
Maritime Administration  
National Highway and Traffic Safety Administration  
Research and Special Programs Administration  
Standards Division  
United States Coast Guard  
Marine Safety, Security, and Environmental Protection  
Auxiliary, Boating, and Consumer Affairs Division

**Treasury, Department of**

Bureau of Alcohol, Tobacco, and Firearms  
National Laboratory Center  
Internal Revenue Service  
Standards and Data Administration  
U.S. Customs Service  
Commercial Operations  
Research Division—Laboratories and Scientific Services

**Veterans Affairs, Department of**

Acquisition and Material Management

(Source: National Research Council, 1995)

18.23 This is also the field of the National Institute of Standards and Technology (“NIST”) at the Department of Commerce (“DoC”). NIST (established in 1901 as the National Bureau of Standards, with responsibility for developing standards of weights and measures) is not a regulatory agency, but is active in aspects of public and private standard setting. In 1988 the bureau was given the mission of helping industry advance its performance in developing and applying technology. Scientists in its laboratories conduct research in a wide range of physical sciences, one goal being to advance the science of testing and apply the advances to standardisation.

## Connection to International Standards Development

18.24 The two predominant international standards-setting bodies are the International Organization for Standardization ("ISO") and the International Electro-technical Commission ("IEC"). ISO and IEC are private organisations developing standards in nearly all sectors of industry and technology. (The largest exception to their coverage is telecommunications, the area of the International Telecommunications Union ("ITU").) ANSI is the US member of ISO and IEC, the latter through the ANSI-coordinated US National Committee. (In addition, the US has had success obtaining secretariats of ISO and IEC technical committees and subcommittees in industry sectors with high volumes of exports. For example, the US holds the secretariats of ISO/IEC JTC1 for IT; the ISO Technical Committee (TC)20, covering aircraft and space vehicles; ISOTC 61 for plastics; and ISO TC 67 for petroleum industry materials and equipment. All these committees set international standards in industry sectors that are among the top 10 US export industry sectors.)

## Conformity assessment areas

18.25 Conformity assessment is the comprehensive term for measures taken by manufacturers, their customers, regulatory authorities, and independent, third parties to assess conformity to standards: a standard does not have the intended effect if products designed to conform to it do not actually do so. US conformity assessment is also relatively decentralised, consisting of four areas (the terms used being for manufactured products in particular, although the same concepts apply to processes and services).

18.26 The first area in US understanding is 'manufacturer's declaration of conformity', an assessment by the manufacturer based on internal testing and quality assurance mechanisms; the second is 'testing of products, parts, and materials', done by independent, typically private laboratories for manufacturers; the third is 'certification', meaning formal verification by an unbiased third party through testing and other means, that a product conforms to specific standards (examples of certification include the Underwriters Laboratories product safety certificate). The final area is 'quality system registration', the result of independent audit and approval of the manufacturer's quality system (a quality system being a management system, including procedures, training, and documentation, for ensuring consistency in product quality).<sup>75</sup>

## THE EUROPEAN UNION SYSTEM

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### Overview of standards and conformity assessment

18.27 Before the creation of the EU, each country imposed its own technical requirements, with varying standards and conformity assessment procedures forcing exporters to target smaller numbers of countries. The new laws which were created by Brussels at the end of the 1990s were called the New Approach Directives,<sup>76</sup> with regulation of relevant products fairly generic and broadly limited to 'Essential Health and Safety Requirements'. The table 4 outlines the range of these:

<sup>75</sup> National Research Council. (1995). *Standards, Conformity Assessment and Trade into the 21st Century*. Washington, DC.

<sup>76</sup> National Institute of Standards and Technology (2000). *NIST Special Publication 951: A Guide to EU Standards and Conformity Assessment*. (Delaney and van der Zende, Eds.)

Table 4: The New Approach Directives

DIRECTIVE REF.	DIRECTIVE SUBJECT
90/396/EEC	Appliances Burning Gaseous Fuels
93/68/EEC	CE Marking Directive (Council Directive Amending Other Directives)
89/106/EEC	Construction Products
89/336/EEC	Electromagnetic Compatibility
96/57/EC	Energy Efficiency Requirements for Household Electric Refrigerators, Freezers, and Combinations Thereof
94/9/EEC	Equipment and Protective Systems in Potentially Explosive Atmospheres
93/15/EEC	Explosives for Civil Uses
96/48/EC	Interoperability of Trans-European High-Speed Rail System
95/116/EC	Lifts (Elevators)
73/23/EEC	Low Voltage Equipment
98/37/EC	Machinery, Safety of
96/98/EC	Marine Equipment
90/385/EEC	Medical Devices: Active Implantable
93/42/EEC	Medical Devices: General
98/79/EC	Medical Devices: In Vitro Diagnostic
90/384/EEC	Non-Automatic Weighing Instruments
94/62/EC	Packaging and Packaging Waste
89/686/EEC	Personal Protective Equipment
COM(93)322	Precious Metals (Not Formally Proposed)
97/23/EC	Pressure Equipment
87/404/EEC	Pressure Vessels, Simple
1999/5/EC	Radio Equipment and Telecommunications Terminal Equipment and The Mutual Recognition of Their Conformity
94/25/EC	Recreational Craft
88/378/EEC	Toys, Safety of

- 18.28 The point of the New Approach Directives was to eliminate differences between national laws, thus eliminating barriers to trade between member states. Differences in national standards, and testing and certification procedures however were also central trade barriers, and a new scheme for technical harmonisation was deemed necessary. This was implemented in two major Decisions: a) the Module Decision, and b) the regulation on CE Marking (detailed below). This policy was called the Global Approach, incorporating conformity assessment procedure into New Approach Directives.<sup>77</sup>
- 18.29 First, the Module system varies in complexity. For instance, Module A permits manufacturers to take responsibility for conformity assessment, and if a product is manufactured to Harmonised Standards and the risk not unusually high (e.g. in most machinery), manufacturers can rely on internal manufacturing checks, compiling a Technical File, issuing a Declaration of Conformity to appropriate directives and standards, applies the CE mark and may place a product on the market. Some Modules (e.g. for active implantable medical devices) however could call for type examination, and a production quality assurance system. In Europe, these are designated by the Commission authorities, and are named Notified Bodies.<sup>78</sup>

### The EU standards institutions

- 18.30 The overall direction of standards is now set by the European Commission, issuing directives listing the relatively little-detailed 'essential requirements' for safety that regulated products must meet. The Commission has officially delegated to the private sector the writing of new technical standards linked to EU-wide essential requirements, but these directives set a required level of safety without dictating the means by which it should be achieved.
- 18.31 Pan-European technical standards are being developed, under contract with and funded by the Commission, by three private standards-developing organisations (in a much more *dirigiste* structure than in the US). These are the European Commission for Standardization ("CEN"), the European Commission for Electrotechnical Standardization ("CENELEC"), and the European Telecommunications Standards Institute ("ETSI"). The members of CEN and CENELEC are national standards bodies from across Europe; ETSI membership is more *ad hoc*, including national telecommunication agencies, manufacturers and industry associations. Standards developed by these organisations play a central role in determining the products that may be marketed in Europe.
- 18.32 CEN, CENELEC, and ETSI standards are not the only standards the EU will accept as meeting essential product directives—products complying with other standards are acceptable, as long as the alternative standards also meet essential EU requirements. The burden of proof in such cases however is on manufacturers. This means product approval is easier to obtain through compliance with the CEN/ CENELEC/ETSI standards, and direct participation in their standards-writing work is thus of clear benefit to firms marketing regulated products in Europe.
- 18.33 Unlike most US standards-developing organisations, CEN, CENELEC, and ETSI are not usually open to foreign participants, and US firms (for example) without major European subsidiaries

<sup>77</sup>. *Ibid.*

<sup>78</sup>. *Ibid.*

must use other avenues to influence their standard-setting work. An outline of the three main European standards-developing organisations is as follows:<sup>79</sup>

**CEN:** *Comite Europeen de Normalisation* (European Committee for Standardization). Based in Brussels, CEN has a membership consisting of the national standards-writing organisations of 18 European countries (the EU and EFTA members). CEN develops voluntary European Standards in all product sectors excluding the electrical standards covered by CENELEC. With funding from the European Commission, CEN also writes standards to meet the 'essential requirements' for product safety mandated in EU product directives. The standards work programme is directed by seven sector boards, in building and civil engineering; mechanical engineering; IT; workplace safety; healthcare; heating and cooling; and transport and packaging.

**CENELEC:** *Comite Europeen de Normalisation Electrotechnique* (European Committee for Electrotechnical Standardisation), also based in Brussels and with 18 European standards bodies ('national electrotechnical committees') as members. CENELEC develops European Standards for electrotechnology, including electricity generation, consumer electronics, electromagnetic compatibility, and IT (however international standards developed by the International Electrotechnical Commission ("IEC") are the basis for 89 percent of CENELEC standards). Around 35,000 technical experts participate in the standards-writing committees of CENELEC.

**ETSI:** the European Telecommunications Standards Institute, based in Sophia Antipolis, France, but has a cooperation agreement with the CEN/CENELEC structure. Membership is composed of the public telecommunications administrations of EU and EFTA nations, as well as manufacturers and trade associations. ETSI develops European Telecommunications Standards in particular, which may be adopted as mandatory by European national telecommunications systems. To hasten the standards development process, ETSI has due process procedures that require less consensus than CEN and CENELEC.<sup>80</sup>

18.34 It is also useful to note the role of the European Organization for Testing and Certification ("EOTC"):

**EOTC:** European Organization for Testing and Certification. In 1991, CENELEC and CEN (reluctantly) agreed with the EC for the founding of the EOTC, formed to coordinate national bodies engaged in the certification process. As the EOTC is to some extent a competitor to ETSI, this has caused confusion for business, and the replication of activity. The EOTC Council is composed of fifteen members from various industrial and national interests and is a coordinating body with the various other standards organisations above, while gathering ad hoc committees on various industrial sectoral questions. EOTC is intended as a monitoring forum to monitor industry concerns and opinion on standards and conformity.

79. Egan, M. (2001). *Constructing a European Market: Standards, Regulation and Governance*. Oxford University Press

80. National Institute of Standards and Technology (2000) states: 'There is a relationship between US standards activities and those in the EU. Two organisations, the American National Standards Institute (ANSI) in the United States, and the International Organization for Standardization (ISO) in Geneva, Switzerland, act as bridges to CEN, and ANSI, via the United States National Committee (USNC), and the International Electrotechnical Commission (IEC) in Geneva, Switzerland, act as bridges to CENELEC' (National Institute of Standards and Technology (2000). NIST Special Publication 951: *A Guide to EU Standards and Conformity Assessment*. (Delaney and van der Zende, Eds.)).

- 18.35 Each member state is responsible for overseeing the certification bodies within its own jurisdiction, and must notify the European Commission's Enterprise Directorate-General ("DG") of its approvals. These testing and certification laboratories thus called 'notified bodies'. However national organisations replace national standards with EU standards whenever they are decreed.
- 18.36 To the extent that European standards vary (without apparent justification) from international standards in equivalent sectors, they also represent barriers to imports from outside Europe (although this danger is somewhat reduced by the CEN and CENELEC pledges to defer writing standards when ISO and IEC standards exist or are under development in the same product sectors: this underscores the importance of US industry participation in ISO/IEC committee work). Direct participation in CEN, CENELEC and ETSI standards development is prohibited, however, for US firms without a very substantial European presence, but foreign firms have access to participate in the US voluntary consensus standards system.
- 18.37 Harmonised Standards are therefore standards that support European legislation, and have been a) mandated by the EC, b) developed by the European Standards Bodies above, c) address essential requirements of the New Approach Directives, and d) notification of their development has been published in the *Official Journal of the European Communities*.
- 18.38 As mentioned above, technically speaking the use of a Harmonised Standard is voluntary, in that manufacturers can choose to use a Harmonised or non-Harmonised Standard (e.g. a US standard). However using anything other than a Harmonised Standard will put the burden of proof that the product meets essential requirements on the manufacturer, and will sometimes not be recognised by insurers, lenders, retailers, conformity assessment bodies, and may limit acceptance of a product by the market, especially when a European Standard already exists.<sup>81</sup> Meanwhile, as we have seen, in product sectors where third-party product testing, certification, or quality system registration is required by law, approval may be granted only by organisations designated, or 'notified', to the Commission by the member states as technically competent. Only 'notified bodies' give final product approval for the European market.
- 18.39 Certified products are identified with the European 'CE Mark', and those without the CE Mark cannot be marketed in Europe. The requirement that final assessments be performed by European notified bodies raises the costs of testing and certification to US manufacturers in many sectors (and the contrast with the US system presents an opportunity for a new voluntary/private-led system in the UK).
- 18.40 The CE Mark is 'not a quality mark, nor is it a mark for consumers. Intended for Member State authorities, it is the visible sign to those authorities that your product is in compliance with the New Approach Directives'<sup>82</sup> (compliance also requires determining which directives apply to the product, as a product may be regulated by more than one directive). Most products covered by New Approach Directives can be self-certified by a manufacturer and do not require intervention of a Notified Body. To self-certify, manufacturers must assess product conformity to applicable directives, and standards if applied. Manufacturers may affix the CE mark to products, and prepare and sign the Declaration of Conformity, providing the manufacturer

81. National Institute of Standards and Technology (2000). NIST Special Publication 951: *A Guide to EU Standards and Conformity Assessment*. (Delaney and van der Zende, Eds.)

82. *Ibid.*



can prove conformity to applicable requirements (manufacturers must provide proof in the Technical File). Some (higher risk) products may not be self-certified, but must be subject to EU type examination through inspection by a Notified Body<sup>83</sup> (i.e. in Europe, or by a subsidiary or subcontractor, excluding MRA products).

- 18.41 Even with mutual recognition in place, a 142-page Commission report on the 'Evaluation of the Application of the mutual recognition principle in the field of goods' for the Commission suggests that the principle (*between* EU member states) 'is still not achieving its objectives', particularly as knowledge of the principle is generally at a rather low level among companies and member state authorities. Implementation is so problematic that *Business Europe* (a trade body) has complained that national standards are interfering with the goods' circulation. In the round, MRAs and harmonisation are more realistic in a condition of 'mutual trust between states'.<sup>84</sup>

## THE DIFFICULTIES THE US HAS FACED IN ITS MRAS WITH THE EU

- 18.42 The EU expectation of the negotiations was that an MRA with the US would create formal US government assurance that US entities within an MRA are competent to perform 'essential' services in inspection and certification. For US producers, before this, US firms had three ways to obtain required third-party certifications for the EU market: they could ship samples to Europe to be tested and certified through a European 'notified body', pay expenses for European inspectors to inspect their plants in the United States, or could have testing and certification performed by one of a number of US subsidiaries of European laboratories (in some product sectors they could also have testing performed by a US laboratory subcontracting to a European certifier. In this case, the US laboratory performs the tests, forwarding test data to a European laboratory for evaluation and final approval to obtain a CE Mark). However, without MRAs in a given sector, all three of those avenues exclude US testing laboratories from the final stage of certification, constituting a barrier to US exports. Under MRA, US organisations are also performing testing and certification of exports to the EU, as mutual recognition involves US government involvement in guaranteeing the competence of private US conformity assessment organisations before they are accepted by EU regulatory authorities.

- 18.43 The Office of the US Trade Representative and the Commission's Trade Directorate-General ("DG") led the negotiations of the MRA framework agreement. Each annex was negotiated by the regulatory agency or agencies responsible for the sector. On the European side, the process was simpler because of the centralisation of the relevant agency officials within DG Enterprise, and their experience of coordinating the goals of regulation and trade within a single market. In the US however, separate (and independent) federal agencies negotiated annexes.<sup>85</sup> Negotiations were slowed by European negotiators' concern about the complexity of the US conformity assessment system, with its variety of private certification systems. (They noted, for instance, the lack of a US national or North American mark for entry into the United States, Canada, and Mexico analogous to the European 'CE Mark', which may still allow in the UK-US context, the ultimate aim of more regional multi-country marks in the longer-term.) Brussels officials were also concerned about the ability of US regulators to guarantee competence and

83. *Ibid.*

84. Schmidt, S.K. (2007). 'Mutual Recognition as a New Mode of Governance.' *Journal of European Public Policy*, 14: 5, pp.668-687.

85. Nicolaidis, K. and Shaffer, G. (2005). 'Transnational Mutual Recognition Regimes: Governance Without Global Government.' *Law and Contemporary Problems*. 68, pp.263-317

quality of US conformity assessment bodies, and as a result in the US, NIST created the National Voluntary Conformity Assessment Program.

- 18.44 On each side of the Atlantic, businesses have worked through the Transatlantic Business Dialogue ("TABD") to promote MRAs in policy.<sup>86</sup> TABD has since highlighted areas of concern and put pressure on officials to timetable MRAs (Paula Stern, former chair of the US International Trade Commission and advisor to TABD, stated, 'TABD quickly established the Trans-Atlantic Advisory Committee on Standards, Certification and Regulatory Policy ("TACS") to formulate recommendations, organised on a sectoral basis, for the elimination of regulatory barriers between the two economies').<sup>87</sup>
- 18.45 A number of studies of the MRAs assess what spurred these agreements, the actors participating in negotiation, the constraints on their implementation (both political and market forces), and ultimately the prospects and limits for their adoption in other areas (these papers may help inform future US-UK MRAs and how they can improve upon the US-EU agreement that has been signed).
- 18.46 One assessment of the 1997 US-EC MRA (and its six sectoral annexes, which are sometimes informally referred to as separate MRAs) suggests first that the US appears to have implemented most of the changes involved in the MRAs.<sup>88</sup> The US and EU entered into discussion on MRAs in eleven sectors: information technology, telecommunications products attached to public networks, medical devices, electrical safety, electromagnetic interference, pharmaceuticals, pressure equipment, road safety equipment, lawn mowers, recreational boats, and personal protective equipment such as helmets. Negotiators ultimately reduced this to six: telecommunications equipment, electromagnetic compatibility, electrical safety, recreational craft, medical devices, and pharmaceutical good manufacturing practices (a UK-US MRA(s) may as an early priority add the other five areas). Nicolaidis and Shaffer state: 'It has proven impossible, however, to expand this approach to services in which individual US states wield most regulatory power'.<sup>89</sup>
- 18.47 The MRA that was settled upon also established a new transatlantic structure for overseeing implementation. First, the MRA created a Joint Committee of US and EC trade officials meeting twice annually. Second, the annexes created Joint Sectoral Committees, overseeing the separate annexes' implementation. These Committees are important in implementing the MRA, consisting of the actual regulatory authorities who must oversee the protection of health and safety on each side of the Atlantic. In some cases, however, collaboration between these regulatory authorities has reportedly been ineffective—see below).
- 18.48 Businesses and some government representatives hoped US-EU arrangements would be a stepping-stone for reaching MRAs with third countries, leading to increased access to East Asian markets for example. The WTO Agreement on Technical Barriers to Trade ("TBT"), discussed below, and the General Agreement on Trade in Services encourage and give legal support to the expansion of transatlantic MRAs, and can be used to expand future UK/US MRA(s) to broader areas. Under WTO rules, countries that do not 'give mutual satisfaction' to third countries offering 'equivalent' procedures or standards may be subject to WTO anti-discrimination claims under WTO most-favoured nations ("MFN") clauses.

<sup>86.</sup> *Ibid.*

<sup>87.</sup> *Ibid.*

<sup>88.</sup> Shaffer, G. (2002). 'Reconciling Trade and Regulatory Goals: The Prospects and Limits of New Approaches to Transatlantic Governance through Mutual Recognition and Safe Harbour Agreements'. *Columbia Journal of European Law*, 9: pp. 29-77.

<sup>89.</sup> Nicolaidis, K. and Shaffer, G. (2005). 'Transnational Mutual Recognition Regimes: Governance Without Global Government.' *Law and Contemporary Problems*. 68, pp.263-317

- 18.49 While the prospect of these claims remains relatively remote at this stage, business organisations like TABD are already using WTO agreements for additional leverage.<sup>90</sup> More importantly than potential legal claims, each new MRA puts pressure on third countries to enter into negotiations so that their firms are not disadvantaged—a likely 'contagion effect'.<sup>91</sup> Each MRA thus provides leverage to domestic firms to demand new MRAs (e.g. with third country counterparts) to equalise market access. The transatlantic MRA can thus be seen as a step towards the extension of MRAs globally.
- 18.50 With respect to MRAs and conformity assessments, research recommends developing a private-led ecosystem with lighter state oversight. By permitting 'over-extended and under-resourced' state agencies to outsource testing and evaluation to private bodies, state resource can be allocated to areas of higher concern, retaining 'high product and process standards and post-market surveillance controls'. Research suggests that there is no necessary link between private certification and increased risk to public health and safety,<sup>92</sup> provided certification processes are based on high health and safety standards and complemented by regulatory oversight. This means constructing systems whereby government agencies keep oversight of critical regulatory and procurement standards in public health, safety, environment, and national security, with assessment of conformity to those standards performed most efficiently by the private sector. Government should act in an oversight capacity, evaluating private sector organisations as competent to accredit testing laboratories, product certifiers, and quality system registrars.<sup>93</sup>
- 18.51 As the US has given the NIST a mandate to phase out federally-operated conformity assessment activities, with government relying on private activities in all but the most vital cases for public health, safety, environment, and national security, the UK may also receive a similar private sector-led system, with the British Standards Institute ("BSI") given an ANSI-type role in coordinating a private ecosystem of testing relationships, which can also be formally encouraged to develop transatlantic relationships to harmonise UK and US standards. In the US, standards-related trade issues are focussed to some extent on the duties of the Office of the USTR, while the NIST is also involved in helping the USTR in areas related to international standards (the UK may choose to adopt a similar structure in rejuvenating the BSI).
- 18.52 Under a policy of harmonisation of conformity assessment procedures—i.e. a more developed approach than less ambitious MRAs—regulators in separate jurisdictions agree to adopt the same substantive standards and procedures. This harmonisation facilitates trade as well as cross-border regulatory cooperation because of regulators' comfort with similar standards. However, MRAs mean greater challenges for regulatory cooperation because of regulators' unfamiliarity with foreign standards (under a policy of mutual recognition, regulators retain separate standards for internally-produced products, but agree to recognise the other jurisdiction's standards for products imported from it).
- 18.53 The UK/US FTA and its MRAs allow the mutual development of the kind of private-led system as laid out in 17.50 above. This should be the focus of efforts to develop the UK-US relationship, starting with the expansion of MRAs into the 11 sectors original laid out in the 1997 US-EU MRA (see section 17.45).

90. Trachtman, J.P. (2006) *Embedding Mutual Recognition at the WTO*. Tufts University.

91. Nicolaidis, K. and Shaffer, G. (2005). 'Transnational Mutual Recognition Regimes: Governance Without Global Government.' *Law and Contemporary Problems*. 68, pp.263-317

92. Egan, M. (2001). *Constructing a European Market: Standards, Regulation and Governance*. Oxford University Press

93. *Ibid.*

## WTO TBT CONTEXT

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- 18.54 The UK-US agreement is an opportunity for the UK and US to mutually re-commit to the WTO Agreement on TBT agreement. The TBT review process has revealed a number of trade barriers in global trade in this area.
- 18.55 The TBT agreement, or Standards Code, was first incorporated into the Tokyo Round of GATT. TBT, which is binding on all members and aims to help support progress toward market liberalisation worldwide, has important implications for standards set by national, sub-national and regional governments (such as the EU), and private-sector bodies. Here we outline the central elements of the agreement, as well as areas of uncertainty in its implementation and its impact on trade. TBT was clarified in the Uruguay Round (completed 1994), as follows:
- 18.56 'The requirement of transparency and non-discriminatory procedures for issuing product approval was expanded to cover the range of conformity assessment procedures, including testing, certification, accreditation, and quality system registration; encourages mutual recognition of conformity assessment procedures between countries; expands coverage to nongovernmental and regional standards development.'<sup>94</sup>
- 18.57 The TBT states explicitly: 'Members shall give positive consideration to accepting as equivalent technical regulations of other Members, even if these regulations differ from their own, provided they are satisfied that these regulations adequately fulfil the objectives of their own regulations.'
- 18.58 The TBT also states that technical regulations should not be maintained if the circumstances or objectives giving rise to their adoption no longer exist, or if the objectives could be approached in a less trade-restrictive way. Having been expanded to include standards for processes as well as products, the requirement of transparent and non-discriminatory procedures for issuing product approval was also expanded beyond testing and certification to cover the range of conformity assessment procedures. The TBT also applies the principles of national treatment and non-discrimination to product testing and certification programmes, and extends the obligation of national treatment and nondiscrimination to laboratory accreditation, recognition, and quality system registration programmes. As we discuss below, the TBT constitutes progress in extending rules to private standards organisations, such as the ANSI. The Code of Good Practice for the Preparation, Adoption and Application of Standards contained in Annex 3 of the TBT agreement also creates a foundation for extending rules to private standards bodies.
- 18.59 The TBT basis to encourage acceptance of the results of tests or laboratory accreditation across national borders is limited however, though Article 6 of the TBT Code exhorts signatories to move toward harmonisation of conformity assessment through mutual recognition of procedures. Article 6 requires that 'whenever possible, that the results of conformity assessment procedures in other Members are accepted, even when those procedures differ from their own, provided they are satisfied that those procedures offer an assurance of conformity.' Adoption of the Code is voluntary and currently lacks an enforcement mechanism. Efforts by governments to negotiate mutual recognition of conformity assessment procedures may

<sup>94</sup>. Trachtman, J.P. (2006) *Embedding Mutual Recognition at the WTO*. Tufts University.

therefore provide greater likelihood of reduced barriers than reliance only on the TBT, albeit with TBT's encouragement.

18.60 Trachtman<sup>95</sup> analyses how these WTO agreements uphold and encourage MRAs generally, arguing that 'mutual recognition at the WTO, as a type of liberalism, must be embedded in a process of governance that [includes] mutual recognition [and] can only take place to the extent of satisfactory essential harmonisation: to the extent that states can legitimately agree on an appropriate level of regulatory protection. This political process is necessary in order to establish an agreed minimum level of regulation.' Meanwhile, mutual recognition 'is not so much a rule of governance in the normal sense, but a rule of choice of governance': it thus requires trust, entailing 'an agreement to compromise local regulatory autonomy, by accepting that the exporting state regulation is 'good enough.'" MRAs can also allow the maintenance of 'safeguards' allowing states to protect against threats to public policy.

18.61 We have shown the areas where a US-UK FTA would be needed to ensure open trade, competitive markets and property rights protection. However, it is important to look at how feasible such an agreement would be.

<sup>95</sup> *Ibid.*

## 19. HOW POSSIBLE IS A US-UK FTA?

- 19.1 The below is our assessment of the relative ease or difficulty of reaching agreement on each sector in the UK-US FTA, based on the existing political economies in each country. As an overarching theme, one of the challenges for the UK will be balancing its negotiations with the US with the demands of the EU in any parallel FTA, which could affect its ability to be flexible in some areas.
- 19.2 President Trump's statements on withdrawing from TTIP and TPP negotiations have been accompanied by a commitment to reducing the trade deficit. This does not necessarily mean that there is no potential for a US-UK trade agreement. First, Paul Ryan, US Republican Speaker of the House of Representatives, has recently reiterated the commitment to achieving a bilateral trade agreement between the US and the UK.<sup>96</sup> This was also accompanied by the statement that the US will also work closely with the EU to chart a path forward on TTIP. President Trump has also moved from the rhetoric of terminating NAFTA to renegotiation instead. These indicate that there is appetite in the US to continue with trade negotiations and agreements, including with the UK. The point is that by the yardstick the Trump administration uses to measure the relationship, the UK does not present the challenge that less developed or more distorted markets do.
- 19.3 Second, in terms of the statements on reducing the trade deficit, this would not necessarily be a barrier to greater trade with the UK. Interestingly, US and UK trade data show very different pictures of the trade relationship. The UK data for 2015 indicates a trade surplus in goods and services, with UK exports to the US greater than UK imports from the US by £39,318m.<sup>97</sup> The US trade data, however, indicates that the US had a trade surplus with the UK in terms of goods and services of \$12,008m in 2015.<sup>98</sup> Apart from highlighting the challenges with consistency in international trade data, this demonstrates that greater trade with the UK will not necessarily be incompatible with US stated objectives.
- 19.4 Finally, the Trump Administration has stated that it wants 'trade deals that work for all Americans'.<sup>99</sup> The focus is on supporting US manufacturing; the comparative advantage of trade for the UK is in services, particularly financial services, and so in any US-UK trade deal, the UK should not be seen as a direct competitive threat.
- 19.5 Our view of the potential ease of agreement across the specific areas, taking into complexity of subject matter, political will on both sides, against potential payoffs from agreement is illustrated in Figure 3, with specific discussion following.

### FOOD AND AGRICULTURE

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- 19.6 The challenges to an agreement on agricultural products may include the US seeking greater access even in products that the UK produces, such as dairy and meats. Further, any changes

96. <https://www.theguardian.com/us-news/2017/apr/19/paul-ryan-london-visit-us-uk-trade-agreement-brexit>

97. ONS, The Pink Book 2016

98. US Census Bureau and US Bureau of Economic Analysis, *US International Trade in Goods and Services*, February 2017

99. <https://www.whitehouse.gov/trade-deals-working-all-americans>

to required standards is likely to be opposed by consumer groups, as demonstrated by the public outcry and concerns about 'chlorinated chicken' and 'hormone-fed beef' accessing the UK market under an agreement with the US. While an agreement in this area may be relatively simple in terms of complexity of arrangements, it may be politically more difficult. However, to the extent that providing access on agricultural products to the US allows for agreement in other areas that are more important for UK trade, such as financial services, the potential payoffs are large.

## GOVERNMENT PROCUREMENT

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19.7 The new 'Buy American, Hire American' executive order is likely to make an agreement in this area more challenging, particularly if this leads the way for state governments to mandate similar requirements. The outcomes of the review of agencies and of FTAs in this context will provide useful guidance as to the potential use of this policy. The challenge will be with negotiating a special arrangement for the UK with respect to government procurement under BAA.

## DEFENCE

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19.8 The political will of the parties is already aligned in this respect. As both parties already work closely together in the fields of defence and security, and have significant investment in defence industries in each other's territories, it is likely that agreement regarding defence will be straightforward.

## INTELLECTUAL PROPERTY PROTECTION

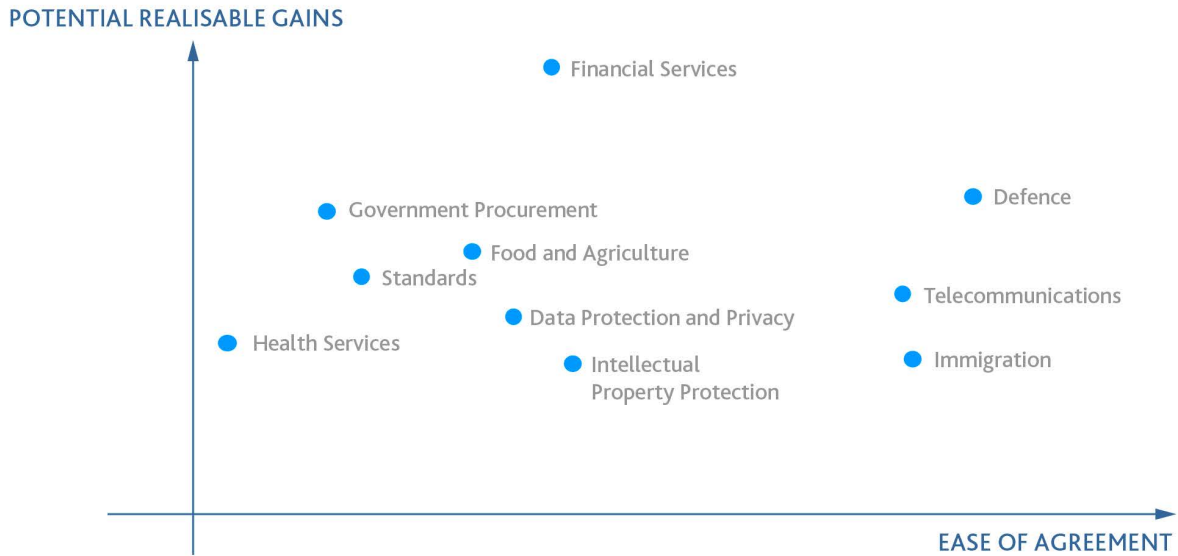
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19.9 The UK and the US will both want to implement strong intellectual property protection, and so this should not present challenges. The challenge rather will be in parallel arrangements with the EU. Strong IP rights will support investment. Any changes however, will also need to consider implications on different sector, and may need to be politically managed, such as through assuaging public concerns about the price of pharmaceuticals rising.

## FINANCIAL SERVICES

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19.10 Transatlantic trade in financial services is relatively free in terms of market access, but the challenge is in removing regulatory barriers, such as through mutual recognition. During the TTIP negotiations, the US was reluctant to include a forum for coordination on financial services regulation; while market access would be included, the US Trade Representative stated that regulatory cooperation was not a trade issue but rather should be discussed within existing other fora. As discussed in section 10, the agreement between SEC and ASIC is indicative that it is possible that the US would be willing to undertake a similar agreement with the UK on mutual recognition in certain areas of financial services.



Above: Figure 3  
Relative ease and  
payoffs from agreement  
across specific key areas

## TELECOMMUNICATIONS

19.11 Both parties will be keen to agree a competitive and free flow of digital services. The US has already shown initial willing to formalise agreement in this space by including provisions to this effect in the TPP. However, the extent to which the UK can be flexible in this area might be restricted by its membership of the Council of Europe Convention on Transfrontier Television and it will need to balance the benefits of retaining such existing commitments against the demands of the US.

## DATA PROTECTION AND PRIVACY

19.12 From the UK perspective, UK lawmakers and consumers have certain expectations as to the use and protection of personal data that the UK may look to have addressed by the US in an FTA, which could also make the parallel negotiation with the EU less problematic.



For example, on 29 March 2017, the Trump administration overturned Federal Communications Commission (“FCC”) rules that required internet service providers (“ISPs”) to obtain consumers’ permission before sharing their browsing history with other companies. The FCC rules had not yet taken effect but would have required ISPs to obtain consumer consent before using their personal data (including precise geolocation, financial information, health information, children’s information and web browsing history for advertising and marketing).<sup>100</sup> This approach is unlikely to be acceptable to UK lawmakers and consumers, and, if no barriers to data transfer to the US from the UK are in place, could result in the EU imposing an absolute barrier to free flow of data to the UK.

## HEALTH SERVICES

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19.13 It is likely that the status quo regarding health care services will be maintained and not formally addressed in the US-UK FTA. The structure and ownership of the NHS is a politically sensitive topic. It was previously reported that the UK government had not ruled out more involvement by US companies in healthcare services as part of a UK-US trade deal,<sup>101</sup> however any such discussions would be likely to delay the finalisation of a UK-US FTA. In any event, there has been little to no appetite from the Trump Administration in this respect.

## IMMIGRATION

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19.14 The Trump administration has been vocal in its defence of pursuing a tough immigration policy, however focus has previously centred on restricting immigration from certain countries for security reasons (not including the UK). In reality, discussions on this issue are likely to be straightforward as both parties will want to agree a mutually advantageous immigration policy with reciprocal rights that ensures a needs-based flow of skilled labour between the jurisdictions. Mutual flows of skilled workers can support greater knowledge exchange and innovation in both countries.

## STANDARDS

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19.15 Earlier sections have discussed in detail the challenges of MRA negotiations between the US and the EU. The challenge for the UK will be to develop a new conformity assessment system for standards that can support the creation of MRAs in new trading arrangements, including with the EU and the UK

19.16 While there will certainly be challenges in negotiating a deep trading agreement, the potential benefits are also high. UK ministers should start engaging with US counterparts immediately to discuss the opportunities for collaboration, and prioritising areas for negotiation and agreement.

<sup>100</sup> <http://www.reuters.com/article/us-usa-internet-trump-idUSKBN1752PR>

<sup>101</sup> <http://www.independent.co.uk/news/uk/politics/theresa-may-donald-trump-nhs-us-trade-deal-brexit-torture-a7548156.html>

## 20. THE WIDER CONTEXT: RELATIONSHIP WITH OTHER US AGREEMENTS

- 20.1 President Trump signed an executive order withdrawing the US from the TPP on 23 January 2017. The ratification process for other countries to sign up to the TPP requires a minimum level of global trade to be covered. Had the US not withdrawn from the TPP, the TPP would have come into force two months after all the original signatories complete their own domestic ratification procedures. The second route for ratification under the TPP is that if at least six countries, which between them represent at least 85 percent of the total GDP of the original 12, have ratified it within two years, the agreement will come into effect. However, due to the extent of the US' GDP, if the US is not a party, the TPP cannot be ratified by the other parties unless the ratification process is changed by mutual agreement. The problem is that many of the countries offered concessions (such as Japan on Agriculture and Vietnam on SOEs) in order to have better access to the US market. If this is no longer on offer, the Agreement itself may make less sense to them. This will be a major stumbling block to the TPP. If the TPP were to survive in its current form, albeit without the US, then it would be possible for the UK to accede to it. That would not be a trivial exercise as it would involve a twelve country schedule negotiation, which would also implicate the UK's WTO rectification process which is moving forward at the same time. However, if the TPP's future is indeed very uncertain, its demise creates an opportunity for the UK. By bringing together like-minded countries whose original high level ambition gave rise to the TPP (such as New Zealand and Singapore whose initial bilateral led to the P4, then the P4 plus 1, then the TPP), these countries could develop a new Prosperity Zone characterised by open trade, competition on the merits as an organising principle and property rights protection, as outlined in 3.1. Note that if TPP were a live agreement, and if agreed with the other parties, on the day after the UK's exit date, the UK could join the TPP.

### NAFTA RENEGOTIATION PROCESS

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- 20.2 The North American Free Trade Agreement ("NAFTA") entered into force on the 1st of January, 1994. Today, it covers 14% of world trade, and 6 million American jobs depend on trade generated with Mexico under NAFTA; a further 8 million jobs depend on trade with Canada.<sup>102</sup> Although a 2014 study found that the agreement costs 15,000 US jobs each year, each one of those jobs lost represents a \$450,000 increase in net welfare effects for the US.<sup>103</sup> NAFTA was the first free trade agreement to accord equal status to partners from the developed and developing world and pioneered advanced standards on IPR and investor-state dispute settlement ("ISDS"). NAFTA was also an early example of a strategic free trade agreement. One of the implicit goals of the negotiation was to prevent any regression on Mexican domestic liberalisation which had begun in the 1980s; it was also seen as a tool for the US to kick-start the slowing Uruguay Round in the WTO.

<sup>102</sup> <https://www.foreignaffairs.com/articles/canada/2013-12-06/naftas-economic-upside>

<sup>103</sup> <https://piie.com/sites/default/files/publications/pb/pb14-13.pdf>

- 20.3 In terms of international trade (especially for the US, Canada and Mexico), the two main legacies of NAFTA are: (1) including non-tariff barriers in free trade agreements in recognition of the fact that NTBs can have an equal if not greater dampening effect on trade than traditional tariff measures; and (2) pursuing free trade agreements in a strategic manner to guarantee the highest-possible standards. These principles can be seen most clearly in the TPP, which began as an FTA between New Zealand and Singapore in 2001 and grew to include advanced economies (e.g., the US, Japan, Canada) alongside small, distorted economies (e.g., Vietnam) in an agreement which tackled state-owned enterprises, competition and other regulatory issues traditionally considered to be the domain of domestic legislatures.
- 20.4 President Trump has pulled the US out of the TPP and formally notified Congress of his intention to renegotiate NAFTA with a view to its “modernization”. The legal process and timeline associated with withdrawing from NAFTA are relatively straightforward, but it should be noted that the US has never formally withdrawn from a trade agreement before (and in only one instance, the US-Canada FTA, has it suspended a trade agreement). Article 22.05 of NAFTA states that “a Party may withdraw from this Agreement six months after it provides written notice of withdrawal to the other Parties”.<sup>104</sup>
- 20.5 As NAFTA is a congressional-executive agreement rather than a treaty (in the context of US law) and its provisions are not self-implementing, a congressional process for repealing the relevant provisions of NAFTA would be required.<sup>105</sup> Under the provisions of NAFTA, withdrawal (and therefore the end of trade preferences) could occur six months after notification; however, the Trade Act of 1974 (which was applied to NAFTA in the implementing legislation passed by Congress) stipulates that trade preferences must remain in effect until one year after withdrawal from a trade agreement, unless the president adjusts the rates/until the president recommends new rates to Congress, which he is required to do within sixty days of exiting an agreement. Again, it is worth noting that this stipulation (from Section 125, subsection (e)) has never undergone judicial scrutiny.<sup>106</sup>
- 20.6 The legal process and timeline associated with renegotiating NAFTA are far more fluid. The Congressional Research Service has stated that it is ‘likely’ that a fully renegotiated deal would have to be approved by both houses of Congress.<sup>107</sup> Article 22.02 of NAFTA provides for the modification of the agreement but does not specify how modifications would/should enter into force. The President would have the authority to unilaterally enact certain changes relating to tariff lines or rules of origin, but his authority is less clear on more complex provisions including ISDS. A 90-day congressional consultation process is required before the US formally enters into a renegotiation of the agreement; this has now been commenced. A document released by the Mexican Foreign and Economic Ministries in late January 2017 suggested that consultations had begun simultaneously with a similar process in Mexico.
- 20.7 On 18 May 2017, USTR Robert Lighthizer wrote to Congress, triggering the NAFTA renegotiation process. This letter initiates a 90 day process of consultations, after which the US will open negotiations with Canada and Mexico. The letter sets out the USTR’s key objectives for the renegotiation. Prior to the letter, there had been much speculation as to what that renegotiation would involve. It was not clear whether President Trump meant to withdraw the US from of NAFTA

104. <https://www.nafta-sec-alena.org/Home/Legal-Texts/North-American-Free-Trade-Agreement?mvid=1&secid=d5a8ba07-1fb2-4f28-88d0-a8eac08611a2>

105. <https://fas.org/sgp/crs/misc/97-896.pdf>

106. <https://fas.org/sgp/crs/misc/R44630.pdf>

107. <http://www.strtrade.com/news-publications-NAFTA-renegotiate-president-Congress-020117.html>

completely, or whether would seek to impose punitive tariffs on imports from Mexico. Instead, and contrary to much of the speculation, President Trump's trade envoy has signalled that the US will aim to modernise the NAFTA by adding provisions on regulatory practices, state-owned enterprises ("SOEs") and intellectual property rights (among other things). Many of these matters are dealt with extensively in the TPP, and it is likely that any new NAFTA provisions will be drawn from the provisions of the TPP in these areas.

- 20.8 Broadly these objectives, especially the provisions on SOEs and regulatory practices, are intended to deal with behind the border barriers to trade, regulatory issues and anti-competitive market distortions. These objectives have not been newly devised for this process, but represent an evolution of ideas to deal with the realities of trade in the 21st century.<sup>108</sup> These ideas were initially included in the US-Singapore agreement where provisions to deal with SOEs were added. There has been a gradual evolution of the SOE issue from a concern about the nature of ownership (the US-Singapore agreement contains a detailed annex which is focused on identifying what type of entity qualifies as an SOE) to a concern about the effect of the SOE on global trade if it benefits from state privileges and immunities that lead to an artificial reduction of cost. A NAFTA renegotiation could play a significant role in this area. Stronger measures in these areas which guarantee both free and fair trade are to be welcomed, and such changes would make it easier for the UK to come to an agreement with the US, and to even contemplate potential NAFTA accession in the future. It should be noted however that while there is currently bi-partisan support for a bilateral agreement between the UK and the US, it is not a given that there would be the same support for a UK NAFTA accession (or the necessary support from Canada and Mexico).
- 20.9 Although not specifically referenced in the letter, rules of origin dictating the percentage composition of a product required for it to qualify for preferential tariff rates will also be a likely topic of discussion. Any move to raise the percentage required to qualify under rules of origin would be designed to increase sourcing from the US, particularly for Mexican manufacturers; however, such a move would likely hurt US manufacturers more than their Mexican counterparts. Mexico has the option to trade at an average 2.5% tariff with the US under the non-preferential MFN rates and would therefore face little economic pressure to dramatically change its sourcing practices. Likewise, any further restrictions on government procurement (e.g., strengthened requirements for the Buy America programme) could be expected to bring equal retaliatory measures from the Mexican government. As major American firms have far greater economic ties with the Mexican government (e.g. Microsoft) than do their Mexican counterparts with the US government, this would seem doubly unwise for US taxpayers.
- 20.10 A host of **non-trade issues** could also be expected to feature prominently. The Trump administration has a particular interest in stemming the tide of illegal immigration, drug and arms trafficking from Central America through Mexico, and would probably demand further cooperation on these issues in exchange for continued free trade. **Investor-state dispute settlement** would also be a likely flashpoint, as it enjoys little domestic support or understanding in the US and Canada. The **environment and labour** side letters which accompanied the original agreement might well be revised or expanded. President Trump won an unexpected berth of support in the

<sup>108</sup> See *Trade Tools for the 21st Century* *ibid*

labour union-strongholds of Michigan, Pennsylvania, Ohio and Wisconsin on protectionist rhetoric; while he does not enjoy good relations with established labour (the AFL-CIO), he may well attempt to strengthen the labour side letter to win further favour with those voters. Similarly, President Trump has shown little interest in the environmental movement, but might use the environmental side letter to further restrict trade, especially in manufactured goods, on the basis that Mexican environmental standards are weaker than those in the US. He will at the same time be looking to weaken US environmental protections. Trump has already taken several steps to do this domestically. On 28 March 2017, Trump signed an executive order instructing US environmental regulators to make key changes to existing rules relating to the lowering of carbon emissions, including lifting a moratorium on federal coal leasing and removal of the requirement that federal officials consider the impact of climate change when making decisions.

- 20.11 Re-opening NAFTA presents some opportunities for Mexico and Canada. The US has many vulnerabilities in the area of behind the border barriers (see earlier sections and appendices). Access for all parties could be increased in several sectors, including but not limited to: maritime, ground transport, medical tourism, defence contracting, and antitrust standards. For example, the Jones Act restricts foreign-flagged vessels from delivering cargo to multiple US ports<sup>109</sup> and was carved out as an exemption in NAFTA; ground transportation as a cross-border service is also restricted, save in designated commercial zones near the border. These restrictions represent real costs to American, Mexican and Canadian consumers; one estimate puts the cost of the US-Mexico ground transport restrictions at \$400 million a year.<sup>110</sup>
- 20.12 One of the many things the Trump administration should consider is improving the existing trade adjustment assistance (“TAA”). Wage insurance provides a guaranteed income (some percentage of a worker’s annual salary) for several years after their job is moved abroad; trade adjustment assistance more broadly provides retraining and relocation services. Wage insurance, while costly, might be an acceptable proposition if applied only to those workers who are 60 years of age or older, as this demographic is the least likely to be retrained and the least likely to find new gainful employment. However, TAA has historically not been very effective. In a study by the American University, Washington D.C.,<sup>111</sup> it was found that TAA participants earned 30 percent less on average than they made in their previous positions before entering the programme. In a comparison group made up of individuals that didn’t receive TAA training or benefits, a reduction in wages was identified, but only by 9.4 percent. A further study by policy research firm Mathematica found the costs of TAA outweighed the benefits by nearly \$54,000 per participant.<sup>112</sup> Accordingly, any policy suggesting this alone as a way of solving trade concerns is unlikely to be effective.
- 20.13 Applying an ACMD-based metric to imports from Mexico might also allay American fears of unfair competition. Unlike the triggers for anti-dumping measures and counter-vailing duties, anti-competitive market distortions include all non-competitive benefits bestowed upon a firm or product, such as laws and regulations that eliminate or suppress competition, differential application of laws and regulations, activities of state owned enterprises and anti-competitive state aid and support.<sup>113</sup> Operating a mechanism to address these matters in NAFTA would allow the US to impose tariffs on imports from Mexico and Canada where a domestic producer is able to

109. The Jones Act requires US-flagged carriers to conduct traffic and cargo operations between US ports.

110. <http://www.coha.org/us%E2%80%93mexico-nafta-transportation-agreement-imperiled/>

111. <http://w.american.edu/cas/economics/repec/amu/workingpapers/2008-12.pdf>

112. <https://www.mathematica-mpr.com/our-publications-and-findings/publications/the-benefits-and-costs-of-the-trade-adjustment-assistance-taa-program-under-the-2002-amendments>

113. As further identified and described by Shanker A Singham and Molly Kiniry in *Introduction to Anti-Competitive Market Distortions and the Distortions Index* (September 2016)

demonstrate that: i) they have suffered harm; ii) as a result of a distorting measure by the exporting country's government; iii) that has an anti-competitive effect in the relevant market.

- 20.14 In terms of the impact that the NAFTA renegotiation will have on the UK's trade negotiating prospects post-Brexit, most options are broadly positive. The complete implosion of NAFTA would make Canada and Mexico more open to a fully liberalised Prosperity Zone than they might be given the uncertainties of NAFTA. Any reduction in the scope of NAFTA leading to a loss in North American trade would also make Canada and especially Mexico more likely to seek out some form of hedge against what the US might do *vis a vis* NAFTA.
- 20.15 If the NAFTA renegotiation deals with the issue of ACMDs in a positive manner, then it is very likely that the NAFTA countries can accede to the emerging Prosperity Zone. Indeed, such a transition would be a great advantage for such an agreement.
- 20.16 Any NAFTA renegotiation would have to be approved by Congress, and Congressional approval of substantial changes to the NAFTA that would restrict trade and risk existing supply chains is unlikely.

## US BORDER TAX PROPOSAL

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- 20.17 House Speaker Paul Ryan and Ways and Means Chairman Kevin Brady have released a Blueprint for revising the US tax code which has received support from the Trump administration. It seeks to "fuel job creation and deliver opportunity for all Americans, simplify the broken tax code and make it fairer and less burdensome, and transform the broken IRS into an agency focused on customer service." Professor David Bradford's work on developing an X tax—a progressive VAT-model tax which could be used in the US—is the intellectual basis of this proposal. The proposed reforms include collapsing the current seven-tier bracket system for income tax into just three tax brackets. Under the new plan, income taxes will be levied at rates of 35 percent, 25 percent and 10 percent. In addition, the proposals include a reduced rate for small businesses and corporations.
- 20.18 Under this proposal, companies would be taxed at a rate of 20% on their cash flow in the US, minus the cost of labour, the cost of US goods, and the cost of services (the border adjustment applies only to goods, so all services would remain deductible from the tax base). This is functionally a VAT tax of the consumption type, fundamentally focused on determining cash flow. It is designed to deter companies currently operating in the US from leaving for lower-tax or lower-cost markets and then exporting their products back to the US. It would correct many of the current inconsistencies in the US tax code, including the fact that labour is taxed twice, and that foreign investment is essentially subsidised by the ability to easily invest abroad and repatriate revenues at low tax rates. It would discourage consumption and incentivise saving and investment at the personal and corporate levels.
- 20.19 It is important to note that this Blueprint is still in draft form and subject to further revision in the House before it goes to the Senate, where Sen. Ron Wyden of Oregon, the ranking member on the Senate Finance Committee has already expressed scepticism (Sen. Wyden's home state is also the headquarters of Nike, a company highly dependent on the ability to cheaply import foreign-made goods). Sen. Ben Cardin of Maryland has begun drafting a response to Speaker Ryan's

CURRENT US SYSTEM	PROPOSED US TAX SYSTEM (IN CONGRESS)
<ul style="list-style-type: none"> <li>• Income tax for corporations and individuals</li> <li>• Corporate income is taxed at 35%</li> <li>• Many personal and corporate deductions exist, including carried interest</li> <li>• A universal taxation system; companies and individuals are taxed on their income at home and abroad</li> <li>• Labour is effectively taxed twice—first for corporations, and again for individuals</li> </ul>	<ul style="list-style-type: none"> <li>• Eliminates corporate and personal income tax</li> <li>• A true territorial tax system</li> <li>• Replaces corporate income tax with a border-adjusted tax of 20%</li> <li>• The border-adjusted tax will be based on cash flow with labour costs deducted</li> <li>• Eliminates carried interest</li> <li>• Simplifies/reduces many exemptions currently in place</li> </ul>

proposal, which more closely resembles a credit and invoice VAT system. It is likely that in the conference negotiations between House Ways and Means and Senate Finance, a more moderate proposal will be brought forward. It is also worth noting that the White House may press for further amendments—President Trump has historically expressed a preference for simple tariff barriers, stating that this proposal is “too complicated”.

20.20 A proposal along these lines could impact US-UK trade, and a potential US-UK FTA, in a variety of ways. First, the Double Taxation Agreement of 2002 is predicated in part on the US corporate and personal income tax system, and so some modification of the Agreement will likely be required (failing that, ‘income tax’ will have to be left on the Federal Register in the US in a nominal way so as to keep the relevant provisions of the Agreement valid). Second, it would disadvantage goods exports from Britain to the US. The US is the UK’s biggest export market (£47 billion in goods, £53 billion in services, in 2015). Britain’s services exports would not be affected by this proposal. Third, and perhaps more significantly, this new tax code would remove the current incentives for foreign investment by US corporates solely driven by tax reasons. The UK is the largest beneficiary of US FDI, and would likely suffer a cash crunch under this new system. A sudden, sharp reduction in FDI from the US could systemically increase the cost of doing business across the UK.

20.21 At the time of writing it this proposal seems to have lost favour with the White House, and has been widely opposed by import-reliant retailers (though welcomed by exporters), but is still being supported by Brady and Ryan,<sup>113a</sup> so may progress in some form. Even if this reform is abandoned, issues on taxation will remain, and HM Treasury should begin conducting conversations with the US Treasury Department to scope out the possible implications of this Blueprint on the Double Tax Agreement, and express the interests of British industry in maintaining the free flow of goods, services and investment across the Atlantic. This would likely be a more productive route for achieving HMG’s goals on international tax policy than continuing the Base Erosion and Profit Shifting (“BEPS”) talks in the OECD. There is palpable hostility in the US treasury regarding the UK’s role in BEPS. A shift in focus by the UK would be warmly received in Washington.

<sup>113a</sup> <https://www.bloomberg.com/politics/articles/2017-05-23/house-chief-tax-writer-signals-openness-to-gop-plan-alternatives>

## 21. THE WIDER CONTEXT: UK'S SIMULTANEOUS NEGOTIATIONS WITH US AND EU

21.1 The fact that the UK will be simultaneously negotiating with the UK and EU presents opportunities and challenges. We have summarised the opportunities and challenges below.

### OPPORTUNITY

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21.2 In many areas of law and regulation the UK sits between the US and EU. Negotiating with both parties at the same time means that the UK can act as a bridge between the US and EU in certain key areas. For example, the UK has a commitment to animal welfare which it would wish to continue to have enshrined in its regulatory system, and such an “ask” would be a difficult issue to consider in a US-UK agreement. However, the UK may be prepared to give on some of the difficult SPS issues in poultry and beef as long as animal welfare issues were properly addressed in the agreement, particularly with respect to specific hormones such as ractopamine. Such an outcome would ease the difficult agricultural issues in an UK-EU agreement.

### CHALLENGES

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21.3 The specific challenges associated with the UK negotiating jointly with the EU and the US are obvious. In areas where the US and EU regulate in very different ways, and it may not be possible in certain cases to have an agreement that works for both parties and enables a single supply chain across the US-UK-EU region. Too much divergence between US/UK regulatory system and the EU regulatory system will make it difficult for UK entities to trade simultaneously with the US and the EU, unless they produce separately for both markets, and sometimes it is simply not possible to service both markets due to directly conflicting SPS measures, for example. For example, in financial services, the UK-EU arrangements will start from a point of regulatory convergence. However, the US-UK agreement may drive towards principles-based, pro-competitive regulation and (together with the UK's domestic concerns) therefore increase the possibility of regulatory divergence between the UK and EU. Managing this divergence will be one of the great challenges for coordinating across both of these agreements. There are a number of other specific areas where challenges arise.



## DATA AND PRIVACY ISSUES

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21.4 Other countries, notably the Swiss have had to manage these divergences and the Swiss approach is to adopt its own version of GDPR which it hopes will be compatible with the rules of the EEA. The Swiss model of the GDPR has the following key differences:

For example, the Swiss draft DPA is less strict in the following areas:

- a) Consent requirements (GDPR says consent cannot be bundled with other issues).
- b) Data coverage is less
- c) More information to be provided to data subjects for GDPR
- d) Under GDPR, no-EU processors of data must appoint an EU based processor no matter how minor their data processing role actually is.
- e) DPA is generally less prescriptive than the requirements of GDPR
- f) DPA fines are much lower (GDPR fines are up to 4% of annual turnover).

The question is whether the Commission will accept the Swiss DPA as ensuring adequate protection for EU citizens' data, and maintains Switzerland's position on its approved whitelist, allowing transfer of personal data to Switzerland without further safeguards. This negotiation will indicate the room for manoeuvre of the US and UK in their agreements.

## FINANCIAL SERVICES

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21.5 The simultaneous negotiations between the US and EU present serious issues in financial services. In order to ensure that UK firms can continue to transact business in the EEA without being locally licensed and supervised, there will have to be some sort of mutual recognition and ongoing co-ordination of regulation, especially prudential regulation. We set this out in our paper *A New UK/EU Relationship in Financial Services—a Bilateral Regulatory Partnership*.<sup>114</sup> The question is whether this can be extended to include the US and other countries. If dual regulation systems are also governed by principles that allow the regulation and supervision of financial services providers of one jurisdiction to be recognised in the other, subject to compliance with international and other agreed parameters, and the parties to the US-UK agreement agree to work cooperatively in the international sphere to ensure that global standards reflect consumer welfare enhancing regulation, this will itself lead to greater levels of innovation. International financial services institutions will want to operate in such environments and these principles will also be important for consumers of those services.

21.6 Financial centres such as Singapore, Hong Kong, London, New York and Zurich have an interest in a common approach which will maximise consumer welfare, and thus innovation and wealth creation.

<sup>114</sup> <http://www.li.com/activities/publications>

## 22. CONCLUSION

- 22.1 We recommend that any agreement between the UK and the US should be comprehensive and deal with as many of the historic demands of both sides as possible. There is a temptation on both sides for a “quick win” and a political agreement which will benefit the UK in its negotiations with the EU. This temptation should be resisted. There are real gains for both the UK and the US in a comprehensive free trade agreement. There are also advantages to negotiating with the US and the EU at the same time, which will be necessary for the UK to act as a bridge between the two. While this “triangulation” also presents challenges, a wise negotiator will seek to maximise the opportunities whilst realistically tackling the challenges.

## APPENDIX 1

### US Barriers

	US BARRIERS	EFFECT
<b>Agriculture</b>	Agricultural Adjustment Act (1938), Agriculture Act (1949), Commodity Credit Corporation Charter Act (1948) and the Farm Act (2014) form the basis of US agricultural subsidies	The extensive subsidisation of US agriculture distorts the market in favour of domestic producers and certain crops, adding an extra barrier for foreign producers to export to the US market.
	Special Agricultural Safeguard measures across 188 tariff lines	These safeguard measures allow the US to impose additional tariffs for the related products if import prices dip below a certain point—the US has itself advocated for the removal of agricultural safeguard measures in the WTO.
	Tariff rate quotas on 44 lines, including: dairy, beef, citrus, sugar, chocolate, olives, tobacco, cotton, and animal feed	TRQs allow a given quantity of a good to be imported at one tariff level which then rises when the quota is 'used up'; these are market distorting measures, especially when administered on a first-come, first-served basis, which encourages frontloading imports.
	Agricultural product fees on imports via Animal and Plant Health Inspection Service ("APHIS"), authorised under Section 2509 of the Food, Agriculture, Conservation, and Trade Act of 1990	Agricultural quarantine fees must be paid to APHIS for inspecting every shipment of agricultural/veterinary goods entering the United States; as of 2017, these fees were \$825 per commercial cargo vessel and \$225 per commercial aircraft.
	Excise taxes on tobacco and alcohol products may be levied at the federal, state or local municipal level	Three levels of government can and do levy 'sin' taxes on alcohol and tobacco products; at the federal level, this is roughly \$0.05 per can of beer, \$0.31 per bottle of wine, \$2.14 per handle of hard spirits, and \$2.11 per pack of cigarettes. Additional taxes are levied at the state and local level.
	The Department of the Interior maintains import and export licenses for fish and wildlife	These licences cost \$100 per annum and require a US agent for foreign exporters, as well as a record-keeper responsible for maintaining the licence records for five years after the expiration of the licence.
	Current Good Manufacturing Practice, Hazard Analysis, and Risk-Based Preventive Controls for Human Food (80 FR 55907)	This regulation requires a written safety plan which analyses foreseeable hazards, implements preventative controls, monitoring, product verification through third party labs, and strict control of supply chains—these steps all represent significant additional costs for anyone operating a farm or food processing plant in the US.
	Foreign Supplier Verification Programs for Importers of Food for Humans and Animals (FSVP Rule) (80 FR 74225)	US owners or consignees of imported food and/or the US agency or representative of the foreign owner of consignee are responsible for determining known or foreseeable hazards, evaluating the risk of imported food products, and conducting supplier verification activities through application of a written plan. Violations can lead to prosecution.
	Standards for the Growing, Harvesting, Packing, and Holding of Produce for Human Consumption (Produce Safety Rule) (80 FR 74353)	These regulations place strict requirements on agricultural water and soil quality permitted the in growing of produce, and also on worker training and equipment/buildings safety.
	Mitigation Strategies to Protect Food Against Intentional Adulteration (Intentional Adulteration Rule) (81 FR 34165)	This regulation is designed to prevent disgruntled employees, competitors or domestic terrorists from negatively impacting the food supply. The Intentional Adulteration Rule requires firms to identify each 'actionable step' at which they could implement safety measures against intentional adulteration, and then implement them. These are left to the discretion of the firm, except for bulk liquid receiving/storing, liquid storage/handling, secondary ingredient handling and mixing activities, all of which require the implementation of safety precautions.

	US BARRIERS	EFFECT
<b>Agriculture</b> <i>continued</i>	Sanitary Transportation of Human and Animal Food (Sanitary Transportation Rule) (81 FR 20091)	This rule applies to shippers, receivers, loaders and carriers who handle food within the US, including those in foreign countries who intend to ship food to the US; it specifies certain requirements in the design of transportation equipment and its maintenance, including temperature controls, cross-contamination prevention and separation of raw/ready-to-eat food, as well as training of carrier personnel and maintenance of extensive records.
	Information Required in Prior Notice of Imported Food (78 FR 32359), under the Public Health Security and Bioterrorism Preparedness and Response Act of 2002	Advance notice of import shipments of food must be given to the FDA and GBP; this can be provided through two channels but must be submitted no more than 15 days out from shipment for PNSI and 30 days out from shipment for ABI/ACS. If shipment of the same food has been refused in another country, the importer must notify the FDA.
	FSIS of DOA maintains a positive list for the import of certain livestock products.	Of the four nations, only England and Northern Ireland are certified to export pork to the US; beef and poultry products (including eggs) require further verification, including on-site inspection. <sup>115</sup>
	Sugar program (price supports and supply control) under the Farm Bill of 1990	Sugar production and processing are heavily subsidised in the US, leading to diminished market access for foreign competitors operating at world prices. Producers are guaranteed minimum prices at which the USDA will buy their product (\$18.75 per pound of raw cane sugar and \$24.09 per pound of refined beet sugar). 85% of domestic sugar demand must be met by domestic suppliers; the USDA annually allocates a share of the expected market to sugar producers. Additionally, imports are managed through TRQs—these allocations are based on the domestic market from 1975—1981 and is often criticised for not reflecting the current market conditions.
	Margin Protection Program for Dairy Producers; Dairy Product Donation Program, and Federal Milk Marketing Orders (subsidised insurance for margins, market support measures, etc)	The MPP covers producers by paying them when dairy margins dip below a given margin; coverage of \$4 per hundredweight is free, and coverage at 50-cent increments up to \$8 per hundredweight is available for a premium. Producers have the option to 'protect' between 25 and 90% of their production history. Under the Dairy Product Donation Program, the USDA is required to purchase dairy products for donation to food banks and individuals on food assistance programs if margins fall below \$4 per hundredweight for two consecutive months.
<b>Defence</b>	International Traffic in Arms Regulation, 22 USC 2778 of the Arms Export Control Act and Executive Order 13637	ITAR is a set of deeply comprehensive and wide-ranging set of regulations originally designed to match the export arms control regulations in place in the Eastern Bloc of the Soviet Union. Since 1999, it has been managed by the State Department. Manufacturers, exporters and brokers of defence articles, services, or related technical data must register with the State Department (at a cost of \$2,250 per annum); registration allows the designee to then apply for export licences. Retransfer (the foreign buyer selling the article to another foreign buyer) is very strictly prohibited unless included in the initial authorisation. The State Department aggressively pursues violations of ITAR; famously fining ITT \$100 million for retransfer of night vision technology; major defence contractors including Northrup Grumman, Boeing and Lockheed Martin have also faced stiff penalties. ITAR represents a serious and prohibitive cost for global defence trade.

115. [https://www.fsis.usda.gov/wps/wcm/connect/4872809d-90c6-4fa6-a2a8-baa77f48e9af/Countries\\_Products\\_Eligible\\_for\\_Export.pdf?MOD=AJPERES](https://www.fsis.usda.gov/wps/wcm/connect/4872809d-90c6-4fa6-a2a8-baa77f48e9af/Countries_Products_Eligible_for_Export.pdf?MOD=AJPERES)

	US BARRIERS	EFFECT
<b>Financial Services</b>	Dodd-Frank Wall Street Reform and Protection Act of 2010 (PL 111-203,H.R. 4173)	Dodd-Frank was the primary response of the US government to the financial crisis of 2008. It establishes the Financial Stability Oversight Council and the Office of Financial Research in the Treasury Department to monitor systemic risk in the financial services sector, with the right to place nonbank companies under the supervision of the Federal Reserve, to issue legally binding 'suggestions' to the relevant supervisory authority as regards certain activities, to subpoena witnesses, and to require any bank or nonbank institution to provide certified financial reports; it allows the Treasury to label certain institutions as 'systemically important financial institutions', which automatically places them under a stricter set of regulations; it requires certain institutions to create 'living wills'; it expands the number and type of institutions under 'liquidation authority' for the Federal Deposit Insurance Corporation; to levy 'assessment fees' to cover the costs of the Orderly Liquidation Fund; it requires hedge fund managers and private wealth managers to register under the Investment Advisers Act of 1940; it establishes the Federal Insurance Office, which is responsible for monitoring the industry, including the extent to which traditionally underserved and minority groups are able to access the insurance market, and implementing the Terrorism Insurance Program; it establishes the Volcker Rule by amending the Bank Holding Company Act of 1956, thereby limiting the right of banking entities to own more than 3% of the total ownership interest of a hedge fund and/or to have investments in a hedge fund which exceed 3% of the value of their Tier 1 capital; it requires that derivative swaps be cleared through exchanges; it repeals the exemptions which were given to derivatives swaps under the Gramm-Leach-Bliley Act; it enhances the role of the Federal Reserve in supervising the activities of systemically important institutions; and it gives increased power to the Securities and Exchange Commission, among other provisions. The Dodd-Frank Act has dramatically altered the landscape of financial services in the US and taken measures which, while designed to protect the public and the industry itself, ultimately limit profitability.
	International Banking Act of 1978—governs the operations of foreign banks in the US	This Act brings all American branches of foreign banks under American jurisdiction, with the rights (FDIC insurance) and responsibilities (capital adequacy requirements and auditing schedules) as domestic banks.
	Securities Exchange Act of 1934	This Act established the Securities and Exchange Commission and regulates the secondary trading of securities, which represents a market worth trillions of dollars annually.
	Gramm-Leach-Bliley Act (Financial Services Modernization) of 1999—regulates the consolidated financial sector	The GLBA repealed the provisions of Glass-Steagall relating to combinations of investment/commercial banks and investment companies to allow further consolidation in the market; it also established privacy provisions which must be given to every customer to allow them to opt-out of third-party information sharing.
	Bank Holding Company Act of 1956	This Act regulates US banks affiliating with other financial services companies by setting up a bank holding company; it specifies that the Federal Reserve Board of Governors must approve the establishment of bank holding companies and banned interstate competition amongst bank holding companies. Much of this Act was subsequently repealed by Riegle-Neal and Gramm-Leach-Bliley.

	US BARRIERS	EFFECT
<b>Financial Services</b> <i>continued</i>	Riegle-Neal Interstate Banking and Branching Act of 1994—regulates branching by merger	This Act repealed portions of the Bank Holding Company Act to increase the competitiveness of banks operating on a federal charter to match that of banks operating on a state charter. It mandated review of a bank's performance on Community Reinvestment Act compliance before expansion could be authorised.
	Investment Company Act of 1940	This Act regulates conflicts of interest by requiring disclosure of material details and places restrictions on certain mutual fund activities, including short-selling. It is used primarily as a regulatory vehicle for the Securities and Exchanges Commission, whose powers it broadens.
	Investment Advisers Act of 1940	This Act requires investment advisers of every stripe to register with the SEC; it prohibits advisers from profiting from market activity caused by their advice to clients and gives them a fiduciary duty to their clients.
	Sarbanes-Oxley Act of 2002	This Act establishes and reinforces the responsibilities of public company boards, management and accounting firms. It establishes the Public Company Accounting Oversight Board and requires enhanced disclosure of financial transactions. It also increases the criminal and civil penalties for white collar crime and makes the CEO responsible for the company tax return.
<b>Fisheries</b>	Magnuson-Stevens Fishery Conservation and Management Act	This Act maintains a positive list of countries whose fishing practices are acceptable and eligible for export to the US; the UK is on this list.
	Subsidy programs: Columbia River Fishery Development Program, Sea Grant College Program, Saltonstall-Kennedy Grant Program: Fisheries R&D, Fisheries Finance Program	As with broader agricultural subsidy programs, these artificially lower the prices of domestic suppliers and inhibit the ability of foreign fish to compete in the US market.
<b>Government Procurement</b>	Only 37 states and the federal government are signatories to the GPA	This means that any municipal contracts are not subject to the GPA, thereby reducing market access for foreign firms. Furthermore, the Buy American Act is excluded from the GPA's coverage. GPA thresholds vary by country and are assigned on a reciprocal basis through free trade agreements.
	Buy American Act (1933), Trade Agreements Act (1977, which provides for waivers to the BAA), Federal Property and Administrative Services Act (1949), Competition in Contracting Act (1984), Federal Acquisition Streamlining Act (1994), and the Services Acquisition Reform Act	These Acts require the federal government to 'prefer' domestic goods and companies when making purchases—this extends to third party purchasing made with federal funding, e.g. the construction of state highways.  Exceptions from the BAA are granted under certain circumstances; one of these circumstances is proof that use of a domestic supplier would yield an 'unreasonable' price; this is defined as 6% more than an international supplier generally, 12% more if a small business is concerned, and 50% more for any purchases for the DOD.
<b>Insurance</b>	McCarran-Ferguson Act of 1945 (US Code Title 15, Chapter 20)	This Act states that regulation of the insurance sector should take place at the state level, effectively creating a 50-state market which is difficult for foreign competitors to break into. The GLB specifies 13 areas of state insurance regulation that may not be pre-empted by federal law

	US BARRIERS	EFFECT
<b>Investment</b>	FINSA/CFIUS	<p>Officially, CFIUS has 30 days to conduct a review, 45 days to conduct an investigation, and 15 days for the President to take a decision. Unofficially, an ‘informal’ stage has become part of the de facto functioning of CFIUS; this is of an unspecified length of time and allows the firms party to CFIUS review and CFIUS staff to identify potential issues with a filing and restructure transactions to address national security issues. Firms participating in transactions which may raise national security issues (normally relating to foreign investment/a foreign buyer) may voluntarily submit a CFIUS filing; CFIUS may also ‘request’ a filing.<sup>116</sup> If a ‘request’ is ignored, CFIUS may legally require a filing. If CFIUS reviews a transaction for which no notification was filed and finds that the transaction threatens national security, it has the authority to ‘unwind’ that transaction. Such a decision would not be subject to judicial review. True greenfield investments are the only transactions outside of CFIUS’ scope.</p> <p>An amendment of the current law would need to be approved by both houses of Congress; any easing of the CFIUS process would likely face opposition from a body which has historically demanded more control over foreign investment in the United States, not less (see the case of Dubai Ports World). The ‘easiest’ case would likely be for fully private, fully British-owned firms which have already undergone national security vetting of some kind in the US (under the US-UK Defense Trade Cooperation Treaty, for example).</p>
<b>Maritime</b>	Merchant Marine Act of 1920/Jones Act (PL 66-261)	The Jones Act regulates maritime commerce in the US; its primary impact is to require that all goods transported via water between US ports (including US territories) be carried on ships flying the US flag, that were built in the US, and owned/operated/crewed by Americans.
<b>Telecoms</b>	Telecommunications Act of 1996	This Act attempted to correct many of the anti-competitive features of the Communications Act of 1934. It maintains the Universal Service obligation; includes the internet in broadcasting/spectrum allotment; allows cross-ownership in media; and forces incumbents to make access to their networks available at wholesale rates.
	Communications Act of 1934 as amended by the Telecommunications Act of 1996	This Act created the Federal Communications Commission and delegated the regulation of interstate telephone services to the FCC. The way in which this Act regulated new technologies prevented new entrants to the market and effectively created monopolies.
	Open Internet Order (commonly known as the FCC net neutrality decision)	The Open Internet Order makes ‘net neutrality’ the official policy of the United States—that is to say, that all internet traffic is treated equally. It forces internet service providers to disclose their network management practices and performance statistics; does not allow ISOs to block lawful content or applications; and forbids unreasonable discrimination against certain types of internet traffic.

<sup>116</sup> [http://www.jonesday.com/common\\_misconceptions\\_regarding\\_cfius/](http://www.jonesday.com/common_misconceptions_regarding_cfius/)

## UK Barriers

	UK BARRIERS	EFFECT
Agriculture	Nutritional labelling—EU framework regulation 1169/2011	This regulation regulates the display of product information on product packaging and online stores ostensibly to provide consumers with information related to nutrition, ingredients and allergens.
	GMOs—Directive 2015/412, Member State opt-out provision	Member states (including regional governments) are given the option of deciding whether or not GMO crops should be allowed to be grown in their territory—nineteen member states have opted out for all or part of their territories.
	GMOs—Directive 2001/18/EC	Cultivation of GMOs requires authorisation from the relevant national authority and the Commission; if one or more Member States raises objections, the European Food Safety Agency must submit a risk assessment. GMOs must be labelled as such, monitored, and recorded in a register.
	Fertiliser—Council Regulation 2003/2003	This regulation defines the composition, marking, labelling, packaging and identification requirements for designation as 'EC fertilisers', which can be freely sold and used across the EU. Laboratories capable of determining conformity with these standards are designated at the national level.
	Pesticides—Commission Regulation 1107/2009; Commission Regulation 396/2005; Commission Implementing Regulation 540/2011	Pesticides are broadly covered by REACH regulation; there is a very long process for the approval of active substances in pesticides (2.5 to 3.5 years in theory, in practice much longer).
	Hormones and beta agonists—Directive 96/22/EC, as amended by Directive 2003/74/EC	The EU effectively bans the import of hormone-treated beef beyond what has been considered 'sound science' in the WTO.
	Pathogen reduction treatments—EC Regulation 853/2004	This regulation bans the import of meat which has been subjected to any pathogen reduction treatment other than water—this primarily affects chlorine-washed poultry products from the US.
	Export certification—Council Regulation 338/97	This regulation defines the conditions under which import, export and trade of wild flora and fauna can occur. It creates and mandates import and export permits, re-export certificates, import notifications and internal trade certificates required for trade in the hundreds of plant species listed in the Appendix to this regulation.
	Somatic cell count (milk)—EC Regulation 853/2004, Annex III Section IX	This regulation defines somatic cell count as an indication of milk quality and specifies what amounts of SCC may be present for milk to be sold on the EU market; an SCC of 200,000 per ml of milk means that a cow is likely to have at least one infected udder; 300,000 or higher means that a cow is likely to have a significant infection, and 400,000 or higher means that milk from this cow is unfit for human consumption. The limit in the US is 750,000.
	Citrus canker—Council Directive 2000/29/EC	Fruit bound for EU export is subject to inspection in the grove pre-harvest and post-harvest inspection before shipping. If any canker lesions are found on a piece of fruit bound for export, the entire production block is disqualified for export to the EU.
	EU framework regulation 1151/2012	This regulation is broadly focused on 'inclusive growth' in the European agricultural market through 2020. It sets out the framework for quality schemes and protected designation of origin and protected geographical indication schemes. By their very definition, these schemes exclude foreign competition from the EU market for products under these designations (e.g., feta, parma ham, Herefordshire cider, etc.).



	UK BARRIERS	EFFECT
<b>Agriculture</b> <i>continued</i>	Wine traditional terms—Council Regulation 479/08; Commission Regulation 607/09; Commission Regulation 1308/2013	These regulations set up the support programmes, trade regulations, quality controls and production limits for wine production in the EU. It also creates the vineyard register, compulsory declarations on harvest, production and transport, and records on transport and wine-making processes. It lays out the 'authorised wine making practices', acceptable levels of sulphur dioxide and volatile acidity, lays out the traditional terms/PGIs/PDOs associated with wine and disallows coupage of third country grapes in the EU.
	Whisky aging requirements—EC Regulation 110/2008, Annex II Category 2; Scotch Whisky Regulations 2009	The Commission has started discussions with the member states on a possible simplification of wine labelling set out in Regulation 607/2009, but appears to be facing resistance to any changes that would lessen the protection of traditional terms.
	Trucks: Maximum Authorised Dimensions—Directive 2015/719/EU	These regulations mandate aging requirements for 'whisky/whiskey' products to be sold on the EU market; US whiskey manufacturers often age their whiskey for less time in a different type of barrel which produces similar results. These regulations exist to protect the domestic Scotch Whisky association.
<b>Automobiles</b>	Emissions—Directive 2007/46/EC, Euro 5 and 6 Regulation 715/2007/EC, Regulation 692/2008/EC, Regulation (EU) 2016/427, Regulation 595/2009/EC, Regulation (EU) 582/2011	This directive favours trucks manufactured in the EU to this standard over those manufactured in the US; there is no measurable safety differential between the two types of truck.
	Airbus subsidies	The EU maintains strict regulations designed to curb carbon dioxide emissions. The suite of regulations provides a legal framework for the type approval of cars, vans, trucks, buses and coaches and set the emission limits for cars for regulated pollutants, in particular nitrogen oxides for light and heavy-duty vehicles.
<b>Aviation</b>	REACH—European Parliament and Council Regulation 1907/2006	Airbus receives roughly £8 billion a year in subsidies from the European Union, despite being required by the WTO to cut these subsidies.
<b>Chemicals</b>	Renewable Energy Directive—2009/28/EC	REACH is the extraordinarily complex and wide-ranging set of regulations governing the production, sale and trade of chemicals in the EU. Broadly speaking, it requires registration and authorisation of chemicals used in the EU; disclosure of chemicals found in a given product within 45 days of a consumer request; that tests be conducted on vertebrates before market access is granted (and that the results of these tests be sold for a 'reasonable' price); and restricts the registration of chemicals to representatives based in EU countries.
<b>Energy</b>	Uranium—The Corfu Declaration (1994)	This directive mandates certain levels of renewable energy usage in the EU; this has been set at 20% by 2020, with a further reduction of carbon dioxide emissions by 20% and to achieve energy savings of 20%. The UK remains significantly behind these targets.
	Financial Services and Markets Act 2000, Regulated Activities Order and Markets in Financial Investments Regulation ("MiFIR")	The Commission presented a new Renewable Energy Directive ("RED II") for the period 2020-2030 as part of a comprehensive "Winter Energy Package" of legislative proposals which includes initiatives on bioenergy sustainability (liquid biofuels and biomass). RED II was adopted by the Commission on November 30, 2016.
<b>Financial Services</b>	Solvency II	This declaration effectively shields 80% of the European uranium market from import competition.

	UK BARRIERS	EFFECT
<b>Financial Services</b> <i>continued</i>	Alternative Investment Fund Managers Directive 2011/61/EU ("AIFMD")	Requires that businesses must be authorised by the Financial Conduct Authority in the UK to provide certain financial and investment services. MiFIR sets out a number of additional reporting requirements in relation to the disclosure of trade data to the public and competent authorities (to come into effect in January 2018).
	European Market Infrastructure Regulation ("EMIR")	Solvency II was primarily introduced by the EU to regulate the amount of capital that EU insurance companies must hold to reduce the risk of insolvency and to harmonise the EU insurance market. It includes quantitative requirements (for example, the amount of capital an insurer should hold), requirements for the governance and risk management of insurers, as well as for the effective supervision of insurers and disclosure and transparency requirements.
	Fish products labelling—Commission Regulation 1379/2013	AIFMD imposes requirements on Alternative Investment Fund Managers ("AIFMs"), including authorisation by a home state regulator, strict operating conditions, transparency requirements. The directive arguably puts non-EU funds at a disadvantage as EU funds managed by EU managers may be marketed across the EU under the AIFMD passport, which is not available for non-EU managers.
<b>Fisheries</b>	EU Utilities Directive	EMIR includes strict rules relating to OTC derivatives, central counterparties and trade repositories. EMIR includes detailed reporting requirements, rules on clearing and monitoring requirements by market participants.
<b>Government Procurement</b>	Data Protection Directive 1995/46—to be replaced by the General Data Protection Regulation and range of measures on privacy and e-commerce	This regulation requires that all fish products be labelled to show the commercial name of the species, their country of origin and method of production.
<b>Information Services</b>	Directive on Audiovisual Media Services	These directives specify the procurement provisions in place for public utilities companies in the EU. Specifically, it calls for non-discrimination, equal treatment, proportionality, transparency and mutual recognition in awarding government procurement contracts in this sector. EU companies are given preference in bids concerning water, energy, postal services and urban transport; moreover, if the majority of a bid's goods come from outside the EU, they can be rejected.
<b>Media</b>	Transport Fuel: Fuel Quality Directive 2009/30/EC	The EU maintains strict rules for the sharing and protection of personal data. This includes the right to be forgotten, mandatory requests for the usage of cookies on websites, etc.
<b>Road &amp; Rail</b>	Single market in telecommunications—TSM	The AVMS requires member states to comply with certain content requirements in exchange for the ability to automatically distribute their country's content to other EU member states; this includes a requirement to reserve a certain amount of airtime for 'European works'.
<b>Telecoms</b>	Conformity assessment framework—Commission Regulation 765/2008 and Decision 768/2008	This directive gives specification to petrol and diesel products which can be sold in the EU and requires suppliers to reduce the carbon-intensity of fuels used for road transport.
<b>Standards</b>		The TSM covers all aspects of telecommunications, including broadband, radio, television and phone networks. Historically, it has been difficult for US telecoms operators to penetrate the EU telecoms market, due to the existing dominance of national incumbent operators and the presence of multiple localised anti-competitive barriers to entry in each Member State.
		These regulations provide a legal framework for accreditation services across Europe, including testing facilities, inspection services, conformity assessments of products, management systems or persons, and emissions verifiers for carbon targets.

## APPENDIX 2

### Telecommunications Equipment

RELEVANT REGULATION	
EC	USA
<p>Directive 98/13/EC of the European Parliament and of the Council of 12 February 1998 relating to telecommunications terminal equipment and satellite earth station equipment, including the mutual recognition of their conformity, and interpretation thereof;</p>	<p><b>Communications Act of 1934</b>, as amended by the <b>Telecommunication Act of 1996, (Title 47 of the United States Code)</b>.</p> <p>The US regulatory and administrative provisions in respect of telecommunication equipment, including 47 CFR Part 68, and FCC interpretation thereof;</p>
<p>(The Parties recognise that the Handbook on the implementation of Directive 98/13/EC (ADLNB and ACTE approved), provides useful guidelines for the implementation of conformity assessment procedures falling under this Directive.);</p> <p>Commission Decisions ("CTRs") established under Directive 98/13/EC;</p> <p>The EC Member States' legislation and regulations in respect of:</p> <ul style="list-style-type: none"> <li>(a) non-harmonised analogue connection to the public telecommunications network;</li> <li>b) non-harmonised radio transmitters for which there is a civilian equipment authorisation requirement.</li> </ul>	<p>(The Parties recognise that the FCC Form 730 Application Guide provides useful guidelines for the implementation of conformity assessment procedures for telecommunication terminal equipment falling within these regulations.);</p> <p>The US regulatory and administrative provisions in respect of all radio transmitters subject to an equipment authorisation requirement. A non-exclusive list of FCC regulations are contained in Section II.</p>

AFFECTED PRODUCTS	
EC	USA
<p>The following equipment categories are included:</p> <ul style="list-style-type: none"> <li>• ISDN Basic Rate Access</li> <li>• ISDN Primary Rate Access</li> <li>• ISDN Telephony</li> <li>• X21/V.24/V.35 Access</li> <li>• X25 Access</li> <li>• PSTN Non-Voice</li> <li>• PSTN Voice Band (Analog)</li> <li>• ONP Leased Line Terminal types: <ul style="list-style-type: none"> <li>• 64 kbits/sec</li> <li>• 2048 kbits/sec unstructured</li> <li>• 2048 kbits/sec structured</li> <li>• 4 Mbits/sec access</li> <li>• 140 Mbits/sec access</li> <li>• 2 wire analogue</li> <li>• 4 wire analogue</li> </ul> </li> </ul>	<p>Equipment categories covered under 47 CFR, Part 68, including:</p> <ul style="list-style-type: none"> <li>• ISDN Basic Access</li> <li>• ISDN Primary Rate Access</li> <li>• Digital Service Access: <ul style="list-style-type: none"> <li>• 2.4 kbps</li> <li>• 3.2 kbps (2.4 kbps with Secondary Channel)</li> <li>• 4.8 kbps</li> <li>• 6.4 kbps (4.8 kbps with SC)</li> <li>• 9.6 kbps</li> <li>• 12.8 kbps (9.6 kbps with SC)</li> <li>• 19.2 kbps</li> <li>• 25.0 kbps (19.2 kbps with SC)</li> <li>• 56.0 kbps</li> <li>• 64.0 kbps (uses 72 kbps channel)</li> <li>• 72.0 kbps (56.0 kbps with SC)</li> <li>• 1.544 Mbps</li> <li>• 2-wire analogue tie trunks/ops</li> <li>• 4-wire analogue tie trunks/ops</li> <li>• PSTN-Voice Band (Analog) Access</li> <li>• Private Line (Analog) Access</li> </ul> </li> </ul>
<p>Radio transmitters subject to an equipment authorisation requirement, including:</p> <ul style="list-style-type: none"> <li>• Short range devices, including low power devices such as cordless telephones/microphones</li> <li>• Land mobile, including: <ul style="list-style-type: none"> <li>• Private Mobile Radio (PMR/PAMR)</li> <li>• Mobile telecom</li> <li>• Paging systems</li> <li>• Terrestrial fixed</li> <li>• Satellite mobile</li> <li>• Satellite fixed</li> <li>• Broadcast</li> <li>• Radio determination</li> </ul> </li> </ul>	<p>Radio transmitters subject to an equipment authorisation requirement, including:</p> <ul style="list-style-type: none"> <li>• Commercial Mobile Radio (Part 20)</li> <li>• Domestic Public Fixed (Part 21)</li> <li>• Domestic Mobile (Part 22)</li> <li>• Personal Communication Service (Part 24)</li> <li>• Satellite Communications (Part 25)</li> <li>• Broadcast (Part 73)</li> <li>• Auxiliary Broadcast (Part 74)</li> <li>• Cable Television Radio (Part 78)</li> <li>• Maritime (Part 80)</li> <li>• GMDSS (Part 80W)</li> <li>• Private Land Mobile (Part 90)</li> <li>• Private-Fixed Microwave (Part 94)</li> <li>• Personal Radio Services (Part 95)</li> <li>• IVDS (Part 95F)</li> <li>• Amateur Radio (Part 97)</li> <li>• Radio Frequency Devices (Part 15)</li> <li>• Fixed Microwave Services (Part 101)</li> </ul>

## Electromagnetic Compatibility

RELEVANT REGULATION	
EC	USA
<p><b>Council Directive 89/336/EEC</b>, as amended by <b>Council Directive 92/31/EEC</b>, and <b>Directive 98/13/EC</b> of the European Parliament and of the Council and interpretation thereof.</p>	<p><b>Communications Act of 1934</b>, as amended by the <b>Telecommunication Act of 1996, (Title 47 of the United States Code)</b>.</p> <p>The US regulatory and administrative provisions in respect of equipment subject to electromagnetic requirements including:</p> <p>47 CFR Part 15 47 CFR Part 18 And FCC interpretation thereof.</p>
AFFECTED PRODUCTS	
EC	USA
<ul style="list-style-type: none"> <li>Any product falling under the scope of Council Directive 89/336/EEC.</li> </ul>	<ul style="list-style-type: none"> <li>Any products falling under the scope of 47 CFR Part 15 and 18.</li> </ul>

## Electrical Safety

RELEVANT REGULATION	
EC	USA
<p><b>Council Directive 73/23/EEC</b> of 19 February 1973 as amended by <b>Directive 98/13/EC</b> of the European Parliament and of the Council.</p>	<p><b>29 USC 651 et seq. US 29 CFR 1910.7</b></p> <p>Products that are certified or approved under the Federal Mine Safety and Health Act (30 USC 801 et seq.) or its regulations and used in areas under the authority of the Mine Safety and Health Administration, are not covered under this Annex.</p> <p>OSHA will consider regulatory and legislative changes needed to support the objectives of the MRA.</p>

AFFECTED PRODUCTS	
EC	USA
<p>The electrical safety requirements of products falling under the scope of <b>Council Directive 73/23/EEC</b> on the harmonisation of the laws of the Member States relating to electrical equipment designed or use within certain voltage limits.</p>	<ul style="list-style-type: none"> <li>The electrical safety requirements of products falling under the scope of 29 CFR 1910 subpart S. This includes the electrical safety aspects for workplace safety of medical equipment and telecommunication terminal equipment within the scope of those Sectoral Annexes.</li> <li>Products that are certified or approved under the Federal Mine Safety and Health Act (30 USC 801 et seq.) or its regulations and used in areas under the authority of the Mine Safety and Health Administration, are not covered under this Annex.</li> </ul>

## Recreational Craft

RELEVANT REGULATION	
EC	USA
<p><b>Directive 94/25/EC</b> of the European Parliament and of the Council of 16 June 1994 on the approximation of the laws, regulations, and administrative provisions of the Member States relating to recreational craft.</p>	<p><b>46 USC Chapter 43, 33 CFR 81, 84, 159, 179, 181, 183 and 46 CFR 58.</b></p>

AFFECTED PRODUCTS	
EC	USA
<p>Recreational craft as defined in Directive 94/25/EC.</p>	<p>Any product falling under the scope of 46 USC Chapter 43, 33 CFR 81, 84, 159, 179, 181, 183 and 46 CFR 58.</p>

## Pharmaceutical Good Manufacturing Practices

RELEVANT REGULATION	
EC	USA
<ul style="list-style-type: none"> <li>• <b>Council Directive 65/65/EEC</b> of 26 January 1965 on the approximation of provisions laid down by law, regulation or administrative action relating to proprietary medicinal products, as extended, widened and amended.</li> <li>• <b>Council Directive 75/319/EEC</b> of 20 May 1975 on the approximation of provisions laid down by law, regulation or administrative action relating to proprietary medicinal products, as extended, widened and amended.</li> <li>• <b>Council Directive 81/851/EEC</b> of 28 September 1981 on the approximation of the laws of the Member States relating to veterinary medicinal products, as widened and amended.</li> <li>• <b>Council Directive 91/356/EEC</b> of 13 June 1991 laying down the principles and guidelines of good manufacturing practice for medicinal products for human use.</li> <li>• <b>Commission Directive 91/412/EEC</b> of 23 July 1991 laying down the principles and guidelines of good manufacturing practice for veterinary medicinal products.</li> <li>• <b>Council Regulation (EEC) No 2309/93</b> of 22 July 1993 laying down Community procedures for the authorisation and supervision of medicinal products for human and veterinary use and establishing a European Agency for the Evaluation of Medicinal Products.</li> <li>• <b>Council Directive 92/25/EEC</b> of 31 March 1992 on the wholesale distribution of medicinal products for human use.</li> <li>• <b>Guide to Good Distribution Practice (94/C 63/03)</b>.</li> <li>• Current version of the Guide to Good Manufacturing Practice, Rules Governing Medicinal Products in the European Community, Volume IV.</li> </ul>	<ul style="list-style-type: none"> <li>• Relevant sections of the <b>United States Federal Food, Drug, and Cosmetic Act</b> and the <b>United States Public Health Service Act</b>.</li> <li>• Relevant sections of <b>Title 21, United States Code of Federal Regulations (CFR) Parts 1-99, Parts 200-299, Parts 500-599, and Parts 600-799</b>.</li> <li>• Relevant sections of the <b>FDA Investigations Operations Manual, the FDA Regulatory Procedures Manual, the FDA Compliance Policy Guidance Manual, the FDA Compliance Program Guidance Manual, and other FDA guidances</b>.</li> </ul>
AFFECTED PRODUCTS	
EC	USA
<ul style="list-style-type: none"> <li>• Human medicinal products including prescription and non-prescription drugs;</li> <li>• Human biologicals including vaccines, and immunologicals;</li> <li>• Veterinary pharmaceuticals, including prescription and non-prescription drugs, with the exclusion of veterinary immunologicals;</li> <li>• Pre-mixes for the preparation of veterinary medicated feeds</li> <li>• Intermediate products and active pharmaceutical ingredients or starting materials</li> <li>• Human blood, human plasma, and human tissues and organs are excluded</li> <li>• Investigational medicinal products/new drugs, human radiopharmaceuticals and medicinal gases are excluded during the transitional phase, to be reconsidered at the end of the transitional phase</li> </ul>	<ul style="list-style-type: none"> <li>• Human medicinal products including prescription and non-prescription drugs;</li> <li>• Human biologicals including vaccines, and immunologicals;</li> <li>• Veterinary pharmaceuticals, including prescription and non-prescription drugs, with the exclusion of veterinary immunologicals;</li> <li>• Type A medicated articles for the preparation of veterinary medicated feeds</li> <li>• Intermediate products and active pharmaceutical ingredients or bulk pharmaceuticals</li> <li>• Human blood, human plasma, and human tissues and organs are excluded</li> <li>• Investigational medicinal products/new drugs, human radiopharmaceuticals and medicinal gases are excluded during the transitional phase, to be reconsidered at the end of the transitional phase</li> </ul>

## Medical Devices

RELEVANT REGULATION	
EC	USA
<p><b>Council Directive 90/385/EEC</b> of 20 June 1990 on the approximation of the laws of the Member States relating to active implantable medical devices.</p> <ul style="list-style-type: none"> <li>• Annex II (with the exception of section 4)</li> <li>• Annex IV</li> <li>• Annex V</li> </ul> <p><b>Council Directive 93/42/EEC</b> of 14 June 1993 concerning medical devices.</p> <ul style="list-style-type: none"> <li>• Annex II (with the exception of section 4)</li> <li>• Annex III</li> <li>• Annex IV</li> <li>• Annex V</li> <li>• Annex VI</li> </ul>	<ul style="list-style-type: none"> <li>• <b>The Federal Food, Drug and Cosmetic Act</b>, 21. USC. §§ 321 et seq.</li> <li>• <b>The Public Health Service Act</b>, 42 USC. §§ 201 et seq.;</li> <li>• Regulations of the United States Food and Drug Administration found at 21 C.F.R., in particular, Parts 800 to 1299;</li> <li>• <b>Medical Devices; Third-Party Review of Selected Premarket Notifications; Pilot Program</b>, 61 Fed. Reg. 14,789-14,796 (April 3, 1996).</li> </ul>

AFFECTED PRODUCTS	
EC	USA
<p>See: Sectoral Annex on Medical Devices, Appendix II</p> <ul style="list-style-type: none"> <li>• Table I: Class I products requiring premarket evaluations in the US, included in a scope of product coverage at the beginning of a transition period, including: <ul style="list-style-type: none"> <li>— Anaesthesiology, Dentistry, Ear/Nose/Throat, Gastroenterology—Urology, General Hospital, Neurology, Ophthalmology, Orthopaedics, Physical Medicine, Radiology, General and Plastic Surgery</li> </ul> </li> <li>• Table II: Class II medical devices included in scope of product coverage at the beginning of the transition period, including: <ul style="list-style-type: none"> <li>— Diagnostic ultrasound, diagnostic x-ray devices (except mammographic x-ray systems), ECG devices, ophthalmic instruments, blood pressure measurement devices, clinical thermometers, hypodermic needles (except anti-stick and self-destruct), external fixators (except devices with no external components), selected dental materials, and latex condoms</li> </ul> </li> <li>• Table III: Medical devices for possible inclusion in scope of product coverage during operational period, including: <ul style="list-style-type: none"> <li>— Anaesthesiology, Cardiology, Dentistry, Ear/Nose/Throat, Gastroenterology—Urology, General Hospital, Neurology, Obstetrics/Gynaecology, Orthopaedics, Physical Medicine, Radiology, and General/Plastic Surgery</li> </ul> </li> </ul>	<p>See: Sectoral Annex on Medical Devices, Appendix II</p> <ul style="list-style-type: none"> <li>• Table I: Class I products requiring premarket evaluations in the US, included in a scope of product coverage at the beginning of a transition period, including: <ul style="list-style-type: none"> <li>— Anaesthesiology, Dentistry, Ear/Nose/Throat, Gastroenterology—Urology, General Hospital, Neurology, Ophthalmology, Orthopaedics, Physical Medicine, Radiology, General and Plastic Surgery</li> </ul> </li> <li>• Table II: Class II medical devices included in scope of product coverage at the beginning of the transition period, including: <ul style="list-style-type: none"> <li>— Diagnostic ultrasound, diagnostic x-ray devices (except mammographic x-ray systems), ECG devices, ophthalmic instruments, blood pressure measurement devices, clinical thermometers, hypodermic needles (except anti-stick and self-destruct), external fixators (except devices with no external components), selected dental materials, and latex condoms</li> </ul> </li> <li>• Table III: Medical devices for possible inclusion in scope of product coverage during operational period, including: <ul style="list-style-type: none"> <li>— Anaesthesiology, Cardiology, Dentistry, Ear/Nose/Throat, Gastroenterology—Urology, General Hospital, Neurology, Obstetrics/Gynaecology, Orthopaedics, Physical Medicine, Radiology, and General/Plastic Surgery</li> </ul> </li> </ul>



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## ABOUT THE LEGATUM INSTITUTE SPECIAL TRADE COMMISSION

The Legatum Institute Special Trade Commission (STC) was created in the wake of the British vote to leave the European Union. At this critical historical juncture, the STC aims to present a roadmap for the many trade negotiations which the UK will need to undertake now. It seeks to re-focus the public discussion on Brexit to a positive conversation on opportunities, rather than challenges, while presenting empirical evidence of the dangers of not following an expansive trade negotiating path.

The STC draws upon the talent of experienced former trade negotiators from the US, Canada, Mexico, Australia, New Zealand, and Singapore, among other nations.

In the coming few months, the STC will host a number of public briefings that offer advice to key stakeholders on EU negotiations.

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All commissioners will serve the Commission in an individual capacity.

## MISSION STATEMENT

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The purpose of the Legatum Institute Special Trade Commission (STC) is to understand and guide the process that the UK and other governments are engaged in as a result of the Brexit referendum.

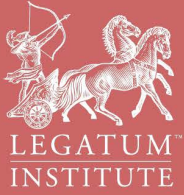
The Commission will provide the academic firepower to enable a successful process that includes:

1. The UK's relationship with Europe;
2. The relationship with the countries that more holistically embrace open trade, competition on the merits as an organising economic principle, and property rights protection;
3. The bilaterals with other key trading partners;
4. The relationship with the Commonwealth and developing countries; and
5. The underpinning WTO relationship.

The STC's combined expertise and experience, spread over two hundred years and hundreds of trade agreements puts it in a unique position to be a trusted and independent advisor to the series of post-Brexit processes that could and should lead to the creation of a global economic engine.

This realises the Legatum Institute's theory of change which is ultimately driven by the need to lift the global poor out of poverty and to create jobs, hope and opportunity for the world's people through the application of property rights protection and open trade systems that are characterised by competition on the merits as the organising economic principle.

The STC's role is to help shepherd governments, stakeholders and others towards increased global prosperity which is available if the inflection point in history that the Brexit vote represents is capitalised on.



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# U.S.-UK Free Trade Agreement: Prospects and Issues for Congress

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## Summary

Prospects for a bilateral free trade agreement (FTA) between the United States and the United Kingdom (UK) are of increasing interest for both sides. In a national referendum held on June 23, 2016, a majority of British voters supported the UK exiting the European Union (EU), a process known as “Brexit.” The Brexit referendum has prompted calls from some Members of Congress and the Trump Administration to launch U.S.-UK FTA negotiations, though some Members have moderated their support with calls to ensure that such negotiations do not constrain the promotion of broader transatlantic trade relations. On January 27, 2017, President Trump and UK Prime Minister Theresa May discussed how the two sides could launch high-level talks and “lay the groundwork” for a future U.S.-UK FTA. Negotiations on a bilateral FTA between the United States and UK would represent a change in U.S. transatlantic trade policy, which has recently focused on negotiating a U.S.-EU Transatlantic Trade and Investment Partnership (T-TIP) FTA.

Formal U.S.-UK FTA negotiations cannot start immediately. On March 29, 2017, Prime Minister May sent a letter to the European Council notifying it of the UK’s intention to leave the EU, triggering the two-year Article 50 exit process under the Treaty of the European Union. Until the UK formally exits, it remains a member of the EU, which retains exclusive competence over trade negotiations. During this time, and in the absence of any preferential trade agreement between the United States and the EU, World Trade Organization (WTO) parameters continue to govern U.S.-UK trade—as they do for U.S. trade with all other EU member states. In the meantime, the United States and the UK could pursue preliminary “informal” discussions on a potential bilateral FTA.

The prospects for a future U.S.-UK FTA depend on a number of variables, including the terms of the UK’s negotiated withdrawal from, and future trade relationship with, the EU, as well as the UK’s redefined terms of trade within the WTO. A U.S.-UK FTA could include reciprocal provisions to expand access to goods, services, agriculture, and government procurement markets; enhance and develop new bilateral trade-related rules and disciplines in areas such as intellectual property rights (IPR), investment, and digital trade; and cooperate on regulatory issues such as transparency and sector-specific concerns.

Congress has important legislative, oversight, and advisory responsibilities with respect to any potential U.S.-UK FTA. The U.S. Constitution grants Congress the power to regulate commerce with foreign nations. Congress also establishes overall U.S. trade negotiating objectives, which it updated in the 2015 Trade Promotion Authority (TPA) legislation (P.L. 114-26). In addition, Congress would need to approve future implementing legislation for a final U.S.-UK FTA to enter into force. Under TPA, an FTA could be eligible to receive expedited legislative consideration if Congress determines that the FTA advances trade negotiating objectives and satisfies TPA’s various other requirements, including notification to and consultations with Congress on the status of the negotiations.

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## Introduction

In a June 23, 2016, national referendum, a majority of British voters supported the United Kingdom (UK) exiting the European Union (EU), a process known as “Brexit.” Since then, various Members of Congress have voiced support for launching U.S.-UK free trade agreement (FTA) negotiations, while other Members have moderated their support with calls to ensure that such negotiations do not undercut the promotion of broader U.S.-EU trade relations.<sup>1</sup> President Donald Trump, since taking office, has continued to express support for Brexit, and stated his intention to negotiate a U.S.-UK FTA “quickly” that is “[g]ood for both sides.”<sup>2</sup> During a meeting on January 27, 2017, President Trump and UK Prime Minister Theresa May discussed how the two sides could launch high-level talks and “lay the groundwork” for a future U.S.-UK FTA.<sup>3</sup>

U.S.-UK FTA negotiations would represent a change in U.S. transatlantic trade policy, which, under the Obama Administration, focused on negotiating a U.S.-EU Transatlantic Trade and Investment Partnership (T-TIP) FTA.<sup>4</sup> Bilateral FTA negotiations also would represent a change from the Obama Administration’s focus on multiparty regional negotiations, such as on T-TIP and notably the Trans-Pacific Partnership (TPP).<sup>5</sup> At the same time, the United States and the UK have had long-standing trade ties. The United States has viewed the UK as a liberalizing force within the EU, and often has found itself more aligned with the UK on trade policy approaches than with the EU overall.

At the same time, the notion of a U.S.-UK FTA is not new. For example, some policymakers expressed interest previously in exploring the possibility of the UK joining the North American Free Trade Agreement (NAFTA).<sup>6</sup> More broadly, the notion of a “special relationship” between the United States and UK is long-standing.<sup>7</sup>

Formal U.S.-UK FTA negotiations cannot start immediately. The UK is legally precluded from engaging in its own trade negotiations under its EU membership terms. On March 29, 2017, Prime Minister May sent a letter to the European Council notifying the body of the UK’s intention to leave the EU. This action triggered the two-year Article 50 exit process under the

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<sup>1</sup> In the 115<sup>th</sup> Congress, see H.Res. 60 (Dent), and U.S. Congress, House Committee on Foreign Affairs, Subcommittee on Terrorism, Nonproliferation, and Trade and Subcommittee on Europe, Eurasia, and Emerging Threats, *Next Steps in the “Special Relationship”-Impact of a U.S.-UK Free Trade Agreement*, 115th Cong., 1st sess., February 1, 2017. In the 114<sup>th</sup> Congress, see S. 3123 (Lee), S.Res. 520 (Rubio), H.Res. 817 (Dent), and concurrent resolutions H.Con.Res. 146 (Brady) and S.Con.Res. 47 (Hatch), as well as Speaker of the House, “Speaker Ryan Calls for Free Trade Agreement with UK After Brexit,” press release, June 27, 2016.

<sup>2</sup> Shawn Donnan, “Trump’s UK Trade Pledge: Hurdles to a Quick Deal,” *Financial Times*, January 15, 2017. For statements since President Trump entered office, see CSPAN, “President Trump and British Prime Minister Theresa Hold News Conference,” January 27, 2017; and CSPAN, “President Trump Rally in Melbourne, Florida,” February 18, 2017. Transcripts for these events are not available on the White House website as of the time of this writing.

<sup>3</sup> The White House, “President Trump and Prime Minister May’s Opening Remarks,” press release, January 27, 2017.

<sup>4</sup> CRS In Focus IF10120, *Transatlantic Trade and Investment Partnership (T-TIP)*, by Shayerah Ilias Akhtar and Vivian C. Jones.

<sup>5</sup> The United States and 11 other Asia-Pacific countries signed the TPP in February 2016 under the Obama Administration, but the United States withdrew from TPP in January 2017 under the Trump Administration. CRS Insight IN10443, *CRS Products on the Trans-Pacific Partnership (TPP)*, by Ian F. Fergusson and Brock R. Williams.

<sup>6</sup> U.S. International Trade Commission (ITC), *The Impact on the U.S. Economy of Including the United Kingdom in a Free Trade Arrangement With the United States, Canada, and Mexico*, Publication 3339, August 2000.

<sup>7</sup> CRS Report RL33105, *The United Kingdom: Background and Relations with the United States*, by Derek E. Mix, The United Kingdom: Background and Relations with the United States, by Derek E. Mix.

Treaty on European Union.<sup>8</sup> Until the UK completes what could be prolonged negotiations with the EU on its terms of withdrawal and formally exits, the UK remains a member of the EU, which retains competence over trade negotiations.<sup>9</sup> So long as the UK is a member of the EU and in the absence of any preferential trade agreement between the United States and the EU, World Trade Organization (WTO) parameters continue to govern U.S.-UK trade—as they do for U.S. trade with all other EU member states. Meanwhile, the United States and the UK could pursue informal discussions on a potential bilateral FTA.

Congress has important legislative, oversight, and advisory responsibilities regarding a potential U.S.-UK FTA. The role of Congress in U.S. trade policy is rooted in Article 1, Section 8, of the U.S. Constitution, which grants Congress the power to regulate commerce with foreign nations. Congress establishes overall U.S. trade negotiating objectives, which it updated in the 2015 Trade Promotion Authority (TPA) legislation (P.L. 114-26).<sup>10</sup> This grant of TPA is valid through 2021 (unless Congress enacts a possible extension disapproval resolution in 2018). Congress also would need to approve future implementing legislation for a U.S.-UK FTA to enter into force. An FTA could receive expedited legislative consideration if Congress determines that it advances trade negotiating objectives in TPA and meets TPA's other requirements, including for the President to notify and consult with Congress on the status and content of the negotiations.

## U.S.-UK Trade and Investment Trends

The United States and the UK have a deep, extensive economic relationship. U.S. firms, large and small, are involved in U.S.-UK trade, directly and as a part of integrated supply chains. In 2016, U.S. goods and services exports to the UK totaled about \$121 billion, and U.S. goods and services imports from the UK reached \$107 billion, yielding a \$15 billion U.S. trade surplus (**Figure 1**).<sup>11</sup> In terms of the EU, the UK accounted for about one-fifth of U.S. total trade with the EU-28, making it the United States' second-largest trading partner within the EU after Germany.

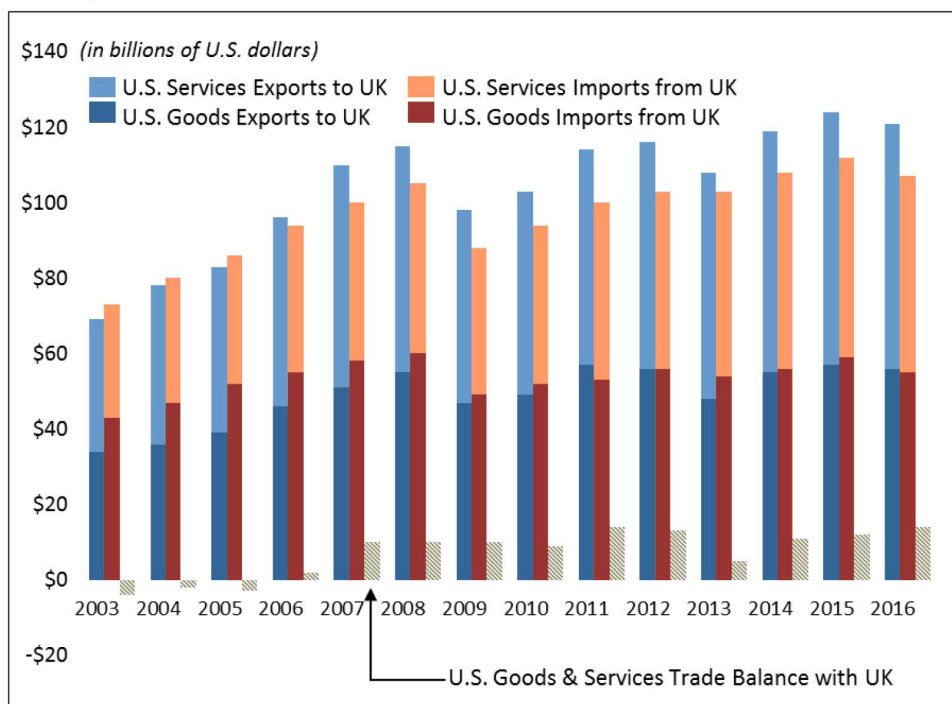
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<sup>8</sup> UK Department of Exiting the EU, "Prime Minister's Letter to Donald Tusk Triggering Article 50," correspondence, March 29, 2017.

<sup>9</sup> CRS Report RS21372, *The European Union: Questions and Answers*, by Kristin Archick.

<sup>10</sup> CRS Report RL33743, *Trade Promotion Authority (TPA) and the Role of Congress in Trade Policy*, by Ian F. Fergusson; and CRS In Focus IF10038, *Trade Promotion Authority (TPA)*, by Ian F. Fergusson.

<sup>11</sup> The UK also reports having an overall surplus in trade in goods and services with the United States. See, e.g., UK Office for National Statistics (ONS), "The UK trade and investment relationship with the United States of America: 2015," September 5, 2016. Factors may include possible methodological differences in U.S. and UK statistical agencies' trade data calculations.

**Figure I. U.S. Trade with the UK in Goods and Services, 2003-2016**

Source: CRS, based on data from Bureau of Economic Analysis (BEA).

Globally, in goods trade, the UK ranked as the United States' fifth-largest export destination and seventh-largest source of imports. Top U.S. goods exports to the UK include civilian aircraft and parts, nonmonetary gold bullion, art, and light fuels. Top U.S. imports from the UK include drug compounds, certain motor fuels (not including gasoline), whiskies, art, and passenger motor vehicles.<sup>12</sup> The UK is the United States' largest services trading partner, accounting for close to one-tenth of U.S. total trade in services and spanning sectors such as financial services, tourism, education, and business services.<sup>13</sup> The United States is the UK's largest food and agricultural trading partner outside the EU for both exports and imports.<sup>14</sup> While the U.S.-UK trade is significant and stands out in particular sectors, it is outweighed by U.S. trade with the rest of the EU (Figure 2).

Bilateral foreign direct investment (FDI) is also prominent in the relationship (see Figure 3). In recent years, U.S. and UK majority-owned multinational enterprises (MNEs) have employed over 2 million employees combined at their subsidiaries in each other's markets.<sup>15</sup> In 2015, U.S.-UK FDI totaled \$1.1 trillion, composed of \$593 billion of U.S. outbound FDI and \$484 billion of inbound FDI to the United States. The UK ranked as the second-largest destination for U.S. FDI abroad (the Netherlands being the largest), and the largest source of FDI in the United States (ahead of Japan and Luxembourg).

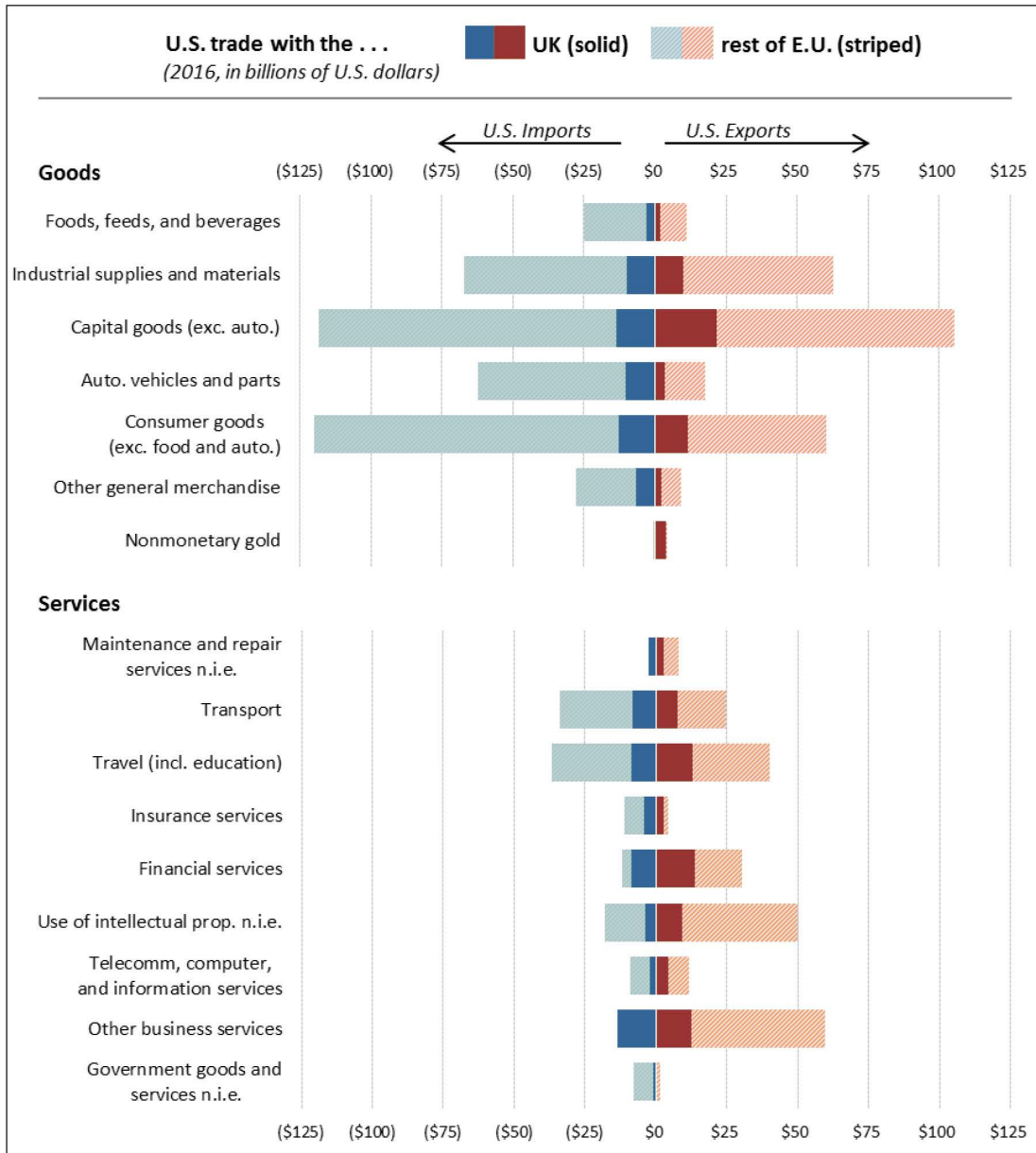
<sup>12</sup> Data from ITC, Dataweb, at 10-digit Harmonized Tariff Schedule (HTS) level.

<sup>13</sup> Data from U.S. Department of Commerce, Bureau of Economic Analysis (BEA).

<sup>14</sup> U.S. Department of Agriculture (USDA), Foreign Agricultural Service (FAS), *United Kingdom: Exporter Guide 2016*, December 13, 2016.

<sup>15</sup> BEA, "United Kingdom – International Trade and Investment Country Facts."

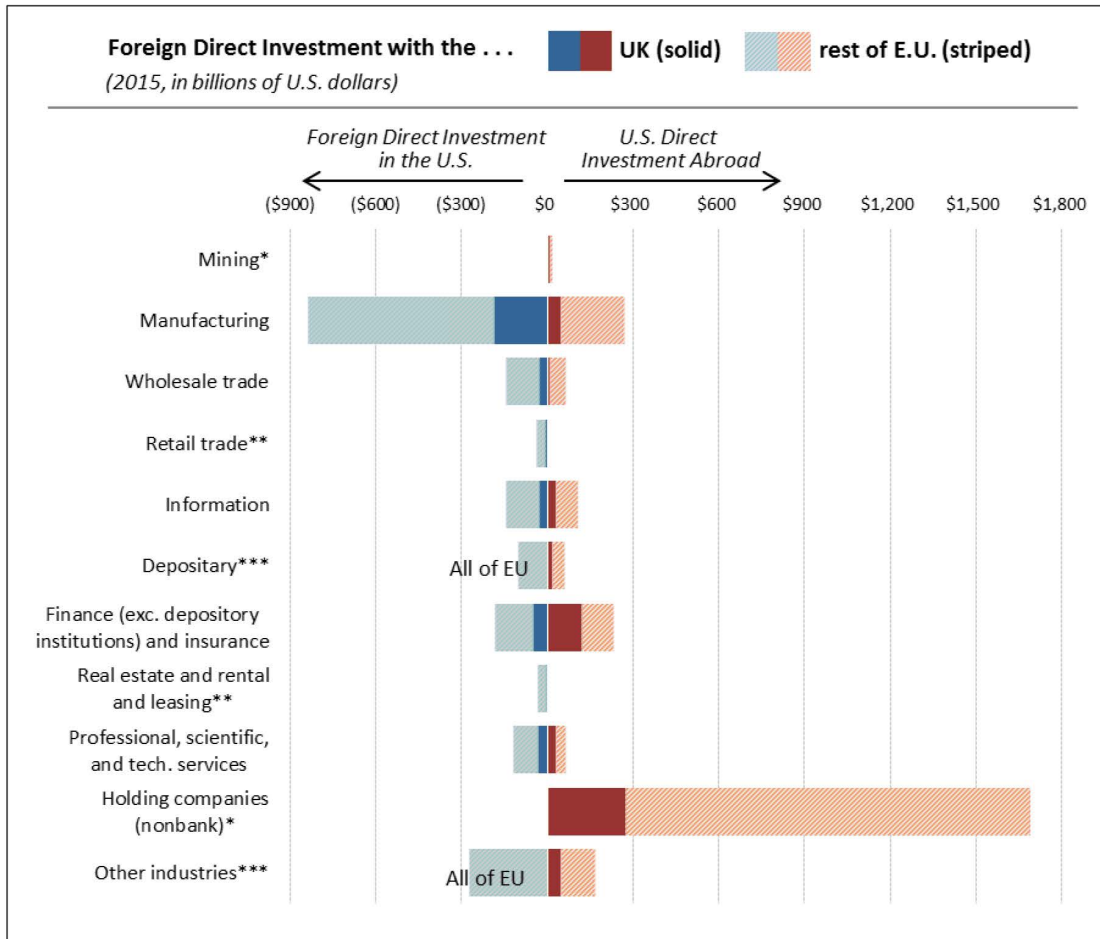
**Figure 2. U.S. Trade with the UK and the Rest of the EU**



**Source:** CRS, data from U.S. Bureau of Economic Analysis.

**Notes:** The term “n.i.e.” denotes “not included elsewhere.” For the maintenance and repair services n.i.e. category and the other business services category, data for U.S. imports from the EU were suppressed to avoid disclosure of individual companies.

**Figure 3. U.S. Investment with the UK and the Rest of the EU**



**Source:** CRS, data from U.S. Bureau of Economic Analysis.

**Notes:**

\*For the categories of mining and holding companies (nonbank), data on UK and EU FDI in the United States were not provided.

\*\*For the categories of retail trade and real estate/rental/leasing, data on U.S. FDI in the UK and EU were not provided.

\*\*\*For the categories of depository institutions and other industries, data on UK FDI in the United States were suppressed to avoid disclosure of individual companies, so data for the EU as a whole are shown.

A number of industries stand out in the U.S.-UK investment relationship, notably finance and insurance, “professional, scientific, and technical” services, and manufacturing (particularly chemicals, transportation, equipment, and primary and fabricated metals). U.S. companies are attracted to the UK for its open business environment, workforce skills, and (current) access to the EU Single Market, among other things. U.S. financial companies in the UK presently can take advantage of “passporting rights,” through which they can set up a “hub” in the UK and then carry out their activities across the EU without having to establish a separate entity and/or obtain authorization in each individual member country.<sup>20</sup>

UK majority-owned MNEs with U.S. operations also play a role in U.S. trade. They represented \$73.5 billion of U.S. exports of goods and \$86.6 billion of U.S. imports of goods with affiliates in 2014.<sup>21</sup>

The United States and UK have had minimal trade frictions. However, the UK notably has been a part of the long-running U.S.-EU dispute in the World Trade Organization (WTO) over subsidies to Boeing and Airbus.

## U.S.-UK FTA Prospects

Brexit is expected to return authority to the UK to set its own external tariffs and its trade policy more broadly, a competence that currently resides with the EU for all EU member states. Formal U.S.-UK FTA negotiations, nevertheless, cannot start immediately. Article 50 of the Treaty on European Union (TEU) sets a two-year period for exit negotiations, although some analysts raise the possibility of the process taking longer. Until the UK completes what could be prolonged negotiations for its withdrawal from the EU and formally exits, the UK remains a member of the EU, and the EU continues to have

### Is Brexit Affecting U.S. Companies Operating in the UK?

Many large U.S. companies, in a range of sectors, have a presence in the UK. The Brexit vote does not immediately affect U.S. trade and investment with the UK, but presumably would when the UK’s withdrawal from the EU takes effect. Meanwhile, the uncertainty over the outcome of Brexit may affect the business planning and investment decisions of U.S. firms operating in the UK. To what extent U.S. companies generally maintain their significant presence in a post-Brexit UK as a base for their European operations is unclear.

One survey found that 40% of U.S. firms with a base in the UK were considering shifting operations to other places in the EU due to Brexit.<sup>16</sup> In contrast, Apple has announced plans to build a new UK headquarters in London.<sup>17</sup> U.S. financial companies may be particularly affected, for instance, if Brexit results in a loss of “passporting rights.” U.S. banks such as Citi, Goldman Sachs, JP Morgan, and Morgan Stanley reportedly are considering reducing their UK presence in preparation for Brexit.<sup>18</sup> Brexit also might affect the attractiveness of the UK as a “jumping-off point” to access the broader EU market for trade; potential loss of UK access to the EU Single Market could increase tariffs for U.S. businesses in the UK that export from the UK to other parts of the EU. Whirlpool is planning to reorient a factory in the UK to focus on producing dryers solely for UK customers, and to use a Poland factory instead to make dryers for continental Europe—a change it said was due to a reorganization of its regional operations, though some see the move as a response to Brexit. Other companies have said that their business decisions in the UK are not related to Brexit. For instance, Ford says that it plans to cut jobs from its Welsh engine facility because of underperformance, not Brexit.<sup>19</sup>

<sup>16</sup> Zlata Rodionova, “Brexit: 40% of US Firms with British Offices are Considering Relocating to the EU,” *Independent*, December 14, 2016.

<sup>17</sup> U.S. Chamber of Commerce, “Apple ‘Optimistic’ About Post-Brexit UK,” press release, February 14, 2017.

<sup>18</sup> Silvia Sciorilli Borrelli, “U.S. Banks Lay Groundwork to Leave London—Reluctantly,” *PoliticoPro*, November 18, 2016.

<sup>19</sup> Peter Campbell and Jim Pickard, “Ford Plans to Cut More Than 1,100 Jobs at UK’s Bridgend Plant,” *Financial Times*, March 1, 2017.

<sup>20</sup> Her Majesty’s Government (HM Government), *Review of the Balance of Competences between the United Kingdom and the European Union, The Single Market: Financial Services and the Movement of Capital*, February 2014, p. 30.

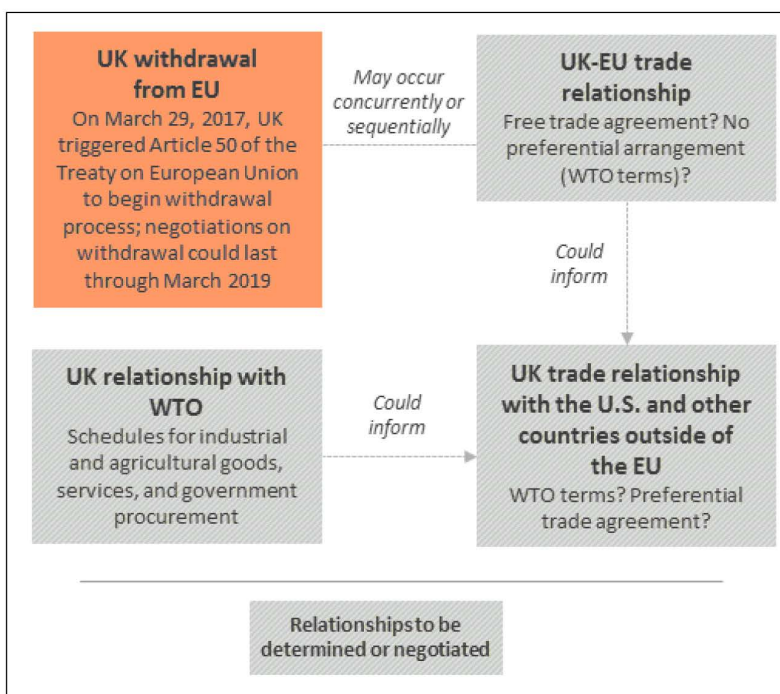
<sup>21</sup> BEA, *Foreign Direct Investment in the United States: Preliminary 2014 Statistics, Majority-Owned Affiliates*.

exclusive competence over the UK’s trade policy as it does for other EU member states—meaning that the EU negotiates a common trade policy with non-EU countries on behalf of (and with input from) its member states.<sup>22</sup> In the meantime, the United States and the UK could pursue preliminary “informal” discussions. The line between “formal” and “informal” negotiations may be blurry, but moves such as exchanging tariff offers presumably would cross the line. A European Commission spokesperson described informal discussions as, “You can read the menu, but you can’t order the food.”<sup>23</sup>

### Brexit Variables Affecting U.S.-UK FTA Prospects

Several variables in Brexit could affect prospects for a U.S.-UK FTA (see **Figure 4**). These include UK-EU negotiations on the UK’s withdrawal from the EU, UK-EU negotiations on their trade relationship once the UK has formally exited the EU, and UK negotiations with other WTO members on its WTO schedule, as well as any transitional arrangements that the UK negotiates until final agreements in these areas are concluded.

**Figure 4. Brexit Variables that May Affect U.S.-UK FTA Prospects**



**Source:** CRS.

**Notes:** This is a highly simplified representation of the many variables in the Brexit process.

How long it takes to negotiate Brexit would affect when the UK is legally free to pursue formal FTA negotiations with the United States or other countries. The trade relationship that the UK negotiates with the EU could affect what positions the United States and the UK may take in their own bilateral FTA negotiations. Finally, the terms that the UK negotiates with the WTO could set

<sup>22</sup> CRS Report RS21372, *The European Union: Questions and Answers*, by Kristin Archick.

<sup>23</sup> Josh Lowe, “Why a U.S.-UK Trade Deal Could Be Harder Than It Sounds,” *Newsweek*, January 26, 2017.

a baseline for the U.S.-UK FTA negotiations, since U.S. FTAs traditionally have built on WTO terms and rules for enhanced market access.

### **UK-EU Trade Relations**

The status of UK trade relations with the United States depends, to a large degree, on UK-EU trade relations going forward, as U.S. businesses that currently trade and invest with the UK benefit from the UK's access to the Single Market. Without clarity on the UK's internal market, it is difficult for U.S. negotiators to know the starting point for negotiating an FTA with the UK.

Future UK-EU trade relations, in turn, depend on the outcomes of two negotiations: (1) the terms of the UK's negotiated withdrawal from the EU under the two-year Article 50 process of the Treaty on European Union (TEU); and (2) UK-EU negotiations on their future trade relationship. Regarding sequencing, the UK favors conducting the negotiations about the UK-EU future partnership in parallel with the withdrawal negotiations.<sup>24</sup> In contrast, the EU has stated that the withdrawal negotiations must precede the negotiations over trade relations.<sup>25</sup>

From a trade policy perspective, Brexit presents the question of the extent to which, if at all, the UK would retain access to the Single Market for goods and services, as well as what EU regulations the UK chooses to retain, and the associated trade-offs. Such questions are key given the high level of integration between the UK and the EU-27; the EU is the UK's largest trading partner for both goods and services (see **Figure 5**), though its share has declined in recent years.

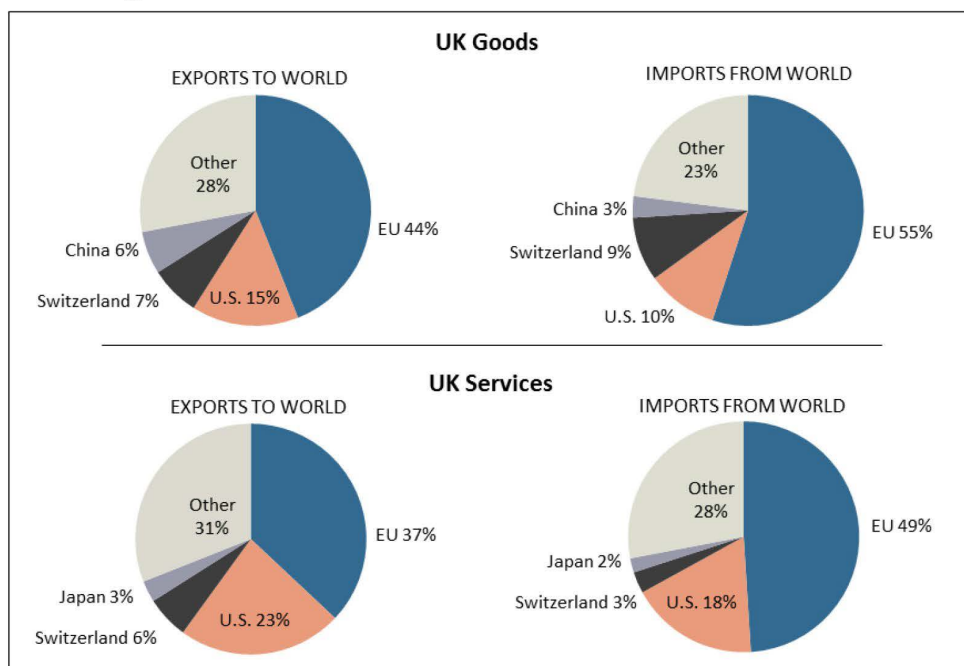
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<sup>24</sup> UK Department of Exiting the EU, "Prime Minister's Letter to Donald Tusk Triggering Article 50," correspondence, March 29, 2017.

<sup>25</sup> European Council, "Statement by the European Council (Art. 50) on the UK Notification," March 29, 2017; Duncan Robinson and Mehreen Khan, "European Parliament Adopts Brexit Resolution," *Financial Times*, April 5, 2017.



**Figure 5. UK Goods and Services Trade with the World, 2015**



**Source:** CRS, data from World Trade Organization.

In the aftermath of the Brexit vote, observers put forward many possible scenarios for the post-Brexit UK-EU trade relationship.<sup>26</sup> These scenarios vary in their level of Single Market access, obligations to implement EU rules and regulations, opportunity to participate in EU decisionmaking, requirements to contribute to the EU’s budget, and political feasibility. UK Secretary of State for Exiting the European Union David Davis stated that the UK was not seeking an “off the shelf” model.<sup>27</sup> Nevertheless, existing arrangements between the EU and other countries could shed light on some possibilities for negotiating approaches (see **text box**).

<sup>26</sup> Jean-Claude Piris, *If the UK Votes to Leave: The Seven Alternatives to EU Membership*, Centre for European Reform, January 2016.

<sup>27</sup> UK Government, “Exiting the European Union: Ministerial Statement,” oral statement by Secretary of State for Exiting the European Union David Davis in the House of Commons on the work of the Department for Exiting the European Union, September 5, 2016.

### Examples of Possible Forms for UK-EU Trade Relationship

**WTO Terms?** If the UK does not negotiate preferential market access with the EU, the “default” would be that WTO commitments govern the UK-EU relationship. WTO terms for the UK and, to some extent, the EU would have to be renegotiated as a result of Brexit (see next section). Under its WTO commitments, EU average tariff rates are low (see **Table I**), but are significant compared to the zero tariffs that apply to intra-EU trade, and would be especially consequential for sectors such as autos where the UK-EU market is deeply integrated.

**Free Trade Agreement?** The UK could negotiate a comprehensive bilateral FTA with the EU. For example, the EU-Canada Comprehensive Economic and Trade Agreement (CETA), concluded in 2014 and awaiting entry-into-force, covers tariff and nontariff barriers related to goods, services, agriculture, investment, government procurement, and regulatory cooperation. EU FTAs have varied in their scope of trade liberalization and rules-setting. The EU has said the UK cannot have a better trade relationship with the EU outside of the Single Market than within it.

**Specialized Arrangements?** Other arrangements could serve as models. For example, Norway, as a member of certain European groupings, has full access to the Single Market, in exchange for which it must implement EU rules for the internal market. In contrast, Switzerland has more limited, but tailored and arguably more complex, access to the Single Market; it has numerous bilateral agreements with the EU covering various sectors, giving it partial access to the Single Market, in exchange for which it must incorporate related EU regulations and directives into its legal framework. Even more limited access occurs for Turkey through its customs union with the EU, which gives it access to the Single Market for goods, but not for agriculture or services. As a customs union member, Turkey adopted the EU’s common external tariff for the products covered. Under these arrangements, the countries have no vote in EU decisions on rules and regulations and, in the case of Norway and Switzerland, must contribute to the EU’s budget.

In a January 17, 2017, speech, Prime Minister May set out the British government’s negotiating objectives and plan for exiting the EU.<sup>28</sup> A February 2017 white paper subsequently released by the UK government elaborated on these positions.<sup>29</sup> The Prime Minister confirmed that the UK is not seeking membership in the EU Single Market, but rather the negotiation of an FTA with the EU to allow “the freest possible trade in goods and services between Britain and the EU’s member states.”<sup>30</sup> The Prime Minister further noted that

[the] agreement [between the UK and EU] may take in elements of current single market arrangements in certain areas—on the export of cars and lorries for example, or the freedom to provide financial services across national borders – as it makes no sense to start again from scratch when Britain and the remaining [m]ember [s]tates have adhered to the same rules for so many years....<sup>31</sup>

At the same time, the Prime Minister left open the possibility of no trade agreement with the EU if negotiations between the UK and the EU do not lead to an acceptable outcome, saying “no deal for Britain is better than a bad deal for Britain.”<sup>32</sup> EU officials and some industry groups have pushed back on this view.<sup>33</sup> Some have characterized scenarios of a negotiated UK-EU trade deal as a “soft” Brexit and the absence of such a deal as a “hard” Brexit.<sup>34</sup>

<sup>28</sup> UK Government, “The Government’s Negotiating Objectives for Exiting the EU: PM Speech,” January 17, 2017. The Single Market entails “four freedoms”— free movement of goods, capital, services, and people within the EU.

<sup>29</sup> HM Government, *The United Kingdom’s exit from and new partnership with the European Union*, white paper, February 2017.

<sup>30</sup> UK Government, “The Government’s Negotiating Objectives for Exiting the EU: PM Speech,” January 17, 2017.

<sup>31</sup> *Ibid.*

<sup>32</sup> *Ibid.*

<sup>33</sup> For instance, see U.S.-UK Business Council, “Toward a New UK-EU Relationship: The Importance of Transitional Arrangements,” January 26, 2017.

<sup>34</sup> The terms “soft Brexit” and “hard Brexit” also have been used to describe the possibilities of the UK exiting the EU with a withdrawal agreement in place or without such an agreement, respectively.

The UK government also stated a goal of being able to pursue new trade agreements with other countries post-Brexit. The Prime Minister observed that “full [c]ustoms [u]nion membership,” which binds the UK to the EU’s common external tariff, prevents the UK from negotiating its own trade deals with other countries, and the white paper stated, “the UK will seek a new customs arrangement with the EU...” For some observers, questions arose over the extent to which the UK might remain a part of the EU customs union. Chancellor of the Exchequer Philip Hammond later confirmed that it is “clear” that the UK cannot stay in the customs union, as that would prevent the UK from independently negotiating its own trade deals outside of the EU.<sup>39</sup>

The EU has relatively low external tariffs on goods, but the UK may seek lower or no tariffs in certain sectors. Some observers expect the UK to focus on certain sectors in its trade negotiations with the EU given these sectors’ high level of UK-EU integration, such as autos, chemicals, manufactured goods, and mineral fuels—sectors in which a large share of UK exports go to the EU.<sup>40</sup> Financial services also may be a focal point (see **text box**). Agriculture may be sensitive, given various interests and the EU’s higher average tariffs on agricultural.

In the meantime, in what may be a lengthy negotiation with the EU of its terms of withdrawal, the UK remains an EU member, and the EU continues to have exclusive competence over the UK’s trade policy as it does for other EU member states.<sup>41</sup> This precludes formal U.S.-UK FTA negotiations starting immediately, but does not preclude informal discussions.

### Financial “Passporting” Rights

Presently, U.S. and other financial companies in the UK can take advantage of “passporting rights,” through which they can incorporate in one EU member state (e.g., the UK) and carry out activities in other member states “solely on the basis of their authori[z]ation and prudential supervision by their state of incorporation.”<sup>35</sup> Brexit confronts financial companies operating in the UK with uncertainty over the level of future access to the broader EU market from the UK. As noted earlier, several U.S. banks, such as Citi, Goldman Sachs, JP Morgan, and Morgan Stanley, reportedly are considering reducing their UK presence in preparation for expected disruption from Brexit.<sup>36</sup> UK banks such as HSBC and UBS also have announced similar plans or considerations.<sup>37</sup> New locations could include Brussels, Dublin, Frankfurt, and New York. Some analysts point out that the EU has established an “equivalence” regime that extends limited access rights to non-EU countries, such as the United States, that have rules that the EU considers to be “equivalent.” This approach grants weaker rights than those under full “passporting.”<sup>38</sup>

<sup>35</sup> HM Government, *Review of the Balance of Competences Between the United Kingdom and the European Union, The Single Market: Financial Services and the Movement of Capital*, February 2014, p. 30.

<sup>36</sup> Silvia Sciorilli Borrelli, “U.S. Banks Lay Groundwork to Leave London—Reluctantly,” PoliticoPro, November 18, 2016.

<sup>37</sup> Pamela Barbagalia, “HSBC, UBS to Shift 1,000 Jobs Each from UK in Brexit Blow to London,” Reuters, January 18, 2017.

<sup>38</sup> Marcin Szczepeński, *Understanding Equivalence and the Single Passport in Financial Services: Third-country Access to the Single Market*, European Parliamentary Research Service, February 2017.

<sup>39</sup> Alex Morales and Robert Hutton, “Hammond Confirms Brexit Means U.K. Also Leaving Customs Union,” Bloomberg Government, March 9, 2017.

<sup>40</sup> Economist Intelligence Unit (EIU), *United Kingdom*, Country Report, generated February 1, 2017.

<sup>41</sup> CRS Report RS21372, *The European Union: Questions and Answers*, by Kristin Archick.

## UK Relations with the WTO

Another variable affecting U.S.-UK FTA prospects is any redefinition of the UK's commitments in the WTO, which would form the basis for any future trade relationships that it negotiates outside the EU, whether with the United States or other countries.<sup>42</sup> Redefinition of the UK's terms of trade in the WTO raises unprecedented issues for the WTO.<sup>43</sup>

The UK is a founding member of the WTO. It currently has WTO membership both on an individual basis and as a part of the EU. The UK's commitments to other WTO members presently are through the EU's schedule of commitments in the WTO. Transitioning to an independent position in the WTO will require the UK to negotiate new goods and services schedules on its WTO market access commitments (see **text box**). The WTO, which currently has 164 members, operates on a consensus basis. Some aspects of the UK's WTO transition, such as establishing its most-favored-nation (MFN) tariff levels, may be relatively straightforward.<sup>44</sup> The UK could "cut and paste" the EU's bound tariff rates to its own schedule, though, of course, the UK's internal economic and political dynamics may lead it to pursue different tariff levels. Establishing tariff-rate quotas (TRQs) may be more complicated, as doing so will require reallocation of the EU's quotas under the WTO. The EU maintains TRQs on products such as beef, poultry, dairy, cereals, rice, sugar, fruits, and vegetables. Other aspects include commitments under the Government Procurement Agreement (GPA), of which the UK is a member through its EU membership but is not currently a nation-state member.

Some observers note that the UK may face difficulty securing approval from WTO members for its proposed schedule, pointing to the possibility that countries that have territorial disputes with the UK—such as Argentina over the Falkland Islands or Spain over Gibraltar—could use the WTO negotiation process as leverage to address these issues with the UK.<sup>45</sup> Others say that any lack of formal approval ("certification") of the UK's proposed new schedule should not be a bar to the UK negotiating trade agreements with other countries. They note that the EU's schedule as

### WTO Schedule of Commitments

Each WTO member negotiates "schedules" on the market access it commits to providing other WTO members. The UK will have to reestablish its independent goods and services schedules, as well as in the plurilateral Government Procurement Agreement (GPA).

**Goods Schedule.** A country's goods schedule includes its most-favored-nation (MFN) "bound" tariff rates (i.e., the maximum tariff level) for manufactured goods and agricultural products. The schedule also includes tariff-rate quotas (TRQs) for agricultural products, under which rates for imports inside a quota are lower, and in many cases significantly so, than for those outside the quota. In addition, agreements on export subsidies and domestic support for particular industries, among other things, are a part of a goods schedule.

**Services Schedule.** Services commitments include commitments to provide market access and national treatment for service activities, subject to any terms and conditions specified in the schedule. Countries can take exception to providing MFN treatment to the services sectors that they specify.

**Government procurement.** A country also specifies which central and sub-central government entities, and above which thresholds, it commits to complying with the GPA, a plurilateral WTO agreement of which both the United States and the EU are members.

<sup>42</sup> UK Government, "The government's negotiating objectives for exiting the EU: PM speech," January 17, 2017.

<sup>43</sup> WTO, "Azevêdo addresses World Trade Symposium in London on the state of global trade," press release, June 7, 2016.

<sup>44</sup> The MFN tariff is the normal nondiscriminatory tariff that a WTO member charges on imports from another WTO member, excluding preferential tariffs under FTAs and other schemes or tariffs charged inside quotas.

<sup>45</sup> Joe Watts, "Brexit: UK's WTO Status 'Could Be Blocked Over Territorial Disputes'," *Independent*, December 11, 2016.

the EU-28 has lacked full certification, and that has not stopped the EU from entering into FTAs. Under this view, so long as the UK does not make its trade terms more restrictive than the EU's schedule, it may not run afoul of WTO obligations.<sup>46</sup>

In terms of sequencing, negotiations for UK's transition in the WTO could happen alongside UK withdrawal negotiations. According to UK's Secretary of State for International Trade Liam Fox,

[i]n order to minimi[z]e disruption to global trade as we leave the EU, over the coming period the Government will prepare the necessary draft schedules which replicate as far as possible our current obligations. The Government will undertake this process in dialogue with the WTO membership. This work is a necessary part of our leaving the EU. It does not prejudice the outcome of the eventual UK-EU trading arrangement.<sup>47</sup>

Meanwhile, the UK's WTO commitments remain as set out in the EU's schedules that apply to all EU member states until Brexit occurs.<sup>48</sup>

In the absence of any preferential trade arrangement with a country, WTO terms would form the basis of the UK's trade relationship with that country. Since the United States and the EU do not have an FTA with each other (T-TIP negotiations are on pause), WTO terms already govern U.S. trade with the UK, as they do with other EU member countries. Those terms would continue to govern unless and until a U.S.-UK FTA is negotiated and enters into force.

## Specific Issues in Potential U.S.-UK FTA

Congress established U.S. trade negotiating objectives in the 2015 Trade Promotion Authority (TPA) legislation (P.L. 114-26).<sup>49</sup> U.S.-UK FTA negotiations, if launched in the next few years, presumably would be conducted under TPA. Such negotiating objectives, as well as TPA's notification and consultation requirements, would be expected to guide the Administration's negotiations on a potential U.S.-UK FTA.

Based on U.S. trade negotiating objectives, the past U.S. approach has been to negotiate comprehensive and high standard FTAs to liberalize trade and investment through reciprocal commitments to reduce and eliminate tariff and nontariff barriers in goods, services, and agriculture, as well as to establish trade rules and disciplines to govern trade among the parties. These commitments expand on WTO obligations and address new issues. It is uncertain how the Trump Administration may approach U.S.-UK FTA negotiations, including whether it may pursue a tariff-only FTA, one focused on a few priority sectors, or a more traditional U.S. FTA. Possible areas in the negotiations are highlighted below.

### Market Access

Commitments to expand and enhance market access have been a core part of U.S. FTAs. Enhanced market access addresses a number of issues, including reducing and eliminating tariff

<sup>46</sup> Geoff Raby, "The EU's Ambiguous Legal Position in the WTO Reduces the Uncertainty over Britain's Post-Brexit Trading Relationships," Policy Exchange, November 19, 2016; Aakanksha Mishra, "A Post Brexit UK in the WTO: The UK's New GATT Tariff Schedule," in *Legal Aspects of Brexit: Implications of the United Kingdom's Decision to Withdraw from the European Union*, ed. Jennifer Hillman and Gary Horlick (Washington, DC 2017).

<sup>47</sup> UK Parliament, "UK's Commitment at the World Trade Organization: Written Statement – HCWS316," made by Secretary of State for International Trade and President of the Board of Trade Liam Fox, December 5, 2016.

<sup>48</sup> Julian Braithwaite, "Ensuring a Smooth Transition in the WTO as We Leave The EU," blog post, January 23, 2017.

<sup>49</sup> CRS Report RL33743, *Trade Promotion Authority (TPA) and the Role of Congress in Trade Policy*, by Ian F. Fergusson.

and nontariff barriers. Tariff liberalization could be a component of a potential U.S.-UK FTA. Industrial tariffs applied by the United States and UK (through the EU's tariff schedule) are already relatively low (see **Table 1**), but higher in certain sensitive sectors.<sup>50</sup> For instance, EU tariffs on automobiles are 10%. Expanding agricultural market access could be a key area of focus for the United States, given high EU average tariffs or tariff-rate quotas (TRQs) on products such as meat, fish, sugar, dairy products, soft drinks, and wine. It remains to be seen if a U.S.-UK FTA would face the same issues with respect to market access that confronted U.S. and EU negotiators in T-TIP. In those negotiations, the United States and the EU exchanged tariff offers to reduce and eliminate tariffs on most industrial goods, but opted to leave agricultural tariff issues, which were highly sensitive, until “end-game” negotiations.

**Table 1. U.S. and UK WTO Tariff Profiles**  
(percentage)

Tariff Rate	UK (EU tariff schedule)	United States
<b>Overall</b>		
Simple average MFN applied	5.1	3.5
Trade-weighted average	2.7	2.2
<b>Agriculture</b>		
Simple average MFN applied	10.7	5.2
Trade-weighted average	8.5	3.8
<b>Non-agriculture</b>		
Simple average MFN applied	4.2	3.2
Trade-weighted average	2.3	2.1

**Source:** CRS compilation, WTO Tariff Profiles.

**Notes:** Data for “simple average MFN applied” are from 2015, and for “trade-weighted average” from 2014.

Services market access could be significant in potential FTA negotiations, given the high level of U.S.-UK services trade. Regulatory and other barriers to trade in services could be a focal point (see “Regulatory Cooperation and Standard-Setting” section below). Other areas of interest could include issues such as licensing and qualification requirements for professional service providers, as well as rules on the movement of foreign nationals for temporary entry and stay for business travel.<sup>51</sup> Some services issues that were complex in T-TIP may be less so in U.S.-UK FTA negotiations. For instance, “cultural exceptions” were controversial in T-TIP due to the interest of countries like France in protecting its audiovisual sector.<sup>52</sup>

Other market access issues could arise in terms of public procurement. U.S. FTAs include rules to ensure transparent, nondiscriminatory access for U.S. firms to trading partners’ public

<sup>50</sup> WTO, Tariff Profiles.

<sup>51</sup> CRS Report R44354, *Trade in Services Agreement (TiSA) Negotiations: Overview and Issues for Congress*, by Rachel F. Fefer.

<sup>52</sup> Through cultural exceptions, countries provide special support to domestic industries that they consider culturally sensitive, such as through broadcasting quotas, subsidies, and local content requirements. These measures can limit market access to such industries for foreigners. For example, France maintains cultural exceptions for its film and television industries. Led by France, some EU member states have called for the exclusion of the audiovisual services sector from the T-TIP negotiations.

procurement markets in covered sectors at certain thresholds, and vice versa. In the transatlantic context, frictions have included, on the U.S. side, concerns about the transparency of EU public procurement policies, and on the EU side, concerns about U.S. restrictions to certain sensitive sectors, Buy American legislation, and access to U.S. state-level government procurement markets.<sup>53</sup> These issues could also be politically sensitive in U.S.-UK FTA negotiations. President Trump has advocated for a “Buy American” and “Hire American” policy, while the UK released a post-Brexit industrial strategy including a goal of using “strategic government procurement to drive innovation and enable the development of UK supply chains.”<sup>54</sup> More restrictive Buy American policies may run afoul of the WTO Government Procurement Agreement (GPA); the United States is a member of the GPA, and the UK also is a GPA member through its membership in the EU (but is not currently a nation-state member of that agreement).

## Trade-Related Rules

U.S. FTAs contain rules and disciplines governing a range of trade-related areas. Potential areas of interest in a bilateral FTA include the following.

**Investment.** Given high levels of bilateral FDI, investment rules could be a major part of a U.S.-UK FTA. U.S. international agreements on investment typically include market access commitments, investor protections such as nondiscriminatory and minimum standard of treatment, and compensation for direct and, in limited cases, indirect expropriation, as well as enforcement of these obligations through investor-state dispute settlement (ISDS).<sup>55</sup> An open question could be treatment of ISDS, a mechanism for an investor to take a host country to binding arbitration for alleged breaches of obligations. ISDS has been a core part of many U.S. and European investment agreements, but was highly contested in public debates over T-TIP on both sides of the Atlantic. In the UK, as in the United States, the debate reflected differing stakeholder views on ISDS. The UK government previously sought to dispel what it termed as “myths and misconceptions” about aspects of T-TIP, such as the notion that potential new ISDS provisions could threaten regulatory sovereignty.<sup>56</sup> An added dynamic is the EU’s proposal to establish a new “Investment Court System” in place of ISDS. The EU included the Investment Court System in its recent trade agreements with Canada and Vietnam. This new system has some key differences from traditional ISDS, including its inclusion of an appellate mechanism. The Obama Administration favored maintaining ISDS, and U.S. industry groups criticized the Investment Court System. It is not clear what position the Trump Administration or the UK would take regarding this issue.

**Digital trade.** Cross-border data flows are key to the U.S.-UK trading relationship, whether for manufacturing operations or financial services firms. Similar to provisions in TPP, a U.S.-UK FTA could address ways to facilitate cross-border data flows for business transactions and reduce barriers to digital trade, such as “forced” localization requirements.<sup>57</sup> Any future UK-EU regulatory relationship may inform the nature of U.S.-UK FTA negotiations on digital trade. For instance, the extent to which the U.S.-EU Privacy Shield applies or whether the UK adopts

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<sup>53</sup> European Commission, *Report from the Commission to the Council and the European Parliament on Trade and Investment Barriers and Protectionist Trends*, for the period July 1, 2014 through December 31, 2015, June 20, 2016.

<sup>54</sup> HM Government, *Building our Industrial Strategy*, Green Paper, January 2017.

<sup>55</sup> CRS In Focus IF10052, *U.S. International Investment Agreements (IIAs)*, by Martin A. Weiss and Shayerah Ilias Akhtar.

<sup>56</sup> Government of the United Kingdom, “TTIP: Separating Myth from Fact,” April 25, 2016.

<sup>57</sup> CRS Report R44565, *Digital Trade and U.S. Trade Policy*, coordinated by Rachel F. Fefer.

policies consistent with the EU's General Data Protection Regulation (GDPR) may have bearing. Discussions on cross-border flows in a bilateral FTA may not have the same level of sensitivities over privacy issues that constrained the T-TIP negotiations in the wake of disclosures of National Security Agency (NSA) surveillance activity.<sup>58</sup> Such issues were particularly controversial for countries like Germany.

**Intellectual property rights.** Another area of significant interest is rules on intellectual property (IP) protection and enforcement. Both the United States and the UK are major centers of research and development and innovation, view IP as a source of comparative advantage, and are strong proponents of advancing trade-related rules for IP protection and enforcement.<sup>59</sup> A U.S.-UK FTA could present opportunities for cooperation on IP issues, such as combating cyber theft of trade secrets and enhancing protections for biologics. A bilateral FTA may not face the same challenges as did T-TIP on IP issues such as geographical indications (GIs), which protect regional food names. Protection of GIs is a key priority for countries like France and Italy, but less so for the UK (though the UK does have over 60 registered GIs, including for Stilton Cheese and Cornish Pasty).<sup>60</sup> The United States has favored protecting regional food names primarily through trademarks.

**Other issues.** A U.S.-UK FTA could also include rules and disciplines in a range of other areas. Some of these are areas that “traditionally” have been a part of U.S. FTAs, such as labor and the environment. The UK's status as a developed economy with strong environmental protections could mitigate concerns of some stakeholders about U.S. outsourcing or reducing environmental standards through an FTA. Other issues for possible discussion have been more recent additions to U.S. FTAs, including rules on state-owned enterprises (SOEs) and commitments to support exports by small- and medium-sized enterprises (SMEs).<sup>61</sup>

## Regulatory Cooperation and Standard-Setting

A U.S.-UK FTA could include commitments on regulatory cooperation and standard-setting, both in terms of horizontal commitments, such as transparency and stakeholder input in regulatory processes, as well as sector-specific commitments. Many of the products in which in the United States and UK trade are in high-value-added but heavily regulated sectors that intersect with consumer safety issues.<sup>62</sup> Sectoral issues of potential interest might include motor vehicle, pharmaceutical, chemical, and food safety regulatory regimes. The United States may view a U.S.-UK FTA as an opportunity to open the UK market to U.S. exports currently constrained by EU restrictions, such as sanitary and phytosanitary (SPS) barriers and technical barriers to trade (TBT). For instance, frictions on the U.S. side have included EU restrictions such as those on chlorine-washed chicken, hormone-raised beef, and genetically engineered food.<sup>63</sup> In general, the UK is more closely aligned with the U.S. approach to regulatory issues than the EU but not

<sup>58</sup> CRS Report R44257, *U.S.-EU Data Privacy: From Safe Harbor to Privacy Shield*, by Martin A. Weiss and Kristin Archick.

<sup>59</sup> UK Government, “IP and Brexit: The Facts,” August 2, 2016.

<sup>60</sup> EU, Database of Origin & Registration (DOOR), accessed March 15, 2017. For background, see CRS Report R44556, *Geographical Indications (GIs) in U.S. Food and Agricultural Trade*, by Renée Johnson.

<sup>61</sup> CRS Insight IN10443, *CRS Products on the Trans-Pacific Partnership (TPP)*, by Ian F. Fergusson and Brock R. Williams.

<sup>62</sup> Chad P. Bown, “A UK-US Trade Stumbling Block: Regulations” (video), Peterson Institute for International Economics, January 27, 2017.

<sup>63</sup> CRS Report R44564, *Agriculture and the Transatlantic Trade and Investment Partnership (T-TIP) Negotiations*, by Renée Johnson.



necessarily in all areas. For instance, some UK consumers continue to reject genetically engineered foods.

Regulatory cooperation has been a major sticking point in the overall transatlantic relationship because of differing regulatory approaches. Broadly speaking, the United States prefers risk-based assessments, while the EU favors the “precautionary principle” through preventative decisionmaking in case of risk; both sides view their approaches as science-based.<sup>64</sup> T-TIP negotiations became weighted down by EU public debate over the impact of a U.S.-EU FTA on food safety and other regulatory concerns, though subsequent progress has been made in some areas. For example, in March 2017, the United States and the EU amended a 1998 U.S.-EU Mutual Recognition Agreement to allow for U.S. and EU regulators to rely upon each other’s inspections of pharmaceutical manufacturing facilities to avoid duplication of inspections.<sup>65</sup>

How the United States and the UK approach regulatory cooperation and standard setting within the context of a bilateral FTA will depend in large part on the extent to which the UK reclaims its regulatory authority from the EU during Brexit negotiations, including whether the UK will choose to retain EU regulations or adopt its own national regulations. The UK has said that it plans to introduce a “Great Repeal Bill” to remove the European Communities Act 1972 from its statute book and convert the body of existing EU law (known as “acquis”) into domestic law where practical and appropriate, after which the UK will decide which elements of the law to keep, amend, or repeal.<sup>66</sup> To the extent that UK regulations align with EU regulations, it may be easier for the UK to continue trading with the EU, but compatibility with U.S. standards could be an issue. In some areas, UK divergences from the EU in regulatory approaches that minimize inefficiencies could translate into advantages for UK trade relations with the United States or other countries.

### Financial Services Regulatory Cooperation?

Regulatory cooperation in the financial services sector, a key sector in the bilateral economic relationship, could be a significant focus in FTA negotiations. In the T-TIP context, UK officials and financial services industries favored including financial services regulatory issues as part of the U.S.-EU FTA negotiations, a sentiment echoed by some in the U.S. Congress and in the U.S. financial services sector. Some Members of Congress previously called on the Obama Administration to address regulatory discrepancies between the U.S. and EU financial systems in the negotiations, while other Members raised concerns about potentially reopening the Dodd-Frank Wall Street Reform and Consumer Protection Act (P.L. 111-203). However, under the Obama Administration, the Department of the Treasury resisted including financial services regulatory issues in the T-TIP negotiations, in part over concern about interfering with discussions in other forums, such as the G-20. It is unclear what position the Trump Administration may take on such issues in the context of a U.S.-UK FTA.

<sup>64</sup> CRS Report R43450, *Sanitary and Phytosanitary (SPS) and Related Non-Tariff Barriers to Agricultural Trade*, by Renée Johnson.

<sup>65</sup> U.S. Food & Drug Administration, “Mutual Recognition Promises New Framework for Pharmaceutical Inspections for United States and European Union,” press release, March 2, 2017.

<sup>66</sup> HM Government, *The United Kingdom’s Exit From and a New Partnership with the European Union*, February 2017, p. 9.

## Issues for Congress

### Prospects for a “Successful” U.S.-UK FTA

Prospects for a U.S.-UK FTA depend on a number of factors over which Congress may conduct oversight in the near term. These include how U.S.-UK FTA negotiations could best advance U.S. trade negotiating objectives established in TPA, as well as the barriers to addressing those negotiating objectives. Other issues include timing for when formal negotiations could start legally. As discussed, this depends in large part on the outcome of the UK’s Brexit negotiations with the EU. The United States and UK also may have political considerations to take into account in determining when to launch trade negotiations, including in the context of overall trade policy priorities. Capacity to negotiate may be an issue on the UK side. The UK has “outsourced” trade negotiating skills to Brussels for decades as part of the EU’s exclusive competence over trade policy, but has sought to rebuild that capacity in recent months. The UK has also indicated interest in negotiating a number of trade agreements, including with countries that have FTAs with the EU and those that do not. The EU has concluded over 50 trade agreements worldwide.<sup>67</sup> Given the many directions UK interest could go and the still growing UK negotiating capacity, an open question is where a U.S.-UK FTA would rank in the priorities.

Some analysts believe that, once legal and procedural roadblocks to U.S.-UK FTA negotiations are removed, the negotiations would be relatively easy and fast to conclude. One reason is that the UK has been characterized as a liberalizing force within the EU that has shared the United States’ traditional support for trade liberalization and a rules-based international trade system. Another reason is that the negotiating dynamics presumably would be less complex because U.S.-UK FTA negotiations would involve two economies, rather than T-TIP’s 29 economies (United States and EU-28 member states). Some may counter, however, that the economic impact of a U.S.-UK FTA also would be smaller than T-TIP (see next section).

Some analysts believe that U.S.-UK FTA negotiations would not face the level of substantive and procedural difficulty that beset the T-TIP negotiations. Given these dynamics, some have called for a U.S.-UK FTA to be implemented within 90 days after Brexit—90 days being the amount of time the executive branch must give Congress before it signs a trade agreement under TPA.<sup>68</sup> Others caution that U.S. FTAs typically take much longer to negotiate and that, even among like-minded trading partners, domestic political interests can complicate trade negotiations.<sup>69</sup>

### Economic and Strategic Impact

Presently, U.S.-UK FTA negotiations are in an informal, prenegotiations stage. U.S. FTAs are generally viewed as having widely distributed economic benefits and concentrated economic costs. The economic impact of a specific FTA would depend, in part, on the breadth and depth of FTA commitments. Yet, broad macroeconomic factors generally are considered to play an

<sup>67</sup> European Commission, “The EU’s Bilateral Trade and Investment Agreements – where are we?”, memo, December 3, 2013, [http://trade.ec.europa.eu/doclib/docs/2012/november/tradoc\\_150129.pdf](http://trade.ec.europa.eu/doclib/docs/2012/november/tradoc_150129.pdf).

<sup>68</sup> U.S. Congress, House Committee on Foreign Affairs, Subcommittee on Terrorism, Nonproliferation, and Trade, *Next Steps in the “Special Relationship”: Impact of a U.S.-UK Free Trade Agreement*, Testimony by Nile Gardiner, The Heritage Foundation, 115th Cong., 1st sess., February 1, 2017.

<sup>69</sup> Caroline Freund and Christine McDaniel, “How Long Does It Take to Conclude a Trade Agreement With the US?”, blog, Peterson Institute for International Economics, July 21, 2016; Doug Palmer, “Trump Could Face Long Path to US-UK Trade Deal,” POLITICO, December 30, 2016.

important role in affecting the U.S. economy as a whole.<sup>70</sup> Given the openness of the U.S. and UK economies, a U.S.-UK FTA may be expected to generate modest economic benefits.<sup>71</sup> Nevertheless, due to the size of the bilateral economic relationship, further trade liberalization could yield significant benefits for particular industries. Regarding the enhanced market access and other benefits that a concluded FTA could bring, some experts caution that no U.S.-UK FTA would replicate the broader EU market access that U.S. affiliates in the UK enjoy by virtue of the UK's membership in the EU and access to the EU Single Market.<sup>72</sup> A potential bilateral FTA could present costs, such as in terms of job losses and other transition costs stemming from increased competition. Such costs, however, could be less than those of other U.S. FTAs, as the United States and the UK are both highly advanced economies.

As U.S.-UK FTA negotiations advance, Congress likely would examine various studies by the U.S. government (e.g., the U.S. International Trade Commission) and external organizations to assess the expected impact of the agreement on the U.S. economy.<sup>73</sup> It should be kept in mind that economic models are highly sensitive to assumptions. Further, data limitations and other issues—including the fact that a number of variables beyond trade affect economic performance—make it difficult to develop precise estimates of the impact of a particular trade agreement on the economy.

Any economic impact of a U.S.-UK FTA is in the longer term, given that the commencement of U.S.-UK FTA negotiations is at least two years away. Over the short run, Brexit-specific factors may have more economic impact on the United States. These factors include the economic impact of Brexit on the EU and on the UK, the amount of time it takes for the UK withdrawal from the EU, and the final composition of the UK-EU economic relationship—all of which could have implications for U.S. trade and investment with both the UK and the EU. Another aspect of the economic relationship is the impact Brexit will have on financial flows and any secondary impact on the dollar if markets perceive additional uncertainty for a EU economic recovery.

A U.S.-UK FTA could have broader strategic implications. For instance, a U.S.-UK FTA could play a similar role to what TPP and T-TIP were expected to play in setting globally relevant rules and disciplines to support economic growth and multilateral trade liberalization through the WTO.<sup>74</sup> It also could strengthen the broader U.S.-UK relationship and add a new dimension to the transatlantic trade relationship. In addition, a U.S.-UK FTA could apply pressure on unlocking past stumbling blocks to progress in T-TIP, assuming that both the United States and EU seek to continue negotiations.

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<sup>70</sup> CRS Report R44546, *The Economic Effects of Trade: Overview and Policy Challenges*, by James K. Jackson.

<sup>71</sup> For instance, the ITC conducted a study finding that, in 2012, existing U.S. bilateral and regional trade agreements expanded U.S. aggregate trade by about 3%, and U.S. real gross domestic product (GDP) and U.S. employment each by less than 1%. See ITC, *Economic Impact of Trade Agreements Implemented Under Trade Authorities Procedures, 2016 Report*, Publication Number: 4614, June 2016.

<sup>72</sup> Daniel S. Hamilton and Joseph P. Quinlan, *The Transatlantic Economy 2017*, American Chamber of Commerce to the European Union (AmCham EU) and Center for Transatlantic Relations, p. 2.

<sup>73</sup> Of historical interest may be an ITC study exploring the economic impact of the UK joining the NAFTA. ITC, *The Impact on the U.S. Economy of Including the United Kingdom in a Free Trade Arrangement With the United States, Canada, and Mexico*, Publication 3339, August 2000, p. iii.

<sup>74</sup> CRS Report R44361, *The Trans-Pacific Partnership (TPP): Strategic Implications*, coordinated by Ben Dolven and Brock R. Williams.

## Role in U.S. Trade Policy

A potential U.S.-UK FTA would fit into a new U.S. emphasis on bilateral trade deals under the Trump Administration, which has expressed a clear preference for focusing on bilateral trade deals in lieu of multiparty ones.<sup>75</sup> The Trump Administration has argued that a bilateral approach allows the United States to use its economic strength and focus on U.S. priorities. This represents a shift from the Obama Administration, which made it a priority to negotiate multiparty regional trade deals, such as TPP and T-TIP. Regional negotiations, while more complex, offer the opportunity for mutually beneficial but politically challenging trade-offs to occur across multiple countries.<sup>76</sup> At the same time, U.S. Trade Representative nominee Robert Lighthizer, while noting that elections in France, Germany, and other EU member states would make it difficult to resume T-TIP negotiations “until at least the end of this year,” stated that the Administration “would be open to exploring ways to address barriers to U.S. exports and to expand trade with the EU and its member states.”<sup>77</sup>

Once Brexit procedural roadblocks to U.S.-UK FTA negotiations are overcome, the question arises of when the Administration may launch formal negotiations, amid other potential U.S. trade negotiations and other trade policy actions. The Trump Administration says that it aims to focus its future trade efforts on the possibility of renegotiating and reviewing existing FTAs, turning first to the North American Free Trade Agreement (NAFTA),<sup>78</sup> and pursuing new bilateral FTAs, including with TPP participants, particularly Japan, and possibly other countries.

Given the already relatively low levels of trade and investment barriers between the United States and the UK, some question whether it is appropriate for the Administration to give priority to negotiating a U.S.-UK FTA. Proponents of a U.S.-UK FTA argue that concluding a bilateral FTA between two economic and political international heavyweights will contribute to future trade liberalization efforts. Others say that, in light of resource constraints and other factors, the United States should pursue FTAs with other countries that present greater barriers to trade. For example, some may argue that the United States would benefit more from resuming T-TIP negotiations, revisiting TPP, or pursuing bilateral deals with countries that were a part of the TPP.

## Implications for T-TIP and Transatlantic Relations

Since July 2013, the United States and the EU have engaged in T-TIP negotiations to liberalize U.S.-EU trade and investment and set globally relevant rules and disciplines to boost economic growth and support multilateral trade liberalization.<sup>79</sup> The 15<sup>th</sup> round, the last under the Obama Administration, occurred in October 2016. By then, the United States and the EU had consolidated texts in a number of areas, but unresolved complex and sensitive issues remained and there was debate over whether political momentum would exist to overcome differences. For instance, public opposition to T-TIP runs high in the EU due to concerns over issues such as over

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<sup>75</sup> USTR, *The President's 2017 Trade Policy Agenda*, March 2017.

<sup>76</sup> Center for Strategic and International Studies (CSIS), “The Future of Global Trade” Armchair Conversation with: Ambassador Michael Froman, USTR, and John J. Hamre, President and CEO, CSIS, January 13, 2016.

<sup>77</sup> U.S. Congress, Senate Committee on Finance, *Hearing on the Nomination of Robert E. Lighthizer to be United States Trade Representative*, Responses to Questions for the Record, 115th Cong., 1st sess., March 17, 2017, p. 65.

<sup>78</sup> U.S. Congress, Senate Committee on Commerce, Science, and Transportation, *Nomination Hearing for Wilbur Ross to be next Secretary of Commerce*, 115th Cong., January 5, 2017. For an overview of NAFTA, see CRS In Focus IF10047, *North American Free Trade Agreement (NAFTA)*, by M. Angeles Villarreal.

<sup>79</sup> CRS In Focus IF10120, *Transatlantic Trade and Investment Partnership (T-TIP)*, by Shayerah Ilias Akhtar and Vivian C. Jones.

food safety regulations, ISDS, and data privacy. Aspects of T-TIP also were controversial among U.S. stakeholders.

T-TIP negotiations are on pause, and the Trump Administration has stated that it is “currently evaluating the status of these negotiations.”<sup>80</sup> Brexit’s impact on T-TIP is an open question. Should the United States and the EU decide to resume T-TIP negotiations prior to the UK exiting the EU, the European Commission would continue negotiating the T-TIP on behalf of all 28 member states, including the UK. Some observers argue that Brexit creates greater uncertainty and is a major setback to the already difficult T-TIP negotiations, given the UK’s historically liberalizing role in the EU on trade issues.<sup>81</sup> Others argue that a U.S.-UK FTA could put pressure on the EU to reenergize T-TIP negotiations. After Brexit, the UK could seek to remain in the T-TIP negotiations or could join a T-TIP agreement, if concluded, to ensure reciprocal trade treatment among the United States, EU, and UK.

## Outlook

While U.S. and UK interest in negotiating a bilateral FTA is high, including on the part of the Administration and many Members of Congress, the Brexit process means that formal negotiations are at least two years off. In the meantime, the United States and UK can discuss an FTA informally, though such discussions may be constrained by uncertainty surrounding the status of the future UK-EU trade relationship, among other factors. Congress has an important role in examining a potential U.S.-UK trade agreement, U.S. trade negotiating priorities, and other issues through oversight of, and consultations with, the Trump Administration.

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<sup>80</sup> USTR, *2017 Trade Policy Agenda and 2016 Annual Report*, March 2017, p. 136.

<sup>81</sup> Victoria Guida and Adam Beshudi, “Brexit Kills Remaining Hope for TTIP Deal in 2016,” *POLITICO*, June 26, 2016.

## Fwd: SoS speech to AEI - final version

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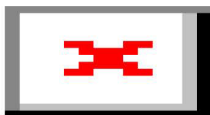
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The SoS' AEI speech is attached, for transmission to USTR.

Thanks,  
(b) (6)



(b) (6)  
Senior Private Secretary to the Rt Hon Dr Liam Fox  
MP  
Secretary of State and President of the Board of Trade  
(b) (6)  
(b) @trade.gsi.gov.uk

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**Speech to the American Enterprise Institute**

**Washington D.C.**

**Secretary of State for International Trade**

**24/07/17**

I would like to begin by thanking AEI and for hosting us today, and for the warm welcome we have had here in the US.

As the UK prepares to leave the European Union, Britain enters a new chapter in our history.

We will do so proudly championing the cause of global free trade, unashamedly promoting the importance of the rules-based system, and helping to ensure that the proceeds of prosperity are distributed to all.



This is a global responsibility, and not one that Britain can realise alone.

To achieve our ambition at home, we will seek a full and comprehensive trading relationship with our European neighbours, retaining the ties of commerce, standards and shared interests that have long united us.

Yet we will also set our sights wider, strengthening our ties with new friends and old allies alike, as we seek to build a truly global Britain.

As far as our own trading relationship with the EU goes, we begin from a mutually advantageous position.

Never before have two parties seeking a new trade agreement begun with the advantages of complete regulatory equivalence and a zero tariff environment.

Our challenge is not primarily economic, but practical.

At all stages, whether at the WTO in Geneva, ensuring the transitional adoption of existing EU agreements into UK law, or passing trade legislation through Parliament, we will strive to ensure stability, continuity, and no disruption to market access.

And throughout this process, our overriding aim is to provide maximum predictability and transparency not only to businesses and consumers alike, but to our international partners.

At the same time we must ensure that government works together with those in our economy that drive our prosperity.

This year marks two centuries since David Ricardo introduced his Theory of Comparative Advantage.

As everyone will know, the theory states that, if nations are allowed to engage in free and open trade, specialising in the export of certain goods and the import of others to meet their needs, then there is a mutual increase in economic welfare between nations, making those countries richer as a result.

It is one of the most powerful concepts in economics, described by the economist Paul Samuelson as the only proposition in all the social sciences that is both true and non-trivial and remains, to this day, the most fundamental justification of the power of free trade.

Since 1817, the world has changed beyond all recognition, yet the experiences of globalisation, and of technological advances unimaginable in Ricardo's time, have only served to validate his theory.

The principles of free and open trade have underpinned the multilateral institutions, rules and alliances that helped rebuild post-war Europe and the world beyond.

They helped usher the fall of communism and the tearing down of the Iron Curtain; they facilitated 70 years of global prosperity, and they have raised the living standards of hundreds of millions of people across the world.

Commercial liberalism imparts vast economic benefits, but there is also a robust moral case for promoting free trade which we must constantly reiterate.

As the world's developing and emerging economies have liberalised their trade practices, prosperity has spread across the globe, bringing industry, jobs and stability where once there was only poverty.

According to the World Bank, the three decades between 1981 and 2011 witnessed the single greatest decrease in material deprivation in human history – a truly remarkable achievement.

Take India as an example. In 1993, around 45% of India's population sat below the poverty line, as defined by the World Bank. In 2011 it was 22%.

It is no coincidence that in the intervening period India embraced globalisation and started to liberalise its economy.

It is hard to imagine an international aid programme, even one as generous as our own, that would, or could, have ever been as effective.

It is also, sadly, easy to find examples of where a lack of free trade has harmed the most vulnerable. If you want to see the contrasting results of

open and closed economies then look across from China to the Korean peninsula.

In 1945, both North and South Korea began from a very similar base, but while South Korea was more embracing of open trade and free markets, Pyongyang turned inwards with the tragic consequences for its citizens that we see to this day.

Seoul is now at the heart of a thriving economy and dynamic democracy where freedom and prosperity are shared among its people.

It should come as no surprise that while over 80% of South Koreans have access to the Internet, less than 0.1% of North Koreans enjoy the same. More tragically, there is a greater than 10 year discrepancy in the life expectancy of those North and South of the demilitarised zone.

For all its humanitarian benefits, the value of free trade also lies in its promotion of commercial, industrial and economic interests.

As Adam Smith famously observed, free trade appeals not to one's benevolence, but to the idea that prosperity is achieved when we are at liberty to pursue our own interests. It just so happens that we have many shared interests, ones sought by the UK and US alike.

It is perhaps a cliché for a British Secretary of State to come to the US and talk about the Special Relationship.

Yet the fact that a phrase is well-used does not make it any less true.

Britain and America are united by language, culture, history, defence, and of course commerce and trade.

It is perhaps fortuitous that we are also the world's first and fifth largest economies.

The economic value of our bond cannot be overstated.

The United States is Britain's largest export market, buying more than £150 billion of UK goods and services every year – more than France and Germany put together.

The stock of investment we hold in each other's economies currently stands at \$1 trillion. The US is the number one destination for UK investment – thousands of British firms have a presence in the US, from car companies to financial services.



US firms employ one million people in the UK and UK firms employ one million Americans here.

These companies see a familiar environment, built on economic fundamentals which allow businesses to flourish.

They are attracted by our low tax and low regulation economy; universities which sit alongside their American counterparts in all global top-ten lists; a highly skilled and educated workforce; and the ability to operate in the perfect time zone for global trading.

These fundamentals will not change; the UK will always be open for business.

In fact, the importance of this sentiment is embodied in the fact that one year ago, my Department for International Trade was founded to promote

Britain's exports abroad, attract inward investment, formulate trade policy, and protect our closest trading relationships.

Our task is to build a Britain that strengthens our commercial ties with friends and allies across the world, utilising Britain's newly independent trade policy to create new opportunities for British businesses.

Yet this will not come at the expense of our European partners.

Britain wants the EU to succeed. There will be no closing off of relations, economic or otherwise, and no abdication of our responsibilities. Continuity and stability will be our watchwords.

But any who are tempted to see our exit from the EU as evidence of Britain looking inwards should think again. We have just chosen another path – to embrace the wider horizons of a truly global Britain.

As we contemplate our new place in the world, we do so with a renewed confidence and optimism, acknowledging the vast opportunities that lie before us, especially when it comes to strengthening our connection with our single largest trading partner.

My department recognises how important our relationship with the USA is.

That is why we have established a US-UK Trade and Investment Working Group, dedicated to comprehensively strengthening our bilateral relationship.

As a priority, the Working Group will seek to provide stability, certainty and confidence for businesses on both sides of the Atlantic. Indeed, the first discussions will focus on providing commercial continuity as the UK leaves the EU.

But our ambitions are much wider. The Working Group is designed to provide a springboard, laying the groundwork for a comprehensive free trade agreement between our two nations post-Brexit – the start of a new and exciting chapter in our special relationship.

As well as strengthening our international relationship, DIT is also working to build upon the tens of thousands of local commercial ties that bind our two countries.

Tomorrow, I will launch a report that details the UK's trade and investment relationship with each of the 435 Congressional Districts within the United States.

The report will detail each district's goods and services trade flows with the UK, identify how many jobs are supported by these investments, and detail the top UK companies in each district.

For the first time, each Member of the House of Representatives will have a snapshot of the importance of UK trade to their district. Equally, we will be able to see where the opportunities lie to strengthen our existing partnerships or forge ahead with new, mutually beneficial, ones.

We believe that an open, free, and fair trading system is an unequivocal force for good.

But for the first time in decades, the established order of fair, free and open global commerce, which has done so much to enrich and empower the world's nations, is under threat.

In April, the World Trade Organisation noted that in 2016 world trade in goods grew by only 1.3% - the first time since 2001 that trade grew more slowly than GDP.

This threat to growth and prosperity is going largely unrecognised. Countries across the world, including the nations of the G7 and the G20, are allowing trade restrictive practices to establish themselves, limiting access to these leading economies for developed and developing nations alike.

Research by the OECD that shows that protectionist instincts have grown since the financial crisis of 2008. By 2010 G7 and G20 countries were estimated to be operating some 300 non-tariff barriers to trade – by 2015 this had mushroomed to over 1200.

This matters because the silting up of the global trading environment has implications beyond mere economics.

For the economic prosperity that a liberal trading system generated is a potent force for social stability.

That social stability underpins political stability, which in turn contributes to our collective security.

Prosperity, stability, and security form a continuum where one element cannot be interrupted without disrupting the whole.

Geopolitical stability is particularly important for countries, like the USA and the UK, with open economies and who hold large amounts of investments overseas.

We understand well that instability in any part of the global economy, whatever the cause, will ricochet across our interdependent, globalised world.

So what is to be done?

Firstly, we must lead by example, and work to encourage our trading partners across the world to support, and adhere to, the rules-based global trading system.

But such a system must ensure that rules are rigorously and effectively policed and enforced. Free trade is not a free for all.

Playing by the rules means taking firm action against illegal subsidies, structural overcapacities and dumping.

Trade remedy measures can be implemented at relatively short notice, and when used proportionally, can level the playing field, ensuring that global trade is fair as well as free.

It is worth remembering that these rules are not an external imposition on our economies, but were largely shaped and codified by the work of successive US and British governments.



In 1948, our nations were founding members of the General Agreement on Tariffs and Trade.

In 1986 it was the US, under President Reagan, that launched the Uruguay Round of multilateral negotiations that led to the establishment of the World Trade Organisation.

Today, the WTO continues to be a repository of those values of freedom and fairness in world trade.

Of course, the system that we established in 1995 may be in need of some refurbishment, as I said myself in Geneva last week, but that does not mean that we should abandon its principles and processes.

If the United States and the United Kingdom are to effectively rise to meet the economic challenges of the future, then, like the WTO, we too must prepare to for the new realities and demands of the global economy.

Conceptually, we need to re-evaluate some of our traditional institutional frameworks. In the face of the rapidly changing global economy, this means a re-assessment of the great 20<sup>th</sup> Century structure – the bloc.

The concept of geographical blocs for the purposes of defence still make sense, although greater flexibility and wider, more diverse global alliances will be necessary to navigate the multiplicity of the security elements of the globalised economy.

For trade, however, the case is less clear. The more mature an economy becomes, and the more it diversifies into services rather than goods, then the less value a geographically contiguous trade bloc has.

For the most advanced economies like the United States, or the UK, where almost 80% of our economic activity is services-based, we can afford to seek closer partnerships with those whose demands complement our output, not necessarily those who are geographically proximate.

As I have often said, if Francis Fukuyama had called his book 'the end of geography' not 'the end of history' it would have been much closer to describing the world in which we now find ourselves.

I am not by any means underplaying the importance of our trade in goods, especially for developing markets, but we also need to harness the speed and flexibility that the globalised world demands.

This requires the ability to sell more into the full range of global markets – developed and less developed, mature and maturing, even if they are further away.

We cannot forget, though, that free trade has the capacity to spread wealth to all nations – a rising tide of affluence that lifts all boats.

It is incumbent upon all developed nations to extend the benefits of free trade to emerging economies, and offer them a route to prosperity.

Those who have benefitted most from an open, liberal trading environment have a duty to ensure that others are able to take advantage of the same benefits in the future.

After all, such action is not simply altruistic. It develops the trade partners of the future, and allows developed nations to build links to those economies that will become the future drivers of global growth.

This principle underpins our pursuit of free trade.

If we are to continue to prosper in an age where knowledge and services are as economically important as oil, or cars, then we must work to build an international framework that keeps up with modern demands.

Over the past 70 years much work has been done by the United States, Britain, and our partners to abolish tariffs on the movement of goods.

All of us here today have witnessed the prosperity that this has created. It is time to realise those same benefits for our newest and most innovative industries.

Extending trading freedoms to our service sector means unlocking new, global markets for our tech companies, our finance industry, and the wider knowledge-based economy.

These are the areas in which advanced economies can continue to lead the world. We should ensure that we give our industries the right conditions to retain that competitive edge.

That is why the United Kingdom supports the conclusion of the Trade in Services Agreement, or TiSA, as soon as is practicable.

Fundamentally, it aims to bestow upon our newest industries those same freedoms that powered global growth in the last century.

It is about giving this generation the chance to match the success of the last.

I will say again that this is not to forget the contribution that manufacturing still brings to our respective economies, nor does it seek to duck the challenge of productivity, and the opportunities of automation.

It is an acceptance of the economic reality of today, and the trading potential that it brings.

We must never forget that trade underpins our prosperity. That prosperity underpins our security. And that security is the basis of our freedom.

I will leave you today with the words of President Reagan:

**“The freer the flow of world trade, the stronger the tides of human progress and peace among nations”**

There is no greater prize than that.

Thank you.

**END.**

## RE: US-UK Call on Friday

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**From:** (b) (6) (b) (6)@trade.gsi.gov.uk>  
**To:** "Wedding, Timothy J. EOP/USTR" <timothy\_j\_wedding@ustr.eop.gov>  
"Griffiths Oliver (Capability)" <(b) (6)@trade.gsi.gov.uk>, "Salt Richard (Trade)" <(b) (6)@trade.gsi.gov.uk>, "(b) (6) (Trade)" <(b) (6)@trade.gsi.gov.uk>, "(b) (6) (FCO Washington - Sensitive)" <(b) (6)@fco.gsi.gov.uk>, "(b) (6)@fco.gov.uk",  
**Cc:** (b) (6)@fco.gsi.gov.uk, "Mullaney, Dan D. EOP/USTR" <daniel\_mullaney@ustr.eop.gov>, "Weiner, David A. EOP/USTR" <david\_weiner@ustr.eop.gov>, "Rizzo, Sam R. EOP/USTR" <samuel\_r\_rizzo@ustr.eop.gov>, "Pavlovskis, Raimonds M. EOP/USTR" <raimonds.m.pavlovskis@ustr.eop.gov>  
**Date:** Thu, 31 Aug 2017 12:50:45 -0400

### Attachments

:

(b) (1) (A), (b) (1) (B)

Tim,

Many thanks for your suggested agenda for the call tomorrow – it lines up very closely with what we were thinking. We don't have any new areas to add but thought it might be helpful to specify a couple of points of detail under two of your headings (in red below) – do these work for you?

(b) (1) (A), (b) (1) (B)

Very many thanks,

(b) (6)

### Agenda

1. Continuity agreements
2. Short term outcomes
3. Other next steps following the July meetings for various groups (beyond #1 and #2)



- (b) (1) (A), (b) (1) (B)
  - (b) (1) (A), (b) (1) (B)
4. Calendar - next meetings/trips
    - Dan Mullaney UK visit
    - Next TIWG group (to include date and potential approach)
  5. Stakeholder outreach
  6. UK Brexit policy papers (b) (1) (A), (b) (1) (B)

Regards,

(b) (6)



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**From:** [Wedding, Timothy J. EOP/USTR](#)  
**Sent:** 30 August 2017 21:54  
**To:** [Griffiths Oliver \(Capability\)](#); [Salt Richard \(Trade\)](#); (b) (6) (FCO Washington - Sensitive); (b) (6) @fco.gov.uk  
**Cc:** [Mullaney, Dan D. EOP/USTR](#); [Weiner, David A. EOP/USTR](#); [Rizzo, Sam R. EOP/USTR](#); [Pavlovskis, Raimonds M. EOP/USTR](#)  
**Subject:** US-UK Call on Friday

Oliver and Richard,

Hope you both have had a good August! The weather has just turned cool here in Washington and you can feel fall starting to make its entrance.

For our call on Friday, I wanted to propose a simple agenda – lots of detail to discuss under each of these, but we can move efficiently through them. Please let me know if there are any additional topics you'd like to discuss:

1. Continuity agreements
2. Short term outcomes

3. Other next steps following the July meetings for various groups (beyond #1 and #2)
4. Calendar - next meetings/trips
5. Stakeholder outreach
6. UK Brexit policy papers (b) (1) (A), (b) (1) (B)

Best,  
Tim

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**[EXTERNAL] RE: Questions** (b) (1) (A), (b) (1) (B)

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**From:** (b) (6) @fco.gov.uk  
**To:** "Wedding, Timothy J. EOP/USTR" <timothy\_j\_wedding@ustr.eop.gov>  
**Cc:** "Savich, Silvia EOP/USTR" <silvia.savich@ustr.eop.gov>, (b) (6) @fco.gov.uk, (b) (6) @fco.gov.uk  
**Date:** Tue, 24 Apr 2018 08:17:03 -0400

Good Morning Tim,

Thank you so much for your responses. These are very helpful, I'll pass them onto colleagues in London and let you know if there are any questions!

Regards,

(b) (6)

(b) (6) | Trade Policy Analyst | British Embassy, 3100 Massachusetts Avenue NW, Washington DC 20008-3600 | Email: (b) (6) @fco.gov.uk | ☎: +1 (b) (6)

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**From:** Wedding, Timothy J. EOP/USTR [mailto:Timothy\_J\_Wedding@ustr.eop.gov]  
**Sent:** 23 April 2018 17:05  
**To:** (b) (6) (Sensitive) <(b) (6) @fco.gsi.gov.uk>  
**Cc:** Savich, Silvia EOP/USTR <Silvia.Savich@ustr.eop.gov>; (b) (6) (Sensitive) (b) (6) @fco.gsi.gov.uk; (b) (6) (Sensitive) (b) (6) @fco.gsi.gov.uk  
**Subject:** FW: Questions (b) (1) (A), (b) (1) (B)

(b) (6)

(b) (1) (A), (b) (1) (B)

Here are a few acronyms (which you probably know, but just in case):

TPA = Trade Promotion Authority (legislation that provides a vehicle for Congressional approval of certain trade agreements)

GSP = Generalized System of Preferences (a tariff preference program for developing countries)

USITC = U.S. International Trade Commission (an independent agencies that maintains the official tariff schedule, in addition to other functions)

Best,

Tim

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**From:** (b) (6) @fco.gov.uk (b) (6) @fco.gov.uk  
**Sent:** Thursday, April 19, 2018 4:39 PM  
**To:** Wedding, Timothy J. EOP/USTR <Timothy\_J\_Wedding@ustr.eop.gov>  
**Cc:** (b) (6) @fco.gov.uk (b) (6) @fco.gov.uk; Savich, Silvia EOP/USTR <Silvia.Savich@ustr.eop.gov>  
**Subject:** [EXTERNAL] Questions (b) (1) (A), (b) (1) (B)

Good Afternoon Tim,

Hope you are doing well after a busy March! We had a few conversations with colleagues in London this week regarding (b) (1) (A), (b) (1) (B)

[REDACTED]  
[REDACTED]  
[REDACTED] We had a few questions, and I wonder if you would be able to answer these or point us in the direction of someone who can?

The main questions are:

1. (b) (1) (A), (b) (1) (B)  
[REDACTED]  
[REDACTED]  
[REDACTED]  
[REDACTED]

A: (b) (1) (A), (b) (1) (B)  
[REDACTED]  
[REDACTED]  
[REDACTED]  
[REDACTED]  
[REDACTED]  
[REDACTED]  
[REDACTED]  
[REDACTED]  
[REDACTED]

2. (b) (1) (A), (b) (1) (B)  
[REDACTED]

A: (b) (1) (A), (b) (1) (B)  
[Redacted]

3. (b) (1) (A), (b) (1) (B)  
[Redacted]

A: (b) (1) (A), (b) (1) (B)  
[Redacted]

(b) (1) (A), (b) (1) (B)  
[Redacted]

Thanks so much for your assistance. Happy to call and explain some background on these questions or speak in more detail!

Regards,

(b)

(b) (6) | Trade Policy Analyst | British Embassy, 3100 Massachusetts Avenue NW, Washington DC  
20008-3600 | Email: (b) (6)@fco.gov.uk | ☎: +1 (b) (6)

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