

QUESTIONS AND ANSWERS ON

LABOUR AND BREXIT

1. **What is the latest state of play on the EU-UK Brexit negotiations?**

The summer has slipped by during which progress in the talks between Michel Barnier and David Frost on the relationship between the UK and the EU once the current transition period ends on 31st December 2020 have made little progress. The two major outstanding issues remain the same – fishing and the “level playing field”. If agreement could be reached on this second major issue it seems unlikely that fishing would be allowed to block an overall deal being reached, although this would cause a major upset in countries such as France and Spain. The really fundamental area of disagreement is on the extent to which the EU should be allowed to oversee and control UK policy on issues such as state aid once the UK is outside the Single Market and the Customs Union.

2. **What are the major “level playing field” issues?**

The EU’s stance on the level playing field issues is that if the UK is to have the benefit of low-friction access to the Single Market, it should be within a framework which will preclude the UK from securing unfair competitive advantages by adopting standards below those in the EU, or by using government subsidies to provide UK companies with unfair competitive advantages. The EU admits that it has not applied these tests when negotiating deals with countries such as Canada or Japan, but claims that the UK has to be an exception because of the scale of our trade with the EU generated by our proximity to the European market. The UK’s case is that there is no reason why the UK should be treated by the European Union any

differently from any other country which is outside the EU and that, as an independent nation, it is not appropriate for the EU to have legislative control through the European Court of Justice (ECJ) over whatever economic policies the UK decides to pursue. If the UK decides to adopt policies which are outside those generally accepted as being reasonable, the remedy which the EU should adopt ought to be for it to appeal against them through World Trade Organisation (WTO) dispute resolution procedures and not via the ECJ. The UK will have no representation on the ECJ once the transition period is over, opening up questions as to its impartiality and appropriateness to act in a judicial capacity.

3 **Is the EU's "level playing field" stance reasonable?**

There are other reasons too why the EU's level playing field stance is widely held by those taking a relatively dispassionate view to be unreasonable. The benefits from international trade do not depend on participants running their economies in similar ways. They depend on the comparative advantage which some countries have in producing particular goods, services and commodities compared to the production of other exports which different countries can produce more cheaply. The benefits to be secured by international trade do not therefore depend on level playing fields. Countries with very widely varying wage levels, industrial practices and regulations can trade with each other to their mutual benefit. This does not stop some countries trying to seize unfair advantages, for example by selling exports at below cost, and there needs to be an international mechanism to stop this happening. This needs to be done, however, through even-handed resolution disputes procedures between equally sovereign states, not by one country or union of countries having control over the economic policies of another.

4 **What about the balance of payments?**

There are also some highly material practical considerations. The UK has for many years had a very large balance of payments deficit with the EU. In 2019 it totalled £110bn, compared with a surplus of £27bn with the rest of the world. The resulting overall foreign payments deficit sustained by the UK has been hugely to our disadvantage. It has led to a combination of borrowing from abroad and net sales of UK assets on a scale which has topped a total of £1trn since 2000. The result has been both excessive debt and widespread loss of control by the UK of domestic assets as we have sold off huge quantities of properties, bonds and shares in UK companies, to finance a standard of living which we have not been earning. At some stage, possibly sooner rather than later in the light of the coronavirus crisis, the UK

may well want to take action to curtail these recurring deficits, perhaps by encouraging or at least acquiescing in a reduction in the international value of sterling. This could potentially have a much larger impact on our trade with the EU than any conceivable industrial interventions which recovery from Covid-19, in particular, might make necessary. If increased UK competitiveness is an eventuality which may well legitimately need to come to pass, it makes the current EU level playing field approach look doubly unfair and irrational.

5. **What seems likely to happen now?**

Faced with all these considerations, what is the UK government likely to do? At some stage in the near future it is going have to decide whether to acquiesce to the EU on the substance of their level playing field demands or to stand the UK's ground. If the UK negotiators stand firm, the EU may then make sufficient concessions to make a deal of some sort possible, but it is far from clear that this will happen. Time is running short and EU leaders at present have many other major preoccupations. It now seems very unlikely that there will be a draft agreement to be considered by a meeting of the European Council scheduled to take place on 15th and 16th October 2020. There might be a separate special Brexit leaders' summit allowing for agreement to be reached at a later date, possibly with a short extension beyond 31st December 2020. Clearly, however, time constraints are making it more difficult to get an agreement in place in sufficient time to be implemented by the end of this year.

6. **What will happen if there is no agreement?**

If there is no agreement on the outstanding issues, the fall-back position is that trade between the UK and the EU will revert to being on WTO terms. Trade will then be subject to WTO tariffs which are relatively low – averaging no more than about 2.5% on most industrial goods, but higher on some, such as vehicles and their components, and on agricultural products. Since EU countries sell a lot more to the UK than we do to them, the total value of tariffs collected by the UK on EU imports (around £13bn) will be significantly higher than those the EU collects on UK imports (approximately £6bn). Will there be a significant drop in UK-EU trade? This could happen from any one of three main reasons: additional costs because of tariffs; greater inconvenience and charges because of additional paperwork; and congestion at the ports. It seems unlikely that trade will be much reduced by a 2.5% tariff barrier which – as a point of reference – is less than the amount by which the pound had appreciated on the foreign exchanges over the last two months. The additional

paperwork required – mainly certificates of origin – will add only small additional charges, especially in relation to the costs of clearing through customs full lorry or container loads. Preparations for handling traffic on WTO terms are well advanced and, although there are bound to be some delays and disruption, they do not look likely to be all that great. Most of the trade done by the UK – with China, India, Australia and the USA, for example – is done on WTO terms without any major problems and, after what will probably be a short settling in period, there is no reason why the same will not happen again with the UK's trade with the EU.

7. **What is the final outcome likely to be?**

It is still uncertain, despite the current fraught stage of the negotiations, whether a deal will be done between the UK and the EU which maintains tariff- and quota-free trade between the UK beyond the end of 2020. Logically, there should be an agreement to secure this end if there is any merit in the arguments advanced by both the EU and the UK in favour of free trade agreements generally. From this standpoint, it makes no sense for the UK and the EU to erect even relatively small barriers to trade between themselves, while at the same time attempting to negotiate free trade deals with much more distant and less obvious partners. In EU affairs, however, politics usually trumps economics and, especially at a time when the benefits of globalisation are being questioned more vigorously than before, it is not clear that conventional economic logic will prevail. Both the UK and the EU have taken up relatively intransigent positions from which it is going to be difficult for either side to climb down. The UK negotiators in particular – backed by the outcome of the December 2019 general election - believe that on both fishing and the role of the UCI, right is on their side. Time is running very short, especially considering the relatively complicated and protracted affirmatory process which has to be undertaken to ratify any agreement which is made. All is complicated by the impact of the coronavirus pandemic, making it more difficult for meetings to be held at which negotiation progress can be made. All the same, the EU has a long tradition of taking difficult negotiations to the wire and coming to a deal at the last minute. This may well still be what happens again in this case