



**OFFICIAL REPORT**  
AITHISG OIFIGEIL

# Culture, Tourism, Europe and External Relations Committee

**Thursday 3 November 2016**

**Session 5**



The Scottish Parliament  
Pàrlamaid na h-Alba



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**CULTURE, TOURISM, EUROPE AND EXTERNAL RELATIONS COMMITTEE**  
**10<sup>th</sup> Meeting 2016, Session 5**

**CONVENER**

\*Joan McAlpine (South Scotland) (SNP)

**DEPUTY CONVENER**

\*Lewis Macdonald (North East Scotland) (Lab)

**COMMITTEE MEMBERS**

\*Jackson Carlaw (Eastwood) (Con)

\*Ross Greer (West Scotland) (Green)

\*Rachael Hamilton (South Scotland) (Con)

\*Emma Harper (South Scotland) (SNP)

\*Richard Lochhead (Moray) (SNP)

\*Stuart McMillan (Greenock and Inverclyde) (SNP)

\*Tavish Scott (Shetland Islands) (LD)

\*attended

**THE FOLLOWING ALSO PARTICIPATED:**

Dr Matias Margulis (University of Stirling)

Dr Gracia Marin-Duran (University of Edinburgh)

Professor Stephen Woolcock (London School of Economics)

Professor Ian Wooton (University of Strathclyde)

**CLERK TO THE COMMITTEE**

Katy Orr

**LOCATION**

The Adam Smith Room (CR5)



# Scottish Parliament

## Culture, Tourism, Europe and External Relations Committee

Thursday 3 November 2016

*[The Convener opened the meeting at 09:05]*

### European Union Referendum (Implications for Scotland)

**The Convener (Joan McAlpine):** Good morning and welcome to the 10th meeting in session 5 of the Culture, Tourism, Europe and External Relations Committee. I remind members and the public to turn off mobile phones. Members who use electronic devices to access papers during the meeting should ensure that they are switched to silent, please. No apologies have been received.

Our first item of business is an evidence session on the implications of the European Union referendum for Scotland. In this session, we will focus on future trading relationships.

I welcome to the meeting Professor Ian Wooton of the University of Strathclyde, Professor Stephen Woolcock of the London School of Economics, Dr Matias Margulis of the University of Stirling, and Dr Gracia Marin-Duran of the University of Edinburgh. I thank you all for attending the meeting.

I invite each of our witnesses to make short opening remarks. I emphasise that we are quite restricted for time on Thursday mornings, so the witnesses should keep their remarks as brief as possible.

Would Professor Wooton like to start?

**Professor Ian Wooton (University of Strathclyde):** Okay, convener.

I am delighted to have been invited to be a witness at the committee. However, I think that I share with the other witnesses the wish that we were meeting under different circumstances. I never thought that I would have to contemplate Brexit in my career. For the past 30 years, I have worked on aspects of international trade, and preferential trading agreements in particular. It is quite troubling that we are now at a stage at which we have to disassemble a trading agreement that has been very successful for the United Kingdom and Scotland for decades.

On alternatives, I was given a steer that one aspect that is of interest to the committee is the possibility of a reversion to the World Trade Organization and the relationships that we have

there. In my opening remarks, I want to speak about how that will not be a feasible alternative for us. The notion of the hardest form of Brexit will be quite troubling and very difficult for Scotland and the United Kingdom.

That said, the multilateral trading system, which was established as the general agreement on tariffs and trade system and evolved into the World Trade Organization system, has been enormously successful. It has been around since 1948 and has achieved a tremendous amount of success in opening up markets for virtually all countries in the world. To take an example, the United Kingdom has been a member since 1948. At the conclusion of the second world war, tariffs among the industrialised countries were in the order of 40 per cent, so there was a 40 per cent tax on every good that was traded internationally. Through the multiple rounds of multilateral negotiations that have taken place under the WTO and its GATT predecessor, the average tax is now in the order of 4 to 5 per cent. That is an absolutely enormous reduction. The United Kingdom's most-favoured nation WTO tariff on non-agricultural goods is 4.2 per cent, which is exactly the same as the European Union rate.

If we had a very hard Brexit and abandoned all the special trading agreements that we have with other countries—particularly the European Union—we would undoubtedly remain a member of the WTO. Some of the other witnesses will be able to discuss the details of our reverting to individual membership of the WTO rather than having membership as part of the European Union.

I do not think that continued membership has ever been in doubt, but I would like to argue that we cannot count on the WTO as being the agent of change that it has been for the past few decades.

When the World Trade Organization was started up, a relatively small number of countries were involved in negotiations and they picked the low-hanging fruit. They cut the tariffs that were relatively easy. In each successive round, they made quite substantial cuts. Those rounds, which happened every five or six years, were concluded relatively quickly. However, the last—the Uruguay round—which was in some respects the most challenging, took longer and made some quite significant changes, particularly for developing countries and the coverage of goods.

Since the conclusion of the Uruguay round, there have been 15 years of negotiations under the Doha development round, and almost everybody except those in Geneva is prepared to say that the multilateral negotiations are completely stuck and there is going to be no resolution in the near future.

As a country leaving Europe, we cannot look to the WTO to give us future trade deals. We have to consider deviations from the multilateral route. Despite the fact that we are breaking with the common market that we have with Europe, we are going to have to consider free-trade agreements with other countries, in particular those in Europe but also other important trading partners. This is not going to be a quick fix. The comprehensive economic and trade agreement took five years, and the Canada-US trade agreement took almost 100 years to get sorted. After the two years of article 50, it is going to take a very long time to sort things out.

**The Convener:** Thank you. As a matter of guidance, I suggest three or four minutes for introductory remarks.

**Professor Stephen Woolcock (London School of Economics):** I am very pleased to be here.

I agree with Professor Wooton that the WTO is a fairly poor alternative to preferential trade agreements, for the reasons that he specified. In other words, the WTO is not making any significant progress in addressing the barriers to trade that exist in the modern international economy.

I will spend a couple of minutes on what those barriers are. They are tariffs but, as Professor Wooton says, tariffs on non-agricultural products are pretty low. The trade-weighted average EU tariff is 2.9 per cent on manufactured goods and 22 per cent on agricultural products.

Border measures, not tariffs, are the real issue: the cost of shipping goods across borders, especially with global supply chains. Border measures are customs, rules of origin and checking that products comply with national safety rules. Non-tariff barriers, and their divergence from legitimate regulation of health, environment, consumer and prudential matters, are more important. They are the subject of international trade negotiations such as the transatlantic trade and investment partnership and CETA.

Non-tariff barriers are not adequately covered in the WTO, which is why we have seen the negotiation of the big preferential trade agreements. What the WTO offers is non-discrimination. It has what is called national treatment in most-favoured nation arrangements, which means that countries are not allowed to discriminate between suppliers or between products that are exported. In order to gain effective access to markets these days, however, you need more than that. You need positive action in the form of regulatory co-operation, mutual recognition, and some approximation of regulatory policies.

The single European market is the most advanced form of that approach, because it aims to facilitate trade while allowing the pursuit of legitimate policy objectives in the environment, health and safety, labour standards and so on. If you move out of that, you move into an area where UK and Scottish-based companies would be able to trade—people who talk about Brexit say, “You can always trade”, which is true—but at a disadvantage compared with your main international competitors.

09:15

**Dr Matias Margulis (University of Stirling):** First, I support the statements made by my two colleagues.

I want to highlight three key challenges at a very general level. First, all the Brexit trade options on the table for the UK are likely to leave the UK economically worse off and to result in lower standards of living for UK citizens in the short to medium term. Few countries have proposed policies to de-integrate their economies from the global economy in such a profound way and on purpose, as entailed by Brexit, and that presents policy makers with the dilemma of how to steer a situation in which thick webs of economic interconnections and interdependence that have taken decades to build up are supposed to be unravelled.

The second challenge is the complexity of the Brexit process in respect of the UK's renegotiation of its trade relationship with not only the EU but the rest of the world, and how that will work in practice. That matters not just to the UK's trading relationship with regard to its access to the EU; how Brexit is managed is very important to how the UK will trade with the rest of the world. Essentially, what we are talking about in the short to medium term is a renegotiation of the market access that the UK currently enjoys, not additional free-trade deals. Such a process would, as my colleague has just pointed out, normally take years if not decades, and I re-emphasise that this is just for the UK to achieve the market access that it currently enjoys and nothing in addition.

The third and final challenge is a more practical one about the UK Government's preparedness and capacity to meet the task ahead. As my colleague Dr Kristen Hopewell of the University of Edinburgh and I have previously stated, policy makers face a Herculean task. The UK has not negotiated its own trade deals since the 1970s, and, as with all areas of work, trade negotiations require know-how and experience to be successful. We know from research that countries with more trade negotiation expertise and experience secure better deals for their businesses and citizens than countries with less

negotiating capacity. That is the reason why the EU has been very successful at negotiating trade deals that serve its interest. Because the UK will be entering trade negotiations with the EU and other countries with far more capacity and experience, it will be at a disadvantage.

**Dr Gracia Marin-Duran (University of Edinburgh):** I am equally delighted to be a member of the panel, and I will be concentrating mainly on the legal issues that might arise with regard to the UK position in the WTO post Brexit. It is not that I disagree with anyone; I very much align myself with my co-panellist's statement that trading on WTO terms will leave the UK worse off than it would have been trading in the single market or under any preferential trade agreement. Clearly the purpose of having regional trade agreements is to have better terms of access than what we currently have under the WTO. In that sense, the European Union has, despite its problems, been the most successful attempt at regional economic integration that we have seen in the WTO.

However, I do not want to deal with the UK's trade policy options; instead, I want to look at the legal questions, and perhaps I should start by clarifying what, in my view, are and are not the legal issues.

The easiest part is what are not the legal issues. There has been a lot of talk in the press and elsewhere—it has almost become conventional wisdom—that once the UK leaves the EU, it will have to resume or renegotiate its membership of the WTO. I maintain that that is not correct. The UK was an original member of the WTO, is currently a member of the WTO and will remain a member of the WTO, independently of its legal EU membership, unless the UK is also planning to withdraw from the WTO, and I am not aware of such a plan.

There is a procedure to withdraw under article 15 of the WTO agreement. That procedure is much simpler than the article 50 procedure. However, as far as I know the UK Government has not communicated its intention to withdraw from the WTO. That means that the UK remains a member of the WTO and already has WTO rights and obligations—it is not like a new entrant or an acceding country. The substantial part of the WTO rights and obligations that are of general application to all members—non-discrimination, rules on technical regulations, rules on sanitary and phytosanitary measures, trade-related intellectual property rights, and the dispute settlement understanding, as my co-panellists mentioned—will continue to apply to the UK after Brexit, unless it decides to leave the WTO.

There are three qualifications to that statement, which are where the legal issues are and on which

I can elaborate. First, those rights and obligations that the UK has jointly committed to with the European Union—in other words, not the general rights and obligations that are applicable to all members but those that we call member-specific commitments—raise a legal question. In the case of the UK, those commitments have been agreed jointly with the European Union and the other 27 member states in the schedules of concessions. There is a legal question as to what happens to those. Does the UK need to negotiate a new schedule of concessions for goods and services or can it simply adopt the one that applies to the EU?

The second legal question is an exception to what I have just said and is the plurilateral agreement on Government procurement and the fact that only the EU is a party to the revised version of the 2014 WTO agreement—unlike with all the other WTO agreements, it is not the EU and its member states that have acceded to the agreement. By leaving the EU, the UK will no longer be bound by that agreement, unlike the other agreements. That does not mean that the UK cannot become a party to the agreement, but there is a legal issue there.

The third point that needs to be made is not so much a legal issue as one of clarification. Although I have said that for the most part the UK will retain the very same rights and obligations under the WTO that it currently has, once the UK leaves the EU—like my co-panellists, I am taking that as a fact although I am very sad about it—what will change in practice is that the exercise of those rights, and ensuring the performance of those obligations, will not be done by the EU on behalf of the UK as it is currently, but will be done by the UK itself.

We hardly see the EU member states in the WTO—it is the EU that exercises those rights and assumes responsibility for the performance of obligations, notably in the WTO dispute settlement. There will be practical challenges, rather than legal ones, in relation to how the UK takes up the role of exercising its rights and obligations under WTO law, including by participating in the WTO dispute settlement system. I can elaborate further on those points during the discussion if the committee is interested.

**The Convener:** I very much hope that we do not have to try to get our heads round an article 15 as well as an article 50—you have raised a frightening prospect.

Thank you for your contributions so far. I would like to drill down to a specific and contemporary issue. I seek your expert opinion on the letter that the UK Government has written to Nissan to secure the future of car manufacturing in Sunderland. Is it reasonable to assume that some

access to the single market and the customs union must have been guaranteed to Nissan?

**Dr Margulis:** The Nissan deal has been in the news quite a bit. At this point, the details of the deal are not known, but it has been suggested that part of the proposed package would be zero-tariff access for UK automobile exports to the EU. Under WTO law, such an arrangement is possible only under a comprehensive regional trade agreement—basically, under the single market. It is very unlikely that a one-off deal for the automobile sector would be WTO compliant.

**The Convener:** Does anyone else want to comment on that?

**Professor Wooton:** There is a precedent for such an arrangement in Canada, which is a common country of Matias Margulis and me. Canada and the United States had a free-trade agreement on automobiles—cars and trucks—that was deemed to be compliant with WTO rules, but that is something of an exception, and I very much doubt whether it would be supported nowadays.

The issue is that if a special deal appears to have been struck within the automotive sector, it will spill out to other manufacturers and, beyond that, to other industries. Frankly, I do not think that it will be sustainable.

**The Convener:** Do you agree that it suggests that the UK Government has told Nissan that the UK will remain within the customs union?

**Professor Woolcock:** I find it difficult to see how the UK can stay in the customs union, given how tied up the customs union is with membership of the EU. It is feasible, but it would mean, in effect, that the UK would have no independent trade policy, because it would simply follow the common external tariff of the EU. Such an arrangement would reduce the border costs, but I cannot see how, politically, it would be accepted by the EU.

Within the UK, that does not seem to square, politically, with the argument for leaving the EU, which, on trade at any rate, is to get an independent trade policy. In such an arrangement, the UK would have no independent trade policy. As part of a soft Brexit, it might be possible, but if we stayed part of the customs union, we would not be changing the status quo very much. We would solve various problems—for example, there would be no border controls and, although rules of origin might have to be proved, we would cut back on a lot of the trade costs associated with leaving the customs union—but we would more or less just be following EU policy without having any significant say in it.

**The Convener:** So if that is not feasible—

**Professor Woolcock:** It is feasible, but it does not seem to be very politically viable. My take on the Nissan situation is that what has been given is a commitment to negotiate, but what will happen depends on the person one is negotiating with—in other words, the other 27 member states.

09:30

**Professor Wooton:** Nissan is being guaranteed market access. That is not in the gift of the UK Government, but it is in the gift of Europe, after article 50 has been triggered and at the end of the negotiations. It is very difficult to imagine how the offer can be credible unless, behind it, there is some offsetting subsidy that would compensate for any tariffs that were left in place at the end of the negotiations.

**The Convener:** That would amount to millions of pounds, I would imagine.

**Professor Wooton:** Very much so.

**The Convener:** Other sectors will be looking for similar deals.

**Professor Wooton:** They will be lining up. It was an opportunistic thing to do, because of the fears of losing Nissan, but in the long run it could be extremely expensive for the UK Government.

**The Convener:** Last week, when the Secretary of State for Scotland was before the committee, he said that the UK was negotiating a “bespoke”—that seems to be the word of the moment—deal, with no tariffs and no barriers. Is that feasible?

**Professor Woolcock:** I will have a go at starting off a response to that. I have always thought that the most viable option would be a comprehensive free-trade agreement. That is probably what is meant by a bespoke deal. Under that, you could negotiate tariff-free access. As we have suggested, tariffs are not that high—they are not the main problem. You could maybe negotiate a mutual recognition agreement that would deal with some of the non-tariff barriers. If you look at the existing preferential agreements that are negotiated around the world, you can see what shape a bespoke agreement would be. It would be a form of comprehensive free-trade agreement.

**Lewis Macdonald (North East Scotland) (Lab):** I thank the witnesses for their interesting submissions. First, I will quickly respond to Professor Stephen Woolcock's comments. Membership of the customs union need not be the same as membership of the single market. The latter would clearly involve no independent decision making on a range of policy areas, whereas membership of the customs union—or a customs union with the customs union, which is an existing precedent—would not necessarily involve that, would it? That would remove trade flexibility



but it would not, for example, prevent the UK Government from having a different position on freedom of movement from the European single market.

**Professor Woolcock:** That is true—the UK would not have a separate tariff policy. My argument is that tariffs are not the main problem. Access to the rest of the European market is about differences in regulation. I would characterise the single market not simply as being the four freedoms, but as being full regulatory mutual recognition, which means that what is shipped here can be sold throughout the EU without any further checks or the need to prove compliance with EU regulations. That full recognition is far more important than tariffs. Tariffs are probably going to be negotiated away anyway through preferential trade agreements.

It is true that the UK could keep the customs union and that that would save some of the border costs; it would also maybe solve the problem in Northern Ireland. However, it would not provide equivalent market access to what has been negotiated in other agreements.

**Lewis Macdonald:** Keeping the customs union would meet what you speculated in relation to Nissan.

**Professor Woolcock:** No. You can negotiate tariff-free access in any free-trade agreement. However, Nissan also needs type approval, which means that a Nissan car produced here can be simply sold in the rest of Europe. Without that, the potential tariff-equivalent costs are anything up to—or even more than—20 per cent.

**Dr Marin-Duran:** I support the point that tariffs are not really the key issue. If we look at the more than 514 disputes we have had in the WTO since it was established in 1995, with the exception of agriculture, there have hardly been any disputes on tariffs. All the disputes have been on regulatory measures such as technical barriers to trade, and sanitary and phytosanitary measures. Disputes between WTO members are mainly on non-tariff barriers to trade.

**Lewis Macdonald:** The wider question that arises from Dr Marin-Duran's initial contribution is that of membership of the World Trade Organization. There are a range of options for the future UK relationship with the European Union, including membership of the European Economic Area, negotiation on the model of Switzerland or negotiation of a free-trade agreement. All of those involve the UK being a member, in its own right, of the WTO. Do they all involve the UK negotiating its own schedule of concessions in its own right, even if the UK remains within the single market through the EEA?

**Dr Marin-Duran:** That is one of the legal questions that arise. What happens to the schedules of concessions that are currently jointly binding on the European Union and the UK once the UK leaves the EU? You are right that that very much depends on what the EU-UK trade relationship is post Brexit. Clearly, if the UK remains part of the customs union—I agree that that is perhaps not very viable politically, but it is a legal option—it could keep the EU schedule of concessions because that would mean that, like Turkey, it would have to adopt the common tariff that is stipulated at EU level.

That said, there are two other aspects of the schedule of concessions that will nonetheless be tricky. One is whether the UK will keep the tariff-rate quotas currently applied by the EU, which are bound in part III of the schedule, as well as the right that it currently has to subsidise agricultural production up to a certain level, which is bound in part IV of that schedule. That goes beyond the issue of the common external tariff in itself, which is what the customs union sets. It says that all the members will keep the same common external tariff. That is dealt with in part I of the schedule, but it does not tell us much about what we are doing with the tariff-rate quotas and subsidies to agriculture, which are dealt with in parts III and IV of the schedule. Those issues, as well as the tariff, are open to question if, instead of the customs union, the UK-EU relationship post Brexit moves into other forms of regional integration, such as a free-trade agreement, in which the independent parties keep their right to set external tariffs, so those would not be harmonised. That becomes an issue.

We can talk only about legal options, because the WTO does not have a procedure—whoever claims the contrary is being inaccurate, legally speaking—on how to deal with the current situation of one member leaving a customs territory. The WTO has a procedure for how to deal with a customs territory enlarging, and it has done that through the successive EU enlargements, as new members have acceded to the EU. There is a procedure in article 24 for what needs to be done vis-à-vis other members.

However, there is no procedure for when one member of a customs territory decides to leave. There is no procedure for how we regulate that. There are two legal options. First, it could be argued that that member is modifying the schedule of concessions. That means that, if the UK decides to adopt a completely new trade regime from the one that is currently found at EU level, it will have to modify the schedule of concessions, which will clearly require a renegotiation, with all WTO members having a substantial interest in that new trade regime.

The second option is if the UK does not want to substantially modify or amend the current trade regime to which it is bound at EU level but simply to continue to apply it as the UK. If that is the policy option that the UK Government decides to go for—although, as I say, there is not a clear procedure—it may be that it could make the argument that that is not a modification of the schedule that requires renegotiation with all the other members but simply a rectification of the schedule. We have already heard UK Government officials trying to make that argument.

A rectification of a schedule means only a formal change because, in practice, the same concessions are being applied. It is just that it is not the EU applying them any more but the UK independently. The concessions remain the same. That does not involve renegotiating with the members; it involves notifying the WTO of the rectification and hoping that no member objects. If a member objects, it could always take the UK through the WTO dispute settlement system. That would be a simpler and faster procedure than the whole process of having to adopt an entirely new trade regime, with new tariffs and so on, and having to modify the schedule of concessions through negotiations with other members and compensatory adjustment. In that case, the UK would need to compensate the other members for any change that it wanted to make to the current EU-bound regime.

I hope that that answers your question.

**Lewis Macdonald:** It does. That is very helpful.

**Dr Margulis:** I just want to clarify that, the moment the UK leaves the single market, it has to adopt the schedules. As my colleague stated, that would involve negotiation not just with the EU but with the rest of the WTO.

It is really important to emphasise that those specific concessions—particularly on agricultural subsidies—are the most contentious issue at the WTO. That is the issue that has led to stalemate in negotiations at the WTO. Therefore, it is not some minor issue that the UK could hope to deal with under the radar. It is the number 1 issue, so the UK would require a lot of political good will from other members to entertain the idea of negotiating a favourable share of the EU's concessions. That is if the EU is willing to give that, because you cannot make the assumption that it would be willing to give the UK part of its concessions under the WTO. It is really important to remember that this is going to be extremely politically contentious—much more so than the EU negotiations themselves. I think that it is a much more difficult task than the actual EU negotiations.

**The Convener:** On that specific point, I take it that you are saying that it only takes one member

of the WTO to object for the whole thing to be held up for a long time.

**Dr Margulis:** Yes.

**The Convener:** Is it more likely that the WTO will give the EU concessions than the UK? Is it more likely to object to the UK?

**Dr Margulis:** The EU does not require any concessions—it can continue as is. It is up to the EU to decide whether it wants to give the UK any part of the concessions that it currently enjoys. For example, on levels of agricultural subsidies, it is up to the EU to decide how much of its current commitment it is willing to give to the UK. Then the rest of the members have to agree to accept that. They are very likely to ask for some sort of compensation or to make additional demands, because the UK will essentially be putting itself out there and will therefore be open to those kinds of demands. It cannot say no if countries say, “You must give us something”. If the UK wants to keep that part of the EU concessions, it will be obligated to do so.

**Emma Harper (South Scotland) (SNP):** This is quite complicated. You talk about tariffs not mattering except for agriculture. Scotland's food and drink industry was worth £14.2 billion this year and it is to be hoped that it will expand. However, much of our industry in food and drink is in agriculture and, in the south-west of Scotland in particular, it is in dairy. Our committee papers say that there would be tariffs of about 42 per cent on dairy products and 12 per cent on agricultural products. Could you help me understand a bit better what you are saying about agriculture and tariffs?

09:45

**Professor Woolcock:** I was talking in general terms about the trends in trade and the relative importance of tariffs. Tariffs in agriculture tend to be higher. The figure that I think you are looking at, which I quote in my paper, is the EU's common external tariff on agricultural products. That is potentially the tariff that agricultural exporters would face in exporting to the EU. The impact would be significant in certain sectors. You are quite right—we have to look at individual sectors in order to be able to assess the general impact.

**Professor Wooton:** If I may, I will give a little bit of historical context. Agriculture was part of the initial multilateral negotiations when the WTO was founded in 1948, but it was set aside. It was too contentious, so it did not feature in many of the negotiating rounds. The grand reductions of, on average, 30 per cent at the end of each round generally took place in relation to manufacturers. Agriculture was formally brought back into the WTO system only with the successful conclusion

of the Uruguay round, and we have not had a round of negotiations since then. Historically, agricultural tariffs have not had an opportunity to be brought down, and they are so tied to a nation's culture and environment that they remain a contentious area for negotiation.

**Professor Woolcock:** It is right to stress that agricultural tariffs are higher, but the non-tariff barriers in agriculture are equally important—what are called sanitary and phytosanitary measures. In other words, food safety and the regulation of food products are arguably more important in terms of access even than the tariffs. At present, the UK complies with all the European standards, so there is no barrier. However, if there is divergence from the European standards, there could be a progressive increase in the costs of complying with different SPS standards.

**Dr Marin-Duran:** I agree with everything that has been said so far about tariffs, but it has concerned mainly the UK being out of the single market and having to trade with the EU on a most-favoured nation basis. Another challenge for the UK is to access tariff-rate quotas that other countries have for the EU. For instance, the US has a quota with a preferential tariff for accessing EU cheese. Subject to EU and UK negotiations, that is something that the UK is likely to lose.

In other words, concessions have been made by others with regard to tariff-rate quotas for agriculture products, such as in the example of the US and EU cheese, and that has been done vis-à-vis the EU. If the UK leaves the EU, there is no reason why the US will need to continue to grant that preferential tariff to the UK, because it will no longer be a member of the EU, legally speaking. The UK could negotiate another preferential tariff-rate quota with the US but, even though the UK economy is considerable and it has weight economically, it clearly does not have the weight that the EU has when it negotiates with the US.

In considering how many concessions the UK will have to give other countries in order to keep what was agreed with the EU, and how far it is going to be able to do that, we need to bear in mind the size of the market. The WTO is about what you can get in exchange for what you can offer. Obviously, when you are negotiating as a trading bloc of 28 countries, what you can put on the table is more than you can when you are only one. That will be a practical challenge. As I say, it is a negotiation and not a legal problem, but it will be a practical challenge to negotiate as an individual country that has a market that is an important size but which is not equivalent to that of the EU 28.

**Rachael Hamilton (South Scotland) (Con):** We have high standards of food production in the UK. What makes you so sceptical that we would

not keep up those high standards of regulation? It could be one of our unique selling points when we look to negotiate with other countries.

**Professor Stephen Woolcock:** The UK Government has said that it will adopt all EU standards into UK legislation. At the moment, the standards are all the same high standards but one question in my mind is that there will still be a need for the UK to prove that in a way that it has not had to prove it in the past. In other words, other importers and other EU member states might say that they need more evidence that the UK is compliant.

If the UK keeps to the same standards, fine; nothing will change, that is true. However, it is a question of managing the divergence. Over time, the EU might introduce new standards. They might not be significantly higher but they might be different. If the standards or regulatory requirements are different, the UK will have to adapt to those and prove that it is adapting to them to ensure full access to the single market.

Let us take the famous chlorinated chicken example. EU rules say that you cannot use chlorinated wash to clean chicken carcasses. However, a lot of scientists say that that rule is not necessary. If the UK agricultural regulators say that it is not necessary and it is an additional cost for our farmers, we might not follow it. If that is the case, UK chicken exports would not be able to get into the EU market.

Another example is genetically modified crops. Will there be a divergence there? Will there be pressure to introduce more GM crops in the UK because they might be more efficient? If that is done, there will be difficulty with exporting a wide range of products into the EU market.

It is a question of how divergence is managed. It is clearly possible but it will require a procedural agreement between the UK and the EU.

**Dr Margulis:** I have two quick additional points to make about agriculture, because it is an exceptional sector. We have not discussed tariff-rate quotas related to imports. For example, much of the UK's sugar, which is used in confectionery, enters through tariff-rate quota arrangements, particularly with African and Caribbean countries. Should the UK leave the single market, it will disrupt those particular import TRQs and supply chains, which could be quite disruptive for existing supply chains for imports that go into the food and drink sector. That aspect needs to be further thought out.

We have also not talked about agricultural subsidies, which are quite important in the Scotland context because Scotland receives about one fifth of the UK's share of agricultural subsidies as part of the EU's commitment. For Scotland, the

question of agricultural subsidies, which provide a fairly high percentage of farmers' income, is particularly important and their importance to the Scottish economy and how tricky that negotiation will be with the EU and the rest of the WTO membership should not be understated.

**The Convener:** I go back to Ms Harper's point about dairy products. As Professor Woolcock rightly said, the 42 per cent tariff for dairy products applies to those who have favoured nation status if there is no trade agreement.

We have been told that Nissan has been assured that it will have full tariff-free access to EU markets. Would dairy producers have to negotiate? Would they be part of the deal that is negotiated between the UK and the EU? If not, they would end up paying a tariff of 42 per cent. Given that there is a glut of dairy products globally at the moment, how likely is it that that 42 per cent tariff would be negotiated away as part of a deal?

**Dr Margulis:** Dairy is a special case.

**Dr Gracia Marin-Duran:** It is difficult to say how likely that is, as it will be part of a broader package in the negotiations about the exit terms. I have not followed the political debate in this country closely enough but, as an outsider, I have some problem with the thinking that all you want to do is to maintain what you currently have in the EU, including the SPS standards. Most EU regulations in that area are about minimum standards so, under the current rules, you can have the EU standards or higher. Why would you want to be in the situation where you just copy and paste those standards without having any say in them? It is legally possible, but is it going to be politically feasible as part of the negotiations to get into a situation that is basically the same as now, yet without having a say over anything? It is difficult to believe that that will be acceptable. In particular, it is one thing to say that we are going to guarantee you the same access, but is the same access really guaranteed by agreeing to follow EU standards for ever without ever having a say on those standards?

**Richard Lochhead (Moray) (SNP):** I have two questions. The first is linked to the previous questions about food and drink. The Scotch Whisky Association is very relaxed about the possibility of additional tariffs or the possibility of being disadvantaged by the exit from the European Union. Does the panel believe that the association is correct to be so relaxed?

**Professor Wooton:** One of the reasons why it is so relaxed is that it already has very low tariffs for the major industrialised markets. There is already free-trade access for whisky into the United States and, currently, there is free-trade access into Europe. In effect, the industry will

retain its market access and I think that the opportunity that it would like to embrace is the possibility of the UK pursuing other free-trade agreements. We keep on hearing about Brazil, Russia, India and China—the BRIC countries—as potentially large markets that could be accessed through free-trade agreements and, under the status quo, there are high tariffs for whisky in those markets. Opportunistically, for the Scotch whisky industry, the threat of change through Brexit is not too substantial and there are opportunities for future deals that the industry could benefit from.

**Richard Lochhead:** My second question is about Nissan and the letter—the difficulty is that we do not know what is in the letter. Ironically, the French Government, which has a stake in Nissan, probably knows what is in the letter, but the Scottish Government does not. That says a lot about being kept in the loop regarding the UK's negotiating strategy.

When Stephen Woolcock was speaking about the issue earlier, he seemed to put a lot of emphasis on membership of the single market being more important than the customs union to the car industry. However, prior to the referendum this year, the UK Government tended to put the emphasis on the customs union, on the massive bureaucracy and cost of the rules of origin being implemented and so on.

I am trying to understand the relative importance of membership of the customs union and membership of the single market to the car industry, given that there are thousands of components in a car engine and that the rules of origin are implemented. I am trying to get to the bottom of what the UK offered Nissan to see off those threats.

10:00

**Professor Stephen Woolcock:** Again, that is a difficult question to answer.

The cost of not being part of a customs union, of proving rules of origin and border controls, depends a bit on what you negotiate. In other words, the WTO has a trade facilitation agreement, which aims to speed the flow of goods across borders. There are various techniques to do that, such as digital methods and pre-acceptance of export customs documents.

If the UK left the customs union, it could still negotiate a fairly advanced co-operation arrangement between UK customs authorities and the customs authorities in the EU that would reduce border costs so that, for example, trucks would not line up at the borders. Typically, the cost of proving conformance with rules of origin, border controls and the like can be 5 per cent of the

factory-gate costs, but those figures are a bit rough and ready. If the UK producers did not have full mutual recognition for the car sector, the cost could be greater. The estimates for the car sector in the transatlantic relationship show that a move towards approximation of car standards and regulatory requirements could provide significant savings. That would be one of the major benefits from a transatlantic agreement.

I am a bit reluctant to give specific figures, because specific figures do not really exist. The average figure for compliance with EU regulatory requirements in the car sector is about 20 per cent for manufactured goods. I still maintain that the cost of moving away from full mutual recognition could be potentially greater than the cost of leaving a customs union.

**Dr Margulis:** I want to reiterate that my earlier comment was that the idea of a sectoral stand-alone deal is unlikely when it comes to automobiles. It would have to be part of a much larger and more comprehensive package. A stand-alone car deal is not possible and a stand-alone dairy deal is not possible; a larger, comprehensive package is.

The other point that is probably not in the Nissan letter concerns compensation. The UK Government under WTO law would be prevented from providing direct compensation to Nissan. The idea of direct compensation to the industry is something that would be very difficult and would expose the UK to trade disputes.

**Jackson Carlaw (Eastwood) (Con):** I would like to pursue the Nissan point. I spent 25 years in the retail motor sector. Indeed, colleagues of mine left the business to found Nissan UK and the plant in Sunderland in the 1980s.

In my time in the retail and the broader automotive sector, I never found senior executives to be fools. These are international businesses and international businessmen, and they are capable of judging the value and worth of whatever they have on a piece of paper.

I was interested in Professor Wooton's comment that it was more likely to be a letter of intent than a letter of commitment, because a letter of commitment would contain things that would be either undeliverable or unsustainable. The letter is now another example of the great plethora of speculative areas that everyone is seeking to shed some light on. Is it not more likely that, at best, it can be a letter of intent setting out the Government's intended direction instead of some letter of commitment that, as I think several of you have suggested, might make commitments that would be legally or financially undeliverable? Given the intelligence that one presumes the companies have and the investment that they

have at stake, would they not be able to understand that and, therefore, be less impressed with something like that instead of something that sets out the direction of travel that the UK Government has indicated that it intends to pursue?

**Professor Wooton:** I think that it can be only a letter of intent. As we have not yet triggered article 50, the EU has not yet begun to reveal its hand and, at the moment, it is not clear whether the UK Government knows what is in its own hand. I think that this is a stop-gap measure. I am sure that the Government is very sincere in telling Nissan that it will do everything that it possibly can, but it would be unbelievable if the letter contained a firm commitment.

**Jackson Carlaw:** In effect, Nissan executives have made a judgment about that and have decided to pursue their investment.

**Professor Wooton:** I presume so.

**Dr Margulis:** I think that the investment will happen several years down the road when the details of Brexit are clear. Clearly, this is not an immediate decision to move ahead.

**Stuart McMillan (Greenock and Inverclyde) (SNP):** Good morning. The WTO has 164 members. With the UK needing to renegotiate the schedules, is there any possibility of other WTO members deciding that this would be an opportune moment to make things really difficult for the UK, either because of some economic advantage to them or because of some political advantage to be had in their own countries?

**Dr Marin-Duran:** The opportunity will certainly be taken to ask for concessions. That is always the case in a renegotiation; all the members involved are not going to agree to a change for free. The point is whether, legally speaking, the UK will have to renegotiate. That will clearly be the case if the UK Government decides to adopt a trade regime that is more restrictive than the one that we currently have with the EU; in that case, it will have to renegotiate its schedule.

On the other hand, the UK might want to adopt the same or a more liberal regime, and I should point out that nothing in WTO law prevents you from being more liberal than that to which you are bound. Either you respect what you are bound to or you can, in practice, have a more liberal trade policy than what you are bound to respect. However, you cannot have both. If you want to become more restrictive, you will have to renegotiate, which I think will be a challenge for the UK. First, the WTO now has 164 members, and it had fewer members when the original EU schedules were negotiated in 1994. Secondly, even though the UK is, in economic terms, an important member, it does not have the same

weight by itself as it has when it negotiates as part of a trading bloc. The concessions that you are likely to get in promising the other side access to the EU market as a whole as opposed to the UK market by itself might not be the same.

As I have said, that will be the case only if you seek to adopt a more restrictive trade regime. If you wanted to maintain the same EU trade regime or apply a more liberal approach, things could be easier. You could, for example, go down the road of rectification, by which I mean that the UK would say, "We're keeping this schedule as our own—we're not going to modify its substance." That approach would not require it to renegotiate with 164 members from the outset. However, it might be challenged later in the WTO dispute settlement process for going down that route. As I have said, the WTO does not have a clear procedure for a member that leaves a customs territory. It is a legal option, but there is no specific procedure for it. There is a possibility of other members challenging the UK later in the dispute settlement process and saying, "We object to your adopting the EU schedule as your own."

It is not clear yet that the UK would need to negotiate a new schedule from the outset with 164 members; that would be the case only if the UK Government decided that it wanted to adopt a more trade-restrictive regime. However, I hear that the UK Government wants to do the opposite and be more liberal than the EU currently is.

**Dr Margulis:** I have two points to add. It is a very astute observation that there would be a lot of potential economic and political incentives for other WTO members to seek additional concessions from the UK. That would be logical given that the UK has very little leverage because it wants to renegotiate its current level of access and needs to give more to get what it currently enjoys. However, there are two broader issues at play. The first is that the WTO is an institution in political paralysis, which would affect whether its members wanted to deal with a UK issue or just kick it down the line. It is uncertain when the WTO members would get around to dealing with any renegotiated concessions for the UK; they might not be interested in doing that any time soon because it would just add more complexity.

The second issue is that what really matters for a country's negotiating position at the WTO is alliances and having allies in the room. However, in essence, what the UK has done is alienate its largest group of allies: the EU countries. The UK therefore cannot assume that it would have a lot of political good will across the broad membership of the WTO. There are many reasons why many countries—especially developing countries, which are the majority of WTO members—might have a lot of long-standing grievances against the UK.

The UK would not enter the WTO as a member with many friends and the ability to influence people—that context needs to be considered.

**Stuart McMillan:** After article 50 is triggered, we will have the two-year period. You said that the WTO is in paralysis, so what would happen with discussions between the UK and WTO members?

**Dr Margulis:** My understanding is that the UK would be unlikely to be able to start discussions with the WTO until after its new trading relationship with the EU was settled, so it would depend on whether that process took two years or longer. The UK might want to pursue a CETA-like model, but CETA negotiations took seven or eight years. There has just been agreement to move ahead on CETA, but the process is still not finished and the agreement needs ratification. If the UK followed the CETA model, the whole process could take a decade. There would be the time taken for the UK to renegotiate its terms of trade with the EU and then potentially many more years to renegotiate agreements with other countries—it would be a long-term game.

**Stuart McMillan:** What would happen to UK exports and imports?

**Dr Marin-Duran:** Legally speaking, for the WTO, if the UK does not communicate any change to its current schedule, the UK schedule remains the EU schedule. That is why I said that the UK would not be in the position of being a new entrant to the WTO. A new entrant to the WTO has nothing; it has no rights or obligations and needs to negotiate everything from scratch. That would not be the UK's position.

From the WTO's perspective, what is happening in Europe at the moment is an internal matter. Similarly, for the EU, what is happening in the UK is an internal matter until article 50 is triggered. As far as WTO members are concerned, until the UK notifies a change to the current schedule of commitments that it has jointly with the EU, that is the UK's schedule. Following the UK agreeing with the EU what it wanted to do with that schedule, the UK would have to communicate to the WTO that it wanted either a modification, if it wanted to change the trade regime completely, or a rectification. If that is not done by the UK, it remains bound by the EU schedule; it is not that the UK has no schedule. That is the difference between the UK and a country newly acceding to the WTO that has no schedule.

**The Convener:** Members and witnesses might wish to know that the High Court has just ruled that the UK Government has to consult Parliament before triggering article 50.

10:15

**Dr Margulis:** I have a quick point to add. Dealing with areas such as terrorism would be straightforward, but there would be issues with other commitments, such as agricultural subsidies. Once the UK has renegotiated its relationship and trading regime with the EU and has figured out what proportion of the EU subsidies it will maintain, it would still need to get that deal approved by other WTO members. Politically, there are lots of reasons why there could be uncertainty about whether the UK could provide certain programmes until it had the broad agreement of WTO members. That is an unknown.

**Dr Marin-Duran:** It is not clear. We are bound to a level up to which the EU can subsidise agricultural production, and—this might provide a little bit of flexibility in the negotiations between the UK and the EU—the EU is using only about 7 per cent of the aggregate support measurement to which it is bound at the WTO. There is still a margin for the UK to get a share above that 7 per cent level.

So long as you are not going to change or go above the maximum level, it is not clear whether you need the consent of other WTO members. Their consent is clearly needed when you are trying to change or go above the concessions; you cannot do that alone. If you try to remain at the same level or apply anything below the level that you are bound to, it is not clear whether you need other members' consent. Again, how far you need to go with the WTO all depends on what is negotiated with the EU and what the exit terms are.

**Ross Greer (West Scotland) (Green):** I was going to ask about timescales, but Stuart McMillan's questions have covered that area quite fully.

There are pretty fundamental issues, in that, two years from next spring, we will find ourselves outwith the European Union but only beginning the process of negotiating new trade agreements. CETA and TTIP have been mentioned. CETA took seven years to negotiate and almost fell at the final hurdle; TTIP looks to be dead in the water, but it has taken about the same amount of time to fall. That presents huge issues for us moving forward.

To complicate the matter further, there are significantly different political and economic desires in the UK about what the relationship with the EU should be. Are differentiated agreements possible? In other words, is it possible for Scotland to retain closer relations with the rest of Europe? Could Scotland be in the EEA, with the rest of the UK not in the EEA?

**Professor Wooton:** That is a huge question to ask so late on in our discussion. It very much depends. Given the structure of the negotiations, it is unclear whether the UK Government will afford us such a possibility.

On a fundamental level, our exit from the EU as the whole of the UK will inevitably involve some form of border. Essentially, with the single market, we have been borderless, and what you are raising is the location of that border. It is a fascinating question, but this is uncharted territory—unless any of my fellow panellists have an insight into the matter. The question exercises me, but at present I have no answers.

**Professor Woolcock:** From a Brussels point of view, the EU has exclusive competence over trade. I am not sure whether Ross Greer is talking about after or before the UK leaves the EU, or before the article 50 process is completed—if we go into an article 50 process. However, there is no way that any part of the EU can negotiate a trade agreement because the EU has exclusive competence over most aspects of international trade.

There is scope for Scotland or any other region to promote its own economy only in areas where there is no exclusive competence, such as trade promotion or investment promotion. There is no scope to conclude specific agreements. Subsequent to the UK leaving the EU, it would be a question of who had competence for negotiating international trade agreements and whether that would be Scotland or the UK.

**Lewis Macdonald:** I want to go back to Dr Margulis's point that a stand-alone car deal is not possible, although he noted that there was a stand-alone car deal within WTO rules between the US and Canada some years ago. I take it that the matter is one for political judgment rather than there being a legal prohibition.

**Dr Margulis:** It is a combination of both. Professor Wooton referred to the US-Canada auto pact, which is a unique and very old agreement from the 1960s. Historically, because of its role in the global economy and global politics, the US has always been able to get special deals in the GATT international trade system. However, it is important to note that the UK is not the US: it does not have that kind of special significance to the global trading economy and is not such a significant player. There is a political dimension to the matter, but legally there cannot be special sectoral deals unless they are under a comprehensive trade agreement. There must be both.

**Lewis Macdonald:** So the point is that there is a clear legal prohibition.

**Dr Marin-Duran:** Yes. The WTO rule is that, when a free-trade agreement is being entered into,

the requirements of article XXIV of the GATT must be satisfied. That requires a free-trade agreement to be negotiated that covers “substantially all the trade” between the parties. No matter how big one sector is, I do not think that in most instances its trade will qualify as being equivalent to “substantially all the trade”, which means around 80 or 90 per cent of the trade between the parties that are entering the agreement. Unless that one sector covers 80 or 90 per cent of the party’s trade with the other party, the WTO rules will be infringed.

**The Convener:** I know that CETA is considered to be one of the most comprehensive free-trade agreements ever to be negotiated, but our briefing shows that a number of exceptions are involved. It does not cover financial services, and tariffs are applied to pork and beef after 50,000 tonnes have been exported. It is clear that even the most comprehensive free-trade agreement is not nearly as comprehensive as single market membership.

**Professor Wooton:** I am not a legal expert, but there seems to be a degree of flexibility in article XXIV. As Dr Marin-Duran has said, a free-trade agreement has to cover “substantially all the trade”, but that gives some wiggle room, of course. As far as I am aware, none of the free-trade agreements that have gone through—the WTO has accepted hundreds of them—has been turned down on the basis of article XXIV. That includes the European free-trade area, which was only for manufacturing when it was established and excluded agriculture and fisheries. On whether we can go back to the days of the Canada-US auto pact and say, “Oh, well, if it works for Canada and the United States, Nissan can get the same deal”, I think that that is probably pushing things too far. In the practical application of the rule, there is room to interpret the word “substantially”, but I do not think the car industry will be enough.

**Dr Marin-Duran:** There are two issues. The phrase “substantially all the trade” gives some flexibility, but if we look at the practice of the WTO, we see that the risk of being challenged in terms of a dispute settlement because the free-trade agreement is not compliant with article XXIV is very small. We do not know what “substantially all the trade” means, because that has never been interpreted. WTO members do not challenge one another on the compliance of their regional trade agreements, because they are all involved in them. If you challenge me and there is a clear interpretation of what “substantially all the trade” means, I will then challenge you. There has been political pragmatism in avoiding direct challenges to regional trade agreements in the WTO. We do not know whether there has been compliance. Agreements have not been challenged.

**The Convener:** That is all very interesting.

Thank you very much for your contributions. We could have gone on longer, but we are over our time already, unfortunately. Thank you very much for coming to give evidence.

*Meeting closed at 10:25.*



This is the final edition of the *Official Report* of this meeting. It is part of the Scottish Parliament *Official Report* archive and has been sent for legal deposit.

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Published in Edinburgh by the Scottish Parliamentary Corporate Body, the Scottish Parliament, Edinburgh, EH99 1SP

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