CULTURE, TOURISM, EUROPE AND EXTERNAL AFFAIRS COMMITTEE

INQUIRY ON THE NEGOTIATION OF THE FUTURE RELATIONSHIP BETWEEN THE EUROPEAN UNION AND THE UK GOVERNMENT

SUBMISSION FROM PROFESSOR SARAH HALL

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The evidence responds to the issues raised by the Committee with a particular focus on the services sector.

Extending the transition period

1. The UK’s economy has been shaped in profound ways by the membership of the EU’s single market. Whilst much of the public attention has focused on manufacturing, for good reasons, it is important to fully consider the implications of extending the transition period or not for the services sector. The UK is predominately a services economy. Services contribute around 81% of the economy and employ around 30 Million people or around 84% of jobs.¹

2. The end of the transition period will bring significant changes to the services sector. For some activities, such as financial services, the impact will be felt most acutely in terms of the lack of single market access. For example, it is estimated that just over a quarter of this sector’s activity currently stems from EU related business.²

3. Other parts of the services sector rely heavily on migrants from the EU in terms of labour markets including in financial services, education, the health service and road haulage. The end of free movement will mean that these labour market requirements will need to be met through the government’s proposed new immigration regime. For some services, the proposed salary threshold proposed of £25,600 for migrants coming to the UK is unlikely to pose a significant barrier to entry – though employers will still have to go through the bureaucracy of applying for visas and there will be significant costs to pay that do not apply not to EEA nationals coming to work in the UK now. However, close to 80% of works in the hotel and restaurant sector and over 50% of those in the leisure sector earn less than £400 per week and hence may not be allowed to come and work in the UK.

4. Some services businesses have begun to plan for the UK’s economic future outside of the EU. For example, in financial services, companies have begun to transfer assets and/or employees to European hubs including Frankfurt, Dublin, Luxembourg, Amsterdam and Paris in order to maintain single market access. Estimates suggest that over 320 firms may have already undertaken relocations of some kind to date.¹

¹ https://www.ons.gov.uk/economy/grossvalueaddedgva/datasets/nominalandrealregionalgrossvalueaddedbalancedbyindustry
5. There are significant and diverse implications for service sector businesses of leaving the single market including: greater barriers to single market access for exports; regulatory issues such as the likely requirements for permits in haulage; possible additional costs for the creative industries of accessing EU markets for live events; and greater administration for selling UK TV programming into the EU to name but a few. Responding to these changes will require time and planning. Given the considerable economic contraction that the UK economy is currently undergoing following COVID-19 there is a clear economic rationale to extend the transition period to give more time for services business to plan for the UK’s future outside of the single market.

**Leaving transition with a deal**

6. The UK is seeking a Comprehensive Free Trade Agreement (FTA) with the EU. For the services sector, it is important to note that FTAs typically do not assist trade to the same extent as they do for goods.

7. The UK’s negotiating position is based on the EU-Canada Comprehensive Economic and Trade Agreement (CETA). CETA goes further on assisting services trade than is typical in FTAs but does not replicate single market access. For example, government analysis undertaken in 2018 estimated that the value of services trade from the UK could decline by 8% without a deal and by 5% under a typical FTA.³

8. Whilst the UK’s position is based on CETA, in some areas, it asks for greater single market access than CETA does. Academic research shows that economic trade is typically greater between geographically close trading partners such as the UK and the EU. This gives rise to EU concerns that the CETA deal may not be appropriate for its relationship with the UK because the UK could seek to obtain competitive advantage by de-regulating compared to the EU, for instance by lower reporting standards or using tax policy to attract international services investment. If a large and geographically close competitor to the EU does that, while retaining relatively easy access to the single market, it could make it harder for the EU to compete internationally whilst maintaining its own rules. This could leave to difficulties in agreeing the draft deal as set out by the UK.

9. In the services sector, there are also differences between the UK and the EU on the sectoral coverage of any deal. For example, the UK wants to include audio-visual services including the Television and film sectors but the EU does not include these typically in its FTAs.

10. The areas where the UK is seeking more to support services trade include on the mutual recognition of qualifications such as for lawyers and architects and on the ways in which financial services trade will be facilitated (discussed in more detail below).

11. At the same time as seeking greater market access in these areas than is typical in EU FTAs, the government is seeking to preserve its own regulatory autonomy,

allowing the possibility of significant divergence. This is in stark contrast to service sector regulatory alignment that underpins the EU’s single market in services. It is not yet clear whether there are any areas where the UK would be prepared to accept greater regulatory alignment in return for securing greater market access to the single market.

Leaving with or without a deal

Below, I set out what the UK is seeking in three key service areas, how this compares to existing EU FTAs, notably the EU’s deal with Canada and what the implications could be at the end of a transition, if a deal is made and under a no deal end to transition.

Financial services

12. The UK’s financial service sector relies on the single market for the current size and shape of its EU exports. Single market access is currently facilitated through what are known as passporting arrangements between the UK and EU member states. Passporting means that a financial services firm authorized to undertake activity by the regulatory of one EU member state can apply for a passport that allows it to conduct the same business throughout the EU/EEA without the need for further authorization. Using passporting arrangements, it is estimated that 67% of UK financial services (not including insurance) supplied to the EU are delivered cross border from a UK base.4

13. Whilst passporting has continued during the transition period, it will end at the end of transition. The UK’s draft agreement text follows CETA and seeks to allow the cross border supply of financial services between the UK and the EU. This may appear to be the same as current passporting arrangements. However, it is important to note that CETA does not match current passporting arrangements. It is usually interpreted as relating to only a limited types of financial services including particular aspects of insurance e.g. maritime, certain banking activities and portfolio management.

14. CETA also includes a most favoured nation (MFN) clause (and the UK’s draft text includes the provision for the UK to include the same). The fact that this is in CETA is likely to limit the degree of bespoke single market access the UK may be able to negotiate since if the EU offered the UK a more favourable deal, it would have to offer this to Canada alongside other countries with whom it has trade deals including an MFN provision.

15. CETA relies on equivalence decisions in the place of passporting and the same approach is developed in the UK’s draft agreement. These legal provisions enable financial firms outside the EU to conduct business within the single market and/or with EU counterparts without being subject to EU regulation in addition to their home country regulation, provided that the EU determines that the legal and regulatory system of the third country is deemed ‘equivalent’. However, equivalence does not provide the same breadth of market access across the same number of services as

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passporting. For example, core banking services such as lending and deposit taking typically cannot secure single market access through equivalence.\textsuperscript{5}

16. Equivalence also provides much less certainty because the EU can revoke its decision to grant equivalence with only 30 days notice. To try to overcome this, the UK draft agreement text seeks ‘transparency and appropriate consultation in the process of adoption, suspension and withdrawal of equivalence decisions’ (p170) in order to provide UK financial services firms with more certainty about what type of EU market access they will have.

17. Beyond the question of equivalence and passporting, there are a number of areas where the UK’s draft text goes beyond the market access provided for in CETA in small but important ways. For example, the UK’s draft agreement seeks to essentially future proof the definition of what counts as a financial services supplier by including individuals or business who supply or ‘wish to’ supply financial services. The draft is also seeking greater collaboration on things like consumer protection through ‘innovation’ in financial services. Both of these differences might be read as an attempt to ensure that the fintech sector, which the UK has developed global leadership in, is protect by the proposed UK deal.

18. The UK draft is seeking the establishment of a Financial Services Committee that would meet once a quarter to oversee the implementation of the agreement. The importance the UK attaches to financial services is reflected in the fact that the equivalent committee under CETA usually meets once a year.

19. The UK is therefore seeking a slightly modified version of CETA in financial services. However, crucially it wants to secure this enhanced degree of market access without the level of regulatory alignment that would be typical of EU enhanced market access. This reflects the government’s position that given the unique size and importance of financial services in the UK, it should not become a ‘rule taker’ from Brussels.

20. The Centre for Economic and Business Research (CEBR) estimated that leaving the single market with no, or only modest trading agreements in place beyond WTO terms would lead to export losses of around 15% in financial services.\textsuperscript{6} Depending on the extent to which these are replaced by new trade relationships, this could lead to a decline in GDP of between 1.4 to 2%. Some of this could be reversed if additional trade deals and relationships are established between the UK and countries outside of the EU.

\textit{Mutual recognition of professional qualifications and business travel in the services sector}

21. An important aspect of the negotiations for services relates to the rules governing who is able to travel between the UK and the EU to provide services. At the moment it is relatively easy to travel to do business in another member state, and UK professional qualifications, such as those needed to practice as a lawyer or an

\footnotesize{\textsuperscript{5} https://www.bba.org.uk/wp-content/uploads/2016/12/webversion-BQB-4-1.pdf
\textsuperscript{6} https://cebr.com/reports/the-economic-impact-on-services-from-the-uk-losing-single-market-access/}
architect, are recognised throughout the EU. This is called the mutual recognition of professional qualifications.

22. This is an important issue for business services, the largest form of UK-EU services trade, and most especially those that are reliant on what are called regulated professions. A regulated profession is one in which an individual is not authorised to provide the service in a particular country until they have met the regulatory requirements of that country to do so. This includes lawyers, accountants and architects, who are typically allowed to practice and use a professional title once they have undertaken approved education and training. This system of authorisation is typically nationally based so someone trained and qualified in one country cannot automatically practice in another. The process is usually managed by a trade association or a professional body which makes implementation of any changes as a result of the negotiations harder than if it was a government run process.

23. The UK negotiating document is ambitious in this area going beyond other FTAs and CETA. The position set out by the UK takes mutual recognition as the default (ie a continuation of the current single market access) and outlines a framework to facilitate this. In contrast, in CETA a framework is set out to work towards mutual recognition where it has been recommended by a Joint Committee on Mutual Recognition established by that agreement.

24. The EU’s position is rather different. In a notice to stakeholders, the EU Commission has stated that:

“The recognition of professional qualifications of United Kingdom nationals in an EU 27 Member State will be governed by the national policies and rules of that Member State, irrespective of whether the qualifications of the United Kingdom national were obtained in the United Kingdom, in another third country or in an EU-27 Member State”  

25. The non-recognition of UK qualifications would not just apply to UK citizens – it would also apply to EU citizens who hold a UK qualification and are working in other EU countries.

26. Legal services illustrate how the risks of not securing an agreement in this area might work out in practice. Currently solicitors have the right to be recognised as lawyers by other European bars, they have the protection of legal professional privilege (LPP) when advising clients in the EU and they have the right to represent clients at the Court of Justice of the European Union. This is reciprocated with the UK’s automatic recognition of other European bars, enabling the UK’s legal sector to recruit lawyers from across the continent. Moreover, a UK limited liability partnership (LLP) can open branches within member states France. However, without a new agreement, this would not be the case in all member states. For example, UK LLPs

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would not automatically be recognised as a legal form in France, which requires 75% of partners holding 75% of shares to be fully admitted to an EU/EEA/Swiss bar.  

27. For some services, such as management consultancy, professional qualifications are less significant, but easy and frequent access to clients within the single market is important. Currently, such travel involves very little in the way of paperwork and fees. However, at the end of the transition period, if no deal is agreed, businesses could be faced with having to navigate the range of visa requirements and associated fees required by member states.

28. The UK is seeking to address this by including short term business trips and people moving between their firms’ office for short periods of time, known as intra-company transferees, within the agreement.

29. The UK’s draft agreement aims for individuals to be able to travel between the EU and the UK, and stay on a temporary basis in order to deliver services. Here the UK is following both CETA and the EU-Japan EPA which have gone much further than other FTAs in this area. For example, the draft calls for the requirements for visas to be dropped for short term business visitors. It also follows CETA in proposing that entry be granted for the families and dependents of service providers themselves. If this is agreed this will assist the range of individuals, from professional musicians, to management consultants and financiers who travel frequently between the UK and EU member states to provide services on a ‘fly-in-fly-out basis’, though this will still fall short of the ease of movement they currently enjoy.

30. Without an agreement there could be significant disruption to this mode of cross border service supply. In this scenario, individuals planning to travel from the UK to the EU will also need to consider any changes needed to the paperwork required to take equipment with them at the end of the transition period. For example, the Chief Executive of UK Music cautioned that the additional challenges associated with travel to the EU if a trade deal was not struck could lead to touring artists cancelling performances.

Audiovisual

31. The audio visual sector (including film, TV and TV related businesses) is one of the services sectors where the EU and the UK appear farthest apart. In common with its other FTAs, the EU is proposing that the sector would be excluded from any deal with the UK. Meanwhile, the UK has included the sector in its draft agreement.

32. The UK’s aim of including the sector within the negotiations reflects the fact that the UK has the largest audiovisual sector in Europe. Its GVA in 2014 was 20 percent

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10 https://www.theguardian.com/politics/2019/oct/03/no-deal-brexit-may-make-touring-europe-simply-unviable-for-uk-artists
larger than Germany’s and 50 percent larger than France’s.\textsuperscript{11} It is particularly developed in Video on demand services (VoD), with 31 percent of the total EU market by value and 29 percent of subscribers. The sector employs over 200,000 people in the UK and has a £1.3 billion trade surplus with the EU.\textsuperscript{12} The UK hosts three of the top ten broadcasters in the EU (Sky, BBC, ITV). In addition to television, the UK is a strong player in the European feature film sector. It ranks number two (after France) for the number of film exports in cinemas and on TV, and number one for the film exports on VoD. EU countries’ markets account for a quarter of UK-origin films’ worldwide theatrical admissions.

33. The UK’s audiovisual sector has successfully exported into the EU through the use of two main regulations. First, the Audiovisual Media Services Directive (AVMSD) is based on the principle of ‘country of origin’ and essentially means that a UK broadcasting license issued by Ofcom to a UK channel allows that channel to broadcast throughout the EU without needing to comply with any additional regulations in these export markets. The advantages for providers are that they only need to comply with Ofcom rules in order to provide audiovisual services in any EU member state. The UK draft agreement sets out a process through which Ofcom, as the UK’s regulator could be authorized by the EU ‘without undue delay’ such that a broadcasting licence issued by Ofcom would continue to be recognized within the EU’s single market.

34. Without an agreement in this area, at the end of the transition period, the UK becomes a third-country, which means Ofcom will no longer be recognised under the AVMSD. As a result, the cost and complexity of exporting to the EU will increase as broadcasters and providers of video on demand services will need to ensure they meet the regulatory requirements to broadcast in their target export market.

35. The second piece of regulation is the Council of Europe’s European Convention on Transfrontier Television (ECTT) which came into force in 1993. This convention guarantees that programming can be shared cross border via terrestrial, satellite and cable services but it does not include on demand – which didn’t exist in any meaningful way in 1993. As a signatory to the Convention, at the end of the transition period, the UK will still have the right to broadcast to the other 20 member states who have ratified it, but not through on demand services. This is important because the Country of Origin principle has made the UK an attractive location for the headquarters of global broadcasters who use this base to produce on demand content for the EU.

36. In theory, the ECTT would mean that UK audiovisual services would maintain market access to at least the majority of EU member states at the end of the transition period. This is because the AVMSD also insists on quota provisions to promote content produced in Europe or ‘European works’. These provisions envisage that a majority proportion of broadcasting time will be dedicated to European works (excluding the time apportioned to news, sports and advertising). The AVMSD defines European works as originating in an EU Member State or a European State which has


signed the ECTT. This means that content produced in the UK will still be classed as a European work when the transition period ends.

37. However, if the UK seeks to use the ECTT as a fall-back, it is limited in a number of ways. First, it does include every Member State. Belgium, Ireland and Denmark did not sign the Convention and Greece, Luxembourg, the Netherlands and Sweden have not ratified it. Second, VoD services are excluded from the scope of the ECTT. Given this is the medium that has the highest potential for growth, this is a major drawback for relying on the ECTT. Third, there is no enforcement mechanism in place for the ECTT.

Summary

38. The services sector is strategically important in the UK economy and needs to be considered in the negotiations because of the ways it is shaped by UK single market access.

39. At the end of the transition period, with or without a deal of the kind being sought by the UK, the services sector is likely to be smaller and differently structured with implications for wider economic growth.

40. For some areas, such as financial services, the impact on their EU markets could be such that it makes more sense trends already underway to move parts of their business to European financial centres such as Dublin and Paris to intensify in order to maintain market access. For other sectors that rely on low waged EU labour, such as food businesses and hotels, the end of the transition period could bring with it labour shortages as EU nationals are unable to travel to the EU to work because they do not meet the salary threshold set out in the government’s post Brexit migration regime.

50. In some ways, the UK’s draft agreement mirrors FTAs already agreed with the EU. However, this does not make EU agreement guaranteed. There are significant differences between the size and scope of UK-EU trade as compared to that with Canada which will understandably make the EU cautious in replicating Canadian agreements with such a close and large trading partner.

51. In other areas, such as professional services like law and architecture the UK is asking for more access to the single market than the EU has granted other countries. However, even in these areas, it is important to note that this does not replicate the UK current trading relationship with the EU. This has led some to argue, such as parts of the City of London, that there could be advantages in seeking complete regulatory control without any preferential single market access as would be expected within a FTA.

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1 With regard to the estimate referred to in my written submission concerning the number of financial services firms, the estimate comes from a report by New Financial called Brexit and the City. They updated this in October 2019 to suggest that the figure could by that point 330 firms. The moves they are counting are either employees or assets. Because firms typically do not want to share this kind of information about their corporate strategy in a competitive market, this report suggests that this figure could be an under estimate.
This has impacted Scottish based businesses. I've provided details of two of the most notable below:

1. **Standard Life Aberdeen** has opened a portfolio management and distribution service in Dublin to service clients in the EU 27. This can be understood as a response to the end of passporting and the end of single market access that will bring for financial firms. Opening within the EU27 makes sense in terms of maintaining that market access. They have also expanded the size of their Luxembourg office.

2. **Royal Bank of Scotland** began operating a banking entity in the Netherlands, based in Amsterdam in March 2019. They are using this to serve from of their non UK EEA customers. They use this as a base for a network of branches (in London, Dublin, Frankfurt, Madrid, Milan, Paris and Stockholm). They have also established Natwest Bank Branch in Frankfurt to support Euro Payments and Euro Liquidity through the Bundesbank.