Engineering and Machinery Alliance

EAMA evidence to the **UK-EU trading relationship inquiry of the International Trade Committee**

The Engineering and Machinery Alliance comprises ten lead trade associations, serving the machinery and component supply chain. Our member firms manufacture, supply can support essential machinery to customers across the economy and are much involved in exporting and importing from the EU and around the world. EAMA is represented on the Department for International Trade's Automotive, Aerospace and Marine Trade Advisory Group.

The responses here relate only to the business impacts to firms represented by EAMA.

Key points

- The TCA has weakened the business model of the UK being a European hub for a) manufacturing and b) goods distribution. This will influence investment for years to come.
- The net result so far of the TCA and UK regulatory reform so far has been to increase the "red tape" burden on UK businesses.
- Government is undermining exports through poor post-TCA administration in some areas.
- Proposals for regulatory divergence must be fully assessed with industry for business impact.
- Uncertainty about our future relationship is unwelcome.
- We support calls for greater discussion of trade and regulatory policy.
- The TCA, and other trade developments, strengthen the case greater government support for the advanced engineering sector.

1. What has been the experience of businesses and other stakeholders in the UK regarding implementation of the trade provisions in the UK-EU Trade and Co-operation Agreement?

1 EAMA's trade associations have heard of a range of experiences from their members, some positive, most negative, with some unaffected.

2 Plusses for UK firms include a surge in enquiries in the early months of 2021 from UK businesses that had hitherto been buying from European engineering and manufacturing suppliers. The change was due to transport problems and the new complexities of the TCA. At a gathering of members of one of EAMA's member trade associations, several members commented that Brexit had turned out to be "one of the best things ever".

3 The UK General Tariff has reduced certain input costs for UK firms, where supplies are bought outside Europe. This may help some firms to decide to remain in the UK, which might otherwise have relocated.

4 We anticipate hearing detail, in early 2022, about the potential impact of freeports; at the same time as noting the Office of Budget Responsibility's (OBR) view that while there may be some movement of businesses, there will be little net gain to the UK economy.

5 We have heard of UK distribution operations being opened where the UK was previously served directly from the continent, and there has been some on-shoring, also called reshoring, of manufacturing to serve UK customers. These examples are in addition to a broader trend towards reshoring, some of which may prove to be short-term, that has resulted from global supply chain disruptions and changes due to the coronavirus pandemic.

6 For most companies, the overall experience of Brexit has been negative. Reflecting on the prime minister's statement on Christmas Eve, 2020, it is true that the UK regained sovereignty on matters including immigration and regulation. However, several of the PM's assertions have proved unfounded:

- If there has not been a "palisade of tariffs on Jan 1", then there is at least an administrative obstacle course of barriers to be negotiated to take advantage of tariff-free access;
- The claim that there would be no non-tariff barriers to trade has proved to be untrue, in the movement of both goods and support engineers;
- It was "a deal which will if anything should [sic] allow our companies and our exporters to do even more business with our European friends". This cannot be so, unless compared with no trade deal; at any rate trade with the EU has fallen sharply.

7 By creating both tariff and non-tariff barriers to trade in goods, and professional support services, the TCA has weakened the business model of the UK being a European hub for a) manufacturing and b) goods distribution. The "UK and Europe" and "UK & Ireland" models are being rethought. Firms have had to open European manufacturing and distribution operations previously served from the UK, adding to cost. Migration of business from the UK has taken place and more engineering and distribution activities will move to the EU.

8 Dominic Raab, as foreign secretary, suggested that the UK should "bank the baseline of our trade" with the EU (and look to grow elsewhere, including Indo-Pacific. (Source: http://news.bbc.co.uk/1/shared/bsp/hi/pdfs/14022101.pdf) This looks unachievable. More likely, our EU trade will diminish and that is borne out by 2021 trade statistics.

9 UK manufacturing subsidiaries of global companies, supplying Europe, are dismissive of the government's idea that they can compensate by expanding exports to the Indo-Pacific region. Their parent companies already have facilities in Indo-Pacific serving that region.

10 The extent and the speed of change created problems for all businesses, especially SMEs. Guidance, available on gov.uk, tells firms what the rules are (although not always clearly). This guidance falls well short of advice as to what firms need to do and should do, however. The normal phase-in period for advice from trade associations and others, and for decision-making, was greatly curtailed. Covid added to practical difficulties.

11 Firms that exported only to Europe became exporters for the first time, in terms of the realities of business processes and customer relations; as is true of continental and Irish suppliers which sold only within the EU.

12 Rules of Origin: Exporters in both directions had to demonstrate that they met the TCA's content rules to ship tariff-free. For firms used to shipping outside the EU, this was straightforward; for many others, it was a new and complex challenge. The delay in requiring the appropriate paperwork for imports was helpful, but some firms may now be exposed to tax back-claims. Some tariff-exempt goods were shipped tariff-paid, to ensure compliance, and firms are now seeking tariff refunds – for which there is a process.

13 Transport difficulties early in 2021 were expected, and stocks were built in late-2020. But importers and exporters had insufficient support from freight forwarders. Firms gave insufficient attention to Incoterms. Exported machines and components got lost for as long as six-to-eight weeks. The UK arm of well-known carriers seemed to be better prepared than continental subsidiaries of the same organisation.

14 Customs officials were ill-prepared – assuming they were not simply obstructive. Most complaints related to the performance of German customs. We had reports of German customs failing to recognise that some UK EORI numbers closely resembled VAT numbers, due to the way they had been allocated by HMRC, as late as mid-February.

15 By spring 2021, EAMA member firms were mostly much more comfortable with transport arrangements to and from Europe, although others said problems persisted, either with the forwarder or at customs.

16 The UK government has been ill-prepared for the impact of the TCA. One example is the lack of support for traders. The Export Academy, long mooted and launched in May 2018, ahead of the Export Strategy of that year, had made little impact when the revised Export Strategy re-launched the Export Academy in November 2021. The creation of Export Support Service in autumn 2021 with a focus on exporting to the EU, is an implicit, late recognition of the scale of the task being faced by companies.

17 Poor UK government processes threaten certain activities. For example, UK firms have an excellent reputation within the EU for servicing and calibrating advanced equipment. We are world leaders in this area thanks to our technical expertise and competitiveness in both price and turnaround times. Devices are shipped to the UK by the customer, usually via fast parcel services, go through a servicing or calibration procedure, and are then shipped back to the customer. This process has become more burdensome for the customer, to the extent that EU suppliers may be a more convenient option, because of our inward and outward processing systems for VAT; even if the UK firms do most of the customs work on behalf of their customers. Service and calibration work is already being lost; and as these support services are often an important element of the original sale, export sales of equipment are also at risk.

18 Because we are no longer in the EU, we have an opportunity to change our processes. HMRC must work with industry to introduce new, more efficient systems whilst finding a balance between the trade benefits and fiscal risks to the exchequer for high volume, low revenue per item work. We are a smart nation, full of smart people - we can do better.

19 While we are waiting for HMRC to amend its processes, the fast parcel operators must be encouraged to update their systems so that those sending goods to the UK can provide the necessary information to allow UK companies to use the current inward processing and outward VAT processing facilities.

20 EAMA exporters have experienced long delays in the Export Control Joint Unit's (ECJU) processing of export licence applications for military, dual use or other sensitive goods and technology exports. They attribute the delays, at least in part, to the ECJU taking insufficient account of the fact that, for the first time, exports to the EU came within scope. There appears to be an acute shortage of experienced staff to review applications, particularly within the Ministry of Defence. The ECJU's target for granting or rejecting licence applications is two weeks, but firms report waiting for up to six months. Firms have lost not only specific orders but also suffered reputational damage, undermining their export potential. Firms understand the need for an export licensing system but maintain that it must work efficiently, to support UK technology, jobs, exports and influence.

21 It is no longer straightforward for qualified engineers to travel to Europe to support customers. Understanding the new rules as to what work can be undertaken in each country is an additional burden on business and makes the provision of essential product support more difficult for UK firms.

22 Rules for Northern Ireland created problems from the start and continue to do so. Britain has left the EU Single Market, but Northern Ireland has left the UK Single Market.

23 EU business sentiment towards the UK has caused concern. There has been a cooling towards UK firms among some potential suppliers and potential customers, which goes beyond the new regulatory demands. Ministers must be mindful of the impact on business sentiment in Europe of the tone they adopt, as they take forward negotiations with the EU.

Regulatory divergence and change

24 In his statement on December 24th 2020, the PM said that the TCA would create mutually beneficial regulatory competition between the UK and the EU. The extent to which the UK will diverge from EU regulations has become a new, resource-intensive area of work. It is important for EAMA's trade associations to keep abreast of government intentions and actions, so that they can contribute to policy development and inform members.

25 Processes for engagement with the UK government on regulatory developments leading to divergence are still bedding in. We can see no government-wide standard approach.

26 EAMA member firms have as yet shown little enthusiasm for regulatory divergence, due to the potential for damaging commercial impacts on UK firms' businesses. That is not to say that there is no positive scope for the UK to innovate. The UK has played a leading role in helping to shape current EU regulations affecting EAMA members and, potentially, will have much to offer in future, including in areas of new and green technology. Government must, however, have a clear view of the costs and benefits to UK business and engage fully with the sectors concerned. EAMA trade associations can contribute much to such a dialogue.

27 The introduction of the UKCA mark provides an example of the pitfalls of rapid, unforced regulatory change which can be costly to businesses. The December 31st 2021 deadline was shown to be unworkable and a further stay granted, rather late, in September 2021. The failure to win a mutual

recognition agreement with the EU is disappointing, if unsurprising. Detailed guidance on UKCA was slow and still incomplete by the end of 2021. Meanwhile, many firms remain unclear as to the purpose of the UKCA regulations.

2. **How effectively is the UK-EU trade relationship being managed through the mechanisms under the Agreement, including the Partnership Council and the bodies that sit beneath it?**

28 Michel Barnier described the TCA as "a barebones agreement", which seems about right. A year on from signing, there is little flesh on the bones. There has been little progress thus far, it seems, beyond discussion of procedure. Lord Frost noted that building our new relationship will be a "long term task". Whether the TCA will endure is questioned.

29 We are heartened that the UK government appears still to be monitoring developments in Brussels in the machinery sector, as this will strengthen the positive regulatory competition referred to by the PM.

3. **What impact is the Agreement having, and what might be its future impact, on the UK's wider trade policy – including in relation to trade with non-EU countries?**

30 EAMA welcomes the finding of the National Audit Office, in its report on progress in UK trade negotiations, that "there is now an opportunity for DIT to set out in one place how international trade will support the UK's domestic and wider policy objectives and provide greater clarity to the public and stakeholders". Lord Frost has, since his resignation, called for wider debate and we support that.

31 The TCA is signed but far from settled, the Northern Ireland Protocol is in dispute and there is a vigorous debate within the Conservative Party as to future policy. All this creates uncertainty for business. The NIP disagreement is reported, by the Financial Times, to be adversely affecting trade talks with the US, whose tariffs on UK steel remain in place, to the detriment of British exporters, jobs and tax revenues. (See, for example: https://www.bbc.co.uk/news/business-59857275)

32 The UK and the EU appear often to be running on parallel tracks, seeking trade deals with the US, or with India, or on digital trade and green technologies. It may be that the UK has the potential to do deals more quickly than the EU and to drop tariffs more quickly, although it is as yet unclear the extent to which they will be to the benefit of UK firms.

33 We hope to understand better, not least from government, the extent of opportunities for trade deals outside Europe, especially in Indo-Pacific and in areas such as digital; and how these will conflict with opportunities in the EU.

4. **How is implementation of the Agreement, along with the wider UK-EU trade relationship, likely to evolve**

34 Firms have little idea on this issue. Implementation of the NIP remains a point of dispute with no obvious resolution in sight. Lord Frost said (September 2021) that it has the potential to poison the whole UK-EU relationship. At Christmas 2021, it has led to the EU freezing the participation of the UK in Horizon Europe, terms for which had been agreed. As above, progress at the Partnership Council is at best slow. The UK's position on issues from Data Adequacy to the revised EU Machinery Directive are unclear.

35 The OBR said in October 2021 that its prediction of a 15% reduction in trade intensity to and from the EU has proved accurate, and that may fall further as more trade barriers were still to be introduced. We agree when it says that "the full effect of the referendum outcome and higher trade barriers will probably take several years to come through, with businesses needing considerable time to adjust". The initial impact of Brexit on UK trade with the EU - Office for Budget Responsibility (obr.uk).

36 The OBR predicts a "long-term reduction in UK productivity [i.e. growth] of 4%". This is twice as great as its estimate of the scarring of the economy from the Covid pandemic. The 4% figure may rise further, depending on how the TCA develops, the OBR says – and as Lord Frost suggested, progress so far is not encouraging. This merits more debate.

37 The evolution of our trading relationship depends on at least three factors. Firstly, finding a resolution to the NIP disagreement, which has fostered what Lord Frost called a "cold mistrust" (autumn 2021).

38 Secondly, the attitude of the UK towards the EU, Northern Ireland aside. Lord Frost said (in autumn 2021) that disagreement over the NIP had held back what he saw as "the potential for a new era of cooperation between like-minded states in a world which needs us to work together effectively". We would like greater understanding of what he had in mind. Lord Frost's departure from government does nothing to change the fundamental issues.

39 There are evident disagreements within government as to the pace and extent to which we should reform the economy, including diverging from the EU (also para 32) and no debate that might lead to cross-party consensus that might provide some consistency, should the government change. EAMA would like to see constructive co-operation between the UK and Europe, and to see us doing more than simply banking – to use Raab's term - our current core business with the EU.

40 Thirdly, the approach and future of the EU itself, which has its own challenges of unity and agreement. In recent months the Commission appears to have turned away from excessive new regulation in the machinery sector, which is positive.

41 One concluding point. To achieve sustainable economic recovery, wealthy creation and a positive trading performance, the UK needs a healthier, growing advanced engineering and manufacturing sector. The TCA has been a step backward in achieving that, at a critical time of technological change, investment, supply chain re-alignment and protective domestic policies in world trade. The UK's potential is great but the risk is that we decline further. Government must step up its support in terms of skills, investment and opportunity.

Jack Semple
Director of Policy

12th January 2022