

**SMMT POSITION PAPER
UK-JAPAN TRADE NEGOTIATIONS**

JULY 2020

Introduction

1. The Society of Motor Manufacturers and Traders (SMMT) is one of the largest and most influential trade associations in the UK. SMMT is the voice of the UK motor industry, supporting and promoting its members' interests, at home and abroad, to government, stakeholders and the media. SMMT represents more than 700 automotive companies in the UK, providing them with a forum to voice their views on issues affecting the sector, helping to guide strategies and build positive relationships with government and regulatory authorities.
2. The automotive sector is a key driver of growth and prosperity across the UK. 168,000 people are employed directly in manufacturing and 823,000 across the wider automotive industry. More than 30 manufacturers build in excess of 70 models of vehicle in the UK supported by more than 2,400 component providers and some of the world's most skilled engineers. A major hub for digital innovation and technological advancement, UK automotive invests £3.75 billion each year in research and development and is one of the UK's most productive sectors.¹
3. In addition, the industry is a vital part of the UK economy accounting for more than £82 billion turnover and £18.6 billion value added. Automotive generates more than £100 billion in trade for the UK and is the UK's largest single exporter of goods, accounting for 13% of total goods exports.²
4. The UK has developed a long-standing trading and investment relationship with Japan since the early-1980s with many Japanese automotive investors choosing to make the UK their gateway into the European market. The UK's historically favourable business environment and the integration within the EU single market have been essential factors in attracting Japanese investment. With deep and historic bilateral ties, government must aim to secure and reinvigorate the British-Japanese automotive partnership which has been pivotal for the sector over the last 40 years.
5. The automotive industry supports the ambitions of the UK government to secure a free trade agreement with Japan, one which builds on the benefits agreed in the EU-Japan Economic Partnership Agreement (EPA). The EPA is by far the most robust trading agreement currently applicable on trade exchanges between the UK and Japan and includes a number of provisions which are beneficial to British automotive exporters that are not included in the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), such as a far-reaching automotive annex and measures allowing extended cumulation for key automotive parts.
6. The sector is pleased to see HM Government recognise the importance of pursuing negotiations on trade with Japan in a timely manner given the prominence of Japanese businesses within the UK economy and the need for business continuity. However, the UK automotive sector can only fully benefit from a new FTA with Japan if a deal between the EU and the UK is concluded before the end of the transition period. For this reason, it is critically important that UK-Japan negotiations take place alongside, and at pace with, UK-EU negotiations and with the aim that a future UK-Japan Agreement is not drastically different from the conditions currently in existence.
7. Whilst the UK-Japan relationship, which is built on a mutual commitment to trade and investment, needs to be sustained and strengthened, the priority must be securing an FTA with the EU. A close bilateral trading relationship with Japan alone cannot make up for the impact nor the loss of integration that would result from the UK exiting the EU without securing an ambitious deal with the sector's biggest trading partner and without replicating existing deals with other common preferential trading partners.

¹ SMMT Motor Industry Facts 2020, <https://www.smmt.co.uk/wp-content/uploads/sites/2/SMMT-Motor-Industry-Facts-JUNE-2020-FINAL.pdf>

² 2020 UK Automotive Trade Report, <https://www.smmt.co.uk/wp-content/uploads/sites/2/SMMT-Automotive-Trade-Report-2020.pdf>

Executive Summary

8. Several Japanese investors choose to base some of their European manufacturing operations in the UK, contributing significantly to the British automotive market, as well as employing a substantial percentage of the UK automotive workforce. Indeed, a significant portion of Japanese automotive investment is concentrated in the North East of England, supporting OEM manufacturers and their extensive supply chains, and subsequently contributing considerably to regional prosperity.
9. Japan is a hugely important global partner for the UK automotive industry. In 2019, more than 143,000 vehicles registered in the UK were imported from Japan, worth almost £1.5 billion. This represented an increase of 5.9% from 2018 and accounted for 3.5% of all UK imports and 6.2% of the entire UK market.
10. Whilst the UK has historically imported large volumes from Japan, recently it has become a major exporting market for UK passenger cars, with the growth thanks, in part, to an increasing appetite for the UK's premium, luxury and high performance models.
11. In total, more than 33,500 UK-built cars were exported to Japan in 2019, worth more than £1 billion and equating to 3.2% of total UK exports by volume. Japan is the UK's fourth largest export market for cars, after the EU, the U.S. and China. Before a minor slowdown in 2019, Japan held the distinction of being one of the fastest growing export destinations for UK cars, with a growth rate of 26% in 2018.³ In addition, 2018 ONS figures show that road vehicles are the highest-value export to Japan from England.⁴
12. Japan enjoys a significant trade surplus in bilateral exchanges of engines, parts and components. The UK imports £458 million worth of parts, accessories and components and £120 million worth of engines, 14.8% of all engine imports, from Japan. Exports of UK automotive parts, accessories and components to Japan represent £65 million. Exports of engines to Japan in 2019 were valued at £16 million. Imports of Japanese parts is a key driver of competitiveness, in particular for the highly integrated supply chain of Japanese investors manufacturing in the UK. However, UK suppliers are underperforming in terms of exports to Japan. A future trade deal should seek new opportunities for UK producers of parts and components.
13. With the UK-EU transition period ending on December 31 2020, the UK needs to approach trade talks with Japan by taking into consideration the complex interactions between a bilateral UK-Japan deal and its impact on the future trading relationship the UK has with the EU.
14. Agreeing an ambitious deal with the EU is an essential precondition to fully benefit from a bilateral agreement between the UK and Japan. In the absence of an ambitious deal with the EU, the value of an agreement between the UK and Japan risks being greatly diminished. Against this background, UK automotive supports the following priorities in UK-Japan trade negotiations:
 - i. Timing – The UK should aim to secure a trade deal with Japan before the end of the transition period. Negotiations with Japan should progress in parallel to negotiations with the EU, recognising the strategic importance and impact the future UK-EU agreement will have on elements of the UK's trade with other markets, including Japan.
 - ii. Tariffs – Duties should be progressively removed on all automotive products. UK automotive is keen to avoid any scenario where WTO tariffs would apply, such as would occur in the absence of a deal at the end of the transition period. Phase-out of

³ 2019 UK Automotive Trade Report

⁴ ONS Trade 2019

existing tariffs should continue according to the existing schedule without restarting from the base rate after the end of the transition period.

- iii. Regulatory barriers – The UK must prioritise maintaining key elements of the existing automotive annex in the EU-Japan EPA and possibly upgrading it where appropriate.
- iv. Rules of Origin – The UK should maintain existing EPA rules of origin for key inputs of production to provide business continuity. This could be instrumental to allow Japanese content assembled in UK vehicles to qualify for preferential treatment when shipped to the EU without altering the existing competitive conditions in trade across the Channel.
- v. Trade facilitation – UK and Japanese mutual recognition of Authorised Economic Operators (AEO's) must be guaranteed.
- vi. Investment - The automotive industry wishes to maintain the privileged position the UK currently enjoys for Japanese investment. A future UK-Japan trade agreement should therefore include investment protection clauses to help strengthen investor confidence.
- vii. Labour mobility – Automotive would welcome measures to further facilitate movement of personnel, professionals and business visitors.
- viii. Digital trade – Equivalent recognition of data protection systems and bilateral free flow of data should be maintained, while more ambitious commitments should be achieved on e-commerce and digital trade.

Automotive Priorities for UK – Japan trade Negotiations

Timing

- 14. Government should avoid a cliff-edge in the application of the EU-Japan EPA to the UK and ensure a smooth adjustment to a post-transition trade relationship between the UK and Japan by concluding in parallel an ambitious UK-EU FTA and a new UK-Japan FTA.
- 15. The absence of a UK-Japan FTA at the end of the transitional period would result in the reapplication of WTO tariffs on automotive products imported from Japan. These tariffs are currently being phased-out and a sudden reintroduction of import duties would significantly disrupt business planning and affect UK consumers and importers. A timely agreement on key elements of a UK-Japan FTA would also support a coherent and transparent approach to negotiations with the EU, in particular on issues such as rules of origin.
- 16. In consideration of the need to allow significant time for Japan's ratification procedures, the parties should focus on replicating the terms of the existing EPA and limit discussions on enhanced provisions where these would delay the conclusion of the negotiations.

Tariffs

- 17. Under an ambitious agreement, tariffs should be removed and national governments should seek greater collaboration to remove transactional costs hindering bilateral trade. Under a new UK-Japan FTA, progressive tariff liberalisation should continue without gaps. Annual tariff reductions should begin from the tariff level exacted on Japanese imports at the end of the UK's transition period with the EU. Tariffs should not revert to MFN duty levels at any point after the end of the transition period.
- 18. Negotiators should take into account the potential impact of tariff liberalisation on the UK economy, UK automotive manufacturing and negotiations with the EU. To ensure consistency

for both UK-based and Japanese-based businesses, parties should agree to continue liberalisation based on the agreed timeframe of the EU-Japan EPA phase-out schedule.

19. Any changes to the existing tariff staging should be considered with great caution. Faster liberalisation can be agreed exclusively with industry consent and only if compatible with future EU-UK cumulation arrangements. In this regard, the parties must maintain the same liberalisation schedule for Japanese parts and components incorporated in UK-assembled vehicles shipped to the EU. Liberalisation of finished vehicles should recognise the potential for negative impacts on UK jobs and output, as highlighted in government's own assessment, if not appropriately handled.
20. Government should also provide a robust safety net for UK automotive businesses which might be negatively affected by increased competition from Japanese imports. This could be achieved by establishing a UK support scheme similar to the EU Globalisation Adjustment Fund or the US Trade Adjustment Assistance programme. In consideration of the exceptional circumstances posed by the UK's withdrawal from the EU and of the potential incentive offered by a new bilateral FTA to direct exports from Japan, such schemes should be strengthened to provide employment protection as well as enhanced UK automotive business competitiveness.

Rules of origin

21. Future rules of origin in a UK-Japan FTA should ensure meaningful preferential market access to both parties. The parties should take into account their respective supplier bases and changes to current trade terms determined by the UK's withdrawal from the EU.
22. The EU-Japan EPA allows to cumulate content originating in Japan and the EU, as well as the value added in the territory of the parties on non-originating materials. Bilateral and full cumulation provisions should be fully replicated in the future UK-Japan FTA.
23. In order to preserve business continuity in bilateral trade between the UK and Japan, the possibility to cumulate EU originating content and EU value added on non-originating materials could also be maintained after the end of the transition period. If compatible with future cumulation arrangements between the UK and the EU, this can be achieved through the inclusion in the UK-Japan FTA of a specific clause providing extended cumulation of EU content. Given that Japan does not charge tariffs on all key automotive tariff lines, cumulation of EU content would help Japanese exporters avoid UK MFN tariffs even when incorporating a significant number of EU materials in their products.
24. Allowing cumulation of EU content could represent an important step towards the strategic target of creating a trilateral EU-UK-Japan cumulation zone for automotive inputs. However, this could be achieved only if other conditions are also met:
 - a. First, cumulation of Japanese content in trade between the UK and the EU cannot happen in the absence of a UK-Japan deal. Having FTAs in place between all parties is an essential pre-condition of any cumulation arrangement between the EU, the UK and common preferential trading partners, further underscoring the importance of securing an ambitious and comprehensive agreements between all interested parties before the end of the transition period.
 - b. Second, the UK and Japan should agree to maintaining **identical rules of origin for key parts and components**. This would be a fundamental step forward to ensure the compatibility of the EU-Japan EPA and the UK-Japan FTA's protocols on rules of origin.
25. Any changes to existing rules of origin applicable to automotive products should be discussed with the industry and limited to products not used as input of production by UK manufacturers.

Regulation

26. The parties should replicate existing commitments enshrined in the “Annex on Motor Vehicles and Parts” to the EU-Japan EPA. The absence of a replication of the Annex would detract a future UK-Japan EPA of any meaningful benefit for UK automotive exporters, given that Japan does not charge tariffs on automotive imports.
27. Potentially, the implementation of the Annex allows significant cost reductions on bilateral automotive exchanges by eliminating testing, documentation, certification or marking requirements on all automotive products covered by the list of regulations which are currently applied by both parties according to the Annex. The mutual recognition of automotive regulations would also deliver a large gain for UK automotive companies. In 2018, a UK government-commissioned impact analysis of the EU-Japan EPA estimated that UK exporters of motor vehicle stood to gain between £0.3 and £0.8 billion from the reduction of non-tariff barriers (NTBs) in Japan. According to the same study, Japanese exporters stood to gain between £0.7 and £2 billion from the reduction of UK NTBs⁵.
28. The Annex included in the EU-Japan EPA allows marketing of type-approved vehicles without additional checks for products covered under UN regulations applied by both parties. This facilitation must be fully replicated in the future UK-Japan FTA.
29. Without prejudice to a timely ratification of the deal before the end of the transitional period, the UK and Japan could consider upgrading the Automotive Annex and include mutually applied UNECE regulations that came into force after the conclusion of negotiations of the EU-Japan EPA. (See Annex below).
30. Any decision to upgrade the Annex should be reviewed with involvement from the entire automotive sector to understand potential benefits to the industry and with consideration given to the UK’s future relationship with the EU.
31. The replication of the EPA automotive Annex in a future bilateral UK-Japan trade deal would reduce the risk of new regulatory checks on UK automotive products exported to Japan and vice versa also thanks to provisions designed to ensure:
 - c. continued regulatory convergence into the future;
 - d. enhanced collaboration in developing and amending regulations in the context of the World Forum for Harmonization of Vehicle Regulations (WP.29);
 - e. improved coordination in the implementation of UNECE regulations;
 - f. enhanced cooperation in developing domestic regulations in areas not covered by UNECE regulations;
 - g. trade-restrictive measures are not introduced on covered products incorporating new technologies.
32. Notably, these simplifications are currently available for all EU and Japan’s products covered by the 1958 and 1998 agreements, without the need to comply with the EPA rules of origin to benefit from reduced regulatory barriers. The same should apply to all UK and Japanese products after the end of the transition period.

Trade Facilitation

33. The EU and Japan mutually recognize their respective AEO programmes. UK and Japanese AEO’s should also be mutually recognised under all circumstances to ensure business continuity at the end of the transitional period.
34. Without prejudice to a timely conclusion of UK-Japan negotiations and to future trade relations between the UK and the EU, the parties should consider reversing the burden of responsibility for origin verification procedures from the importer to the exporter’s customs authorities. This

⁵ “Impact assessment of the EU-Japan Economic Partnership Agreement (EPA) on the UK”, 24/05/2018.

change would benefit both UK and Japanese automotive traders. Ensuring responsibility of origin verification lies with the exporter's customs authorities allows exporters to comply with one interpretation of rules of origin provisions, specifically the interpretation of their domestic customs authorities.

35. For small and medium enterprises or occasional exporters, flexibility on origin documentation would be beneficial.

Investment

36. The automotive industry wishes to maintain the privileged position the UK currently enjoys for Japanese investment. A future UK-Japan trade agreement should therefore include robust mechanisms to protect bilateral investment from the date of entry into force of the agreement.
37. With the UK home to many Japanese investors and the UK withdrawing from the EU, it is critical for the continued success of UK automotive that government ensures the UK remains open to Japanese investors. Existing commitments on investment liberalisation under Chapter 8, Section B of the EU-Japan EPA should therefore be fully replicated.

Labour mobility

38. The UK has very limited commitments on movement of personnel and service providers under the existing EU-Japan EPA and UK automotive would benefit from the inclusion of provisions to facilitate intra-corporate transferees, movement of service providers, professionals, business visitors for establishment purposes.
39. A simplification of processes across all visa types would help facilitate the entry and temporary stay of business visitors, intra-corporate transferees, investors, contractual service suppliers, independent professional and short-term business visitors.

Digital trade

40. A future bilateral trade agreement should replicate and, possibly, achieve more ambitious commitments on e-commerce and digital trade, including obligations regarding software source codes and bilateral free flow of data.
41. The EU and Japan adopted decisions in January 2019 to allow personal data to flow freely and safely between the two partners. They agreed to recognise each other's data protection systems as equivalent', creating the world's largest area of safe data flows. Similar adequacy decisions should be adopted by the UK and Japan even in the absence of a new FTA by the end of the transition period.

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Annex – Candidate regulations for upgrading the existing EU-Japan automotive annex

Regulation No.	Title
R144	Uniform provisions concerning: Ia. Accident Emergency Call Components (AECC); Ib. Accident Emergency Call Devices(AECD) which are intended to be fitted to vehicles of categories M ₁ and N ₁ ; II. Vehicles with regard to their Accident Emergency Call Systems (AECS) when equipped with an AECD of an approved type; III. Vehicles with regard to their Accident Emergency Call Systems (AECS) when equipped with an AECD of non-approved type
R145	Uniform provisions concerning the approval of vehicles with regard to ISOFIX anchorage systems ISOFIX top tether anchorages and i-Size seating positions
R146	Uniform provisions concerning the approval of motor vehicles and their components with regard to the safety-related performance of hydrogen-fuelled vehicles of categories L ₁ , L ₂ , L ₃ , L ₄ and L ₅
R147	Uniform provisions concerning the approval of mechanical coupling components of combinations of agricultural vehicles
R148	Uniform provisions concerning the approval of light-signalling devices (lamps) for power-driven vehicles and their trailers
R149	Uniform provisions concerning the approval of road illumination devices (lamps) and systems for power-driven vehicles
R150	Uniform provisions concerning the approval of retro-reflective devices and markings for power-driven vehicles and their trailers
R151	Uniform provisions concerning the approval of motor vehicles with regard to the Blind Spot Information System for the Detection of Bicycles
R152	Uniform provisions concerning the approval of motor vehicles with regard to the Advanced Emergency Braking System (AEBS) for M1 and N1 vehicles