

## **DELIVERING UK AUTOMOTIVE BREXIT PRIORITIES SMMT DISCUSSION PAPER – 7 JULY 2017**

### **Introduction**

This paper outlines key areas in delivering the UK automotive industry's position on the UK's withdrawal from the European Union. SMMT's position remains unchanged in relation to the five main priorities in this paper and builds on previous work to provide focus on what next steps the government should take to deliver on automotive priorities.

SMMT welcomes statements made by government in highlighting the importance of the UK automotive industry to the economy and a determination to prioritise the sector's key issues as part of the UK's negotiations with the EU. The Prime Minister's January 2017 speech and government white paper outlined the basis and broad strategy for the UK entering negotiations with the EU. SMMT now calls on government to outline how it will deliver on the industry's priorities to sustain business confidence, attract investment and secure the growth ambitions of the sector.

Government must secure interim arrangements to safeguard the future of the UK automotive industry and avoid a cliff edge. Clarity and certainty is urgently needed for businesses to enable them to plan and secure investment following the March 2019 Article 50 deadline. SMMT calls on government to maintain Single Market and customs union membership until a final agreement on a new relationship with the EU has been agreed and implemented.

### **SMMT's priorities focus on five areas:**

**Single Market** – To achieve automotive priorities on tariff-free trade and avoiding non-tariff barriers, government must demonstrate how it intends to secure a future trade agreement with the EU that affords the automotive industry the benefits currently enjoyed as members of the Single Market.

**Customs** – Under a new customs agreement with the EU, government should prioritise the free-flow of automotive goods at the border to avoid costs, maintain competitiveness and support the just-in-time manufacturing process. Key issues include continued application of common customs rules and procedures without burdensome checks or reporting.

**Talent** – Government must address the needs of the automotive industry in its ability to recruit and access talent when assessing how the UK ends freedom of movement and implements new immigration controls. Key issues include access to labour to fill skills gaps and the current ability for automotive companies to quickly and easily move employees to address operational issues or support project teams.

**Regulation** – Government should demonstrate how existing automotive regulation fits within plans for the 'Repeal Bill' and work through options for how future EU regulation affecting the UK automotive industry can be effectively implemented. Key issues include future influence on regulations affecting the UK automotive industry, the potential to create non-tariff barriers through regulatory divergence and the ability for the UK to type approve vehicles for the European market.

**Trade** – Clarity is needed on how the UK will treat both existing EU Free Trade Agreements and those currently under negotiation. Key issues include establishing solutions to issues around Rules of Origin, understanding how existing preferential access to markets can be secured as well as benefits from regulatory discussions between the EU and other key markets.

### **Transition and certainty**

The result of the referendum on the UK's membership of the EU has already created uncertainty within the automotive sector. There is concern that this will lead to an increase in the cost of trade which will, in turn, undermine competitiveness and make the UK a less attractive place to invest. Automotive manufacturers work on four to seven-year product cycles and investment decisions being taken today have to take into account this risk. It is essential that government does everything that it can to provide reassurance to the whole sector and remove this uncertainty as soon as possible.

During the negotiations, the UK government and the EU should set out in as much detail as possible the terms of trade for automotive to avoid any risk of a “cliff-edge”. If such a “cliff-edge” occurred, the UK would be required to trade on the basis of World Trade Organisation (WTO) rules. This would see the application of a 10% tariff on vehicles and an average 4.5% tariff on components which will increase the cost of production, undermine competitiveness and potentially increase the cost of cars for consumers. SMMT analysis suggests that the UK motor industry faces a £4.5 billion tariff cost for cars alone which could add at least an annual £2.7 billion to imports and £1.8 billion to exports. Import tariffs could push up the list price of cars imported to the UK from the EU by an average of £1,500 if brands and their retail networks were unable to absorb these additional costs. It could also result in the introduction of significant non-tariff barriers, the loss of passporting rights for services and the prospect of having to certify exports as being compliant with EU rules which will create significant administrative burdens and additional costs.

Should at the end of the negotiating period there not be an agreement on a future relationship, current arrangements should continue to apply, including maintaining membership of the Single Market and customs union to ensure continuity and certainty. In the longer term, government must ensure that the UK's new trading terms with the EU and the rest of the world are as good as or better than those already enjoyed by the automotive sector. To secure this, government and industry must strategically engage throughout the negotiations on the transition towards a new trading relationship with the EU and the establishment of new global opportunities.

### **About UK automotive**

The UK's automotive sector is diverse and currently thriving. It is a critical part of the UK's industrial footprint and a significant contributor to the broader economy, accounting for more than £71.6 billion turnover and £18.9 billion value added each year, alongside £2.5 billion of investment in automotive R&D. Its success is based on many factors - a highly productive workforce, engineering excellence, world-class production quality, cutting-edge technology, products with global appeal and, critically, the favourable trading conditions it enjoys with its most important market, the EU.

## Single Market

**Objective:** Secure arrangements to ensure that the automotive industry is able to operate without tariff or non-tariff barriers when trading with and within the Single Market.

**In delivery of automotive priorities on the Single Market, government should:**

- Detail how it envisages “Single Market arrangements” for automotive and discuss with industry the suitability of such arrangements in maintaining the free-flow of trade
- Set out its ambition for zero tariffs on automotive related goods
- Provide a clear plan on how it will avoid regulatory divergence for automotive regulation

The Prime Minister has outlined that government will seek an ambitious comprehensive free trade agreement with the EU where “single market arrangements” for automotive could be considered. The UK’s membership of the Single Market has enabled the automotive sector to trade freely with the EU without incurring the cost of tariff and non-tariff barriers. It can access talent from right across the EU and enjoys regulatory certainty through harmonisation. The Single Market has been critical to the competitiveness of the UK automotive sector and it is vital that government works with the industry to assess how “single market arrangements” could maintain these benefits and ensure a complete absence of tariff and non-tariff barriers.

The application of tariffs would put the UK automotive industry for both vehicles and parts at an immediate competitive disadvantage, which could ultimately make automotive manufacturing in the UK unviable. SMMT analysis suggests that under WTO tariffs, the UK motor industry faces a £4.5 billion tariff cost for cars alone, which could add at least an annual £2.7 billion to imports and £1.8 billion to exports. Import tariffs could push up the list price of cars imported to the UK from the EU by an average of £1,500.

Government must explore ways in which continuity in the common rules applied to the automotive sector in the UK and the EU currently derived through membership of the Single Market can remain in order to enable a level-playing field and ensure that the movement of automotive goods continues, free of regulatory barriers. By not being part of a common automotive regulatory framework there is a longer-term risk of increasing burdens from non-tariff barriers where regulatory regimes may diverge and create additional costs, both in terms of automotive product regulation as well as cross-sector regulation on data, the manufacturing environment and financial services. Any future access to the Single Market must be both tariff-free and without any regulatory barriers due to the critical importance of NTBs.

The EU is by far the largest market for the UK automotive sector. 57.5% of cars exported from the UK in 2015 went to the EU, while 81.8% of cars imported into the UK come from the EU. The UK automotive industry is also highly integrated with the European industry. It operates complex supply chains that stretch right across the EU. Furthermore, the UK is home to some automotive manufacturer's European headquarters, who use the UK as their gateway to the EU. Some automotive businesses also base their finance arms in the UK, using the UK as a base for providing a critical service to the whole of the EU. Any change in the ability of the UK automotive industry to move goods and provide services from the UK right across the EU will significantly impact the competitiveness of the industry and attractiveness of the UK as a place to invest.

## Customs

**Objective:** To continue customs arrangements that maintain the free, frictionless and non-burdensome flow of goods across borders.

**In delivery of automotive priorities on customs, government should:**

- Outline in further detail the options being considered to ensure frictionless and seamless trade across UK borders
- Carry out an impact assessment to demonstrate how changes to customs procedures will affect automotive manufacturing processes
- Continue the full implementation of customs regulation (Union Customs Code) and outline plans for future system of customs legislation.

Government has indicated that it wants to seek a new customs agreement with the EU with the objective of ensuring trade between the EU and UK is as frictionless and seamless as possible. SMMT has supported continued membership of the Customs Union in order to maintain a smooth and free-flow of goods across borders to avoid delays and additional costs. Government's intention not to share an external tariff with the EU and not be part of a common commercial policy challenges the position of remaining within the Customs Union.

SMMT seeks continuity in the trade of goods across borders between the UK and EU with customs arrangements that maintain the free, frictionless and non-burdensome flow of goods. Government should prioritise delivering the 'freest' possible trading zone with minimal procedural and compliance costs. Frictionless trade should deliver improved security measures without increased physical burdens on businesses, services or people, through a data led solution that will ensure the free flowing movement of trade between the UK, EU and third countries.

At present the UK enjoys free-flow of goods through ports and fee-free passage of goods through customs. Automotive goods imported from or exported to the rest of the EU from the UK are not currently subject to customs procedures. In addition, the automotive industry operates both lean and just-in-time procedures which rely upon highly efficient logistics and the elimination of delays at the border. As a member of the Customs Union delays are very rarely incurred on trade between the EU and UK.

Key priorities on customs for the UK automotive industry include continued application of a common customs code and procedures, ensuring that rules of origin issues are addressed and preventing customs duties being applied. SMMT calls on government to continue to implement in full the Union Customs Code to deliver regulatory continuity for customs arrangements. Further consideration should be given to any future changes to the UK's customs regulatory regime to avoid barriers to trade or cost increases from potential divergence with EU rules.

There are risks that introducing new customs procedures would create additional administrative burdens and considerable impacts on the UK automotive sector, raising costs and damaging competitiveness. New procedures including additional declaration processes, more detailed Rules of Origin reporting, border checks and potential inspections would result in delays and create a need for additional warehousing which would further increase costs and put at risk the efficiency of the manufacturing process. This would have a negative impact on both the productivity and competitiveness of the UK automotive sector.

As government considers elements to include within a new customs framework for the UK, approaches should be considered to identify how costs and delays from new arrangements can be mitigated. It is also important that government assesses the physical infrastructure and resourcing that may be required in moving to a new customs arrangement with the EU. Capacity and operational issues need to be clarified as soon as possible. Government should explore with the industry the viability of solutions such as authorised economic operator/trusted trader status, self-assessment, and digital processes in being able to deliver continuation of frictionless trade for automotive, taking into account the needs of both larger and smaller companies where new administrative requirements need to be minimised.

## Talent

**Objective:** Ensure the UK automotive industry has unrestricted access to talent at all levels across Europe.

### In delivery of automotive priorities on talent government should:

- Explore options to ensure continued and unrestricted access to talent and professional expertise
- Ensure that the UK has beneficial access to the EU skills market so as to allow manufacturers to fill key roles and address skills gaps and ensure that a preferential agreement is put in place for these workers to travel freely between the UK and EU
- As an immediate priority, make a clear statement confirming the continuing right-to-work of EU nationals already in the UK. This is critical for business planning purposes.

Controlling immigration is one of government's top priorities in its approach to Brexit, outlining that the Free Movement Directive will no longer apply with the migration of EU nationals subject to UK law in the future. Moving away from free movement of labour to a new immigration system will be a key challenge for the automotive industry.

The automotive industry is committed to nurturing and developing our skilled workforce which promotes competitiveness and supports job opportunities in the UK. The efficiency and flexibility of the labour market are key strengths of the UK economy. 814,000 are employed across the automotive industry, 169,000 employed directly in manufacturing. UK automotive companies of all types and sizes have a significant workforce of non-UK EU workers; with SMMT estimates of on average 10%, but some companies over 50% and this is at all levels of the business. There are up to 5,000 current vacancies in the automotive industry causing significant impact on business operations and by 2020 the automotive sector may need as many as 50,000 more people than currently work in the industry to meet growth opportunities.

Free movement of labour within the EU has enabled global advanced manufacturing businesses the ability to blend UK and international talent at all levels of the industry. The industry faces acute skills challenges at a UK, European and global level which requires both further investment and access to labour to fill skills gaps. Retention of talent is important for automotive companies where certainty around the status of current non-UK EU workers and their dependants is a key issue.

The ability to quickly and easily move employees across sites in different countries is essential to the smooth operation of automotive businesses. Peaks in demand or faults on the production line can require employees to be moved from one country to another, often at short notice. As a global industry we have a wealth of nationalities and requirements for free movement around Europe and international assignments, whether senior management roles, teams to implement new product processes, problem response teams or teams to train staff. Europe also needs access to UK talent. How government addresses the need for free movement within the automotive industry without any burdens or limits is cost, time and competitiveness critical. Current free movement arrangements provides manufacturers with the flexibility they need to meet new challenges and customer demands.

Any changes to the current provisions relating to the free movement of labour risk increasing costs for UK automotive businesses and creating serious business planning challenges. Long-term prosperity requires a suitably skilled and experienced workforce, and for UK advanced manufacturing there is a shortage of qualified scientists, engineers and technologists (SET) and STEM skills in the pipeline. The EU-wide talent pool is critically important in filling business-critical vacancies.

## Regulation

**Objective:** Provide certainty on automotive regulation through harmonisation and ensure UK automotive interests can be reflected in future European legislation.

### In delivery of automotive priorities on regulation, government should:

- Provide assurance to industry on the future of type approval in the UK
- Clarify the mechanism of implementing existing automotive regulations as part of the ‘Repeal Bill’ process
- Seek to establish appropriate, clear and non-burdensome structures that enable application and implementation of future EU legislation affecting the automotive sector
- Develop proposals to maintain the UK’s influence in the shaping of automotive regulations at a European level
- Ensure needs of SMEs and UK premium and specialist vehicle manufacturers are met under a future regulatory system

On the future regulatory and legislative environment for the UK, government has set out its intention to put EU-derived legislation on a UK legal footing through a proposed “Repeal Bill” as well as ending the jurisdiction of the Court of Justice of the European Union in the UK. The automotive industry has benefitted from a common automotive regulatory system that enables market access and a level playing field for automotive products and services across European markets. It is essential that not only existing automotive regulation be adopted by the UK but that an effective future regulatory framework can be established that guarantees the current level of market access for automotive.

It is essential that there is certainty and continuity through harmonisation of EU and UK regulations affecting the automotive sector to support both UK manufacturing and the UK vehicle market. Government should establish appropriate, clear and non-burdensome structures that enable application and implementation of crucial EU legislation. Regulatory divergence or uncertainty in the legal framework for the automotive industry would amount to non-tariff trade barriers, increasing costs and reducing the competitiveness of both the manufacturing base and ability to sell vehicles.

Influence in regulatory development is important to ensure the requirements of the UK automotive industry, particularly the UK’s unique premium and specialist vehicle manufacturers, are understood and reflected in global automotive regulatory development. EU standards are often adopted by other non-EU countries, such as the growing Chinese market, and the UK’s influential and respected voice must continue to be a part of these vital discussions.

The UK should prioritise the following policy areas when seeking to secure regulatory harmonisation with the EU:

- Safety and type approval
- CO<sub>2</sub>
- Emissions / Euro standards
- End of Life Vehicles (ELV) and recycling
- Data protection regulation
- Intellectual property rights and patents

An area which requires urgent legal clarification is the future ability for the Vehicle Certification Agency (VCA) to grant European approvals and the validity of existing type approvals issued by the VCA once the UK has left the EU. Government should issue, as a matter of urgency, a statement outlining its position with regards to type approval in the context of the UK’s withdrawal from the EU. This should include a statement on government’s position regarding whether or not it will ensure that a UK approval authority can issue European type approvals and make clear through which mechanism it intends for this to be delivered. The impacts of the VCA losing the ability to issue EU type approvals could have a major impact on the desirability of the UK as a leading place to invest in innovation and research. If the validity of existing approvals cannot be clarified, or it is determined that existing approvals would lose their validity, UK government should begin discussions with European partners now to ensure that an agreement is reached which allows UK approvals to remain valid. A strong, independent and trusted UK type approval body supports investments by manufacturers in their product development and manufacturing capabilities. Without a UK type approval body able to

issue EU type approvals, the attractiveness of the UK for key automotive research activities is diminished as well as the potential loss of engineering skills.

Regulation and standards at a European level enable a level-playing field as well as supporting technology developments and investments. For a leading innovative and technologically-advanced sector like automotive, guaranteed access to future EU funding calls is essential. This not only provides access to critical R&D funding, but facilitates cross-European collaboration and helps the UK to promote itself as a preeminent global location for R&D. The Government should seek to maintain the UK's participation in Horizon 2020, replace lost European Structural and Investment funds (including those from the European Investment Bank) where they have been used to support R&D and clarify the status of already committed but unspent structural funds, especially where these have been match-funded by industry.

## Trade

**Objective:** Secure the UK’s position in current EU trade agreements, those under negotiation and provide clarity on the UK’s future trade strategy

### In delivery of automotive priorities on trade, government should:

- Confirm “grandfathering” arrangements and continuity in trade relationships currently maintained through EU Free Trade Agreements (FTAs)
- Detail how intended benefits through FTAs currently under negotiation can be retained
- Outline a solution to maintain cumulation with EU automotive goods to resolve issues around Rules of Origin
- Provide clarity on its approach and priorities for future UK trade agreements

Government has clearly demonstrated its ambition secure new trade agreements with non-EU markets following the UK’s withdrawal from the EU. Government’s White Paper restated this intention and set out ways in which the UK will demonstrate its independent trade policy. A key aspect of government’s trade policy must include continuity in current trading relationships.

The UK’s withdrawal from the EU brings into question its access to existing EU trade agreements as well as those that are currently being negotiated (such as free trade agreements (FTAs), customs and partnership agreements, and investment agreements). Government must prioritise negotiations with the World Trade Organisation to agree its commitments and schedules as a key first step in enabling the UK to establish the foundations and rules needed for its trading relationships. There are substantial global trade opportunities for the UK automotive sector and government’s role in enabling the industry to access markets is critical. Clarity from government is needed on how current trade benefits gained through the EU will be secured and how government intends to pursue other trade opportunities.

The UK should explore every option for retaining the trading arrangements that currently apply to it as a result of trade agreements signed by the EU with third countries, such as the EU-South Korea FTA and the Comprehensive Economic and Trade Agreement with Canada (CETA). Government should also explore options for ensuring that the UK benefits from trade agreements that are currently under negotiation such as the EU-Japan FTA and the Transatlantic Trade and Investment Partnership (TTIP). Government should clarify the status of these trading relationships and the rules under which companies can access these third markets before pursuing new bilateral trade negotiations.

A critical issue for the automotive industry is Rules of Origin. Government should ensure that, for the purpose of future trade agreements signed by the UK, automotive goods originating in the UK and those originating in the EU are considered as originating content. This could be achieved through the application of the “diagonal cumulation of origin principle”, which would create an accumulation zone that recognised content produced in both the UK and EU as local content, reflecting the integrated nature of the automotive supply chain. Furthermore, government should explore the option of the UK becoming a contracting party to the Regional Convention on pan-Euro-Mediterranean preferential rules of origin to ensure the UK continues to benefit from diagonal cumulation arrangements currently enjoyed by EU member states.

### Automotive trade flow values for 2016 in top 10 markets (trade in vehicles)

Market	Total value of automotive trade - £ (vehicle exports and imports)
EU27	42,228,706,251
U.S.A.	6,477,102,024
China	3,433,008,879
Japan	2,249,381,926
South Korea	1,748,806,836
Turkey	1,221,527,054

Australia	750,052,204
UAE	571,082,225
Canada	535,899,054
Russia	505,954,377

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