



## Flexibility does not come for free

by Sam Lowe  
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**An EU-UK free trade agreement will result in new barriers to trade and border friction even if the UK chooses to unilaterally align itself with EU rules and regulations.**

Prime Minister Boris Johnson has said that the UK will “not align” with EU rules in any future EU-UK free trade agreement (FTA). European Commission President Ursula von der Leyen has [responded](#) by pointing out that “the more divergence there is, the more distant the partnership has to be”. Her statement reflects the EU’s general principle that access to the EU market is intrinsically linked to a country’s acceptance of EU rules, institutions and legal obligations. But in practice the EU’s approach is likely to be even tougher than von der Leyen’s words suggest: the greater the UK’s ability to diverge is, the more distant the partnership will be. The moment the UK obtains the right to choose whether it diverges or not from EU rules, it will – in most areas – be treated by the EU as if it has already done so.

So it matters little that on day one of a new EU-UK FTA, all UK rules and regulations would be the same as the EU’s. Once the UK leaves the EU’s single market rule book and institutions, British exports to the EU will broadly be treated as if they came from any EU FTA partner. The British government claims to have accepted that gaining the freedom to regulate as it sees fit will mean new trade friction. But it is not yet clear that businesses and the public have understood what this means in [practice](#).

Unilateral UK alignment with EU rules post-Brexit does have benefits for businesses: it avoids a situation whereby they have to produce to two different sets of rules when selling to both markets. It does not, however, lead to a substantive reduction in regulatory barriers to trade, if the UK has secured the ability to diverge if it wants to. For example, once the UK is outside of the EU’s food hygiene (SPS) regime, British exports of products of animal origin will face new regulatory controls at the EU border in the form of new paperwork and physical inspections. This will occur whether the UK applies the same food hygiene regime in practice or not. Thus, the upfront costs of being outside of the EU’s SPS regime are large. However, if the UK does then decide to diverge, and, for example, accept US production methods, this would not lead to a significantly larger increase in trading friction with the EU. The additional trade costs associated with choosing to diverge are large; the relative costs of then actually diverging are smaller.

To give another example, the moment the UK is outside of the EU’s single market, even if British producers continue to produce to EU standards, they will not be able to place them directly on the European market.

Instead they will need an EU-established entity to take on the legal responsibility for ensuring the product complies with EU product rules. This could be the EU-based importer or an EU-based legal representative of the British company. No longer being able to place products directly on the EU market creates an additional cost for British businesses selling to Europe, no matter what the UK's domestic regime. Whether the UK then decides to introduce its own product standards (as is currently the ambition), or accepts certain US standards, the barriers facing British exporters selling to the EU remain the same.

Of course there are exceptions – areas where unilateral alignment with EU rules can lead to greater market access. One of these is financial services, and particularly the areas which are eligible for consideration under the EU's financial equivalence regime. Here, unilateral adherence to EU rules could lead to the EU allowing certain financial services activity, focused on the EU-27, to continue to take place in the UK. Another area where unilateral alignment has clear benefits is data protection, where the UK is more likely to receive an adequacy ruling from the EU – which would mean that companies are able to continue storing the personal data of EU citizens in data centres located in the UK – if it continues to mirror EU rules. But these equivalence/adequacy rulings are unilateral – what the EU gives, it can easily take away, and the EU is both judge and jury. Switzerland provides a recent example of this happening, where the EU allowed an equivalence decision permitting EU stocks to trade on Swiss exchanges to lapse as a means of pushing Switzerland into signing up to an, unrelated, institutional framework agreement.

There has been some additional confusion about the concept of regulatory divergence in the recent Brexit debate. In the context of the negotiations on the future EU-UK relationship, the EU will ask the UK to commit to preserving existing environment and labour protections, and to continue adhering to EU state aid rules, as pre-conditions for a tariff and quota-free trade agreement. But it is important to note that the areas in which the EU has asked the UK to make regulatory commitments do not on the whole relate to the standards of products. Rather, the EU is focusing on preventing the UK from deregulating or increasing state financial support to make British industry more competitive than companies based in the EU-27. And compliance will not be rewarded with fewer regulatory hurdles to trade; it is simply a necessary condition to secure an FTA and the removal of tariffs and quotas.

In practice, there are few areas where the UK is likely to diverge significantly. European product standards are recognised globally, beyond just the EU, and there is little to no appetite from businesses to increase their compliance burden by having to certify their products separately for the UK market. The EU is a regulatory superpower, and the UK is stuck in its orbit by virtue of geography. The real question remains whether the UK attempts to reap the full benefits of convergence by legally binding itself to EU rules and institutions; or whether it continues to prioritise political rhetoric of 'taking back control' over the economic interests of entire sectors.

The big upfront cost of flexibility does come with one upside. Decisions that currently look politically difficult – such as conceding to US demands on food standards as a condition of getting a free trade agreement – might become easier once the initial cost of being able to diverge has already been paid. But the converse is also true: gaining flexibility with no intention of ever using it, for politically salient reasons or otherwise, comes with a significant price tag. Flexibility for flexibility's sake is a costly exercise, and one that is difficult to rectify after the fact.

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