

BREXIT, trade and the environment – the highest standards rule

Dieter Helm

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Trade has become an economic battleground in the retreat from globalisation. The US has made trade core to its foreign policy, mainly in respect of China, but also the EU and Russia. Trade sanctions are the weapon of choice in US global politics.

Even Trump's harshest critics acknowledge that China has not played by the rules. It provides widespread state aid, it allows intellectual property to be ignored and insists on its transfer. China even steals it. Its exchange rate, though less controlled now, is manipulated. China's home market is very political, and companies can find themselves disadvantaged if they offend Chinese political preferences, for example over the recognition of Taiwan. Its "Made in China" policy is quite explicit in its intentions.

Into this fraught territory the UK has embarked on BREXIT (now formally done) and the radical redesign of its trade policies and is negotiating multiple deals, most notably with the US and the EU.

In both the negotiations with the US and EU, the subject of environmental standards has come up (and it ought to with China). The UK government promised to uphold EU environmental standards post BREXIT. The UK is setting up the Office for Environmental Protection to ensure that these do not slip, though these standards and the associated targets are currently not to be set through legislation itself but rather by ministers from time to time, and many of them will not be statutory once set.

UK agricultural lobbyists have argued forcefully that no trade deal should be struck with the US without a legally binding commitment that imported food meets UK environmental and animal welfare standards. At the same time, the UK government insists that it will not sign up to EU environmental standards and reserves the right to diverge, raising the possibility that in some areas, like pesticides, the UK may allow the use of specific chemicals and gene editing that may be prohibited within the EU, both supported by some elements of the UK farming lobby bodies. The UK may stop US

imports on grounds of lower US agricultural standards, but want to export to the EU with lower UK ones. Presumably the EU would therefore ban these imports from the UK.

All these heated debates raise a central question: how should the environment enter into trade arrangements?

An environmental level playing field

Many environmentalists take at best a sceptical view of the claimed benefits from trade, and in particular globalisation. Self-sufficiency and local production have less air and freight miles. Small scale is preferred to mass production. For them, small is indeed beautiful. They see the scale of environmental destruction that has accompanied the great industrial expansion of China as evidence that globalisation has not been good for the environment.

China is the central pin of the globalisation since 1980. That is why its environmental performance matters. Others may pollute more, but the aggregate effect of almost every other country is dwarfed by China. Its phenomenal economic growth has been accompanied by an environmental catastrophe on a scale not seen in previous world history. It has massively increased greenhouse gas emissions, and its development has been built, at least initially, on the export of carbon-intensive products, fuelled by coal. The three great rivers have been rendered close to biologically dead in parts, it has dammed the Upper Mekong, and in the name of its *Belt and Road* project encouraged Laos in particular to build lots more dams. The cost of China's great expansion has been more climate change, more water pollution, the slow death of the great Mekong rainforests, and the pollution of the South China Sea. Its plastic waste pollutes the oceans.

When it comes to the absence of a proper account of the pollution, these environmentalists have a strong point. If the great expansion of China has come at this environmental price, what is to like about it? Not much is the obvious environmental

answer. It is incompatible with limiting global warming, and incompatible with the protection of biodiversity.

It would however be a mistake to think that there is a simple trade-off between trade and the environment, and less trade does not necessarily mean a better environment. Rather it is about trade on a level playing field where the environmental impacts are fully priced in.

This is a long way from “free” trade. Free trade and fair trade are not the same thing. Free trade means that anyone can sell to anyone else, regardless of location, and without any tariffs. A moment’s reflection tells us that this is not necessarily a very attractive state of affairs. Slave labour can lead to low costs and lots of market buyers, but it violates basic human rights. Slavery was a key part of the expansion of European trade and the clamour for free trade in the seventeenth and early eighteenth centuries, and cheap ex-slaves continued to provide the basis of post-abolition trade. State aids can undercut competitors and build monopolies. Polluting companies can gain market share at the expense of cleaner ones.

Free trade can lead to a race to the bottom, and the bottom can be very low. Indeed it is: Chinese coal and carbon-intensive steel displaces European cleaner steel, cheaper labour pushes out well protected workers, and Chinese state subsidies to solar businesses have bankrupted US and EU companies. Mass internment of Uigurs in Northwest China produces prison labour for export markets.

The lowest standards are not acceptable for good reasons in most civilised countries. For this reason, unregulated free trade is a very bad idea.

Fair trade is very different. It is trade on a level playing field. That is what makes it fair. The level playing field is one that takes account of workers’ rights, environmental standards, and animal welfare amongst other things.

Which level playing field?

The trouble with fair trade is that most countries differ as to what constitutes that level playing field. Labour law varies widely, as do pollution standards and pollution taxes, and the role of the state varies from where it is central (as in the Chinese communist state) to where it is minimised.

Whose level playing field should the UK adopt? There are two possible answers to this. We could take the standards of one of the big global economies – those of the US, EU, Japan, and in due course even China. As the UK is discovering, these each have the ability to dictate the conditions for trade to other countries, as a price of market access for smaller countries like the UK. It is not surprising that in practice all the main smaller countries broadly adhere to one of these sets of standards, and the EU customs union and internal market is a successful example, and those who trade most with other EU countries have ended up either joining the EU, or accepting its trade terms (as Norway and Switzerland have done). Since the UK trades most with the EU, it will probably end up *de facto* following its standards. Sovereignty gives the right not to accept others' terms, but it does not abolish the consequences of that choice.

The second answer is to try to establish some supranational rules, through a global institution. That is where the WTO comes in. Yet it ultimately relies on the willingness of the main trading blocks to allow it to enforce the level playing field rules. It can do this to smaller countries, but it is much more difficult when it comes to China, the US, Japan, Russia or the EU. It has proved powerless in the US-China trade disputes. The WTO has no troops to enforce its decisions. It does not even currently have a quorate appeals body.

Given that countries have different approaches to fairness, what happens when one country takes a different view from others? For example, what happens when the UK decides that “fair” means UK animal and environmental standards or above? The trade arrangement could be struck to exclude these items, or at least apply this conditionality. That is what the UK wants to do with agricultural trade with the US, and what the EU does more generally. The UK wants its standards to apply. Only if US standards are like the UK would the UK be prepared to trade.

In principle, this menu of conditions could work, but it is easy to see how it would not in practice. The worry in respect of British agriculture is that the underlying motivation is protection from competition. In a game of self-interest, lobbyists want access to markets for their exports, but protection from imports. If the UK producers were more competitive than the importers, then there would be no need for the highest standards rule, because there would be no imports.

Climate change and carbon border prices

Carbon is an example of where trade and targets can come into conflict. Climate change is a global phenomenon. The location of carbon emissions does not matter. It needs a global agreement to cut emissions, not least because there is a classic prisoners' dilemma. A trading country that free rides on others' efforts benefits from a lower explicit or implicit carbon price. Chinese steel gains a march on European steel as a result. The higher the carbon price, the greater the competitive advantage to the free rider.

And that is what has happened since the baseline for unilateral, national territorial emissions targets have been set, as explained in my forthcoming book – *Net Zero*.¹ Not only is the polluting exporter given a competitive advantage, but the importer has a positive incentive to switch from domestic production into imports, since it makes it easier to meet its own domestic unilateral target. The result is that although the EU has pushed hard on the unilateral territorial emissions route, the impact on the concentration of carbon in the atmosphere has been negligible. Why? Because the EU's carbon consumption has followed a very different trajectory to its home carbon production.

The clear example is the UK and its shiny new net zero target. The Climate Change Committee (CCC) claimed that “By reducing emissions produced in the UK to zero, we

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Net Zero: How We Stop Causing Climate Change by Dieter Helm - Hardcover | HarperCollins | [Available to pre-order](#)

also end our contribution to rising global temperatures". It is of course nonsense: we will never reach zero, and we will be causing climate change as long as we are engaged in carbon consumption, which includes imports for countries that are not net zero. Ironically at the time the CCC was advising the UK government to go for a net zero territorial production target, the future of British Steel was under threat. Think about it from the UK's new net zero perspective. The best strategy would be close it, and therefore eliminate its emissions from the UK territorial emissions inventory. The steel could be imported from China instead. Think of the resulting emissions. Chinese steel is around 70-80% coal-based, and then the steel has to get to the Chinese ports and be shipped halfway around the world, before being unloaded at the UK's ports and taken to its end use.

Why would any serious environmentalist think this is a good idea? Free trade with China for steel in the presence of a UK unilateral territorial emissions target is a way to *increase* global warming. Does this mean that we should prohibit China's steel imports, getting rid of any tariffs? No: the right answer is to apply the same carbon price to the imports as domestically, and that is a carbon border adjustment or tax.

Vested interests protest that this is unworkable, but it isn't. The bulk of carbon imports are made up of five key products – fertilisers, steel, cement, aluminium and petrochemicals. For each of these products, the share of coal in the energy sector is a good starting point: roughly right rather than precisely wrong. The really good thing about a carbon border adjustment is that it is only paid if the exporting country does not have equivalent or better carbon prices at home. The exporter now has a choice: introduce a carbon tax at home and pay this to the home government, or do not have a carbon price at home and pay that price to the importing government. It is a neat incentive mechanism to get the globalisation of carbon pricing, and much better than trying to get top down emissions targets into an international agreement. Even better, it might actually work.

Fair trade is environmentally OK if the carbon price is applied to both parties. Not to price carbon is to distort trade, and in this case further exacerbates global warming. Free trade in the absence of common carbon pricing makes the environmental

outcomes worse. Think of the carbon price as a carbon tariff. Eliminating environmental tariffs is a bad idea, damaging the environment and damaging economic efficiency in the process. All costs should be in the prices, not just some.

Agriculture and trade deals

Most trade deals start with an argument about agriculture and end up protecting it. This is the pattern for the US-UK negotiations. The UK side starts with a panic about “chlorinated chickens” and the US farmers start with the opportunities to export to the UK.

Why does agriculture have such a grip, given that for many countries it is economically pretty insignificant? In the UK, it is about 0.6% GDP. Of that 0.6%, a third is direct subsidies and probably another third is the pollution and other costs agriculture causes, from silt, to nitrates and pesticides in water systems, to the carbon and air pollution.

Agriculture takes central stage despite its relative insignificance because of politics and lobbying, not economics and efficiency. The US and the UK have territorial electoral systems, and within Europe there is a lot of decentralisation. US politicians need mid-western votes, British politicians (particularly Conservatives and LibDems) need the South West and other rural voters. Add to this the fact that the sheer scale of subsidies attracts lobbying and it is no wonder that the farming interests have amongst the most powerful lobby groups of any sector in the US, UK and the EU.

Yet there is more to the importance of agriculture than its scale or subsidies. In the UK, it is 70% of the land area, and there is enormous scope to improve upon this land use, but also scope to make it even worse. The important fact to bear in mind is that much of British agriculture is uncompetitive on a purely free trade basis. A lot would be wiped out by simple zero tariffs and open free trade agreements with the US and other countries.

The reasons for this un-competitiveness is partly about poor productivity, low take-up of digital technologies and the ageing work force. It is also due to the UK's extraordinary

geology and geography. UK agriculture is made up of a patchwork quilt of small fields and hedgerows, of national parks and densely populated catchments. That is the way most people like it, for the very good reason that they appreciate the multiple natural capitals and the benefits they get from the land, including but not limited to the food that is produced. The 70% land area is made up of rivers and water, recreation and leisure, mental and physical well-being opportunities. It has the capacity to deliver a much better carbon outcome, playing its part in naturally sequestering carbon rather than emitting it, to enhance biodiversity, and provide a lot more access.

Think in contrast of the vast bread baskets of the US mid-west or Ukraine. Think of the cattle ranches of Argentina and the US. Think of sheep farming in New Zealand. How could the UK ever compete on free trade basis?

UK farmers fear free trade for good and bad reasons. They want to be sheltered from competition, but they also want subsidies too. This is where the “standards and welfare” argument comes in. Farmers’ lobby groups want imports to meet UK standards. But they are not prepared to go the full way to argue that they want UK standards but not subsidies. They want both: state aid *and* UK standards. The last thing UK farmers want is a level playing field: they want it decidedly tilted in their favour. In this their political weight tells.

Yet a genuinely level playing field would bring benefits to both sides. If the standards followed the highest standards rule, not the lowest, then there would be little beef and poultry exports from the US. But the US would export grain. The UK would export whatever was competitive against US production. Better still if there was a common carbon price, things would get a lot more interesting. All those fertilisers and pesticides imported from the US would have to pay their carbon dues, and the carbon pollution from transport and especially shipping would be added. The end result might be very little agricultural trade, and probably confined mainly to premium products – more manufactured food products, less raw food.

Would this matter? Not much: it is not a big share of GDP, and environmentally producing food nearer to the final market would have many environmental benefits. But

it would make a difference to food prices: protected markets are typically more expensive, and the UK consumer would not have access to really cheap chickens and cheaper beef. Pollution and standards would be priced in: high standards, higher costs and higher prices; low standards, lower costs and lower prices.

The level playing field – fair trade – is probably one with even less agricultural trade than now, and it means more expensive food. From an environmental perspective this is good news, but not for politicians worried about food prices for the less well-off.

When it comes to the EU, the standards argument has until now been an easy one. The standards are the same across the EU. The EU sets them, and the EU pays out the CAP subsidies. Disputes arise only when there are for example, disease outbreaks like BSE and foot and mouth, but otherwise trade is straightforward, and the playing field is level because the EU sets the rules.

Post-BREXIT things become much more interesting. The UK wants its sovereignty back and for the government this means the right to set its own environmental and welfare standards. Now the highest standards rule gets a bit trickier. When environmental and welfare standards diverge, whose apply? Whilst there might be some animal welfare differences in specific cases (such as veal crates perhaps), broadly these might not diverge much for quite a while. Live transport of animals over longer distances might raise issues perhaps, and with big impacts on UK lamb exports. But these specific cases could be dealt with on their own merits.

Where it becomes much more contentious is chemical and biological regulation. The EU is tough on GMOs and very worried about gene editing (which it treats on a similar basis to gene editing). It does not much like neonicotines and glyphosate. It is possible to image a scenario in which the UK takes a more relaxed attitude on both the genetics and the pesticides. Then what? The highest standards rule is the EU standards not the UK's. So, should UK exports to the EU be banned?

It is quite understandable that the EU worries about the UK deregulating and reducing the constraints on the environment, and wants the level playing field to be accepted by

both sides of the trade negotiations. It is also understandable that the UK wants the right to diverge. After all, what would be the point of BREXIT if the UK ends up following the rules without having any say in them? The resolution: the highest standards rule would dictate that where the UK diverges on the downside, its exports are banned from the EU markets.

BREXIT has a price and for some Brexiters this is a price worth paying. It is not a free lunch. Sovereignty has costs, and the highest standards rule would have a big impact on some farmers.

A related case is the UK-EU fishing negotiations. It is not hard to show that the EU management of fisheries has not been a startling success. The UK wants to take back control of its coastal waters. It wants to decide who fishes for what and where. It wants to do this for sovereignty reasons, and the government also argues that it will be a better manager.

So far, so good, except for one little inconvenient detail: the UK's main market for its wet fish and shellfish is Europe. It is critical to the UK fishermen that all those lorries get to France and Spain and other EU markets, and with as little hassle and delay as possible. Fresh fish has to be fast fish.

The UK want to control its fisheries and to have fast access to EU markets. For this it needs the ports to wave through the lorries, with minimum customs controls. Presumably too the UK wants to ban fish entering the UK from the EU from fisheries which are not so well managed – assuming of course that it is actually true that UK fisheries management is better. And the UK also wants access to the other EU fishing waters too. This is important to its own fleet, not least because fish have a habit of ignoring territorial waters and swim around quite a lot.

It is hard to conclude other than the highest standards rule would reduce fish trade, and possibly quite a lot. If EU boats cannot access UK waters, or are rationed on grounds other than the EU's common fishing policies allow, then the reciprocal rules will apply.

Does it matter? From a GDP perspective, UK fishing is at best 0.1% GDP. The UK territorial waters are a very important environmental asset, with biodiversity, carbon sinks and recreational uses, as well now as a location for fish farms. If UK fishing was reduced or even stopped because access to EU markets was constricted, the natural capital gains to GDP properly measured, might be greater than the 0.1% loss, and especially once the subsidies are taken into account. The compromise, allowing some continued environmental damage, with trade based upon the highest standards rule would be some contraction.

As with agriculture, the perplexing question is why both fishers and farmers voted for BREXIT. They either believed that sovereignty is more important than economic gain, or they assumed that UK politicians would make sure it turned out alright, because they could rely on their lobbyists to extract their political pound of flesh.

Policing trade

The highest standards rule needs to be enforced. Who is going to do this? In theory this requires a customs inspectorate, trained in for example detecting GMOs and gene edited animals and plants and chlorine in chickens, and able to do environmental assessments of standards applied in the country of origin.

This is no small undertaking, and with the EU where most UK food and fish trade is located, this means a new regulatory effort, since the EU membership rendered this not necessary as the standards were common. The inspectors and regulators would need detailed scientific and administrative skills. They would need detailed databases. Think for a moment how hard testing for coronavirus has proved. Now think about the multiple ways plants and animals can be produced.

As with so much customs inspection and deregulation, there would be scope for self-certification, special arrangements for different jurisdictions and fines and penalties for violations. None of this is new. But it would not be cheap or easy.

In the case of carbon and carbon border taxes, this may be made easier by concentrating on the small number of carbon-intensive products, as discussed above. It would be made even easier if the UK adopts the EUETS price and the EU carbon border adjustment tariff as the metrics. It would then not need to inspect or tax within EU traded goods itself, like Norway. But the border adjustment would still need to be applied to China and the US.

What happens if there are no deals?

It is very hard to see how the UK-EU and UK-US trade negotiations are going to deliver a better outcome in the short run than what currently exists. Would no deals be better? The answer depends upon the policy principles the UK government chooses to follow.

Suppose the government means what it says: there will be no reduction in standards in the UK, no agricultural imports will be tolerated which are below UK standards, and UK territorial waters will be a matter of UK sovereignty only. The UK has further stated that it intends to have higher environmental standards than the EU.

In these circumstances, applying the highest standards rule should mean: a carbon border tax applied to any imports from a country either without or with a lower domestic carbon price; and few if any meat imports from the US. It will also mean less chemical imports from the US because it does not have a carbon price, probably switching to importing EU produced fertilisers and pesticides.

If however, the UK lowers its standards, for example by permitting the continued use of a number of pesticides, then it can expect retaliation from the EU, banning UK exports to the EU in these categories. Applying the highest standards rule to the UK-EU and UK-US trade deals means less trade, not more. This is not a bad environmental outcome, and it is much better than free trade.

The UK government suggests that no deal is not that bad: it could fall back on the WTO rules. Putting aside the fact that the WTO is hardly functioning at all now and its rules have become practically unenforceable, the WTO is based upon the reduction of tariffs –

free trade – and not on fair trade and the highest standards rule. If this is what no deal means, then it is best to be honest: free trade will probably not be good for the environment.