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THE IMPACT OF BREXIT ON UK SERVICES

FOREWORD

The service sector stands as a clear exemplar of the trade-offs entailed by Brexit. The emphasis placed by the government on reclaiming regulatory autonomy during the negotiations over the Trade and Cooperation Agreement (TCA), and the particular importance of ending freedom of movement had particularly serious consequences for those who import or export services. In this report, Sarah Hall and Martin Heneghan explore the consequences to date of Brexit, and particularly of the TCA, for service providers.

I'm immensely grateful to both authors not only for providing a wonderfully clear and informative piece of work, but also for the good humour with which they have done so, and with which they have responded to countless suggestions for revisions and edits.

On which note, my thanks to Jonathan Portes and Jill Rutter for supplying these suggestions, and to Sarah Overton for drawing up the figures in the report and overseeing the reviews. John-Paul Salter again deployed his editorial skills, while Navjyot Lehl was responsible for the design and production of the finished product.

I'm convinced the report that follows makes an important and original contribution on an extremely important topic. I hope you find it interesting.

Professor Anand Menon
Director, The UK in a Changing Europe

8 December 2021

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SUMMARY

- Services are a strength of the UK economy. The UK runs a trade surplus in services and before the UK's departure from the EU and the Covid-19 pandemic, the EU was typically the destination for around 40% of UK services exports.
- Trade in services between the UK and the EU has become more difficult under the terms of the 2020 Brexit trade deal.
- The UK-EU trade deal was accompanied by additional agreements in areas such as financial services and data. These agreements and decisions provide a framework for dialogue and greater UK-EU trade opportunities than are currently provided for. However, progress to date has been limited.
- The UK's new migration regime and increased restrictions on mobility between the UK and the EU affect the ability of UK businesses to employ EU citizens, and for UK service providers to travel to the EU for work. These restrictions carry important implications for a range of services that have previously relied on migrant labour and for activities that rely on frequent travel to the EU.
- Outside the single market, the UK can now set its own regulatory frameworks for services. The government intends to use this freedom to increase the UK's competitiveness by tailoring regulation to the specific needs of the UK economy, particularly in areas such as financial services, technology and green growth.
- As yet, it is too early to assess the success of this strategy but the more the UK diverges from the EU, the less likely the prospects for building on the Trade and Cooperation Agreement and for deepening trade with the EU.
- The UK can now sign new free-trade and bilateral agreements with other countries. However, trade agreements do not typically liberalise trade in services to the same extent as in goods, and services trade is typically greatest with geographically proximate partners. As a result, offsetting any EU trade lost as a result of Brexit with that with non-EU countries will be a challenge.

- Given the long-term implications of Brexit for the UK services sector, the government should learn from the experiences of the transition period and recognise that providing clarity and as much certainty as possible is extremely important for businesses. It needs a clear strategy that is realistic about the prospects, and risks, associated with policy developments in relation to trade, immigration and mobility and regulation of the services sector.

INTRODUCTION

The UK is a services economy. Latest figures [show](#) that services make up 80% of economic output (Gross Value Added) and 82% of employment. Unlike in goods, the UK runs a trade surplus in services. Before the UK's departure from the EU and the Covid-19 pandemic, the EU constituted close to 39% of UK services exports.

This report identifies four main ways in which Brexit is having an impact the UK services sector.

First, under the Trade and Cooperation Agreement (TCA) agreed between the UK and the EU in December 2020, trade in services between the UK and the EU is now more difficult than it was during the UK's membership, with new regulations and paperwork required for businesses to operate in the EU. Membership of the single market offers much more in the liberalisation of services trade than is typical of free-trade agreements. During the Brexit trade negotiations, the EU was clear that it would not allow the UK to retain selective benefits of single market membership, such as market access for financial services, while rejecting freedom of movement. Consequently, the TCA reduces barriers to UK-EU goods trade more than it does for services.

For some sectors, such as financial services and digital trade, decisions made in parallel to the TCA were more significant than the TCA itself. These decisions (what are known as 'equivalence' and 'adequacy' respectively) provide a potential framework for dialogue and greater UK-EU trade opportunities than are currently provided for. However, progress on further negotiations to date has been limited.

Second, Brexit is having profound effects on the UK's labour market. The ending of the free movement of labour precipitated a new UK migration regime and restrictions on mobility between the UK and the EU. These changes affect the ability of UK-based businesses to employ EU citizens and for UK service providers to travel to the EU for work. This is important given that services sectors such as hospitality and financial services employed significant numbers of EU citizens before the end of the transition period. The changes also make business travel and mobility from the UK to the EU more difficult through, for instance, the introduction of visa requirements. To date, this has particularly affected accountants, architects, performing artists and musicians. However, because Covid-19 restrictions have significantly reduced travel more generally, the full impact of these changes is not yet known.

The third area in which Brexit is affecting UK-EU services trade is through UK domestic policy changes as the government exercises its new-found regulatory freedom. Given that it is less than a year since the end of the transition period, the UK's strategy for domestic regulatory reform is in its infancy but it is clearly focussed on financial services, digital services and green growth (in a bid to capitalise on hosting COP-26). The UK has also begun to [diverge](#) from the EU's regulatory framework in areas such as financial services and haulage with the aim of increasing competitiveness by better tailoring regulation to the UK economy. It is too soon to fully assess the success, or otherwise, of this strategy but the greater the divergence away from the EU, and the more businesses adjust to the costs and opportunities this strategy brings, the less likely the prospects for building on the TCA and deepening trade with the EU.

The fourth impact arises from new free-trade and bilateral agreements that the UK signs with other countries. The government has been keen to stress the trade opportunities for the UK beyond the EU as part its 'Global Britain' agenda, but [research](#) shows that trade in services is typically greatest with geographically proximate partners, which suggests that offsetting any lost services trade with the with trade with non-EU countries is likely to be a challenge.

Our report starts by setting out the nature of UK services at the end of 2020 — before the end of the transition period and before the outbreak of Covid-19. This provides a baseline from which the effects of Brexit on UK services to date can be assessed. Next we set out the nature of the new trading relationship with the EU under the TCA, and the decisions made by the EU and the UK that accompanied it. In the following section, the impacts of the ending of free movement and the implementation of the UK's new migration regimes are examined. In the second half of the report, we explore the impacts for specific service sectors that were particularly exposed to Brexit, as well as the UK's policy responses. The final section addresses the emerging shape of the UK services sector post-Brexit and Covid-19. We examine the extent to which the UK's new post-Brexit trade policy adequately promotes its service sector and the tools available to do this through both building on the TCA and signing new trade agreements.

UK SERVICES TRADE UNDER EU MEMBERSHIP

The services sector is characterised by its breadth. It includes high-street services such as retail, hospitality and entertainment alongside business services, such as finance, law and business administration and professional services such as legal services, accountancy and architecture. It also includes tourism and higher education.

The UK is the world's second largest exporter of services (behind the US) and is more dependent on their trade than any other advanced economy. In 2019, before the end of the Brexit transition period, and the onset of the pandemic, the UK ran a trade surplus in services of [£100.4 billion](#).

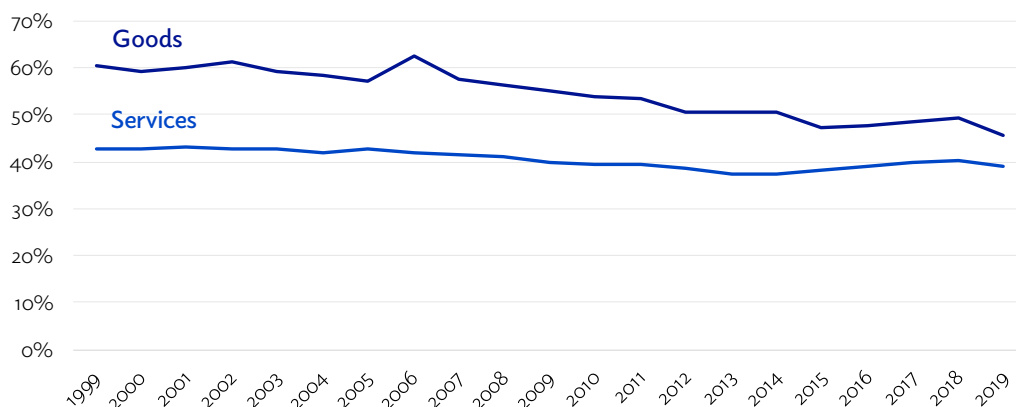
As a member of the EU, the UK pushed for the liberalisation of services trade within the EU's single market, because services trade is typically [greatest](#) with geographically close trading partners. Although the single market does not liberalise services to the same extent as goods trade, it does go much further than is typical for free trade agreements in facilitating the cross-border supply of services.

UK services benefited from this liberalisation. In 2019, the UK had a trade surplus in services with the EU of [£18 billion](#). Services exports to the EU made up 39% of total UK services exports in 2019. As Figure 1 [shows](#), this proportion has remained at a relatively constant 40% since 1999. In contrast, the proportion of UK goods exported to the EU declined during the same period, from 60% in

In 1999, 60% of all UK goods exports were to the EU; this share has generally fallen since.

Figure 1: UK exports with the EU, 1999–2019 (% total).

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Source: ONS Pinkbook 2020.

1999 to 46% twenty years later. However, it is important to remember that the full impact of Brexit on services is unclear because Covid-19 travel restrictions have had a dramatic impact on the way in which services were delivered. Some services pivoted online and others, such as hospitality, were essentially closed during the pandemic lockdowns.

EU MEMBERSHIP AND THE UK'S LABOUR MARKET IN SERVICES

Single market membership significantly shaped the UK labour market. As the Office for National Statistics [notes](#), the precise number of EU citizens working in the UK (as well as citizens from other countries) is hard to pin down. However, it is [clear](#) that free movement meant that EU citizens are an important source of labour across a range of service sectors. Hospitality and transportation have been particularly reliant on EU citizens but higher paid services such as financial services and ICT also employed significant numbers of EU citizens.

Single market membership harmonised regulations between member states making it straightforward for UK citizens to travel and deliver their services in another member state and vice versa. This enabled UK service providers to travel to the EU to deliver services, attend meetings, and offer training, for example, without the need for onerous paperwork, fees and visas. This was important in a range of business and professional services. Businesses could send staff to Europe from the UK on a frequent, short-term basis, often termed 'fly in, fly out' services. Obtaining data on the magnitude and importance of this freedom of travel is difficult but this form of business activity was [valued](#) at around 1.6% of UK GDP in the mid-2010s.

For services that require recognised professional qualifications, such as legal services, auditing and architecture, UK certification was recognised throughout the EU and vice versa during the UK's membership. For seven professions (nurses, midwives, doctors, dentists, pharmacists, architects and veterinary surgeons), mutual recognition of qualifications across member states is automatic, whereas for others — such as lawyers — a process to agree mutual recognition is set out by the Commission. Once recognised, this allowed lawyers based in London, to travel to and work in Paris for a day without the need for a visa or to qualify as a French practitioner.

The UK's negotiating [mandate](#) did not seek to retain the benefits of single market membership for UK services. Instead, it privileged regulatory autonomy from the EU for the UK after Brexit, while aiming to secure more for services than existing EU trade agreements with third parties. This included provisions for a 'pathway for the mutual recognition of qualifications' and the inclusion of audiovisual services within the agreement. This meant that, for some important

service sectors, notably finance, it was evident long before the end of the transition period that even a trade deal would do little to ease UK-EU trade. As a result, financial services firms began executing parts of their no-deal plan well in advance of December 2020, resulting in a more gradual change in trading arrangements rather than a ‘Brexit shock’ at the end of the transition period.

Despite the absence of shocks, the remainder of this report shows that significant changes in UK-EU services trade are unfolding in important ways over longer time scales.

UK SERVICES AND COVID-19

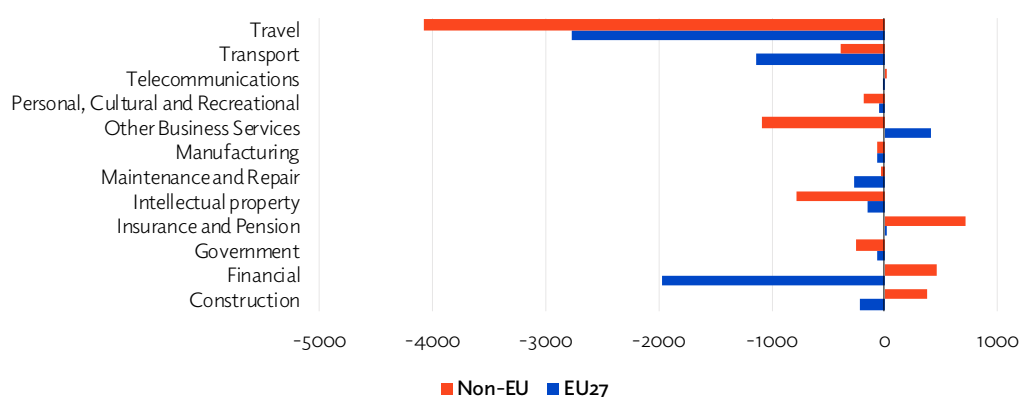
Tracking changes in the service economy has been made more difficult by the pandemic. As in other parts of the economy, the impacts of Covid-19 vary. Overall, output in services as of August 2021, [remained](#) 1.3% below its pre-pandemic level in February 2020.

Focusing specifically on exports, Figure 2 [shows](#) changes in the composition of service exports between 2Q2019 (before the end of the Brexit transition period and before the economic impacts of the pandemic were widely felt) and 2Q2021 (following the end of the transition period). It includes embedded services in manufacturing — such as financing contracts and insurance that often accompany the purchase of goods. Services that relied on the cross-border mobility of people have declined particularly sharply in both EU and non-EU markets — particularly travel and transport — as a result of Covid-19 travel restrictions. Other services that were better placed to move to home-working, such as financial services, have been less impacted by the pandemic lockdowns.

Exports of travel services made up a much smaller proportion of UK services trade in Quarter 2 2021 compared with Quarter 2 2019.

Figure 2: Change in composition of UK services exports, Quarter 2 2019 compared with Quarter 2 2021 (£ million).

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Source: ONS, November 2021.

However, for financial services, it is notable that non-EU exports grew slightly more than EU trade.

The different timings and scale of Brexit and Covid-19 impacts on the UK services sector is reflected in the findings of the “Captains of Industry” survey, conducted by Ipsos Mori for UK in a Changing Europe, between May and September 2021. The sample size is small (63 participants in the services sector at Chairperson, CEO or similar level). 93% of respondents in the services sector felt that the pandemic had had the biggest impact on how their business was run in the previous six months. Views on whether Brexit or Covid would have the greatest impact over five years were more evenly split with 1 in 3 saying Brexit would have the greatest impact and a similar number saying Covid-19 would have the greatest impact. 95% of respondents in the services sector said there had been no positive effects for their business from the TCA agreed in December 2020.

THE IMPACT OF THE TCA AND THE UK'S NEW RELATIONSHIP WITH THE EU FOR SERVICES

UK negotiators did not seek to retain UK membership of the single market or freedom of movement, both of which had benefitted the UK services sector. Instead, they sought autonomy for the UK in regulatory divergence from the EU, with the aim of securing a Brexit dividend that would enable future regulation to be designed to the specifics of the UK economy. This stance was reiterated on 3 February 2020 when Boris Johnson made it clear that the UK would not accept any trade deal with the EU that included 'high alignment' with the EU's regulatory frameworks. This included the UK no longer being subject to the European Court of Justice at the end of the transition period.

The UK's approach to the trade negotiations on the future relationship with the EU was [published](#) in February 2020, and a [draft](#) of its proposed FTA was released in May 2020. These documents reiterated the UK's position that the future relationship between the UK and EU should be based around a Comprehensive Free Trade Agreement (CFTA) together with a limited number of supplementary international agreements in areas such as law enforcement, fisheries and transport.

In services-trade negotiations, the barriers to trade are not customs checks and quotas, as is the case in goods trade (discussed in our forthcoming report on Manufacturing and Brexit).

For services, barriers to trade are so-called non-tariff barriers that regulate both services delivered cross-border and the person delivering them, for example, by specifying the qualifications and work experience of the service provider. Trade agreements in services aim to make delivery of cross-border services easier by reducing (or removing) these barriers, by, for example, recognising qualifications from other jurisdictions so that individuals no longer require checks and paperwork. They also include provisions that make it easier to establish an office overseas.

The UK negotiating team emphasised that it was seeking an agreement based on existing EU free trade agreements, particularly the EU-Canada Comprehensive Economic and Trade Agreement (CETA) and the EU-Japan Economic Partnership

Agreement (EU-Japan EPA). In some areas, the draft text published by the UK was in fact identical to CETA. However, reflecting the comparative strength of UK services, it sought greater market access than had been provided by the EU previously in some areas. For example, the UK wanted to make it easier for UK professionals such as lawyers and architects to work in the EU than is the case for individuals holding Canadian qualifications. The UK also sought greater sectoral coverage than the EU has agreed with other countries. For example, the UK wanted to include the audiovisual sector within the deal, something that the EU has not yet agreed with other third countries.

The EU favoured a single, comprehensive agreement, reflecting its commitment to ensuring that agreements in different areas were linked within the trade deal. In particular, the EU was clear that the UK could not enjoy selected benefits of single market membership related to particular activities, such as financial services, without adhering to all of the obligations of single market membership, in particular the free movement of labour. In 2018, President Macron [stated](#) that “there should be no cherry-picking in the single market because that’s a dismantling of the single market”.

THE TCA AND THE SERVICES SECTOR

The TCA was agreed in December 2020. It closely reflects pre-existing EU agreements with Japan and Canada and contains more provisions for goods trade than it does for services, as our forthcoming manufacturing report shows. For services, it includes provisions in important areas such as digital services, mobility for specific types of business travellers (dependent on the activity they are undertaking and the EU member state they are travelling to) and in relation to intellectual property. It is also accompanied by side-agreements on financial services and data, which is discussed in more detail below. Overall, however services trade between the UK and the EU has become much more difficult than it was before Brexit through the increase in non-tariff trade barriers.

For example, with regard to professional qualifications, limited provisions were made to support the mutual recognition of UK legal qualifications by the EU but for other professions, the TCA follows the model of CETA. In so doing, it sets up a framework for a future process to decide if qualifications can be mutually recognised but does not grant recognition immediately. This means that many UK services providers such as architects, accountants and auditors no longer have their qualifications recognised in the EU, and this does not seem likely to change in the short term.

Some critical decisions for services lie outside the scope of the TCA. In financial services, a Joint Declaration on Financial Services Regulatory Cooperation

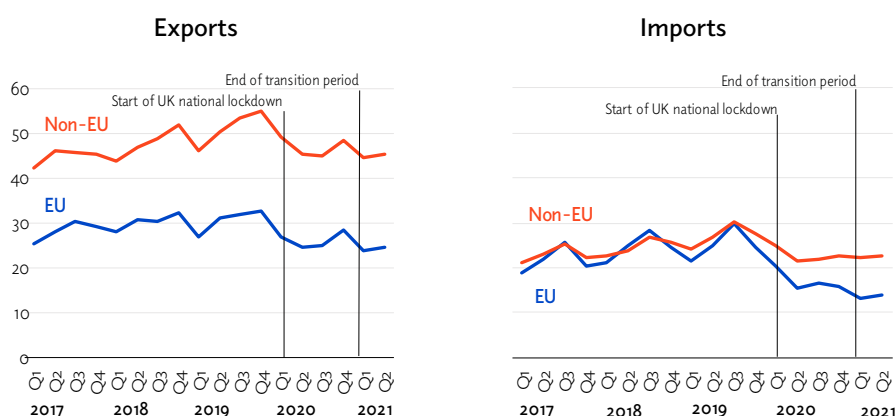
between the UK and the EU was published alongside the TCA. This committed both parties to agree to a memorandum of understanding (MoU) that would establish a framework for structured dialogue on financial services regulatory cooperation by 2021. Both parties have indicated that a text has been agreed in principle, but there has been no formal announcement or publication. Decisions on the terms of EU market access for UK financial services firms and vice versa, also fall outside the TCA. However, whereas the UK has granted widespread access for EU financial services firms, the EU has not reciprocated, even though many felt at the time that agreeing a trade agreement would make such decisions more likely.

Implementation of the TCA is at an early stage and it is hard to fully understand its impact on services because of the ongoing impact of COVID-19 on services. UK service exports globally in 2Q2021 were [down](#) 14.2% on the same quarter in 2019. The equivalent figure for imports is 29.3%. However, there are [signs](#) that larger declines are impacting UK-EU trade as compared with UK-non-EU trade, suggesting that Brexit is having an impact as shown in Figure 3. Over the same two-year period, UK service exports to the EU were 20.3% lower compared with 10.5% for trade with non-EU countries. Imports of services from the EU were down 43.7% over the same period. Services imports from non-EU countries were down 16% over the same two-year period.

UK service exports and imports have decreased since 2019 to both EU and non-EU countries.

Figure 3: UK exports and imports of services to EU and non-EU countries, Quarter 1 2017 to Quarter 2 2021 (£ billion).

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Source: ONS, November 2021.

UK REGULATORY AUTONOMY AFTER BREXIT

The UK government's stated [aim](#) is to deliver a Brexit dividend by tailoring regulation to the specific nature of the UK economy with the aim of stimulating innovation, competitiveness and foreign investment. We are only in the early

stages of learning precisely what form these changes will take, but there is no evidence as yet that they would offset the loss of services trade with the EU, as reflected in the OBR's forecasts on Brexit impacts.

Early insights into the government's strategy for post Brexit regulatory change can be found in the recent published Taskforce on Innovation, Growth and Regulatory Reform (TIGRR) [report](#). TIGRR was created by Boris Johnson in February 2020 to 'scope out and propose options for how the UK can take advantage of our new-found regulatory freedom'. Led by the Conservative backbench MP Iain Duncan Smith, its 130-page report sets out 'ways to refresh the UK's approach to regulation' to stimulate 'innovation and growth' after Brexit. It makes a number of recommendations for services. For example, financial services and clinical trials are the sectors for which the largest number of recommendations are made (15 each) whereas five are made in relation to mobility and transport.

The government also created a Brexit Opportunities Unit within the Cabinet Office in May 2021, reporting to Lord David Frost. The unit is intended to shape the UK's post Brexit regulatory strategy as well as to scrutinise the impacts of regulatory changes and new trade deals agreed by the UK. Its overall aim is to ensure that these changes simulate innovation and increase the competitiveness of the UK after Brexit.

It is also important to note that, unlike for trade in goods, the TCA applies to Northern Ireland for services. This is significant because in [2019](#), 75% of Northern Ireland's GVA came from services, and services made up 22% of external sales by Northern Irish firms (that is, sales to either Great Britain or the EU). Northern Ireland service providers face largely the same new barriers to trade with the EU, including with the Republic of Ireland, as their counterparts in the rest of Great Britain. However, there are some areas of difference that reflect the close trading ties across the island of Ireland. For example, under the TCA, UK road haulage operators were only [permitted](#) to undertake one loaded journey within an EU member state under what are known as cabotage rules. However, Northern Ireland based operators are allowed to undertake two of these types of journeys within Ireland and the TCA allows for the continuation of cross-border passenger transport services.

IMMIGRATION, FREE MOVEMENT AND LABOUR MOBILITY

The Trade and Cooperation Agreement does not cover immigration and labour mobility. Instead, immigration to the UK for work is governed by the new “points-based” immigration system introduced on 1 January 2021. The key provisions of the new system are that

- new migrants must have a job paying more than £25,600 p.a. or the lower quartile of the average salary, whichever is higher, and be in an occupation requiring skills equivalent to at least A-level standard (“RQF3”);
- there will be a lower initial threshold for new entrants and for those in shortage-occupations, meaning that for some occupations the salary threshold may be as low as about £20,000 p.a.;
- there will be a lower threshold for those with doctorates, especially in STEM subjects;
- for the National Health Service and education sectors, there will in effect be no salary threshold. If the job is at an appropriate skill level, then paying the appropriate salary according to existing national pay scales will suffice;
- there will be an expanded Seasonal Agricultural Workers Scheme, but no other sectoral schemes for workers who do not meet the skill threshold, and in particular not for the social care sector or other sectors particularly dependent on migrant workers.

In other words, EU citizens no longer have the automatic right to work here; they will have to qualify under the rules above, which represent a much more restrictive regime. Importantly, however, EU citizens who were resident in the UK on or before 1 January 2020 were eligible to apply for ‘settled’ or ‘pre-settled status’; over 6 million such applications have been [made](#), and over 5.4 million applications have been [approved](#) as of the end of October 2021.

The sectoral and regional impact of these changes for UK services will vary considerably:

- Hospitality and transport are particularly dependent on EU-origin

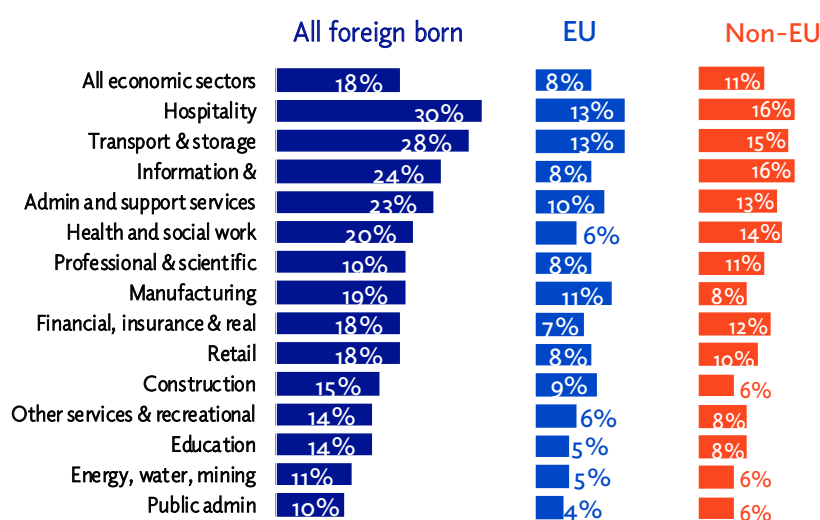
workers, who make up more than 1 in 8 of the workforce. Turnover is also relatively high in these sectors.

- EU-origin workers are highly concentrated in London, constituting one in six of the workforce. Importantly, they are employed not just in sectors like hospitality; they comprise 15% of the workforce in finance and only slightly less in ICT.
- It is a common misconception that EU migration is primarily for “low-skilled” (or low-paid) work. In fact, although EU-origin workers are more likely to be employed in low-skilled jobs, about half are in ‘high-skilled’ or ‘medium-high skilled’ occupations — only slightly lower than the UK average.

Foreign workers make up 18% of the UK workforce across all economic sectors.

Figure 4: The percentage of workers per sector who are foreign born, from EU and non-EU states.

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Source: Migration Observatory analysis of the Annual Population Survey 2019.

In the short term, the impact of changes to immigration rules has been largely hidden by the pandemic. Since the ending of almost all Covid-19-related restrictions, there have been consistent reports of staff and skill shortages as businesses reopen. Meanwhile, the number of EU-origin workers on company payrolls (which omits the self-employed) fell by about 200,000 in 2020. Although the exodus of EU workers in 2020 was primarily driven by the pandemic, their failure to return (or to be replaced by new migrants) is likely to be driven by Brexit. Consistent with this, sectors particularly dependent on EU workers — accommodation and food services, transport and storage — have reported particularly high levels of vacancies. Chronic staff shortages in social

care also appear to have worsened. The most visible impact has been on HGV drivers, where shortages — partly but not wholly due to a fall in the number of EU-origin drivers — have led to significant blockages in supply chains.

However, conditions in the immediate aftermath of the reopening of the economy will, almost by definition, be temporary and transitory. Longer term impacts are less certain. The government's response has been to argue that employers should respond by raising wages and/or increasing productivity, however, the scope for doing so in these sectors may be limited. If labour supply is indeed reduced more than demand, then there are a variety of possible responses: higher employment for UK-origin workers, higher wages (which in turn would likely mean higher prices), higher productivity, or lower output/fewer businesses. The Office of Budget Responsibility was pessimistic, noting that although “shortages of labour or other inputs may catalyse productivity improvements in some businesses, there is little evidence that supply constraints drive up economy-wide productivity or real wages. For instance, higher levels of immigration are generally found to have a positive effect on productivity.”

Consistent with this, the empirical evidence suggests that the main impact of the ending of free movement will be through lower overall employment and output. There will be no significant increase in employment for the UK-born population; there will be some, but probably a rather small, increase in relative real wages for workers in the most affected sectors (offset by an even smaller fall in relative real wages for other workers who consume the outputs of those sectors). Finally, there will be no offsetting increase in productivity (indeed, as discussed above productivity, may even fall).

However, although the end of the freedom of movement will present a major challenge for some sectors, it is important to remember that the new immigration regime represents a considerable liberalisation for non-EU migrants, with lower salary and skill thresholds, and no overall cap on numbers. Approximately 68% of UK employees work in occupations requiring RQF3 level skills or above. The requirement for new migrants to be paid at or above the lower quartile of earnings for an occupation implies about half of all full-time jobs would, in principle, qualify an applicant for a visa.

This represents a substantial increase of opportunity — perhaps double that under the previous system for non-EU nationals, which was, for most of the 2012-19 period, subject to an overall quota and a resident labour-market test designed to ensure that UK-settled workers, including EEA nationals, had the opportunity to apply for vacancies before other groups of migrants. It also makes the new system considerably more liberal with respect to non-European migrants than that of most EU member states, which typically apply much more restrictive

(de facto and/or de jure) skill or salary thresholds, and often enforce a resident labour-market test. This could, in principle, be of considerable benefit to the UK, particularly to sectors like financial services and ICT, which employ substantial numbers of non-EU nationals, and could expect to benefit from a simpler and less restrictive system.

LABOUR MOBILITY

The TCA also introduces a much more restrictive regime for shorter term labour-market mobility to deliver cross-border services compared to single market membership. UK nationals are only permitted to travel to the EU to deliver services within the EU, if they fall into one of five specified categories [listed](#) below:

- business visitors for establishment purposes — i.e., those going to help their own company set up a business in the host state;
- intra-corporate transferees (ICTs) — i.e., managers or trainees being sent temporarily to another part of the company in another state;
- contractual service suppliers (CSSs) — e.g., those providing services on behalf of a UK company in France;
- independent professionals (IPs) — e.g., UK self-employed professionals providing services to a German consumer;
- short-term business visitors (STBVs) — e.g., those attending meetings, training seminars, trade fairs in another state.

Each of the five categories also comes with a list of conditions and rights. For example, a business visitor for establishment purposes must hold a senior position in their company, an independent professional must have 6 years professional experience and a degree, or an equivalent qualification, plus a professional qualification. Short-term business visitors must not obtain remuneration from a source located in the host country or sell goods or services to the general public without a visa or a work permit. Short-term business visitors have the right to a 90-day stay within a six-month period, whereas contractual service providers are entitled to a cumulative period of 12 months or the duration of the contract — whichever is the shorter of the two.

There are also a significant number of country-specific restrictions set out in over 200 pages of highly technical annexes in the TCA that restrict business mobility. In practice, this means professional and business services are dealing with 27 different trading regimes rather than a single EU one. For [example](#), a UK management consultancy working in Austria must satisfy an ‘economic needs test’ showing no EU firm can carry out the work. For accountants and

bookkeepers in Italy, residence or business domicile is required for enrolment in the professional register, which is necessary for the provision of accounting and bookkeeping services.

Different and more liberal terms apply to labour mobility between the UK and Ireland because of the Common Travel Area between the two countries. This was established before the UK and Ireland joined the EU and continues to apply. Citizens of Ireland and the UK continue to be able to travel and work freely across the two jurisdictions.

Taken together, the UK's new points-based immigration system, alongside the more restrictive labour mobility framework under the TCA, makes it more difficult for some parts of the services sector to employ EU nationals, and more difficult for UK citizens to travel to sell their services in the EU. The resulting shortages in the labour market may be filled by new immigration patterns between the UK and non-EU states. However, the implications of changes for the UK labour market are yet to emerge, changes that are also entangled in the consequences of COVID-19. Some EU nationals have left the UK to be closer to family during the pandemic, and travel restrictions brought into manage virus transmission mean that the implications for businesses of the labour mobility aspects of the TCA are only now beginning to be explored in practice.

KEY ISSUES FOR THE UK SERVICES SECTOR IN THE TCA

Brexit's impact will vary depending on the type of service activity being considered. In the following, we consider some of the main issues for specific parts of the UK services sector before assessing its future prospects.

FINANCIAL SERVICES

Finance is a diverse sector that has been particularly important for UK economic growth for at least the past thirty years. In 2019, financial services contributed [£132 billion](#) to the UK economy — close to 7% of the UK's total economic output, though this is less than its peak contribution of 8.4% in 2009.

Half of this output was generated in London but there are also significant clusters in cities such as Edinburgh, Leeds and Manchester, and towns such as Swindon, Bournemouth and Northampton. In the first quarter of 2020, there were 1.1 million people employed in financial services, 3.2% of total UK jobs.

Financial service exports are a vital area for the UK economy. In 2019, the UK ran a trade surplus in financial services of £41 billion.

Financial services trade under EU membership

During its EU membership, the UK developed significant EU exports in financial services thanks to the passporting arrangements in place. Passporting allowed firms to sell their services into the EU from their UK base without the need for additional regulatory clearances.

The EU accounted for 40% of UK financial services exports (£24 billion) and 32% of UK financial services imports (£6 billion) in 2019.

However, while the majority of financial service providers, particularly in the areas of banking and insurance, favoured remaining in the EU, other parts of the sector — notably hedge funds — identified opportunities through the domestic regulatory control leaving the EU would bring.

Financial services and the TCA

Following the Political Declaration of October 2019, agreed by the UK and the EU alongside the Withdrawal Agreement, it was clear that UK financial services would lose their passporting rights into the single market. It was also clear that these would not be replaced under the terms of the TCA and that, instead, single

market access for UK firms — and access to the UK market for EU firms — would be governed through equivalence decisions.

Equivalence is not decided through bilateral negotiation but by each party independently deciding what access it will grant. Equivalence does not provide a full replacement for passporting. Even if it is granted, equivalence as set out by the EU does not cover the full range of financial services. Core banking services, such as lending, payments and deposit taking are excluded. Neither does equivalence grant permanent access rights. The EU can withdraw equivalence determinations with 30-days' notice.

Given that the UK was equivalent to the EU up until the point it left the single market, it could have technically expected the EU to make positive equivalence determinations. However, the EU has taken a restrictive approach, reflecting its concerns that the UK is seeking to obtain competitive advantage through divergence from EU regulation in the future. The EU only granted time-limited equivalence decisions for derivatives clearing (for 18 months) and settling Irish securities (for an initial 6 months and now expired). Both these decisions were driven by the need to avoid short-term disruption within the EU.

In contrast, the Chancellor, Rishi Sunak, announced in November 2020 that the UK would be adopting a more liberal approach, granting equivalence from 1 January 2021 to EEA-based financial services in a range of areas as shown in Figure 5. This reflects the UK's wider strategy of significantly liberalising inbound services trade. The UK has also made clear that its approach to equivalence differs from that of the EU, implicitly criticising the EU's approach in the process. For example, as part of a wider emphasis on the importance of transparency and outcomes within the UK's approach to equivalence, the Treasury has said that the withdrawal of equivalence would be considered only "as a last resort" and would be accompanied by adaptation periods, rather than the 30 days' notice period of the EU approach.

The limited number of equivalence decisions granted by the EU means that UK financial services trade has less single-market access than other leading international financial centres such as New York and Singapore. As of [February 2021](#), the US has 21 equivalence decisions from the EU, Singapore has 15, whereas the UK only has two. The profoundly different equivalence regimes being applied to London suggests that the EU's approach to the UK may be motivated more by concerns to develop its own competencies in financial markets than by the merits of the UK's domestic approach to regulation.

The UK has implemented a Temporary Permissions Regime, currently scheduled to run for three years until the end of 2023. This allows EEA firms and funds that

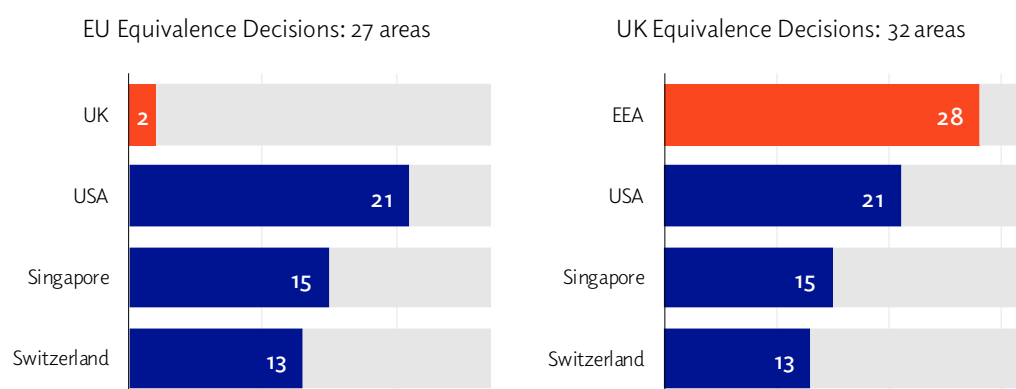
were using a passport to access the UK market during the transition to continue to do so, provided they notified the Financial Conduct Authority that they would use the permissions regime before the end of transition. There is no equivalent EU-wide scheme for UK firms operating in the EU, although some member states, such as Ireland and Denmark, have [established](#) temporary permissions for UK firms that were passporting into particular parts of financial markets for specific periods of time from 1 January 2021.

As it became clear during the trade negotiations that the UK's passporting rights would be withdrawn and be replaced by limited equivalence decisions, financial services' activity began to relocate from London to European cities, notably Frankfurt, Amsterdam, Luxembourg, Paris and Dublin as well as other global centres such as New York. Although official statistics do not track these relocations systematically, a range of other information sources reveals the changes to date.

The UK has granted the EEA equivalence in 28 areas whereas the EU has granted the UK equivalence in only two areas.

**UK IN A
CHANGING
EUROPE**

Figure 5: EU and UK Equivalence Decisions.



Sources: European Commission (10/02/2021); HM Treasury (14/01/2021).

[Research](#) indicates that around 7,500 jobs in financial services have left the UK for the EU since 2016 involving relocations from within 440 firms. Given the difficulties of obtaining reliable data, this is likely to be a conservative estimate and is a small proportion of the 1.1 million jobs in financial services. The figures also do not account for new jobs created outside the UK that would have been in the UK without Brexit. Bank assets valued at £900 billion have been relocated, equal to around 10% of the UK's banking system, although this does not translate into a commensurate relocation of economic activity (as measured by employment or value-added). There are also [reports](#) that financial institutions are intending to resume relocation activity into the EU as the height of the

Covid-19 pandemic eases, suggesting that it will take some time for the final post Brexit footprint of financial services between the UK and the EU to emerge.

No single European city has emerged as the stand-out competitor to London. Instead, there is evidence of different specialisations emerging, with Frankfurt dominating in banking and Dublin in asset management relocations. Amsterdam has dominated in the relocation of activity that supports financial market transactions — so-called market infrastructure. Amsterdam overtook London as the primary location for European share trading in January and London's derivatives platforms lost three-quarters of their euro volumes to Amsterdam and New York.

Recent figures from the Office for National Statistics [show](#) that a realignment of UK trade in financial services away from the EU to other geographical markets appears to be underway. Between 2Q2019 and 2 Q2021, non-EU exports of financial services increased by £0.5 billion (5.1%) and imports by £0.01 billion (0.4%). Over the same period, EU exports declined by £2.0 billion (-30.6%) and EU imports by £0.3 billion (-21.3%). ONS analysis [suggests](#) that the decline in financial services trade with the EU is being driven by declines in exports to France, Ireland, Germany and the Netherlands.

Building on the TCA in financial services

The TCA is accompanied by a non-binding Joint Declaration committing the UK and the EU to cooperation on matters of financial regulation. This is intended to be facilitated by a memorandum of understanding (MoU). However, although the UK government [announced](#) that the technical discussions underpinning the MoU had successfully concluded in March 2021, no formal text has emerged.

An MoU is not unique to UK-EU trade in financial services. Similar commitments are in place between the EU and the US and Japan, for example. However, a general commitment to regulatory cooperation is no replacement for certainty regarding single-market access for UK financial services firms.

Further equivalence decisions from the EU do not appear likely. Despite the UK being equivalent at the point of departure, the EU has [stated](#) that it requires further information in order to make equivalence decisions.

The EU is also keen to attract more financial services activity into the single market, partly in order to prevent possible systemic risks associated with not having core financial market activity that it relies on outside its own regulatory border. This is particularly true in relation to clearing. Currently the one area of equivalence granted to the UK by the EU is in clearing, which is due to expire in June 2022. This allows EU traders to use the more liquid clearing infrastructure

available in London. The EU granted this to prevent market instability at the end of transition, but needs to develop its own capabilities in this area. In a sign that this has proved difficult, the EU's commissioner for financial services, Mairead McGuinness announced in November 2021 that she would recommend an extension to this particular equivalence decision. However, she also reiterated the need for the EU to develop its own capabilities, stating that in 2022 she would bring forward measures aimed at increasing the EU's competitiveness in this area.

Meanwhile, there are signs that the UK will diverge from EU financial services regulation. In summer 2021, Rishi Sunak appeared to confirm that the UK intends to prioritise regulatory freedom over potentially [enhanced](#) single-market access for financial services in his Mansion House [speech](#). The June 2021 Taskforce on Innovation, Growth and Regulatory Reform (TIGRR) also contains a number of recommendations for changes to the UK financial regulatory framework. This includes changes in the rules governing the relationship between researchers and advisors in investment firms, currently set under EU law through in the Markets in Financial Instruments Directive (MiFID II), which the UK retained after Brexit. The UK's proposals for MiFID II are similar to those of the EU's 'quick fix' package approved in March 2021, but are more flexible in scope, particularly for smaller firms. TIGRR also suggests the UK should adopt a more Australian-style approach to open banking by tailoring the regulatory requirements of firms to their size to encourage the growth of smaller challenger banks — something not possible under EU regulation.

Further details of how such regulatory opportunities will be exploited by the UK were set out in [Sunak's](#) 'New Chapter for Financial Services' published in July 2021. This identifies both sectoral and geographical foci for financial services post Brexit, with Sunak arguing that the UK should "push for closer co-operation and more cross-border access with other like-minded financial centres in markets around the world".

In terms of sectoral foci, the UK Treasury is keen to cement the UK's position as a global fintech hub and is also working to make the UK the main global centre for sustainable finance. Work on fintech has coalesced around the Kalifa Review that seeks to [support](#) the fintech sector through 15 recommendations across five policy areas: policy and regulation, skills and talent; investment; international attractiveness and competitiveness; and national connectivity. Recent [data](#) show that in 2021 the UK is second to the US in terms of investment in fintech. Concerns remain, however, about the supply of highly skilled labour in this area, as fintech was particularly reliant on EU nationals.

The UK government is also keen to use the hosting of COP26 in Glasgow in November 2021 to underscore the UK's leadership position in green and

sustainable finance. The government published its [Green Finance Framework](#) in June 2021, setting out plans to finance expenditures on sustainable technologies and infrastructure through the issuance of green gilts and the retail Green Savings Bond launched in October 2021. The inaugural [sale](#) of two green gilts raised £16 billion in October 2021. The government has also published its [Greening Finance Roadmap](#), which sets out the plans for economy-wide Sustainability Disclosure Requirements (SDR) in which firms across sectors will need to report on sustainability. It also includes plans for a UK Green Taxonomy to list all economic activities that UK regulators consider to be environmentally sustainable.

At one level, this roadmap reflects the UK's post-Brexit ambitions to use its new-found domestic regulatory control to set international financial standards through engaging with and shaping international regulatory architectures. The roadmap includes provisions to align the UK's new SDR with the international Task Force of Climate-Related Financial Disclosures framework which was developed at an international level with significant input from the UK through the Financial Stability Board.

The green taxonomy is essentially a classification system that set out the criteria that economic activities need to meet to be classified as environmentally sustainable. The structure of the UK's taxonomy will draw on the existing EU Green Taxonomy to which the UK contributed as a member state, but [will](#) 'take an approach that is suitable for the UK market and consistent with UK government policy'. This signals the possibility of divergence in approach and/or scope from the EU.

In terms of geographical reach, the UK has adopted a bilateral strategy based around regulatory dialogue. So far, the UK has agreed a UK-Singapore Financial Partnership [aimed](#) at using regulatory cooperation to increase bilateral financial services trade. The UK has also announced that it is pursuing mutual recognition of regulatory standards with Switzerland. This is an important set of negotiations because, if agreed, it would facilitate financial services trade liberalisation similar to that within the EU — including passporting between the UK and Switzerland — but on a bilateral basis and without the political architecture of the EU. As such, it is seen as a potential template for UK financial services agreements elsewhere.

In terms of new trade deals, the UK-Japan Comprehensive Economic Partnership Agreement (CEPA) signed in October 2020 contains some important financial services elements that are not generally contained in trade agreements. For example, it prohibits requirements that mandate the local storage of data held

by firms (with some exceptions for public purposes) and includes measures to facilitate the free transfer of this data between the two countries. Data mobility is important in banking and payment businesses that operate across multiple jurisdictions and is becoming increasingly important with the growth of digital payments. The free trade agreement with Australia, agreed in June 2021, includes an annexe aimed at fostering regulatory cooperation on financial services regulation.

However, there are some policy areas, notably in relation to EU regulation on bankers' bonuses, where the UK could now diverge from the EU but has chosen not to do so. A reflection of the domestic political [optics](#) of not being seen to use a Brexit regulatory dividend to enhance bankers' salaries, while at the same time emphasising government ambitions to 'level up' the UK economy.

In sum, a deregulatory race to the bottom, or a form of widespread deregulation as happened under Big Bang in the 1980s, seems unlikely in UK financial services. Piecemeal regulatory changes will and are being made, particularly where they link to other key policy objectives in relation to digital and green growth. Even so, it seems likely that these changes will not be sufficient to offset lost financial services exports to the EU. It will take some time to assess this outcome, but it does seem likely that London will be a smaller, albeit still large, financial centre in the medium term.

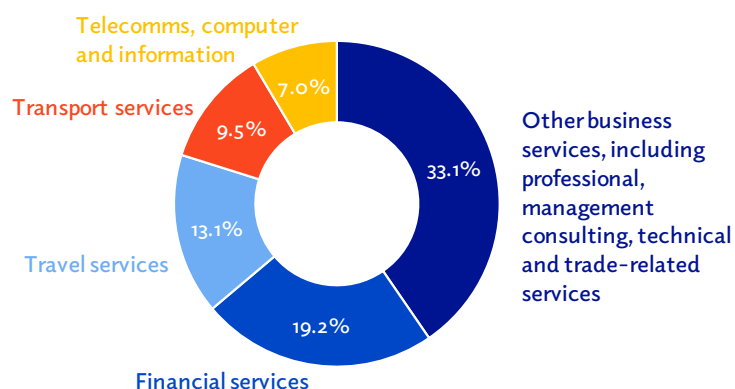
PROFESSIONAL AND BUSINESS SERVICES

The Professional and Business Services sector (PBS) consists of a range of knowledge-intensive industries and support functions, providing highly skilled and specialised services to businesses and the public sector. It includes accountancy, architecture, auditing, call centres, credit services, event organisers, legal services, management consultancy, market research and recruitment services, among others. The sector is often included as an addendum to financial services, although it is a distinct sector in its own right. However, it is closely linked to financial services, particularly in London and the South-East. The PBS sector also supports trade in goods by offering legal advice on trading in a new territory or through the after-care services offered with the purchase of manufactured goods.

PBS is an important component of the UK economy and the sector is the largest source of services exports. London and the South-East alone account for around 50 per cent of these exports, with the rest from other parts of the UK. These exports were valued at [£105 billion](#) in 2019 — 33 per cent of all service exports — higher than financial services. The UK is [second](#) only to the United States in the total value of its PBS exports.

Business services made up approximately one third of UK services exports in 2019.

Figure 6: Top 5 UK services exports (2019).



Source: Department for International Trade, UK Trade in Numbers, February 2021.

The latest available figures show that, before Brexit, the EU was the largest market for UK exports of PBS, accounting for 37 per cent of the sector's exports. The US, which is the largest single destination for UK exports, received 28 per cent of PBS exports. The UK ran a trade surplus of £12.4 and £10.6 billion with these markets respectively in 2019. Accountancy, legal services and management consultancy are particularly reliant on the EU market for exports.

Professional and Business Services trade under EU Membership

An important distinction within the PBS sector, for those seeking to export services, is between tightly regulated professions that clearly specify who is able to provide services and those professions without such proscription. In the case of tightly regulated professions, such as legal services, the Mutual Recognition of Professional Qualifications within the EU made it easier for UK lawyers to practise in EU/EEA countries without an onerous requalification process or visa restrictions. The transition period enabled professionals practising in EU/EEA countries to have their qualifications recognised but this is not available for newly qualified professionals after Brexit. Early career architects, engineers or auditors now have less ability to work in the EU than their more senior colleagues.

At the other end of the spectrum are more loosely regulated professions and business services such as management consultancy, advertising and public relations. These professions do not require a qualification that is recognised by the member state to deliver their service within the EU. Under EU membership, the benefits for these sectors lay not in the mutual recognition of qualifications, but in the freedom movement rules. The ability to move people quickly to forge relations with clients, set up teams or change filming locations without visa

restrictions or national employment requirements was a significant facilitator of exports in these sub-sectors.

Professional and Business Services and the TCA

For professional business services such as audit and architecture, the ending of the Mutual Recognition of Professional Qualifications has erected new trade barriers with the EU. The UK had pressed for automatic recognition to continue in the TCA, but the EU refused. Instead, a process similar to that in the CETA was reached, whereby professional bodies will have to separately negotiate mutual recognition agreements. This is likely to be a drawn-out process: so far only the [architecture](#) profession has started the process. The only exception in the TCA is for lawyers. The TCA allows British lawyers to practise under their UK title and provide advice in the EU on UK and international law. However the Law Society of England and Wales has [warned](#) that some EU member states have restrictions and exemptions set out in the TCA, which could limit the ability of lawyers to use their home title to practice in these jurisdictions.

Legal services face further uncertainty because the UK's application to the Lugano Convention was turned down in summer 2021. This sets out which countries' courts have jurisdiction in cross-border civil and commercial disputes between the EU, Denmark, Iceland, Norway and Switzerland. It also ensures that ensuing judgements can be enforced overseas. This means that the process of litigating cases that involve both UK and EU parties is likely to become more complex.

Disentangling the impact of the TCA from that of the pandemic is fraught with difficulties for a sector that used the labour mobility facilitated through single market membership to develop significant EU export markets from its UK base. In an early attempt to isolate the impact of Covid-19 from the new trading arrangements, the [ONS](#) used business surveys on exports between June 2020 and April 2021. The number of PBS businesses reporting normal export activity fell from 59 per cent in December to 54 per cent in January. This recovered in February to the level before the transition period ended in December, suggesting that the Covid-19 impacts in this area may be waning — it remains to be seen precisely what form Brexit impacts take and for how long.

The UK's approach to recognising overseas professional qualifications is based on that of the EU, which was incorporated into UK law as part of the withdrawal legislation. The government [consulted](#) on the future UK framework for the recognition of professional qualifications and the regulation of professions in September and October 2020. This consultation [led](#) to a policy paper that set out how the UK can 'take advantage of the flexibility that

the UK has being outside of the EU'. As a result, the government introduced the Professional Qualifications Bill in Spring 2021, which sets out a new framework for recognition of professional qualifications obtained outside the UK. This now differs from the EU's approach in that it emphasises the need to target recognition on shortage professions and to open up pathways to mutual recognition with partners outside the EEA. The Bill is passing through the House of Commons at the time of writing.

Building on the TCA in professional and business services

Some professional bodies have begun to try to build on the provisions within the TCA. The UK Architect's Registration Board and the Architects Council of Europe have set up a joint task force aimed at making preparations for a mutual recognition of qualifications agreement. The Law Society of England and Wales is exploring the potential for an agreement with the Council of European Bars and Law Societies on whether bilateral agreements could be made. There is no [agreement](#) amongst legal experts as to whether bilateral mutual recognition could be sought for particular sectors between the UK and individual member states, despite some trade bodies suggesting that a network of bilateral agreements could be developed.

This suggests that any future development towards the mutual recognition of qualifications and, by extension, the impacts of the TCA on professional and business services, are going to take some time to emerge.

DATA AND DIGITAL SERVICES

The flow of personal data between the UK and EU is vital for both economies. Data flows are at the heart of most trade in goods and services. They include cloud-based emailing and data storage; payments processing, data processing in core business functions such as human resources and the analysis of data to assist with order tracking and supply chain management.

Data, digital services and the TCA

As a third country, the UK now requires an 'adequacy decision' from the EU to facilitate the free flow of personal data from the EU to the UK without further safeguards being required (the UK designated EU and EEA member states as 'adequate' in relation to its data prior to the end of transition). The EU's approach to data and data adequacy is set out in its General Data Protection Regulation (GDPR), which protects the rights of EU citizens by insisting on the highest standards for data protection in situations when an EU citizen's personal data is processed. The Commission assesses a third country's data protection and, if deemed equivalent to EU standards, adequacy can be granted.

It was therefore a relief to British and EU businesses when the TCA included a six month ‘data bridge’ enabling the continued flow of personal data from the EU to the UK after the transition period ended in December 2020, until an adequacy decision was reached by the EU Commission. There was further relief when the EU Commission published two draft adequacy decisions for the UK on 19 February 2021, which were then adopted on 28 June 2021 — one under the GDPR and the other for the Law Enforcement Directive. This was based on the EU’s [assessment](#) the UK’s data protection system ‘continues to be based on the same rules that were applicable when the UK was a Member State of the EU’. This was to be expected given the UK had fully incorporated the principles of the GDPR into UK law. There were some reservations on the part of EU counterparts regarding the access of personal data by public authorities in the UK, particularly for security reasons. The UK was able to offer appropriate safeguards, such as the requirement of prior authorisation for data collection from an independent judicial authority.

However, for the first time, the adequacy decision granted by the EU Commission contains a ‘sunset clause’, limiting its duration. The decision will expire four years after coming into force. Renewal will be contingent on the UK continuing to ensure adequate levels of data protection from the perspective of the EU Commission. The Commission will also continue to monitor the legal situation around data protection in the UK and will intervene if it believes the UK has deviated from its current level of protection. The unilateral nature of the adequacy decision also means that the EU could, in principle, choose to terminate it at any time for reasons unrelated to the substance of the UK’s data protection regime, for example if the current dispute with respect to the Northern Ireland Protocol escalates further.

Building on the TCA in data and digital services

The Taskforce for Innovation, Growth and Regulatory Reform (TIGRR), which was given the task of exploring opportunities for regulatory divergence now the UK has left the EU, has recommended the UK replace GDPR with a new ‘UK Framework of Citizen Data Rights’ — an approach that has been [supported](#) by Lord Frost. The taskforce argues that GDPR is prescriptive and inflexible, undermining the opportunity Brexit gives the UK to be a world leader in data and evolving technologies such as Artificial Intelligence and blockchain (a form of distributed ledger technology that underpins crypto-currencies such as bitcoin). The taskforce takes particular issue with Article 22 of GDPR, which guarantees that people have the right to a human review of an algorithmic decision. Examples of such decisions given in the UK GDPR [include](#) an online decision to award a loan or a recruitment aptitude test, which uses pre-programmed algorithms and

criteria. Article 22 of GDPR stipulates that individuals should ‘[not] be subject to a decision based solely on automated processing, including profiling, which produces legal effects concerning him or her, or similarly significantly affects him or her’. TIGRR argues ‘this requirement makes it burdensome, costly and impractical for organisations to use AI to automate routine processes because they must also have a manual process for individuals who opt out of automatic processing’.

The emphasis on tailoring UK regulation to reflect the distinctive nature of the UK economy set out in the TIGRR report is reflected in a [consultation](#) on proposals set out to reform the UK’s data governance framework after Brexit by the Department for Digital, Culture, Media and Sport in September 2021. The government is planning to diverge from GDPR by developing a ‘[light touch](#)’ approach. The proposals set out a new approach to making adequacy decisions for the UK, with priority placed on reducing administrative burdens for businesses and individuals as well as identifying a list of countries with which the UK will prioritise data partnerships (this includes the USA, Australia, Columbia, Singapore, South Korea and Dubai). The aim is to use a more flexible and agile regulatory framework to create a ‘data dividend’ in which innovation is better facilitated, particularly for small businesses

However, in making any changes to the current approach to data governance, the UK will need to set out how it will reassure the EU that the UK is not diverging from EU standards, if it wishes to retain its adequacy agreement with the EU. In particular, the EU adequacy decision with the UK requires that the data of EU citizens is not transferred to jurisdictions that don’t have such a decision in place. The costs of losing EU adequacy have been [estimated](#) to be millions of pounds per year for large firms, as businesses would need to comply with two regimes, that of the UK and the EU.

ROAD HAULAGE

As a member of the EU and during the transition period, the UK’s Driver and Vehicle Licensing Agency (DVLA) was able to issue EU Community Licences for drivers in possession of a standard international vehicle operator licence so they could transport goods to the EU/EEA. As a result, UK hauliers offered road haulage services in other member states on an unrestricted basis and vice versa.

For a number of years before Brexit, the number of UK nationals working in logistics had been falling. Free movement helped address this labour market shortage. Before Brexit, [13%](#) of the UK’s logistics workforce were EU nationals.

The TCA and haulage

The TCA averted the worst fears of the haulage industry in terms of a no deal Brexit. Without a deal, UK driving licences might not have been recognised by

EU member states, requiring drivers to apply for international driving permits for cross-border assignments. These permits are limited in number and would have fallen far short of the number required for the level of activity undertaken by drivers from the UK.

The TCA's provisions continued the status quo. In particular, the UK Licence for the Community has replaced the EU Community Licence for UK drivers. It allows UK drivers to transport goods to the EU, Liechtenstein, Norway and Switzerland. Like other UK travellers, UK drivers now need at least six months on their UK passport to travel to the EU but can continue to operate in the EU without the need for a visa as long as they do not remain in the EU for more than 90 days within a 180-day period.

However, despite the UK seeking a more liberal regime, the TCA only permits basic cabotage (cabotage refers to a trip between two destinations outside the home company of the haulage firm, such as a British driver making a delivery in Lyon followed by one in Marseilles). During membership, UK hauliers were able to offer road haulage services in other EU member states on an unrestricted basis. They are now only able to undertake one cabotage operation on any journey — which will have a significant impact on touring artists, for example. In addition, UK hauliers also need to ensure they are in possession of customs declarations that are [required](#) from the exporter.

Building on the TCA in road haulage

The road haulage industry has seen some of the most significant challenges to its previous operating model as a result of the combined impacts of Brexit and the Covid-19 pandemic. Disentangling one set of impacts from the other and from the longer-term structural issues in the sector is not simple. There has also been wider supply chain disruption, particularly in relation to fuel.

The first issue is the structure of the labour market prior to the pandemic and Brexit. As we noted in our [report](#) on the services sector in June 2020, the number of UK workers employed in logistics has been falling in recent years as the workforce has aged and retiring drivers have not been replaced with younger UK workers. The Road Haulage Association notes that the average age of a UK HGV driver is 57 and less than 1% of drivers are under the age of 25.

The sector was reliant on free movement during the UK's EU membership, with EU nationals working in the UK to make up some of the shortfall. However, following the UK's withdrawal and the travel restrictions imposed in response to Covid-19 there has been a significant decline in the number of EU migrants working in the UK.

At the beginning of the pandemic, 40,000 of the 300,000 truck drivers in the UK were from the EU. One year later this had [fallen](#) to 20,000. Approximately 5,000 returned once travel restrictions eased, but this left a shortage of 15,000 EU drivers which, given issues with the data, is likely to be an underestimate.

The importance of the ageing domestic haulage labour market coupled with the reliance on EU nationals to address the shortage before Brexit is reflected in a recent survey of haulage firms conducted by the Road Haulage Association. Of the 616 responses to their survey on the causes of the driver shortages conducted in June 2021, 58% said that Brexit was a cause of current driver shortages and 59% said it was down to retiring drivers. These were the top two responses in a survey where respondents could select more than one cause.

HGV driving is also not listed as an eligible high-skilled occupation under the government's post-Brexit immigration rules that came into force on 1 January 2021. As a result, HGV drivers from outside the UK, including the EU, are ineligible for skilled visas to work in the UK. Given that there are vacancies for drivers within the EU that is suffering its own a driver shortage, this acts as a further barrier to EU drivers working in the UK.

Brexit has also impacted on the ease with which EU drivers can operate in the UK (and vice versa), further limiting the UK haulage labour force. The risk that loads may have incorrect paperwork for new customs checks at the UK-EU border means that lorries may be at a standstill while waiting for the paperwork to be corrected. Any period where a freight lorry is not moving costs the haulage company money and hence EU operators may choose to concentrate on work within the EU to avoid this uncertainty.

Although these factors in the industry were known before the UK's departure from the EU, Covid-19 has exacerbated these trends. Most notably, as the UK economy shutdown in the early stages of the pandemic, many EU national drivers returned home to the EU. The uncertainty surrounding how they could operate in the UK after Brexit, coupled with strong demand for drivers in the EU, has meant that many have remained in the EU as the pandemic has progressed.

Additionally, the pandemic has created a backlog in HGV-driver tests causing a slowdown in the rate at which new UK drivers qualify. The Road Haulage Association estimates that the shutdown of vocational driving tests for much of 2020 led to 25,000 fewer tests being passed compared with 2019.

The government responded by launching a new temporary visa [scheme](#) in October 2021 for EU drivers, making 4,700 HGV food-driver visas available. Applications need to be made by 1 December, with the visas expiring on 28 February 2022. The timings are in reality even tighter, because it will take three weeks to process

applications. These HGV drivers will need to hold a licence that is recognised for use in the UK, and the scheme only applies to EU, EEA and Swiss licence holders. A different scheme is in place for HGV fuel drivers. This scheme grants drivers arriving between 1 and 15 October permission to operate in the UK until 31 March 2022 subject to checks made by the UK Border Force.

In a further attempt to address the shortage of drivers, the government announced a relaxation in permitted HGV-driver hours. As a member state, the UK followed EU Driver Hours rules. These stipulate that the driver must take a 45-minute break after driving for 4.5 hours. At the end of the transition period the UK continued to follow these rules because the UK is a signatory of the European Agreement Concerning the Work of Crews of Vehicles Engaged in International Road Transport, which includes other non-member states such as Ukraine. The UK's temporary changes increase the daily driving limits from 9 to 10 hours per week with one of 11 hours allowed up to twice a week. Initially, these changes were in place until 8/8/21 but they have been extended until 9 January 2022.

Both the changes in visas and driver hours are only temporary solutions to the structural issues of labour shortages in UK haulage. Longer term planning around the working conditions for drivers and the skills policy supporting driver recruitment will be needed to address the structural nature of labour shortages in the haulage industry that extend beyond those caused directly by Brexit.

HOSPITALITY AND TOURISM

Brexit presents two major challenges to the hospitality and tourism sector: labour shortages and new travel requirements for European visitors. The former is particularly acute in the short-term and is another example of how Brexit and the pandemic have interacted to make service provision more complicated after Brexit. The latter will take longer to materialise but could be significant in the long run.

The ending of the free movement of labour has significant consequences for any industry reliant on EU workers. It was immediately apparent last year in sectors where the majority of the workforce consists of seasonal migrant labour such as fruit-picking. However, when labour shortages in British fields were making the headlines, most of the hospitality sector was closed due to Covid-19, and the transition period for the UK's membership of the EU Single Market had not ended. It has become more apparent in 2021 as the sector has reopened, and customer confidence has returned because of vaccines, that there are significant staff shortages. A KPMG [study](#) conducted in 2017 for the British Hospitality Association estimated that 75 per cent of waiting staff, 23 per cent of chefs and 37 per cent of housekeeping staff were EU workers. It is therefore no surprise that

the significant numbers who returned home during the pandemic and have not returned to the UK since travel restrictions ended have led to labour shortages in the sector.

Earlier this year, an industry job site, caterer.com, estimated that vacancies have increased by [342%](#) in 2021 as fewer and fewer workers are available to fill them. In a further example of the interaction of the pandemic and Brexit, the sector's labour shortages as a result of Brexit were exacerbated over the summer by the so-called 'pingdemic' in which significant numbers of workers were instructed to self-isolate through the UK's track and trace app to limit COVID-19 transmission. Table 1 compares vacancies and applications between the months of July 2019 and July 2021. The hospitality sector shows strong signs of growth as the Covid-19 restrictions have been lifted, with 21% more vacancies than at the same point two years ago. However, the number of applications has fallen by over 50%.

The hospitality sector has seen 21% more vacancies in July 2021 than two years before. However, the number of applications has fallen by 50%.



Table 1: Jobs posts and applications in the hospitality sector.

	July 2019	July 2021	
Job postings	32,366	39,061	+21%
Applications	720,555	452,852	-37%
Apps per vacancy	22.4	10.9	-51%

Source: Caterer.com (August 2021).

Building on the TCA in the hospitality and tourism sector

The longer-term implication of the UK's new immigration policy will hit the hospitality sector later this year. From October 2021, the UK no longer accepts National ID cards for European citizens in place of a passport. This is likely to impact the number of EU citizens travelling to the UK as a tourist destination. For EU citizens, the possession of an ID card is sufficient to travel throughout the EU. For this reason, a smaller proportion of EU than UK citizens hold passports. For example, in 2016, out of a population of over 17 million, there were only [8.8 million](#) passports in circulation in the Netherlands. A portion of those citizens may decide to change their holiday destinations to one that accepts their identity documents rather than the UK.

One specific type of travel that will be particularly affected is school trips. Given that French and German schools have a policy of [all go or none go](#), insistence on passports is likely to significantly reduce the number of school trips to the UK. France alone sends 10,000 groups per year amounting to around 500,000 travellers, and a direct input of £100 million into the UK economy. Germany

sends a further 7,000 groups. This represents the potential for a significant hit to the UK hospitality sector and related services such as foreign language schools.

THE CREATIVE INDUSTRIES

Audiovisual

As we highlighted in the Services and Brexit [Report](#) of 2020, while the UK was a member state, the audiovisual sector was governed within the EU through the use of two main regulations: the Audiovisual Media Services Directive (AVMS) and the Council of Europe's European Convention on Transfrontier Television (ECTT). The AVMS allows broadcasters regulated in one member state to broadcast across the EU without the need to meet the separate regulatory requirements of individual member states. This enabled the UK to develop the largest audiovisual sector in Europe.

During the Brexit trade negotiations, the UK sought to include a similar arrangement in the TCA, even though the EU has no other FTA that covers this sector. The EU did not concede, so on 1 January 2021 the UK became a 'third country' for the purposes of the AVMS, which means it must comply with national regulations in order to broadcast across the EU.

However, that is made easier to some extent by the second piece of regulation governing audiovisual services, the ECTT. This Council of Europe convention guarantees that programmes can be shared cross-border via terrestrial, satellite and cable services to all those who are signatories. However, it does not include Video on Demand (VoD), which did not exist in any meaningful way when the convention came into operation in 1993. In addition, not every member of the EU is a signatory. Belgium, Ireland and Denmark did not sign, and Greece, Luxembourg, the Netherlands and Sweden have not ratified it. The result is a fragmented regulatory environment for the UK's audiovisual sector.

Alongside broadcasting rights, the AVMS also insists on quota provisions to promote content produced in Europe or 'European works'. These provisions envisage that a majority of broadcasting time will be dedicated to European works (excluding the time apportioned to news, sports and advertising). The AVMS defines European works as originating in an EU member state or a European state, which has signed the ECTT. This means that content produced in the UK is still classed as a European work.

The impact of the new trading relationship on the sector so far

The UK's negotiating set out a process by which Ofcom, the UK's regulator, would be authorized 'without undue delay' such that a broadcasting licence

issued by Ofcom would continue to be recognised within the EU's single market. This would have meant that UK broadcasters would be able to broadcast throughout the EU without needing to comply with any additional regulations. However, Ofcom is no longer recognised by the EU. As a result, the cost and complexity of exporting to the EU has increased as broadcasters and providers of video on demand services need to ensure they meet the regulatory requirements to broadcast in their target export market.

The most significant and immediate impact on the sector has been a large-scale migration of broadcasting licences away from the UK to the EU. The European Audiovisual Observatory has [reported](#) that the number of channels based in the UK has halved in response to this licensing change. Between 2018 and the end of 2020, the number of channels in the UK fell from 1230 to 586. The UK remains the leading television market in Europe, but there has been significant migration to the Netherlands, Spain and Luxembourg, with 70% of channels broadcasting to Europe falling in one of these jurisdictions. This includes a migration of UK-orientated channels such as Discovery, Disney, NBC, Sony and Turner, alongside the international arms of Sky and the BBC. In total 250 broadcasting licences relocated during this period.

TOURING ARTISTS

The performing industries are similar in size to the UK's construction industry, employing over 100,000 people. It is also a strength of the UK economy. For example, before Brexit, [UK hauliers](#) made up 80% of the EU's music haulage activity.

The full details of the UK's negotiating position for touring artists have not been made public but it has been [reported](#) that the UK sought to agree a visa-free travel arrangement for musicians for 30 days. Former Secretary of State for Culture, Media and Sport, Oliver Dowden said that the UK's position would mean that 'musicians, artists, entertainers and support staff would have been captured through the list of permitted activities for short term business visitors'. The EU proposed a more general mobility arrangement for the sector through a visa waiver scheme, but the UK rejected this proposal.

The result is that under the TCA it is far harder for performers from the UK to tour the EU than before. These changes are made more significant because the sector has been particularly badly hit by the shutdown of live events during the pandemic.

Although the TCA does allow for visa-free travel of 90 days within a 180-day period, it sets out restrictions regarding the types of activities that are permitted (short-term business visitors, independent professionals or contractual service

suppliers). These activities have further restrictions that mean they cannot be used by travelling musicians. For example, the requirement for independent professionals to have six years' experience alongside a degree does not sit straightforwardly with the career path of musicians.

There are no special provisions for performing artists in the TCA, so they need to meet the requirements of each member state. This may include obtaining visas or work permits as well as following rules on haulage for the transportation of equipment. In the case of national visa/permit restrictions, Austria and Lithuania provide permit exemptions for musicians. However, for a single gig in Spain or Italy a [visa](#) costs £500 and £600 respectively, a prohibitive cost for a small band. Touring artists also need their equipment transported but this faces new restrictions under the terms of the TCA. This has made music tours from the UK to the EU more difficult than before Brexit, with some performers reporting that EU venues now prefer to hire EU artists as a result.

The sector is also negatively impacted by the haulage changes implemented because a critical part of tours is moving large amounts of equipment. Under cabotage rules, UK haulage companies can now only make two drop offs in the EU before returning to the UK. This limits their ability to service multi-stop European tours.

The House of Lords European Affairs Committee reports from its evidence sessions on this sector that the implications of the TCA for touring creative professionals are so significant that it [poses](#) 'a serious threat to sections of the industry'. Its intervention, which includes a letter [sent](#) to Lord Frost expressing concerns for the sector as a result of the TCA, urges the government to consider regulatory changes that could be made both to the visa requirements for travelling artists and to the haulage industry which would make touring easier within the EU for UK artists than is currently the case.

SERVICES TRADE AND 'GLOBAL BRITAIN'

The UK has started to agree new trade deals with third countries, which it could not previously do on its own behalf as a member state. But although the responsible department, the Department for International Trade (DIT), was established in July 2016, it is only since the transition period ended that it has been able to conclude those new deals. Much of the early focus of DIT was on 'rolling over' the deals the UK had enjoyed as an EU member state to allow UK business to trade on the same terms after Brexit.

In terms of the geographical priorities for such trade deals, the government has aligned its emerging trade policy with its wider 'Global Britain' agenda, as set out most fully in the July 2021 [Integrated Review](#). Both the Integrated Review and the DIT's approach to trade focus on enhancing the UK's trading relationship eastwards in a general sense, on Commonwealth countries, notably Australia and New Zealand, and on rapidly growing Asian economies, such as Singapore, and the US.

As the table below shows, it makes sense economically to focus on the US, as it is the largest single destination for UK services exports. However, under President Biden, the US has downplayed the prospects of a US-UK trade deal.

The US is the single largest destination for UK services exports.

UK IN A
CHANGING
EUROPE

Table 2: The UK's largest services export markets, 3Q 2019 (non-seasonally adjusted, latest data available).

Country	£ million 3Q 2019	% total services exports, 3Q 2019
United States	19,456	23.7
Germany	5,261	6.4
France	4,687	5.7
Netherlands	4,481	5.5
Ireland	3,913	4.8
Switzerland	3,274	4.0
Italy	2,948	3.6
Spain	2,202	2.7
Japan	1,917	2.3
Australia	1,764	2.2
Rest of world	32,136	39.2

Source: ONS, January 2020.

Currently the UK has signed [67](#) trade agreements in addition to the TCA with the EU. The majority of these are 'rollover deals'.

Free-trade agreements typically do little to liberalise services trade. However, given the strategic importance of services to the UK economy, there is a lot of interest in seeing what the UK manages to negotiate with respect to services in its new trade deals because these have the potential to set the benchmark for future trade agreements in services. Where provisions are made to facilitate services trade, they typically focus on supporting and providing greater [certainty](#) for existing market access, rather than opening up markets for overseas providers.

The UK's trade deal with Japan, formally the UK-Japan comprehensive economic partnership agreement (CEPA), gives an [indication](#) of the benefits that an FTA offers UK services. Then UK trade secretary Liz Truss argued that it [represented](#) 'a British-shaped deal tailored to our economy'.

The UK did not obtain additional market access for its services sectors in Japan, but it did largely ensure that existing levels of market access were retained, thereby providing additional stability and certainty for businesses. On financial services, the UK emphasised in promotional literature that it had secured additional benefits for financial services beyond those of the EU-Japan deal, which the UK was operating under previously. However, this does not mean that additional market access into Japan has been agreed. In practice, the deal allows financial firms to store Japanese data in Britain (as was the case previously) and made the process clearer for UK financial firms seeking to obtain a license to operate in Japan. The agreement creates a formal structure for regulatory dialogue, something that the UK also included in the TCA. This will provide a structure through which the UK could influence Japanese regulatory policy, something that could allow greater market access for UK financial services in the future, but is not new — the EU-Japan trade deal also includes provisions for regulatory dialogue

The UK agreement with Japan also follows the EU-Japan trade deal on the temporary movement of people. This means that subsidiaries of British companies operating in Japan can move their UK staff to Japan on a medium-term basis and vice versa. Service suppliers can also move between the UK and Japan to deliver services on a short-term basis. It does not provide for the automatic mutual recognition of qualifications in areas such as legal services, but it does create a framework for developing this in the future.

One of the most innovative aspects of the Japan deal relates to commitments on data services. Both the UK and Japan agreed not to implement a data locational policy that would stipulate where data has to be stored. It also means that algorithms and code providers do not have to share proprietary information without 'good reason'. This does go further than the EU-Japan agreement, reflecting the UK's ambition in digital services and digital trade. However, there

are not automatic new opportunities for British digital companies in Japan because the agreement essentially commits the parties to maintain existing practice.

In June 2021, the UK secured agreement in principle to a trade deal with Australia, which does not have an FTA with the EU — although it is negotiating one. This was seen as politically important given Australia's Commonwealth membership and its wider significance for Global Britain's 'Indo-Pacific tilt', as demonstrated in the AUKUS nuclear submarine deal. Before the deal, Australia [contributed](#) 1% of UK imports and the UK accounted for 4% of Australian exports. The government's own analysis suggests that the deal could increase UK GDP by 0.02% in the long term with the equivalent growth for Australia estimated to be up to 0.06%.

The deal covers services trade and goes beyond the UK-EU deal in recognising professional qualifications and aiming to enhance mobility while opening up financial services and investment. However, although the former is likely to be beneficial to particularly early career UK nationals wanting international experience, research [shows](#) that services trade is typically greater with geographically proximate partners. So despite virtual modes of delivery that were developed during the pandemic, the potential for significant increases in cross border UK-Australia financial services trade should be taken with a pinch of salt.

The deal is particularly interesting for services with respect to the mutual recognition of professional qualifications and mobility. It includes provisions for UK and Australian lawyers to advise clients in the other country. It also includes changes to youth mobility schemes, permitting citizens under 35 to stay for up to three years while also removing the requirement for UK nationals to work on Australian farms.

The real significance of the Australia trade deal lies in its wider political signalling rather than its immediate economic impact. In addition to the agreement with New Zealand of October 2021, the deal with Australia is a step towards the UK's aim of joining the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) and some of its provisions, such as those on environmental and labour provisions, largely follow those in CPTPP.

However, potential CPTPP membership may not be compatible with the UK's current adequacy decision from the EU on data. Under EU GDPR regulations, personal data stored by companies must be kept in the EU or in third countries outside the EU that are judged by the EU to have an adequate or equivalent level of data protection. Under the CPTPP this would be viewed as a form of enforced data location, which is prohibited under the terms of the CPTPP.

Given the limitations of free trade agreements in liberalising services trade, the UK has also sought to develop bilateral agreements with individual countries to support specific service sectors. For example, in June 2021, the UK and Singapore agreed a Financial Partnership that aims to use closer regulatory cooperation to support trade in financial services and investment into the UK. The UK and Switzerland have also committed to seeking a bilateral agreement for the mutual recognition of their respective financial regulatory frameworks. This is being watched closely because if agreed, it would facilitate passporting and cross border supply in financial services. Both Switzerland and the UK agreed in early 2021 to grant equivalence to each other's stock exchanges. It is also geopolitically significant because both London and Zurich are significant European financial centres outside the EU's regulatory control. Any strengthening of the UK-Swiss bilateral relationship in this area is likely to further raise concerns about the ability of both countries to out compete the EU on financial services.

FUTURE PROSPECTS FOR POST BREXIT UK SERVICES

This report shows the significant and wide-ranging impacts of Brexit that are beginning to emerge across the UK services sector. UK trade to the EU in services is more difficult under the terms of the TCA than when the UK was a member state. At the same time, the lack of agreement between the UK and the EU on a post-Brexit mobility regime means that firms and individuals are navigating a complex patchwork of new rules regarding travel. The conflation of Brexit with the pandemic restrictions means the implications have yet to play out.

The government's response centres on the development of a new, post-Brexit international trade policy and a domestic focus on tailoring regulation to stimulate innovation and competitiveness. However, the data presented in this report suggests that it is far from clear that what the government regards as Brexit dividends will offset the negative impacts of increased trade barriers with the UK's closest trading partner. The challenge remains because trade, including services trade, is typically deepest with geographical proximate trading partners. This runs counter to Lord Frost's [assertion](#) that 'trade in services is relatively indifferent to geography'.

Crucially these changes will not emerge overnight. Rather than a short sharp shock, the impacts of Brexit on services will unfold gradually over time. This is particularly true in relation to the end of free movement and the introduction UK's new immigration regime.

It is all the more important that the government develops a clear strategy for services after Brexit and is realistic about the prospects, and risks, associated with deepening services trade with non-EU partners. For example, deepening trade relations with Australia sits neatly with the governments 'Global Britain' agenda but does little to enhance UK GDP and could put ongoing data adequacy decisions with the EU at risk. Similarly, diverging from EU regulation in financial services may mean that the City of London is increasingly focused on green and digital finance, but this does not remove the fact that the EU is, by virtue of its location, likely to remain the largest potential market for UK financial services exports. These could be strengthened by fostering greater goodwill between the UK and the EU on financial services regulatory cooperation.

Given the long-term implications of Brexit for the UK services sector, the government should learn from the experiences of the transition period and recognise that providing clarity and as much certainty as possible is vital

for businesses and households. This is particularly important given that the regulatory framework analysed in this report that currently underpins EU-UK services trade is not necessarily stable. In services, the TCA (which itself includes review clauses) is tied into a web of unilateral decisions, not treaties, in areas such as financial services and data, that could be withdrawn with little warning. Managing these uncertainties requires cooperation with the EU, alongside the domestic policies on post-Brexit regulation and new international trade strategies beyond the EU. Without such cooperation, there is a risk that ongoing disputes and threats of significant changes in UK-EU trade relations reduce confidence in the UK economy, limiting investment and productivity improvements that would then hamper the development of the UK's post-Brexit services sector.

The UK in a Changing Europe promotes rigorous, high-quality and independent research into the complex and ever changing relationship between the UK and the EU. It is funded by the Economic and Social Research Council and based at King's College London.

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