

Global Britain—Brexit and the customs union (part two)

Public Law analysis: Lourdes Catrain and Eleni Theodoropoulou of Hogan Lovells, Brussels, further examine how the EU customs union works in practice and looks at some of the UK's trade options and considerations outside the customs union.

How does the EU customs union operate? What is its scope?

Under World Trade Organisation (WTO) law (see Article I:1 of the General Agreement on Tariffs and Trade (GATT)), WTO members are under a general obligation to accord each other equal treatment in respect of customs duties or other import/export charges, which is known as the 'most-favoured nation' (MFN) principle. WTO law defines a customs union as a territory in which customs duties and other restrictive measures are eliminated with respect to 'substantially all trade' between the constituent territories of the union, and the same duties apply to goods imported from other territories (see Article XXIV:8 of the GATT). The MFN principle is disapplied in the case of a customs union or a free trade area.

The EU is not only a customs union, but a highly integrated economic and political union, allowing the EU to act on behalf of its Member States on various matters including trade, where empowered to do so.

The EU customs union aims at facilitating trade in goods among the EU Member States. Within the EU, the application of any tariffs, quantitative restrictions or other charges having equivalent effect, or customs controls, is prohibited. Once imports from third countries have entered the EU and all import formalities have been complied with, the goods can move freely across all the EU Member States.

The EU has a common customs tariff (CCT) that is applied to imports from third countries. This CCT is fixed by the Council of the EU following the proposal of the European Commission. The tariffs applicable to the imported goods are set out in the Annex I to the Combined Nomenclature (CN) [Regulation \(EEC\) 2658/87](#) an updated version of which is published every year in the Official Journal of the EU. Moreover, the EU has common customs rules embodied in the Union Customs Code (UCC), which provides for the rules and procedures that apply to goods imported into or exported from the EU territory (see [Regulation \(EU\) 952/2013](#)).

The customs union is an integral part of the EU common commercial policy, for which the EU has exclusive competence conferred on it by the EU Member States.

What is the UK's current negotiating approach in regard to the customs union?

The UK has been advocating in favour of leaving the customs union. The UK government explicitly stated in the [Brexit White Paper](#) that the country will pursue a 'new strategic partnership with the EU, including...a new customs agreement', with the aim of making trade with the EU as 'frictionless' as possible.

It is the aim of the UK to be able to conclude preferential trade agreements with third countries and, to this end, not to be bound by the CCT or participate in the common commercial policy. The White Paper remains open on how to achieve this new customs arrangement with the EU, suggesting there are a number of options including the conclusion of a completely new customs agreement, as well as the UK remaining a signatory to some elements of the existing EU customs arrangements.

The primary goal of the UK is to conclude a ‘mutually beneficial customs arrangement’ that will allow trade in goods between the EU and the UK to continue with the least disruption possible. Models adopted between other countries will be reviewed, but no replication will be sought to be made, with the intention being to seek the best possible deal for the UK. The UK will work with businesses and infrastructure providers on the customs processes themselves, and specifies the need to use ‘digital technologies’ in its aim of achieving frictionless trade.

This approach was confirmed in the [Queen’s Speech 2017](#), where the Queen stated:

‘New Bills on trade and customs will help to implement an independent trade policy, and support will be given to help the UK’s businesses export to markets around the world.’

What are the implications of leaving the customs union?

Upon leaving the customs union, the UK will be treated as a third country vis-à-vis the EU for customs purposes. The UK will no longer be bound by the EU common commercial policy and it will be free to conclude international trade agreements with third countries.

UK goods imported into the EU will have to comply with all formalities provided in the UCC and be subject to the tariffs set out in the CN, subject to the content of the future EU-UK trade agreement. This is likely to entail delays and administrative costs, part of which would be borne by the UK exporters.

Rules of origin determine the ‘economic nationality’ of goods for import purposes. There are two types of rules of origin—preferential and non-preferential. Preferential rules of origin are established through free trade agreements (FTAs) or unilateral acts of the EU in respect of certain countries and entail entry at a reduced or zero tariff-rate for the imported goods. Non-preferential rules of origin apply in the absence of any trade preferences between the states concerned. In the latter case, trade is conducted on a MFN basis.

Under WTO rules, the MFN principle prohibits discrimination between WTO members outside the context of a customs union or free trade arrangement. With respect to trade in goods, the MFN principle obliges a WTO member to extend any advantage afforded to one country with respect to customs duties and charges to the like products originating in or destined to all other WTO members. Trade on a MFN basis is generally subject to higher duties than those provided for in a preferential trade agreement.

The application of rules of origin would be necessary for UK imports into the EU after Brexit. This would have a knock-on effect for example on products produced partly in the UK with inputs/components from EU Member States. Goods previously determined as EU origin may become UK origin, even if some value is added elsewhere in the EU.

What would remaining within the customs union mean for the Department for International Trade’s plans for negotiating trade deals with third countries?

Remaining within the customs union would entail that the UK is bound by the EU CCT regarding third countries and by the common commercial policy. For example, under the EU-Turkey customs union agreement, Turkey

has to apply provisions that are ‘substantially similar’ to those included in the EU common commercial policy, such as regulations concerning rules on imports and exports, procedures for administering quantitative quotas.

Moreover, Turkey must progressively align itself with the preferential customs regimes of the EU, including the preferential agreements with third countries, with the view to harmonising its commercial policy with EU trade policies. In doing so, Turkey must apply identical rules of origin with those included in such preferential arrangements between the EU and third countries.

If a similar model is applied between the EU and the UK, the UK would be, in practice, bound to negotiate FTAs with the EU trading partners, in which essentially the same preferences would be granted, both in terms of applicable duties and rules of origin without being part of the EU decision-making process. This could result in asymmetries, including possible reluctance of third countries to negotiate with the UK agreements comparable with those of the EU, thus leaving UK businesses in comparative disadvantage to EU exporters.

In theory, the UK could attempt to negotiate different arrangements with the EU regarding its ability to negotiate and conclude trade agreements with third countries while being part of the customs union. It is likely, however, that the EU would object to this.

What are the options in regard to a new bespoke arrangement? What would this mean for UK trade in goods and services? Could it follow a sector by sector approach?

The arrangement that would best address UK’s goals and interests to ensure the least disruption possible for its economy would be achieved through the negotiation and conclusion of a comprehensive FTA with the EU. Despite the practical considerations involved in terms of process and time, a FTA could cover both goods and services, as well as other matters important to the UK, eg protection of foreign investments.

Such an agreement would need to cover substantially all trade in goods and have a substantial sectoral coverage for services. This would exclude concluding different agreements for different sectors. The extent of the concessions given to the UK in each sector is a matter of the negotiations between the two partners.

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