



RECENT EU TRADE POLICY AND THE IMPLICATIONS FOR THE NEGOTIATIONS ON FUTURE RELATIONSHIP WITH THE UK

EU trade policy is likely to receive considerable attention over the next few months, as the EU negotiates its future trading relationship with the UK.

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The UK formally left the EU on 31 January 2020. It is currently in a transition period, which is scheduled to expire on 31 December 2020. There is a possibility that the transition period could be extended by a single period of up to one or two years beyond 31 December 2020, provided that this extension is agreed before 1 July 2020. However, given the UK Government's current resistance to an extension, an extension currently appears unlikely.

During the transition period, trade between the UK and the EU continues to take place on the same terms as prior to the UK's exit. For example, UK goods have full tariff-free access to the EU market and vice-versa.

However, unless the UK and the EU reach an agreement on the future terms on which trade between them will take place before the end of the transition period, trade between the UK and the EU will take place on 'WTO Rules' following the end of the transition period.

A switch to 'WTO rules' could have significant effects. Some potential changes have been widely discussed. For example, tariffs could be introduced on UK goods exported to the EU, UK service suppliers might be unable to sell on a cross-border basis

to the EU, and the reintroduction of customs checks could lead to delays which could hinder both manufacturers reliant on complex supply-chains and retailers reliant on 'just-in-time' deliveries.

Other changes are less obvious but also significant. For example, companies may be required to go through an additional conformity check in order to sell their products in both the UK and the EU, and UK exporters could find their product targeted by EU anti-dumping duties.

If negotiations on future relationship lead to an agreement on the future terms of trade, then future trade will take place under those rules, rather than WTO rules (other than in situations where the parties have not reached an agreement on a topic which is governed by WTO rules). However, even if an agreement is reached, it is still likely that there will be substantial changes to the current rules.

By opening negotiations for a free trade agreement (FTA) with the USA on 5 May 2020, the UK Government has confirmed its intention to have a trade policy which is independent of the EU, which precludes the possibility of the UK continuing to be a member of the European Customs Union. In addition, the UK

Government's position - outlined in its negotiating policy paper published on 27 February 2020 - is that it will not agree to obligations for the UK's laws to be aligned to EU laws on an ongoing basis and will not accept any EU institution, including the Court of Justice of the European Union, having jurisdiction in the UK.

This means that it is almost certain that the UK will no longer be a part of the European single market, as this would require the UK to adhere to EU legislation underpinning the 'four freedoms' of free movement of goods, services, capital and labour which make up the European single market. Instead, it is likely that, if agreement on the future trading relationship is reached, this agreement will bear resemblance to recent FTAs agreed between the EU and third countries such as Japan and Canada.

As the outcome of the negotiations will result in significant changes for business, it is instructive to understand recent EU trade policy on FTAs, and how these are unlikely to impact on the unfolding negotiations.

EU trade policy on FTAs

Prior to the last decade, the EU had previously entered into limited 'traditional' FTAs focussed on tariffs, such as that with Mexico in 2000, and had also included aspects of

trade liberalisation as part of wide association agreements with close geographic partners. The defining feature of the last decade of EU trade policy has been the pursuit of ambitious and comprehensive FTAs globally. Partially, this is due to the fact that the Lisbon Treaty gave the EU exclusive competence over more aspects of trade policy than it had previously, for example foreign investment, which means that the EU's trade agreements can be more comprehensive than before. However, it can also be seen as part of the recent failure of the WTO to progress liberalism in trade on a multilateral basis, in particular in areas which are novel but of increasing significance, such as digital trade.

A traditional FTA can be described as an agreement which takes advantage of at least one of the two key exemptions from the general obligation under WTO law not to discriminate between WTO members. These exemptions are contained at Article XXIV of the GATT and Article V of the GATS. They allow individual members to provide favourable tariff or market access treatment for services to another WTO member, provided that they do so on a widespread basis. The EU's recent comprehensive FTAs move beyond this traditional model by including measures that, broadly speaking, do one or more of three things:

1. Measures which provide even greater direct market access outside of the scope of reduced tariff access or improved market access for providers of services, such as those on public procurement.
2. Measures which promote greater regulatory alignment between the FTA partners. In general, these measures are intended to consolidate direct market access gains that have been made, such as provisions on the mutual recognition of standards. However, other measures, such as on labour standards and the environment, target the establishment or consolidation of global civic standards.

3. Measures which are intended to promote greater economic integration between the two economies. Provisions on investment and investment protection are the most prominent example of this.

In the past decade the EU has completed what can be categorised as comprehensive FTAs with South Korea, Canada, Singapore and Japan. An FTA with Vietnam is expected to come into force during 2020, following ratification by Vietnam. Negotiations of FTAs with Australia, New Zealand and the South American members of MERCOSUR, as well as an updated comprehensive FTA with Mexico are ongoing. However, the EU has also met with two notable recent failures.

In 2007, the EU originally pursued a region-to-region FTA with the Association of South East Asian Nations. This strategy was replaced by pursuing bilateral FTAs with individual ASEAN members, only one of which, with Singapore, is now in force, following significant delays, and having been shorn of its ambitious investment chapter. Another, with Vietnam, should enter into force shortly. But negotiations with Thailand, Malaysia, the Philippines and Indonesia have all stalled.

The other major failure is TTIP, undoubtedly the negotiations to attract the most significant attention. A combination of widespread public criticism, in particular over the perceived features of the Investor-State Dispute Settlement mechanism, conflict between the parties on key issues such as regulatory standards for agriculture, and increasing isolationism on the part of the Trump administration resulted in the agreement of a deal becoming a step too far.

As a result, the EU's recent success in negotiating FTAs can be regarded as mixed. It should be admitted that external factors, such as the 2014 military coup in Thailand, and President Trump's election, have contributed to this. However, this highlights that there is no certainty that an FTA will be concluded once negotiations have been opened:

there is no guarantee that the EU and the UK will reach agreement on their future trading relationship, especially within the restrictive timeframe.

The potential for no agreement to be reached is heightened by an increasing assertiveness to recent EU trade policy, which may make it more difficult for trade partners, including the UK, to agree to what is being asked of them in return for favourable access to the EU market.

In its 2015 policy document 'Trade for All' DG Trade stated that, *"By engaging partners in regulatory cooperation, the Commission can exchange ideas and best practices and promote EU standards in a way that will help consumers everywhere to benefit from the highest and most effective levels of protection. Trade agreements are a way to give political momentum to this kind of dialogue. However, regulatory cooperation is not about give and take or trading one regulation for another."*

But, in its 2019 Trade Management Plan, former European Commission President Juncker is quoted as saying that FTAs *"help us export Europe's high standards for food safety, workers' rights, the environment and consumer rights far beyond our borders."*

Similarly, in 2020, in a speech at the Centre for European Reform, available on the European Commission's website, Trade Commissioner Hogan stated that, *"When we sign deals with global partners, we expect them to meet our standards."*

The EU has therefore moved from a position where FTAs are seen as a way of promoting European standards to one where they are seen as a way of enforcing European standards.

Brexit

This shift can also be seen in the EU negotiating mandate for the future relationship negotiations with the UK, and its repeated references to the establishment of a 'level playing field' between the EU and the UK. In particular, the mandate states that, *"the envisaged partnership must ensure open and fair competition, encompassing robust commitments to ensure a level playing field..."*

the envisaged agreement should uphold common high standards, and corresponding high standards over time with Union standards as a reference point, in the areas of State aid, competition, state-owned enterprises, social and employment standards, environmental standards, climate change, relevant tax matters and other regulatory measures and practices in these areas. In so doing, the agreement should rely on appropriate and relevant Union and international standards.”

A common intention to uphold high standards, informed by relevant international standards, in the specified policy areas to ensure a level playing field between two entities which are bound together by a significant degree of economic integration is not controversial. What is controversial is that the mandate states that the high standards which the UK should uphold over time should take the EU’s standards as their reference point, and suggests that the EU should be able to take retaliatory measures if those standards are not upheld in the UK. This position is at odds with the UK Government’s statement that it will not agree to obligations for UK’s laws to be aligned to EU laws on an ongoing basis.

The UK and the EU have, as of 15th May 2020, concluded their third round of negotiations. To date, neither side has appeared to be willing to shift their position on the fundamental issue of whether the UK should be obliged to guarantee its alignment with certain EU legislation in order to reach an agreement. Ultimately, for an agreement to be reached, the EU is likely to have to accept that whilst the UK may commit to high standards in key public policy areas through its laws, such as State aid, it cannot commit to the EU’s version of those standards. Notwithstanding the UK Government’s stated intention that it is not willing to do this, it would be difficult for any Government to justify to its electorate the need to confer significant powers to institutions over which that electorate does not have any control. But for the EU to accept this would entail a significant U-turn, and it may be that it has dug itself into an entrenched policy position. The battle over the future relationship is far from over.

We will continue to monitor developments closely.

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