

Future of UK Trade and Customs Policy Debate on 5 December 2017

Summary

On 5 December 2017 the House of Lords is due to debate a motion moved by Baroness Fairhead, Minister of State at the Department for International Trade, that “this House takes note of the future of United Kingdom trade and customs policy in the light of Her Majesty’s Government white papers [Preparing for our Future UK Trade Policy](#) (Cm 9470) and [Customs Bill: Legislating for the UK’s Future Customs](#) (Cm 9502)”.

This Lords Library Briefing sets out the background to the publication of these two white papers and briefly summarises their contents. A selection of key documents, including some commentary on the Government’s proposals for customs and trade policy, is identified at the end of the briefing.

This briefing does not focus on the specific issues relating to Northern Ireland, or proposals to avoid the creation of a hard border between Northern Ireland and Ireland. The Government has issued a separate publication, [Northern Ireland and Ireland: Position Paper](#), which outlined how it believed customs might be managed between Northern Ireland and Ireland. Further background information can be found in the House of Lords Library briefing, [Leaving the European Union: The UK and Ireland](#) (13 March 2017), whilst the latest state of negotiations is discussed in the House of Commons Library briefing, [Brexit: The November Negotiations](#) (24 November 2017).

Government and EU Trade Relations

Following the June 2016 referendum vote in favour of leaving the European Union, one of the key issues to emerge is the future of UK trade, both with the EU and with the world more widely. The EU, taken as a whole is the UK’s largest trading partner.¹ In 2016, UK exports to the EU were £236 billion, equivalent to 43 percent of all UK exports. UK imports from the EU were £318 billion, equivalent to 54 percent of all UK imports.²

Negotiations between the European Union and the UK to date have not included any discussion of future trade arrangements between the EU and UK. Instead, the negotiations have been limited to issues such as the rights of UK citizens in the EU and EU citizens in the UK after Brexit, reaching a financial settlement, and what happens with the border between the Republic of Ireland and Northern Ireland. The European Commission currently has no mandate to discuss transitional arrangements or future relations with the UK, with negotiating directives stating: “As soon as the European Council decides that sufficient progress has been achieved to allow negotiations to proceed to the second phase, there will be new sets of negotiating directives”.³ On 14 and 15 December the leaders of the other 27 European Union countries are due to meet at the European Council to discuss whether sufficient progress has been made in negotiations to justify moving to phase two of the negotiations, that is those on the future relationship between the EU and UK and transitional arrangements.

Although discussions regarding transitional arrangements and the future relationship have not yet commenced, there have been several indicators as to what the Government would like to achieve with regards to trade. In its white paper on [The United Kingdom's Exit From and New Partnership with the European Union](#) (February 2017), the Government confirmed that it would leave the single market and the customs union, and stated:

The Government will prioritise securing the freest and most frictionless trade possible in goods and services between the UK and the EU. We will not be seeking membership of the single market, but will pursue instead a new strategic partnership with the EU, including an ambitious and comprehensive free trade agreement and a new customs agreement [...] By leaving the EU we will have the opportunity to strike free trade agreements with countries around the world. We will be champions of free trade driving forward liberalisation bilaterally, as well as in wider groupings, and we will continue to support the international rules based system.⁴

More recently, during a speech in Florence on 22 September 2017, the Prime Minister, Theresa May, reiterated her support for a transitional period “of around two years”, during which access to markets would continue on current terms and Britain would continue to take part in existing security measures. In addition, she rejected the “stark and unimaginative choice” between a model based on European Economic Area membership and a traditional free trade agreement, commenting “we can do so much better than this”.⁵

Single Market

At present the UK is, by virtue of being a member of the EU, part of the customs union and the single market. Being part of the single market means that there are no tariffs or quotas on goods between the UK and other EU member states. In addition, non-tariff barriers to trade, such as differing regulations on labelling, are removed. The single market is based on “four freedoms”; free movement of goods, services, capital and people. The freedom of movement of people, in particular, was an issue that was raised during the referendum campaign with some Leave campaigners arguing that leaving the EU would mean the UK would “take back control” of its borders and immigration.⁶

Explaining the Government’s decision to leave the single market, the Prime Minister stated: “we understand that the single market’s four freedoms are indivisible for our European friends. We recognise that the single market is built on a balance of rights and obligations. And we do not pretend that you can have all the benefits of membership of the single market without its obligations”.⁷

Customs Union

The UK is also currently part of the EU customs union. Customs unions are extensions of conventional free trade agreements (FTAs), where parties to the agreement have agreed to provide each other with trade benefits such as reduced or removed tariffs.⁸ In addition to this basic premise, customs unions apply a common external tariff across their members. Therefore, goods imported from outside the customs union into one member of a customs union should attract the same tariffs as those imported into another. Customs unions can help facilitate trade between their members by removing the need for complex ‘rules of origin’ for goods imported into the trade area from third countries. Members of the World Trade Organisation are able to establish customs unions (and FTAs) in accordance with article XXIV of the General Agreement on Tariffs and Trade.⁹

However, membership of the customs union restricts a member state's ability to negotiate its own trade policies. Whilst the UK remains a member of the EU customs union, and is bound by the Common Commercial Policy, it is unable to sign its own FTAs with countries outside of the EU.

The Government's assessment of options for a new customs agreement with the EU was outlined in the Government's [Future Customs Arrangements: A Future Partnership Paper](#) (August 2017). In addition, the Department for International Trade's white paper, [Preparing for our Future UK Trade Policy](#), noted:

The United Kingdom has a long and proud history as a great trading nation and champion of free trade with all parts of the world. We want to maximise our trade opportunities globally and across all countries—both by boosting our trading relationships with old friends and new allies, and by seeking a deep and special partnership with the EU.¹⁰

Both publications are discussed in more detail below.

European Economic Area and Free Trade Agreements

One of the other permutations for a trade relationship with the EU dismissed by the Prime Minister in her Florence speech was membership of the European Economic Area (EEA). The Agreement on the European Economic Area entered into force on 1 January 1994. It brings together the EU member states and Iceland, Liechtenstein and Norway in a single market. The EEA Agreement:

[...] guarantees equal rights and obligations within the internal market for individuals and economic operators in the EEA. It provides for the inclusion of EU legislation covering the four freedoms—the free movement of goods, services, persons and capital—throughout the 31 EEA States. In addition, the Agreement covers cooperation in other important areas such as research and development, education, social policy, the environment, consumer protection, tourism and culture, collectively known as “flanking and horizontal” policies. The Agreement guarantees equal rights and obligations within the internal market for citizens and economic operators in the EEA. The EEA Agreement also states that when a country becomes a member of the European Union, it shall also apply to become party to the EEA Agreement (Article 128), thus leading to an enlargement of the EEA.¹¹

The EEA does not include membership of the customs union, therefore rules of origin do apply. In addition, EEA members are subject to EU legislation regarding the four freedoms. During her September 2017 speech in Florence, the Prime Minister outlined why the UK would not be seeking a model based on EEA membership:

European Economic Area membership would mean the UK having to adopt at home—automatically and in their entirety—new EU rules. Rules over which, in future, we will have little influence and no vote. Such a loss of democratic control could not work for the British people.¹²

In addition, the Prime Minister rejected “traditional free trade agreements, such as that the EU has recently negotiated with Canada”. She noted that an agreement such as that between the EU and Canada, though advanced, would mark a restriction in the mutual market access currently enjoyed by the EU and UK. In addition, she argued, it did not take account of the pre-existing regulatory relationship between the EU and UK.¹³

Future Customs Relations Arrangements

In August 2017, the Government published [Future Customs Arrangements—A Future Partnership Paper](#). The document outlined the Government’s three strategic aims in its future relationship with the EU outside the EU customs union: ensuring UK-EU trade is as frictionless as possible; avoiding a ‘hard border’ between Ireland and Northern Ireland; and establishing an independent international trade policy.¹⁴ The paper suggested two possible approaches to the future customs relationship with the EU:

A highly streamlined customs arrangement between the UK and the EU, streamlining and simplifying requirements, leaving as few additional requirements on EU trade as possible. This would aim to: continue some of the existing arrangements between the UK and the EU; put in place new negotiated and potentially unilateral facilitations to reduce and remove barriers to trade; and implement technology-based solutions to make it easier to comply with customs procedures. This approach involves utilising the UK’s existing tried and trusted third country processes for UK-EU trade, building on EU and international precedents, and developing new innovative facilitations to deliver as frictionless a customs border as possible.

A new customs partnership with the EU, aligning our approach to the customs border in a way that removes the need for a UK-EU customs border. One potential approach would involve the UK mirroring the EU’s requirements for imports from the rest of the world where their final destination is the EU. This is of course unprecedented as an approach and could be challenging to implement and we will look to explore the principles of this with business and the EU.¹⁵

The paper also suggested a time-limited interim period to implement the new customs arrangements and avoid a ‘cliff-edge’ for businesses and individuals in both the EU and UK.

In October 2017, HM Treasury published the white paper, [Customs Bill: Legislating for the UK’s Future Customs, VAT and Excise Regimes](#). The white paper reiterated the Government’s strategic objectives set out in the future partnership paper, namely ensuring UK-EU trade is as frictionless as possible; avoiding a ‘hard border’ between Ireland and Northern Ireland; and establishing an independent international trade policy. The paper also echoed the Florence speech of the Prime Minister, highlighting that the UK would not look to replicate models which other countries have in place for their trade relations with the EU, but instead pursuing an option that would work best for the UK.

The paper called for a time-limited interim implementation period to assist businesses and people in the UK, by ensuring that they would only need to adjust once to a new customs relationship.¹⁶ In addition, as the UK leaves the EU, the Government would seek to keep UK law as consistent as possible with EU law, responding to business requests for continuity and certainty.¹⁷ With regards to the situation in Northern Ireland, the Government noted that the land border with Ireland made it a “unique case”, and argued that there would be “no return to the borders of the past”.¹⁸

Finally, the customs bill white paper provided more details regarding the proposed domestic legislation concerning customs, VAT and excise. This legislation was introduced to the House of Commons in November 2017. The [Taxation \(Cross-Border\) Trade Bill](#) seeks to implement a standalone customs regime, and to amend the VAT and excise regimes so that they can function effectively after the UK has left the EU.

At present the authority to charge customs duty is contained in the European Communities Act 1972 (as amended) which will be repealed by the European Union (Withdrawal) Bill. As explained in the white paper, the powers in the Withdrawal Bill cannot be used to impose or increase taxation, which includes customs duties, excise or VAT; separate legislation, in the form of the Taxation (Cross-Border Trade) Bill, was therefore required.¹⁹ The Bill would include provisions to amend the VAT and excise regimes so that they would be able to function after the UK has left the EU, both in relation to trade with the EU, but also with the world more widely. The Bill would make provision for any agreement that was made with the EU, including a time limited implementation period. The Bill would also allow for a customs regime in the event that no agreement is negotiated between the EU and UK.

At present, no date has been set for the second reading of the Bill; although debate did take place on the ways and means resolutions which accompanied the Bill's first reading in the House of Commons on 20 November 2017.

UK Trade: Outside the EU

Figures from the Office for National Statistics' most recent publication of the *Pink Book* show that the UK had a trade deficit of £82 billion with the EU in 2016 but a surplus of £39 billion with non-EU countries.²⁰ Aside from the EU, the United States is the UK's largest trading partner, while the Commonwealth accounts for around 10 percent of UK trade.²¹

While the UK has been part of the European Union it has been unable to operate its own independent trade policy because trade agreements are negotiated by the EU; to date the EU has trade agreements with around 60 countries.²² In October 2017, the Department for International Trade published [Preparing for our Future UK Trade Policy](#), which seeks to outline the Government's approach to establishing an independent international trade policy. The paper provides background on issues, such as trade remedies and becoming a member of the Agreement on Government Procurement, which would be provided for in future domestic legislation.

In addition, it outlines some of the Government's ambitions and priorities. For example, the paper emphasises the importance of the World Trade Organisation (WTO) and a "rules based global trading environment". The paper also highlights the Government's ambition to boost trade relationships, stating:

We already have a range of trade relationships in place with different markets, and will continue to improve and progress our bilateral trading relationships. There are many ways in which the UK can strengthen its trade and investment relationships with partners across the world. One important way is to agree a Free Trade Agreement (FTA) and a number of countries have shown a keen interest in doing so. But a range of options is available to us, from discrete bilateral agreements to broader regional types of partnerships. We will examine the range of relationships that are appropriate and available to us, drawing on best practice from the EU and elsewhere.²³

It reiterates the Government's desire for a time-limited transition period with the EU, during which access to each other's markets should continue on current terms. In addition, the paper suggests that the Government "will seek to transition all existing EU trade agreements and other EU preferential arrangements".²⁴ It is not clear whether transition of EU trade arrangements and preferential arrangements with third countries will automatically apply to the UK when it leaves the EU. Both the House of Lords European Union Committee and House of Commons International Trade Committee have urged the Government to seek clarification on the issue.²⁵

The paper also discusses how the Government will seek to build new trade arrangements, through improving bilateral trading arrangements, for example through trade reviews and ministerial dialogues, and deepening trading links.²⁶ In relation to developing countries, the paper seeks views on a unilateral trade preference scheme, which would put in place a preference scheme for developing countries which, as a minimum, provides the same level of access as the current EU trade preference scheme for developing countries.²⁷

The Government's white paper was followed by the [Trade Bill](#), which was introduced into the House of Commons on 7 November 2017. The Bill seeks to implement measures to build a future trade policy for the UK once it has left the EU, as outlined in the white paper. It includes provisions that would create powers to ensure that the UK can implement any procurement obligations arising from the UK becoming a member of the Agreement on Government Procurement (currently the UK is a member by virtue of EU membership), implementation of agreements with partner countries corresponding to the EU's FTAs and other trade agreements in place before the UK's exit from the EU; and setting out the basis of a new Trade Remedies Authority (TRA) to deliver the new UK trade remedies framework.

Key Documents

- HM Treasury, [Customs Bill: Legislating for the UK's Future Customs, VAT and Excise Regimes](#), October 2017, Cm 9502, pp 3–4
- Department for International Trade, [Preparing for Our Future UK Trade Policy](#), October 2017, Cm 9470, pp 5–9
- Daniel Boffey, '[Brexit: UK Likely to End up with Canadian-style Deal, warns Barnier](#)', *Guardian*, 24 October 2017
- Ben Kentish, '[Labour Would Strike EU Deal to Give UK 'Unimpeded Access to the Single Market after Brexit,' says Jeremy Corbyn](#)', *Independent*, 27 September 2017
- Liberal Democrats, '[Responding to Keir Starmer's Speech to Labour Conference](#)', accessed 30 November 2017
- Nikhil Datta and Dr Swati Dhingra, '[Post-Brexit UK Trade Policy: Still just a Wish List](#)', *The UK and a Changing Europe*, 9 November 2017
- Confederation of British Industry, [CBI Response to the HMT White Paper on Customs](#), November 2017
- Dr Michael Gasiorek '[Groundhog Day: Is the Government White Paper on Trade and Customs Bill a Step Forward?](#)', UK Trade Policy Observatory, 11 October 2017

Further Information

- Institute for Government, [Implementing Brexit: Customs](#), September 2017
- Institute for Government, [Frictionless Trade? What Brexit means for Cross-Border Trade in Goods](#), August 2017
- European Parliament, [The Consequences of Brexit for the Customs Union and the Internal Market Acquis for Goods](#), October 2017
- House of Commons International Trade Committee, [UK Trade Options Beyond 2019](#), 7 March 2017, HC 817 of session 2016–17; and [Government Response](#)
- House of Lords European Union Committee, [Brexit: Trade in Non-Financial Services](#), 22 March 2017, HL Paper 135 of session 2016–17; and [Brexit: Trade in Goods](#), 14 March 2017, HL Paper 129 of session 2016–17

- House of Lords Library, [Leaving the European Union: Customs Unions—An Introduction](#), 27 January 2017

¹ Office for National Statistics, [UK Balance of Payments: The Pink Book 2017](#), 31 October 2017. For more detailed analysis of the figures see: House of Commons Library, [Statistics on UK-EU Trade](#), 7 November 2017.

² House of Commons Library, [Statistics on UK-EU Trade](#), 7 November 2017, p 3.

³ Council of the European Union, [Directives for the Negotiation of an Agreement with the United Kingdom of Great Britain and Northern Ireland Setting out the Arrangements for its Withdrawal from the European Union](#), 22 May 2017.

⁴ HM Government, [The United Kingdom's Exit From and New Partnership with the European Union](#), February 2017, Cm 9417, pp 35 and 51.

⁵ Foreign and Commonwealth Office et al, [PM's Florence Speech: A New Era of Cooperation and Partnership between the UK and the EU](#), 22 September 2017.

⁶ Ben Riley-Smith, 'Leave or Remain in the EU? The Arguments for and against Brexit', *Telegraph* (£), 20 June 2016.

⁷ Foreign and Commonwealth Office et al, [PM's Florence Speech: A New Era of Cooperation and Partnership between the UK and the EU](#), 22 September 2017.

⁸ House of Lords Library, [Leaving the European Union: Customs Unions—An Introduction](#), 27 January 2017, p 1.

⁹ For more information on how customs unions operate, how they differ from free trade agreements, and how they interact with World Trade Organisation rules on most-favoured-nation status, see: House of Lords Library, [Leaving the European Union: Customs Unions—An Introduction](#), 27 January 2017.

¹⁰ Department of International Trade, [Preparing for our Future UK Trade Policy](#), October 2017, Cm 9470, p 5.

¹¹ European Free Trade Association, 'EEA Agreement', accessed 29 November 2017.

¹² Foreign and Commonwealth Office et al, [PM's Florence Speech: A New Era of Cooperation and Partnership between the UK and the EU](#), 22 September 2017.

¹³ *ibid.*

¹⁴ HM Government, [Future Customs Arrangements—A Future Partnership Paper](#), August 2017, p 6.

¹⁵ *ibid.*, p 2.

¹⁶ HM Treasury, [Customs Bill: Legislating for the UK's Future Customs, VAT and Excise Regimes](#), October 2017, Cm 9502, p 3.

¹⁷ *ibid.*, p 3,

¹⁸ *ibid.*, p 4.

¹⁹ *ibid.*, p 11.

²⁰ Office for National Statistics, [UK Balance of Payments: The Pink Book 2017](#), 31 October 2017, table 9.3.

²¹ For more details see: House of Commons Library, [Geographical Pattern of UK Trade](#), 7 November 2017.

²² House of Commons Library, [Brexit: Trade Aspects](#), 9 October 2017, p 26,

²³ Department for International Trade, [Preparing for our Future UK Trade Policy](#), October 2017, Cm 9470, p 29.

²⁴ *ibid.*, p 8.

²⁵ House of Lords European Union Committee, [Brexit: The Options for Trade](#), 13 December 2016, HL Paper 72 of session 2016–17, p 50, para 168; and House of Commons International Trade Committee, [UK Trade Options Beyond 2019](#), 7 March 2017, HC 817 of session 2016–7, pp 59–60, para 202.

²⁶ Department for International Trade, [Preparing for our Future UK Trade Policy](#), October 2017, Cm 9470, p 29.

²⁷ *ibid.*, p 31.

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