

The temporary tariff regime: the magic pill for the post-Brexit EU-UK trade headache?

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Introduction

After multiple rejections of the Withdrawal Bill by the House of Commons, it has become more likely that the United Kingdom (UK) will leave the European Union (EU) under the 'no-deal option'. Such failure to enter into an agreement with the EU before 'Brexit Day' (now 12 April or 22 May 2019),^[1] means that speculations are rife about the options for continuation of the trading relations between the EU and the UK under the no-deal scenario. Thankfully, it has already been clarified that trade under the World Trade Organization (WTO) rules is the default option for trade between the EU and the UK in absence of an agreement before Brexit.^[2]

The trade under WTO terms has been considered as the 'most costly in economic terms' and imposes significant restrictions on preferential treatment by the UK and the EU for each other.^[3] If the UK chooses to counteract this situation through a system of low tariffs for the EU products, it will have to replicate the same for third countries keeping in view the Most Favoured Nation (MFN) principle of Article I:1 of the GATT. Trade under the WTO rules leaves no simple options for the UK in its aim to prevent sudden price increases as a result of restriction on free trade with the EU, its largest trading partner and a key supplier of essential commodities. The UK and EU economies are closely interlinked and the UK will have to take exceptional measures such as near zero tariffs to prevent any sudden shocks to businesses.

The hard truth on trade with the EU under WTO rules

First things first: what does trading under WTO rules mean for EU-UK trade? The UK will have to impose tariffs on products from the EU which are equivalent to the tariffs

imposed by it on other WTO Members under the MFN principle. On the opposite side, the EU will impose its Common Customs Tariffs (CCT) on imports from the UK at the same rate it imposes on other third countries.[4] This means a major change since the UK currently trades under a tariff-free regime with the EU as part of the EU Single Market.[5] Beyond the EU, the UK has also not been able to enter into FTAs with third countries and in practice only a few agreements (*inter alia* with Switzerland, Fiji/Papua New Guinea, Chile and Faroe Islands) have been signed.[6]

The UK realises that any tariffs that it imposes on imports from EU can have severe consequences on supply chains and keeping this in mind, the UK Department for International Trade has published its Temporary Tariff Regime (TTR) for a no-deal Brexit with very low tariffs or zero tariffs being applied for up to 12 months after a no-deal Brexit.[7] As per the declaration, 87% of goods imported into the UK will enjoy temporary tariff-free access and for the remaining 13% of goods, low tariffs will be imposed. The goods with the (low) tariffs originate in sensitive sectors, *inter alia* the agriculture and automotive sectors. Notably, the temporary tariffs will not apply to goods from Ireland crossing the border into Northern Ireland.

Essentially, the UK has attempted to recreate the present free trade situation with the EU and its trading partners by choosing the path of applying low tariffs under the no-deal option to make sure prices in the UK do not go up drastically. The TTR acts as a bridge between the current free trade situation and the application of WTO rules on trade with the EU and the rest of the world. Even if the UK may not have wanted to extend the benefits of near zero and low tariffs to the non-EU countries, it was forced to do so owing to the MFN principle of the WTO.

While, the UK has attempted to soften the impact of the new tariff-based trading regime with the EU, it is still an imperfect solution considering that it imposes restrictions on certain products from the EU (agricultural products, fish, certain garments) which previously enjoyed tariff free access. Even though such a low tariff regime may ensure low prices for the consumers, it can create significant impediments in government decisions on trade policy and affect the UK bargaining position in future trade negotiations where there will be no incentives for the negotiating partners to reduce tariffs since they can already access the UK market at very low tariffs.

It is also remarkable that the TTR focusses entirely on tariff measures following a no-deal Brexit. Non-tariff barriers (NTBs) such as import licenses, customs valuations,

standards and rules of origin give rise to costs considerably higher than tariff costs.[8] Under the current EU rules, these costs have been eliminated based on mutual arrangements with trade partners or harmonized rules within the EU such as the regulation on mutual recognition of products[9] and harmonised standards.[10] Despite the fact that the European Union (Withdrawal) Act sets out in principle that direct EU legislation will be incorporated as domestic UK law on Brexit Day,[11] the EU can in theory hold exports from the UK at the border to execute physical checks and controls to establish compliance with EU rules in the absence of mutual agreements between the two trading partners.[12] Considering this impact, the UK may also be required to undertake (temporary) arrangements to overcome the burden of NTBs.

The Temporary Tariff Regime: WTO rules-compliant ... or not?

The TTR tries to find a middle ground between having to extend the current tariff free trade regime with the EU to all other WTO Members resulting in a free access to its market on the one hand and preventing a sudden impact on the UK economy resulting from tariff barriers on trade with the EU on the other hand. The UK has designed the TTR in a manner through which it seeks to protect its economy from a sudden shock. To achieve this, it has extended the benefit of this tariff free regime to all WTO Members uniformly, thereby *prima facie* respecting the Most Favoured Nation (MFN) principle enshrined in Article I:1 GATT.

Even with the balancing act, the TTR has attracted immediate controversy upon its announcement due to the unique provision for separate tariffs for Northern Ireland and the rest of the UK. This exception at first glance indicates a textbook violation of the MFN principle since products coming through or from Ireland have been provided duty free access to Northern Ireland, while the TTR (and its tariffs) will apply to imports of the same products in the rest of the UK. While the UK Government itself realises that the measure may be challenged in the WTO,[13] on ground, this situation has raised concerns about the smuggling of products into the UK mainland in the absence of customs checks for products being transferred to mainland UK through Northern Ireland.[14] While this may be a political concern, this special exemption for Northern Ireland appears to be a violation of the MFN principle since different tariffs are imposed on the same products within the same country.[15]

Can the UK justify a possible violation?

The legality of the TTR will ultimately be determined under the WTO dispute resolution procedures if any WTO Member raises a formal complaint against it. In such a scenario, the UK government could put forward a few different arguments justifying this potential violation of the MFN principle while providing the special exemption for Northern Ireland starting with the public morals exception of Article XX(a) of the GATT.

Theoretically, the use of an Article XX GATT exception can indeed act as an exemption to the implementation of the MFN principle, but the use of such an exception has to be justified by the implementing state through a two-tiered test as laid down by the Appellate Body in *US - Gasoline*.^[16] First, the justification of the measure under the exception itself and second under the chapeau of Article XX. In this test, under the first step, the measure has to be covered under the principle of 'public morals'. The meaning of the term 'public morals' has been considered to be quite wide by the Panel in *China - Publications and Audiovisual Products* which has determined that it 'denotes standards of right and wrong conduct maintained by or on behalf of a community or nation', but is 'influenced by each Members' prevailing social, cultural, ethical and religious values'.^[17] It has however been prescribed that to fulfil the test, the measure must be 'designed' to protect public morals and must be 'not incapable of' protecting public morals. In the present situation, it can at least be argued on paper that the current measure of providing for tariff free trade on the Irish border has a linkage to the need for continued maintenance of relationships between the closely-knit Irish community, a part of which resides in Northern Ireland. In other words, the measure was 'necessary' because of the need for protecting the hundreds of years of relationships of the Northern Irish residents with the other side of the border. This argument can be strengthened by stating that there was no 'reasonably available' alternative. Ireland and Northern Ireland share a long common land border where the alternative option of imposing border checks after dividing the boundaries would be unreasonable owing to the sensitiveness of the Good Friday Agreement.

For the second step, even if a justification of the exception could be made using the specific provision of Article XX GATT, the validity of the measure is subject to the fulfilment of the chapeau requirement that no arbitrary or unjustifiable discrimination nor a disguised restriction of international trade may be implemented by applying an exception. The burden of proof to justify a measure as compliant with the chapeau is a higher burden than proving the exception under the specific provision itself.^[18] In the present case, determining that the measure is not arbitrary as per the conditions of the chapeau could be challenging and whether such a

defence would be successful is subject to final determination by the Panel and the Appellate Body. However, in practical terms, the dispute may not even reach the Appellate Body since the TTR is only for a 12-month period and Panel proceedings normally take around the same time and hence by the time, the Panel reaches a decision, the TTR may no longer be in force thus removing the need for determining its validity.

Will the UK go down the road 'not' to be taken?

The possibility for justification of the Irish exemption through the provisions of the national security exception (Article XXI GATT) has also been proposed. The potential misuse of the national security exemption is already under debate owing to its use by the US to justify the 2018 steel tariffs.^[19] The national security exception is considered by certain states to be a self-judging exception,^[20] but owing to its extraordinary nature has rarely been used and is considered as a measure of last resort.^[21] Traditionally, WTO Members have sought to hide behind the defence of the self-judging nature of Article XXI GATT to prevent potential judicial scrutiny of measures. Potentially, the UK could follow this view and declare that its exceptional measures for Northern Ireland are based on the exception, thus effectively excluding adjudication before a WTO Panel. This would, however, add fuel to the current debate on misuse of the provision. Also, contrary to the traditional view, a recent submission by the EU in the *Russia – Measures Concerning Traffic in Transit* case shows a gradual change in position of states regarding this provision, wherein they now consider that invocation of the national security exception should also come under the scrutiny of the WTO-DSB.^[22]

Are issues about MFN the only concern?

Beyond the potential violation of the MFN principle, another major question is whether the UK also violates its obligation to administer trade laws in a 'uniform, impartial and reasonable manner' as enshrined in Article X:3 GATT. By planning to implement the tariffs in a non-uniform way across its territory (zero tariffs for Northern Ireland, tariffs for the rest of the UK), the UK may be in violation of its obligations under this provision. While a legal interpretation by a WTO Panel or the Appellate Body is missing for this provision, the same term 'uniform' has been interpreted as covering a geographical dimension by a Panel, and the Appellate Body under Article X:2 GATT.^[23] If this interpretation is any indication, then the varied implementation of the TTR within its borders may indeed be a violation of Article X:3

GATT by the UK. Whether the current situation of applying no tariffs on Irish products at the Northern Irish border violates this UK obligation is unclear and must be decided in an adjudicatory procedure.

Conclusion

From the beginning, it was clear that the default option of trade under the WTO rules is an undesired outcome of Brexit. In an attempt to mitigate the impact of such no-deal Brexit, the UK has tried to replicate the trade arrangement it currently enjoys through low tariffs under the Temporary Tariff Regime to provide a transition period to adjust to the new realities. Such measures are, however, insufficient to prevent a tariff shock in the UK and are in addition vulnerable to a potentially successful WTO challenge arising from the special situation for Irish goods crossing the Northern Ireland border, should a WTO Member decide to challenge the regime.

[1] For discussions on the new Brexit dates, see <https://www.politico.eu/article/eu-leaders-grant-brexit-extension-with-strings-attached/> (28/3/2019).

[2] The Official Position of the UK Government on this issue can be seen at <https://www.gov.uk/government/publications/existing-trade-agreements-if-the-uk-leaves-the-eu-without-a-deal/existing-trade-agreements-if-the-uk-leaves-the-eu-without-a-deal> (28/3/2019).

[3] The House of Commons Briefing Paper on Brexit: Trade Aspects, January 2017. The paper can be accessed at http://www.europarl.europa.eu/meetdocs/2014_2019/documents/deea/dv/8-1-brexit-trade_20170209_/8-1-brexit-trade_20170209_en.pdf (28/3/2019).

[4] The Regulation on Common Customs Tariff Legislation can be accessed at <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:31987R2658&from=en> (28/3/2019).

[5] For a discussion on this issue, see, <https://verfassungsblog.de/wto-option-in-practice-how-a-no-deal-brexit-would-seriously-damage-key-uk-industries/> (28/3/2019).

[6] The list of post-Brexit trade agreements can be seen at <https://www.gov.uk/government/publications/existing-trade-agreements-if-the->

[uk-leaves-the-eu-without-a-deal/existing-trade-agreements-if-the-uk-leaves-the-eu-without-a-deal](#) (28/3/2019).

[7] The Temporary Tariff Regime can be accessed at <https://www.gov.uk/government/news/temporary-tariff-regime-for-no-deal-brex-it-published> (28/3/2019).

[8] For discussion on this issue, see <https://voxeu.org/article/impact-non-tariff-barriers-eu-goods-trade-after-brex-it> (28/3/2019) and <https://www.bbc.com/news/uk-45112872> (28/3/2019).

[9] The EU Regulation on mutual recognition of products can be found at: <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:32008R0764> (28/3/2019).

[10] Harmonised Standards, https://ec.europa.eu/growth/single-market/european-standards/harmonised-standards_en (28/3/2019).

[11] The text of the Withdrawal Act can be found at <http://www.legislation.gov.uk/ukpga/2018/16/contents/enacted> (28/3/2019).

[12] Brexit Briefing, http://www.cbi.org.uk/cbi-prod/assets/File/pdf/17%2009%2011%20No%20Deal%20write%20up_FINAL.pdf (28/3/2019).

[13] Zero tariff plan for Irish border could face WTO legal threat, says Gove, The Guardian, <https://www.theguardian.com/politics/2019/mar/27/zero-tariff-plan-irish-border-could-face-wto-legal-threat-gove-brex-it> (28/3/2019).

[14] Smugglers big winners from UK's Ireland border plan, Politico, <https://www.politico.eu/article/smugglers-paradise-ireland-no-deal-brex-it/> (28/3/2019).

[15] Brexit: Does NI tariffs plan violate WTO law? BBC, <https://www.bbc.com/news/uk-northern-ireland-47559880> (28/3/2019).

[16] Report of the AB, *United States – Standards for Reformulated and Conventional Gasoline*, WT/DS2/AB/R, 29 April 1996.

[17] Report of the Panel, *China – Publications and Audiovisual Products*, WT/DS363/R, 12 August 2009, para. 7.759.

[18] Report of the AB, *United States – Standards for Reformulated and Conventional Gasoline*, WT/DS2/AB/R, 29 April 1996, p. 22 and 23.

[19] Communication from the United States, *United States – Certain Measures on Steel and Aluminium Products*, WT/DS544/2, 17 April 2018.

[20] For a detailed study on its perceived self-judging nature (arguable), see Peter Lindsay, *The Ambiguity of GATT Article XXI: Subtle Success or Rampant Failure*, 52 *Duke Law Journal* 1277-1313 (2003).

[21] Summary Record of the Twenty-Second Meeting of the Contracting Parties (GATT), CP.3/SR22 - II/28, 8 June 1949.

[22] Third Party Oral Statement by the European Union, *Russia – Measures Concerning Traffic in Transit*, DS512, 25 January 2018.

[23] Report of the Panel, *United States – Certain Country of Origin Labelling (Cool) Requirements*, WT/DS384/R WT/DS386/R, 18 November 2011, para. 7.876; Report of the AB, *United States – Countervailing And Anti-Dumping Measures On Certain Products From China*, AB-2014-4, 14 April, 2014, para. 4.82.