Brexit in perspective

Episode 2: Global Britain – A Free Trading Future?

March 2017

BRUNSWICK

The trade negotiations arising from Britain's exit from the EU will provide businesses with a unique opportunity to help set the terms of their trade with the rest of the world for a generation.

The UK Government's Brexit White Paper makes clear that Britain will leave the Single Market: the EU's project to deepen economic cooperation through the 'four freedoms' of goods, services, workers and capital.

The document also suggests that Britain will leave the Customs Union, which allows UK goods to circulate freely within the EU without tariffs or customs checks for conformity with EU standards.

These changes require a new legal framework to be put in place, one which is compliant with existing World Trade Organization rules, and clearly establishes the UK's new trading relationship with the EU.

Trade negotiations take around five years on average and agreements are only re-visited every 20-30 years. It is therefore critical that businesses consider their trading interests and present them clearly and strongly to key policy-makers on all sides of the negotiations to ensure their future success.

Alongside these opportunities, however, are unprecedented risks. Increasingly engaged activists, controversy around traditional trade agreement clauses including investor state dispute settlement, intellectual property and agriculture tariffs, combined with the election of anti-trade populist leaders around the world mean that global trade liberalisation can no longer be taken for granted.

For businesses to succeed in this environment, it is essential that they have the right support from the beginning of the negotiation process.

They need to start thinking actively about how to engage Westminster and Whitehall, as well as the European Commission and foreign governments, on their priorities and cannot assume that these actors understand their sector or their needs.

Companies and sectors that fail to get their priorities into the government's negotiating brief will be playing catch up for the next five years or more.

To help clients prepare for Britain's post-Brexit trading environment, Brunswick has an unparalleled network of European and international offices to provide critical advice and support before, during and after the negotiations.

This note looks at the different scenarios for post-Brexit trade and distils some of the key advice from recent Brunswick events with trade negotiators so companies can prepare their engagement strategies and ensure the best outcomes for their business and sector, no matter the shape of the final deal.

Trade rules at a glance

The UK is leaving the EU Single Market and Customs Union. What is the global trade framework?

World Trade Organization

- In the absence of EU Membership and ratified Free Trade Agreements (FTAs), Britain's ability to trade around the world is governed by the World Trade Organization (WTO).
- The UK entered the WTO as part of the EU and will need to disentangle its current membership as part of the Brexit process.
- The UK's tariff levels for goods and services are currently agreed and listed as part of the EU's schedules. Britain has committed to replicating its current schedules as far as possible to ensure a predictable and comprehensive outcome.
- The UK's new schedules will need to be agreed by all of the other 163 WTO Member States as part of the WTO's consensus decision making process.
- The WTO uses members bound tariff rates and the most favoured nation (MFN) clause to keep tariffs down. Members may apply tariff rates below their binding agreements, but cannot raise them, and members must offer all others the same tariff rates they offer to their MFN partner.
- Countries may, however, enter into bilateral and regional FTAs without offering the same tariff reductions to all WTO Members provided that they have established free trade on substantially all trade within the FTA, and that the parties do not raise their tariffs or other barriers against countries outside the agreement.
- In the event of a country breaching WTO rules, it can be taken before the WTO's dispute resolution system by another member. Dispute resolution decisions may involve the application of punitive tariffs.

Investor State Dispute Settlement (ISDS)

ISDS is a standard provision in FTAs and Bilateral Investment Treaties (BITs), that allows corporations to take governments to binding arbitration in the event of legislation that hurts expected future profits or interest, if there is expropriation, discrimination or denial of justice within the country of investment. Whilst the broad framework is standard, ISDS provisions vary considerably among agreements.

ISDS has become increasingly controversial as NGOs and protest groups have accused companies of exploiting arbitration provisions in FTAs and BITs in order to overturn domestic legislation, in opposition to public interest. Much of the strong opposition that helped derail the proposed EU- US FTA (TTIP) was based on concerns around the proposed ISDS provisions.

European Union Free Trade Agreement

The UK's proposed negotiation of an FTA with the EU is unique in trade negotiation history. Both sides are already starting with zero tariffs on goods and a common regulatory framework.

The UK Government's White Paper confirms that Britain will be seeking continued tariff-free trade in goods, meaning that the primary focus of the negotiations is likely to be services and regulations, although agricultural products and movement of labour are also likely to prove contentious. Implementing a customs border between the UK and the EU will pose an enormous logistical challenge, almost certainly necessitating a transition period as the new arrangements come into force.

Expectations are for the final deal to resemble the EU Canada 'Comprehensive Economic and Trade Agreement' (CETA), the EU's most recently negotiated and ambitious trade agreement. CETA provides for trade liberalisation and reduced barriers across areas such as investment, government procurement, labour and the environment as well as goods and services. CETA does not, however, cover financial services – a key negotiating interest for the UK in its deal with the EU.

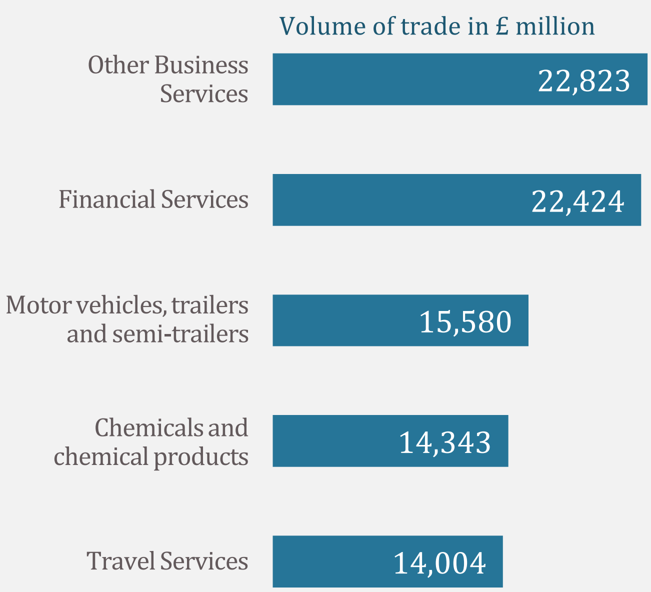
Given the starting point, the UK is likely to seek a deal with the EU that improves on CETA's outcomes, particularly in services and agriculture, an outcome commonly referred to as 'CETA Plus'.

The final deal will also need to agree a mechanism for addressing disputes between the parties, another potential flashpoint given UK determination to 'take back control' of its sovereignty, as well as the current hostile public environment towards ISDS.

As with CETA, any trade agreement between the UK and the EU will almost certainly need to be ratified by all member states, including by national and sub-national parliaments, as well as the European Parliament. This is a complicated process which can take up to a year depending on parliamentary schedules and is vulnerable to opposition from special interests. In particular, the deal risks attracting the ire of anti-trade groups which have been vocal in their opposition to CETA and to the proposed EU FTA with the USA (TTIP).

It will therefore be extremely difficult to conclude and ratify a comprehensive UK-EU FTA before March 2019, when it is expected that Brexit will take effect.

Top 5 UK Exports to the EU (2015)



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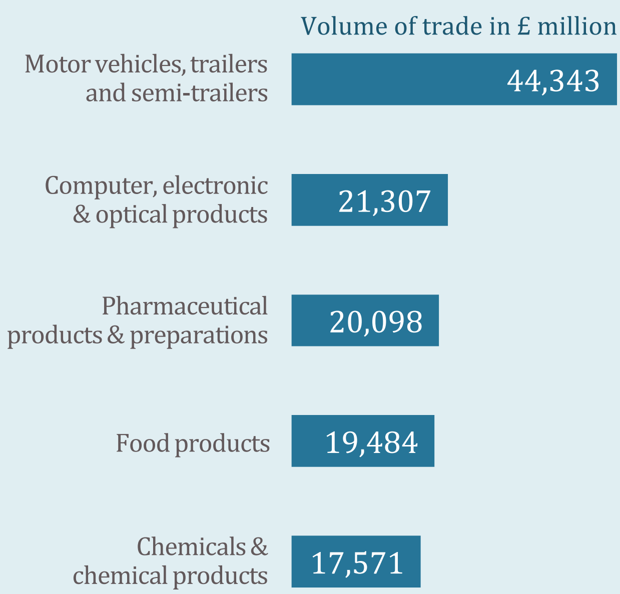


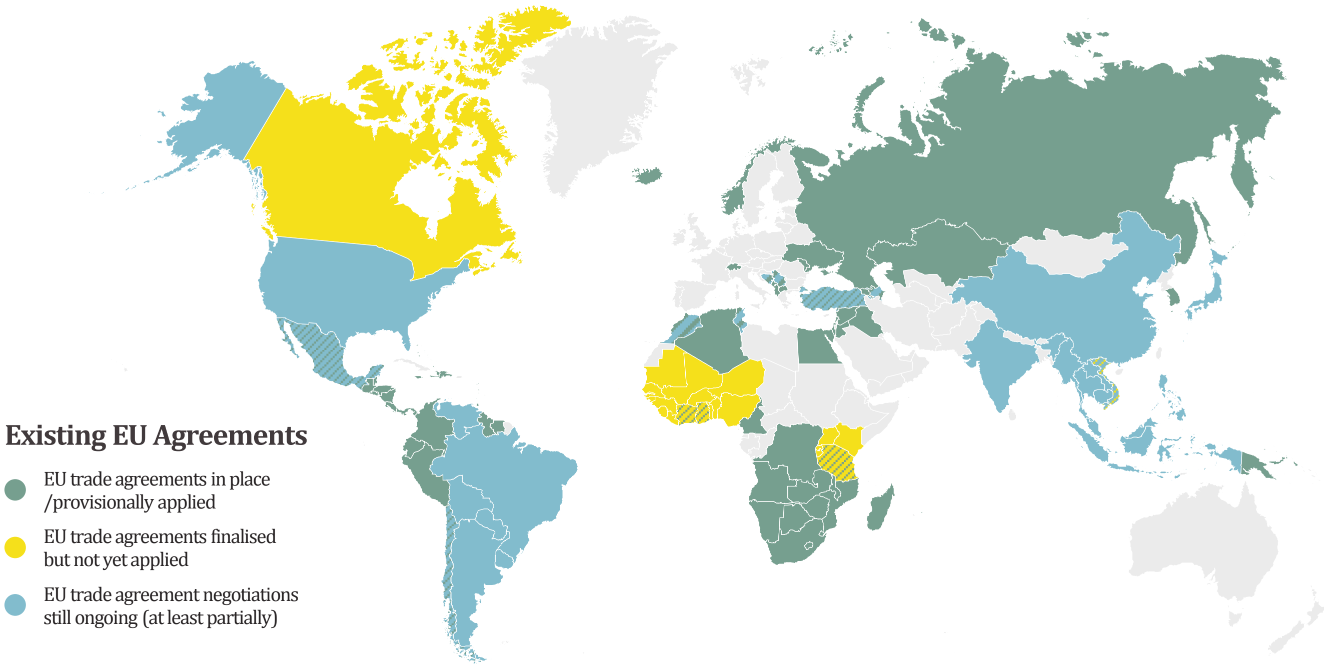
Bilateral Free Trade Agreements

As well as unfettered access to the Single Market, leaving the EU will mean that the UK will lose its access to preferential trade with the over 60 states with which the EU currently has FTAs.

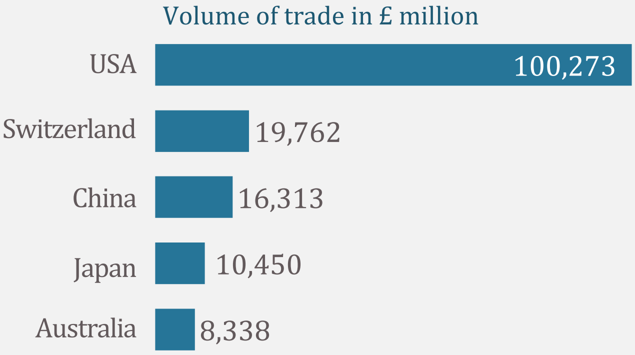
Although the UK could attempt to transpose its share in these agreements into national law, disentangling quotas and tariff rates, particularly on agricultural products, may prove substantially more complicated than negotiating new agreements from scratch. As the existing EU FTAs also reflect compromise outcomes between all 28 Member States, the UK should be able to seek better targeted outcomes for its businesses and consumers through new bilateral FTAs.

Whilst the UK is technically prohibited from negotiating separate bilateral FTAs as long as it remains an EU Member, Britain's Government has stated its desire to begin exploratory discussions with key bilateral partners to enable it to rapidly negotiate FTAs following its formal exit from the EU. Agreements have been proposed with the US, Canada, Australia, New Zealand, South Africa, India and China, among others.

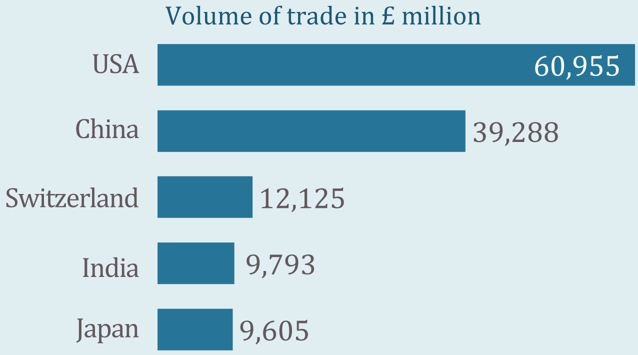
Despite strong political support, bilateral agreements cannot be finalised until third countries know the outcome of the UK/EU negotiations and the UK's final WTO schedules.



Top UK non-EU Export Goods and Services Partners (2015)



Top UK non-EU Imports Goods and Services Partners (2015)



Securing Your Trading Future
10 tips from trade negotiators

Brunswick has held a number of recent events with current and former trade negotiators. Here is their advice for business.

1. Businesses need to start thinking now about how to engage key governments on trade negotiations. Do not wait for negotiating stances to become clearer as it may be too late.
2. Companies cannot assume that negotiators understand their business or sectoral needs. They must spend the time and appropriate resources to do necessary analysis themselves.
3. Businesses should work with their sector to ensure that – where possible – they have a coordinated approach to the negotiations.
4. Business should ensure that the specific disruption caused by lack of trade is communicated and understood.
5. Companies and sectors need to map key stakeholders in the negotiations both within ministries and parliaments.
6. Business needs to engage at every level of each government involved in the negotiations in order to ensure the best possible outcomes.
7. Businesses and industry groups are more likely to see their priorities represented in trade negotiations if they formulate clear and practical proposals that negotiators can feed into the draft agreements.
8. Businesses need to understand the scope of the negotiations, in particular where other sectoral interests may impact their priorities.
9. Businesses should consider whether to influence the debate publicly via the media.
10. Companies need to be prepared for potential public opposition to trade agreements and make sure they have clear and effective responses.

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