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BREXIT AND BEYOND

THE LEGAL FRAMEWORK FOR UK-EU AND GLOBAL TRADE

DAVID COLLINS

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INTRODUCTION

Now that the negotiations are underway for Britain's departure from the EU in March 2019, the UK's priority is to move the focus to future trade. For both the EU and the UK a common aim will be to maintain and build on the volume of exports in both goods and services after Brexit, keeping existing arrangements as close as possible while recognizing the reality that the UK is now fully autonomous from the EU. For the UK such autonomy would over time lead to divergence of rules and laws as the country adapts for greater trade liberalisation. That would not impinge on the UK's aim to continue mutual free trade and have close ties of friendship with the EU after Brexit. This is rightly viewed as a top priority given the importance of trade to economic prosperity and our close economic ties. But as with the Canada-EU trade deal, CETA, each party is free under its own jurisdiction to make its own rules and disputes are resolved by international tribunals.

For the UK, which historically has been a global trading nation with strong continental links, there are equally strong reasons to maintain and expand EU trade as well as build on the UK's expanding global markets in Asia and elsewhere, which experts believe will comprise most of the world's economic growth in the coming decades. Britain has for centuries paid its way by producing and selling goods and services across the world, with and without trade treaties in place. Since 1973 when it joined the EEC and ceded control of trade to the EU, trade treaties with other states were negotiated by the EU binding the UK under the EU framework of trade law and treaties and the regulations binding the Single Market - including the 'four freedoms' for the movement of goods, capital, persons and to establish services. They are binding on all EU member states and also members of the EEA and under the jurisdiction of the European Court of Justice.

That model was rejected by the UK in June 2016 when a majority of voters decided to leave the EU and return powers to make the law to Westminster. In the general election one year later both main parties pledged to honour the referendum decision and the Conservatives were returned with 318 seats to Labour's 262. The smaller parties committed to remaining under EU arrangements (the Liberal Democrats and the SNP) lost support. The Conservatives, who formed a new government with the support of the DUP, are pledged under their election manifesto to the same approach as outlined by the prime minister in January 2017 and developed subsequently: to leave the EU and the Single Market and seek a bespoke trade agreement with the EU. Some who backed remaining in the EU have demanded that the government abandon its manifesto pledge and seek a so-called 'soft' Brexit, in which membership of either the EU customs' union or a somehow reformed Single Market, or both would in one way or another continue, or that membership of the EEA (the 'Norway' option), in which EU legislation on the Single Market, including the rules requiring free movement or governing competition and state aid rules would apply. The UK government has rightly rejected these plans. Keeping Britain's laws and border within the preserve of the EU, not the UK parliament, would be contrary to the referendum vote to leave.

This paper sets out a clear legal framework to achieve these goals for future trade with the EU and the rest of the world which will make for future mutual prosperity. The UK must both negotiate the basis for trade with the EU while preparing as much as possible for its future trade with other countries, so all is ready for trade agreements to come into operation as quickly as possible with other trading partners. For trade with the EU two options are outlined, a free trade deal with the EU or, without one, trade under WTO rules based on the Most Favoured Nation principle. For trade with the rest of the world, it is proposed that most of the WTO groundwork should be prepared before March 2019 to ensure a smooth transition for importers and exporters around the world and at home.

Preliminary negotiations for bilateral and regional trade agreements with other countries should begin as soon as possible with a view to concluding these trade agreements as soon as possible after departure from the EU.

The discussion concludes with a clear set of 'next steps' for the UK government and the EU. For trade treaties with the rest of the world, though these cannot come into force before departure from the EU, now is the time to prepare much of the ground work so these agreements can be brought into operation as rapidly as possible on departure. For the UK's future relationship with the EU, two options are considered: a proposed Free Trade Agreement (FTA) with the EU for goods and services- anticipated in a transitional agreement- or if that were not forthcoming, the alternative of trading under WTO rules on the basis of the MFN principle. The matters to resolve consist essentially of establishing the UK's tariff schedule for goods along with its services commitments based on its existing status as a member of the EU. Each of the options proposed offers a sensible and feasible way forward. The message is that the UK should approach the changes to the legal framework for its trading future with confidence and boldness.

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UK TRADE: THE AIMS

For both the UK and the EU one principal aim is to prepare the legal framework for future trade after March 2019 when the EU's membership in the EU terminates. The UK has made clear that after it leaves the EU and the Single Market in March 2019 it seeks a free trade agreement with the EU, allowing both countries the ability to replicate as closely as possible the tariff free access they enjoy currently to each other's markets for goods and services. This could be achieved faster than some of the EU's recent FTAs, e.g. the Canada EU free trade agreement (CETA) given that both parties would be starting from the same legal framework, which will be broadly preserved through the UK's Great Repeal Bill. For the UK a second priority is to prepare its position with respect to international trade with the rest of the world. In the unfortunate event that a free trade agreement with Europe is not immediately forthcoming following March 2019 or the conclusion of a transition period, the UK's international trade regime will also cover the EU. From the outset there are, therefore, two principal, if separate, aims – to prepare for future trade with the EU and to prepare for trade with the rest of the world. There are therefore two scenarios to be considered, each of which will be expanded upon below.

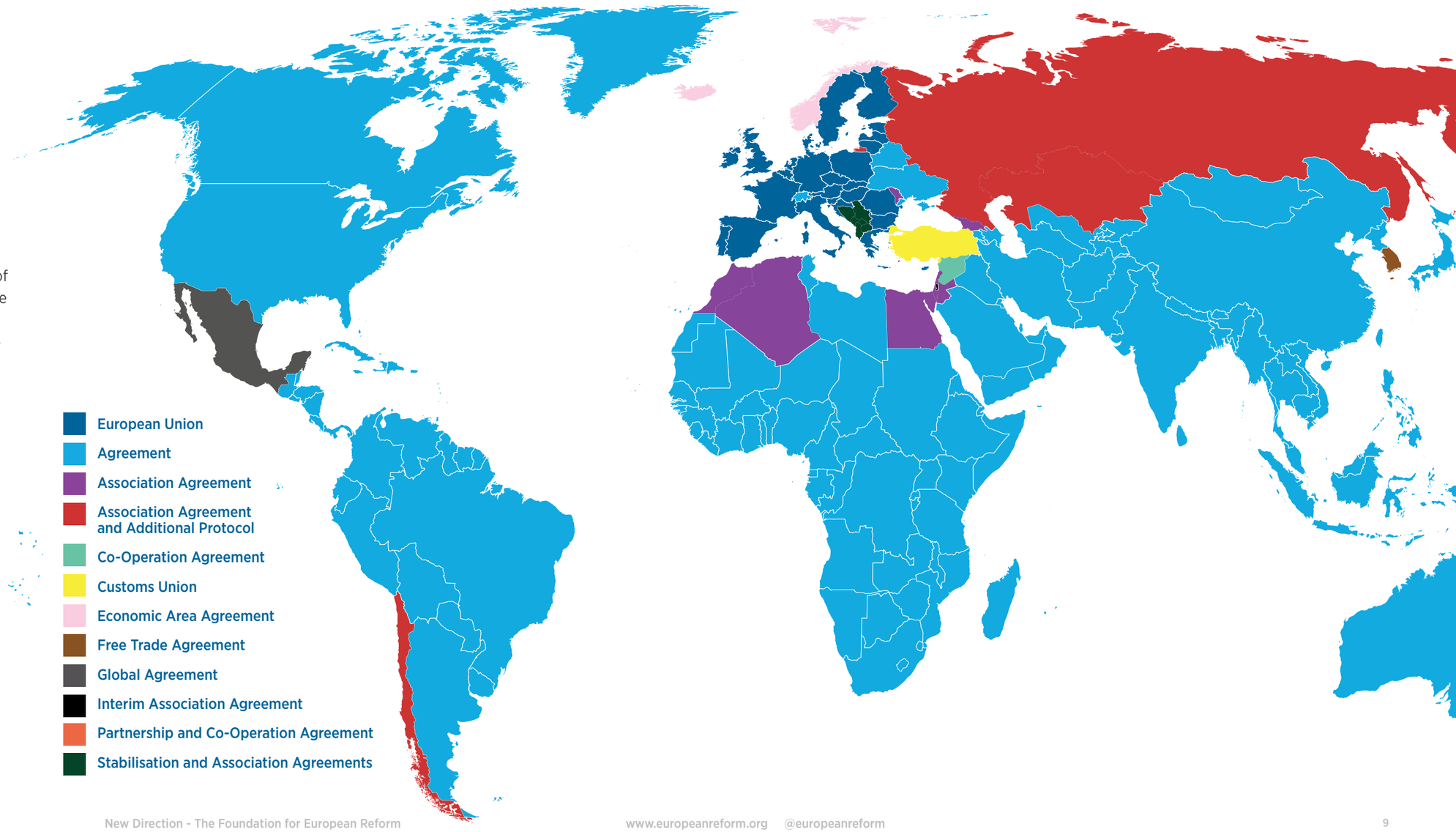
If, as the UK proposed, there is to be a transition period, a formal future trade agreement must also be agreed during the Article 50 period. It is envisaged that this would involve a situation closely resembling that of the EU's single market for goods and services, to the extent that the EU is prepared to grant this arrangement without free movement of persons and compulsory jurisdiction of the European Court of Justice (ECJ).

The UK has announced that it intends a transition period of no more than 2 years for which an interim agreement will be necessary. This is premised on the notion that prolonging existing arrangements would

CURRENT EU TRADE AGREEMENTS

Source: European Commission

Albania (Western Balkans): Stabilisation and Association Agreement / **Algeria**: Association Agreement / **Andorra**: Customs Union / **Armenia**: Partnership and Cooperation Agreement / **Azerbaijan**: Partnership and Cooperation Agreement / **Bosnia and Herzegovina** (Western Balkans): Stabilisation and Association Agreement / **Chile**: Association Agreement and Additional Protocol / **Egypt**: Association Agreement / **Faroe Islands**: Agreement / **Georgia**: Association Agreement / **Iceland**: Economic Area Agreement / **Israel**: Association Agreement / **Jordan**: Association Agreement / **Kazakhstan**: Partnership and Cooperation Agreement / **Kosovo** (UNSCR 1244): Stabilisation and Association Agreement / **Lebanon**: Association Agreement / **Macedonia**: Stabilisation and Association Agreement / **Mexico**: Global Agreement / **Moldova**: Association Agreement / **Montenegro** (Western Balkans): Stabilisation and Association Agreement / **Morocco**: Association Agreement / **Norway**: Economic Area Agreement / **Palestinian Authority**: Interim Association Agreement / **Russia**: Partnership and Cooperation Agreement / **San Marino**: Customs Union / **Serbia** (Western Balkans): Stabilisation and Association Agreement / **South Korea**: Free Trade Agreement / **Switzerland**: Agreement / **Syria**: Co-operation Agreement / **Tunisia**: Association Agreement / **Turkey**: Customs Union



operate to smooth the transition for UK businesses which need to adapt their processes to conform to the trade regime post-Brexit. For the UK, the presumption is that during the transition phase the UK and EU would have tariff free mutual trade, although this is by no means established as the EU may resist such arrangement. The transition period may operate as a virtual extension of the Article 50 period and as such it must have a definitive termination date in no more than two years (i.e. March 2021).

While it is always best to adopt an approach of flexibility when dealing with our EU allies, the interim agreement should not include the concessions to which voters have objected, such as free movement of people. This is not to say that migration from the EU will not be welcome. There should be an efficient process in place to ensure that EU workers are able to access the UK labour market provided that they fit with the UK's domestic needs. This may include access on favourable or vis a vis the rest of the world, in keeping with the arrangement under the EU, providing again requisite skills and UK market needs. On-line registration should help facilitate these processes. The rights of EU citizens currently residing in the UK must also be assured, although retaining jurisdiction of the European Court of Justice (ECJ) over these individuals within the UK would be legally complicated and untenable over time. Furthermore, although the UK should continue to cooperate closely with EU institutions to effect a smooth transfer, there would be no formal rule-making role played by these bodies.

This means that the jurisdiction of the ECJ would cease when the transition period begins. Judgments of the ECJ will continue to play a prominent role as a source of persuasive precedent under the UK common law, particularly in relation to EU laws which are retained in similar form. But judgments of the ECJ would lose their status as binding precedent.

Should the EU refuse to accept termination of the ECJ's law-making power in the UK as a condition of a transition period (or indeed of a full FTA) in order to ensure the quality of goods and services entering its territory, a suitable compromise is an international court, composed of both British and EU judges. This court would assess the validity of UK regulations for their conformity with EU law, and vice-versa. Such forms of dispute settlement are common to FTAs, including notably the investment chapter of the recent CETA between Canada and the EU. Appointing members of the CETA court is currently underway.

Under Article XXIV of the GATT, which facilitates regional integration agreements, there is a built-in presumption that both parties have agreed in principle to an FTA for the future in order for an interim agreement to be legally valid. Indeed it is arguable that an interim arrangement, such as the proposed transition period for Brexit would be unlawful under WTO law unless it expressly contemplates a full FTA upon its expiration. As such, the UK must not contemplate a transition period which will not end with an FTA.

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THE OPTIONS

A UK-EU FREE TRADE AGREEMENT (FTA)

This process, though likely to be more protracted than it had appeared initially in light of the fact that the Article 50 separation negotiations between the UK and the EU have not proceeded from the outset in tandem with a UK-EU FTA and given ongoing discussions over the quantum of UK's financial obligations to the EU. While the EU is entitled to demand payment of money owed to it by the UK if a sum is owed, about which there is doubt, framing this as a pre-condition to the negotiation of a trade agreement which is in the interests of both parties has not been productive. The so-called "divorce settlement" must accordingly be resolved as soon as feasibly possible.

It is suggested at this point that the UK and the EU should consider resolving the question over the UK's alleged financial obligations to a neutral arbitrator empowered to issue a binding determination if the UK conceded either that such a payment was due or that it wished to make an ex gratia payment. An international tribunal composed of neutral arbitrators with expertise in EU and international law would be best-placed to render this judgment in a timely fashion. The final amount (whether an ex gratia or an owed sum), which appears to be an amount of at least 20 billion euros, could be paid on a schedule which facilitated trade discussions. This would be in the best interest of British and EU citizens, allowing the UK to make its own internal budget allocations and to support the ongoing functionality of the EU government. By allocating authority to a neutral international tribunal, trade negotiations would be able to commence immediately and not be predicated on the quantum of final award, whether higher or lower than the UK government expects. International tribunals governing disputes between states are a well-recognized feature of international law and have precedent in both the International Court of Justice, the Dispute Settlement System of the WTO and regional trade agreements like the CETA.

With the issue of a UK payment resolved, an FTA with the EU is achievable within the next few years, although it will be difficult to do so before March 2019. In the event that it is not in place for the date of departure, an interim agreement, perhaps based on an extension of the transition agreement, or in fact identical to it, could smooth UK-EU trade relations in the lead up to a full FTA. Again, interim arrangements leading up to a regional integration agreement are permitted under Article XXIV of the GATT as an exception to the MFN principle.

UK-EU TRADE UNDER THE WTO FRAMEWORK

If the EU does not agree to a FTA with the UK, then the second option would be to trade with the EU under the framework of the WTO. While trade with the EU purely on the basis of WTO rules would represent a sub-optimal outcome which would undoubtedly raise tariffs on a number of goods and potentially engender difficulties for some services, a WTO-based relationship should not be viewed as a disastrous situation. The UK will be able to source many products from outside the EU cheaper than it does currently, and while it will be a disappointment to many that closer economic integration with the EU cannot be maintained, EU goods and services will of course remain available, at marginally higher prices – a price offset by cheaper goods from non-EU countries. It is up to consumers in the UK to decide if they are willing to pay these prices and presumably many will continue to do so given the high quality of many European exports. There is no reason that, even in the event of a failure to negotiate an FTA in 2019 is not feasible, that such an arrangement cannot be revisited at some point in the near future. In short, the UK's trade ties with the Europe are solid and can outlast the UK's EU membership.

THE UK, THE REST OF THE WORLD AND THE WTO FRAMEWORK

The UK has indicated that it intends to pursue bilateral and possibly regional FTAs with other countries, including notably those of the United States, China and India, as well as potentially regionally under initiatives like the Trade in Services Agreement (TiSA), the TPP11 and NAFTA. This is a sensible strategy and while FTAs are never easy, it is likely that the UK will enjoy reasonable success in concluding these arrangements given its strong economic position at some point in the future, even if not within the next year or two. Progress in this regard could be facilitated by the creation of working groups and participating as an observer in TPP11 and NAFTA negotiations. Furthermore, the UK will be able to respond more nimbly to negotiations with third countries without needing to make compromises in favour of 27 other EU member states. After leaving the EU, trade terms with the rest of the world will be under the framework of the WTO, irrespective of which route is agreed with the EU.

UK-EU WTO FRAMEWORK

Trade terms under the framework of the WTO is also one option for future trade with the EU if no EU-UK FTA is reached. Often unhelpfully described as a "no deal scenario", much of global trade is conducted under WTO rules. This includes trade which takes place between all those member countries which do not have FTAs with each other, like the US and the EU and Australia and the EU. While every country in the world operates at least one FTA, it should be noted that many countries do not actually avail themselves of preferential FTA-based market access because of difficulties associated with complying with rules of origin (demonstrating that goods actually originate from one of the party states). Such compliance can be onerous, particularly where the tariff difference between the FTA and the WTO is minimal. As such WTO rules are more important than many commentators recognize.

A UK-EU FTA

The WTO would continue to operate along with a future UK-EU FTA, however this FTA would presumably offer even better trade terms than exist under the WTO, including most likely lower tariffs and deeper market access for more services. Under the expectation that rules of origin would not be overly difficult, making compliance problematic, it would be this regime which would govern UK trade in goods and services with the EU going forward.

Under the WTO and in the absence of an FTA with the EU, goods arrangements will be based on the negotiated tariffs offered by each of the 164 WTO Members available to all states on the basis of the MFN principle contained in Article I of the GATT. For services, the terms of trade are contained in the negotiated schedules found in each member's schedule of concessions under the GATS, also extended on an MFN basis under Article II of that agreement. Tariffs on most goods are quite low, although some, such as automobiles and some agricultural products are high (between 5-15 per cent). The UK should unilaterally lower tariffs on a wide range of goods, which will represent significant gains to domestic consumers. The UK should conduct studies regarding the products upon which the UK should offer zero tariffs unilaterally, as there may be some sectors where this would harm domestic producers. The starting point here should be products which are not produced in the UK, such as tropical fruits and coffee.

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THE WTO POSITION

To avail itself of the WTO regime, the UK must prepare its WTO position as an autonomous member within the 2-year time period specified by the Article 50 procedure. It is encouraging that the UK government has indicated that this work is already underway. This involves essentially duplicating the EU's tariff rates on all products to ensure that no WTO member is made worse off by the UK's departure, establishing the UK's own schedule of concessions for services, derived in part from those committed as a member of the EU under the GATS, and establishing the UK's portion of tariff rate quotas. This last exercise has proven more difficult than anticipated given objections from the US and others, however this is a matter that can be resolved without too much difficulty over time, likely by the UK adopting a more generous portion of these quotas than the EU, a sacrifice which may itself play into the divorce payment negotiations. Finally, the UK must set up its own agencies for monitoring and imposing trade remedies such as anti-dumping and countervailing duties, which it is wisely doing through the creation of the Trade Remedies Authority. The UK has also sensibly indicated its intention to join the WTO Agreement on Government Procurement.

ESTABLISHING THE UK'S SHARE OF EU AGRICULTURAL SUBSIDIES COMMITMENTS

Agricultural subsidies are an enormous aspect of the EU's commercial and trade policy. The Common Agricultural Policy (CAP) which governs subsidies comprises something near 40 per cent of the EU's total budget. The failure to curtail agricultural subsidies extended by developed countries like the EU and the US (and in so doing suppressing the natural competitive advantage of the developing world) has historically been perhaps the WTO's single greatest failure. The reality is, however, that without the WTO, agricultural subsidies in the EU would be considerably larger and more distortive than they are today and for this the organization deserves much credit in eliminating much of this harmful feature of domestic economic policy.

The key issue for the UK after Brexit will be establishing its share of the EU's commitment not to subsidize its agricultural sector beyond the threshold set by the EU, which the EU has rightly cut back on the basis of its WTO commitments. The UK, as with all other EU Member states, is entitled to subsidize its agriculture sector up to a certain degree (known as the Total Aggregate Measure of Support), based on the EU's obligations as a member of the WTO. This is the so-called Amber Box of agricultural subsidies specified under Article 6 of the WTO Agreement on Agriculture. These are subsidies which are considered to distort production and trade so should be minimized. It is likely that this issue will not be significantly problematic, however, because as enormous as they still are, the EU's level of agricultural subsidies is only at about 7 per cent of the total value which it is allowed (about 6 billion euros out of 72 billion per year across all agricultural products) and the EU (like all developed countries) is committed to phasing out its export subsidies on agricultural products by 2020 under WTO rules. In other words, there is quite a bit of room for the UK to extend lawful agricultural subsidies of the Amber Box variety based on the EU's commitment even with only a small share of the EU's allocation, whatever that level might be. The UK must negotiate its share of Amber Box subsidies following Brexit, likely based on its allocation of the CAP budget. The EU implications here are minimal as this essentially represents an issue of UK domestic policy with regards to its own agricultural sector.

Still, the UK's share of the EU's right to subsidize could be problematic if it exceeded this entitlement, leaving itself open to a complaint from another WTO Member that the UK was unlawfully subsidizing its agricultural sector. The best way to deal with this issue is for the UK to establish a level of subsidization

EU MFN APPLIED TARIFFS, 2013

WTO EU Trade Policy Review 2013', Professor Alan Matthews, Department of Economics, Trinity College, Dublin

	Simple average (%)	Tariff range (%)
WTO agricultural products	14.9	0-197
Animal products	20.4	0-192.1
Dairy products	31.7	1.5-164.9
Fruit, vegetables and plants	13.3	0-197
Coffee, tea, cocoa and preparations	11.6	0-18.7
Cereals and preparations	18.1	0-94
Oilseeds, fats, oils and their products	7.5	0-154.1
Sugars and confectionary	25.4	0-135.3
Beverages, spirits and tobacco	14.2	0-196.3
Cotton	0	0
Other agricultural products, n.e.s.	5.6	0-83.5

that represents the portion of the EU's agricultural subsidies which are currently granted to the UK or have been in the last three years as a representative period. The information informing this decision is readily available. This amount would be the UK's share of the benefits it derives from the EU's CAP. Alternatively, the share could be assessed based on the UK's contributions to the CAP, which are tied to its share of the EU GDP.

It should be noted that the UK will still be free to subsidize its agricultural sector in other ways without WTO restriction (under the Agreement on Agriculture's Blue and Green Box subsidies respectively). The amount of money available to do so may change based on the UK's contributions to and drawings from the CAP as negotiated during the Article 50 process, but they do not engage WTO compliance issues. Following departure from the EU, a new regime for assisting UK farmers will probably need to be established, recognising that smaller and more vulnerable farmers will need to be helped. It might be a good opportunity to terminate other distortive and environmentally harmful subsidies on certain classes of farmers.

SERVICES: REPLICATING THE GATS SCHEDULE AND TOWARDS GREATER LIBERALIZATION

The EU's GATS services commitments under Article XVI and XVII were undertaken on an individual member basis: the EU's schedule of commitments specified different levels of services liberalization for each of the 28 Member States. The EU's GATS schedule sets out a framework for market access which is modified by each member's derogations in particular sub-sectors (horizontal) and modes of supply (vertical). Around 160 types of services are covered across the four modes of supply with varying derogations across the Member states, some of which are more onerous than others.

Again, as the UK exports about £220 billion and imports about £130 billion of services per year, maintaining an open trading arrangement in services with the rest of the world through the WTO will be crucial. The UK's under-performing services exports to non-EU countries like Canada and India are believed to be even larger than those relating to goods, representing massive potential gains post-Brexit. For example, the UK insurance industry has been poorly supported by the EU due to language barriers and legal differences. It is most likely that the UK initially will simply adopt its existing schedule of concessions within the EU's overall schedule as its own upon Brexit. This will involve extracting the various UK specific commitments from within the EU's certified schedule, which should be fairly straightforward, if time-consuming. The EU's own schedule of concessions, and those scheduled by the 27 Member states may remain intact as is.

Should the UK wish to make changes to its GATS services offer through a new services schedule after Brexit this will require a WTO certification procedure essentially involving notification. This should not be a problem so long as the UK does not decrease its overall level of services liberalization from its earlier status under the EU, which the UK is unlikely to do as it has a comparative advantage in most services and again, is expected to achieve significant export gains with many non-EU countries. Should the UK decrease its offer under GATS, however, then there could be an issue regarding breach of other WTO Members' legitimate expectations. Changes to GATS concessions, while permitted subject to notice, could result in arbitration through the WTO in order to ascertain appropriate compensation. The starting point for the UK post-Brexit would therefore be to replicate its GATS commitments as autonomous WTO member with a view to possibly modifying these going forward in line with objectives of greater market access liberalization.

With respect to the UK's supply of services to the EU (£59 billion worth of services are exported to the EU every year) GATS will represent significantly weaker market access than the UK currently enjoys as a member of the EU's Single Market. This is because very few WTO Members, including the EU-27 made significant GATS commitments to the rest of the world. Outside of the EU, UK services firms will need to examine the EU schedule of GATS commitments and each Member State's derivations from it to see what treatment they are entitled to. Such entitlements are extended automatically via the GATS MFN obligation. However, the GATS-only situation may not be as bad as is often thought because, since countries are free to apply more liberal services policies than they committed to under the GATS, many in fact do so. Actual services policy regimes among the EU-27 typically afford (much) better market access than what GATS schedules would prescribe. So market access and national treatment for the UK as a WTO member post-Brexit may appear to be somewhat worse compared to the status quo as an EU member yet in reality, it may not be as bad as a reading of GATS schedules might suggest. Of course applied regimes (which are extended on a Most Favoured Nation basis) lack the legal certainty of membership in the Single Market.

Finally, it should be noted that the EU's schedule of GATS services is not complete – schedules for the 16 newer EU Member States have not been incorporated into the EU's commitments, so the extent to which the UK will be able to supply services into the EU purely on WTO terms is not readily discernible. The EU will likely move to certify its schedules with the WTO in the future.

THE GOVERNMENT PROCUREMENT AGREEMENT (GPA)

The GPA is what is known as a plurilateral WTO agreement, which means that it is optional to existing (and future) WTO Members. It is important to recognize that the EU is a party to this agreement, not the UK, which means that the EU is responsible for fulfilling the obligations under the treaty, including those which are within the competence of its Member States. The UK has stated its intention to join as a signatory of the GPA upon its departure from the EU and this is the right decision. There is a practical problem that the UK does not currently have the institutional infrastructure to fulfil or enforce GPA obligations (for example relating to tendering procedures) and it will need to get this in order fairly quickly or else it will risk facing complaints by other WTO members for failure to uphold its GPA obligations.

TRADE LEADERSHIP

As a nation with a long history of free trade and one of the world's largest economies, the UK should take an active role in WTO affairs going forward as a leading voice for multilateral negotiations on trade liberalization. One of the ways it can do this is by nominating individuals to the indicative list of panellists at the WTO dispute settlement system. It has not done this for some time and there is no reason why there should not be more UK panellists on the list, as many other WTO members continue to nominate individuals on a regular basis. Another way that the UK can demonstrate trade leadership is by becoming involved in the proposals for the

Services Facilitation Agreement, initially submitted by India, as well as work underway at the WTO on digital trade. The UK and the EU will be allies in maintaining a strong multilateral trade system and will work together with respect to reforms to the system, such as those regarding dispute settlement.

THE UK: WHAT STEPS FOR ADOPTING ITS OWN WTO COMMITMENTS?

Since the UK is already a WTO member in its own right, the process of the UK adopting its own WTO commitments for the future can happen in two ways: "rectification" or "modification". The former is relatively simple, only requiring that no WTO Member state raises any objections to be approved,

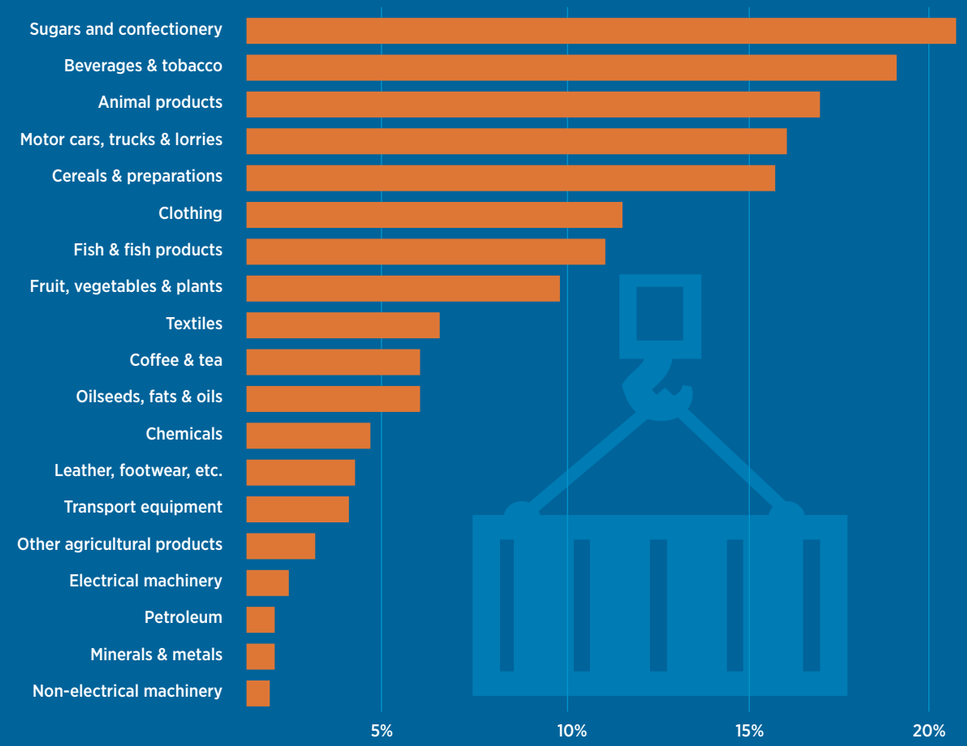
which is unlikely given the interests that most countries would have in continuing to trade with the UK under legal certainty. A full modification process on the other hand, would require rounds of negotiations over the scheduled tariffs, tariff rate quotas and services schedules and could take many years. Rectification is possible for rearrangements which do not alter the scope of a concession and other changes of a purely formal character. Modification of schedules implies the substantive change of a concession. The border between the two is determined by establishing whether the changes made will put another WTO member in a position worse off under the new rules than it was before Brexit. If the UK amended its schedules by means of a rectification of the EU's schedules, the process could be completed in a few months. So long as the UK maintains the same tariff schedule as that of the EU, there would not be any great difficulty in classifying UK's new schedule as a rectification of the schedule. If the UK changes its schedule substantively, for example by offering a lower level of liberalization than it did through the EU, then this could be viewed as a modification which would require a new tariff schedule, requiring the consensus of 163 members including the 27 countries that are also EU members. This scenario is both inadvisable and unlikely. As suggested above, the UK should lower its tariffs on goods, in some cases to zero. The UK should begin investigating now which products should receive zero tariffs, starting with those for which there is no domestic production.

APPLYING FOR A WAIVER

It should be recognized that the UK may avail itself of a WTO waiver if it is concerned that it will transgress its WTO obligations during or immediately after the Brexit negotiations. WTO members anticipating a breach of WTO obligations may request waivers by application citing the reasons which prevent the WTO member from achieving policy objectives. Under Article IX of the WTO Agreement, the waivers last for two years unless extended, which they can be, without limit. The function of a waiver is to relieve a WTO Member, for a specified period of time, from a particular obligation and are exceptional in nature, subject to strict disciplines. Waivers may be used to add flexibility to international law and in so doing deal with the tension between practical domestic needs and international requirements. This acts to relieve potential conflict by suspending the law before the tensions escalate to the point where nations may be forced to use the dispute settlement system formally. Clearly Brexit is an exceptional situation and there is little doubt that it would justify a waiver. This could be used to cover any time gap between the UK leaving the EU and formalizing its schedules, allowing it to continue trading under current arrangements. It could also be used to neutralize the effect of any political blockage arising from one of more WTO members implementing reservations to any proposed schedule in the unlikely event this were to happen, allowing time for mediation and ultimate resolution. WTO members could conceivably allow both the UK and the EU transitional periods or temporary waivers to allow the negotiations to continue after the day of formal Brexit. The application for a waiver would be done by official notice to either or both of the WTO Council for Trade in Goods or Council for Trade in Services, depending on the nature of the waiver sought by the UK. A recommendation is made by this body to the Ministerial Conference which requires support from three fourths of the WTO Membership.

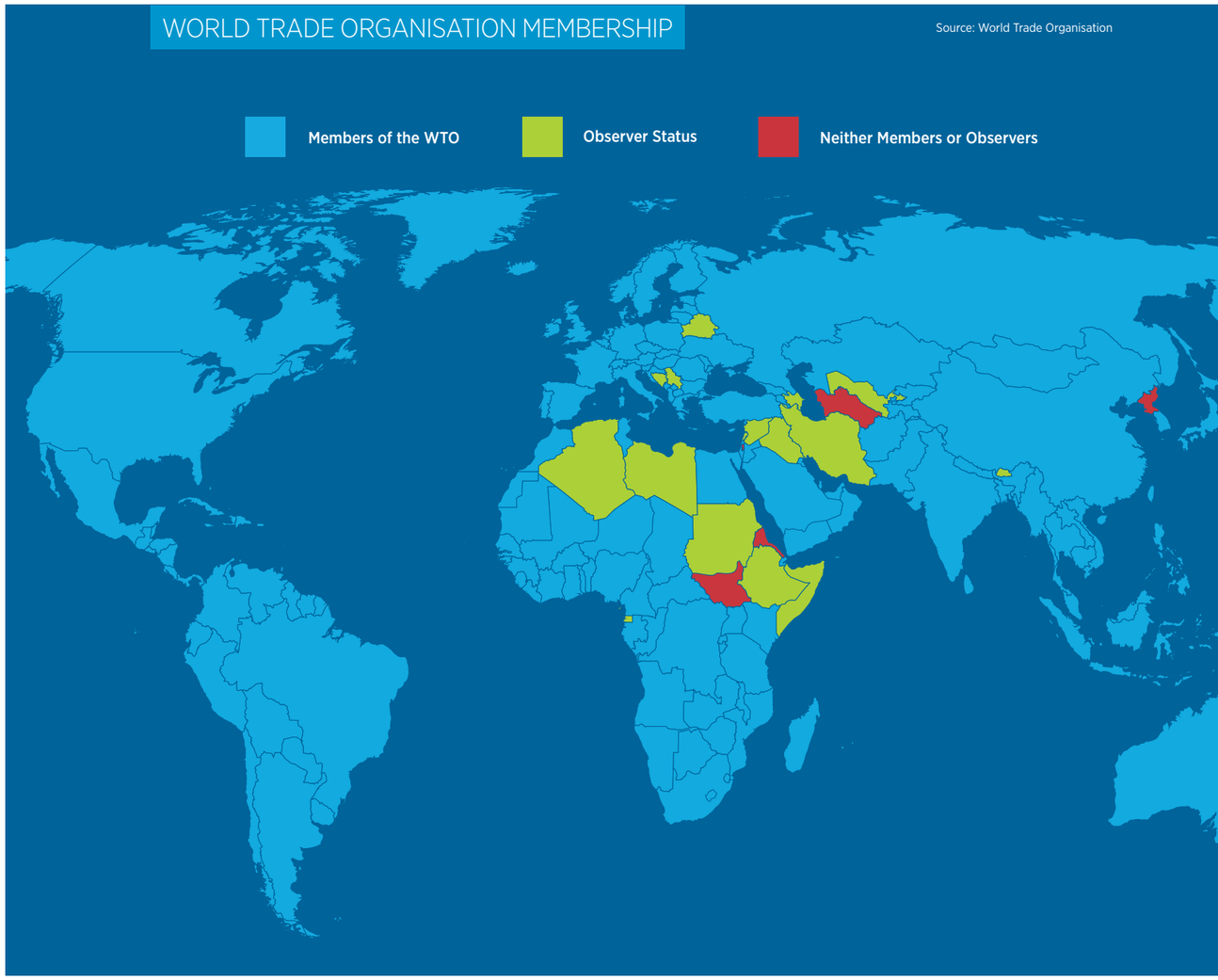
AVERAGE FINAL BOUND TARIFF RATED APPLIED BY THE EU BY BROAD CATEGORY OF GOODS

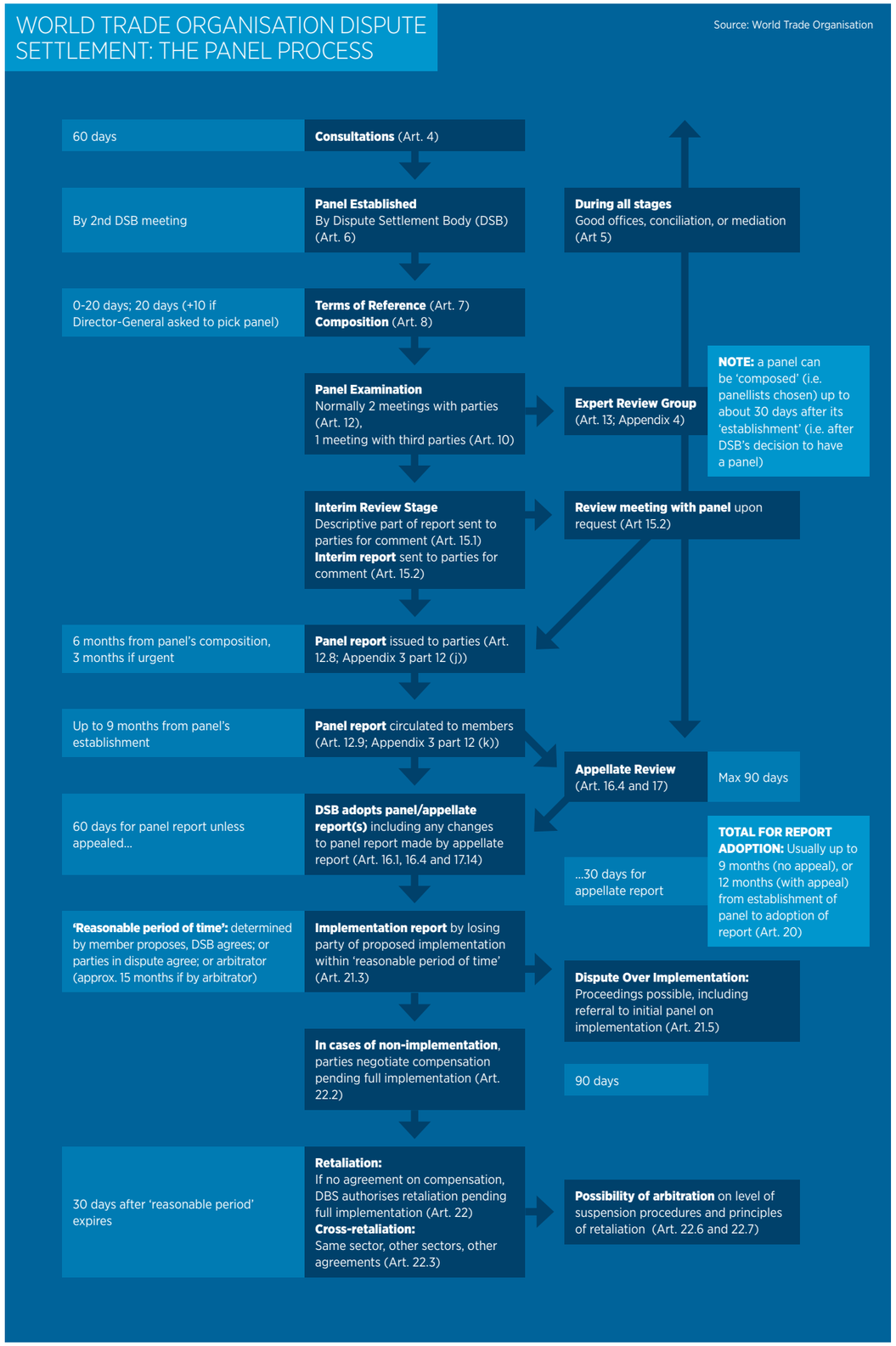
House of Lords European Union Committee, 'Brexit: the options for trade', 5th Report of Session 2016-17, 13 December 2016, HL Paper 72
Source: WTO



WORLD TRADE ORGANISATION MEMBERSHIP

Source: World Trade Organisation





5

UK-EU FREE TRADE AGREEMENT (FTA)

This section will set out the main features which should be sought in the UK-EU FTA.

TIMING

One of the potentially problematic issues which appears to have arisen is timing. The Article 50 negotiations have not proceeded in tandem with discussions for a UK-EU FTA, the EU preferring to negotiate the 'divorce settlement' payment in the opening stages. While time is running out, there is no reason why this must be the case and the UK should still seek to negotiate the FTA as part of the Brexit process if possible. Conceding authority to ascertain the extent of the "divorce" payment to an international tribunal could expedite this process, *whether owed or ex gratia.* There is ample precedent in international law for such dispute resolution. It need not be viewed as an escalation of hostilities but rather a pragmatic way of resolving a politically volatile impasse.

If this approach fails, there could be at least some period of time when the UK will be neither a member of the EU or party to an FTA with the EU. A transition period, which appears increasingly likely, could provide more time for the UK and the EU to reach a trade arrangement which could allow for continued free trade, but with independent international tribunals composed of arbitrators chosen by each side in place of ECJ jurisdiction. This scenario could leave the UK (and the EU for that matter) open to the accusation from another WTO Member that the UK and the EU are, through the "transitional arrangement" breaching the MFN principle under Art I of GATT by treating each other better than they treat everyone else without their being an Article XXIV-compliant FTA in place. However, Article XXIV(5) c) states that any such "interim agreement" should provide for the formation of an FTA "within a reasonable length of time", meaning that it does not have to be in place immediately. So a transitional arrangement with the EU, provided that it leads to an FTA reasonably quickly (perhaps within 2 years) should be able to foreclose any MFN-based complaints from other WTO members.

The main question for the UK and many individual EU states exporting to Britain is whether and how soon the EU can negotiate tariff free trade/a free trade agreement with the UK post-Brexit, as proposed by the UK prime minister. A UK-EU FTA will involve agreement on a number of matters such as goods and product standards, services and foreign investment. This section will consider such issues which will most likely arise during the negotiation of a UK-EU FTA. It explains what would be involved in the UK's taking over certain responsibilities from the EU and the preparations that need now be undertaken under WTO rules and framework to transfer responsibilities from the EU to the UK. These include tariffs, non-tariff or technical barriers to trade or sanitary and phytosanitary measures and customs. The options for a FTA in services and for foreign investment are also considered.

GOODS AND PRODUCT STANDARDS

First, under such an agreement the UK will seek to replicate as closely as possible the zero-tariff environment which existed through its membership in the EU. This will be of interest to both parties and should not be problematic. Article XXIV of the WTO's General Agreement on Tariffs and Trade (GATT) facilitates FTAs in which FTA parties grant preferential tariffs to those within it relative to other WTO members, which would otherwise violate

the GATT's Article I Most Favoured Nation (MFN) obligation, obliging members to treat goods from all other countries the same as each other. The only requirements for an FTA are that there must be a notification to the WTO and, somewhat more problematically, that the FTA must cover "substantially all trade." The precise meaning of this phrase is uncertain, but we know that sector-specific FTAs would not be permitted. In other words, there could be no UK-EU Free Trade Agreement on Automobiles, for example. While some products could be excluded, the expectation is that the arrangement will cover almost everything.

TECHNICAL BARRIERS TO TRADE (TBTS)

One of the most difficult aspects of the goods component of the UK-EU FTA will undoubtedly relate to non-tariff product standards, otherwise known as Technical Barriers to Trade (TBTs) or Sanitary and Phytosanitary (SPS) measures in the case of foods. These have the potential to be quite controversial, given that one of the motivations for Brexit appears to have been the distaste within the UK for EU regulations which are perceived by some as unnecessary. The EU has resisted importation of a range of goods which do not fit with European sensibilities in relation to health (e.g. hormone treated beef and genetically modified organisms or biotech products) originating from countries like the US. It remains to be seen what stance the UK government will take on these matters, but presumably should the UK insist on its capacity to import these products from other countries, the EU would be free to restrict these from entering its territory. As the UK has retained regulatory convergence with the EU through the Great Repeal Bill, there should be limited difficulty in this issue, at least until the point at which the UK chooses to change its product standards. It should be noted that many of these are based on international standards and unlikely that the UK will deviate from these.

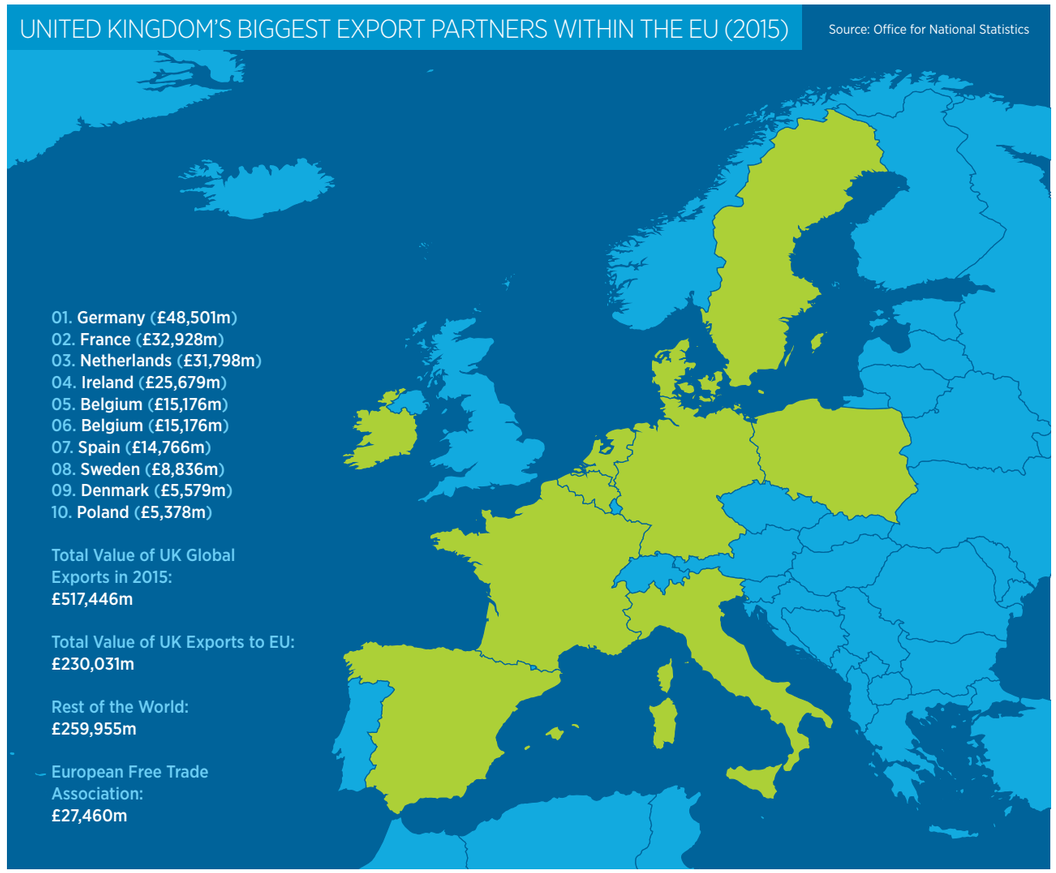
The UK-EU FTA could resemble that of the CETA where there was agreement to recognize each other's product standards, conforming to the WTO SPS and TBT Agreements. Under CETA the EU remains free to impose its own regulatory controls on products like hormone-treated beef and genetically modified organisms, both of which are produced in Canada. This did not require acceptance of the jurisdiction of the ECJ over product standards by Canada. Dispute settlement under the CETA will be conducted by international tribunals composed of arbitrators chosen by the state parties.

CUSTOMS ARRANGEMENTS

Another pressing concern following the UK's departure from the EU will be customs arrangements regarding goods. Outside of the customs union, all goods traded between the two countries will be subject to customs inspections and verification for rules of origin which is a key component of granting low-tariff access through an FTA. These procedures can be time-consuming and costly (adding several days and up to 10 per cent to costs according to some studies). These issues are even more problematic for products which are part of production chains with components from several countries, like automobiles. The UK government has spoken of the desire for "frictionless trade" in goods. This could involve some kind of simplified customs procedures, possibly using a virtual border involving periodic customs self-assessments by exporters coupled with the use of information technology like bar code scanning. A border which does not involve physical checks, or where physical checks are removed from the border at designated "control points" could help address some of the tensions associated with the Northern Ireland border. Resources must be committed to ensure that customs procedures do not overwhelm commerce and it is encouraging to see that the UK government has recognized the importance of this issue. Furthermore, the EU would certainly require reassurance that the UK does not position itself as a "backdoor to the EU" by allowing goods into its territory from a third state which could then be shipped into the EU as if they were UK goods.

It should be noted that under Article VII of the GATT, WTO member states must ensure that their customs procedures are no more onerous than necessary. Furthermore, the Trade Facilitation Agreement, which the EU has ratified, obliges member states to provide smooth border procedures for goods. As such, the EU can be expected to do its utmost to ensure that there are no unnecessary impediments to trade in goods through our ports and other border crossings.

As noted earlier, the regulatory environment on goods will remain the same after the UK leaves the EU because the UK is not changing its own



conformity assessment / testing procedures – this is precisely the purpose of the Great Repeal Bill. They will remain identical to the way they currently are within the EU, at least for the time being. The only 'change' is that the UK will not be an EU member – this is not a change in the level of scientific risk on food or any other products, which might justify additional procedures at the border. Any additional regulatory barriers would consequently be arbitrary and unjustified. The UK would promptly complain through the WTO dispute settlement procedure and the EU would almost certainly lose. Customs procedures could be somewhat more difficult because of the need to verify compliance with rules of origin, meaning identifying that the products do in fact originate from the UK. It is expected that these issues can be tackled through enhanced technologies at our borders, provided that the resources are made available and preparations should begin right away. Not only have such arrangements have already worked in practice, but the legal framework exists to accommodate them.

SERVICES

Ensuring market access for services is perhaps a more pressing concern for future UK-EU relations given the growth of this sector of the economy as well as the difficulty in controlling non-tariff barriers to trade, such as licensing and professional qualification verification for service suppliers.

The lucrative financial services market comprising industries like banking, legal, insurance, and accounting is particularly important. Market access for financial services in the EU will be a crucial feature of the UK-EU FTA because of its importance to the UK economy (over 10 per cent of the UK's GDP, £176 billion per year in value and over 7 per cent of employment). The UK's objective here will be to preserve the conditions which sustain the UK's dominance in services. The Brexit White Paper indicated the UK's intention of securing a comprehensive multi-sector FTA with the EU that provides the greatest possible

access to each other's markets, including services. Since the UK is not going to seek membership of the Single Market, this effectively precludes access via existing EU "passporting" or European Economic Area (EEA) models. The UK should be able to maintain its trade in financial services with the EU-27 based on a mutual recognition arrangement, as specified under Article VII of the GATS.

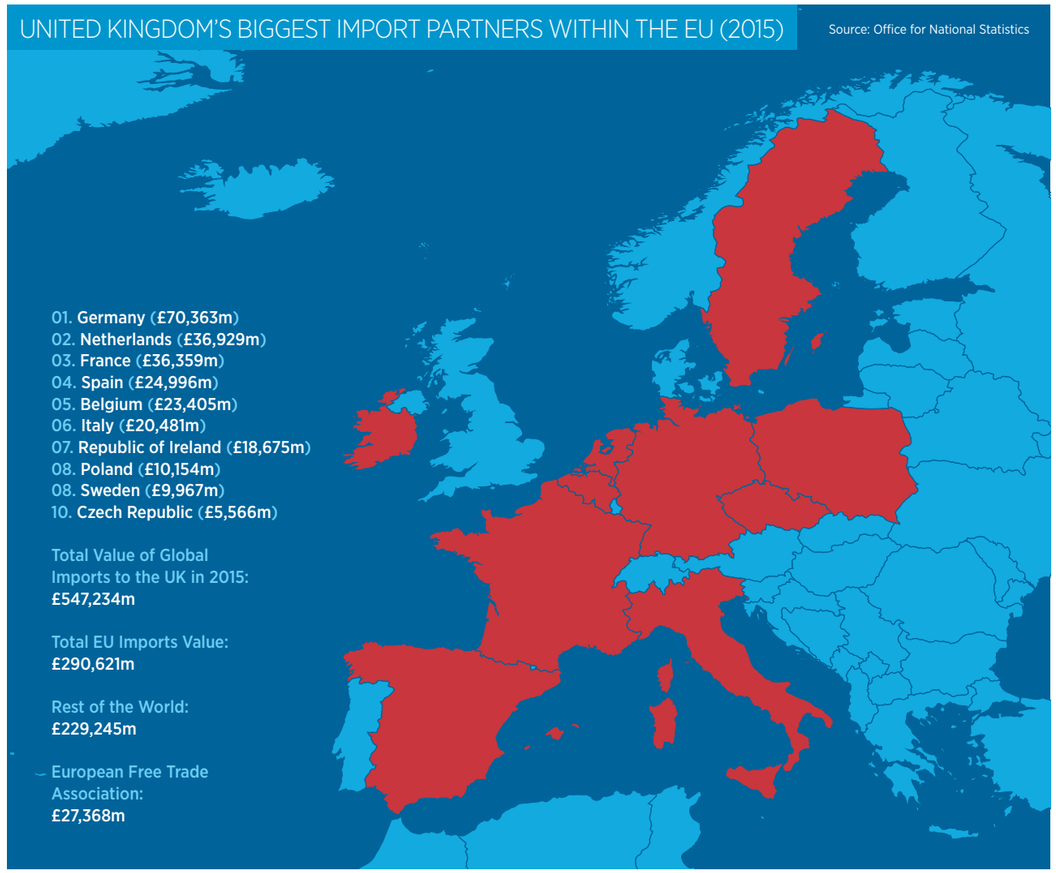
This would be a bespoke arrangement for reciprocal access for financial services, meaning that EU financial services firms would enjoy the same rights in the UK as those from the UK would in the EU. This could be achieved by the UK enacting all financial services regulations through the Great Repeal Bill which correspond to those of the EU, essentially duplicating the existing regulatory regime that was in place as a member of the EU. Falling short of full duplication of all EU financial services rules there could be a customized arrangement based on the understanding that the two regulatory and supervisory regimes were broadly consistent with each other in that they have common regulatory objectives and aim to deliver comparable outcomes. This is somewhat less than strict "equivalence." Focusing on outcomes should allow some flexibility in the position of both parties, particularly since financial sector regulatory regimes tend to evolve over time. The EU has offered similar arrangements to other countries and would be precluded under the MFN obligation of the GATS from denying them to the UK where standards or outcomes were broadly similar.

In either case, the UK and the EU would also need to agree on a consultation mechanism should a change in the regulatory regime in one jurisdiction render this consistency in doubt. Since the UK has been a long-standing member of the EU and that there is a history of cooperation between the EU and its member states such an arrangement is quite feasible. The UK will wish to exclude the jurisdiction of the ECJ over financial services matters which will require some form of neutral arbitration mechanism, possibly modelled on the CETA's Investment Court System could be achieved. The EU is willing to allow international courts to resolve disputes regarding foreign investment and there is no clear reason why something like this could not also be extended to financial services.

Mutual recognition for the regulation of financial services of the kind described above could be achieved under an FTA and concluded under Article 207 (governing the common commercial policy of the EU) and Art 218 (governing Free Trade Agreements) of the Treaty on the Functioning of the European Union (TFEU). It would also need to comply with Article V of the General Agreement on Trade in Services (GATS, the WTO agreement covering trade in services, of which more below). In this regard, it is important to note that GATS Art V, like GATT Article XXIV, requires "substantial sectoral coverage" which means that FTAs cannot be concluded on a sectoral basis – there can be no "Financial Services FTA." All or near all services must be covered. So, in the event that the negotiations of the UK-EU do not progress rapidly on all areas, it would be feasible to create a Mutual Recognition Agreement for financial services on its own, apart from a full FTA. Unlike comprehensive FTAs in services (granting market access and non-discrimination), such arrangements may be sector-specific. These agreements must satisfy Art VII of the GATS, which allows WTO Members to recognize qualifications and standards of services suppliers originating from certain other members. There are no WTO rules on how such agreements must be structured, except that the parties must have included market access coverage for the relevant sectors in their GATS commitments. Both the UK and the EU have made extensive financial services commitments under GATS, having undertaken the Understanding on Commitments in Financial Services.

FOREIGN INVESTMENT

While foreign investment is distinct from trade it is important to address some key issues here as an FTA with the EU is likely to include an investment chapter. Freedom of establishment was one of the pillars of the Single Market and the UK will seek to create a future arrangement where its firms enjoy comparable conditions, just as it will wish to remain attractive to EU firms seeking a commercial presence in the UK. Some studies have suggested that foreign direct investment from Europe is at risk of shrinking post-Brexit and having an FTA with standard investor protections in place could help prevent this outcome. The agreement should accordingly contain guarantees against discrimination and unfair treatment as well as compensation in the event of expropriation which are standard in these instruments.



Traditional investment treaties (which the UK was able to conclude before the Lisbon Treaty) contain Investor-State Dispute Settlement (ISDS) mechanisms, which permit private investors to bring claims directly against host states in international arbitration, with party appointed arbitrators – a system which has worked well for the UK over several decades. This process has become controversial in recent years. This sentiment was captured by the negative response elicited from the EU Commissions' public consultation on ISDS in the run up to the TTIP negotiations with the US. As a consequence the EU devised an Investment Court System (ICS) which consists of state appointed arbitrators (rather than party appointed ones, as under traditional ISDS) coupled with an appeal court of standing judges. The procedure will have enhanced transparency and the judges will be experts in international law, rather than in commercial matters as typically the case in normal ISDS. The CETA between the EU and Canada contains this procedure and it would seem as though the EU intends to include the ICS in its future IIAs. Recent negotiations for the Trans Pacific Partnership without the US, the so-called TPP11 or Comprehensive and Progressive Pacific Trade Agreement, will apparently contain some capacity for signatories to opt-out of ISDS in certain circumstances or for certain sectors. It is important that the UK government monitors these developments closely and assess whether there are any sensitive sectors which it feels should not be within the jurisdiction of an international investment tribunal in its future investment treaties.

While the UK may not have much leeway to negotiate an investment chapter in its FTA with the EU without the ICS, to the extent that this is possible, until we have a better idea how the ICS will work in practice it would be preferable for the UK to avoid this mechanism in favour of conventional ISDS. The UK has a good track record in ISDS, having faced only one claim as a respondent in more than 40 years of investment treaty practice. British firms have won 13 of 27 cases they have brought against foreign governments, which is a respectable success rate

given that states normally win such cases. The ICS procedure will be expensive, most likely doubling the cost to participants, and it is not clear that it will add much in terms of consistency and predictability given that investment cases tend to be heavily fact-based and focused on achieving pragmatic solutions rather than the creation of a "system" of precedent in the manner of public international law. The judges to be appointed to the ICS court will require expertise in public international law but not necessarily knowledge of the relevant industries in which the disputes are focused. It should be noted that a recent ruling of the ECJ has indicated that dispute settlement regimes for investors in FTAs are within the competence of EU Member states, which suggests that future FTAs may omit this feature entirely with a view to facilitating the ratification process (in light of the resistance presented by Wallonia to the CETA). This would mean that UK investors operating in the EU would be subjected to the jurisdiction of the ECJ, just as EU investors operating with the UK would be subjected to the UK courts.

INTELLECTUAL PROPERTY, DIGITAL TRADE, PROCUREMENT AND COMPETITION

A comprehensive FTA between the UK and the EU should also involve other matters such as intellectual property, digital trade, procurement and competition. Given that UK laws in these spheres generally correspond to those of the EU already by virtue of the UK's long-standing membership in the EU, it is expected that there will be limited legal difficulties in these areas, however there may be short-term pragmatic problems concerning the UK's lack of institutional infrastructure to enforce some of these regulations. The EU's priority will rightly be to maintain healthy competition across a range of services industries along with consumer protection and to safeguard national security and maintain financial stability. These objectives are fundamentally in line with those of the UK. Both countries are committed to rule of law, transparency and properly functioning markets.

MOVEMENT OF PERSONS

Free movement of persons will almost certainly not form part of the FTA negotiations as the UK government has indicated that free movement will cease following Brexit and it is unlikely that this is negotiable. However, the UK government has wisely indicated that it intends to ensure that the UK will remain open to EU workers in spheres where there is need. Presumably this will require some migrant registration and assessment process, possibly including a points-style system which is common to many countries. Given national security concerns and the pressure on social services such as the NHS, such procedures are entirely sensible and it is difficult to see how the EU would object to them. Moreover, provided minimal qualifications are satisfied, there is no reason why EU workers should not be granted preferential access to employment opportunities in the UK as part of a FTA. This could include simplified procedures for obtaining work visas along the lines of the the North American Free Trade Agreement (NAFTA) professional visa which lasts for three years, is inexpensive and may be obtained quickly if an offer of employment has been made.

DISPUTE SETTLEMENT

In order to resolve the tension regarding the jurisdiction of the ECJ going forward and the need for the UK to retain a degree of regulatory convergence with the EU in order to facilitate as open trade as possible under an FTA, there will be a need for a neutral dispute settlement body for trade issues arising between the UK and the EU. This tribunal should be composed of individuals with suitable legal qualifications chosen from both the UK and the EU. In the case of the EU it is likely that such individuals will be chosen from across the 27 Member states. Rather than operating as a standing court, this body should be composed of ad hoc panels selected from an established roster, in the manner of the WTO panels. This structure is in keeping with similar dispute settlement panels which exist under other FTAs, such as NAFTA.

6

UK GLOBAL TRADE

The UK should seek FTAs with third countries as soon as possible with a view to these going to into effect following the departure from the UK or the conclusion of a transition period. The UK's top priorities in this regard should be treaties which offer the most in terms of economic gains and which may realistically take the most time. The most important trading partners are the US, China and India. Easier trade deals with the Commonwealth must also be pursued, however the gains from these treaties (such as with Australia and New Zealand) will be minimal because the volume of trade with these countries is small.Participation in regional arrangements, such as the TPP11 and NAFTA is also an excellent strategy.

TARIFF REMOVAL

The UK's trade agreements with other countries should prioritize the removal of tariffs on a wide range of goods, including some which have been protected in the past at the behest of other EU member states and for which there is no UK domestic market needing protection. These represent potential efficiency gains which may compensate for some of the losses engendered by declines in trade with the EU. As a consequence of the success of the WTO/GATT regime, tariffs on most manufactured goods around the world are quite low, but some agricultural goods bear very high tariffs as do some manufactured goods such as automobiles. Under Article XXIV of the GATT and Article V of GATS, FTAs may offer lower tariffs than those extended to other WTO members outside the FTA. But, as noted earlier, such FTAs must cover "substantially all trade" meaning that there cannot be sector-specific arrangements. FTAs may cover goods or service, although the convention is to have FTAs covering both. Should the UK choose unilaterally to remove tariffs on a range of products upon departure from the EU (which it must offer to all WTO Members through the MFN principle) then there will be less leeway to use tariffs as a "bargaining chip" in bilateral trade negotiations. Consequently services, investment, competition and e-commerce will become the key negotiating features of these treaties.

PRODUCT STANDARDS

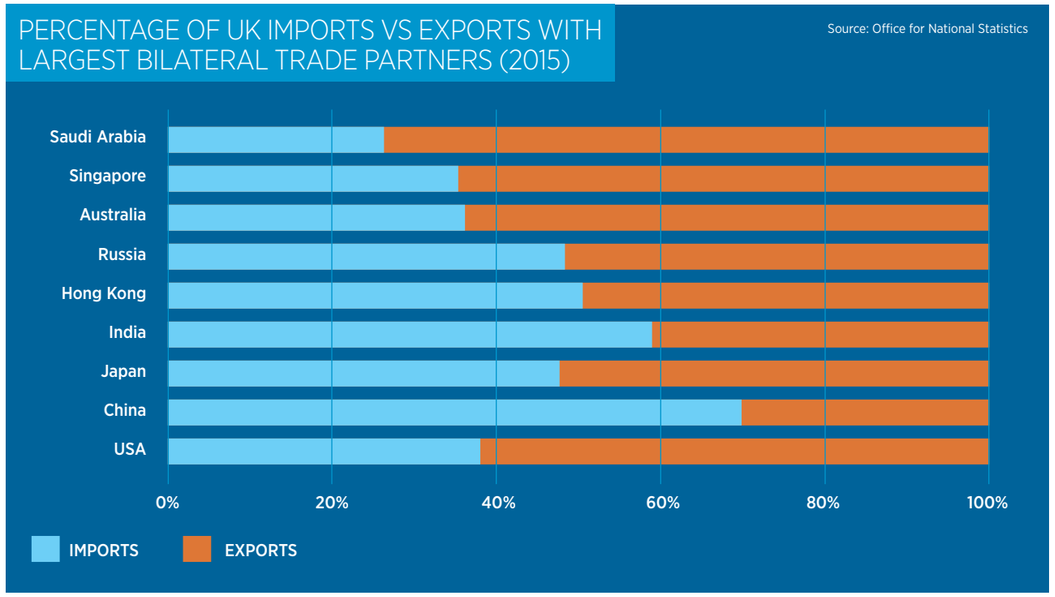
The issue of product standards regarding health and safety will be more complex and raise some difficulties from a negotiating standpoint. As noted above, it is not clear what stance the UK will take regarding certain controversial products like hormone treated beef or genetically modified organisms. Ministers have said they will be guided by UK food

safety and standards guidance and will ensure consumer safety. This could present an obstacle to an FTA with a country like the US were the UK to insist on retaining EU-type restrictions on these products. As the WTO dispute settlement panel ruled against the EU's restrictions on both these classes of products the UK could follow global scientific consensus and allow these products by recognizing US product assessment procedures, to the extent that they also conform to WTO SPS and TBT requirements. The UK would be advised to take a liberal stance on imports from the US and other countries with a view to securing trade deals. Insistence on strict labelling would shift the choice regarding these products away from the government to consumers.

SERVICES

It is unquestionable that the UK's FTAs with the rest of the world will include services given that the UK exports £220 billion in services per year to the EU and the rest of the world and represents its key comparative advantage. Priority in this regard will be liberalizing financial services as well as securing mutual recognition agreements for professional qualifications to allow movement of services professionals on a temporary basis. Recall that Article V of the GATS which facilitates FTAs, requires that such arrangements cannot be sector-based. GATS Art V requires "substantial sectoral coverage" which means that all or near all services must be covered in an FTA. Although there could be a services only FTA this would be unlikely given modern international treaty practice. This means that the UK cannot conclude a Financial Services Agreement with Canada, for example, although it can conclude bilateral investment treaties (BITs) of which more will be discussed below. It should be pointed out here that Switzerland is often cited as a country which has concluded sector-specific agreements with the EU and that this is something which the UK could do either with the EU or other countries. However, the Swiss agreements, which are indeed sectoral (there is a Switzerland-EU Insurance Agreement) are not actually trade agreements. They are investment agreements which cover commercial presence establishment rights (only one of the three modes of services delivery) and mutual recognition agreements for qualifications under GATS Article VII. This means that they are not "caught" by GATS Article V. The UK must pursue mutual recognition agreements for professional qualifications across a range of services, notably financial services, but also legal services.

Services negotiations in FTAs are bound to be more complex because of the highly regulated nature of this kind of economic activity. The UK's priority will be financial services and it will seek arrangements such as those indicated above in relation to the EU. Since, as noted earlier, the UK is very much a global leader in financial services regulation it is expected that the UK will be in a strong bargaining position with respect to setting the terms of such agreements. A US-UK FTA could be somewhat more problematic in this regard given the US dominance and the evident intent of the new US government to de-regulate financial services going forward. The UK should use the new TPP11 as a template for progressive chapters on digital trade and trade in services as these are expected to become the standard for services agreements in the future.



PUBLIC SERVICES

Another issue relating to services under a US FTA is the much-maligned liberalization of public services like the NHS, meaning that public health services would be opened to supply by US firms. This is almost certainly a non-issue and appears to be a classic case of scare-mongering. The UK government recently clarified that public health would not be included in a FTA with the US (it would not have formed part of TTIP). This comes as no surprise given that the blueprint for international services treaties, the GATS, specifies (in Article I (3)b) that it does not cover "services supplied in the exercise of governmental authority" meaning a service "which is supplied neither on a commercial basis, nor in competition with one or more services suppliers." In other words, it excludes public health services like the NHS. Virtually all FTAs with services chapters contain this kind of language and it is likely that the UK would conserve this approach in its FTAs with other countries, including the US. Still, it would be worthwhile for the UK to consider whether various public services which are delivered in a quasi-private capacity, such as some health services, could be opened to international markets. This could lower costs for consumers and aid in the conclusion of FTAs.

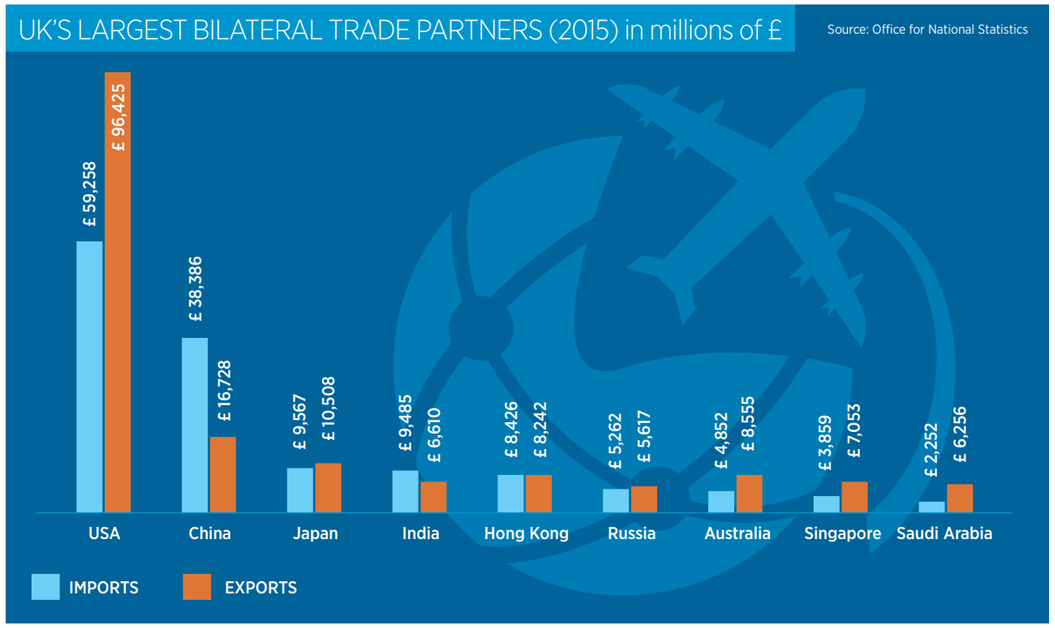
TRADE IN SERVICES AGREEMENT (TISA)

As mentioned earlier, the Trade in Services Agreement (TiSA) is a FTA covering services currently being negotiated among 23 WTO Member States including the EU and many other developed countries. Together these countries comprise approximately 70 per cent of world trade in services. TiSA is essentially an expansion of the WTO GATS, meaning that the participants will commit to greater liberalization for their services than they did under GATS in part because, as developed countries, these parties have more interest in opening services than most WTO Members (two-thirds of which are developing countries) so negotiations on TiSA could proceed more efficiently than it would were 164 Members involved. While negotiations under TiSA are currently moribund due to the lack of participation by the US, the plan is eventually to incorporate the TiSA into the WTO with a view to it encouraging other WTO members to join incrementally. The last round of negotiations for the TiSA concluded in November 2016 and there is no set deadline to terminate the negotiations. The UK would be advised to proceed with negotiations under this agreement as an independent signatory after the 2-year Article 50 period ends. Recent statements by the government encouragingly indicate a willingness to pursue this initiative. Since the TiSA will be structured like the GATS, the UK will be free to make the services commitments that it wishes in line with its economic needs.

ROLLING OVER EXISTING FREE TRADE AGREEMENTS

The UK should aggressively negotiate with the countries with whom the more than 60 countries with which the EU has already concluded FTAs for these to be rolled over into agreements with the UK on similar terms. Canada has already indicated that it may be prepared to offer the UK the same terms as it did the EU under CETA. Grandfathering of the EU's trade deals with Korea, Singapore and Peru are similarly feasible. There may be a problem with satisfying rules of origin under some of these treaties and in some cases such negotiations may need to be pursued trilaterally along with the EU. The quantum of the "divorce" payment should be predicated on the EU's willingness to assist in this regard. From the perspective of the EU, it is unlikely that the EU's existing trading partners will seek renegotiation of their treaties as a consequence of the UK's departure. Should there be resistance from third countries in this regard, the UK should be willing to assist the EU in negotiating retention of these arrangements with its treaty partners.

The UK may also consider joining negotiations under the new Trans Pacific Partnership or TPP11, which has been mentioned before. This new agreement, which is apparently proceeding without the US, involves 11 Pacific Rim countries including the UK's key trading partners Japan and Canada. The TPP11 will be comprehensive, covering goods, services and investment. It will also be progressive with labour and environmental standards as well as material on



digital commerce. There may be opportunities for the UK eventually to join NAFTA and other regional arrangements. In order to facilitate inclusion in such regional agreements, the UK should considering joining in the negotiations of these treaties as an observer.

INVESTMENT

Foreign investment is a vital component of the UK economy, with inward and outward FDI stocks roughly even at just under £1 billion per year respectively. The UK has 97 Bilateral Investment Treaties (BITs) currently still in force, most of which are with developing countries. It is a party to the Energy Charter Treaty, which facilitates trade and investment in the energy sector. As indicated above in relation to the UK-EU FTA, the UK should include an investment chapter in its future FTAs with other countries offering foreign investors the basic protections contained in these treaties. It could also pursue BITs covering investment only without trade, as it did in the past before the Lisbon Treaty transferred this competence to the EU. Whether as part of FTAs or through BITs, the UK should take this opportunity to update its investment treaty practice from its Model BIT of 2008 in line with modern trends. These include providing clearer definitions of indirect expropriation and Fair and Equitable Treatment, the standard under which most investment claims have been brought. It would be advised to include provisions specifying the right to regulate in matters of public interest in order to foreclose claims based, for example, on regulations designed to address public health matters. Such precautions should not be viewed as interferences with normal market conditions in the UK, but rather insurance against frivolous claims, which, although rare, are best avoided.

As indicated above, the UK should maintain standard investor-state dispute settlement (ISDS) in its investment treaties as this represents an attractive feature to foreign investors and could be advantageous to UK firms operating overseas in environments with weak rule of law. As many of the UK's future investment partners will be emerging and developing countries the importance of the procedural and substantive protections of investment treaties must not be underestimated. In keeping with recent expected practice in relation to the new TPP, the UK could consider excluding the application of ISDS to sensitive sectors, for example financial services.

The UK should consider taking a more active role as a signatory state of the Washington Convention by recommending arbitrators and mediators to the roster of the International Centre for the Settlement of Investment Disputes (ICSID). It has not done this in a number of years and there is no reason why it should not do so.

THE IMPLICATIONS FOR THE EU

Although the EU will certainly lose out on beneficial trade with the UK in the absence of an FTA, it seems clear that the EU may be unwilling to conclude such an agreement because of pressing issues relating to the jurisdiction of the ECJ, free movement of people and Brexit separation payments, to name a few. Nonetheless in respect of the WTO, and regardless of such sticking points, the EU must treat the UK as an equal member of the WTO, as to do otherwise would amount to a breach of its commitments as a member of that organization. The EU has a long-standing reputation for leadership and international cooperation through the WTO and it this can be expected to continue going forward.

Beyond its relationship with the UK as a fellow member of the WTO, the UK's capacity to form international trade agreements with third states following Brexit should be of limited interest to the EU. As economists will readily point out, international trade is not a zero-sum game and the UK's conclusion of trade agreements with other countries does not mean that the EU will not also be able to form such arrangements. While it is true that each country has a finite negotiating capacity for international trade treaties, the infamous notion that there is some negotiating "queue" in which a country is either at the back or front is disingenuous.

Still, there has been some debate as to whether the UK can commence trade negotiations with third countries while still a member of the EU. Some have suggested that to do so represents an affront to the principles of EU law. There is nothing in the EU agreements which prevents the UK from negotiating such treaties as long as they do not go into effect before the date of Brexit. Whether or not this might change given an interim agreement (it is suggested here that the UK should not surrender this capacity as part of an interim agreement negotiation, which has been mooted) it may be that the UK's act of so doing might be viewed as a gesture of bad faith on the part of the EU, frustrating EU-FTA agreements. Were this the case, then UK trade negotiators should clearly prioritize the EU-FTA. However, it is hoped that preliminary, informal trade negotiations should be able to proceed on multiple fronts and it is encouraging that UK representatives have begun to do so accordingly. The UK must set up working groups for trade negotiations with priority countries, especially the US and China. To the extent that there is a limited budget for trade negotiations, these countries, along with the mega-regionals noted above, should be the UK's top priority. The economic gains here will outweigh those of smaller countries, such as Australia and New Zealand, even if such FTAs are more feasible. A long-term perspective must be maintained.

The aim should be to have such agreements with other countries underway upon the UK's departure from the EU after the two-year Article 50 period ends in March 2019. At that stage the UK will be in a position legally to bring into force agreements with other countries, and as such should have greater credibility as a potential treaty party. This process could be frustrated if there is a prolonged EU transition period, depending on the nature of that agreement. Retaining temporary membership in the customs union has been discussed as an aspect of the transitional agreement and this could make third countries unwilling to commit resources to negotiating with the UK – indeed Japan has said this. This is precisely why a transition period must not last longer than two years.

Again, as noted above the implications for the EU are minimal since there is no reason that the EU cannot continue its negotiation and conclusion of FTAs with third states, although it will offer somewhat diminished market access in the absence of its second largest economy. The EU will continue to engage in trade leadership worldwide and is expected to achieve economically beneficial trade deals with countries such as Japan and ultimately the US in the coming years. Some commentators have suggested that competition for trade deals may actually spur countries to negotiate agreements faster and with the UK entering the world stage this added pressure may result in quicker conclusion of FTAs and plurilateral agreements like TiSA.

7

CHECKLIST FOR THE UK

Departure from the EU represents an extraordinary opportunity for the UK to take advantage of its economic strengths and its reputation as a robust and dynamic trading nation committed to rule of law and open markets. The UK can achieve mutually beneficial trading relationship with Europe based on common commitment to these principles. While trade agreements take time, an interim arrangement may be possible which will lay the groundwork for comprehensive trade with the EU and a close alliance with Europe after departure from the EU, while preserving regulatory and judicial autonomy and restricting freedom of movement of persons. Should such an agreement with the EU not be immediately forthcoming, the UK will enjoy the low tariffs and market access offered through its status as a Member of the WTO. The UK will be well positioned to form favourable bilateral trade agreements with other countries leveraging its competitive advantages as required. A prosperous trading future is a realistic goal that should underpin the UK's negotiating position with the EU and other partner countries going forward.

- **WTO Schedules of Commitments for Goods and Services** - Prepare its WTO Schedules of Commitments for Goods and Services – initially keeping those offered to other WTO Members at the same level it did as a Member of the EU. The UK should move to unilaterally lower tariffs on a range of goods quickly, starting with those products where there is no domestic production.

- **UK Share of Tariff Rate Quotas** - Prepare its position on its share of the EU's Tariff Rate Quotas, binding its past tariff commitments on all products which were covered by tariff rate quotas for the next few years. This will involve consultations with affected WTO members.

- **UK Entitlement to Agricultural Subsidies** - Prepare its position on its entitlement to the EU's Aggregate Measure of Support for agriculture, likely to be based on the portion of the UK's contributions to the EU's CAP.

- **UK Regulatory Capacity for Trade Matters** – continue to enhance its domestic regulatory capacity for trade matters through the Trade Remedy Authority including resourcing customs procedures and procurement taking advantage of new technologies.

- **The Basis for an Interim Agreement** - The transition period should be limited to 2 years and should not include the elements of EU membership to which voters have objected. In law, the assumption is that it must also culminate in a comprehensive FTA with the EU.

- **UK-EU FTA** - Negotiate a comprehensive FTA with the EU replicating as closely as possible the tariff-free access for goods, services and investment under the Single Market while avoiding ECJ jurisdiction and free movement of persons. Resolution of the Brexit settlement payments should be deferred to a third-party adjudicator to facilitate negotiations. The UK's aim and strategy should be designed to ensure the EU's participation in roll over negotiations regarding existing EU FTAs with third states. It should also aim to ensure an FTA allows the UK freedom to diverge from the EU with respect to regulations on goods and services, avoiding any UK commitment to alignment.

- **Financial Services** - If 6 is not forthcoming, seek a Mutual Recognition Agreement for Financial Services based on common regulatory outcomes.

- **UK Trade with US and Commonwealth** - Prepare for expiry of Art 50 period and negotiate FTAs with strategic economic partners, especially United States and China, followed by the Commonwealth. Seek to roll over existing trading relationships achieved through the EU. Seek to join the TPP11 and NAFTA, initially by joining these negotiations as an observer.

- **UK Global Trade Leadership** - Actively pursue trade negotiations under the WTO, TiSA, and other regional initiatives with a view to setting the agenda as a leader in global trade.

8

CHECKLIST FOR THE EU

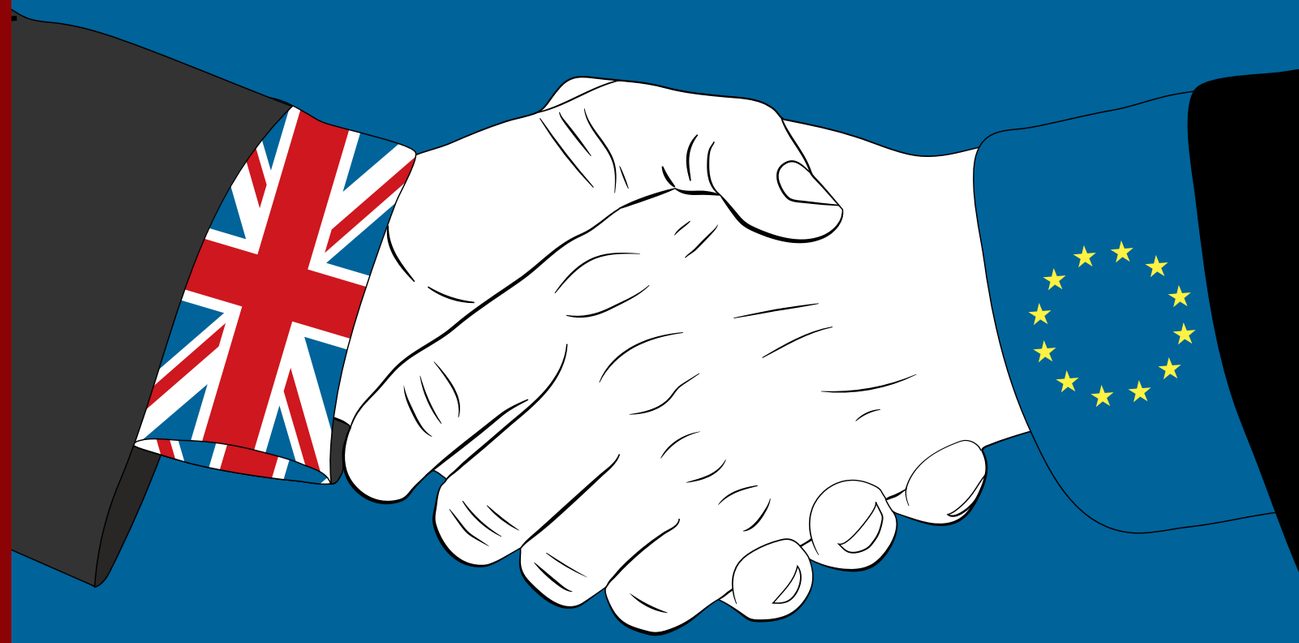
- Pursue negotiations with the UK for an FTA – This should be done soon, possibly via an interim arrangement which preserves some aspects of the existing relationship. Financial matters should be resolved by a neutral third party so that attention can be devoted towards trade.

- Prepare for the above FTA by working with the UK to establish a bilateral trade dispute settlement panel.

- If an FTA with the UK is not achievable, use mutual recognition agreements to facilitate market access for UK financial services under existing GATS arrangements. Prepare customs infrastructure at ports to be ready for UK exports after March 2019.

- Seek to maintain existing trade agreements with third countries on the same terms following the departure of the UK.

- Continue to pursue trade leadership at the WTO and bilateral, regional trade negotiations with other countries.



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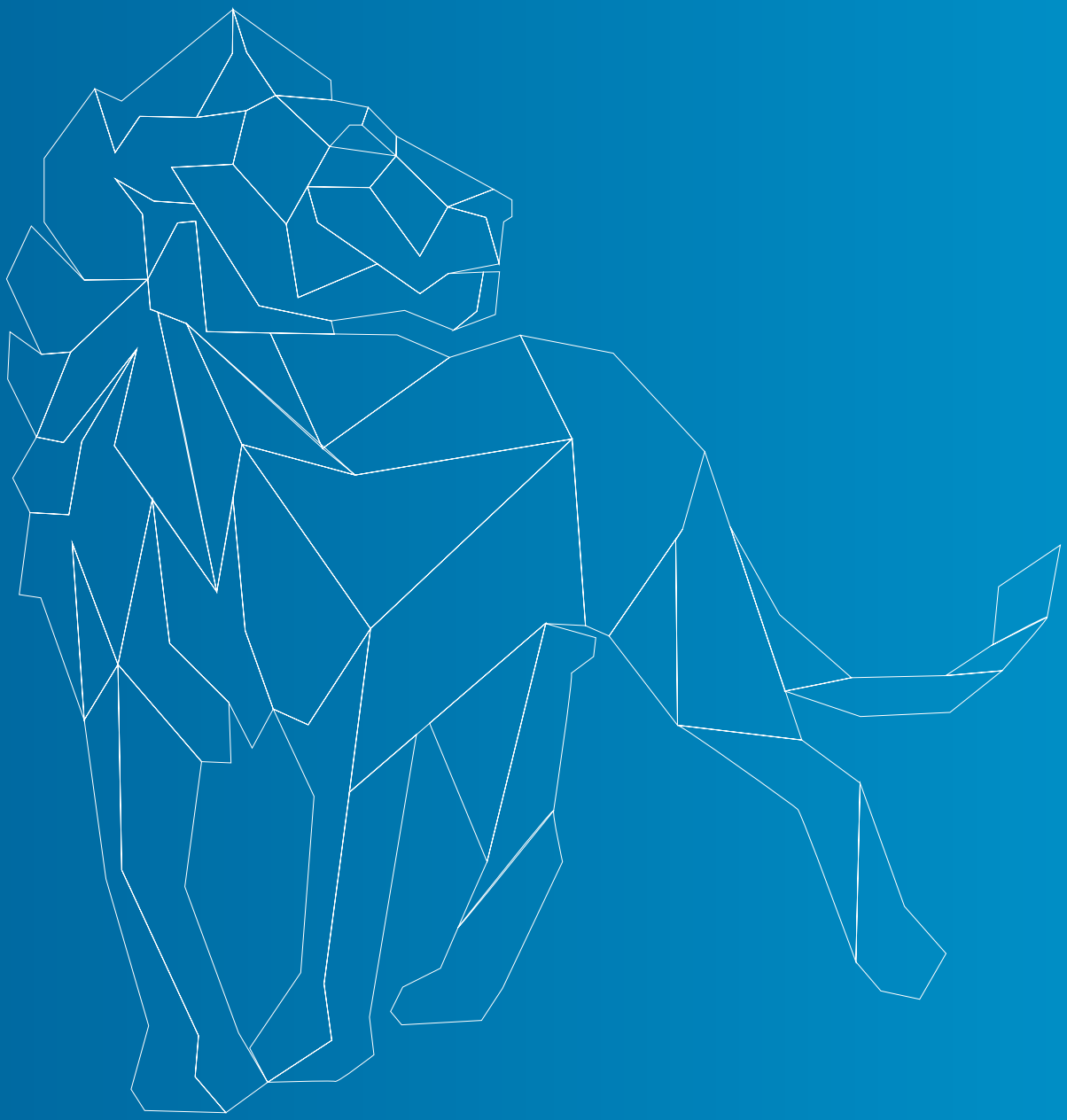
GLOSSARY

BIT	Bilateral Investment Treaty
CAP	Common Agricultural Policy
CETA	Comprehensive Economic and Trade Agreement
DUP	Democratic Unionist Party
ECJ	European Court of Justice
EEA	European Economic Area
EEC	European Economic Community
FTA	Free Trade Agreement
ICSID	International Centre for the Settlement of Investment Disputes
ISDS	Investor-State Dispute Settlement
MFN	Most Favoured Nation
NAFTA	North American Free Trade Agreement
GATT	General Agreement on Tariffs and Trade
GDP	Gross Domestic Product
GPA	Government Procurement Agreement
SNP	Scottish National Party
SPS	Sanitary and Phytosanitary
TBT	Technical Barrier to Trade
TiSA	Trade in Services Agreement
TPP11	Trans Pacific Partnership without the US (Comprehensive and Progressive Pacific Trade Agreement)
TTIP	Transatlantic Trade and Investment Partnership
WTO	World Trade Organisation



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