

Re: Northern Ireland and Custom Union Deal

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General Comments

As things currently stand, the proposal for the acceptance of EU single market rules and customs union by NI remains very vague. It is not clear to us whether the ultimate aim is to maintain Northern Ireland within the EU customs union and single market or whether it is merely intended as a commitment to ensure that Northern Ireland would mimic the customs union and EU rules in a post-Brexit scenario. The latest reports indicate that the commitment for regulatory alignment would apply in a no-deal (i.e., hard Brexit) scenario. In that case, merely mimicking EU single market rules and the EU customs union would not be enough to remove all barriers to trade between Northern Ireland and the Republic of Ireland.

Such lack of clarity most likely reflects the fact that stage one of Article 50 TEU negotiations are focused on articulating policy outcomes rather than determining how such outcomes can be achieved in practice.

The comments below are premised on the assumption that the model currently being discussed is one where Northern Ireland would be granted a special status where it remains part of the EU customs union and is required to comply with EU internal market rules on goods.

WTO: Is this model compliant with WTO rules?

As discussed, based on available information, there are two potential areas where the NI proposals might prove problematic from a WTO law perspective. Firstly, if only Northern Ireland is to remain within the customs union and comply with EU single market rules then goods moving from Northern Ireland to the rest of the GB would have to go through customs control and pay tariffs. In the absence of a trade agreement between the EU and the GB, if the GB chooses not to apply tariffs to goods originating from Northern Ireland this would constitute a clear violation of the most-favoured nation obligation under WTO law.

Another source of non-compliance concerns the fact that under WTO law preferential trade arrangements must cover “substantially all trade” in goods between the two negotiating parties. A preferential trade arrangement between the EU and a region of the GB would arguably fail to meet the “substantially all trade” threshold. However, we do not believe there is a significant risk of this being the subject of litigation at WTO level. Most preferential trade arrangements violate WTO law but no complaint has ever been lodged before the WTO Dispute Settlement Mechanism. WTO Members are very reluctant to engage in litigation on the legality of PTAs because they do not want their own PTAs to be subject to scrutiny.

GB to NI trade: How this solution would impact on goods moving from GB to NI? Would NI in effect remain in the EU Customs Union while GB sits outside of this framework, resulting in MFN tariffs and NTBs being applied to GB goods entering NI?

It depends on the exact nature of the arrangement that is actually being proposed (see general comments above). If the idea is for Northern Ireland, alone, to remain within the EU customs union and comply with single market rules, barriers to trade with GB would be inevitable. The extent of those barriers would then depend on the future trade relationship between the EU and the GB.

- If no agreement is reached between the EU and the GB, goods from NI would be subject to MFN treatment and NTBs.
- If a FTA is signed between the EU and the GB, which removes all tariffs, products originating from NI and intended to the GB would still need to be checked to ensure, for example, that they comply with GB regulations and standards (and vice versa).
- If the GB opts for a soft Brexit (Norway option), customs checks will be required to ensure compliance with rules of origin (i.e., that goods imported from Northern Ireland originate from the EU customs union, rather than a non-EU country).

In other words, nothing short of continued participation in the customs union and the single market rules on goods by the United Kingdom as a whole would ensure the removal of all barriers to trade between GB and NI.

NI to GB trade: Could the GB Government unilaterally allow NI goods into GB? Is there any precedence of one region of a state having different regulatory standards but maintaining market access to the wider regions?

See first answer. To the best of our knowledge, there is no known case of a region being granted completely unfettered access to a markets whilst maintain some level of regulatory divergence.

Classification of goods: Do WTO rules allow goods to have ‘dual citizenship’? I.e. could goods be British or Irish depending on which market their sold to?

If NI retains a special regime de-facto aligned to the EU in terms of regulatory equivalence and, supposedly, no tariffs at the border, NI goods will be subject to one regime (the EU). If a EU-originating good enters NI from the Republic of Ireland it will receive no customs checks and, once in NI, it will be treated like a local product. If the same good is then shipped to GB to be sold in the GB market (Scotland, Wales, and England), it will be subject to GB customs. In this case, the customs checks will be done by the customs authorities in GB. In our view, the NI customs authorities will act on behalf of the EU in checking the origin of the good and its customs classification. Here are the scenarios:

- Goods produced in NI and going to the Republic will not be subject to customs checks.

- Goods produced in the GB and going to NI will be subject to customs checks in GB as if they were shipped to Spain.
- Goods entering to NI from the rest of the world, would have to be subject to EU customs. If the goods are then sold to the GB, they will have to be subject to customs checks at the GB custom border.

GB independent trade policy: Could NI still access the benefits of a GB independent trade policy in this scenario? E.g., could NI businesses avail of a GB-USA trade deal and export products to American under a preferential tariff? Can NI still have access to EU FTAs?

If NI was to remain within the customs union and required to maintain regulatory equivalence on goods with the EU it could continue to benefit from EU FTAs with respect to goods. For example, Jersey is currently part of the EU customs union but is only covered by EU FTA provisions that relate directly to trade in goods. In theory, one could also envisage a scenario where NI would be covered by future GB FTAs with respect to areas not covered by the customs union and where it maintains the competence to diverge from EU single market rules (e.g., services).

Practically speaking, however, this would be difficult to implement and it's debatable whether from a policy perspective NI would benefit from being subject to two different trade policies simultaneously.

Back door risk: Northern Ireland becoming a 'back door' the GB market and potential disputes from WTO members resulting from Ireland having preferential access to GB via the land border.

The risk is on the EU side.

Operationalisation: How could this model be implemented? Would it require trade policy to be devolved to the NI Assembly?

Legally speaking, GB could still retain the power to decide the NI trade policy as it does under the current Customs and International Trade Bills. Politically, however, it will be very difficult for the GB government to justify why NI should not have significant powers devolved in this area since its trade policy will, by definition, have to be aligned with the EU's.

From a practical perspective, NI should call for greater powers in matters of customs and international trade, in addition to the powers it already has under the current devolution arrangements.

Suggestion: Northern Ireland as an Independent Custom Territory?

We think that a potential solution that would enable NI to remain in the GB whilst at the same time avoid a hard border with the Republic is to devolve independent customs and trade

policy powers to NI. There are a number of models that could be followed in this respect (e.g., Hong Kong SAR with China).

For example, NI could become an independent custom territory and would then adopt a fully open trade policy towards the GB and the EU. The scenario would be as follows:

NI would be given constitutional powers to set customs duties and implement certain regulations in key goods and services industries. The powers would have to be detailed in a separate Bill and, possibly, a modified devolution arrangement between the GB and NI. NI would maintain a zero-tariff profile with the GB and the EU through separate trade deals. From a political perspective, this solution would not breach PM May's commitment that NI would leave the EU on the same terms as the GB, because NI will not apply any tariffs towards the GB.

NI would then enter into two separate customs agreements: one with the GB and one with the EU

- The agreement with the EU entails no tariffs on all goods to and from the EU and NI as well as regulatory equivalence on key sectors. De facto, NI's regulatory perimeter would be aligned to the EU's.
- The agreement with the GB would entail the removal of customs checks between NI and the GB and vice-versa. There could potentially be regulatory divergence between NI and the GB in certain sectors, notably goods. This means that NTBs would still be a factor and border barriers would have to be put in place with respect to NI-GB trade.

If NI becomes an independent custom territory, all exports from NI to the rest of the world would be subject to customs duties at the border in the export destination, as NI goods cannot qualify as EU or GB originating goods. NI will then have a choice of becoming an independent WTO Member to benefit from MFN tariffs, or to bypass the WTO membership and simply strike selective FTAs with key export destinations such as the US.

Under this arrangement, NI could also adopt the Singaporean model and use its open trade policy to its advantage by creating free trade zones and export processing zones where goods could be assembled or reshipped. The real risk in this scenario is that other regions in the GB will block the deal as NI will be in a position of competitive advantage against the rest of the GB. NI will become the preferential entry point for EU goods going to the GB and vice-versa.

The VAT Question

The customs union/regulatory alignment proposals would not entirely eradicate the need for customs control. Businesses located within the EU do not pay any VAT to trade with each other. However, upon leaving the EU, EU-UK trade in goods will be treated as imports (rather than an intra-EU transaction) meaning that import VAT would be due at customs before the goods can be released. Since the EU VAT regime is separate to the EU customs union, the

removal of border barriers between NI and the Republic also requires some sort of agreement on VAT issues.