

13.11.2017

EU-UK trade relations after Brexit – updated position of the dairy trade

As negotiations continue for the Brexit, it seems increasingly unlikely that this political process will be reversed. Since the publication of our last position paper in February 2017, we have had time to reflect further on some of the implications of Brexit and on some of the considerations that need to be taken into account as the UK gears up to exit the EU at the end of March 2019.

Our baseline position remains unchanged: the future trade relationship between the EU and the UK should be as close to the present situation as possible. We accept that if the UK is no longer part of the single market or the customs union, trade cannot be as frictionless as today. However, milk and dairy products should circulate as freely as possible between the two markets, without being subject to any tariffs or unnecessary non-tariff barriers and only subject to minimal customs controls and procedures.

Moreover, although the widely publicised ‘end game’ is March 2019, negotiations should continue for as long as is necessary to avoid a ‘cliff-edge’ scenario in which no specific parameters for the new relationship have been decided. Agreeing on a transitional or implementation period should be a top priority at this stage. The continuation of the ‘status quo’ would be the ideal option while the EU and the UK discuss the best deal possible.

1. Transitional period

To avoid a hard border with 40% to 80% duties on dairy products and countless non-tariff barriers, a transitional period between Brexit and the entry into force of the future permanent arrangement is required. Since no one knows how the future arrangement will look like, the most sensible option for the transitional period is a prolongation of the status quo by extending the two year period as provided for in article 50 (3) TEU or by agreeing on a later withdrawal date in the withdrawal agreement. This would mean that the UK remains a full member of the EU during the transitional period. This solution has the considerable advantage that trade will only have to adjust once to a new reality (once the new framework is in place) rather than twice (on the day of exit and again when the new arrangement is in place). With less than a year left and negotiations still in the first phase, a mutually agreed prolongation of EU membership may also be the only feasible option. There may not be sufficient time to negotiate another kind of temporary deal.



2. Definitive trade relationship

From our perspective, the form and label of the future trade deal (association agreement or other) is secondary. What matters is that it is as comprehensive as possible, going beyond any of the existing trade agreements in terms of ambition. For dairy trade, we see three crucial components for the future EU-UK trade arrangement: the absence of tariffs, alignment or equivalence of food legislation and customs facilitations.

No tariffs

Current dairy trade flows between the EU and UK amount to some 4 billion € per year. We do not have tariffs in place today and we do not see any reason why import duties on dairy products should be reintroduced in the future. This would only create additional costs for both businesses and consumers. Tariff free trade between the EU and UK is in no way contradictory with the UK's desire to conduct its own trade policy as the duty-free treatment should only apply to goods of EU and UK origin. The extension of benefits to other countries can be excluded with rules of origin, like in any free trade agreement.

If the current EU external tariffs were applied by both sides, the dairy sector would be among those hardest hit, with estimates suggesting more than 90% of current trade being eliminated. This said, the UK is only about 81% self-sufficient in dairy and as such will have to continue importing large volumes of dairy products, in particular cheese.

Customs facilitation solutions

The rhetoric from the UK since March 2017 has left no doubt that the UK will be taking permanent leave of the Customs Union. The main reasoning behind this decision would be to allow the UK to independently negotiate FTAs with third countries, however it poses many unanswered questions with respect to the future customs relationship between the EU and the UK.

In its position and white papers on customs, the UK has put forward some rather interesting ideas to limit the additional burden on trade, such as waiving the need for entry and extra summary declarations for the movement of goods between the EU and the UK, mutual recognition of Authorised Economic Operators (AEOs) and various administrative simplification measures.

The possibility of an enhanced 'customs partnership' is also put on the table, aligning the UK import regime with that of the EU external customs border. The second option outlined in the UK papers seems the most desirable as it would eliminate the need for customs checks between the EU and UK, however it poses some challenges in relation to the application of rules of origin on goods from third countries with which either the EU or the UK will have a



free trade agreement in place. We would support creative solutions to ensure that movement of goods is disrupted to the least extent possible.

Sanitary and veterinary solutions

In addition to keeping customs channels open, we also wish to see continued alignment and co-operation in the field of food safety and veterinary rules. This would prevent cumbersome divergence in rules and standards in the years to come and would 'keep the milk moving' across the border. It is worth reflecting that the starting position with the UK is very different to that of a regular third country trading partner. Currently there is already perfect alignment.

Nonetheless, looking at the pre-existing solutions for veterinary co-operation between the EU and third countries, the most comprehensive is that between the EU and Switzerland, which allows for the movement of dairy products without veterinary controls. This represents the baseline of what we should accept in an eventual EU-UK deal.

There has been equivalence applicable to health and safety requirements for all foods of animal origin between the EU and Switzerland since 2006 and border checks between the two territories have been abolished since 2009. Veterinary certificates are no longer a requirement in this common veterinary area.

As a result, a very positive environment for trade in cheese (to which no tariffs apply) exists between the EU and Switzerland, with volumes constantly increasing. We sincerely hope a similar solution can be found for EU-UK trade.

To avoid the creation of trade barriers in the future through diverging legislation, a regulatory committee should be set up to ensure continuous coherence between the EU and UK on food safety matters.

The particular case of (Northern) Ireland

As has been widely documented, Ireland will be by far the most affected Member State by Brexit. In terms of dairy trade, Ireland is both the main supplier and customer of the UK. Next to dairy consumer products and commodities, huge volumes of (highly perishable) raw milk are being transported every day from Northern Ireland to the Republic. It is evident that a creative solution maintaining the free movement on the island of Ireland has to be found. Apart from the trade between the UK and Ireland, most Irish exports to mainland Europe and beyond also transit via the UK. The customs arrangements should also make sure that this "land bridge" function of the UK is not damaged.

3. Impact on trade with third countries - breakdown of existing WTO TRQs

Next to trade between the UK and the remaining 27 Member States, the UK's decision to take its leave of the EU also has consequences on the international commitments of both the EU and the UK. While we understand that the EU will simply inherit all existing free trade agreements without any change to them, this is not the case for the commitments made under the WTO, of which the UK is also a member. In this context, we welcome the decision by the UK to at least initially replicate the EU external tariff after its exit from the bloc as this will probably facilitate discussions on the future framework for trade between the EU and UK.

The EU and UK have also already adopted a joint position regarding existing WTO tariff rate quotas (allowing for preferential imports into the EU) which need to be revisited as the concessions offered by the EU at the WTO were calculated on the basis of the UK being a member of the EU.

The EU-UK understanding on the way forward, to be discussed with other WTO members, bases the split on 'current trade flows' and indicates that any disruption to trade with third country partners would be minimised.

Establishing an exact breakdown of 'imports per Member State' for the purposes of dividing up existing WTO quotas (e.g. the New Zealand butter quota) could however prove tricky, based on the so-called 'Rotterdam effect', whereby a large proportion of product imported under the quota enters the EU via one port (e.g. Rotterdam) before being distributed to different Member States. Additionally, basing the division of the quota on current imports does not take into account certain *erga omnes* quotas, which have not been used in recent years.

Alternative solutions could be to break down the quota volumes based on national production in the UK and the EU Member States respectively or to base the breakdown on market size. Looking at trade volumes in isolation outside of the quota could be another avenue to explore.

Conclusion

The first priority should be to avoid a 'hard Brexit' in March 2019 by agreeing on a transitional or implementation period which should run until the end of 2020 at the very least, allowing for sufficient time to come to a mutually acceptable outcome. Beyond that, a comprehensive *sui generis* trade arrangement building on the current situation of barrier free trade and regulatory alignment should be put in place.