

# BREXIT UNIT

## The UK can do better than the EU's Customs Union

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Like most decisions about Brexit, the choice of future customs arrangements is about getting the trade-offs right. Remaining in a customs union with the EU would not just prevent disruptive border checks. It would also allow tariff-free trade to continue after the UK left the Single Market, and could make it easier to replicate the EU's existing trade deals with third countries. These benefits should not be dismissed lightly.

Nonetheless, securing these benefits via a full customs union would come at a significant cost. This option would prevent the UK from making the most of the opportunities to reduce barriers to trade with the rest of the world, whether by signing new deals or simply lowering these barriers unilaterally.

What's more, a full customs union is not the only option. The UK could keep any additional trade frictions with the EU to a minimum with a new and comprehensive free trade agreement, including alternative customs arrangements. There may still be a case for a time-limited extension of the current customs union, perhaps for goods only, during a transition period. However, it is far too soon to conclude that this is the best solution for the longer term, especially as talks about the future relationship haven't even begun.

### The battleground

The government's public position is that the UK will be leaving the EU's Customs Union after Brexit and that it won't simply replicate this arrangement with 'a customs union'. Instead, the UK will seek a new form of customs 'agreement' or 'partnership' that minimises tariff and non-tariff barriers, as part of a comprehensive free trade agreement (FTA).

Nonetheless, the government is also said to be considering the option of remaining in a modified customs union after March 2019, perhaps for trade in goods only. This could simply be a time-limited extension of the current arrangement during the transition period. But some officials and ministers appear to be pushing it as a permanent solution.

### What is a customs union, anyway?

Going back to basics, a customs union eliminates tariffs and minimises border checks on trade between member states. In return, all members agree to impose the same duties and controls on trade with non-members. In practice, this makes it very difficult for any participant in a customs union to operate their own independent trade policies. (It doesn't really matter here whether you capitalise the 'c' and 'u', or not.)

As a member of the EU's Customs Union, the UK is obliged to impose the EU's common external tariffs on imports from the rest of the world. The EU has also created a legally-binding 'Common Commercial Policy', which means that only the Union can conclude trade deals with other countries. This makes external trade the exclusive responsibility of EU, allowing it to negotiate on behalf of all its member states.

### Key points

- The UK government's public position is that it is leaving the EU's Customs Union after Brexit. However, it is also said to be considering the option of remaining in a modified customs union – not just during a transition period, but perhaps permanently.
- A 'customs union' eliminates tariffs and minimises border checks on trade between participating countries. On the other hand, it severely limits the freedom of members to set their own policies for trade with the rest of the world.
- The EU takes this one step further with a 'Common Commercial Policy', which means that only the EU can conclude trade deals with other countries.
- Membership of either the Customs Union or the Single Market delivers tariff-free trade. But the Single Market brings additional rights - and obligations.

The Customs Union is not the same as the Single Market. Indeed, it is possible to participate in one and not the other. Norway, for example, is a member of the Single Market but not the Customs Union, while Turkey participates in a limited Customs Union outside the Single Market.

Membership of either arrangement does rule out the imposition of tariffs on trade between participants. But the Single Market brings additional rights and obligations, including free movement of people and rigid standards and regulations that apply to the whole economy. Members are also expected to contribute to the EU budget.

### **The case for remaining in a customs union ...**

One advantage of remaining in a customs union with the EU would therefore be that it could minimise trade frictions without the UK having to keep all the baggage of the Single Market. This could allow the government to say it is taking back control of 'money, borders and laws', thus respecting the result of the June 2016 referendum. It would also solve the Irish border questions, since there would be no need for customs controls in the first place.

What's more, remaining in a customs union just for goods would still allow the UK to strike its own free trade deals around the world for services, which is where some of the biggest opportunities lie.

### **... and the case against**

However, there are two big downsides. First, remaining in a customs union, even if applied to goods only, would take away one of biggest prizes of Brexit. This is the ability to do independent trade deals with the rest of the world that cover both goods and services, to join other multilateral agreements (such as the Trans-Pacific Partnership), or simply eliminate tariffs on imports of goods unilaterally.

Second, continued membership of a customs union could be a backdoor to keeping many of the obligations of the Single Market. For example, a customs union still requires extensive regulatory alignment to allow goods to move across borders without checks. And even if the EU agreed, it is debatable whether a new customs union that doesn't apply to 'substantially all trade' would be consistent with EU rules (especially if it covered only certain goods, such as cars).

### **So, what are the alternatives?**

The case for remaining in some form of customs union is therefore not as straightforward as some assume. This suggests that it is far too soon to rule out other options, especially as talks on the future relationship have not yet even begun. These talks would still have to go ahead, particularly if the proposal was to limit any new deal to goods only. (What, for example, would this mean for the City?)

In any event, a full customs union is not the only way to minimise trade barriers and customs delays, whether at the Irish border or elsewhere. The UK government has already proposed two alternatives: a highly-streamlined 'customs arrangement' between the UK and the EU; or a new 'customs partnership' which would involve the UK mirroring the EU's requirements for imports from the rest of the world where their final destination is the EU. These options could form part of a comprehensive free trade agreement, covering both goods and services.

To be clear, these alternatives would be technically challenging and details are sketchy. It is unlikely that they would be ready for March 2019, even if there is rapid progress on a comprehensive free trade agreement with the EU. But it is also unlikely that the UK would have a stack of new deals with other countries ready to implement by then. A temporary extension of membership of the/a customs union may therefore be a good bridge to something better a few years later.

Of course, some would still be worried that this might be a Trojan horse to keep the UK in the EU's orbit permanently. However, the EU itself has said that any transition period should run out at the end of December 2020. It would make sense for the UK government to commit to this deadline for any extension of the/a customs union too.

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- Leaving the Single Market while remaining in the Customs Union might therefore be politically appealing. It would allow the UK government to say it is taking back control of 'money, borders and laws' (though not trade policy).
- Remaining in a Customs Union for goods only would still allow the UK to do its own deals for trade in services. However, taking goods off the table would significantly reduce the opportunities.
- It therefore makes sense to explore other options first. The UK government has already proposed the alternatives of a highly-streamlined 'customs arrangement', or a new 'customs partnership', either of which could form part of a comprehensive free trade deal covering both goods and services.
- These alternatives would be technically challenging and are unlikely to be ready in time for a 'clean break' in March 2019.
- A temporary extension of membership of the/a customs union until the end of 2020 may therefore be a good bridge to something better. But it is far too soon to conclude that this is the best solution for the longer term, especially as talks about the future relationship have not even begun.