The Brexit Papers

The Internal Market and the Customs Union

Paper 25

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Brexit Paper 25: The relationship between the single market, the customs union and the European Union

1. Summary

1.1 In her Lancaster House and Florence speeches, the Prime Minister articulated a positive vision of a 'frictionless' and 'deep and special' post-Brexit relationship with the EU, while fully respecting the majority vote for the UK to leave the EU. That vision was accompanied by a commitment to leave both the customs union and the single market, on the basis that remaining within them would be incompatible with underlying reasons for the referendum outcome, to end the 'jurisdiction' of the Court of Justice of the European Union (ECJ) in the United Kingdom and to take back control over the free movement of persons from other Member States to the United Kingdom.

1.2 This paper does not address the political imperatives driving the UK negotiating position. However, the question of UK membership of the customs union and the single market is logically and historically independent of membership of the EU. Each predates the existence of the EU; and a perceived tension between (i) a positive vision of a 'frictionless' relationship between the UK and the EU, particularly in respect of the border with the Republic of Ireland, and (ii) leaving the customs union and the single market, gives rise to the question whether it would be possible for the UK to remain in the EU customs union and single market after ceasing to be a Member State of the EU, or to enter into new equivalent arrangements with the remaining Member States.

1.3 This paper discusses the relationship between the customs union, the single market and the EU from a historical as well as legal perspective, reflecting the relationship between the Member States that prevailed prior to the Maastricht Treaty and the creation of the European Union (i.e. after the first major amendment to the EC Treaties in the Single European Act of 1986), and considers:

a. full membership of the internal market and customs union; but

b. a complete opt out of the EU and those political elements inherent in its creation, notably EU citizenship for UK nationals.

1.4 It is hoped that this analysis will help to inform discussion of the legal options realistically open to the UK in the ongoing UK-EU27 Article 50 negotiations.

2. Introduction

2.1 The negotiations have so far focused on the immediate task of negotiating the withdrawal of the UK from the European Union, yet the key issue is the shape of the UK's relationship with the EU going forward. It is now recognised on all sides to be increasingly urgent to move on to this second stage, in the hope of agreeing at least a framework for such a future relationship before the UK ceases to be a Member State.

2.2 From that wider perspective, the questions for future cooperation between the UK and the EU after UK withdrawal will be (i) which set of rules to apply and (ii) how any disputes about the interpretation or application of those rules are to be determined. Answers to those questions will necessarily involve striking an appropriate balance between national and international interests, whether the UK remains inside or outside a formal trading bloc such as the EU, the EEA or indeed any other major world trade bloc.

2.3 From a legal point of view, there are two essential aspects of the effect of EU membership on UK law:

a. While the UK retains formal control over the adoption and application of its own laws (including rules applicable at its borders with the EU, since it is not a member of the Schengen Agreement), Parliament has adopted special rules in respect of EU law in section 2 of the 1972 Act, giving EU law direct application and supremacy over inconsistent domestic law falling within its scope.

b. While the ECJ has no direct jurisdiction over the interpretation or application of UK law, even where UK law implements EU law, Parliament has adopted a special rule in respect of rulings of the ECJ on the interpretation and application of EU law in section 3 of the 1972 Act, giving effect to its role as the ultimate arbiter of the validity and interpretation of EU law. So far as application of EU law is concerned, enforcement of EU law within the UK is a matter for the UK Courts and authorities to perform in accordance with the duty of sincere cooperation of the UK as a Member State.

2.4 It follows that, while the UK has not given up sovereignty over the terms and application of its own laws within the United Kingdom, it has pooled sovereignty (along with other EU Member States) for some purposes, by agreeing to participate in the institutions and legal structures of the European

Communities, and subsequently the EU, including its court system, in order to gain trade and other benefits. However, this is not unique: in particular, participation in its institutions and structures is required, and has happened, in the WTO context, in return for the benefits provided by membership of the WTO.

2.5 The exceptional aspects of EU law, particularly since the coming into being of the EU itself on 1 November 1993, are: the direct enforceability and legal precedence of its requirements in the national courts; and the scope of its provisions. From the perspective of national sovereignty, the ***political*** project of the European Union, including the creation of a category of European citizenship, a single currency and the abolition of border controls within the Schengen area, involves a much greater pooling of national sovereignty than the ***economic*** projects of a customs union and a common market of the kind provided for prior to the creation of the European Union.

2.6 In strictly ***economic*** terms, the international movement of goods, people, means of transport, data, as well as agreements on the abolition of tariff and non-tariff barriers to trade, all require agreement on at least some of the basic applicable rules; and in many sectors the applicable rules are developed at international level. That is the case independently of UK membership of either the EU or the single market and customs union.

2.7 In this respect, if the UK Government envisages by a 'deep and special relationship' with the EU a trading relationship that achieves a degree of economic integration that goes well beyond any FTA currently agreed, approximating in its scope to membership of the single market (and indeed that may be ***more*** ambitious in certain economic sectors than the current single market rules, for example in respect of the free movement of services), this will not be possible without accepting an extensive institutional pooling of sovereignty that is an inherent part of the latter.

2.8 In respect of interpretation and enforcement, rules concerning international trade are in general enforceable only by countries at a political level, sometimes with agreed forms of dispute resolution and state-state sanctions as is the case under the WTO. As such, citizens or businesses generally need to go through a system of complaining to a governmental body, which then has a discretion whether or not to challenge the other country and to apply the relevant sanction. In addition, inter-governmental dispute resolution processes are slow, opaque to the citizen and the remedies available from such bodies rarely benefit individual citizens/businesses.

2.9 From the perspective of the rule of law and creating/preserving enforceable rights for citizens and businesses, it is desirable both that there be an

authoritative body to interpret relevant international rules and that citizens/businesses should be able to invoke such rules directly before national courts to seek appropriate redress, rather than having to persuade their national government to act.

2.10 Within the EU legal order, the national courts of the Member States have direct jurisdiction to apply and interpret EU law within their national legal orders, enabling EU nationals and businesses to assert their rights directly in the national courts. The ECJ performs the role of final arbiter of EU law, including the rules of the single market and the customs union, as it has done since the creation of the European Economic Community in 1957. However, it does so in cooperation with the national courts, who have broad discretion to determine points of EU law themselves or to refer such points to the ECJ for a definitive legal ruling. The appellate role of the ECJ is limited to decisions by the EU institutions.

2.11 If UK withdrawal is not to cause individuals and businesses a very substantial loss of enforceable legal rights, of a kind that they have enjoyed since 1973, then some equivalent arrangements will be needed to resolve disputes arising under whatever terms are ultimately agreed between the UK and the EU.

3. The relationship between the customs union, the single market and the EU

3.1 As a matter of black letter law, it is correct that UK membership of both the single market and the customs union is provided for by means of UK ratification of the EU Treaties (Articles 26-33 TFEU). It follows that, if and when the UK ceases to be a Member State pursuant to Article 50 TEU (whether on 29 March 2019 or at some later date), it will automatically cease to be party to the relevant provisions of the EU Treaties, and thus leave both the single market and the customs union, subject to any alternative provisions that may have been agreed between the UK and the other EU Member States.

3.2 Nonetheless, it is clear from a broader historical perspective that there is no logical or practical necessity for the UK to be a member of either the EU or the EEA in order to be a member of the internal market or the customs union, so that UK withdrawal from the EU does not form a legal or logical bar to continued memberships of either or both:

a. Both the internal market and the customs union pre-dated the creation of the EU with effect from 1 November 1993 (and the EEA on 1 January 1994):

i. the internal market came into existence on 1 January 1993 (based on the Single European Act of 1986); and

ii. the customs union was one of the founding principles of the Treaty of Rome in 1957 and was joined by the UK in 1973.

b. The 'four freedoms' that underlie the internal market were also founding principles of the Treaty of Rome, including rules on free movement of persons (inherent in the free movement of workers, establishment and services).

3.3 It is also clear from the important opt outs that the UK has achieved since the creation of the EU (e.g. from the Schengen area and the adoption of the euro) that the other Member States have accepted that it is possible for the UK (and other Member States such as Denmark) to be part of the internal market and the customs union without participating in key economic and political elements of the developing EU.

4. Issues that would be likely to arise from continued membership of the customs union and single market after UK withdrawal from the EU

4.1 It follows that, as a matter of law, it would be open to the UK, rather than leaving the customs union and the single market on withdrawal from the EU, to pursue a negotiating strategy modelled on the situation that prevailed under the Single European Act, prior to the negotiations that led to the Maastricht Treaty and the creation of the EU:

a. full membership of the internal market and customs union; but

b. a complete opt out of the EU and the political elements inherent in its creation, notably EU citizenship for UK nationals.

4.2 It is outside the scope of this paper to comment on the political implications of such a negotiating position or why it has been excluded from the outset. However, from a legal perspective, it is possible to identify certain difficulties and advantages that would be likely to arise.

4.3 First, it is clear that there would be important legal and institutional issues that would need to be resolved if this approach were to be pursued:

a. If such a bespoke arrangement were to be negotiated (i.e. a unique relationship between the UK and the EU that was not dependent on membership of either the EEA or the EU), it would require the EU and the UK to consider (in effect) the possibility that the earlier institutional structure of the European Community/European Economic Community could be revived to enable the UK alone to participate in the institutional structures of these earlier forms of integration without participation in the EU itself, possibly even by reviving the EC/EEC itself as a free-

standing institution, or alternatively by modelling a bespoke UK/EU agreement on that pre-existing legal model.

b. Agreement would have to be reached about the degree of participation that the UK and its officials could have in the administration, legislation and adjudication of the rules of this revived administrative structure. In particular, it would have to be agreed whether the UK could have a ***greater*** degree of input into the legislative process than is currently enjoyed by the members of the EEA, including the possibility of retained voting rights on certain measures on an agreed basis. While it appears inevitable that the UK would have a reduced role in the legislative process, for example in the European Parliament, that role would not necessarily be removed altogether for measures falling within the scope of the new arrangements.

c. The status of the rules of the internal market and the customs union in the UK, including in respect of the free movement of persons between the UK and the EU, would have to be agreed. In particular, there would need to be an alternative formulation that more obviously retained the sovereignty of Parliament while providing sufficient assurance to the other Member States that the UK could be relied on to observe the rules of the internal market and customs union (see further below).

d. Unless it were possible to negotiate a bespoke equivalent system, adjudication over the rules of the internal market and the customs union would be retained by the ECJ. In that case, the status of those rulings in the UK would also need to be agreed, as would the degree of participation that would be appropriate for the UK and its judges and lawyers in proceedings before the ECJ of relevance to the UK. One possibility might be a memorandum of understanding governing (i) the status of such rulings in the UK falling short of the strict obligations of membership; and also (ii) the continuing participation of the UK in ECJ proceedings falling within the scope of the new arrangements.

e. Given that the UK would have a general opt-out from the EU and its political elements, there would also need to be a clear demarcation in the jurisdiction of the ECJ, generalising the various opt-outs already enjoyed by the UK under the existing Treaties. While the ECJ would still perform its traditional role in respect of the other Member States, it would have a significantly curtailed jurisdiction in respect of the UK, which would need to be carefully defined.

4.4 While these difficulties are clearly substantial and may prove to be insuperable, this approach could also have significant advantages, including in respect of the three preliminary topics that have to date dominated the negotiations:

a. On UK withdrawal from membership of the EU, UK citizens would no longer be EU citizens and EU citizens would no longer have the status of such citizens within the UK under EU law, but each would continue to enjoy the extensive economic protections that were vested in them prior to the creation of the EU.

b. The border with the Republic of Ireland would continue to have the same open status as it enjoyed from 1973 (and indeed that it has always enjoyed in respect of the free movement of persons). This would be a substantial advantage, avoiding the need for a regulatory border either between Northern Ireland and the Republic or between Northern Ireland and the remainder of the UK.

c. The issue of the liabilities of the UK to the EU would no doubt continue to be a source of difficulty but the parties would have considerably greater room for manoeuvre and compromise, in the context of an ongoing relationship within the single market and customs union, than in the case of a clean break. This would also allow for the possibility of a renegotiation of the UK's fair share of the ongoing costs of the administration of the institutions responsible for the operation of those trading systems.

4.5 In addition to the above difficulties and advantages, there would also need to be agreement on a range of other sectoral issues that are not covered directly by the rules of the internal market, notably the common agricultural and fisheries policies; and on major horizontal policies such as competition and state aid, trade measures and environmental policy.

4.6 These should not be insuperable obstacles to a negotiated agreement: there are many issues on which EU Member States cooperate, principally within the EU but also on a multilateral or bilateral basis. Denmark for example does not participate in measures of civil justice cooperation (such as recognition of court judgments) under the EU but rather by means of bi-lateral treaties between Denmark and the EU. Such agreements could provide for simplified enforcement of judgments, thus ensuring that a UK business which sells goods into the EU has an effective means of enforcing its rights against EU companies.

4.7 There does not appear to be any reason in principle why the UK would not be able to enter into similar such treaties with the EU and/or its Member States. In such areas, it may be that a high degree of convergence without the adoption

of binding rules falling within the jurisdiction of the ECJ could be devised, as indeed they have been in other areas falling ***within*** the scope of the EU Treaties where the UK already has significant 'opt outs', such as the relationship between the UK economy and the Eurozone and foreign and security policy.

5. Specific provisions in relation to the free movement of persons

5.1 With regard to immigration, the current debate is characterised by an 'all or nothing' approach: free movement as practised to date in the UK or a visa system.

5.2 However, these alternatives are two ends of a spectrum with intermediate solutions lying between. One such intermediate solution would be to develop migration rules that enable full participation in the internal market, while respecting the principle that the UK has control over immigration. Such rules would include the right of admission to the UK for EU citizens, without the requirement to obtain a visa; the ability to seek work without restriction; and free movement for the self-employed and those looking to establish businesses, students and the self-sufficient.

5.3 UK control over immigration could be achieved by imposing a requirement to register employment, once it has been obtained; alternatively, by imposing a requirement to register within a short time of arrival in the UK, as is currently the case in Germany and Belgium, for example. Such an arrangement would allow optimum labour market flexibility, while allowing the Government to monitor the numbers of EU citizens coming to the UK to work and for which jobs. It would be a choice of the UK Government in the exercise of sovereignty; it would provide data as to the parts of the economy that draw in economic migrants; and it would avoid the cumbersome, rigid approach of a work permit scheme requiring prior authorisation before a job offer was accepted.

5.4 The domestic labour force would be protected by the continuing security afforded by UK employment law and by the ability to determine at UK level the terms on which EU citizen workers were to be given access to contributory social security schemes and other forms of social assistance. It would permit the Government, where necessary, to use its own criteria to refuse admission or to effect expulsion/deportation.

6. An interim or final position?

6.1 Finally, another critically important issue is one of transition, where the UK has made it clear that it wishes to obtain agreement from the EU to terms of transition (or implementation) after UK withdrawal. Even if the ultimate destination agreed between the UK and the EU involves departure from the single market and/or the customs union, the transitional period will necessarily have some of the features of the above assessment, with the UK party to some if not all of EU law even after ceasing to be a Member State.

6.2 The above approach would be compatible with such a transitional arrangement, whether it was agreed as the ultimate destination or as a basis for a further subsequent loosening of the legal and economic ties between the UK and the EU if subsequently agreed and approved by Parliament.

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