

# The Brexit Papers



# WTO

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## The UK's position in the WTO

### Summary

When the UK ceases to be an EU Member State its external trade policy will no longer be determined collectively at EU level. Instead, the UK will be responsible for its own representation in the World Trade Organization ("WTO") (the Geneva-based organisation which regulates trade in goods and services between 164 Member States). This re-allocation of competence will create potential challenges and concerns in the WTO.

The UK will need to take steps to regularise its position in the WTO. In particular, it will need to:

- Ensure continuity of "WTO protection" for UK exports of goods and services,
- Establish independent and de-consolidated UK schedules of commitments in a manner which minimises the risk of blockage by other WTO Members, and
- Ensure that any transitional arrangement between the UK and the EU-27 complies with WTO law.

This note addresses:

- The extent to which UK exports will continue to be covered by WTO rules post-Brexit,
- The process for establishing independent UK "schedules" in the WTO and the risk of blockage by other WTO Members, and
- Possible WTO challenges to transitional measures between the UK and the UK-27.

## Challenges to the UK's status as a WTO Member

1. WTO rules constrain the ability of importing countries to impose tariffs and other market access barriers on exports from other countries. The most unfavourable scenario for the UK would be one in which WTO rules do not apply post-Brexit.<sup>1</sup> In such a situation, other WTO Members (for example, China or the EU-27) could impose prohibitive tariffs on UK exports of goods (for example, tariffs of 100% on cars) and could choose to favour third-country service providers over UK service providers (for example, grant preferences to American financial services firms over UK financial services firms).

2. The uncertainty about market access in such a situation would create real difficulties for UK-based exporters and broader difficulties for the UK economy. Indeed, WTO protection probably represents the minimum level of protection required for UK business to function effectively.<sup>2</sup> Achieving continuity of WTO protection is, therefore, likely to be a priority for the UK.

3. Contrary to views expressed by some commentators at the time of the referendum, the exit of the UK from the EU will not result in the UK losing its status as a WTO Member. The UK is already a WTO Member in its own right and it does not need to accede (again) to the WTO. This, in turn, implies that the UK will retain the ability to enforce its WTO rights even after Brexit.

4. Moreover, the UK is likely to be able to enforce its WTO rights even if objections by other WTO Members prevent it from establishing revised goods and services "schedules" following Brexit. (WTO schedules set out the level of market access for foreign goods and services that a WTO member commits to offer to all other WTO members -the process for establishing revised "schedules" is discussed further below). This is because nothing in the WTO Agreements provides that the exercise of WTO rights by an existing Member depends on the Member having finalised individual schedules. In this regard it is worth noting that the EU's schedules have been subject to objections from other WTO Members (following successive EU enlargements) but, in practice, this has not prevented the EU from enforcing its WTO rights.

5. Of course, other WTO Members would have good grounds for political complaint in a situation where they are required to comply with their own schedules

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<sup>1</sup> This scenario was alluded to by the WTO's Director General, Roberto Azevedo, in press interview prior to the referendum. See e.g., <http://www.bbc.co.uk/news/business-36470809>.

<sup>2</sup> The assumption in all of the UK Government's economic analysis prior to the referendum was that a reversion to WTO rules post-Brexit would be the most unfavourable outcome for UK trade. See e.g., HM Government, *Alternatives to membership: possible models for the United Kingdom outside the European Union* (March 2016), p. 35 (describing the WTO option as "the minimum threshold" and "the most definitive break with the EU")

vis-à-vis UK exports while the UK itself does not have settled schedules. The obvious way of neutralising this complaint is for the UK to make a unilateral declaration that it will respect draft schedules for the UK (pending their formal approval in the WTO). Again, this is not unprecedented: the EU has followed a similar practice during prior enlargements.

6. In summary, there is a good argument to be made that UK exports are likely to be protected under WTO rules even if the UK is unable to regularise its position in the WTO by establishing valid goods and services schedules by the end of the Article 50 TFEU process.

### **Challenges to the UK's independent schedules of commitments**

7. The UK government has recognised that the UK will need to adopt its own WTO schedules post-Brexit and has announced that it will seek to "*replicate as far as possible ... current [EU] obligations*" in any draft UK schedules.<sup>3</sup>

8. Most of the detail of the EU's existing schedules can be transposed into separate UK schedules without difficulty. Specifically, the UK can simply cut and paste EU commitments which are not expressed using EU-wide volumes. For example the 8% EU-wide tariff on ball bearings, which involves no reference to EU-wide volumes, can easily be transposed into a future UK schedule.

9. However, those commitments which are expressed using EU-wide volume figures - for instance, figures in metric tonnes for the annual volumes of frozen chicken that can be imported into the EU-28 (under an EU-wide "tariff rate quota") or monetary figures for the maximum amount of agricultural subsidies that the EU-28 will grant in a given year – cannot be transposed so easily. These commitments will be much more difficult to transpose because decisions will have to be made about whether aggregate volumes need to be enlarged and about how to allocate volumes between the UK and EU-27. Disagreements about these matters are inevitable and there is no established precedent regarding these matters.

10. The question arises whether some or all of the other 163 WTO Members will have the ability to "veto" separate UK schedules if they disagree with aspects of the UK's new individual schedule of commitments. In broad terms, the legal consequence of any such "veto" will depend on the procedural setting in which it is made. While there are no procedures which apply squarely in this situation (namely the reduced participation in a customs union), there appear to be at least three procedures which may be applied, with suitable adjustments, to give legal effect to new draft schedules:

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<sup>3</sup> Statement of the Secretary of State for International Trade and President of the Board of Trade Dr Liam Fox, 5 December 2016.

- "Certification" under the decisions of 26 March 1980 (L/4962) (for goods) and 14 April 2000 (S/L/83) (for services),
- "Renegotiation" under Article XXVIII of the GATT (for goods) and Article XXI of the GATS (for services), and
- Supplementary negotiations on the basis of bespoke modalities established under Article XXVIII bis of the GATT and/or Article IV of the WTO Agreement.

11. Of these three procedural options, the second (renegotiation) is likely to be the most advantageous to the UK. This is because renegotiation can proceed over the objections of relevant WTO Members (although those WTO Members will retain the ability to make retaliatory adjustments to their own schedules).<sup>4</sup> By way of contrast, every WTO Member has a right to block certification (option (a)) and negotiations in the WTO (option (c)) are usually carried out on the basis of consensus which, again, implies that every WTO Member can block a result it does not like

12. In conclusion, renegotiation under Article XXVIII of the GATT (for goods) and Article XXI of the GATS (for services) (with suitable adjustments) is the WTO procedure which is most likely to facilitate a smooth establishment of independent UK schedules. Renegotiation is also a balanced procedure in that it gives the UK the ability to establish schedules but also gives WTO Members with substantial interests the ability to retaliate if agreement is not reached. Nevertheless, it is important to reiterate that there is no provision within the WTO Agreements dealing squarely with this situation and the ultimate determinant of developments in the WTO will be the diplomatic position adopted by the WTO Membership as a whole.

### **Challenges to transitional arrangements**

13. A third area of challenge could arise if the UK and EU-27 decide to enter transitional arrangements which provide for the gradual introduction of tariffs and other barriers to trade between them.<sup>5</sup>

14. Continuing preferential treatment during any transitional period involves a derogation from WTO rules on non-discrimination. Any such derogation would have

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<sup>4</sup> The renegotiation procedure can be triggered when a customs union is formed (under Article XXIV:6 of the GATT) so there would be nothing unusual in applying it by analogy when a customs union is being dissolved (in part).

<sup>5</sup> The White Paper refers to "*a phased process of implementation*". See HM Government, The United Kingdom's exit from and new partnership with the European Union, Cm 9417, [12.1].

to be justified under the relevant exceptions for preferential trading arrangements. Those exceptions are set out in Article XXIV of the GATT and Article V of the GATS.

15. In a transitional arrangement involving the gradual introduction of tariffs and other barriers there is likely to be a point at which UK-EU trade will no longer involve duty-free treatment for the vast majority of goods traded between the UK and the EU-27. Similarly, there is likely to be a point where the vast majority of services trade between the UK and the EU-27 will no longer be unrestricted. At that point in time the transitional arrangement may no longer be justified under the relevant exceptions for preferential trading arrangements because Article XXIV of the GATT and Article V of the GATS require that "substantially all" trade is unrestricted.

16. It follows that any transitional arrangement with this structure (as opposed to one which merely postpones the date of "Hard Brexit") will need to be authorised by the WTO Membership through a waiver. Three-fourths of the WTO Membership would have to agree to such a waiver. This will give rise to substantial diplomatic challenges for both the UK and the EU-27. There is therefore a risk that some WTO Members may attempt to engage in tactical negotiations in order to extract improved market access from either, or both the UK and the EU-27.<sup>6</sup>

## **Conclusion**

17. The UK is a member of the WTO in its own right and should be able to enforce its market access rights post-Brexit, even if its own schedules of specific commitments have not been finalised.

18. Renegotiation under Article XXVIII of the GATT (for goods) and Article XXI of the GATS (for services) is the WTO procedure which is likely to be the most suited to ensuring that individual UK schedules are established smoothly.

19. Certain forms of transitional arrangements will need to be approved by the WTO Membership by means of a waiver.

20. Given that this is an unusual situation, the smoothness of the UK's transition to separate WTO status will be likely to depend as much on economic diplomacy as on law.

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<sup>6</sup> This can take the form of larger tariff rate quotas, lower tariffs or less restrictive regulations on service providers.