

WTO – what would a hard landing after Brexit look like?

Synopsis

It has been five months since the UK's vote to leave the European Union but the precise consequences of Brexit for the UK's trade relations with the EU and with third countries remain unclear.

What is known is that the UK government intends to start the two-year withdrawal procedure set out in Article 50 of the EU treaty by the end of March 2017. However, that timeframe might be modified if the Supreme Court upholds the High Court's recent decision that Parliament must authorise the Article 50 notice of the UK's intention to withdraw from the EU.

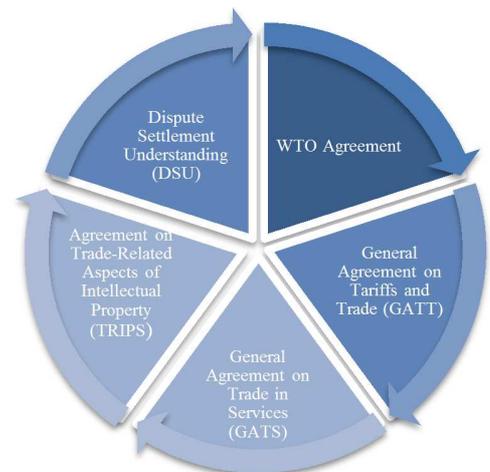
It is also likely that the UK will seek to conclude a new trade agreement with the EU governing the future UK-EU relationship.

However, trade agreement negotiations are notoriously lengthy. Unless all 27 remaining EU member states agree to extend the Article 50 negotiation period or agree to bridge the gap between withdrawal and the entry into force of any new UK-EU trade agreement, there is a real risk that the UK will leave the EU without any agreement in place governing its trade with the EU. If this were to happen, then the rules of the World Trade Organization (WTO) would apply by default. Trade in goods and services between the UK and the EU would become substantially more regulated. Tariffs would become payable on some goods, burdensome customs controls would become the norm and services could not be provided as easily as they are today.

The WTO framework and the UK's membership

The WTO provides a common framework for trade in goods and services. The Marrakesh Agreement Establishing the World Trade Organization (WTO Agreement) provides the basic rules on membership, structure and decision-making. The other four main agreements cover trade in goods, trade in services, intellectual property rights and dispute settlement.

The UK is a member of the WTO in its own right. Brexit will not change that, but the UK will need to establish membership terms separate from the EU's, including the adoption of its own tariff and services schedules. In principle, this could be a relatively straightforward process provided other WTO members (including the EU) consider that their trading interests are not harmed by the UK's proposal. However, it is not certain that this will necessarily be the case.



Brexit and trade in goods under GATT

The General Agreement on Tariffs and Trade (GATT) is the WTO's umbrella agreement intended to liberalise trade in goods by reducing barriers through the application of two underlying non-discrimination principles.

National Treatment

- WTO members must treat foreign goods in the same way as like domestic ones.

Most Favoured Nation (MFN) Treatment

- WTO members must not discriminate between other members, so any concessions granted to one WTO member must, in principle, be granted to all other members.

These principles generally prohibit quotas, import and export licences and other trade restrictions at borders. However, WTO members may:

- apply limited import tariffs as set out in each WTO member's agreed and binding tariff schedules;
- adopt specific protective measures against unfair trade practices in order to safeguard domestic industries (e.g., anti-dumping measures to counteract unfair pricing of imports below prices charged in the home market);
- apply certain exceptions to pursue legitimate public interest objectives, such as the protection of human, animal or plant life or health; and
- accord more favourable treatment to other countries with whom they are in a customs union (CU), or have concluded a free trade agreement (FTA). The EU is an example of such a CU. The EU also has FTAs with over 50 countries including Iceland, Israel, Mexico, Norway, South Korea, Switzerland and Turkey. CUs and FTAs may put in place uniform tariffs towards countries outside the CU or FTA.



If the UK leaves the EU without any agreement in place governing its trade with the EU:





Brexit and trade in services under GATS

The General Agreement on Trade in Services (GATS) aims to liberalise trade in services via a general framework of mandatory general obligations and national schedules of specific commitments.

Specific Commitments

- There is no general obligation to grant market access for services from providers based in other WTO members. Instead, specific commitments on market access for services are included in schedules annexed to the GATS and form an integral part of that agreement. Unlike trade in goods, national treatment in the GATS is negotiable, thus allowing flexibility to WTO members to tailor their commitments on services.
- The national schedules identify the services and service activities for which market access is guaranteed and set out the conditions governing this access. Scheduling can apply across all sectors or only to specific sectors or specific activities. For example, WTO members might allow market access for legal services except legal document drafting. Specific commitments can also be scheduled only for certain modes of supply. For example, WTO members might grant market access for cross-border supply (e.g., a bank providing financial advice into the host country from another member country by telephone) but restrict market access for commercial presence (e.g., the bank would not be permitted to establish a branch within the host country).
- Governments can also either: grant full national treatment if they so wish; impose limitations and qualifications on national treatment and discriminate in favour of nationals; or not grant national treatment at all. GATS is therefore severely limited compared to the current EU regime. For example it does not guarantee a right of establishment for firms or branches, the freedom to provide cross-border services or the automatic mutual recognition of professional qualifications.
- Once agreed, commitments conferring a benefit can only be modified or withdrawn following negotiation of compensation with the country concerned.

There is currently one GATS schedule for the entire EU. When the UK leaves the EU, it would either have to adopt the EU's schedule as its own or create its own. Either way, the UK's schedule might be subject to negotiations with other WTO members. To keep businesses in the UK, the UK may wish to allow other WTO members to provide services in the UK quite freely. However, as the existing national schedules of other WTO members would apply to UK companies providing services outside of the UK post-Brexit (subject to the terms of any preferential trade agreements), this may result in the UK permitting a more liberal regime for incoming services than other WTO members, including the EU, are willing to grant to services exported from the UK.

General Obligations

- Mandatory for WTO members, including the principle of MFN treatment (see above) for services, transparency of trade-restricting regulation and recognition of education and experience.
- WTO members can schedule exceptions to MFN treatment for specific existing measures, for public procurement, or in favour of adjacent countries or members who are parties to FTAs, CUs or integrated labour markets.



What does this mean for the financial services sector?

- WTO members' obligations are more limited for financial services than for other service sectors because of the "prudential carve-out". This clause in the GATS Annex on Financial Services allows WTO members to take prudential measures for the protection of investors and depositors, and to ensure the integrity and stability of the financial system, notwithstanding any other provision of the GATS.
- The GATS therefore does not guarantee very much in the way of market access for financial services providers. The EU's GATS commitments on financial services are also somewhat limited. In practice, the EU has increasingly been pursuing a common EU-wide approach to market access based on "equivalence" recognition – there are now EU-wide regimes allowing some market access, in some financial sectors, if the European Commission deems the regulatory regime applicable to the foreign services provider to be equivalent to the EU's.
- The GATS guarantees against unfair discrimination are highly relevant to any negotiated UK-EU deal on financial services. The MFN principle prohibits a WTO member from giving more favourable treatment to services and service suppliers of one state than it gives to like services and service suppliers of any WTO member. And if a WTO member makes an agreement or arrangement to recognise another state's prudential measures, it must allow any WTO member an opportunity to negotiate a similar agreement or arrangement.
- But a UK-EU deal allowing for special preferential treatment could be negotiated without having to comply with these MFN requirements if it comes within the exception for FTAs. Such a deal would have to have "substantial sectoral coverage" – it could not be limited to financial services only.

Brexit and intellectual property rights under TRIPS

The Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) establishes minimum protection levels for the intellectual property rights of other WTO members' nationals. Brexit should have minimal impact, as the level of protection of intellectual property rights in both the EU and the UK exceeds the requirements set by TRIPS.

Brexit and dispute settlement via the DSU

The Dispute Settlement Understanding (DSU) procedure allows WTO members to settle trade disputes under the WTO regime in a neutral environment. Private individuals and companies cannot bring a case against a WTO member before this forum, but may lobby their government to take up their cases. If disputes arise that concern one or more EU member states, the EU usually acts as claimant or defendant. Following Brexit, the UK itself could be a party to disputes submitted to this procedure.



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