Executive summary

On 15 August 2017, the United Kingdom (UK) published its proposals for a future customs relationship with the European Union (EU) and a model for a time-limited transition period. These proposals will form part of the background to the next round of negotiations starting during the week of 28 August 2017.

The document, Future customs arrangements: a future partnership paper is the first of a series of position papers to be released by the UK over the coming weeks and sets out its aims for the UK's future partnership with the EU. A paper relating to Northern Ireland has now also been published, however, the customs position paper is clear that the answer to avoiding a hard border between Northern Ireland and the Republic of Ireland cannot be to impose a new customs border between Northern Ireland and Great Britain.

Detailed discussion

Overview

The position paper sets out two broad future approaches. Under both, the UK leaves the EU Customs Union.

1. A highly streamlined customs arrangement between the UK and the EU, with customs requirements that are as frictionless as possible. This would include the adoption of technology-based solutions to make it easier for businesses to comply with customs procedures.
2. A new unique customs partnership with the EU, aligning the UK's approach to the customs border in a way that removes the need for a UK-EU customs border. One approach would involve the UK mirroring the EU's requirements for imports from the rest of the world where the final destination is the EU.

The Government is also keen to explore with the EU a model for an interim period immediately after the UK leaves the EU which would ensure that businesses and people in the UK and the EU only have to adjust once to a new customs relationship. The position paper suggests this could involve a new and time-limited customs union between the UK and the EU, based on a shared external tariff and without customs processes and duties between the UK and the EU.

Finally, the position paper notes that, in leaving the EU, the UK will require new domestic legislation. While the Government's preferred option is for an agreement with the EU, the Government believes it is prudent to prepare for every eventuality. Accordingly, its Customs Bill will give the Government the powers necessary to operate standalone customs, value-added tax (VAT) and excise systems, following the UK's exit from the EU.

Options for the future

Until the UK leaves the EU, it will continue to be a member of the EU Customs Union and will continue to apply EU law on customs. Membership of the EU Customs Union means that:

- Goods moving between the UK and other EU Member States are not subject to customs duty, quotas or routine customs processes (including the need to provide customs declarations).
- Member States apply the EU’s Common External Tariff (i.e., the same rates of customs duty) and its quotas and customs processes to goods which are moving between the EU and non-EU countries.
- The EU negotiates trade agreements, including tariffs, on behalf of all Member States.

The position paper confirms that as the UK leaves the EU it will also leave the EU Customs Union. The paper sets out three strategic objectives:

- Ensuring UK-EU trade is as frictionless as possible
- Avoiding a “hard border” between Ireland and Northern Ireland
- Establishing an independent international trade policy

The Government will bring forward a Trade White Paper ahead of the Trade Bill in the autumn. This will set out the Government's approach to developing an independent UK trade policy. In particular, once it has left the EU, the UK intends to pursue new trade negotiations with other nations on its own account.

A highly streamlined customs arrangement

Once outside the EU Customs Union, the UK will need to extend customs processes to all UK trade with EU Member States, as well as continuing to apply these to trade from partners around the world. The paper points out that these processes will need to:

- Ensure businesses declare goods for import or export and provide HM Revenue & Customs (HMRC) with the required documentation, including customs declarations, safety and security information and any licenses required or supporting documentation (such as that required to demonstrate the origin of goods, as may be required under a future trade agreement between the UK and the EU)
- Enable HMRC to verify that a declaration has been made, that it corresponds to the goods arriving and to intervene if necessary
- Ensure that any duties, such as customs duties and import VAT, are paid when goods arrive in the UK and the goods are released

The UK aims to negotiate trade facilitations with the EU and implement unilateral improvements to its domestic regime to make trade with the EU and the rest of the world easier. The paper recognizes that there will be an increase in administration compared with being inside the EU Customs Union. It suggests various ways to reduce the number or complexity of checks needed at borders, as well as speeding up authorization processes for traders.

Some of the examples set out in the paper include:

- Looking to simplify the requirements for moving goods across borders
- Options to reduce the pressure and risk of delays at ports and airports. These include proposals to assist Authorised Economic Operators (AEOs), a status the Government wants to support, through negotiating mutual recognition
- Negotiating customs co-operation, mutual assistance and data-sharing which replicates existing levels of UK cooperation with other Member States to reduce revenue and security risks to the UK.
• Reducing the time and costs of complying with customs administrative requirements through exploring the viability of unilateral measures, primarily in respect of imports

A new customs partnership with the EU

The streamlined customs arrangement above assumes that the UK and the EU trade with each other essentially as third parties and seeks to make the supporting customs processes as efficient as possible. The customs partnership proposal seeks to establish a new approach outside of a customs union arrangement, while still removing the need for customs processes at the border.

A particular approach the UK wishes to explore would involve the UK acting in partnership with the EU to operate a regime for imports that aligns precisely with the EU’s external customs border, for goods that will be consumed in the EU market, even if they are part of a supply chain in the UK first. The UK would need to apply the same tariffs as the EU, and provide the same treatment for rules of origin for those goods arriving in the UK and destined for the EU.

The position paper recognizes that there would need to be a robust enforcement mechanism that ensured goods which had not complied with the EU’s trade policy stayed in the UK. It also acknowledges that this is an “innovative and untested approach that would take time to develop and implement.”

An interim, time-limited arrangement

The Government wishes to avoid any “cliff-edge” in the move from the current UK/EU relationship to whatever future partnership is agreed. It believes both the UK and the EU would benefit from an interim implementation period, which allowed for a smooth and orderly transition. The Government believes it would be helpful if this principle could be agreed early in the process.

The position paper suggests that there could be a “continued close association” with the EU Customs Union for a time-limited period after the UK has left the EU. This could involve a new and time-limited customs union between the UK and the EU Customs Union, based on a shared external tariff and without customs processes and duties between the UK and the EU. The paper recognizes that the length of the interim period needs further consideration and will be linked to the speed at which the implementation of new arrangements could take place.

The position paper makes it clear that, once the UK has left the EU, it intends to pursue new trade negotiations with others. It notes that the UK would not bring into effect any new arrangements with third countries which were not consistent with the terms of the interim agreement, while the interim agreement was in place. This differs slightly from previous speculation that the UK would agree not to bring any new agreements into force until after the completion of the interim period.

What happens if there is no agreement?

While the UK hopes and expects to achieve a negotiated settlement that is in the interests of all parties, the position paper notes that it is only prudent that the Government prepares for every eventuality. Regardless of the outcome of the negotiations, the Government will need new domestic legislation to replace the existing rules which are mostly in EU law. As promised in the Queen’s speech, there will be a Customs Bill published in the autumn which, in addition to providing for negotiated outcomes, will give the Government the powers necessary to operate standalone customs, VAT and excise systems.

In this scenario, without any further facilitations or agreements, the UK would treat trade with the EU as it currently treats trade with non-EU countries. Customs duty and import VAT would be due on EU imports. Traders would need to be registered. Traders exporting to the EU would have to submit an export declaration, and certain goods may require an export license. The EU would also apply the customs rules and VAT to imports from the UK that it applies to non-EU countries. The position paper notes that the Government is actively considering ways in which to mitigate the impacts of such a scenario.

Implications

It remains to be seen how much discussion on the customs position paper will be entertained by the Commission at the next round of talks starting in the week of 28 August. There is, however, a clear link between the question of the border between Northern Ireland and the Republic and any customs arrangement and the UK will hope that setting out its position will advance talks to facilitate “the freest and most frictionless trade possible in goods between the UK and the EU.”

While the shape of any future trade agreement may start to be outlined over the coming months, clarity around the outcome of the complex trade negotiations may not be forthcoming for a while longer. Waiting until the end of the negotiation period may not leave enough time to take measured action before rules and trading arrangements change.
For additional information with respect to this Alert, please contact the following:

**Ernst & Young LLP (United Kingdom), London**
- Marc Bunch +44 20 7980 0298 mbunch@uk.ey.com
- Mats Persson +44 20 7951 1633 mpersson@uk.ey.com
- Gerard Koevoets +44 20 7951 6496 gkoevoets@uk.ey.com
- James Bailey +44 20 7760 9414 jbailey2@uk.ey.com
- Marius Cosnita +44 20 7197 9221 mcosnita@uk.ey.com

**Ernst & Young LLP (United Kingdom), Leeds**
- Penny Isbecque +44 113 298 2447 pisbecque@uk.ey.com

**Ernst & Young LLP (United Kingdom), Glasgow**
- Susan Scott +44 141 226 9343 sscott@uk.ey.com
About EY

EY is a global leader in assurance, tax, transaction and advisory services. The insights and quality services we deliver help build trust and confidence in the capital markets and in economies the world over. We develop outstanding leaders who team to deliver on our promises to all of our stakeholders. In so doing, we play a critical role in building a better working world for our people, for our clients and for our communities.

EY refers to the global organization, and may refer to one or more, of the member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. For more information about our organization, please visit ey.com.

Indirect Tax

© 2017 EYGM Limited.
All Rights Reserved.
EYG no. 04724-171Gbl
1508-1600216 NY
ED None

This material has been prepared for general informational purposes only and is not intended to be relied upon as accounting, tax, or other professional advice. Please refer to your advisors for specific advice.

ey.com