



HOUSE OF COMMONS

LONDON SW1A 0AA

020 7219 4198

08 April 2019

Dear Graham.

Following my appearance at the 1922 committee on Wednesday last week, I committed to sending a letter setting out the issues around a customs union and trade policy.

Let me begin by repeating what I said at the meeting. Trade is not an end in itself but a means to an end. It is the way in which we spread prosperity more widely. That prosperity underpins social cohesion which in turn underpins political stability. That political stability is the building block of our collective security. Thus, a country that is unable to control its own trade policy will find itself not only less able to influence global developments but more likely to be shaped by them.

It has become clear to me in recent days that there is some confusion about what a customs union is, and how it works. A customs union comes about when a group of countries decide to abolish tariffs between them and to have a common external tariff. Importantly, a customs union covers only goods, it does not cover trade in services. The EU has full customs unions with San Marino and Andorra and a partial customs union with Turkey covering mainly industrial goods but excluding coal, steel and agriculture.

As there is a common external tariff among members of a customs union, countries cannot unilaterally lower tariffs for another country, they can only act as a bloc. This means that the UK is obliged to implement the EU's Common Customs Tariff (CTT) which, according to EU Treaty law, is decided by the institutions of the European Union.

Sir Graham Brady MP



I pointed out to the meeting that a customs union between the UK (as a third country) and the EU is not a meeting of equals and is different from the customs union in which we currently participate – the latter being reserved for those countries in the EU only. A customs union, where the UK was obliged to implement the CTT would allow the European Union to negotiate access to UK markets as part of EU trade policy, irrespective of the interests or wishes of the United Kingdom i.e. it will be able to offer access to the world's fifth biggest market as part of any EU offer, without the need to balance this access by negotiating on key UK offensive interests.

This is possible because the UK as a non-EU Member State would have no say under EU treaty law for the formation and agreement of EU trade policy. We would be stuck in the worst of both worlds, not only unable to set our own international trade policy, but subject, without representation, to the policy of an entity over which MPs would have no democratic control. This is something that Labour do not presently seem to understand. As I said at the meeting, in such a scenario the UK would have a new role in the global trading system – we ourselves would be traded. As the famous saying in Brussels goes, if you are not at the table, you are on the menu.

Some have argued that, irrespective of the democratic arguments that we would in a customs union with the EU still be able to negotiate ambitious deep and comprehensive free trade agreements with partners around the world. However, it is worth noting not only that we would have to apply the CCT with third countries, but that countries who negotiate free-trade agreements (FTAs) with the EU would have automatic access to the UK market with the UK having no reciprocal access, unless a new agreement was bilaterally negotiated. The key question is that if a trading partner already had access to the UK for no cost, why would it be interested in negotiating a further bilateral agreement?

I gave the example of Turkey as a country which has a partial customs union with the EU. Given that those countries with which the EU has a trade agreement, already have access to Turkey's market for those goods covered by the customs union, there is little incentive for any third country to negotiate a trade agreement with Turkey. To date, Turkey's trade agreements are largely with those countries where EU Association Agreements already exist. Moreover, given that Turkey is required to subscribe to the EU's Common Commercial Policy – or the EU's trade policy – this limits what, if anything, it can offer in return for preferential access to third country markets.

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In the recent TTIP negotiations many in Turkey were outraged that the EU was able to negotiate access for US automobiles into the Turkish market, but Turkey was unable to gain reciprocal access to the US market. Compare this situation with the fact that the UK is the fifth biggest economy in the world.

Furthermore, a customs union will stymie the UK's ability to open markets around the world to the UK's services sectors – as an 80 per cent services economy, this is a huge area of comparative advantage to the UK. In fact, one of the main aims of UK trade policy is to achieve liberalisation in global services. As the current plurilateral agreement – the Trade in Services Agreement (TiSA) is stalled in Geneva, we are likely to have to increase service access by bilateral agreements. As the UK service sector is itself extremely open, the only way in which we are able to negotiate access to other countries services markets is by allowing increased access to our goods markets. An inability to set our own tariff rates would make this extremely difficult if not impossible, foreclosing opportunities for the UK's world class services exporters to gain access to new and profitable markets.

Similarly, some have claimed that joining a customs union would gain automatic access to 87 EU agreements. Leaving aside the fact that I do not recognise the number of trade agreements mentioned, there would be no automatic continuity for EU trade agreements if we left the EU and join the customs union. Membership of EU trade agreements are part of being a member of the EU, subject to the Treaties of the Functioning of the European Union, outside of those treaties – therefore outside of the EU – but in a customs union, does not give you access to these agreements. In fact, all of these agreements would need to be negotiated again.

I have also heard colleagues and commentators suggest that Japan would be a great prize in a customs union. However, only EU Member States have access to EU trade agreements. So, if the UK were to join a customs union with the EU, we would still need to negotiate a bilateral agreement to secure UK access to the Japanese market. However, as already noted, given that the Japanese would already have secured goods access to the UK through its agreement with the EU, there is no guarantee that Japan would seek to negotiate such a new agreement with the UK.

A customs union would also potentially damage Britain in international trade disputes. For example, the EU produced countermeasures following the recent US application of steel and aluminium tariffs. This followed lengthy consultations with the Member States.

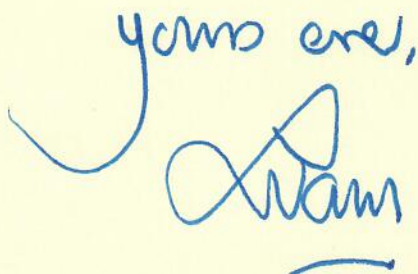
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Were the UK to be a third country, outside the EU but in a customs union, it is entirely possible that the EU could apply tariffs on products important for the UK, but not for other EU Member States. As Britain would have to apply such tariffs as the price of its membership of a customs union, without a say in their formulation, British businesses and consumers could find themselves on the front line of trade disputes while EU members could be more protected.

I mentioned that the application of the CCT could have complications beyond trade policy itself. This Conservative government has been keen to look at ways of bringing our trade and development policies closer together and one of the ways in which we can do this is to use our new found tariff freedom, when we leave the EU, to stimulate trade with countries who currently face tariffs when they add value to their primary produce. A combination of outward direct investment and judicious tariff reduction would go a long way to securing our aim of helping countries to trade their way out of poverty. If we were to remain in a custom union, we would have to apply the EU's trade policy for developing countries, without any say. This could have important implications for the UK's relationship with developing countries, should the EU decide to take an action prejudicial to our interests.

Finally, it is worth saying a word about the government's proposals contained in the Political Declaration. Essentially, the government is seeking to maintain the benefits of a customs union in terms of internal trade (tariffs, quotas and rules of origin) while being outside the EU's common external tariff. This would allow the UK to have an independent trade policy. Such a proposal has never been implemented to my knowledge but being outside the CCT is an absolute prerequisite to Britain being able to benefit from ambitious UK trade and development policies.

Yours ever,  
A handwritten signature in blue ink, appearing to read 'Graham Brady', with a flourish underneath.

Sir Graham Brady MP  
House of Commons  
Westminster  
London  
SW1A 0AA