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Brexit, Movement of Goods and the Supply Chain

by Shanker A. Singham and Victoria Hewson

PROMOTING POLICIES THAT LIFT PEOPLE FROM POVERTY TO PROSPERITY

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With contributions from:

Keith Hobson and **George Kelly**,
iTax UK

Steve Holloway, Corporate
Counsel IOR Global, former official
Australian Customs Service

Tate & Lyle Sugars

Lorand Bartels, Reader in
International Law; Fellow, Director
of Studies and Graduate Tutor,
Trinity Hall, University of Cambridge

Sandy Moroz and **Colleen Brock**,
former customs and rules of origin
negotiators for the Government of
Canada in NAFTA

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1. INTRODUCTION

- 1.1 Handled well, Brexit could be a huge opportunity for the British people. In her speech at Lancaster House, Prime Minister Theresa May referred to it as a prize. However, in order for this vision to be realised, we will need to make sure as the UK exits the EU, it does not unwittingly take any of this prize off the table. The UK government should therefore hold to the following operating pillars of the Brexit negotiation:
 - 1.1.1 **To negotiate trade deals with other countries, we must be fully outside the customs union.** The language we use must be clear enough that trading partners understand that the UK will be ready to sign a trade deal immediately on departure from the EU. If trading partners think this might be extended for an additional two years after exit, they will focus on other agreements with other parties.
 - 1.1.2 **To negotiate on services, a key UK export, we must be able to put our domestic regulation on the table, so we must be out of the single market.**
 - 1.1.3 **To secure trade deals, we must be prepared to be more open on agriculture (as this is the sector that is of key interest to most of our trading partners).**
- 1.2 We believe that the component parts of a successful Brexit include:
 - 1.2.1 a 'Prosperity Zone' consisting of a group of like-minded countries which agree to a massive reduction of trade barriers, behind the border barriers and economic distortions. Members might include US, Canada, Singapore, Australia, New Zealand, Mexico and Switzerland;
 - 1.2.2 bilateral Agreements between the UK and a series of major trading partners such as India and China;
 - 1.2.3 economic partnership agreements with developing countries (primarily in Africa, Caribbean and the Pacific region, so-called ACP countries) that are true economic partnerships involving access for their agricultural products, an end to tariff escalation and reduction of tariffs to advanced manufacturing as well as regulatory reform in these countries, which such countries often need to do but are prevented from doing because of powerful vested interest groups; and
 - 1.2.4 a productivity and consumer welfare agenda in the UK that leads to a reduction of distortions at home and policies that use free trade and free markets to lower key costs such as food and energy.
- 1.3 Achievement of these policy goals could lead to an injection of at least 2-3% into global world product, creating the economic engine that the world currently lacks. They cannot be achieved, however, if the UK stays within the EU customs union or retains membership of the single market, by way of the European Economic Area or otherwise.¹

- 1.4 Leaving the customs union and the single market could entail significant changes to the processes around movement of goods between the UK and the EU and vice versa. In this paper we explore what those changes could be, from the position of the Common External Tariff applying to UK exports to the EU and the same tariffs being applied reciprocally by the UK to imports from the EU, and from the preferred position of both sides agreeing to retain tariff and quota free trade in goods. The position of access to services is not addressed in this paper.
- 1.5 The import and export of goods between the EU and third countries involves customs clearance and conformity assessment. As a member of the single market and customs union, exports from the UK are not currently subject to customs clearance, as no import duties are payable and the conformity of goods with the applicable legal requirements is assumed as the UK is subject to the same harmonised requirements that apply throughout the EU.
- 1.6 Supply chains in manufacturing and sale of goods are highly integrated as a result, and it could be costly for businesses on both sides of the channel and across the Irish border if duties become payable and logistical and administrative barriers come into operation. We have therefore examined the existing processes for importing goods from third countries to the EU which would apply if no bespoke agreement were reached, and the enhanced processes that would be available going forward, based on best practice at the borders of other closely linked trading nations.

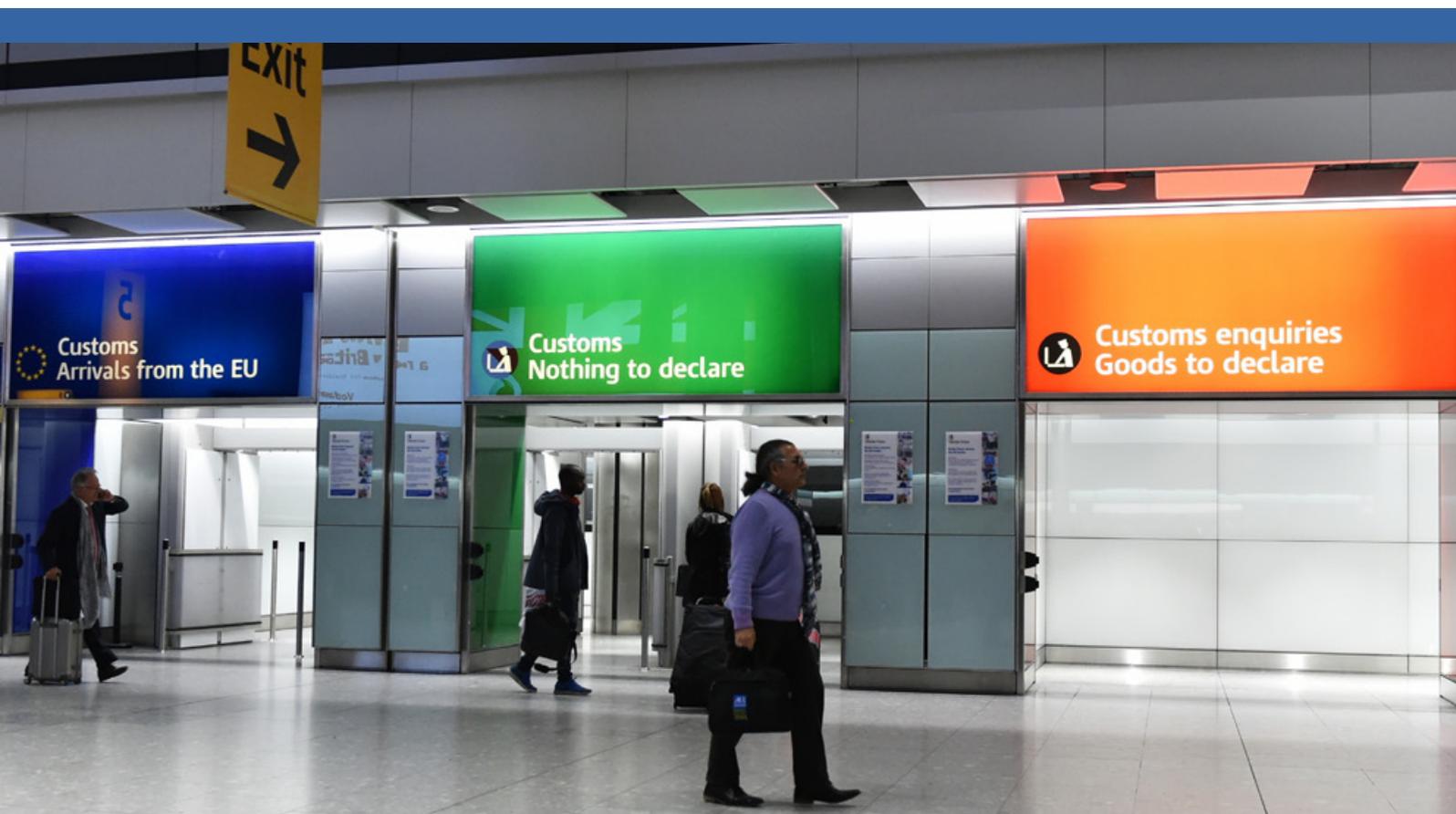
2. EXECUTIVE SUMMARY

- 2.1 The optimal outcome of the negotiation process pursuant to Article 50 TEU in respect of tariffs on trade between the UK and the EU would be a full free trade agreement (FTA). This would deal not only with tariffs and quotas but with all trade, services and investment matters, including customs cooperation and trade facilitation. If this cannot be agreed, either due to differences between the parties or because of the expiry of the two-year negotiation period before terms can be concluded, the UK should offer an agreement that tariffs and quotas will not be applied by either side, as part of the framework for the future relationship, on an interim basis for a limited period with a view to a FTA.
- 2.2 If the EU will not agree to this, it is still possible for the UK to remain competitive and lower the overall cost of manufacturing here by reducing tariffs on imports and benefiting from the depreciation in the value of sterling, for as long as the current exchange rate persists. The shape of such tariff reductions needs careful consideration, as unilateral tariff reductions must be extended to all WTO members under the WTO's MFN rule. We have set out some of the factors to be taken into account and work is continuing to model the likely outcomes of a range of options.
- 2.3 Whether or not tariffs are imposed, the introduction of customs formalities will lead to disruption and additional costs for importers and exporters. However, customs procedures across the UK and member states are highly efficient and mutual recognition of trusted traders under existing schemes and continued close co-operation should ensure that costs and administrative burdens are minimised. The availability of reliefs from payment of duty on materials that are imported for processing then re-exported or are only in transit through a country mean that supply chains will be protected from cumulative duties on components that cross borders multiple times.
- 2.4 Even if tariff free trade is agreed, rules of origin will be applied, which also entail costs to manufacturers. The EU's default rules are relatively liberal, and there are other examples in free trade agreements, including where the EU is a party, where more flexible rules have been agreed. Processes also exist for exporters to self-certify origin and agreeing these and ensuring as many businesses as possible sign up to them should be a priority. Traders may need an interim period to adjust their supply chains and be able to satisfy and certify origin requirements, during which rules of origin should be waived, subject to the UK and the EU maintaining the Common External Tariff on imports from the rest of the world.
- 2.5 HMRC will need to be resourced to deal with the increase in customs activity and should run a programme to raise awareness among businesses who currently trade with EU countries and not outside of the customs union. If it is agreed that tariffs will not apply this will be more straightforward as it will not include payments and applications for reliefs.

- 2.6 Product conformity assessment can be done by manufacturers of goods even where they are outside of the EU, except in respect of certain products where certification by an authorised body is required. In such cases, the EU has mutual recognition agreements with a number of third countries permitting bodies in those countries to assess and certify those goods, and mutual recognition of assessment bodies between the UK and EU should be sought. Membership of standards bodies CEN, CENELEC and ETSI and global regulators such as UNECE is open to non-EU members and the UK should continue its participation.
- 2.7 Close trading partners such as the USA and Canada and Australia and New Zealand, as well as European neighbours such as Switzerland and Norway operate efficient borders to facilitate trade without being in a customs union. Contributors from Australia and Canada have summarised their respective regimes.
- 2.8 Interim measures such as extended membership of the customs union or a transitional arrangement to facilitate customs clearance for a short period of time (no more than one year, to ensure that opportunities with third countries are not lost) to ensure that customs IT systems and personnel are ready and businesses have been able to adapt to rules of origin and other formalities may be required. Ultimately these matters should be covered in a trade facilitation chapter of a free trade agreement.

3. LEAVING THE CUSTOMS UNION

- 3.1 Assuming that it is recognised that continued membership of the single market and the customs union is incompatible with the main aims of Brexit, including restrictions on the free movement of labour, the optimal outcome of the withdrawal from the EU would be a comprehensive free trade agreement between the UK and the EU. The UK should include an offer to conclude an FTA in its Article 50 notice. However, in light of the difficulties from political and practical perspective in concluding such an agreement within the 2 year negotiation period under Article 50, the UK government may need to decide between a range of other possible outcomes.
- 3.2 In the absence of a full FTA, it is still possible to agree tariff free trade on an interim basis for a limited time period² (which would remove the base cost, as well as the administration attached to the payment of import duties and any associated duty relief schemes that either side may elect to operate) and high levels of mutual recognition of product standards and conformity certification. This “zero for zero” offer should be included as an offer that will remain open even if a full FTA cannot be agreed by the Exit Date, to apply on an interim basis until the FTA can be concluded. This would be consistent with the commitment made by the EU at the G20 2016 summit in China to operate “standstill and roll back” of tariffs.³ It is also in line with the treaty requirement in Article 8 of the Treaty on European Union to “develop a special relationship with neighbouring countries, aiming to establish an area of prosperity and good neighbourliness, founded on the values of the Union and characterised by close and peaceful relations based on cooperation”.
- 3.3 Even if this offer is not accepted, with or without tariffs and quotas, existing trade facilitation under the EU’s suite of legislative measures on product compliance and customs requirements is intended to enable efficient customs clearance and importation of goods from third countries. EU customs processes are currently being modernised and new systems and processes which are intended to improve consistency and efficiency are due to be in place during 2018. The UK will be implementing these changes and should be in a position to extend existing customs procedures that apply to the rest of the world to EU imports as part of that programme. The challenge will be ensuring that the HMRC customs IT system, which is in the process of being replaced, will have its capacity increased to deal with the increased volumes of goods that will require clearance.
- 3.4 The EU has also agreed bi-lateral measures with third countries to further simplify the processes, for example sectoral Mutual Recognition Agreements (“MRAs”) with a number of countries and trade facilitation chapters in FTAs like the Comprehensive Economic and Trade Agreement recently concluded between the EU and Canada (“CETA”). As the UK is currently subject to identical regulation to that which pertains in the EU and there are high levels of trust between businesses and authorities on both sides, mutual recognition of assessment and certification bodies and streamlined processes for customs clearance should be established.



The UK should also look to replicate the MRAs with third countries to apply to trade between the UK and the third country. As with the FTAs that the UK currently benefits from as a member of the EU, in the first instance the UK should look to carry these agreements over by way of an exchange of notes whereby both sides agree to continue the current arrangement on a bi-lateral basis.

- 3.5 As well as the gains to be made in international trade by way of FTAs, exiting the Customs Union enables policies that could support an industrial strategy aimed at supporting manufacturing businesses, by reducing and/or eliminating tariffs on imports of components, entering into MRAs for conformity assessment and streamlining customs processes, and establishing freeports⁴ (also referred to as free zones) to stimulate manufacturing in target locations. These trade-related measures would run alongside broader domestic pro-competitive measures such as lowering energy costs, and moving away from the precautionary principle in regulatory promulgation. Having full control of VAT will also give more flexibility around industrial policy options, and could make freeports a more attractive solution than they currently are.

Above: Customs channels at Heathrow Airport. The UK's main aviation hub is the busiest airport in Europe by passenger traffic.

- 3.6 The alternative of the UK staying in the customs union, which has been called for in some quarters,⁵ is, we submit, not desirable or viable. Remaining part of the EU customs territory would sacrifice the UK's ability to negotiate agreements with other customs territories in respect of tariffs, quotas, etc., which would otherwise be a key benefit to leaving the EU leading to lower prices for consumers within the UK and opening up markets for UK exporters of goods and services. The association agreement between Turkey and the EU, under which Turkey joined the EU customs union for industrial products (which comprise around 95% of the trade between the EU and Turkey⁶), has been cited as an example of how the UK could stay within the EU Customs Union. By definition, as part of a customs union the parties must have the same external tariff, and the Turkey precedent suggests that the EU would be likely to require continued harmonisation of law and regulation in respect of relevant products. Decision 1/95 of the EC Turkey Association Council required Turkey to sign up to the internal market rules of the EU relevant to the products falling within the customs union. If the UK were to agree to this, it would not be able to agree bi-lateral FTAs with third countries as it would not be able to agree tariff reduction or elimination. The likelihood of the EU agreeing to this without a significant budgetary contribution and free movement of people is very low, in any event.
- 3.7 It has been suggested that a partial customs union to cover particular vulnerable sectors, such as automotive, could be established that would enable the UK to pursue FTAs to cover all other sectors, but this would contravene Article XXIV of the GATT which requires FTAs and customs unions to be in respect of substantially all trade between the parties,⁷ so both the EU-UK sectoral customs union and any UK-third country FTA that excluded specific sectors would be in breach of the GATT. Article XXIV allows for duties and other "regulations of commerce" to take effect on an interim basis between parties in contemplation of an FTA, as long as they only subsist for a reasonable time under a plan and schedule.⁸ A legal opinion on this issue is included as Appendix 1.
- 3.8 Article XXIV also prohibits duties and regulations of commerce adopted pursuant to an FTA, or interim agreement in anticipation of an FTA, with respect to parties outside of the FTA from being higher or more restrictive than those in existence before the FTA or interim agreement. If a zero for zero arrangement on tariffs is not agreed there could be an argument that this will indirectly lead to duties and regulations applying on trade with third countries who were importing to and trading between the UK and the EU before the Exit Date Irrespective of whether a legacy agreement in the name of the EU could apply directly to the UK, agreeing zero for zero on tariffs removes the risk of a third country bringing a case in the WTO for an adjustment or compensation as a result of the introduction of tariffs and other barriers.
- 3.9 If zero for zero is not agreed, this would affect not only trade between the EU and the UK, but also both sides' trade with third countries as businesses across the EU and UK seek to mitigate their overall costs and tariff burdens by sourcing products from within their own territories ("substitution"), and as a general result of the increase in costs from the imposition of tariffs and other barriers. This could lead to other countries claiming that their benefits under the GATT with respect to trade with the EU and the UK have been nullified or impaired as the deal that they agreed to with the EU and member states was with respect to a free-trading bloc. Such a case can be made out pursuant to Article XXII of the GATT and is known

as a non-violation nullification and impairment (“NVNI”) claim. While these claims are rare, and usually brought alongside other claims (as was done in *Japan: Measures Affecting Photographic Film and Paper* (DS44, 1998)), such a claim can be brought by an affected country whose supply chains have been adversely affected such as the Japanese. Unless the EU and UK agree measures that have no impact on trade more widely there is a risk that countries that are large exporters to both territories will claim that, although there has been no direct violation of the GATT, the application of tariffs and barriers has deprived them of some of the benefits that had accrued to that country have been nullified or impaired. This could lead to both claims for compensation to reflect the loss of benefits and retaliatory measures. Clearly the EU member states and institutions and the UK will wish to avoid this and the most certain way to do so is to maintain tariff free trade with the fewest barriers possible.⁹

- 3.10 It is possible for the UK government to seek the support of countries that would be adversely affected in order to highlight to the European Commission that cases might be brought, and could easily be avoided if zero for zero is agreed at an early stage in the negotiations, ideally as an early harvest measure. We understand that the European Commission is likely to favour a ‘single undertaking’ approach, where nothing is agreed until everything is agreed. This would make early harvest measures difficult to secure.

4. TARIFF AND DUTIES

- 4.1 The impact of tariffs on UK exports is not limited to potential duties imposed on goods exported to the EU market. At present, the fall in the value of the pound against the euro would off-set some, if not all, of the impact of tariffs, were they to be imposed, as exporters may lower their prices to absorb them without impacting on the cost to the final consumer. Clearly this in turn will be offset by the increase in the cost of imported parts and materials and there are also compliance and administration costs to be considered.¹⁰
- 4.2 As set out above, the preferred outcome is tariff free trade between the UK and the EU either under an FTA or an interim "zero for zero" agreement (Scenario 1). If the EU does not agree zero-for-zero on tariffs as part of an FTA or otherwise, the UK will have the right to apply the same tariffs to imports to the EU as it applies to the rest of the world. The UK government has already indicated that it will seek to replicate existing obligations as far as possible¹¹ which in practice means that at least at the outset, the tariffs will be the same as the EU's common external tariff. Under WTO rules, unless the UK agrees a free trade arrangement, even on an interim basis, with the EU it will be obliged to apply the same tariffs to the EU and all other countries. In terms of the application of tariffs and quotas from the Exit Date there are therefore four broad outcomes:
- 4.2.1 **Outcome 1**—the EU and UK agree not to apply tariffs and quotas to trade between them, either on a permanent basis under an FTA or interim basis;
- 4.2.2 **Outcome 2**—no FTA is agreed and the EU rejects the zero for zero offer. The UK elects to apply the common external tariff to imports from the EU. This would have adverse impacts on trade and consumer prices, and revenues from tariffs would not compensate the Treasury for losses from the reductions in economic activity, but would retain the UK's leverage for negotiating its tariffs down in free trade agreements with key supplier countries, so could yield longer term benefits;
- 4.2.3 **Outcome 3**—no FTA is agreed and the EU rejects the zero for zero offer. The UK elects to eliminate tariffs on industrial goods, but retain the common external tariff and quotas on agriculture, other than, perhaps goods that the UK does not produce or compete with. This would mitigate the trade and price impact of tariffs and off-set the impact of tariffs on exports to the EU by reducing the cost of inputs, while retaining agricultural tariffs and quotas which both maintains the UK's leverage to negotiate them down in return for concessions from FTA partners (where in many cases agricultural access represents the key interest) and enables a managed reorganisation of the UK's approach to supporting farmers and food production. It would also increase the competition to which UK manufacturers are subject, but in many cases they are already competitive at world prices (for example over 40% of motor vehicles made in the UK are exported outside of the EU¹²); and

- 4.2.4 **Outcome 4**—no FTA is agreed and the EU rejects the zero for zero offer. The UK elects to unilaterally eliminate tariffs on imports of both agricultural and industrial goods. This would bring substantial trade and welfare benefits to the UK economy, but both reduces leverage in negotiations with third countries of the ability to reduce tariffs and eliminate quotas and cause significant disruption to UK agriculture and foods producers without allowing any time for adjustment and transitional support.
- 4.3 The Legatum Institute Special Trade Commission is continuing work to model the economic impacts of each in detail in order to arrive at a recommendation of which of Outcomes 2—4 would be preferable if Outcome 1 cannot be achieved. The table below summarises some of the pros and cons of each indicated by analysis to date:

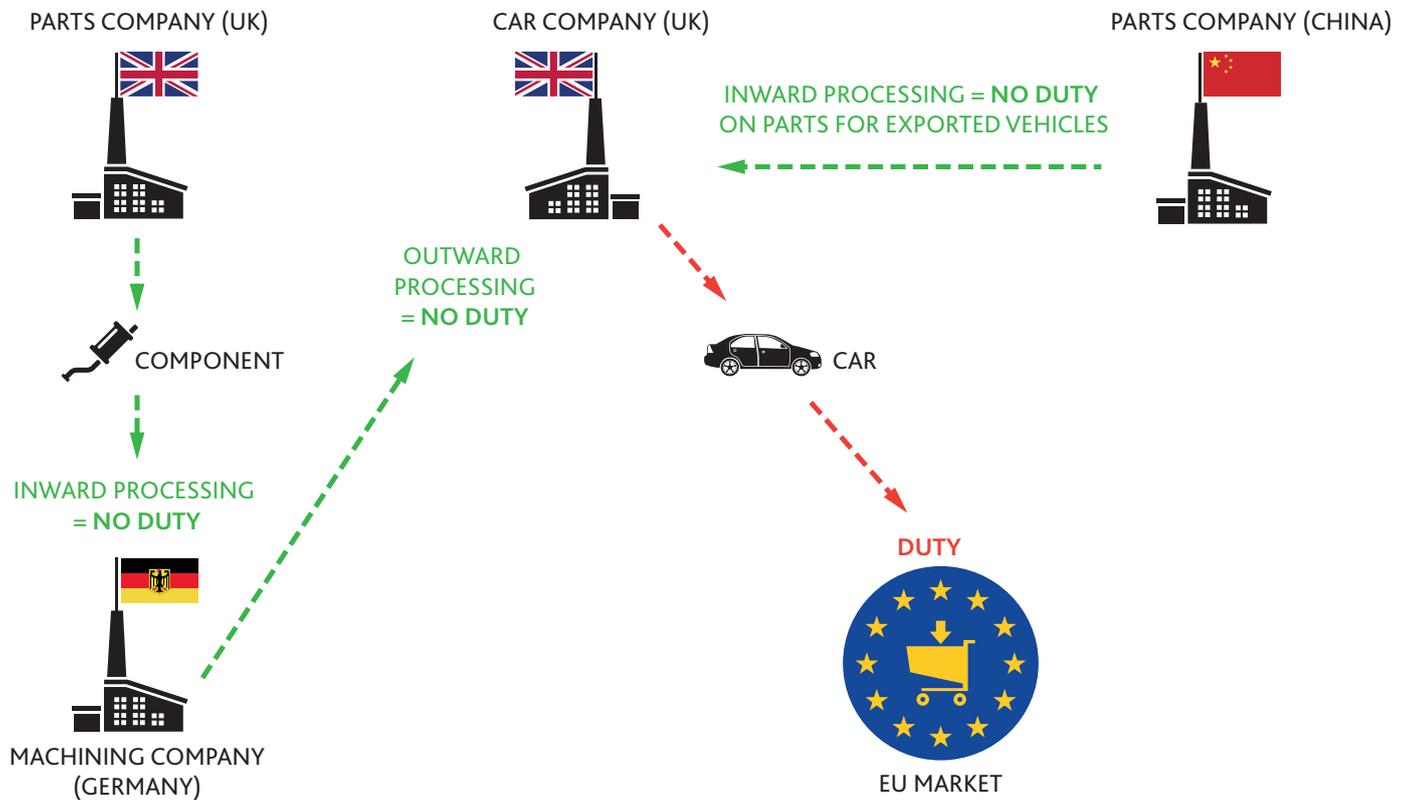
| OUTCOME | POSITIVES | NEGATIVES |
|---------|--|--|
| 1 | Maintains current tariff and quota free trade. Minimises disruption to supply chains. Increases leverage with third countries | None as against the status quo. Maintenance of the Common External Tariff against third countries has adverse effects on consumer welfare and CPI, as against other outcomes. |
| 2 | Retention of leverage with third countries. HMRC tariff revenues. | Adverse consumer welfare impact and CPI increases in particular while the low valuation of the pound persists. Disruption to supply chains and EU and UK manufacturers and consumers substitute products. |
| 3 | Partially mitigates consumer welfare disbenefit and CPI increases. Retains some leverage for tariff reduction in FTAs with third countries where agriculture access is key interest. | Food prices will still be subject to tariffs on imports from EU with an adverse consumer welfare impact as food process increase, in particular while the low valuation of the pound persists. Disruption to supply chains and EU and UK manufacturers and consumers substitute products. |
| 4 | Substantial consumer welfare benefit and CPI reduction. Manufacturing revenues to increase in the short term at current exchange rates, flattening out in the longer term as Sterling recovers its value. | Loss of leverage in negotiations with third countries, delaying or foregoing opportunities for Prosperity Zone and services liberalisation, including bi-lateral agreements with ACP countries because of preference erosion. |

- 4.4 Outcomes 3 and 4 would also have knock-on effects for supplier countries who would be exposed to full global competition for UK markets, in particular developing countries that would expect preferential access under the Generalised System of Preferences and existing FTA partners who may wish to carry over their agreements with the EU to the UK. The UK would need to mitigate preference erosion that would impact ACP countries. The leverage to secure real economic partnership agreements with ACP countries, referred to in section 1.2.3 would also be lost, which could diminish the likelihood of structured reform in those countries.

- 4.5 The import duties that would be payable on imports of goods from the UK to the EU based on current trade has been estimated at £5.2 billion. By the same measure, UK revenues from import duties on imports from the EU, have been estimated at £12.9 billion.¹³ These figures would be unlikely to be delivered in reality, as buying patterns change to reflect the tariffs (as they are designed to do). UK customs revenues would still be significant and it has been argued that they could be invested in general business and productivity support, to mitigate the additional cost of tariffs and customs compliance and lower the total cost of manufacturing borne by UK manufacturers, (for example by way of tax cuts and investing in local infrastructure development) which would mitigate any sourcing substitution. In reality, the commercial and welfare costs of the application of tariffs on imports from the EU (which are ultimately borne by consumers in higher prices, especially in the high tariff products such as food) and the GDP impact to the wider economy far outweigh the benefits that could be delivered by government using tariff revenues.

5. MITIGATING THE IMPACT OF TARIFFS

- 5.1 Focussing specifically on pan-EU supply chains, many goods are tariff free, for example most electronic components, and were tariffs to apply on imports to the EU from the UK, they would average at 4.3%,¹⁴ although there are certain classes of goods, such as motor vehicles at 9.6%, shoes at 8-18% and agricultural and food products, where tariffs vary significantly by product but can go over 100%. Due to cross-border supply chains, which are common across all sectors of manufacturing, if tariffs are applied on imports to the EU from the UK, and vice versa, it has been suggested¹⁵ that many manufacturers would have to pay import duties on the parts they import, which are ultimately exported as part of manufactured goods. These assertions misunderstand the legal position as it stands.
- 5.2 For example, currently the EU's common external tariff (which we will assume for the purposes of this section that the UK would adopt if the EU imposed tariffs on imports from the UK) on some car parts, is 4.5%.¹⁶
- 5.3 Under existing EU customs law, which again we will assume the UK will substantially adopt, at least in the immediate term after the Exit Date, trade facilitation procedures to suspend import duties on imported parts, where the end product is then exported, are available and widely used. It should also be noted that, even if the UK agrees a WTO *bound*, or *capped*, rate of, say, 4.5% for automotive parts as part of its independent GATT schedules, it can still choose to apply lower or no tariffs as the *applied* rate.
- 5.4 There are a number of mechanisms by which liability for import duties in respect of materials/components can be reduced or eliminated, where some or all of the final goods are exported, or where the parts themselves are simply processed and re-exported without entering the market in the import territory. The Union Customs Code¹⁷ ("UCC") provides for a number of mechanisms for relief from import duties when goods enter the customs union.¹⁸ For example Inward Processing Relief¹⁹ ("IPR") suspends liability for import duties on imports of materials from outside of the customs union for processing operations where those same materials are then re-exported out of the customs union. Using the "equivalence" procedure, duty relief can be claimed on identical home-produced goods where they come from multiple sources. Such processing includes working and assembling goods, and repair/restoration. Some of the permitted processing can be minor in nature but still attract the relief. Similarly, the "outward processing" procedure²⁰ applies to give relief from import duty on goods imported from outside of the customs union that are produced from goods previously exported from the customs union.
- 5.5 The following diagram (p14) shows where reliefs and duties would apply in an example of an automotive part manufactured in the UK, shipped to Germany for processing then returned to the UK for assembly into a vehicle which is exported to the EU, or imported from China and assembled into a vehicle that is exported to the EU.



Above: Example of where reliefs and duties would apply.

- 5.6 There are also duty reliefs in respect of temporary admission, specific end uses (such as qualifying aircraft parts), storage (in a customs warehouse or free zone) and transit through the EU. All of these can be retained to operate in mirror image in respect of imports to the UK from the EU, as they currently apply to imports from the rest of the world to the UK as a member of the customs union. Often, these reliefs give a cash flow benefit to the importer even if duty is payable on release to free circulation.
- 5.7 Inward and outward processing relief, specific end uses and temporary admission are subject to prior authorisation by the relevant member state customs authority (which in the UK is HMRC, which would remain responsible for enforcing and overseeing the operation of the UK Customs Code after the Exit Date, without ultimate recourse to the CJEU) which requires a proven economic need, amongst other conditions. These reliefs are also subject to an “economic conditions” test²¹ where certain goods are imported.²² These “sensitive goods”²³ are

mainly agricultural goods and alcohol. Where the imported goods are sensitive goods, there are a number of criteria that can be applied for the economic conditions to be deemed to be fulfilled. IPR is commonly used by importers of goods to the customs union at present. The UK can replicate this for processing operations in the UK and operators in the supply chain in the EU can use it to obtain relief where parts are imported, processed and shipped back to the UK, or for onward sale outside the EU.

- 5.8 Therefore even without agreeing tariff free trade between the UK and the EU (or if tariffs are imposed by the EU only), subject to the issues outlined in section 8 (*Practicalities of Customs Clearance*) the viability of supply chains that involve processing and transit of components between the UK and the EU need not be impacted by the imposition of tariffs as no import duties need accrue where goods are moved around supply chains between the UK and the EU in this way. In fact, it is possible that the overall tariff burden on UK manufacturers could be reduced by the ability of the UK to roll back tariffs on imports of parts and the availability of IPR where end products are exported to the EU.
- 5.9 This is consistent with the WTO Agreement on Subsidies and Countervailing Measures,²⁴ which permits schemes that allow for the remission or drawback (i.e. refund of duty already paid) of import charges levied on inputs that are consumed in the production of an exported product. Inputs consumed in the production process are parts that are physically incorporated and energy, fuels, oil and catalysts which are consumed in the course of their use to obtain the exported product. The amount paid by way of drawback cannot exceed the import charges actually levied on the inputs or they may constitute an export subsidy. FTAs also sometimes include restrictions or prohibitions on duty suspension and drawback on materials for goods that ultimately benefit from preference under that FTA, for example CETA Article 2.5 does this. See the Legal Opinion in the Appendix for analysis on both of these issues.
- 5.10 The availability of relief and drawback described above, and the trade facilitation measures available to operators outside of the customs union described in section 8 (*Practicalities of Customs Clearance*), means that the burden of staying within the customs union would be disproportionate (both in terms of sovereignty and trade/economic losses) to the relative impact of the imposition of tariffs and customs clearance requirements.
- 5.11 Businesses that already trade outside of the customs union will already be operating under some of these measures and will be familiar with the processes required for customs declarations and applying for reliefs. There is a cost and risk attached to extending these to trade with the EU, which is currently the source of 54% of UK imports and destination of 46% of UK exports by value (although this latter proportion has been decreasing for some time now), and the government will need to invest in systems and training to mitigate these additional costs for affected businesses.²⁵ HMRC will also need to consider how to approach enforcement of customs compliance on businesses post-Brexit, as there could be a significant increase in customs debts and non-compliance, which will need to be handled sensitively to avoid bad publicity that could deter businesses from trading internationally. It is worth noting that HMRC usually approach the administration of such major changes with a transitional “light touch” regime, and publicise this accordingly.

- 5.12 Only around 8—11% of UK businesses are thought to export to the EU,²⁶ and, in order to ensure that any industrial strategy is properly calibrated, work will be required to identify which sectors and industries are likely to be most adversely affected by the imposition of tariffs based on how price sensitive and competitive the market for those goods is and how high the tariffs would be if the Common External Tariff were to be applied.²⁷ This would not address the impact on consumers and businesses of higher prices and the distortive effect that the imposition of tariffs would have on trade across the economy so another solution will be required.
- 5.13 In order to be WTO compliant such measures must not violate the WTO's provisions on national treatment, and also not be regarded as an illegal export subsidy under the WTO Agreement on Subsidies and Countervailing Measures (the "Subsidies Agreement"). This means (other than in relation to agriculture, which has specific rules) they must not constitute a payment or other benefit that is contingent upon export performance or on the use of domestic goods over imports.²⁸
- 5.14 It is possible that any such mechanism could violate the Subsidies Agreement. If the EU, or any other WTO member considered that this was the case, they could use the remedies process under the Subsidies Agreement²⁹ which could lead to consultations, WTO dispute settlement and panel proceedings, and finally Appellate Body dispute resolution. This would likely take several years, after which time, in the worst case scenario, the UK would be required to discontinue the measure (which could be done without causing damage to exporters who were relying on the measures if there has been an FTA with the EU by that time), or face countermeasures from the EU or whichever member had complained.

6. RULES OF ORIGIN

- 6.1 Notwithstanding the above, the optimal outcome from the exit negotiation with respect to tariffs would of course be that the parties would agree not to apply any tariffs on trade between the UK and the EU. This could be agreed on at least an interim basis as part of the agreement concluded pursuant to Article 50 TEU (the “Withdrawal Agreement”), even if long term FTA terms cannot be agreed during the two year negotiation period pursuant to Article 50 TEU. As the UK would no longer be bound to the Common External Tariff, this would entail the operation of rules of origin (“RoO”). Rules of origin also apply where there is no preferential arrangement, to allow collection of data for statistical purposes and with reference to quotas and trade remedies like the imposition of anti-dumping duties.
- 6.2 The EU’s current arrangement for countries not subject to preferential treatment is that products are deemed to originate in the state where they are wholly obtained or produced.³⁰ Goods whose production involved more than one country are deemed to originate where they “underwent their last substantial, economically justified processing or working in an undertaking equipped for that purpose and resulting in the manufacture of a new product or representing an important stage of manufacture”.³¹ What constitutes the “last substantial processing” is set out in a comprehensive list of goods in the Delegated Regulation.³² This is mainly focussed on goods changing from one type of good to another as part of the processing, usually resulting in a change of tariff heading under the CET. There is also a list of activities that will not constitute “substantial economically justified processing” which includes operations to preserve the condition of products in transit, simple packaging operations, affixing of marks and labels and simple assembly of parts.³³
- 6.3 Where the EU has agreed preferential measures with a country, the rules of origin that will be applied to establish whether imports from that country will benefit from the tariff reduction and elimination are set out in the relevant agreement.³⁴ Under CETA, for example, goods are deemed to originate in the EU or Canada (as applicable) (“originating products”) and therefore be tariff free in accordance with the CETA Tariff Elimination Schedule³⁵ if they were “wholly obtained” there, produced exclusively from materials that originate there or have undergone “sufficient production” there.³⁶ Sufficient production is subject to fulfilment of conditions set out in the Product Specific Rules of Origin.³⁷ Goods that do not fulfil the conditions can still be originating products if certain tolerances for non-originating content are not exceeded, for example up to 10% by value of non-originating content is permitted.³⁸
- 6.4 CETA also provides for cumulation of preferences, whereby products originating in Canada will be deemed to originate in the EU where they are used as a material to produce products in the EU, and vice versa. There is also provision, subject to agreement of applicable conditions, for the origin of goods from a third country with which both Canada and the EU have an FTA to be taken in to account in determining whether a product is an originating product for the purposes of CETA.

- 6.5 The more liberal RoO under CETA could be a starting point for what the UK should seek to apply to goods traded between the UK and the EU, if a preferential tariff free deal is agreed. Other FTAs around the world such as NAFTA and CAFTA-DR, and the terms that were agreed in TPP should also be examined to establish the optimal solution. The cumulation of preferences attaching to goods originating in each side's territory and the FTAs that the EU has, and which the UK should seek to continue to benefit from,³⁹ should also be pursued. In general, preferential trade agreements have evolved in the last twenty years towards more open frameworks that are underpinned by liberal rules of origin, whereby goods originating in a country in which either party has an FTA qualify as originating products. CAFTA-DR for example employs cumulation rules to ensure that, in particular integrated textile supply chains involving production in Mexico under NAFTA and Africa (which benefit from the Africa Growth and Opportunity Act, "AGOA") are not damaged.
- 6.6 If zero for zero is agreed on tariffs in the Withdrawal Agreement, there will also need to be RoO, even if only on an interim basis until a full FTA is agreed. The UK and EU should look to agree as liberal RoO as exist in any trade agreement today, in order to ensure that it is an open agreement that is trade creative and not trade distortive. Such an agreement would be welcomed by the UK's trading partners.
- 6.7 Proving origin, especially in cases where goods comprise a number of components or ingredients from different countries can be complex. The EU has processes in place with a view to facilitating this, for example where the goods are under a certain value or where the exporter is an approved exporter, a declaration of origin by the exporter on an invoice will be accepted as proof of origin for customs purposes.⁴⁰ Such mechanisms should be put in place and mutual recognition of the Registered Exporter mechanism which comes into force on 1.1.17 agreed. Compliance failure in respect of proof of origin requirements and the consequent adverse impact on an exporter's Registered Exporter status should facilitate a significant degree of accurate self-regulation.
- 6.8 Other ways of minimising the RoO compliance burden include for example, waiving rules of origin requirements on goods that would attract a tariff below a de minimis level of, say 5%. This was a recommendation of the Australian and New Zealand Productivity Commissions' 2012 Report into Strengthening Trans-Tasman Economic Relations.⁴¹ The Productivity Commissions noted that rules of origin are not just an administrative cost, but also entail costs in changing product specifications and sourcing of parts to qualify for preferential status, and estimates the cost of operating rules of trade between Australia and New Zealand at from 1.5 to 6% of the value of the goods, depending on the product. Clearly minimising this potential cost should be a priority for the UK and the EU in the Withdrawal Agreement.

7. PRODUCT COMPLIANCE

- 7.1 To be permitted to be placed on the market in the EU, goods must be compliant with the applicable "Union harmonisation legislation". Products coming from countries outside of the EU are entered for a procedure of release for free circulation and checking by member state authorities responsible for border controls. In line with the GATT requirements on non-discrimination, the Blue Guide affirms that "the basic principle of EU product rules is that irrespective of the origins of the products, they need to be compliant with the applicable Union harmonisation legislation if they are to be made available on the Union market. Products manufactured in the EU and products from non-EU countries are treated alike."
- 7.2 It should be noted that supply of products for further distribution, incorporation into a final product or for further processing with the aim to export the final product outside of the EU does not constitute placement on the market so such parts and unfinished goods do not have to meet the legislative requirements at the point of import. The import and re-export of such transitory goods is therefore not subject to the customs checks for product compliance and certification of conformity is not required. Such goods will still be subject to the customs notifications and declarations and any applicable duties will be payable, subject to the drawback and suspension reliefs described in section 5 (Mitigating the Impact of Tariffs and Duties).
- 7.3 In most cases, manufacturers self-certify that their products are compliant with the relevant legislation and affix the "CE" marking to confirm this. In respect of certain categories of goods, certification must be carried out by a notified body. In others still, including automotive, products must be "type certified" by a member state authority before they can be placed on the market in the EU.
- 7.4 Under the "New Approach" to product requirements, since 2008⁴² as a general rule, EU legislation will avoid going into technical detail" and express only the "essential requirements", other than where product or sector specific needs indicate that more specific regulatory solutions are required or are already in existence, such as feed and food, cosmetic products, agricultural products, medicines and chemicals.⁴³ Detailed technical standards for a range of products is also produced by recognised European Standards Organisations CEN, CENELEC, or ETS, but conformity with these standards is voluntary⁴⁴ and gives rise to a presumption of conformity with the applicable legislative requirements.
- 7.5 The person who places a product on the market under its own name or trade mark is the "manufacturer" for the purposes of EU harmonisation legislation. This is the party who is responsible for the conformity assessment of the product, and who must be in possession of the documentation and certification that demonstrate the conformity. However the assessment need not be carried out by that person and the certification need not be in their name.⁴⁵ The manufacturer is required to carry out the conformity assessment, or, where required by the applicable product regulations (which generally apply to "high risk" products like pharmaceuticals, construction components and motor vehicles and parts), have it carried

out by a third party or using an approved quality system. Such third party assessment is usually required to be carried out by a "notified body". The manufacturer is also required to carry out certain other compliance tasks such as the provision of instruction and safety information, all of which are equally as applicable to manufacturers in or outside of the EU so will be operated in practice by UK manufacturers in any event.

- 7.6 Motor vehicles are subject to "type-authorization" by a member state authority before they can be placed on the market in the EU. Once so authorised, a type-authorized vehicle must be permitted to be sold in all member states. The process for type-authorization is to be updated in a new regulation,⁴⁶ which is also intended to improve market surveillance. The UK should look to agree mutual recognition agreement ("MRA"), as Switzerland has,⁴⁷ providing for a process whereby UK authorities would be recognised for type-authorization so that existing and new authorisation would continue to be valid for marketing in the EU vehicles manufactured in the UK.
- 7.7 The key area where geographical location of manufacturers outside of the EU may have an adverse effect is where the assessment and certification is to be carried out by a notified body. Unless otherwise agreed pursuant to an MRA, a notified body must be established in the EU. The UK is home to a number of notified bodies that test and certify products manufactured in the UK and elsewhere. Unless the EU agrees that these bodies will continue to be recognised for testing and certifying conformity with EU product requirements (and the UK reciprocates recognition of EU notified bodies), alternative arrangements would need to be made to have products certified and there would also be a question over the validity of certificates already issued for products that are in ongoing production and distribution.
- 7.8 As the notified bodies in the UK and the authorities that supervise them are fully compliant with EU law, it would be sensible and viable for the EU to continue to recognise them and accept certification by them. This could be done initially under an MRA, and eventually through a comprehensive FTA. The EU has MRAs in place recognising conformity assessment bodies in Switzerland, Israel, Canada, Australia, New Zealand, Japan and the USA. The UK and EU should look to replicate this and continue to recognise certification issued by UK notified bodies.
- 7.9 Even if such recognition cannot be agreed (which seems unlikely given the strong mutual interest, and the consequences for existing certifications by UK notified bodies that attach to products of manufacturers around the world) it is still possible to have testing and certification carried out in the UK for products that are to be exported in to the EU market.⁴⁸ While it is not permitted for a notified body to be located outside of a member state, they may carry out the activities necessary to test and certify products at the location of the manufacturer. In fact, in the case of some activities such as audit, these can only be carried out at the location of the manufacturer. It is also permitted to delegate their functions to entities that are not established within the EU, provided the authority responsible for monitoring the notifying body is notified and is capable of monitoring the activities of the delegate.⁴⁹ Sub-contractors of notified bodies must be "technically competent and display independence and objectivity according to the same criteria and under the same conditions as the notified body".⁵⁰ Many UK notified bodies have offices and group companies in other member states so repapering arrangements so that the member state based body is formally providing the regulatory certification with the technical work continuing in the UK could be a viable work around if mutual recognition could not be agreed or does not cover all sectors.

- 7.10 There will be certain adjustments to the requirements that apply between UK manufacturers and their EU customers, as product legislation applies obligations on importers that would not previously have applied. These obligations are not onerous, but businesses may need to review their terms of business to reflect them.
- 7.11 A manufacturer of goods placed on the market in the EU does not need to be established in the EU but the products must meet the EU's requirements as laid down in legislation that harmonises requirements across the single market. At present, these requirements apply in the UK, and the UK could consider a commitment to retaining and keeping up to date harmonised product requirements for at least a transitional period until mutual recognition of the parties' respective conformity assessment regimes may be agreed in an FTA. In any event, even after leaving the EU the UK will still be a member of international bodies such as UNECE, Codex Alimentarius, the International Plant Protection Convention and the World Organisation for Animal Health (OIE) which promulgate standards that between them cover motor vehicles and parts, food, protection of plants from pests and trade in animals and animal products) and which the EU transposes into its product regulations in any event. The UK would have an independent voice and vote in these forums, so UK manufacturers would not be disadvantaged by a requirement to continue to comply with the requirements promulgated by them.
- 7.12 The UK could also seek to retain membership of the European Standards Organisations CEN, CENELEC (which already include non-EU and non-EEA countries as members, such as Switzerland, Turkey and Macedonia)⁵¹ and ETSI (which includes 20 non-EU countries as full members and countries from around the world as participants in some way).⁵² BSI has indicated that its ambition is to "continue to participate in the European standards system as a full member of CEN and CENELEC post-'Brexit'"⁵³ This would entail financial contributions to the budgets of such organisations, but the UK government is on the record as considering such financial contributions. The UK would only want to be a member of these Standards Organisations for an interim period so as not to tie itself to EU legislation for an indefinite time. Once an FTA has been agreed between the EU and the UK, this would include key disciplines to ensure that the EU member states do not discriminate against UK products and that appropriate MRAs and Conformity Assessments are in place.
- 7.13 Cooperation with the competent authorities with respect to "exchanging information and technical support, promoting and facilitating access to European systems and promoting activities relating to conformity assessment, market surveillance and accreditation" is specifically provided for in the regulation on requirements for accreditation and market surveillance.⁵⁴ Given the advanced level of cooperation and harmonisation that applies at present, there should be no legal or practical obstacle to agreeing ongoing cooperation when the UK is a third country. The USA and Canada, for example, operate a regulatory Compliance Council⁵⁵ covering a wide range of products including pharmaceuticals, vehicles, food and plants and environmental matters.

8. PRACTICALITIES OF CUSTOMS CLEARANCE

- 8.1 The purposes of customs reporting are the monitoring and enforcement of import and export policies such as payment of duties, enforcement and monitoring of quotas, security, sanitary and phyto-sanitary measures, treaty obligations such as CITES, anti-fraud and counterfeiting. If two territories can rely on each other's respective regulations and border controls from third countries (and especially if they also operate zero tariffs and liberal RoO) border checks can be, and are, minimal.
- 8.2 This section assumes that, in the short term, the UK will retain the existing customs regulations that it currently applies to imports from outside of the customs union. As a result of integrated systems information sharing processes already in place, and subject to further development already in train as the new UCC is fully implemented between UK and other EU member state customs authorities, the UK and the EU should be able to agree efficient trade facilitation.
- 8.3 The UCC has undergone modernisation in its latest iteration, and complies with the requirements of the WTO Trade Facilitation Agreement. Electronic submission of data in EU customs operations has been in place for many years. Operators involved in international trade are already required to register for Economic Operator Registration and Identification ("EORI") status. It is only in the most exceptional circumstances that the registration and the filing of notifications and declarations are done otherwise than electronically.⁵⁶ Customs Freight Simplified Procedures, ("CFSP") for example, allow for electronic pre-notification of freight movements and removes border "choke-points", by allowing for customs control to take place at the importers' premises. There are also benefits in prioritising and further simplifying processes for trusted businesses holding Authorised Economic Operator or "AEO" status.⁵⁷ To achieve this status, international traders must not only demonstrate satisfactory record-keeping capacity, but also physical security in terms of manufacturing processes and logistical arrangements. A key financial benefit of being an AEO is that a mandatory guarantee for potential debts under customs procedures such as IPR may be reduced or waived.⁵⁸ If such customs procedures need to be deployed more widely and in respect of greater sums, funding such a guarantee will be a material financial burden, so AEO status will become more valuable for many businesses in the UK and the EU.
- 8.4 AEO recognition is not compulsory, and at present relatively few businesses in the UK have applied for it. To date 508 UK businesses have been accepted as AEOs, compared to 5,984 in Germany, 1511 in the Netherlands and 412 in France.⁵⁹ As AEO status is a globally recognised accreditation managed by the World Customs Authority, more businesses should be encouraged to consider applying for it, with a view not only to future trade with EU countries but the global trade opportunities that the government will be pursuing. This should be a priority as applications take up to six months to process and could take longer if there is a spike in applications in the run up to the Exit Date.



- 8.5 Because the imports and exports between the EU and the UK will be subject to customs clearance if the UK leaves the customs union (whether or not tariffs are applied) the HMRC IT system will need to have its capacity expanded accordingly. The incumbent CHIEF system is already being replaced with a system known as Customs Declaration Service (“CDS”) in order to implement the changes to the UCC, due to be completed by December 2018.⁶⁰ HMRC have service levels for clearance of imports in different categories⁶¹ (in practice, we understand that the vast majority of entries are cleared automatically based on the data submitted and automated risk assessment in a matter of seconds) but submissions that do not clear the automated risk assessment process will need manual intervention, so additional staff will also be required.
- 8.6 Facilities at ports for dealing with import requiring immediate or real time customs control will need to be attended to. As customs reporting volumes in the main EU ports of entry from the UK will increase, all parties will be incentivised to cooperate to minimise disruption. The UK, France, Belgium, the Netherlands and Germany are all in the global top 10 for

Above: Shipping containers ready for loading on to a freight train for delivery to Felixstowe docks for export. Doncaster Rail Port, Yorkshire, July 2016.

trade facilitation,⁶² and in almost all EU countries, including France, Germany, Belgium and the Netherlands, the time to clear customs for imports is, on average, an hour or less,⁶³ so just-in time supply chains need not be disrupted. As noted above, customs entries are made electronically, and thus, do not produce extra physical paperwork, and supporting documentation in most cases is no different to the commercial documentation that businesses currently are required to retain to evidence VAT zero-rating status on dispatches to the rest of the EU. The costs of documentary and at-border compliance are also very low for importing to EU countries.⁶⁴ To maintain this after the Exit Date, the UK and the EU should continue recognition of EORIs and AEOs registered in each other's jurisdictions⁶⁵ and other similar measures, as well as information sharing and co-operation between authorities, which the EU commonly agrees with trading partners whether or not an FTA is in place (for example with China).⁶⁶ This should be agreed as part of the Withdrawal Agreement.

- 8.7 There will need to be a programme of information and training for traders and carriers who currently trade with EU countries and not with the rest of the world, and who therefore will not have the processes and knowledge in place to manage applications for relief and the administration around customs procedures. Once processes are in place, as noted above, the costs and timeframes for customs clearance around the EU are very efficient. Shipping agents and freight forwarders are already well placed to provide services in this area and will continue to do so as the volumes of goods requiring clearance increases. It should also be noted that businesses who export to the EU at present already need to attend to VAT and Intrastat declarations, as well as keeping full commercial transport documentation (even to the extent of ferry tickets and meal vouchers) to demonstrate physical export of goods, so the incremental burden may not be material in all cases. Further research is required into this as a priority to identify what the costs will be.
- 8.8 It should also be noted that reintroduction of customs controls between the UK and EU will enable HMRC to take more effective action against excise duty diversion fraud, which could also yield an increase in revenues to the UK government. This, and other benefits of customs controls, such as security and prevention of people trafficking will require further research.
- 8.9 Because of the technical and practical implications of introducing customs clearance implementation, the UK government should consider whether staying in the customs union in its entirety for a period of up to 12 months may be required (by the UK and the EU member states) to ensure that systems and resources are in place to deal with increased volumes undergoing clearance, and that businesses have been able to adapt to the new compliance requirements. This will be a consideration whatever the outcome with respect to an FTA or agreement on tariff free trade.
- 8.10 There are specific issues, practical and political, in connection with a customs border with the Republic of Ireland. It is possible to operate a light touch customs border where most consignments are cleared electronically without physical inspection, as is the case at present for imports to the EU from outside of the customs union.⁶⁷ The use of AEO expedited clearance mechanisms and the carrying out of physical inspections of goods and audits of traders by authorities away from the border will minimise the disruption and visibility of the border. This, together with the issues in respect of the immigration border, will be explored further in a later briefing.



CASE STUDY

9. THE TATE & LYLE EXPERIENCE

- 9.1 The procedural cost of doing business from outside the Customs Union is relatively low. Tate & Lyle Sugars are the largest EU importer of raw cane sugar, a product with one of the EU's highest bound import tariffs. In that context we are subject to a rigorous process of Customs procedures when we import raw cane sugar from outside the EU. Taking a look at the complexity and cost of our current import arrangements gives some important clues to the procedural costs of doing business outside the EU Customs Union.
- 9.2 We import cane sugar in two ways. Firstly, we import it in bulk ocean going vessels. These are vessels containing up to 40,000 tonnes of sugar which unload directly at our own private jetty in east London. Secondly, we import a much smaller volume of speciality cane sugars in containers that are imported at specialist container ports located elsewhere in the UK.

Above: The Tate and Lyle Refinery in Silvertown, London, January, 2016.

- 9.3 The cost of administering containers is generally higher per unit of product than bulk raw materials, given the smaller volumes in a container and the relatively fixed nature of the costs. To that end, we illustrate both examples below:

Example 1—Cost of Customs process for 11 containers of cane sugar imported from Mauritius on 16 November 2016 administered through a third-party external customs specialist

During November 2016 eleven 20ft containers arrived from Mauritius at London Gateway container port. Each contained approximately 21 tonnes of speciality brown cane sugars, a total of 232 tonnes of sugar.

For imports that take place at a port outside of our own refinery we employ the services of an external customs agent to manage the customs procedures. The correct shipment documents are sent to the agent in advance together with instructions for the customs process. This is done by our small in-house team of two people who manage all of our imports.

Total costs of customs procedures for these 11 containers was a fixed cost of £37.50 for the Customs Entry levied by the customs agent, a Unique Consignment Number fee of £2.13 per container (£23.43 in total), and a presentation fee of £15.50. These costs are from time to time supplemented by one-off inspection costs that are levied if a container needs to be inspected for customs purposes. These are irregular and are generally between £50 to £100 per container.

In this example our total customs cost was £76.43. This is equivalent to 33 pence per tonne of product imported, or 0.055% of the value of the product.

The value of the consignment was €165,858 in total, or £139,500 at current exchange rates. £76.43 is 0.055% of that total consignment value.

Regarding timing and delays due to customs processes, we cannot point to one example in the last ten years when an importation of containers has been held up by customs procedures. Provided the right paperwork and processes are in place the system has, for us, been seamless.

Example 2—Cost of Customs process for annual imports of bulk raw cane sugar at our Thames Refinery

We import around 600,000 tonnes of raw cane sugar annually direct to our Thames Refinery. We manage the customs process ourselves for all of these volumes. The process is managed by a small team of two full time people. These two people also administer all of the other elements of the raw sugar contract, including managing the shipping programme and arranging payment to suppliers.

The total annual cost of that team is £110,000 including salaries and other employment costs. The value of the sugar itself varies with market conditions, but at current market prices would be around €320 million, or £270 million at current exchange rates. Attributing the whole cost of this team to customs processes would make the customs procedures cost the equivalent of 0.041% of the value of the product. Given the other roles of this team, the true cost is more likely 0.01% to 0.02% of the value of the product.

- 9.4 In conclusion, customs processes have a cost. It is naïve to claim that they don't. But it is also important to have a clear and honest view of what those costs actually are. It is also critical to weigh them against the opportunities that exist outside of the EU Customs Union.
- 9.5 Our example is the experience of only one sector. But it is an experience that is quantifiable. Many businesses will never have traded outside the EU Customs Union and it is natural and understandable to fear the potential cost and complexity of customs processes. Our experience is that in reality they are a tiny cost of the total value of the business. And, provided that procedures are established and followed, in our experience customs processes have never held up our day to day operations. Customs processes and procedures simply do not register as a major business cost or practical risk for us, even though we are the largest importer of one of the most trade sensitive products to the EU.



CASE STUDY

10. THE ANZCERTA EXPERIENCE

- 10.1 Customs clearance between Australia and New Zealand (which do have a Free Trade Agreement but are not members of a customs union) is covered in the Australia New Zealand Closer Economic Relations Trade Agreement (“ANZCERTA”). The advantages of the ANZCERTA model are that it is not narrowly structured and has been able to evolve as the relationship between Australia and New Zealand has evolved. ANZCERTA started out as a bilateral commitment to eliminate tariffs, import licensing and quantitative restrictions but over time has also facilitated free trade in services and underpinned a range of cooperative and institutional arrangements; including mutual recognition and coordination of policy and administration. This latter aspect is particularly applicable to customs and border management and administration.

- 10.2 From a customs perspective, ANZCERTA does not insist on harmonised customs legislation between Australia and New Zealand, nor does it require that both countries administer their customs legislation in the same way. Each customs agency makes its own risk assessments and conducts their day-to-day customs administration within the different contexts pertaining to each country.
- 10.3 There are differences between Australia's and New Zealand's customs legal framework and systems in a number of areas including reporting, revenue and payment requirements, customs clearance, approaches to low value consignments, and customs processing systems.
- 10.4 What ANZCERTA does is provide an effective and mutually accepted framework for ongoing cooperation between the respective customs administrations with the objective of improving border management at the same time as endeavouring as far as possible to reduce compliance costs for business.
- 10.5 As far back as 1988 there was a "Joint Understanding on the Harmonisation of Customs Policies and Procedures" entered into by the respective governments. There are formal annual meetings between Customs Ministers and between Agency Heads. A High Level Steering Group to address border issues was formed in 2005 and a joint time release study was conducted in 2010 to help identify and simply trans-Tasman import/export procedures. There are intelligence sharing arrangements between the respective customs/border agencies which includes tactical/operational level intelligence, the exchange of risk and threat analyses, and exchange of commercial shipping risk assessments. In July 2016 the Australian Department of Immigration and Border Protection and New Zealand Customs Service signed a Mutual Recognition Agreement under the auspices of ANZCERTA to recognise the supply chain security programs of both countries.
- 10.6 The shared goal of both Australian and New Zealand governments under the current ANZCERTA is now "a seamless business environment", with the primary objective to "further reduce compliance costs for businesses operating in both economies, through eliminating duplicate or conflicting regulation". The current work program is focused on four themes:
- 10.6.1 reducing the impact of borders;
 - 10.6.2 regulatory coordination;
 - 10.6.3 improving regulatory effectiveness; and
 - 10.6.4 supporting business opportunities.
- 10.7 ANZCERTA could be used quite effectively as a model for customs cooperation and perhaps mutual recognition of specific approaches to customs/border issues between the UK and EU post-Brexit but at least part of its effectiveness has been the underlying comity between Australia and New Zealand; and the fact that it is implemented between countries that to an extent, share a common regulatory approach to a range of issues. Since it is envisaged under the Great Repeal Bill that product requirements will be transposed into UK law, the regulatory approach between the UK and EU will be identical at the Exit Date. However, as the UK and EU may diverge after this, the framework should reflect the fact that with respect to standards and technical regulations, the ultimate end-state for the UK-EU relationship is a free trade agreement where standards and technical regulations should not be used as disguised barriers to trade.
- 10.8 Its effectiveness as a model for customs cooperation is stronger with respect to alignment of customs procedures and border risk management than with respect to the actual legislation that must be put in place to underpin those procedures. ANZCERTA provides an effective mechanism for mutual recognition, in particular given that the UK will be consistent with the UCC and interoperating with EU member state authorities already.



CASE STUDY

11. THE US CANADA EXPERIENCE

- 11.1 The border between Canada and the USA is subject to the North American Free trade Agreement ("NAFTA") but the two countries are not in a customs union so a full customs border is in operation. Over the period 2011 to 2015, Canada's imports from the USA averaged \$US234.6 billion, about 52% of Canada's total imports. Exports from Canada to the USA accounted for 75% of a total of \$US450 billion. The products imported and exported cross the full spectrum of goods from live animals and fresh and processed foods to natural resources, semi-processed goods and the full range of intermediate and final manufactured products. Motor vehicles and their parts alone accounted for about 20 per cent of this two-way trade, with trade in parts, many of which cross the border more than once during their production before being installed into a vehicle, accounting for about one-third of this trade.

- 11.2 Customs clearance of imported goods is critical for Canada's economic prosperity. The responsibility for customs clearance and related trade facilitation programs in Canada falls to the Canada Border Services Agency ("CBSA"). The mandate of the CBSA is to provide "integrated border services that support national security and public safety priorities and facilitate the free flow of persons and goods, including animals and plants, that meet all requirements under the program legislation".⁶⁸ The CBSA is responsible for the administration of over 90 acts, regulations and international agreements relating to entry and exit of people, goods, animals and plants on behalf of the federal government and the provincial and territorial governments in Canada. It employs approximately 14,000 people, and operates at 117 land-border crossings, 13 international airports, 27 rail sites and 3 international mail processing centres, as well as providing services at 39 locations abroad.⁶⁹
- 11.3 The challenge for the CBSA in managing the customs clearance of imported goods is to balance expediting and facilitating trade to support economic prosperity on the one hand and protecting the safety and security of its citizens and the country on the other. Fulfilling this dual mandate requires managing effectively and efficiently both the flow of goods across the border and the flow of information related to the goods, traders and associated service providers (e.g., carriers, customs brokers, freight forwarders).
- 11.4 Accordingly, the CBSA has developed and continues to update and modernise a wide range of tools and programs designed to fulfil its dual mandate. Five overarching themes characterise the deployment of these tools and programs in processing and managing the high volume of imports crossing into Canada each day:
- 11.4.1 the first is the separation of the flow of information and payment of duties and taxes from the movement of the goods themselves so as to allow goods to be released on minimum documentation at the border, with further documentation and payments of duties and taxes provided after the goods have departed the border.
 - 11.4.2 the second involves the intensive use of advance screening and risk assessment, not only for goods but also for importers, carriers and other service providers, under the CBSA's "push out the border" strategy.⁷⁰ This enables the CBSA to target and focus on high-risk import shipments while allowing low-risk shipments to be processed efficiently, thereby minimising delays at the border for such goods.
 - 11.4.3 the third theme is the ever-increasing use of electronic information technologies in the CBSA's customs clearance programs and processes, including risk assessment programs, such as the Tactical Information Targeting Analysis and Notification System (TITAN). These electronic systems enable importers, carriers and others to send information to the CBSA before goods reach the border and are also used by the CBSA to inform importers when their goods are released from the border, and by importers (or their customs brokers) to send the required post-entry information and pay duties and taxes.
 - 11.4.4 the fourth theme is the continuous need to up-date and modernise programs and processes to address the ever-changing trade and security environment, and enable the CBSA to reduce the time and costs of import clearance for low-risk traders and carriers of low-risk goods and to focus its resources and attention on identifying and addressing high-risk imports.
 - 11.4.5 the fifth theme is close cooperation with other countries, in particular the United States. Reflecting the importance of their bilateral trade, Canada and the United States are working together closely on many customs and related matters, through their joint Beyond the Border Action Plan.
- 11.5 Further information on these themes and the associated programmes, is set out in detail in Appendix 2. Some of the programmes and processes are broadly in place in the UK and EU member states' customs processes, others represent solutions that could be explored for implementation between the UK and EU as trusted trading partners analogous to Canada and the USA.

12. CONCLUSION AND RECOMMENDATIONS

- 12.1 At the outset, the UK should offer to negotiate an FTA with the EU, but should also maintain a “zero for zero” offer on tariffs, whereby if an FTA cannot be agreed by the Exit Date, neither side will introduce any tariffs or quotas on imports of goods from the other for a period while an FTA is negotiated. This is consistent with the commitment made at the G20 2016 summit in China to operate “standstill and roll back” of tariffs. It is also in line with the treaty requirement in Article 8 of the Treaty on European Union to “develop a special relationship with neighbouring countries, aiming to establish an area of prosperity and good neighbourliness, founded on the values of the Union and characterised by close and peaceful relations based on cooperation”. As well as protecting the economies of both the EU and the UK, and without risking any defensive interests that would exist between two territories where barriers exist, this also avoids sending a protectionist message of introducing tariffs at a time when free trade is perceived to be under threat across the globe.
- 12.2 If the EU insists on imposing the common external tariff, or other preferential tariffs, on imports from the UK there are mechanisms available in existing EU customs and standards legislation to facilitate tariff free supply chains and expedite customs clearance. UK exporters will continue to benefit from the depreciation of sterling in the short term and could benefit from measures to improve productivity and competitiveness across the economy in the longer term to mitigate the impact of EU tariffs.
- 12.3 If the UK elected to reciprocate the imposition of tariffs, this would compound the negative impacts of the EU’s tariffs by causing prices to rise for consumers, who ultimately bear the cost, and (inefficient) substitution across supply chains. There are pro- free trade alternatives that protect or enhance consumer welfare and could improve manufacturing productivity and revenues. These include unilaterally eliminating tariffs on all imports in selected categories such as industrial goods and agricultural products that the UK does not produce, or across the board. The latter would likely yield the most immediate consumer welfare and GDP benefits but would diminish the UK’s negotiating strength in negotiations with third countries, so could risk even greater longer term gains.
- 12.4 In any of these scenarios, there are tools available to the UK government through tariff reduction and elimination on selected goods, WTO compliant reliefs like duty drawback and suspension and freeports that the UK will be able to operate in a more trade-creative and less protectionist way than the EU makes available at present. Analysis will be required as to which industries and sectors will be most affected and therefore require support and investment (in ways that will not comprise export subsidies).
- 12.5 Even if the EU and the UK agree an FTA or “zero for zero” preferential deal on tariffs, this would involve added administration and cost for businesses in dealing with customs formalities. These can be minimised by continued close co-operation and mutual recognition (and offset by reducing tariffs and improving trade facilitation and trade in services with rest of world). Other measures that would increase competitiveness and reduce the overall cost of

manufacturing in this country include investing in skills and training, investing in infrastructure and improving planning regulation. The sectors most exposed to additional cost and risk from the introduction of tariffs and customs procedures should be identified, and work should be done to establish what the additional costs of customs compliance will be and where they will fall.

- 12.6 A period of adjustment may be required for customs authorities to ensure systems and resources are in place, businesses can comply with formalities and for manufacturers to comply with RoO. IT systems, facilities at customs borders and human resources will all need to be implemented and tested. Traders may wish to make changes to their supply chains depending on the RoO that are agreed and this, together with the certification process, will take time after the agreed RoO are known. Therefore an interim period after the Exit Date should be considered during which both sides will waive customs checks and rules of origin, provided the UK maintains the Common External Tariff for rest of world imports (so the UK does not become a back door for tariff free trade into the EU). Further research is recommended to establish how long such adjustment period should last, and whether it needs to apply to all goods.
- 12.7 UK operators who trade with the EU should ensure they register for EORIs and, if appropriate, apply to be AEOs. Mutual recognition of such registrations should be included in the Withdrawal Agreement. Comprehensive customs cooperation and recognition of conformity assessment bodies should continue to minimise at-border activity.
- 12.8 Mutual recognition of conformity assessment bodies should be sought as a priority. If necessary, the UK could undertake to retain existing harmonised legislation for products like medicines and motor vehicles for an interim period. A commitment from both sides to mutual recognition and trade facilitation should be sought at the outset of negotiations to reduce uncertainty for businesses.
- 12.9 The UK should maintain its membership of European standards bodies (at least for an interim period) and continue to participate in global fora such as UNECE and Codex Alimentarius in order to continue to have a role in the regulations to which imports of goods to the EU will be subject.

APPENDIX 1

THE WTO LEGALITY OF A DUTY-FREE REGIME FOR IMPORTS OF COMPONENT PRODUCTS USED IN EXPORTED FINAL PRODUCTS

by Lorand Bartels. 16 December 2016

A. THE ISSUE

This memorandum considers the legality, under WTO law, of a UK measure granting duty free treatment for a component product (for example, a car part) that is imported from a third country (for example, Korea) for use in the production of a 'final product' (for example, a car) in the UK which is exported to the EU27 following the UK's departure from the EU.

B. A UNILATERAL DUTY FREE REGIME

1. There is no legal obstacle to the UK granting duty free treatment to any imported product, including a component product, provided that it grants the same duty free treatment to all 'like' component products imported into the UK from all other WTO Members. This follows from the most favoured nation obligation in Article I:1 of the GATT 1994, a non-discrimination provision. Article I:1 states as follows:

In connection with importation or exportation ... any advantage, favour, privilege or immunity granted by any Member to any product originating in or destined for any other country shall be accorded immediately and unconditionally to the like product originating in or destined for the territories of all other Members.⁷¹

2. Article I:1 applies to measures that discriminate against 'like' products both *de jure* (i.e. when the measure is formally discriminatory by specifying different treatment according to the origin of the products at issue) and *de facto* (i.e. when the measure is formally neutral as to origin but as a matter of fact discriminates against products according to

origin). This was clarified by the WTO Appellate Body in *Canada—Automobiles*. This dispute concerned a Canadian measure implementing the Canada-United States 'Auto Pact' Agreement (originally dating from 1965), which consisted of a duty exemption for motor vehicles produced by certain manufacturers. The duty exemption was only available for manufacturers that controlled production facilities and were able to meet certain conditions concerning production in those facilities. Canada argued that Article I:1 did not prohibit the imposition of 'origin-neutral terms and conditions on importation that apply to companies as opposed to the products they import.'⁷² The Appellate Body rejected this argument.⁷³

3. This means that the UK may not grant duty free treatment to a component product used in a particular supply chain unless it grants the same treatment to all 'like' component products.

C. DUTY FREE TREATMENT AS A SUBSIDY

4. In *Canada—Automobiles*, the Appellate Body also determined that the exemption of duties for imports of some but not all automobiles constituted 'government revenue that is otherwise due [that] is foregone or not collected' within the meaning of Article 1.1(a)(1) (ii) of the Agreement on Subsidies and Countervailing Measures (SCM Agreement).⁷⁴ That meant that the duty exemption constituted a 'financial contribution'. Because the duty exemption also conferred a 'benefit', it was a subsidy within the meaning of Article 1.1 of the SCM Agreement.

5. However, the duty exemption in *Canada—Automobiles* was applied to products destined for final consumption in the country of importation.⁷⁵ It is different for duty rebates in respect of products that are destined for re-export. Such rebates fall under footnote 1 of the SCM Agreement, which is attached to Article 1.1(a)(1)(ii). Footnote 1 states that:

In accordance with the provisions of Article XVI of GATT 1994 (Note to Article XVI) and the provisions of Annexes I through III of this Agreement, the exemption of an exported product from duties or taxes borne by the like product when destined for domestic consumption, or the remission of such duties or taxes in amounts not in excess of those which have accrued, shall not be deemed to be a subsidy.⁷⁶

6. This footnote permits rebates of duties on both re-exports of the same imports and on imported component products that are incorporated into exported final products. Both types of rebate are known as 'duty drawback'.⁷⁷
7. Duty drawbacks are justified on the basis of the so-called destination principle, common to many domestic taxation regimes, according to which products should be taxed only at their place of destination. This is relatively straightforward for duty drawbacks on final products, which, technically, only transit through the country in which tax is charged and then rebated.⁷⁸ In theory, it is a little more difficult to justify duty drawbacks on component products, because the country of consumption could be seen as the country of destination for taxation purposes. Nonetheless, the component can still be taxed, as such, in the country to which the final product incorporating the product is exported. This occurs under Article II:ii(a) of the GATT 1994, which permits WTO Members to impose the equivalent of an internal tax on the 'articles' from which an imported product has been produced.⁷⁹ This is typically called a 'border tax adjustment'.
8. The conclusion, for the UK, is that duty free treatment can be afforded to imports destined for export (including both final products and components in

final products) without any equivalent treatment being afforded also to 'like' imports destined for the domestic market. However, the most favoured nation obligation in Article I:1 of the GATT 1994 continues to apply to the treatment of such products. In other words, a duty drawback system can result in duty free treatment of products destined for export but it has to apply to all 'like' products destined for export.⁸⁰

D. CONDITIONS ON DUTY DRAWBACK SYSTEMS

9. The SCM Agreement contains various further provisions on duty drawbacks. Item (i)⁸¹ of Annex I of the SCM Agreement ('Illustrative List of Export Subsidies') sets their limits. It defines an export subsidy as including:

The remission or drawback of import charges in excess of those levied on imported inputs^[original footnote 58] that are consumed in the production of the exported product (making normal allowance for waste)...⁸²

[original footnote 58] ... The term 'import charges' shall mean tariffs, duties, and other fiscal charges not elsewhere enumerated in this note that are levied on imports

10. Export subsidies are prohibited under Article 3.1(a) of the SCM Agreement and must be 'withdrawn' under Article 4.7 of the SCM Agreement.
11. However, Item (i) also contains a conditional exception to the rule on excess drawback by recognising the legality of so-called 'substitution drawback systems'. Such systems are designed allow domestic producers to obtain duty drawbacks in respect of exports that may contain domestic components. The idea—already criticised as outdated in the 1980s⁸³—is to ease the administrative burden on producers (and exporters) of determining precisely when they were using imported as opposed to domestic components. Thus, Item (i) continues, after the sentences quoted above, as follows:

...; provided, however, that in particular cases a firm may use a quantity of home market inputs equal to, and having the same quality

and characteristics as, the imported inputs as a substitute for them in order to benefit from this provision if the import and the corresponding export operations both occur within a reasonable time period, not to exceed two years. ...⁸⁴

12. Further work may be required to determine the practical relevance of this exception in the circumstances at issue.

E. DUTY DRAWBACKS IN FTAS

13. Many free trade agreements prohibit duty drawback systems in relation to imported components from third countries. For example, Article 2.5 of the recently signed EU-Canada Comprehensive Economic and Trade Agreement (CETA) states as follows:

Article 2.5 (Restriction on duty drawback, duty deferral and duty suspension programs)

1. ... a Party shall not refund, defer or suspend a customs duty paid or payable on a non-originating good imported into its territory on the express condition that the good, or an identical, equivalent or similar substitute, is used as a material in the production of another good that is subsequently exported to the territory of the other Party under preferential tariff treatment pursuant to this Agreement.⁸⁵

14. On the other hand, and somewhat controversially,⁸⁶ the EU accepted a negotiating demand by South Korea to include a limited duty drawback system in the 2011 EU-Korea free trade agreement.⁸⁷ This may be an issue that can be negotiated in a future UK-EU free trade agreement.
15. A further question is whether such provisions are still subject to the most favoured nation obligation in Article I:1 of the GATT 1994. This is a question that, in practice, has been ignored, but in theory may well be important.

E. CONCLUSION

16. The conclusions of this analysis may be summarised as follows. It is WTO legal to grant duty free treatment to component products that are incorporated into final products in the UK that are then exported to another country provided that such treatment is accorded on a non-discriminatory basis to imports of 'like' products from all other WTO Members.
17. Such a system is optional, not mandatory. It may also be necessary to negotiate such a system, for non-originating components, in a UK-EU free trade agreement. This could be difficult because, typically, EU free trade agreements exclude duty drawbacks on non-originating components. However, this was done in the EU-Korea free trade agreement. In support of such a negotiated demand, it could also be argued that such a discriminatory prohibition on duty drawbacks in a free trade agreement would violate the most favoured nation obligation in Article I:1 of the GATT 1994 and not justified by Article XXIV of the GATT 1994. This question may deserve further analysis.

APPENDIX 2

NOTE ON THE CANADA BORDER SERVICES AGENCY: CUSTOMS CLEARANCE AND TRADE FACILITATION

by Andrew (Sandy) Moroz and Colleen Brock⁸⁸

The note provides information on Canada's programs and processes for customs clearance of goods and trade facilitation. The discussion on customs clearance examines the overall approach taken by Canada and its current processes, programs and modernisation initiatives in this area. The note then looks at the various programs and initiatives to facilitate both trade and security and safety, including through cooperation with the United States. The final section provides some indicators of Canada's performance as compared to that of other developed countries in the areas of customs clearance and trade facilitation.

For purposes of this note, "border" means the point of arrival in Canada where the good is subject to customs processes. For goods being shipped by highway, this is normally at the customs office located at the physical border crossing; for goods arriving by air or rail mode, this is usually at an inland location (e.g., airport or rail terminal); for goods arriving by marine mode, this is normally the sea terminal in the first port the ship docks.

INTRODUCTION

Canada is a small, open economy that depends on both imports and exports.⁸⁹ For the 2011-2015 period, total imports into Canada averaged annually \$US 451.7 billion.⁹⁰ During the same period, annual imports from the United States, Canada's largest trading partner, averaged \$US 234.6 billion, or about 52 per cent of the value of imports, and comprised the full spectrum of goods from live animals and fresh and processed food products to natural resources, semi-processed goods and the full range of intermediate and final manufactured products. Exports to the United States accounted for around 75 per cent of Canada's total exports,

which averaged annually \$US 450.0 billion during this period, again covering the full range of agricultural and non-agricultural products. The total value of goods crossing the Canada-U.S. border in both directions averaged \$US 575.3 billion, or more than \$US 1.5 billion a day, reflecting Canada's dependence on trade and economic integration, including through value chains, with the United States under the North American Free Trade Agreement (NAFTA). Motor vehicles and their parts alone accounted for about 20 per cent of this two-way trade, with trade in parts, many of which cross the border more than once during their production before being installed into a vehicle, accounting for about one-third of this trade. More broadly, firm-level analysis suggests that intermediate goods account for over half of Canada's total exports and imports of manufactured products.⁹¹

All this to say that customs clearance of imported goods is critical for Canada's economic prosperity. The responsibility for customs clearance and related trade facilitation programs in Canada falls to the Canada Border Services Agency (CBSA). The mandate of the CBSA is to provide "integrated border services that support national security and public safety priorities and facilitate the free flow of persons and goods, including animals and plants, that meet all requirements under the program legislation".⁹² The CBSA is responsible for the administration of over 90 acts, regulations and international agreements relating to entry and exit of people, goods, animals and plants on behalf of the federal government and the provincial and territorial governments in Canada. It employs approximately 14,000 people, and operates at 117 land-border crossings, 13 international airports, 27 rail sites and 3 international mail processing centres, as well as providing services at 39 locations abroad.⁹³

CUSTOMS CLEARANCE OF GOODS

With respect to the commercial importation of goods, the CBSA administers the full range of border services, including on behalf of, or in cooperation and coordination with, other government departments and agencies in the administration and enforcement of their legislation and regulations. The CBSA's border administration and enforcement responsibilities include collecting duties and taxes on imported goods, ensuring compliance with sanitary, phytosanitary, transportation and product health and safety standards and regulations, interdicting prohibited or controlled goods, ensuring prescribed products are clearly marked with their country of origin, collecting statistics, and administering and enforcing trade remedies and specific obligations under Canada's trade agreements.⁹⁴ Certain goods are subject to the regulations of other federal government departments or provincial and territorial governments (henceforth, regulated goods). Importers are required to present permits, certificates, licenses or other authorisations issued by these departments or agencies when the good arrives at the border. Table 1 provides examples of commonly imported regulated goods and the associated federal government departments or agencies.

THE CHALLENGE FOR THE CBSA IN CUSTOMS CLEARANCE OF GOODS

The challenge for the CBSA in managing the customs clearance of imported goods is to balance expediting and facilitating trade to support economic prosperity on the one hand and protecting the safety and security of its citizens and the country on the other. Fulfilling this dual mandate requires managing effectively and efficiently both the flow of goods across the border and the flow of information related to the goods, traders and associated service providers (e.g., carriers, customs brokers, freight forwarders).

As indicated in Table 2, importers and their service providers are required to provide a range of data elements about imported goods, including their description, price, shipping and other costs, names and addresses of vendors, buyers, importers and carriers, the points of shipment and destination, and so forth. This information is used by the CBSA both for security and safety reasons and to calculate

duty and taxes. In addition to this information about the good, the carriers are required to provide cargo and conveyance data on the shipping and warehousing of the good. In addition, importers must also present any permits and certificates required from other departments or agencies for regulated goods when the goods arrive at the border.

Customs officials need to process this information in order not only to determine the applicable duties and taxes, but also to ensure that the goods meet all applicable requirements and do not pose a risk or threat before the goods can be released from the border. This takes time and resources and customs authorities may also need to coordinate with other government departments and agencies, for example, when permits or certificates are required for regulated goods or when there is a need for physical inspection, as in the case of live animals. This, in turn, affects how quickly and efficiently goods can be released from the border and, therefore, the time and costs incurred by businesses. "Efficient clearance procedures at the border are critical to eliminating avoidable delays and to improving supply chain predictability."⁹⁵

As discussed in more detail in the next section, the CBSA has developed, and continues to up-date and modernise, a wide range of tools and programs designed to fulfill its dual mandate. Five overarching themes characterise the deployment of these tools and programs in processing and managing the high volume of imports crossing into Canada each day.

The first is the separation of the flow of information and payment of duties and taxes from the movement of the goods themselves so as to allow goods to be released on minimum documentation at the border, with further documentation and payments of duties and taxes provided after the goods have departed the border.

The second involves the intensive use of advance screening and risk assessment, not only for goods but also for importers, carriers and other service providers, under the CBSA's "push out the border" strategy.⁹⁶ This enables the CBSA to target and focus on high-risk import shipments while allowing low-risk shipments to be processed efficiently, thereby minimising delays at the border for such goods.

The third theme is the ever-increasing use of electronic information technologies in the CBSA's customs clearance programs and processes, including risk assessment programs, such as the Tactical Information Targeting Analysis and Notification System (TITAN). These electronic systems enable importers, carriers and others to send information to the CBSA before goods reach the border and are also used by the CBSA to inform importers when their goods are released from the border, and by importers (or their customs brokers) to send the required post-entry information and pay duties and taxes.

The fourth theme is the continuous need to up-date and modernise programs and processes to address the ever-changing trade and security environment, and enable the CBSA to reduce the time and costs of import clearance for low-risk traders and carriers of low-risk goods and to focus its resources and attention on identifying and addressing high-risk imports.

And the fifth theme is close cooperation with other countries, in particular the United States. Reflecting the importance of their bilateral trade, Canada and the United States are working together closely on many customs and related matters, through their joint Beyond the Border Action Plan, discussed below.

THE CBSA'S PROCESSES AND PROGRAMS

The commercial importation clearance process comprises four key components: cargo and conveyance reporting, release at the border, accounting for the good (i.e., provision of the required information about the good, including correcting any errors and omissions) and payment of duties and taxes. This section provides a description of the CBSA's main processes and programs for customs clearance of goods, including new initiatives to expedite and facilitate the early release of goods from the border.

ELECTRONIC TRANSMISSION OF INFORMATION

The CBSA's use of electronic data interchange (EDI) systems to receive and transmit information to importers, carriers and other service providers plays a key role in its customs clearance processes and in its Trusted Trader programs. The CBSA continues to up-date its EDI systems and expand

the mandatory use of electronic submissions by importers, carriers and others.

The Accelerated Commercial Release Operations Support System (ACROSS) allows importers and brokers to submit electronically the information required for the clearance of a good, both before and after the good reaches the border, thereby enabling customs officials to process more quickly low-risk shipments. In 2015/16, 92.8 per cent of the 16,345,640 import declarations made in Canada were electronic declarations.⁹⁷

The Pre-arrival Review System (PARS) under ACROSS is used by importers to request border release of their goods, and to submit the required import information, under the Release on Minimum Documentation (RMD) program (see below). The PARS can also be used to process the importation of regulated goods, such as those goods regulated by the Canadian Food Inspection Agency (CFIA).

Importers, customs brokers, shippers and other service providers can receive electronically instant notifications of CBSA border release decisions or PARS request approvals by participating in the **Release Notification System (RNS)**.

The **Commercial Cash Entry Processing System (CCEPS)** is a self-service system that allows importers to prepare electronically the necessary importation documents and automatically calculates the duties and taxes owing.

The **Customs Automated Data Exchange (CADEX)** allows importers and customs brokers to prepare and submit final accounting documentation electronically with the CBSA. CADEX also enables participants to receive daily invoices, monthly statements, tariff and exchange rate file updates, as well as notifications of release decisions. Alternatively, importers and customs brokers can use **Customs Declaration (CUSDEC)**, which uses a different EDI technology.

As noted above, certain other departments and agencies require permits or certificates for regulated goods to be provided at the time of importation. Under the **Single Window Initiative (SWI)**, in 2015 the CBSA launched the electronic SWI Integrated Import Declaration as an alternative method to PARS, allowing importers to submit their information simultaneously to all participating departments and agencies for their review and release recommendation. As of December 2016, nine departments

and agencies have become participants: the Canada Food Inspection Agency, The Canadian Nuclear Safety Commission, Environment and Climate Change Canada, Fisheries and Oceans Canada, Global Affairs Canada, Natural Resources Canada, Health Canada, the Public Health Agency of Canada and Transport Canada. In certain cases, the required permit or certificate for regulated goods can be verified electronically when the good arrives at the border, as in the case of Global Affairs Canada's Customs Automated Permit System (EXCAPS) for permits required for importing certain agricultural goods (i.e., dairy, poultry and egg products) that are subject to quantitative import controls. As part of the Canada-U.S. Beyond the Border Action Plan (see below), Canada is working to align the SWI data requirements as much as possible with those of the U.S. Customs and Border Protection and the World Customs Organization Data Model.

The **CBSA Assessment and Revenue Management (CARM)** is a major, multi-year project to transform how the CBSA electronically manages import revenue and trade information from companies involved in Commercial Trade Chain Partners (CCP). Trade Chain Partners are CSA importers in Canada and their partner shippers and vendors located in the United States or Mexico. The overall goal of this project is to enable the CBSA to process assessments, payments and adjustments more quickly and efficiently (including by eliminating repetitive information requests), and to support CBSA's data sharing, compliance verification and fraud detection activities. Once fully implemented, CARM will also provide self-service access by importers to their own information and may also be extended to all importers as a replacement for CADEX and CUSDEC.

The first phase of CARM, the Accounts Receivable Ledger (ARL), was implemented in January 2016. The ARL operates as a fully integrated and centralised commercial client-based accounting and payment system that provides daily notices, monthly financial statements, electronic banking transfers between the CBSA and importers, and online banking options for importers.

RELEASE AND CLEARANCE OF IMPORTED GOODS

Importers can obtain clearance by the CBSA of their imported goods in four ways. Carriers, however, are required to send electronically cargo and conveyance information in advance of the goods arriving at the border in compliance with the CBSA's **Advanced Commercial Information (ACI)** program under any of these methods; otherwise their vehicles will be detained until this information has been received and verified. This CBSA has been phasing in the ACI program over a number of years. Table 3 sets out the current prescribed time-lines for pre-sending cargo and conveyance information for air, marine, rail and highway modes for carriers and for freight forwarders. As the next phase under the ACI program, the CBSA is currently working to implement the eManifest program. Once the eManifest program is fully implemented, carriers, freight forwarders, importers and customs brokers will be required to transmit electronically commercial and shipping information for all modes of transportation within the prescribed time-periods to be set for each mode.

First, importers can obtain clearance by the CBSA of their imported goods by presenting all the stipulated import and shipping data, any required certificates and permits, and paying all duties and taxes owing at the time the good arrives at the border. The CBSA needs to review, assess and process this information and take any other required actions (e.g., contact relevant departments and agencies) before a decision on whether to clear the goods can be made. This takes time and resources, and hence raises the costs of importing goods.

The other three methods provide expedited border release processes. Registered importers can utilise the **Release on Minimum Documentation (RMD)** program. This program allows registered importers or licensed customs brokers who have posted financial security with the CBSA to request release of their goods from the border by submitting interim information on the good, with payment of duties and taxes and submission of the final data on the good deferred until later. RMD requests and information must be submitted electronically, either before or when the good arrives at the border. Their carriers, however, must still send electronically the cargo and conveyance information ahead of the goods arriving within the mode-specific time-lines stipulated by the ACI program.

For import shipments that do not require examination of the goods or further processing on behalf of another department or agency, the goal of the CBSA is to process a RMD request within five minutes unless there is an electronic prompt flagging the need for a review by a border services officer. In the event of a prompt, the goal is to complete the review process within 45 minutes. If the RMD request is submitted through PARS at least one hour before the good arrives at the border, then, according to the CBSA website, “[w]hen a shipment arrives, the CBSA will release it within minutes unless an examination or further processing is required to meet another department’s regulations”.⁹⁸

For high value shipments (exceeding CDN\$ 2,500) under the RMD program, final documentation must be provided to the CBSA within five business days of the date of release of the goods from the border. For low value shipments (not exceeding CDN\$ 2,500), the final documentation must be sent to the CBSA on the 24th day of the month (or the previous business day if that day is weekend or statutory/civic holiday) following the month in which the goods were released. In either case, payment of duties and taxes must be made on the last business day of the month following the month in which the goods were released at the border (i.e., the second month).

Under the third method, pre-approved importers can use the **Customs Self-Assessment (CSA), one of the CBSA’s Trusted Trader programs**. The CSA program allows goods to be released at the border on the basis of limited information sent in advance to the CBSA, with payment of duties and taxes and submission of full data deferred until later, if these importers also use pre-approved carriers. The CSA program also consolidates the customs processes, reduces the number of required electronic transmissions and provides more flexibility for submitting final documentation and paying duties and taxes after the goods have been released from the border, as compared to the RMD program. The importers are not required to submit information about the imported goods before or at the time the goods arrive at the border. Carriers, however, are still required to meet the above mode-specific ACI requirements for sending cargo and conveyance data before the goods reach the border, except in the case of CSA-eligible goods entering Canada by highway mode (see below).

To use the CSA program, importers and carriers must meet the CSA eligibility requirements⁹⁹ and undergo a rigorous screening and two-step approval process. The latter includes providing detailed business and financial information, and demonstrating that their financial records and business systems have the required controls and procedures to support CBSA requirements. Carriers are required to maintain control and assume liability for all shipments until goods are released. In the case of highway mode imports for CSA-eligible goods (see below),¹⁰⁰ commercial drivers must be approved under either the Commercial Driver Registration Program (CDRP) or the Fast and Secure (FAST) program (see below). To qualify under these programs, commercial drivers must go through a rigorous screening and approval process similar to that required of importers and carriers.

CSA importers gain a further advantage when importing CSA-eligible goods, which are goods not subject to the regulations of another government department or agency (henceforth, unregulated goods) that are shipped, using CSA carriers, directly from the United States or Mexico. These goods can move by highway, marine, air or marine mode. CSA-eligible goods are normally released immediately at the border if an electronic verification of importer’s and carrier’s bar-code identifiers (presented by the carrier at the time of arrival) confirms that both are CSA approved and, in the case of a highway mode importation, the driver has a valid CDRP or FAST card.¹⁰¹ No other documentation regarding the imported good itself is required to be provided upon arrival of the good at the border.

CSA importers are responsible for their own self assessment. For shipments exceeding CDN\$ 2,500, the importer has the choice of providing the required import information to the CBSA either on the 18th day of the month following the month in which the good was imported and released or, if the good was released from the border between the 19th of one month and the 18th of the second month, by the last business day of the second month. The information for low value shipments (not exceeding CDN\$ 2,500) must be presented to the CBSA by the 24th day of the month following the month in which the goods were released. Payments of duties in both cases is due on the last business day of the second month, but, unlike for non-CSA importers, the payments can be made to the importers’ own financial institutions. CSA participants are expected to maintain very

high levels of compliance in meeting these reporting and payment requirements, and, more generally, are subject to verifications to ensure on-going compliance with the terms and conditions of the program.

CSA importers can still take advantage of the other benefits of the CSA program discussed above when they import non-CSA-eligible goods (i.e., regulated goods) directly from the United States or Mexico, import goods from any other country, or use non-CSA carriers.

Pursuant to the Canada-U.S. Beyond the Border Action Plan (discussed below), the CBSA has introduced the **CSA-Platinum program**. CSA-approved importers are eligible to apply for this augmented program if they have attained the highest rate of compliance with the CBSA's trade programs, such as tariff classification, preferential tariff treatment and value for duty. The CBSA will review the importers' internal controls and business systems and identify where improvements can be made. CSA Platinum members are responsible for conducting their own trade compliance tests and reporting the results to the CBSA on an annual basis, although the CBSA reserves the right to conduct or have the participant perform verifications for high risk or sensitive issues, including targeted verification priorities. As well, participants will have enhanced access to CBSA officers to address issues and problems. The CBSA may also choose not to resort to more punitive penalties as a first response to cases of non-compliance with its trade compliance programs.

The **Courier Low Value Shipment (CLVS) Program** is a special expedited program for express courier shipments, valued at CDN\$ 2,500 or less, of non-regulated goods. Couriers wishing to participate in the CLVS program must meet several requirements, including being a resident company in Canada, bonded and an approved carrier under Partners in Protection (PIP), which is discussed below. They must also operate an acceptable courier proprietary system that the CBSA can use for report, release, risk assessment and other purposes.

The cargo/release list replaces the normal documentation required for release of the goods at the border, but it must contain the specified minimum information about the goods (e.g., quantities, descriptions, values, countries of origin) and the vendors, importers and consignees. The list is required to be sent electronically at least one hour before arrival at the

border by highway mode and four hours prior to arrival by air, or at time of departure if the flight is less than four hours.

Unless selected for examination, the shipments will be released upon arrival at the border, provided that the importer has posted financial security. Examined shipments will be either released or removed from the cargo/release list. If the latter, then the shipment in question is subject to the CBSA's normal formal release processes.

For shipments released through the cargo/release list process, the CLVS courier is responsible for providing the importer with all release information and supporting documentation within two days after the border release. The importer is required to provide the final information to account for the goods by the 24th day of the month following the month in which the goods were released, with payment of duties and taxes due by the end of that month.

TRADE FACILITATION AND SECURITY/ SAFETY PROGRAMS AND INITIATIVES

In conjunction with the above customs clearance processes and programs, the CBSA has introduced a number of programs and initiatives to facilitate trade and to enhance further the protection of security and public safety.

Partners in Protection

The Partners in Protection (PIP) program is an integral part of the CBSA's suite of Trust Trader programs designed to meet the CBSA's dual mandate. The PIP program directly enlists the cooperation of the private sector. Membership is open to importers, exporters, carriers and couriers, freight forwarders, warehouse operators, customs brokers and shipping agents.

As in the case of the CSA program and FAST (see below), participants must first meet the eligibility criteria, which include owning and operating businesses in Canada or the United States, being solvent and actively engaged in trade, having no convictions under Canadian law, and having a good compliance record with CBSA's trade programs. Businesses can use the CBSA's secure on-line tool, the Trusted Trader Portal (TTP), to submit their PIP applications, and are required to provide a security profile and undergo

a risk assessment and site visit. CSA participants are automatically eligible to apply for the PIP program.

If an applicant qualifies for the PIP program, the CBSA provides security and awareness (e.g., on smuggling trends) assessments and expertise, including recommendations on how the company can improve its security. PIP participants who are also CSA members are automatically eligible to apply to the Free and Secure Trader (FAST) program (see below) and to participate in the Courier Low Value Shipment (CLVS) program. PIP participants are recognised as a Trusted Trader not only at the Canadian border but also by the customs services of the United States, Mexico, Singapore and South Korea under the CBSA's mutual recognition arrangements with the customs services of these countries.

PIP participants are required to keep their information up-dated and provide annual confirmations, and can do so using the TTP. Membership is validated every four years. The CBSA can also, at any time, request an updated security profile and conduct a renewed risk assessment and site visit to ensure members are meeting the terms and conditions of the program.

Free and Secure Trade (FAST)

Free and Secure Trade (FAST) is a joint voluntary program between the CBSA and U.S. Customs and Border Protection (CBP) that is designed to expedite the release of goods at the border for approved importers, carriers and commercial drivers. Participation in this program allows the use of dedicated lanes at highway border crossings, where available, and the release of imports on the presentation of minimum documentation at the border. Currently, dedicated FAST lanes are located at three major bilateral crossing points (Windsor, Ontario / Detroit, Michigan; Sarnia, Ontario / Port Huron, Michigan; and Pacific Highway, British Columbia / Blaine, Washington).

In order to be eligible to use FAST to import goods into Canada, the importers and carriers must be approved in the CSA program (hence, have been risk assessed) and have signed a PIP memorandum of understanding. In the case of shipments to the United States, the importer and carrier must be approved, and goods must be eligible, under the U.S. Customs—Trade Partnership Against Terrorism (C-TPAT)

program. In both countries, the driver must have a valid FAST card, which is valid for five years if all the terms and conditions of the program continue to be met.

FAST-approved importers include retail chains, automotive manufacturers, primary product producers and high technology industries. The list of FAST-approved carriers includes transportation companies from all areas of both Canada and the United States.

Cargo Control and Sufferance Warehouse Modernization

In certain cases, goods are allowed to be transported from the border crossing by bonded carriers to inland licensed warehouses,¹⁰² including sufferance warehouses, before being released by the CBSA to physically enter Canada. All other CBSA requirements, such as providing carrier information before the good arrives at the border, still apply to such imports.

The CBSA is currently developing and consulting with interested parties on its Cargo Control and Sufferance Warehouse Modernization (CCSWM) initiative to modernise the electronic tracking of in-bond cargoes. The goal is to allow bonded carriers to deliver such shipments directly to their own inland facilities or those of a third party. Participants will need to be approved by the CBSA and will be required to accept liability of the goods and to send the CBSA electronically information on the arrival and departure of goods from their warehouses. Any required examination of the good will be done at designated inland centres as opposed to each sufferance warehouse. The CBSA, however, will continue to assess the goods upon arrival at the first customs point at the border to ensure security and safety requirements are met.

Automotive Pre-clearance Program (Transport Canada)

Motor vehicles account for about seven per cent of the value of total Canadian imports, with over 60 per cent of this value imported from the United States. Imported motor vehicles must comply with the Canadian safety standards established under the *Motor Vehicle Safety Act* and the *Motor Vehicle Safety Regulations*, which fall under the responsibility of

Transport Canada. As is the case of other regulated goods, when the new motor vehicles or trailers arrive at the border, the importers involved are normally required to provide the CBSA with the appropriate certifications from Transport Canada that the vehicles meet Canadian regulatory safety standards.

Under Transport Canada's Pre-clearance Program, authorised importers can import new motor vehicles and trailers directly from approved foreign manufacturers without providing the required certificates at the border. The imported vehicles and trailers must fully comply with Canadian safety standards and not have been sold at retail, owned, titled or licensed before the time of importation. Transport Canada has established two lists for its Pre-Clearance program. The first comprises the major global motor vehicle manufacturers who, acting as the importer, can import any of their motor vehicles or trailers intended for sale in Canada. The second list consists of specific vehicles and trailers made by the listed foreign motor vehicle manufacturers which can be imported by any registered commercial importer with the intent for sale in Canada.¹⁰³ These importers on either list must, nevertheless, meet all other import requirements when entering their vehicles into Canada.

Advance Rulings Program

To provide greater transparency and predictability for traders and producers, the CBSA issues advance rulings for the tariff classification of goods and for whether products meet the rules of origin under Canada's various free trade agreements (i.e., FTA rules of origin). It also issues national customs rulings (NCRs) concerning valuation, country of origin markings or if a good qualifies for tariff preferences under a preferential scheme (e.g., Least Developed Country Tariff) other than one of Canada's free trade agreements (henceforth, origin).

Advance rulings for tariff classification can be requested by importers in Canada (or their authorised agents, such as their customs broker) and by exporters or producers outside of Canada. Those for FTA rules of origin application are limited to importers in Canada (or their customs brokers) and to exporters or producers located in Canada's free trade partners. Importers can also seek NCRs for valuation, while NCRs on origin or country of origin marking can be requested by importers, exporters or producers. A request,

with complete information, for an advance ruling or NCR must be submitted to the CBSA at least 120 days prior to the importation of the good. The CBSA will issue the advance ruling within 120 days of receiving all the required information. The CBSA's standard for providing NCRs is 30 days upon receipt of sufficient information, although when laboratory or other complex analysis is required, the standard is 120 days.

Advance rulings and NCRs are binding on both the CBSA and the recipient as long as the original information provided by the recipient remains unchanged or the ruling or NCR is modified or revoked. If the recipient consents, the ruling is then published on the CBSA's website, thereby providing an accessible public repository of rulings for other interested parties.

Given that its responsibilities extend beyond customs clearance of goods, the CBSA also has an array of other programs, such as those related to travellers (including business travellers), consulting with the private sector, administering trade remedies and enforcement and penalties for non-compliance, which are not covered by this note.

The Canada-U.S. Beyond the Border Action Plan

The U.S. Customs and Border Protection (CBP) has many programs that are similar to the CBSA's programs which are designed to facilitate trade and safeguard security and safety and which use risk assessment and electronic transmissions. For example, the U.S. Customs-Trade Partnership Against Terrorism (C-TPAT) and U.S. Importer Self Assessment (ISA) programs share similar objectives, requirements and functions as the CBSA's PIP and CSA—Platinum. Like CBSA's FAST, the U.S. Free and Secure Trade for Commercial Vehicles (FAST) provides dedicated lanes for approved commercial drivers on both the Canadian and Mexican borders, linking the North American supply chain. The CBP's Automated Customs Environment (ACE) system program is being transitioned to an ACE Single Window, similar to CBSA's Single Window initiative.

Given the importance of their bilateral trade, there is a long-standing tradition of close customs cooperation between Canada and the United States. This cooperation, however, has intensified in recent years. In 2011, Canada and

the United States took action to further this cooperation significantly by launching the Beyond the Border Action Plan to enhance security and promote economic competitiveness. This multi-faceted, multi-year joint initiative focusses on four areas of cooperation: addressing threats early; trade facilitation, economic growth and jobs; cross-border law enforcement; and critical infrastructure and cyber-security. It involves the departments and agencies on both sides of the Canada-U.S. border responsible for security, transportation, law enforcement, product safety, travellers and imports and exports of goods.¹⁰⁴ The activities under the Action Plan include sharing of information and intelligence, joint enforcement, up-grading border infrastructure, and aligning and harmonising relevant programs.¹⁰⁵

In the area of customs clearance, Canada and the United States have set out a common framework to align their customs programs with the goal to streamline and simplify bilateral customs clearance processes for low-risk importers, carriers and shipments while ensuring safety and security. On the Canadian side, CBSA's efforts to date have focussed particularly on the CSA—Platinum and PIP programs.¹⁰⁶ The CBSA has also raised its thresholds for the Courier Low Value Shipment (CLVS) program to align with those of the United States.

In addition, the CBSA, Transport Canada and U.S. CBP are jointly developing the Integrated Cargo Security Strategy (ICSS). This initiative is designed to establish harmonised screening processes, including harmonised advance data requirements and targeting and risk assessment methodologies as well as sharing examination results, for cargos arriving in either country from offshore, with the desired end-state of "cleared once, accepted twice". The testing and evaluation of three pilot projects launched in 2012 and 2013 were completed in 2015, with the results providing "lessons learned" for the on-going development of the ICSS.

In 2015, Canada and the United States signed the Agreement on Land, Rail, Marine, and Air Pre-clearance, which, once fully implemented, will see the establishment of pre-clearance operations on both sides of the border for all four modes of transportation. Other customs-related activities include conducting a pilot project on truck cargo pre-inspection along the Canada-U.S. border, reviewing border fees, and harmonising inspections processes for mitigating the risk of wood packaging material pests from offshore.

Other Canadian departments are also involved with their U.S. counterparts on initiatives outside of customs that could, nevertheless, facilitate further the cross-border flow of goods, such as developing harmonised approaches for mitigating plant and animal health risks. In conjunction with the Beyond the Border Action Plan, Canada and the United States established in 2011 the Regulatory Cooperation Council (RCC). A number of joint work plans have been advanced pursuant to the RCC's goal of better aligning the regulatory approaches of the two countries in support of economic competitiveness without compromising the protection of health, safety and the environment.¹⁰⁷

The Auditor General of Canada's 2016 Fall Report examined whether selected departments and agencies, including the CBSA, were making progress in their commitments under the Action Plan to enhance security and expedite the legitimate flow of travel and trade. Overall, the Auditor General concluded that, although a number of the commitments had been met, various departments and agencies were facing challenges and lacked performance indicators to assess results. With respect to trade facilitation, some initiatives had not moved forward significantly, while others were not working as intended or had low adoption rates. In particular, the CBSA's initiatives to extend access to the dedicated FAST lines to all PIP members and to allow companies to have to apply only once to join both its PIPs program and the U.S. C-TPAT program, had been delayed by problems related to information technology (IT) systems. In addition, the adoption by traders of the CBSA's Single Window program had been slower than expected because it was not mandatory and traders faced considerable upfront and ongoing investment costs in IT systems. The CBSA has accepted all the recommendations made by the Auditor General to address the problems in implementing its commitments under the Action.¹⁰⁸

COOPERATION WITH OTHER COUNTRIES AND THE WTO AGREEMENT ON TRADE FACILITATION

The CBSA also actively cooperates with the customs services of other governments, and in the World Customs Organization, on matters related to security and facilitation of trade. For example, Canada has Customs Mutual

Assistance Agreements for exchanging information related to customs fraud with China, the European Union, France, Germany, Israel, Mexico, the Netherlands, South Africa, South Korea and the United States.

On December 16, 2016, Canada ratified the WTO Agreement on Trade Facilitation. The required implementing legislation was enacted on December 12, 2016. Since Canada is already meeting almost all of the provisions of the Agreement, the legislative amendments focussed on the areas of imported non-compliant regulated goods and goods in transit.

North American Free Trade Agreement (NAFTA)

Chapter Five of the North American Free Trade Agreement (NAFTA) sets out the provisions related to the administration and enforcement of the NAFTA rules of origin, which are the responsibility of the CBSA in Canada. These provisions include the Certificate of Origin requirements, the record-keeping requirements for traders, and the origin verification procedures. The Chapter also provides for advance rulings on whether goods qualify as NAFTA originating and hence eligible for the NAFTA tariff preferences. The Chapter also stipulates that producers and traders will have recourse to review and appeal for the origin determinations and advance rulings issued by the customs authorities in the three countries.

The Uniform Regulations provision of Chapter Five was included to ensure uniform and consistent application, administration and enforcement of the rules of origin across the three countries. The three parties jointly prepared the detailed domestic regulations for the NAFTA rules of origin, with the result that these domestic regulations are identical in Canada, Mexico and the United States, except for country-specific references to names of domestic institutions and accounting practices.

The Chapter also establishes a trilateral Working Group on Rules of Origin and Customs Subgroup. The purpose of both is further to ensure effective and consistent administration of the rules of origin and, where needed, to propose amendments to the rules of origin to keep them “always living”. Over the years, the three parties have made amendments to the NAFTA product-specific rules of origin, mainly involving changes to reflect changes in product and production technologies and input availability and sourcing patterns (e.g., emergence of supply chains).

SO HOW IS THE CANADA BORDER SERVICES AGENCY DOING ON CUSTOMS CLEARANCE AND TRADE FACILITATION?

The World Bank’s Logistics Performance Index (LPI) provides a tool to compare Canada’s customs clearance performance with that of other countries. The LPI is based on bi-annual surveys of logistical professionals (i.e., multinational freight forwarders and major express carriers) who operate in foreign countries.¹⁰⁹ The LPI ranks the international logistics performance of 160 countries based on six elements: 1) the efficiency of customs and border management clearance (“Customs”); 2) the quality of trade and transport infrastructure; 3) the ease of arranging competitively priced shipments; 4) the competence and quality of logistics services; 5) the ability to track and trace consignments; and 6) the frequency with which shipments reach consignees within scheduled or expected delivery times (“Timeliness”).¹¹⁰ Countries are ranked from low to high on a scale of one to five.

Table 4 shows the overall LPI and Customs and Timeliness sub-index scores for 2016 for Canada and a number of other major trading developed countries, and for the OECD countries as a group. Table 5 provides the same information on the basis of the weighted average of the scores for 2010, 2012, 2014 and 2016; this is intended to smooth out yearly variations. The other sub-indices are not included in the two tables as they deal with matters that are not likely to be significantly related to the time and efficiency of the customs clearance process.¹¹¹

As shown in Tables 4 and 5, Canada ranked 14th in the overall LPI in 2016, and 13th during the 2010-2016 period, although it would be appropriate not to over-interpret the magnitude of the differences in the scores between countries. The key point is that Canada’s overall performance compares well with that of other developed countries, including those in the European Union (EU) where the scores and ranking reflect responses from logistics professionals involved in internal EU trade as well as external EU trade.

The question asked for the Customs sub-index is: “Rate the efficiency of the clearance process (speed, simplicity and predictability of formalities) by border control agencies, including Customs in ...?”¹¹² As shown in the two tables, Canada ranked 6th in 2016 and 13th for the 2010-2016

period, and above the average for the OECD countries as a group for both periods. The higher ranking in 2016 as compared to the longer period would suggest there has been improvement in Canada's customs performance, following a decline in Canada's score in 2012 and 2014 from that in 2010 (and in 2007, the first year for which LPI scores are available), although it could also reflect a single-year variation. Even taking this possibility into account, Canada's customs performance fares well when compared with that of the United States, major members of the EU and the OECD countries as a group, and ranks above most other countries around the world.

The World Bank's results on Timeliness have been included in Tables 4 and 5 for transparency purposes, but caution is needed in interpreting what this sub-index may say about customs clearance performance, particularly with respect to border release times. The question on "Timeliness" is: "When arranging shipments to ..., how often do they reach the consignee within the scheduled or expected time?"¹¹³ As such, it covers the time it takes for the good to move from the point of exportation to the location of the consignee inside the importing country. The time spent by the good at the customs border point from its arrival to customs release is only one segment of the journey time. There are many factors covering both the journey to the customs border point and the journey after customs release at the border that can affect whether the good reaches the consignee within the scheduled or expected time.

Canada's score and ranking for the Timeliness sub-index for 2016 is 4.01, slightly below the OECD score of 4.09. Canada ranked 25th. Canada's score and rank for this sub-index for the 2010-2016 period are 4.12 and 16, respectively. Looking at the survey results for 2010 through 2014 individually shows a decline over this timeframe in both Canada's score and ranking on Timeliness. In 2010 and 2012, Canada was ranked 5th and 3rd, respectively, but its ranking fell to 11th in 2014, before dropping to 25th in 2016. It is not clear what the reasons are for Canada's relative decline in the Timeliness sub-index over this period; however, the improvement in Canada's score and ranking on the Customs Index in 2016 from those of 2012 and 2014 suggests that the relatively lower score and ranking in 2016 on Timeliness are due to factors other than the time and efficiency of customs release of goods at the border.

This view would appear to be supported by other findings in the World Bank's 2016 LPI study. Table 6 reports for the same countries the results of the LPI survey of logistical professionals operating in the country of importation on clearance time and on the percentage of shipments that undergo physical inspection. For the question on "clearance time", the logistics professionals are asked to provide "an estimate of the average amount of time between the submission of an acceptable customs declaration and the notification of clearance of the shipment".^{114, 115} As Table 6 shows, with zero days (i.e., less than 24 hours) at the border and only three per cent of shipments facing physical inspection, the survey results place Canada's performance in the top ranks of the major developed countries.

Overall, the World Bank's LPI survey suggests that Canada's performance on customs release and clearance compares favourably with that of other major developed countries and ranks high globally.

The OECD has developed Trade Facilitation Indicators (TFIs) for over 150 countries that are designed to measure the extent to which countries have implemented trade facilitation programs and to identify each country's relative strengths and weaknesses in the area of customs processes. These indicators are used to estimate the impact of implementing trade facilitation measures on bilateral trade flows and trade costs. The purpose of these estimates is to help governments prioritise where they should focus their efforts on improving their trade facilitation and where they should target their technical assistance and capacity-building efforts for developing countries. They also offer a tool for assessing the potential impact of implementing the provisions of the WTO Trade Facilitation Agreement.¹¹⁶

The TFIs cover eleven elements of customs processes: advance rulings, appeal procedures, information availability, streamlining of procedures, internal cooperation, external cooperation, fees and charges, simplification of documents, automation, involvement of trade community, and governance and impartiality.¹¹⁷ The OECD has also developed an "average trade facilitation performance index" to measure a country's overall performance. The TFI values range from 0 to 2, with 2 representing the best performance that can be achieved relative to the entire sample of countries included in the study. The OECD published TFIs in 2012 and

released updated TFIs in 2015, based on the most recent data available for each country. This allows the progress in improving a country's performance to be compared to that of other OECD countries.

The TFIs offer insights into each country's relative customs process performance. Table 7 reports the TFIs for Canada, the OECD as a group, the Best Practice Average Top Quartile (henceforth, Best Practice Quartile) and for certain developed countries. Canada's score of 1.7 for Average Trade Facilitation Performance is exceeded only by Australia at 1.8, matches the scores of the United States and the United Kingdom and comes out ahead of the score of 1.6 for Germany, France and Japan. For the other countries listed in the earlier tables but not included in Table 7, the scores are 1.7 for Netherlands and New Zealand, 1.6 for Sweden, South Korea and Italy, 1.5 for Spain and 1.4 for Belgium. In short, on the overall TF indicator, Canada's overall trade facilitation performance compares favourably with that of other top-ranking developed countries.

Also as shown by Table 7, Canada's TFI values provided in the OECD's 2015 report for many of the specific elements compare favourably with those of the OECD average, the Best Practice Quartile and the other individual major OECD countries listed in Table 7. Canada's relatively low 2015 TFI value for automation, however, clouds Canada's overall positive trade TFI (and Canada's relatively high Customs sub-index and ranking in the World Bank's 2016 LPI survey). The decline in Canada's 2015 automation indicator from its score of 2 in 2012 indicates that the progress made by Canada lagged behind that of the Best Practice Quartile and most other OECD countries between 2012 and 2015. The lower relative performance for Canada in 2015 on automation apparently reflects lower scores on the percentage of import and export declarations cleared electronically, and the percentage of procedures that can be expedited electronically, as compared to those of other major OECD countries.¹¹⁸

The up-dated 2015 OECD TFI study covered the 2012-2015 period. The decline in Canada's TFI score on automation could very well reflect the challenges and teething problems that the CBSA faced during this period in introducing or updating its border processing procedures and associated EDI systems. For example, the CBSA only started in early 2015 to interface its EDI systems with those of other

departments under its Single Window initiative, with the last two of the nine departments connected only in late 2016. As noted earlier, traders' adoption of the Single Window program had been slower than expected, and the CBSA experience problems related to its IT systems in its efforts to update its PIP program and FAST.

As regards the other two TFI indicators directly related to border release and clearance formalities, Canada's score of 1.64 for procedures (i.e., streamlining border procedures) exceeds that for the OECD average, the Best Practice Quartile and all the major OECD countries listed in the table except the United States, and represents a significant increase from 1.17 in 2012.

In the case of documents, Canada's score declined from 1.50 in 2012 to 1.33 in 2015. Nevertheless, Canada's 2015 score placed it ahead of that for the OECD average and the United States, Germany, France and Japan, but behind the Best Practice Quartile score of 1.68 and the scores for the United Kingdom and Australia. The main factors for explaining Canada's lower 2015 score on documentation as compared to that of the Best Practice Quartile and the above two countries, apparently relate to the restricted acceptance of the use of copies of documents in either hard or electronic form, the number of required import documents and the fact that Canada has not ratified the 1990 Convention on the Temporary Admission of Goods (Istanbul Convention).¹¹⁹

As regards the other individual TFIs, Canada either maintained or improved its already high TFI value between 2012 and 2015 for the following elements: information availability, streamlining procedures, advance rulings, appeal procedures and governance and impartiality. Canada's TFI values declined for fees and charges, involvement of the trade community and, as noted above, automation and documentation. The OECD does not report 2012 values for internal and external cooperation.

Overall, the OECD TFI indicators for Canada would appear to support the view that Canada's customs clearance processes and trade facilitation efforts compare positively to those of the major OECD countries.

FINAL OBSERVATION

As a last word, the CBSA, like all customs services around the world, continues to face a challenging and ever-changing environment in meeting its dual mandate of safeguarding security and safety while expediting and facilitating trade to support economic progress. As discussed above, this has required on-going changes in the way the CBSA manages and operates its border release and clearance programs and systems. The one certain thing is that the need for continuing to adapt and improve on an on-going basis will remain a constant demand on the CBSA and its resources.

Table 1: Examples of Commonly Imported Regulated Goods and Their Associated Federal Government Department or Agency

| DEPARTMENT, AGENCY OR PROGRAM | PRODUCTS |
|--|---|
| Canadian Firearms Program | Firearms |
| Canadian Heritage | Cultural Products |
| Canadian Food Inspection Agency | Food, plants, animals and related products Food Labelling and Food Recalls Wood Packaging International Waste and Used Machinery/equipment |
| Canadian Nuclear Safety Commission | Radioactive isotopes |
| Competition Bureau Canada | Clothing Labels Marking of Precious Metals Packaging and Labelling of Non-Food Products |
| Controlled Goods Program | Goods and technologies that have military or national security significance |
| Environment and Climate Change Canada | Endangered or threaten plant and animal species Hazardous waste and recyclable material Ozone-depleting substances (ODS) and products containing ODS Wild animal and plant trade |
| Global Affairs Canada | Agricultural products, firearms and other goods under trade controls or embargoes Monitoring of imports of steel and textile and clothing |
| Health Canada | Consumer goods, drugs, food, medical devices, natural health products, pesticides, pharmaceuticals, radiation-emitting devices, toxic substances, vitamins |
| Innovation Science and Economic Development Canada | Radio communications Telecommunications Equipment |
| National Energy Board | Butane, ethane, electricity, gas, oil and propane |
| Natural Resources Canada | Explosive (including fireworks) and ammunition Minerals and metals Regulated energy-using products |
| Transport Canada | Transportation of dangerous goods Vehicles and tyres |

Source: Canada Border Services Agency: <http://www.cbsa-asfc.gc.ca/import/reflist-listeref-eng.html>.

Table 2: Information About the Good Required by the Canada Border Services Agency

- » Vendor (name and address)
- » Date of direct shipment to Canada
- » Other references (include purchaser's order number)
- » Consignee (name and address)
- » Purchaser's name and address (if other than consignee) and their Business Number (BNN)
- » Country of transshipment
- » Country of origin of goods
- » Transportation mode and place of direct shipment to Canada
- » Conditions of sale and terms of payment (i.e. sale, consignment shipment, leased goods, etc.)
- » Currency of settlement
- » Number of packages
- » Detailed specification of the goods (kind of packages, marks and numbers, general description and characteristics (i.e., grade, quality), and condition of good if not new), and tariff classification
- » Quantity (state unit)
- » Selling price: Unit price and total invoice price
- » Total weight—Net and Gross
- » Commercial Invoice Number
- » Exporter's name and address (if other than vendor)
- » Originator (name and address)
- » Any applicable CBSA rulings (e.g., advance ruling on tariff classification)
- » Transportation charges, expenses and insurance from the place of direct shipment to Canada, and to place of direct shipment to Canada
- » Costs for construction, erection and assembly incurred after importation into Canada
- » Export packing cost
- » Amounts for commissions other than buying commissions
- » Identify if royalty payments or subsequent proceeds are paid or payable by the purchaser, or if the purchaser has supplied goods or services for use in the production of these good

Source: Canada Border Services Agency: <http://www.cbsa-asfc.gc.ca/publications/dm-md/d17/d17-1-4-1-eng.html> and <http://www.cbsa-asfc.gc.ca/publications/dm-md/d17/d17-1-4-eng.html>.

Notes: The CBSA allows some exceptions to meeting all of these information requirements in certain situations, such as for shipments below CDN\$ 2,500.

Table 3: Prescribed Time-Lines for Submitting Advance Cargo and Conveyance Data

| MODE | TYPE OF DATA | TIMEFRAME |
|-------------------|---------------------------|---|
| Marine | Cargo and data | <ul style="list-style-type: none"> » 24 hours prior to loading in the foreign port (except US ports) for containerised cargo; » 24 hours prior to arrival for containerised cargo loaded in US ports; » Different timeframes sometimes apply to other types of cargo (e.g., bulk, break bulk) and empty containers depending on where the cargo was loaded |
| | Conveyance data | <ul style="list-style-type: none"> » 96 hours prior to arrival for conveyances with containerised cargo, 24 hours in the case of cargo loaded in the United States » Different timeframes may apply to conveyances carrying other types of cargo (e.g., bulk, break bulk) and empty containers depending on where the cargo is loaded |
| Air | Cargo and conveyance data | <ul style="list-style-type: none"> » Four hours prior to arrival for flights longer than four hours » Before aircraft's time of departure for flights less than four hours |
| Highway | Cargo and conveyance data | » One hour before arrival at the border |
| Rail | Cargo and conveyance data | » Two hours before arrival at the border |
| Freight forwarder | House bill data | » Within the timeframes prescribed for each mode (see above) |

Source: Canada Border Services Agency, Advance Commercial Information, <http://www.cbsa-asfc.gc.ca/prog/aci-ipecc/menu-eng.html>.

Table 4: World Bank's Logistics Performance Index (LPI): Overall Index and Customs and Timeliness Sub-Indexes: Canada and Selected Countries: 2016

| COUNTRY | OVERALL LPI | RANKING | CUSTOMS | RANKING | TIMELINESS (FROM POINT OF EXPORT TO CONSIGNEE) | RANKING |
|-----------------------------|-------------|---------|---------|---------|--|---------|
| Canada | 3.93 | 14 | 3.95 | 6 | 4.01 | 25 |
| United States | 3.99 | 10 | 3.75 | 16 | 4.25 | 11 |
| United Kingdom | 4.07 | 8 | 3.98 | 5 | 4.33 | 8 |
| Germany | 4.23 | 1 | 4.12 | 2 | 4.45 | 2 |
| Sweden | 4.20 | 3 | 3.92 | 8 | 4.45 | 3 |
| Belgium | 4.11 | 6 | 3.83 | 13 | 4.43 | 4 |
| Netherlands | 4.19 | 4 | 4.12 | 3 | 4.41 | 5 |
| France | 3.90 | 16 | 3.71 | 17 | 4.25 | 13 |
| Italy | 3.76 | 21 | 3.45 | 27 | 4.03 | 22 |
| Spain | 3.73 | 23 | 3.48 | 24 | 4.00 | 26 |
| Norway | 3.73 | 22 | 3.57 | 20 | 3.77 | 39 |
| South Korea | 3.72 | 24 | 3.45 | 26 | 4.03 | 23 |
| Japan | 3.97 | 12 | 3.85 | 11 | 4.21 | 15 |
| Australia | 3.79 | 19 | 3.54 | 22 | 4.04 | 21 |
| New Zealand | 3.39 | 37 | 3.18 | 37 | 4.12 | 19 |
| High-Income Countries: OECD | 3.75 | n.a | 3.57 | n.a. | 4.09 | n.a |

Source: Arvis et al, 2016.

Notes: The other top 15 countries for the overall LPI not listed in the table are Luxembourg (2), Singapore (5), Austria (7) and Hong Kong SAR, China (9), Switzerland (11), United Arab Emirates (13) and Finland (15).

Table 5: World Bank's Logistics Performance Index (LPI): Overall Index and Customs and Timeliness Sub-Indexes: Canada and Selected Countries: Weighted mean Scores for 2010, 2012, 2014 and 2016:

| COUNTRY | OVERALL LPI | RANKING | CUSTOMS | RANKING | TIMELINESS | RANKING |
|-----------------------------|-------------|---------|---------|---------|------------|---------|
| Canada | 3.90 | 13 | 3.79 | 13 | 4.12 | 16 |
| United States | 3.95 | 9 | 3.73 | 15 | 4.21 | 10 |
| United Kingdom | 4.02 | 7 | 3.92 | 5 | 4.32 | 7 |
| Germany | 4.17 | 1 | 4.07 | 2 | 4.41 | 2 |
| Sweden | 4.08 | 4 | 3.48 | 9 | 4.37 | 4 |
| Belgium | 4.06 | 6 | 3.82 | 10 | 4.38 | 3 |
| Netherlands | 4.12 | 2 | 4.03 | 3 | 4.36 | 5 |
| France | 3.88 | 14 | 3.68 | 17 | 4.21 | 11 |
| Italy | 3.72 | 21 | 3.41 | 24 | 4.04 | 19 |
| Spain | 3.71 | 22 | 3.51 | 21 | 4.03 | 22 |
| Norway | 3.80 | 17 | 3.74 | 14 | 4.01 | 24 |
| South Korea | 3.70 | 24 | 3.45 | 23 | 4.01 | 23 |
| Japan | 3.95 | 10 | 3.81 | 12 | 4.22 | 8 |
| Australia | 3.79 | 18 | 3.64 | 19 | 4.04 | 20 |
| New Zealand | 3.48 | 31 | 3.45 | 22 | 3.94 | 28 |
| High-Income Countries: OECD | 3.71* | n.a | 3.55 | n.a. | 4.05 | n.a. |

Source: Arvis et al, 2016.

Notes:

- a) To calculate the mean score, each year's scores in each component were given the following weights: 6.7 per cent for 2010, 13.3 per cent for 2012, 26.7 per cent for 2014, and 53.3 per cent for 2016.
- b) *calculated by applying the above weights to the overall score for each year for the High-Income: OECD.
- c) The other top 15 countries for the overall LPI not listed in the table are Singapore (3), Luxembourg (5), and Hong Kong SAR, China (8), Austria (11), Switzerland (12), and Finland (15).

Table 6: World Bank Logistics Performance Index: Number of Customs Forms, Clearance Time, and Percentage of Shipments Subject to Inspections: 2016

| COUNTRY | CLEARANCE TIME (DAYS)* WITHOUT PHYSICAL INSPECTION* | CLEARANCE TIME (DAYS) WITH PHYSICAL INSPECTION | PERCENTAGE OF ALL IMPORTS SHIPMENTS SUBJECT TO PHYSICAL INSPECTION | PERCENTAGE OF SHIPMENTS SUBJECT TO PHYSICAL INSPECTIONS SUBJECT TO MULTIPLE INSPECTIONS |
|-----------------------------|---|--|--|---|
| Canada | 0 | 3 | 3 | 1 |
| United States | 1 | 2 | 4 | 3 |
| United Kingdom | 1 | 1 | 4 | 2 |
| Germany | 1 | 2 | 3 | 2 |
| Sweden | 0 | 1 | 2 | 2 |
| Belgium | 1 | 2 | 2 | 1 |
| Netherlands | 0 | 1 | 2 | 1 |
| France | 1 | 2 | 3 | n.a |
| Italy | 1 | 2 | 4 | 2 |
| Spain | 1 | 1 | 5 | 3 |
| Norway | 0 | 1 | 1 | 1 |
| South Korea | n.a. | n.a. | n.a. | n.a. |
| Japan | 1 | 2 | 1 | 1 |
| Australia | 2 | 4 | 3 | 1 |
| New Zealand | n.a. | n.a. | n.a. | n.a. |
| High-Income Countries: OECD | n.a | n.a | n.a | n.a |

Source: Arvis et al (2016)

Notes: * zero indicates less than 24 hours; 1 indicates 24 to 48 hours, etc.

Table 7: OECD Trade Facilitation Performance Indicators for Canada, OECD, Best Practice Quartile and Selected OECD Countries

| | CANADA | OECD | BEST PRACTICE AVERAGE TOP QUARTILE | UNITED STATES | UNITED KINGDOM | GERMANY | FRANCE | JAPAN | AUSTRALIA |
|--|--------|------|--|---------------|-------------------|---------|--------|-------|-----------|
| Average Trade Facilitation Performance | 1.7 | n.a. | n.a | 1.7 | 1.7 | 1.6 | 1.6 | 1.6 | 1.8 |
| Information Availability | 1.83 | 1.49 | 1.88 | 1.67 | 1.67 | 1.39 | 1.61 | 1.71 | 1.89 |
| Formalities—Procedures | 1.64 | 1.26 | 1.55 | 1.67 | 1.22 | 1.18 | 1.57 | 1.50 | 1.35 |
| Formalities—Automation | 1.29 | 1.64 | 1.92 | 1.71 | 1.43 | 1.71 | 1.57 | 1.14 | 1.71 |
| Formalities—Documents | 1.33 | 1.26 | 1.68 | 1.17 | 1.50 | 1.20 | 0.86 | 1.17 | 1.43 |
| Fees and Charges | 1.50 | 1.54 | 1.80 | 1.50 | 1.67 | 1.75 | 1.33 | 1.75 | 1.75 |
| Advance Rulings | 2.00 | 1.60 | 1.83 | 2.00 | 2.00 | 1.90 | 2.00 | 1.70 | 1.56 |
| Appeal Procedures | 1.67 | 1.77 | 1.89 | 1.50 | 2.00 | 1.20 | 2.00 | 2.00 | 2.00 |
| Governance and Impartiality | 2.00 | 1.76 | 1.90 | 1.50 | 1.89 | 2.00 | 2.00 | 2.00 | 2.00 |
| Cooperation—Internal | 2.00 | 1.51 | 2.00 | 1.89 | 1.67 | 1.50 | 1.25 | 1.50 | 2.00 |
| Cooperation—External | 2.00 | 1.62 | 1.74 | 1.80 | 2.00 | 2.00 | 2.00 | 2.00 | 2.00 |
| Involvement of Trade Community | 1.60 | 1.58 | 1.95 | 1.60 | 1.60 | 1.40 | 1.60 | 1.60 | 1.60 |

Source: OECD: Trade Facilitation Index, Compare Your Country: <http://www2.compareyourcountry.org/trade-facilitation>, last accessed December 20, 2016

Notes:

a) 2 is best performance that can be achieved

b) Definitions:

- Advance rulings: Prior statements by the administration to requesting traders concerning the classification, origin, valuation method, etc., applied to specific goods at the time of importation; the rules and process applied to such statements
- Appeal procedures: The possibility and modalities to appeal administrative decisions by border agencies
- Cooperation—External: Co-operation with neighbouring and third countries
- Cooperation—Internal: Cooperation between various border agencies of the country; control delegation to customs authorities
- Fees & charges: Disciplines on the fees and charges imposed on imports and exports

- Formalities (Automation): Electronic exchange of data; automated border procedures; use of risk management
- Formalities (Documentation): Simplification of trade documents; harmonisation in accordance with international standards; acceptance of copies
- Formalities (Procedures): Streamlining of border controls; single submission points for all required documentation (single windows); post-clearance audits; authorised economic operators
- Governance & impartiality: Customs structures and functions; accountability; ethics policy
- Information availability: Publication of trade information, including on internet; enquiry points
- Involvement of the trade community: Consultations with traders

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2. In order to satisfy the requirements of Article XXIV GATT.
3. <http://www.g20.utoronto.ca/2016/160710-trade.html>.
4. Rishi Sunak, Centre for Policy Studies, *The Free Ports Opportunity* <http://www.cps.org.uk/publications/reports/the-free-ports-opportunity/>
5. For example <https://www.theguardian.com/politics/2016/nov/21/hard-brexite-britain-poorer>
6. http://trade.ec.europa.eu/doclib/docs/2006/september/tradoc_113456.pdf
7. GATT article XXIV (8).
8. GATT article XXIV(5)(b).
9. There remains a risk of claims arising out of the determination of the UK's share of schedules of quotas at the WTO, both NVNI type claims and claims of violation of the WTO Agreement on Agriculture.
10. This is subject to further work by the Special Trade Commission and our partners in modelling the impact on costs and profitability.
11. Written statement by Dr Liam Fox (Secretary of State for International Trade and President of the Board of Trade) 12 December 2016 <https://www.parliament.uk/business/publications/written-questions-answers-statements/written-statement/Commons/2016-12-05/HCWS316/>
12. Society of Motor Manufacturers and Traders data for 2015 <https://www.smmt.co.uk/2016/01/best-year-in-a-decade-for-british-car-manufacturing-as-exports-reach-record-high/>
13. <http://www.civitas.org.uk/content/files/potentialpostbrexittariffcostsforeuuktrade.pdf>
14. Business for Britain *Change or Go* <http://forbritain.org/cogwholebook.pdf>, based on 2013 trade.
15. https://www.global-counsel.co.uk/sites/default/files/analysis/insight/download/GC_HSF_BCG_Trade_post-Brexit.pdf, <https://www.ft.com/content/c397f174-9205-11e6-a72e-b428cb934b78>
16. Though is less for some, for example lights and electronic components at 2.7%.
17. Regulation (EU) No 952/2013
18. Article 210 UCC.
19. Article 256 UCC.
20. Article 259 UCC.
21. Article 211(4)(b) UCC.
22. Article 167 UCC Delegated Regulation 2015/2446.
23. Annex 71-02 UCC Delegated Regulation.
24. https://www.wto.org/english/docs_e/legal_e/24-scm.pdf
25. *Pink Book 2015* table 9.2.
26. <https://fullfact.org/europe/how-many-businesses-export-eu/>
27. See Business for Britain *Change or Go* chapter 27 for analysis of this: forbritain.org/cogwholebook.pdf
28. Article 3 WTO Agreement on Subsidies and Countervailing Measures.
29. Article 4 WTO Agreement on Subsidies and Countervailing Measures.
30. Article 60(1) UCC.
31. Article 60(2) UCC.
32. Annex 22-01 Delegated Regulation.
33. Article 34 Delegated Regulation.
34. Article 64(2) UCC. For countries that benefit from unilateral preferential measures under the GSP and similar, the rules of origin are set out in Article 37 of the Delegated Regulation.
35. Under which 99% of tariffs between the parties will be eliminated; 98% immediately on the agreement coming into force.
36. CETA Protocol on Rules of Origin and Origin Procedures, articles 2 and 4.
37. CETA Annex 5.
38. CETA Protocol on Rules of Origin and Origin Procedures, article 6.
39. By agreeing with the counterparty states to do so.
40. http://ec.europa.eu/taxation_customs/business/calculation-customs-duties/rules-origin/general-aspects-preferential-origin/common-provisions_en
41. <http://www.productivity.govt.nz/sites/default/files/trans-tasman.pdf>
42. https://ec.europa.eu/growth/single-market/goods/new-legislative-framework_en

43. Recital 5, Decision No 768/2008/EC of the European Parliament and the Council on a common framework for the marketing of products.
44. http://ec.europa.eu/growth/single-market/european-standards/harmonised-standards_en
45. *Blue Guide* section 3.1.
46. Proposal for a Regulation of the European parliament and Council on the approval and surveillance of motor vehicles and their trailers, and of systems, components and separate technical units intended for such vehicles COM(2016)31 Final.
47. https://www.seco.admin.ch/...EU/...EU.../MRA_CH-EU_cons_EN_version.pdf
48. For a detailed examination of this area see Andrew Chapman 'Conformity Assessment and the WTO Option' <http://doortofreedom.uk/conformity-assessment-and-the-wto-option>
49. *Blue Guide* section 5.2.2.
50. *Blue Guide* section 5.2.5.
51. <https://standards.cen.eu/dyn/www/f?p=CENWEB:5>
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53. <http://www.bsigroup.com/en-GB/about-bis/uk-national-standards-body/EUReferendum/>
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60. <https://www.ft.com/content/3876648e-9905-11e6-8f9b-70e3cabccfae>
61. <http://webarchive.nationalarchives.gov.uk/20120207131416/http://www.hmrc.gov.uk/jccc/cips/2011/cip-11-24.pdf>
62. World Economic Form *Global Enabling Trade Report* 2016 <http://reports.weforum.org/global-enabling-trade-report-2016/enabling-trade-rankings/n> see also tables 5 and 6 of Appendix 2.
63. World Bank *Doing Business* 2016 <http://www.doingbusiness.org/data/exploretopics/trading-across-borders>
64. World Bank *Doing Business* 2016 <http://www.doingbusiness.org/data/exploretopics/trading-across-borders>
65. In accordance with Article 38(7) of the UCC.
66. http://ec.europa.eu/taxation_customs/business/international-affairs/international-customs-cooperation-mutual-administrative-assistance-agreements/china_en
67. According to the World Bank Logistics Performance Index, the UK carries out physical inspections on just 4% of all import shipments and Ireland inspects just 1% https://wb-lpi-media.s3.amazonaws.com/LPI_Report_2016.pdf
68. Canada Border Services Agency, *What We Do*: <http://www.cbsa-asfc.gc.ca/agency-agence/what-quoi-eng.html>, last accessed 4 December, 2016.
69. *ibid*. Sixty-one of the land-border crossings and ten of the airport sites operate 24 hours a day, seven days a week.
70. As stated in the CBSA's 2015-2016 *Departmental Performance Report*: "The Risk Assessment program "pushes the border out" by seeking to identify high-risk people, goods and conveyances as early as possible in the travel and trade continuum to prevent inadmissible people and goods from entering Canada." See Canada Border Service Agency (2016a).
71. There are several exceptions to Article I:1 of the GATT 1994. Article XX permits measures adopted for public policy reasons. Article XXI permits measures adopted for reasons of national and international security. Article XXIV:5 permits measures necessary to the formation of a valid customs union or free trade agreement, including duties reduced or eliminated in accordance with such an agreement. The Enabling Clause permits measures granting tariff preferences to developing countries, on a non-discriminatory basis between these developing countries. Measures may also be permitted under a waiver granted by WTO Members in accordance with Article IX:3 of the WTO Agreement.
72. WTO Appellate Body Report, *Canada—Automobiles*, WT/DS139/AB/R, adopted 19 June 2000, para 66.
73. *Ibid*, para 79.

74. *Ibid*, para 92
75. In *Canada—Automobiles*, *ibid*, para 92, the Appellate Body rejected an argument by Canada that footnote 1, on which see below, applied by analogy to products destined for the domestic market.
76. In saying that the described practice 'shall not be deemed to be a subsidy', footnote 1 could be taken to mean that the described practice may still be a subsidy even if it is not 'deemed' to be a subsidy. This language must however be read in the context of Article 1, which states that '[f]or the purpose of this Agreement, a subsidy shall be deemed to exist if: ...'. Footnote 1 should therefore be understood as meaning that the described practice 'shall be deemed not to be a subsidy'.
77. Duty drawback on imported final products upon their export was established in s4 of the United States Tariff Act 1789, the second piece of legislation enacted by US Congress.
78. The destination principle explain why some countries permit the refund of domestic sales taxes on products that are exported (e.g. by tourists), and charge an equivalent to a sales tax on imports of products that will not be re-exported (e.g. by tourists returning home, although usually there is a personal allowance).
79. Note that the definition of 'articles' for border tax adjustment purposes is narrower than that of 'inputs' for duty drawback purposes. See note 81 below.
80. It could be argued that the most favoured nation obligation requires a duty drawback to be granted to all like imported products, regardless of whether they are destined for export or domestic sale. However, this would nullify the effect of Footnote 1 of the SCM Agreement contrary to the General Interpretive Note to Annex 1A of the GATT 1994, which states that '[i]n the event of conflict between a provision of the General Agreement on Tariffs and Trade 1994 and a provision of another agreement in Annex 1A [which includes the SCM Agreement], the provision of the other agreement shall prevail to the extent of the conflict.'
81. The paragraphs of Annex I are variously enumerated as 'paragraph' and 'Item'.
82. Annex II establishes guidelines for national investigating authorities making determinations as to whether there have been 'excess' remissions or drawbacks. It also contains some definitions that have proved controversial. In particular, footnote 61, attached to the title of Annex II states: '[i]nputs consumed in the production process are inputs physically incorporated, energy, fuels and oil used in the production process and catalysts which are consumed in the course of their use to obtain the exported product.' Some developing country WTO Members have read the term 'catalysts' in this footnote as including capital goods. This interpretation has been rejected by other WTO Members, on the grounds, *inter alia*, that footnote 61 was drafted expressly to exclude capital goods. See, e.g., the discussion in the *Chairman's Report on the Implementation-Related Issues Referred to the Committee on Subsidies and Countervailing Measures* in the 15 December 2000—*Decision of the General Council, G/SCM/34*, 3 August 2001.
83. Dominic Coppens, *WTO Disciplines on Subsidies and Countervailing Measures* (Cambridge: CUP, 2014) 133.
84. Annex III elaborates on this exception, establishing guidelines for national authorities determining whether substitution drawback systems are export subsidies.
85. This agreement was signed on 30 October 2016 but is not yet provisionally applied or in force.
86. LSE Enterprise Ltd, *An Assessment of the EU-South Korea FTA*, Study for the European Parliament, 2010 (EXPO/B/INTA/FWC/2009-01/Lot7/01-02-03 consolidated), 102.
87. Article 14 of the Protocol concerning the definition of 'originating products' and methods of administrative co-operation to the EU-Korea free trade agreement, provisionally applied since 1 July 2011 [2011] OJ L127/6.
88. We wish to thank Carol Osmond for all her valuable comments and suggestions. All views, errors and omissions in this paper remain the sole responsibility of us, the two authors.
89. During 2011–2015, exports of goods made up about 33 per cent of Canada's Gross Domestic Product (GDP), expenditure based. Services exports accounted for around 6 per cent. Imports of goods were about 35 per cent of GDP, with imports of services around 8 per cent of GDP.
90. All import and export data cited in this paper are sourced from Statistics Canada and the US Census Bureau.
91. See Baldwin and Yan (2016).
92. Canada Border Services Agency, *What We Do*: <http://www.cbsa-asfc.gc.ca/agency-agence/what-quoi-eng.html>, last accessed 4 December, 2016.
93. *Ibid*. Sixty-one of the land-border crossings and ten of the airport sites operate 24 hours a day, seven days a week.
94. About 69 per cent of Canadian tariff lines are MFN free. Imports from specific countries can also enter Canada duty-free under its various free trade agreements and other preferential regimes (e.g., for developing and least developed countries). In 2015, more than 85 per cent of total imports entered duty-free, and over 95 per cent of imports from the United States crossed the border without paying duties. The main taxes collected at the border are federal and provincial value-added sales taxes (e.g., Federal Goods and Services Tax). Certain other products, for example alcoholic beverages, also face excise duties and taxes. Given the high percentage of goods entering Canada duty-free and its relatively low MFN tariff rates for most of the remaining dutiable goods, over 75 per cent of the revenue collected

by the CBSA is related to consumption taxes (see World Customs Organization, 2016).

95. Arvis et al, 2016, page 3
96. As stated in the CBSA's 2015-2016 *Departmental Performance Report*: "The Risk Assessment program "pushes the border out" by seeking to identify high-risk people, goods and conveyances as early as possible in the travel and trade continuum to prevent inadmissible people and goods from entering Canada." See Canada Border Service Agency (2016a).
97. World Customs Organization (2016), WCO Member Profiles:E-Customs.
98. see Canada Border Services Agency, *Pre-Arrival Review System under Other Service Options* at http://www.cbsa-asfc.gc.ca/import/services-eng.html#opt_01, last accessed December 11, 2016. While data are not provided for pre-arrival submissions, the CBSA reported that in 2015/16, 74 per cent of the 622,981 post-arrival RMD requests met the CBSA standard of providing a release decision with 45 minutes of receiving a post-arrival electronic request. CBSA Service Standards, Fiscal Year 2015-2016, <http://www.cbsa-asfc.gc.ca/services/servir/standards-normes-2015-2016-eng.html>, last accessed December 14, 2016.
99. The eligibility criteria include residency in either Canada or the U.S., a history of actively importing for at least 90 days, and no history of contraband activity. Carriers are also required to own and control their own dispatch system.
100. The main difference between CDRP and FAST is that the former was created to handle CSA shipments before FAST was established and is valid only for entry into Canada. Since FAST is a joint initiative between Canada and the United States, its membership card is recognised in both countries.
101. As is the case in all customs importation circumstance, customs border officers retain the right to seek additional information about the shipment and its goods at the time of arrival before making a release decision, and to detain the goods until any outstanding matters are resolved.
102. Sufferance warehouses are privately owned and operated facilities licensed by the CBSA for the short-term storage and the examination of imported goods not yet released by the CBSA.
103. See sections on F Appendix and G Appendix *Pre-Clearance Programs in Importation of Motor Vehicles*, Memorandum D19-12-1, <http://www.cbsa-asfc.gc.ca/publications/dm-md/d19/d19-12-1-eng.html>, last accessed December 18, 2016.
104. On the Canadian side, in addition to the CBSA, the Canadian Food Inspection Agency, Citizenship and Immigration Canada, Global Affairs Canada, the Privy Council of Canada, the Royal Canadian Mounted Police, Public Safety Canada and Transport Canada are participating in the Border Action Plan. The U.S. counterparts are the U.S. Coast Guard, U.S. Customs and Border Protection, U.S. Department of Agriculture, U.S. Immigration and Customs Enforcement, U.S. State Department and the U.S. Transportation Security Administration.
105. For more information, including on the customs related initiatives, see Public Safety Canada (2016a and 2016b).
106. The corresponding U.S. programs are the U.S. Importer Self Assessment (ISA) and the U.S. Customs-Trade Partnership Against Terrorism (C-TPAT) programs.
107. For more details on the RCC and the work underway under it, see Treasury Board Secretariat (2016).
108. See Auditor General of Canada (2016).
109. In 2016, 1,051 logistics professionals participated in the LPI survey. See Arvis et al (2016).
110. See Arvis et al (2016) and World Bank (2016).
111. Canada's ranking for the other sub-indices for 2016 and 2010-2016 are, respectively: 9 and 9 for infrastructure; 29 and 28 for ease of arranging competitively priced shipments; 15 and 12 for logistics; and 9 and 16 for tracking and tracing.
112. *ibid.*
113. *ibid.*
114. *ibid.*
115. In this note, the term "release" is equivalent to "customs clearance" as defined for the purposes of this question in the World Bank's LPI index as both refer to when the good can physically leave the border and enter into the country.
116. See OECD (2016).
117. *ibid.*; also see Notes to Table 7.
118. Information obtained directly from the OECD. The OECD's specific 2016 recommendation for Canada on automation was to expand the proportion of export procedures expedited electronically.; see OECD (2016).
119. Information obtained directly from the OECD. The OECD's specific 2016 recommendation for Canada on documentation was to expand the acceptance of the use of copies of documents; see OECD (2016).

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ABOUT THE AUTHORS

Shanker Singham

Shanker Singham is Director of Economic Policy and Prosperity Studies at the Legatum Institute. He is also a trade and competition lawyer as well as an author and adviser to governments and companies. He holds an M.A. in chemistry from Balliol College, Oxford University and postgraduate legal degrees in both the UK and US. He has lectured, written and spoken extensively, including more than one hundred articles and book chapters and the leading textbook on trade and competition policy. He is a frequent contributor on trade issues to major news outlets. Singham has begun work on identifying and quantifying anti-competitive market distortions and how to create the preconditions necessary for wealth creation, competitiveness, and productivity. He is currently the CEO and Chair of the Competere Group, the Enterprise City development company incubated at Babson College. He is based in London.

Victoria Hewson

Victoria Hewson is a Senior Associate at CMS Cameron McKenna LLP, currently seconded to act as counsel to the Legatum Institute Special Trade Commission. In practice, she advises banks and financial institutions on technology, outsourcing and fintech. She has an LLB from University College London. Before becoming a lawyer, she worked for Procter & Gamble in Frankfurt and Newcastle upon Tyne on finance and employee services projects.

ABOUT THE LEGATUM INSTITUTE SPECIAL TRADE COMMISSION

The Legatum Institute Special Trade Commission (STC) was created in the wake of the British vote to leave the European Union. At this critical historical juncture, the STC aims to present a roadmap for the many trade negotiations which the UK will need to undertake now. It seeks to re-focus the public discussion on Brexit to a positive conversation on opportunities, rather than challenges, while presenting empirical evidence of the dangers of not following an expansive trade negotiating path.

The STC draws upon the talent of experienced former trade negotiators from the US, Canada, Mexico, Australia, New Zealand, and Singapore, among other nations.

In the coming few months, the STC will host a number of public briefings that offer advice to key stakeholders on EU negotiations.

THE COMMISSIONERS

Alden Abbott

Deputy Director, Edwin Meese III Center for Legal and Judicial Studies and John, Barbara, and Victoria Rumpel Senior Legal Fellow, Heritage Foundation, USA; former Director of Antitrust Policy, Federal Trade Commission; Legatum Fellow.

Grant Aldonas

Senior Advisor, Center for Strategic and International Studies (CSIS); former Under Secretary for International Trade (George W Bush administration).

Luis de la Calle

Founding Partner and Managing Director, De la Calle, Madrazo, & Mancera, Mexico; former Undersecretary of International Business Negotiations, Ministry of Economy in Mexico; former Minister of Trade Issues, Mexican Embassy, Washington, DC.

Crawford Falconer

Professor of International Trade, Lincoln University; former New Zealand Ambassador to the WTO; former WTO Agricultural Group Chairman.

Nicholas Niggli

Head, Economy, Finance, Science & Innovation, Embassy of Switzerland in the UK; Chairman, Association of Economic Representatives in London (AERL); Visiting Lecturer, INP Executive Masters, Graduate Institute of International & Development Studies; former Chairman, WTO Government Procurement Agreement, Pension Plan Management Board, Committee on Specific Commitments.

Alan Oxley

Managing Director, ITS Global; former Australian Ambassador to Singapore, the UN, and the WTO; co-founder of the Cairns Group; senior fellow, ECIPE.

Razeen Sally

Associate Professor, Lee Kuan Yew School of Public Policy, National University of Singapore; Chairman, Institute of Policy Studies, Sri Lanka; former Chair, World Economic Forum Global Agenda Council on Competitiveness; Director and co-founder of ECIPE.

Francisco Sanchez

Chairman, CNS Global Advisors; former Under Secretary for International Trade (Barack Obama administration).

Shanker Singham

Chairman of the Legatum Institute Special Trade Commission; Director of Economic Policy and Prosperity Studies, Legatum Institute; CEO of Competere; former Managing Director, Competitiveness and Enterprise Cities project, Babson Global.

John Weekes

Senior Business Adviser at the Canadian law firm Bennett Jones; former Canadian Chief Negotiator for NAFTA, Ambassador to the WTO and Senior Assistant Deputy Minister, Department of Foreign Affairs and International Trade.

All commissioners will serve the Commission in an individual capacity.

MISSION STATEMENT

The purpose of the Legatum Institute Special Trade Commission (STC) is to understand and guide the process that the UK and other governments are engaged in as a result of the Brexit referendum.

The Commission will provide the academic firepower to enable a successful process that includes:

1. The UK's relationship with Europe;
2. The relationship with the countries that more holistically embrace open trade, competition on the merits as an organising economic principle, and property rights protection;
3. The bilaterals with other key trading partners;
4. The relationship with the Commonwealth and developing countries; and
5. The underpinning WTO relationship.

The STC's combined expertise and experience, spread over two hundred years and hundreds of trade agreements puts it in a unique position to be a trusted and independent advisor to the series of post-Brexit processes that could and should lead to the creation of a global economic engine.

This realises the Legatum Institute's theory of change which is ultimately driven by the need to lift the global poor out of poverty and to create jobs, hope and opportunity for the world's people through the application of property rights protection and open trade systems that are characterised by competition on the merits as the organising economic principle.

The STC's role is to help shepherd governments, stakeholders and others towards increased global prosperity which is available if the inflection point in history that the Brexit vote represents is capitalised on.



LEGATUM INSTITUTE

11 Charles Street
Mayfair
London W1J 5DW
United Kingdom

t: +44 (0) 20 7148 5400

Twitter: @LegatumInst

www.li.com

www.prosperity.com

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