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Brexit Pulse Update
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Deal or "No Deal"? Preparing for a "No Deal" Brexit

What Could Happen?

The effective deadline for the UK government and Parliament to decide a way forward is Friday 5 April, possibly slipping to Monday 8 April. The European Council will meet on 10 April to assess the situation and decide whether to extend the Article 50 deadline beyond 12 April. It is impossible to predict what governmental and parliamentary manoeuvres will lead to this week.

Prime Minister Theresa May has said that while she intends to discuss Brexit with Labour leader Jeremy Corbyn to find a way out of the deadlock, the offer is also open to other members across Parliament. With resolute opposition from the DUP (which is to do with keeping Northern Ireland's place within the UK, not a particular Brexit concern), and with Labour MPs concerned that if the Prime Minister's deal is approved it will be implemented by a new Prime Minister who favours a harder Brexit, this might work, but formidable obstacles remain. Given the impossibility to make any significant changes to the Withdrawal Agreement element (which the Prime Minister has effectively ruled out), it is difficult to see how the DUP could ever be brought to support it. Labour MPs would be more open if the Political Declaration was re-negotiated to provide more explicitly for a softer Brexit, but that would re-ignite opposition among Conservative MPs.

Among a wide range of potential outcomes, the three most probable are:

- "No deal" Brexit on 12 April, possibly (if the European Council so decides) with a short extension (not beyond 22 May) so that both sides can finalise preparations
- If Parliament has settled a way forward, which the government accepts and the European Council believes credible, a short extension (again, not beyond 22 May) to revise the Political Declaration to take account of the new way forward, contingent on evidence of Parliament's willingness to approve the Withdrawal Agreement
- A much longer (a year or more) delay to the Article 50 timetable, on EU terms (which are likely to include participation in the European Parliament elections in late May), which would be very likely to lead to a change of Conservative Party leader (and Prime Minister), and possibly a General Election; the chances of a referendum to confirm public support for whatever model of Brexit emerges are also growing

Of these potential outcomes, the first and the third look more likely than the second – the standard of proof the European Council would need to see the second as credible looks hard to achieve in such volatile politics in Westminster. The European Council could allow the UK to shorten the third by ratifying the Withdrawal Agreement, thus providing an incentive to get the process moving forward.

Implications for Retailers

The range of options, and timescales, into the week after the UK should have left the EU remains as wide as ever. We are still some way from knowing what future trading relationships will look like. However, any final "no deal" preparatory steps should be taken between now and 12 April – it is not our predicted outcome, but the chances of it happening have increased.

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Top 10 Impacts of Tariffs on Imports

Changes to UK import policy in the event of a "no deal" Brexit will mean an **increase in tariff costs on a range of imports from the EU** (including some important products for retailers, such as meat, dairy, fish, clothing and ceramics) and a **reduction in tariff costs on a much wider range of products from outside the EU**.

1. Tariff rates need to change following a "no deal" Brexit to avoid price rises

The government knows that in the event of a "no deal" Brexit, there is a danger that imports from the EU could cost more because they will become subject to customs duties for the first time. The impact of these new costs would vary from product to product, but overall, on the basis of existing duty rates and existing trade flows, tariffs on imports from the EU would cost UK retailers alone £7.8 billion per year. Most of those new costs would be concentrated on food and drink imports where tariff rates are particularly high.

The government is concerned that new tariff costs would be passed on to the consumer in the form of higher shop prices. It is particularly concerned about the impact on food prices where existing tariffs are high, EU market share is also high, and alternative domestic sources are insufficient. This is an outcome the government is keen to avoid and it is proposing to change the tariff rates it applies to imports from the EU.

2. The government is proposing to scrap most tariffs at least for a temporary period

In seeking to avoid higher consumer prices, the government has decided to reduce the vast majority of its customs duty rates to 0% on a temporary basis. The measure will stay in effect for a year and will cover 87% of tariff lines. This will mean that for most products, there will be no new tariff costs on imports from the EU.

Not all duty rates will be reduced to zero though. Some duty rates will remain unchanged, such as lamb, sugar, bananas, rum, clothing and textiles, and ceramics. Others will be reduced, but not eliminated altogether, such as beef, poultry, pork, rice, some dairy and fish. For all these products, the cost of importing from the EU will increase, and for some products, significantly.

3. Tariff reductions will *reduce* the cost of importing from outside the EU

The new tariff rates the government has announced must apply equally to all so-called "most-favoured nation" (MFN) suppliers, i.e. any country that does not have a trade agreement with the UK and that is not entitled to special tariff treatment by virtue of being a developing country. This includes important supplier countries such as China and the US.

4. Many non-food imports from China will become cheaper, but not clothing and ceramics

China is a major supplier to UK retail in almost every non-food category. Currently, all of its exports to the UK are subject to MFN duty rates. In many cases, existing rates are already quite low and some are already 0%. However, with the exception of clothing and ceramics, all duties on non-food consumer products will be reduced to 0%. The biggest impact will be on footwear costs where the existing 17% duty on imports of footwear will disappear, as will the anti-dumping duty of 48.5% on imports of Chinese bicycles.

5. Large non-EU agricultural producers will benefit from significant reductions in food and drink tariffs

Many of the world's largest agricultural producers currently have very low levels of market share in the UK. In part, this is due to high tariff barriers in the EU, as meat and dairy rates are often in excess of 30%. In the event of a "no deal" Brexit, many of these rates will disappear overnight. Tariffs on fruit, vegetables and wine will disappear completely, and rates on beef, chicken, pork and dairy will be considerably reduced, making imports from MFN supplier countries far more cost competitive on the UK market (while at the same time, imports from the EU will become more expensive as they become subject to the new rates of duty). Nevertheless, regardless of the level of tariffs, imports from outside the EU will still need to meet strict food safety/animal health/plant health regulations in order to be imported.

6. EU meat and dairy suppliers will face new duties

The UK will maintain MFN duties, albeit at lower levels, on most meat and some dairy products. These will represent new costs when importing from the EU. Only lamb tariffs will be maintained at their current level. Beef and poultry duties will be reduced by roughly half. Duties on pork will be substantially reduced, together with duties on butter, some processed cheese and cheddar. In all cases, it appears that the rationale for maintaining at least some level of duty is to provide protection for UK suppliers.

It is worth noting that in addition to new duty rates, the UK will establish "tariff rate quotas" (TRQs) for beef and poultry. They are fixed quantities that are allowed into the UK free of duty. These TRQs can be accessed by both EU and non-EU suppliers.

7. Turkey loses out

Currently, imports from Turkey enter the UK duty free by virtue of Turkey's customs union with the EU. Leaving the EU without a deal would also mean leaving that customs union and, in turn, would require that the UK treats Turkey as an MFN supplier. Consequently, imports of clothing from Turkey would become liable to the UK's MFN tariff rate of 12%.

8. Imports from developing countries are protected

Separate from the announcement of MFN tariffs, the government has already committed to continue offering preferential treatment to imports from developing countries (i.e. even lower tariff rates). For the very poorest countries (e.g. Bangladesh and Cambodia), all goods will continue to be duty free.

Of course, the relative value of this preferential treatment is significantly reduced if every supplier receives it. That explains why, in a few cases, the government has decided to maintain some MFN tariffs on products even where there is no UK production. For example, the decision to maintain MFN tariffs on bananas is so that imports from poor Caribbean producers, who will continue to enjoy duty free access to the UK, will benefit from a cost advantage over imports of bananas from more powerful and competitive multinational producers in South and Central America. The same is true for MFN duties on clothing. These are being maintained largely to ensure that there is a cost differential between supplies from Bangladesh and other least developed countries (LDCs) compared with China.

9. Imports from some preferential trading partners are protected

So far, the government has secured agreement with many countries to extend their EU free trade agreements to the UK post Brexit. This will mean that imports from these countries will receive the same tariff reductions as of now (unless the new MFN rates of duty happen to be lower). The list of countries is being updated daily, but currently includes Chile, South Africa, Iceland, Norway, Switzerland, Israel, and Pacific and Caribbean islands.

10. Imports from other existing preferential suppliers may revert to MFN rates

The UK has been unable to extend the terms of existing EU free trade deals with Canada, South Korea, Japan and Vietnam. Trade with the first three is likely to revert to MFN terms post Brexit, whereas imports from Vietnam could continue to receive preferential tariff treatment if the UK includes them in the list of developing countries to which it granted unilateral tariff preferences.

Conclusion

In the event of a "no deal" Brexit, there will be considerable changes to the UK's tariffs. These will have a negative impact on the cost of sourcing some goods from the EU. On the other hand, they will make the cost of sourcing lower for many countries outside the EU. Companies that understand the detail concerning the changes the government will implement will be in a much better position to exploit the cost reductions on offer and to avoid new tariffs.

Impact of a "No Deal" on UK/EU Borders

A "no deal" Brexit will mean a sharp end to "free circulation" of goods inside the EU's single market, with goods traded between the EU and UK being treated as "imports" and "exports". This will involve a complete reconfiguration of existing customs formalities carried out at EU and UK borders, with the introduction of import declarations, customs checks and – potentially – customs duties.

As things stand at the moment, goods flow within the bloc with little to no customs administrative burdens. British importers and exporters are not required to register their imports or exports, meaning customs declarations and supporting documentation are not needed for every transaction. That will all change, and each such transaction will have to be reported. Importantly, supporting documents are not only confined merely to customs declarations, but will also include, for example, declarations that goods comply with the requirements for placing on the market, are properly labelled and specify their country of origin.

In addition, any customs agents carrying out these tasks will be required to register in the UK, and as the EU would be treated as a third "country", import VAT on goods will become payable at the border. To mitigate this impact, the UK government has introduced some relaxations to enable businesses to account for import VAT on their VAT return rather than at the time the goods arrive at the border. This note provides further details on how businesses will be able to trade with the EU in the event of a "no deal".

Who will bear the costs of any new import duties on either side of the import/export transaction? Will this be the buyer or the seller?

Who will bear the risks of goods being delayed at ports because of additional customs clearance delays and inspections, a crucial consideration in the case of perishable merchandise such as fresh food products? The allocation of these costs and risks must be decided in advance in order to avoid future disputes and potential litigation.

Implications for Retailers

Retailers should, therefore, prepare and plan for increased timeframes, administrative burdens and the potential for new customs formalities to impact existing operations at both the EU and UK borders in the event of a "no deal" Brexit.

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