THE VIEW FROM BRUSSELS: EU-UK TRADE AND COOPERATION AGREEMENT LEVEL PLAYING FIELD PROVISIONS AND THEIR ENFORCEMENT

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Legal Briefings – By **Eric White** and **Lode Van Den Hende**

We now have an agreement on the future partnership between the UK and the EU. It is given the name Trade and Cooperation Agreement (**TCA**) but is, in EU parlance, an Association Agreement – a type of agreement which, in accordance with its legal basis - Article 217 TFEU, involves "reciprocal rights and obligations, common action and special procedures".

At its heart is a classic but not very ambitious free trade agreement – tariff and quota-free trade in goods but little mutual recognition and very modest commitments on services. The real innovations come with the emphasis on preserving the so-called level playing field and with the "special procedures" that it creates for its governance. These are what we discuss below.

THE LEVEL PLAYING FIELD PROVISIONS

The attention paid to the level playing field in the TCA is best explained by the fact that this is uniquely an agreement to manage divergence and not to promote convergence. Other free trade agreements eliminate tariffs and restrictions and try to promote more trade by creating mechanisms to reduce non-tariff barriers – often called technical barriers to trade – arising out of divergent regulations and standards. They therefore set out the conditions under which products conforming to different regulations can be accepted and set up mechanisms to harmonise these regulations and to encourage convergent approaches to future regulation. The situation prevailing at the conclusion of the TCA between the UK and the EU is however fundamentally different. These jurisdictions are starting off with extensively harmonised regulations and deeply integrated markets and the TCA needs to control the way in which they will diverge in the future.

While convergent trends in regulation equalise competitive conditions, divergent trends give rise to relative changes in competitive conditions. The EU feared that the UK, after leaving the EU single market framework, would be able to improve its competitive position while continuing to enjoy the level of market access that was judged appropriate when it had the same regulatory framework as the EU.

The level playing field provisions of the TCA cover competition, subsidies, state-owned enterprises, taxation, labour and social standards, environment and climate and a portfolio of other trade and sustainable development objectives. They are not all treated in the same way.

The competition rules, for example, are brief and general and the emphasis is on domestic enforcement and cooperation between the parties; dispute settlement has been excluded (as for taxation).

The subsidy rules appear to restate in some detail the State aid rules that currently apply in the EU but with the major difference that they are to be assessed according to the effects on trade and investment between the EU and the UK. This creates an entirely new subsidy regime since the existing EU State aid regime only looks at effects within the EU and not those in or with third countries. The EU will have to introduce legislation to implement this new regime (the TCA is not given direct effect in the EU) and that may be one of the reasons behind the European Commission's White Paper on countering foreign State Aid published last June.

The other level playing field objectives reflect many current concerns of the EU and the UK but the strictest and most detailed rules apply to social and labour standards and certain environmental objectives (including climate policy). Here the dominant approaches are, on the one hand, to list certain areas of regulation and require the parties not to "weaken or reduce, in a manner affecting trade or investment between the Parties" its levels of protection below the levels in place at the end of the transition period (the "non-regression obligations") and, on the other hand, to refer to international conventions that the parties commit to comply with and develop.

Such commitments are not unusual in free trade agreements in the case of reference to international conventions or are likely to be controversial in the case of non-regression. The real problem is how to establish whether these objectives and current levels of protection are being undermined by a party's actions and how to deal with the consequences. This is where the TCA really innovates as we examine below.

THE SPECIAL PROCEDURES

The EU originally proposed that the Court of Justice of the European Union would have a decisive say in interpreting any principle included in the TCA that derives from EU law – which in the EU's original draft proposal was naturally a great deal. That was not acceptable to the UK.

The primary enforcement mechanism for subsidies is through independent agencies charged with policing the disciplines in their respective territories and to cooperate with each other. The EU agency will be the European Commission whose role is well known. The UK agency is yet to be established and does not need to operate in the same way as the Commission; in particular it is not required to exercise *ex ante* control over subsidies.

The enforcement of the subsidy disciplines and most other level playing field disciplines (taxation and state-owned enterprises are notable exceptions) is however also required to be possible for private parties through the courts of each party. This is a striking exception to the general principle set out at the beginning of the TCA (Article COMPROV16) that the TCA is not to create rights for private parties. The parties will have to legislate in order to provide the private enforcement rights that they commit to for the level playing field.

Another interesting feature of the TCA provision on the level playing field is the way in which it is enforced between the parties themselves. Reliance on the general dispute settlement mechanism of the TCA appears to have been considered insufficient and is in some cases excluded. This reflects on the one hand the mood of the times, as evidenced by the fact that US criticism of the WTO dispute settlement system as being too slow and ineffective (as well as sometimes allowing the wrong side to win) is being increasingly supported by the EU. It may also be explained by the fact that the questions raised by level playing field obligations are considered by the parties to be more political and not easily susceptible to being resolved through a normal judicial process.

The solution that has been adopted in the level playing field chapters is therefore to provide for special dispute settlement mechanisms, including provision for unilateral retaliation. These are termed "remedial measures" and "rebalancing" in.

In the case of subsidies, a party that considers that a subsidy granted by the other party "causes, or there is a serious risk that it will cause, a significant negative effect on trade or investment between the Parties" may initiate a process that will allow it *unilaterally* to impose remedial measures after 60 days. The TCA requires notice and an opportunity to comment to be given and also that there must be reliable evidence of harm to identifiable goods, services or economic actors and that the measures must be proportionate but this remains a unilateral determination. This is self-judging at least initially and it is up to the other party to initiate a special accelerated arbitration process to determine whether there is indeed evidence of a significant negative effect, whether the measures are proportionate and whether the procedures have been correctly followed. This arbitration process cannot assess the question of whether the alleged subsidy complies with the substantive principles governing subsidies.

In the case of alleged violations concerning the chapters on labour and social rights and environmental policies including climate protection, the TCA provides an additional dispute settlement mechanism involving a review procedure involving a "panel of experts". This special procedure seems to be an optional alternative to the main arbitration provisions of the dispute settlement chapter of the TCA (many of which it incorporates by reference) and its main advantage seems to be that the panel of experts will have specialised knowledge of these matters.

In the case of provisions concerning subsidies and labour and social, environmental or climate protection, the TCA allows "rebalancing" where divergences arise that are **consistent with the TCA** and other international obligations which either party considers impact trade or investment between the Parties in a manner that changes the circumstances that have formed the basis for the conclusion of the TCA (Article 9.3) . There is no obligation of prior resort to other dispute settlement mechanisms, which is logical since this is designed for measures that are consistent with the TCA. Also, this mechanism can be used either because a party improves its regulations or policies and the other does not to follow or because a party weakens its regulations or policies. This is therefore a kind of "non-violation" complaint reminiscent of that envisaged under the original GATT 1947 but rarely used. The level of rebalancing is in principle entrusted to an arbitration panel but if this does not decide on a level of rebalancing within 30 days of its establishment (which is hardly enough time to ensure a proper judicial process and exercise of rights of defence), the complaining party may proceed to unilateral rebalancing (Article 9.4(3)(c)). There is however an obligation to adjust this rebalancing once the arbitration panel has come to a decision.

COMMENT – THE DE-JUDICIALISATION OF DISPUTE SETTLEMENT?

The TCA is breaking new ground in international dispute settlement.

Before the 20th century, the enforcement of international obligations was normally a matter of taking unilateral retaliatory measures, that is, self-help. If one state considered that another had not complied with its international obligations, it unilaterally adopted countermeasures – in other words, it retaliated. This could be by taking peaceful measures that would otherwise be a violation of international law or even by a resort to force. To avoid parties relying on such self-help, the GATT 1947 provided a mechanism for retaliation involving prior authorisation by the contracting parties, acting as a body. Over the years, this was progressively judicialised through the institution of panels and the development of procedures and conventions, culminating in the adoption of the Dispute Settlement Understanding (**DSU**) as part of the WTO Agreements including the creation of a standing Appellate Body.

The development of the GATT into the WTO also led to diminution of self-help specifically in the field of subsidy control. Article VI GATT 1947 allowed countries to continue the practice of countering foreign subsidisation by adopting duties (countervailing duties) on the import of the subsidised goods going beyond the maximum duties they were allowed to impose under their GATT 1947 commitments. Dissatisfaction with how this was done in practice led to the adoption of the Tokyo Round Subsidies Code and later to the WTO Agreement on Subsidies and Countervailing Duties (the **SCM Agreement**). This requires a detailed investigation to be conducted to establish both the existence of subsidisation and any resulting material injury to a domestic industry and that this determination should also be subject to review under the DSU.

The existence of the Appellate Body led to further judicialisation, not only because panels were wary of having their decisions criticised or reversed but also because panels considered themselves bound by the prior decisions of the Appellate Body. As a consequence, substantive and procedural rules were refined and developed through the case-law. Complexity increased so that neither panels nor the Appellate Body could keep to the tight timelines set out in the DSU.

The EU was originally an enthusiastic supporter of this judicialisation of the settlement of trade dispute, which it saw as promoting the rule of law over that of power politics, and greatly contributed to the development of this mechanism through its systematic participation in all WTO dispute settlement proceedings.

More recently, however, the WTO dispute settlement mechanism has fallen victim to criticism from the US which loudly protests that the WTO case law is moving the law away from what it considers it agreed to in 1994. The US evidently opposes the concept of WTO law developing over time based on the experience of past cases.

The TCA is re-introducing self-help into trade disputes that prior agreements have sought to eliminate and in this sense can be considered as something of a regression from existing standards. One striking recognition of this in the provisions on the level playing field is the prohibition on the parties invoking the WTO or any other international agreement against the taking of remedial measures imposed in response to subsidisation (Article 3.12.13) and against rebalancing measures (Article 9.4(3)(g)) (a prohibition that is repeated in other parts of the TCA).

Another noteworthy feature of the TCA provisions on the level playing field is the assumption that trade is a matter to be decided between sovereigns – who may consult with each other but then decide sovereignly on retaliation, remedial measures and rebalancing. In reality, however, trade is a matter of concern for economic operators. Trade disputes originate in protests from economic operators and action taken in response to these protests affects the interests of multiple other economic operators as well as the protestor. That is why developed countries conduct open investigations allowing the participation of all interested parties before taking trade action, something that does not seem to be contemplated in the TCA or in the EU Decision on signature and provisional application. And because countries do not take account of the interests of foreign economic operators as much as they do of their own, independent arbitration is required by most modern trade agreements before retaliatory action is allowed.

A party wishing to take remedial or rebalancing action under the TCA is likely to find that this action affects economic operators who will oppose the action politically and possibly even legally in the domestic courts. Also, if remedial or rebalancing action is taken that the other considers unjustified then there will be a strong temptation for the other to do likewise; the opportunities to do so will not be difficult to find.

The level playing field provisions of the TCA are a reflection of the attitudes of the parties who negotiated it and their current concerns. They contain many innovations compared to previous agreements. However, whether and how they are used over time remains to be seen.

Beyond Brexit Hub

KEY CONTACTS

If you have any questions, or would like to know how this might affect your business, phone, or email these key contacts.

ERIC WHITE
CONSULTANT, BRUSSELS
+32 477 883 993
eric.white@hsf.com

LODE VAN DEN HENDE
PARTNER, BRUSSELS

+32 477 883 709
Lode.VanDenHende@hsf.com

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