CLIFFORD CHANCE

THE EU TRADE PROCESS EXPLAINED

AUGUST 2020

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PART I: INTRODUCTION TO EU TRADE

THE EU TRADE PROCESS EXPLAINED

This briefing paper provides an overview of the European Union's role in trade policy on behalf of its Member States, the process by which it undertakes different aspects of that policy, and the roles of the various EU institutions.

What is the European Union?

The European Union (EU) is the name given to the formal association of 27 European countries, or Member States, who have chosen to pool their sovereignty in certain (primarily economic) policy areas. The establishment and operation of the EU is based on intergovernmental treaties.

What is the EU's role in trade?

Trade policy is an exclusive EU competence, much of which falls under the Common Commercial Policy, or 'CCP'. The EU legislates on trade policy on behalf of the EU Member States and enters into bilateral and multilateral trade agreements on their behalf. The EU represents the Member States diplomatically and legally at the World Trade Organization (WTO).

Why is the EU's role in trade important?

The EU is the world's largest trading bloc, and its second largest economy (after the USA).

By acting as one in the international trade arena, EU Member States hold an enormous voice in this part of the world stage.

For businesses seeking to understand or influence international trade law and policy, an understanding of the EU trade policy process is critical.

Evolution of the EU's trade competence

- **1948** – The General Agreement on Tariffs and Trade (GATT) signed, establishing global rules on the trade in goods and setting some limits on the tariffs countries can apply to each others' goods.
- **1951** – The Treaty of Paris creates the European Coal and Steel Community – a common market for coal and steel between the six signatory countries (measures included prohibiting tariffs, export and import restrictions, and controls on State aid).
- **1957** – The Treaty of Rome establishes a common market, on almost all goods, moving between the six founding members of the European Economic Community (EEC). Tariffs between the Member States are to be gradually eliminated over a 12 year transition period (1957-1969). The EEC gains a legal personality with the ability to enter into trade agreements.
- **1968** – A common customs tariff enters into force, meaning all goods entering the customs union are charged common tariffs by the Member States, agreed at the European level.
- **1994** – The Marrakesh Agreement signed, establishing the World Trade Organisation (WTO), and expanding the global trade regime to include areas such as services, intellectual property rights, and technical barriers to trade.
- **1997/2001** – The Treaty of Amsterdam and Treaty of Nice add provisions furthering the inclusion of trade in services and trade related aspects of intellectual property rights into the CCP.
- **2009** – The Lisbon Treaty further develops EU competence over trade, adding foreign direct investment to the EU's competencies under the CCP, and extending the role of the European Parliament.

THE EU CUSTOMS UNION

The Customs Union was foreseen in the 1957 Treaty of Rome as a space in which goods could circulate freely within Europe without any tariffs or customs procedures.

Creating a traditional free trade area involves the relatively straightforward liberalisation of trade by the elimination or reduction of tariffs and quotas. A customs union is far more ambitious and there are relatively few such unions globally.

Members of the EU Customs Union form a single customs territory, with the consequence that:

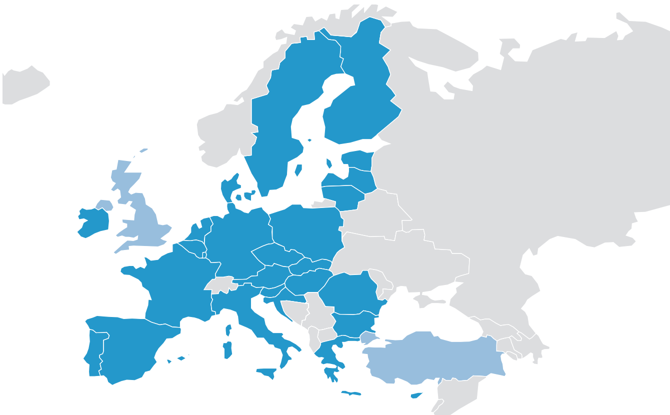
- all goods traded within the Customs Union are exempt from tariffs, quotas, rules of origin and all other trade restrictions; and
- goods legally imported from a third country into any Member State of the Customs Union may freely circulate within the Customs Union, without being subject to any further customs procedures, customs duties, or import VAT.

Today, the EU Customs Union comprises the 27 member countries of the European Union (as well as the Principality of Monaco and, until 1 January 2021, the United Kingdom).

The EU has entered into bilateral customs unions with Andorra, San Marino, and Turkey. These customs unions cover only certain types of goods, with the consequence that not all customs formalities have been removed between the parties.

Article 28 of the Treaty on the Functioning of the European Union

"The Union shall comprise a customs union which shall cover all trade in goods and which shall involve the prohibition between Member States of customs duties on imports and exports and of all charges having equivalent effect, and the adoption of a common customs tariff in their relations with third countries."



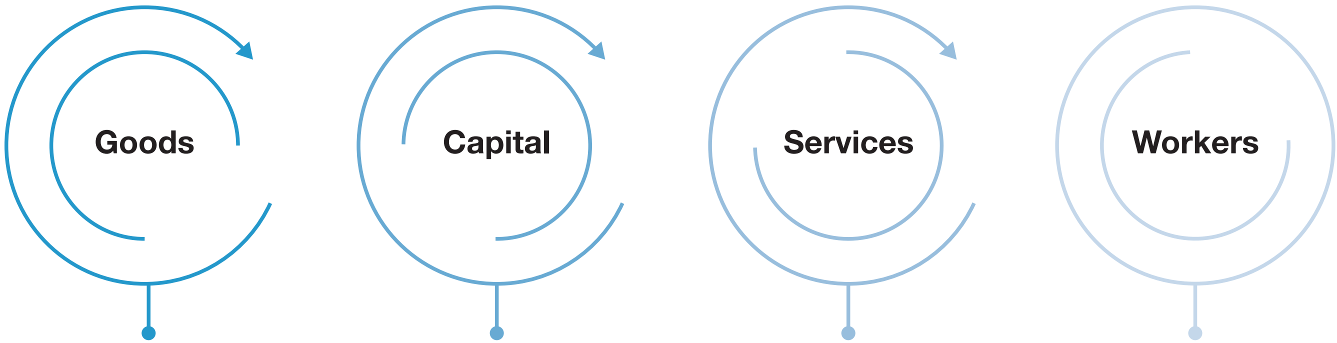
EU member states

Non-EU states which participate in the customs union, or are in bilateral customs unions with the EU

THE EU SINGLE MARKET

A single market is a further level of integration beyond that of a customs union. In addition to the rules found in a customs union, a single market allows for the free movement of the factors of production: goods, capital, services and workers. This allows for the optimal allocation of resources within that single market.

The EU single market (also known as the 'common market') was envisaged by the 1957 Treaty of Rome, and developed over time through further treaties (in particular, the 1986 Single European Act), the jurisprudence of the Court of Justice (through decisions such as Cassis de Dijon), and European secondary legislation which has sought to harmonise laws so that the free exchange of the four factors of production is not impeded by national legislation.



The area in which the EU single market is most advanced. Customs duties, charges having equivalent effect, and many non-tariff barriers have been removed.

'Capital movements' include foreign direct investment, advancement of loans and the issue and trade of securities (e.g. shares and bonds).

Allows, for example, a company established in one Member State to raise money in another.

Aspects of the single market for services include the mutual recognition of professional qualifications, standardised service standards in certain areas, the right to establish a company in any EU Member State and the right to provide or receive services between EU Member States.

The free movement of workers (expanded in the EU to include others categories of persons such as students) allows labour to be efficiently allocated within the single market by facilitating the movement of workers from areas of low demand to high.

> **"An area without internal frontiers in which the free movement of goods, persons, services and capital is ensured in accordance with the provisions of the Treaties"**

Article 26(2) of the Treaty on the Functioning of the European Union establishes the 'four freedoms' that underpin the Single Market

THE EU COMMON COMMERCIAL POLICY

The EU Common Commercial Policy (CCP) is today one of the most significant areas of EU exclusive competence. The CCP establishes common arrangements governing EU trade with third countries. It is a logical consequence of the EU Customs Union and leverages the EU's role as the world's largest trading bloc to further the objectives of its Member States.

Under the CCP, the EU is responsible for negotiating trade agreements on behalf of its Member States with third countries.

On the world stage, the EU acts as one in respect of trade policy – the CCP is an exclusive competence of the EU and Member States may not negotiate their own agreements.

In addition, the Common Commercial Policy encompasses other tools of trade policy, such as rules of origin, quotas, and anti-dumping duties.

EU Member States apply a harmonised customs tariff (the Common External Tariff) to imports.

With EU exports representing 15.2% of global exports, and EU imports representing 15.1% of global imports, the EU is one of the most significant players in international trade.

Areas of EU-Member State mixed competence (Member States must also sign)

- *Financial services*
- *Investor protections*
- *Aspects of trade in services*
- *Intellectual property rights*
- *Labour and environmental standards*

Areas of exclusive EU trade competence under the CCP (The EU can sign agreements on behalf of its Member States)

- *Trade defence instruments*
- *Representation at the WTO*
- *Conclusion of trade agreements*
- *Tariff rates*
- *Quotas*
- *Rules of origin*
- *Geographic indications*
- *Foreign direct investment controls*
- *Customs procedures (the Union Customs Code)*

> **"The common commercial policy shall be based on uniform principles, particularly with regard to changes in tariff rates, the conclusion of tariff and trade agreements relating to trade in goods and services, and the commercial aspects of intellectual property, foreign direct investment, the achievement of uniformity in measures of liberalisation, export policy and measures to protect trade."**

Article 207 of the Treaty on the Functioning of the European Union

MULTILATERAL:
THE EU IN THE WORLD TRADE ORGANISATION (WTO)

Whilst all EU Member States are members of the WTO, they are represented by the single voice of the EU at the WTO and act as one bloc vote (the so called "27 votes, one chair")

The EU in WTO institutions

The EU, as well as each of its Member States, is a member of the WTO in its own right.

The European Commission acts on behalf of all EU Member States in almost all WTO matters and affairs.

Practically, this means that:

- the EU typically assumes sole responsibility in WTO disputes on behalf of Member States, even where alleged breaches of WTO law result only from the action of a single Member State;
- EU Member States are bound by commitments made by the EU at the WTO on their behalf;
- the EU is represented by the EU Trade Commissioner in the WTO's highest decision-making body, the Ministerial Conference, which meets at least once every two years.

The European Commission, acting through its Directorate General for Trade (DG Trade) and the EU Permanent Mission to the WTO, represents the EU in day-to-day WTO fora, including:

- the WTO General Council, which acts on behalf of the Ministerial Conference and meets regularly in various configurations (such as the WTO Dispute Settlement Body); and
- subsidiary WTO councils and committees which report to the General Council, which work on particular areas of world trade (such as the environment and intellectual property).

As in other trade matters, the Commission's work at the EU is subject to the oversight of the European Council's Trade Policy Committee (TPC). The Commission's work is also monitored by the European Parliament's International Trade Committee (INTA).

With the WTO's Appellate Body currently paralyzed and unable to hear appeals of WTO panel decisions, the EU has joined a new arrangement, dubbed the 'Multi-Party Interim Appeal Arbitration Arrangement' (MPIA) as an interim alternative solution to preserve the WTO's appellate function for disputes.

The WTO

The WTO is a consensus-based forum for supervision, liberalisation, and dispute resolution in world trade, comprising 164 governments and customs territories which together account for 98% of world trade.

The WTO was established in 1995 as the successor to the General Agreement on Trade and Tariffs (1945) and is headquartered in Geneva.

The core WTO agreements set out key principles for, amongst other things, the trade in goods and services between Members. Members also accept commitments on issues such as how they will treat intellectual property, public procurement, and agricultural subsidies. Members accept a standard set of procedures for resolving disputes concerning these commitments.

- ***Liberalisation:*** The WTO is a forum for diplomatic efforts to further liberalise international trade (currently on-going in areas such as e-commerce and fishing subsidies)
- ***Supervision:*** The WTO oversees compliance with the WTO agreements (for instance, members must report to the WTO any trade restrictive measures they put in place)
- ***Dispute resolution:*** The WTO is a centre for international trade dispute resolution

BILATERAL: TYPES OF EU TRADE AGREEMENT

The Common Commercial Policy has led the EU to enter into a large number of trade agreements to secure trade liberalisation with partners internationally. As at May 2020, the EU had some 73 trade agreements in place with countries and regions around the world.

Increasing level of integration

	Objective	Example Partners
Single Market	A high level of economic integration with advanced regulatory alignment to facilitate trade and eliminate restrictions on the circulation of goods and (although harder) services.	EEA EFTA States
Customs Union	Members of a customs union form a single territory for customs purposes, with the consequence that substantially all goods traded between members are exempt from customs duties and other trade restrictions.	Andorra, San Marino, Turkey
Preferential trade agreements		
Association Agreements	Bilateral treaties which provide for "*an association involving reciprocal rights and obligations, common action and special procedures*". Typically involve the removal of obstacles to trade and harmonisation of certain areas of legislation of mutual interest (e.g. state aid and public procurement rules, or migration). (Originally used as a preparatory step for accession to the EU).	Mercosur, Central America, Albania, Bosnia and Herzegovina, Kosovo, Montenegro, North Macedonia, Serbia
Deep and Comprehensive Free Trade Agreements	Ambitious free trade agreements which entail the gradual removal or reduction of tariff and non-tariff barriers, and regulatory approximation with EU law. Partners are offered the 'four freedoms' of the Single Market (free movement of goods, services, capital and people).	Georgia, Moldova and Ukraine
Free Trade Agreements	Provide for preferential tariff treatment. Often include provisions covering trade facilitation and rule-making in areas such as investment, intellectual property, government procurement, and sanitary and phytosanitary issues.	Canada, Mexico, Republic of Korea
Economic Partnership Agreements	Trade and development agreements tailored to suit specific regional circumstances and promote sustainable growth and poverty reduction through trade.	Bahamas, Madagascar, the Southern African Development Community (SADC)
Partnership and Cooperation Agreements	Agreements with the goal of strengthening political dialogue and economic integration and cooperation.	Russia, Armenia, Tajikistan
Other trade-related agreements	The EU also pragmatically seeks agreement on issues with trade-impact on an issue-by-issue basis. An example is the US-EU Covered Agreement on insurance.	USA

UNILATERAL: TRADE WITH DEVELOPING COUNTRIES

The EU maintains a range of trade programmes for developing countries under the umbrella of its Generalized System of Preferences (GSP). These GSP programmes implement a 1971 UN Conference on Trade and Development (UNCTAD) recommendation that developing countries' exports should benefit from reduced tariffs, in order to support job creation and economic growth. GSPs represent an exception to the WTO "Most-Favoured Nation" principle.

Standard GSP

This **reduces or removes EU import duties payable on approximately two-thirds of all EU tariff lines**. All countries classed as being 'developing countries' under the relevant EU regulation stand to benefit from standard GSP.

GSP+

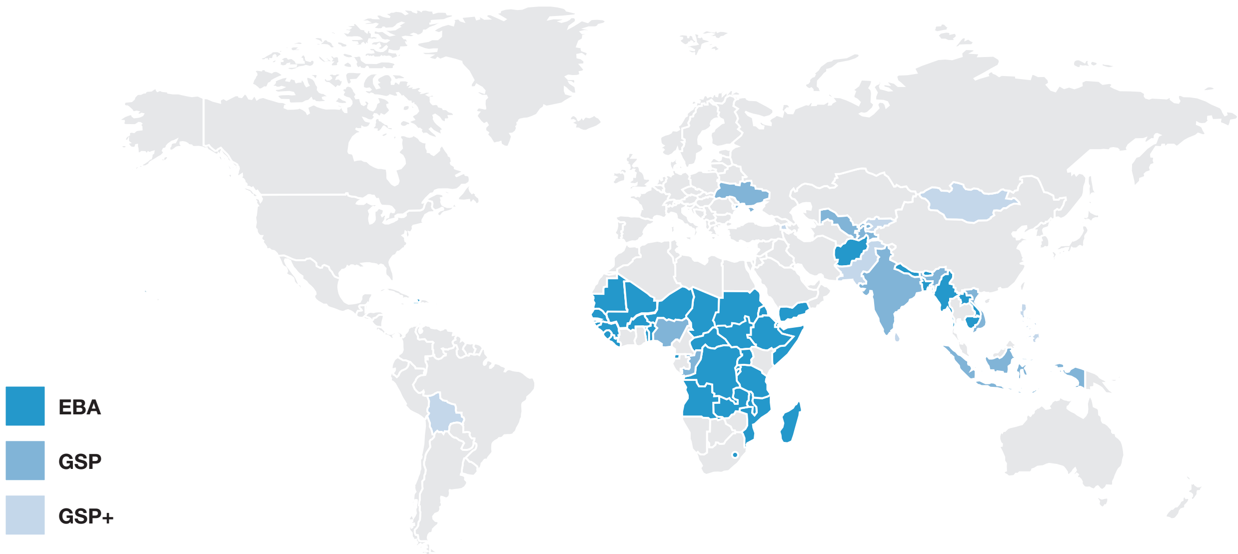
On application, a developing country may benefit from the **complete removal of all EU import duties on approximately two-thirds of all EU tariff lines**. The EU awards GSP+ status to countries that are both particularly vulnerable and meet international good governance standards.

EBA (Everything But Arms)

Countries classified as 'Least Developed Countries' by the UN Committee for Development Policy can benefit from **duty and quota free access to the EU Single Market on all their exports, other than arms and armaments.**

African, Caribbean and Pacific (ACP Countries)

The EU has a special relationship with the former colonies of its Member States, and since the 1975 Lomé Convention has afforded them preferential and non-reciprocal access to the EU market. These arrangements are gradually being replaced by new "Economic Partnership Agreement" (EPA) treaties with each of the ACP countries due to criticism that the previous arrangements may not have been WTO-compliant.



UNILATERAL: TRADE REMEDIES

Trade remedies, or trade defence instruments (TDIs), are provided for in the WTO agreements to allow members to protect their domestic industry from injury caused by unfair trading practices or exceptional circumstances.

The EU is responsible for protecting Member States by investigating situations which might necessitate the imposition of a trade remedy and, where one is found, imposing appropriate measures.

Trade remedies broadly fall into two categories: anti-dumping and countervailing measures, and safeguarding measures.

Anti-dumping and countervailing measures

Dumping occurs when foreign products are sold onto the world market at an artificially low price. This can arise where a third country supports its exports with distorting subsidies, for instance in order to gain an overseas market share (predatory dumping) or to offset a temporary domestic surplus of a product.

To counter this, the EU can impose anti-dumping duties or countervailing duties, which are the most commonly used TDI in practice (other measures available include requiring undertakings from third-country exporting firms or the authorities of the subsidising country).

Following a complaint from EU producers, the Commission can open investigations into whether there is dumping by the producers in the third country concerned, whether EU industry has suffered material injury, and, crucially, whether a causal link exists between dumping and injury.

The Commission can autonomously adopt preliminary anti-dumping measures, and only rejection by qualified majority in the Council can reverse them. The Parliament does not exercise oversight of individual duties but can adopt resolutions and co-legislates the underlying legislative framework under the ordinary legislative procedure.

Safeguard measures

Safeguards (i.e. temporary withdrawal of tariff preferences) can be put in place when an EU industry is suddenly faced with an unforeseen and sharp rise in imports from third countries. They are therefore used very sparingly.

When a Commission investigation concludes that safeguard measures are warranted (based on specific and strict criteria), the Commission can impose quantitative restrictions (i.e. import quotas or tariff quotas that would otherwise be prohibited) and surveillance (where the import of goods is monitored with licenses).

There are two separate safeguard regulations, one for WTO countries (Regulation 2015/478) and another for non-WTO countries (Regulation 2015/755).

Under FTAs, the EU can also apply safeguards in cases of import increases that threaten to seriously injure domestic industry. This was streamlined in 2019 into the Horizontal Safeguards Regulation (2019/287).

Inappropriate use of TDIs can be challenged at the WTO.

PART II: THE EU TRADE NEGOTIATION PROCESS

THE EU TRADE LEGISLATIVE PROCESS

The Treaties and other sources of EU law establish the process by which trade agreements are negotiated and ultimately approved and ratified with the support of the EU Member States and EU institutions.

This section provides an overview of the processes by which the EU undertakes the CCP.

KEY EU INSTITUTIONS INVOLVED IN THE COMMON COMMERICAL POLICY

Member states and legislature

The Council of the European Union

The Council of the European Union (or Council of Ministers) is the EU's principal decision-making body. At the top level it comprises the relevant government ministers or state secretaries of all the Member States.

Trade bodies:

Trade Policy Committee (TPC): The TPC assists and advises the Council in negotiations with third countries and in WTO-related work. The TPC meets monthly in its full-member configuration and the TPC deputies meet weekly. The TPC has also special configurations, namely on services and investment, steel, textiles and other industrial sectors and mutual recognition agreements.

The European Parliament

The European Parliament is a democratically elected body with members (MEPs) elected directly from each of the Member States and grouped according to political, rather than national, affiliation.

International Trade Committee (INTA): INTA is a committee of MEPs who follow trade policy, produce reports for the wider Parliament, and adopt resolutions about trade negotiations and policy (such as how the Commission should approach negotiating rounds) based on its discussions.

Executive bodies

The European Commission

The Commission is the central administrative and policy-making body of the EU. It is made up of Directorates General (DGs) responsible for specific policy areas in a similar way to UK government ministries.

Trade bodies:

DG Trade: The Directorate General for Trade employs some 600 officials working full time on trade policy and is at the forefront of negotiating the EU's trade policy. It is headed up by a Director General who reports to the European Commissioner for Trade. The European Trade Commissioner has a Cabinet made up of between 10 and 15 people working directly for them.

Other DGs: Specialised DGs play a role in aspects of trade agreements relevant to them. DG Agri, for instance, leads on the agricultural aspects of negotiations.

Other EU regulatory bodies

Other EU bodies including executive agencies responsible for the implementation of specific EU policies provide assistance on the negotiation and implementation of EU trade policy.

Examples:

European Medicines Agency (EMA): The EMA provides input on the pharmaceuticals chapters of free trade agreements.

The European Economic and Social Committee (EESC): FTAs contain provisions for the creation of domestic advisory groups and civil society fora, which the EU organises via the EESC.

THE TRADE NEGOTIATION PROCESS

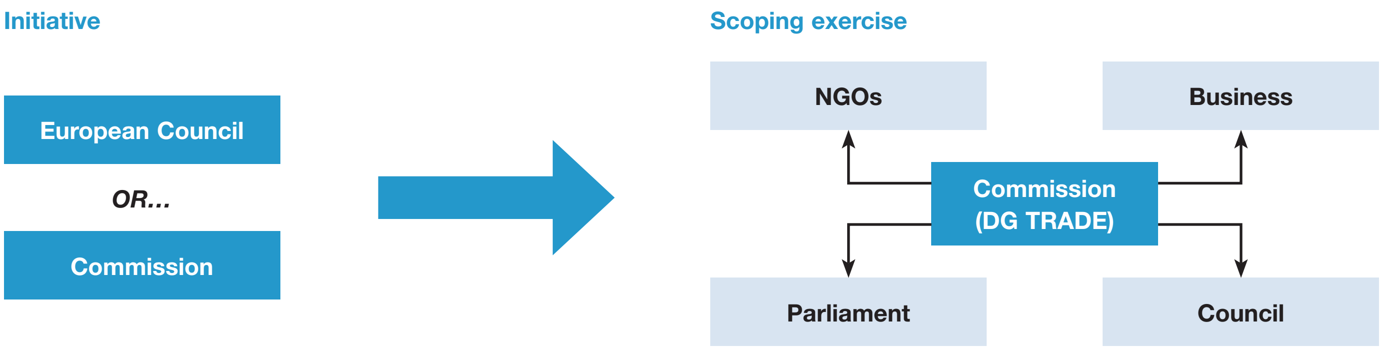
1. Scoping | 2. Mandate | 3. Negotiations | 4. Agreement / Ratification | 5. Application and entry into force

The process towards a trade agreement begins with a Commission “scoping exercise”, during which the Commission opens discussions with stakeholders, including business, NGOs, civil society through “civil society dialogues”, the Council and the Parliament.

This could be done by the Commission on its own initiative, or at the request of the Member States’ Heads of State acting through the European Council.

There are also informal discussions with the partner country throughout the scoping exercise.

This stage can take anything from several months to a few years.



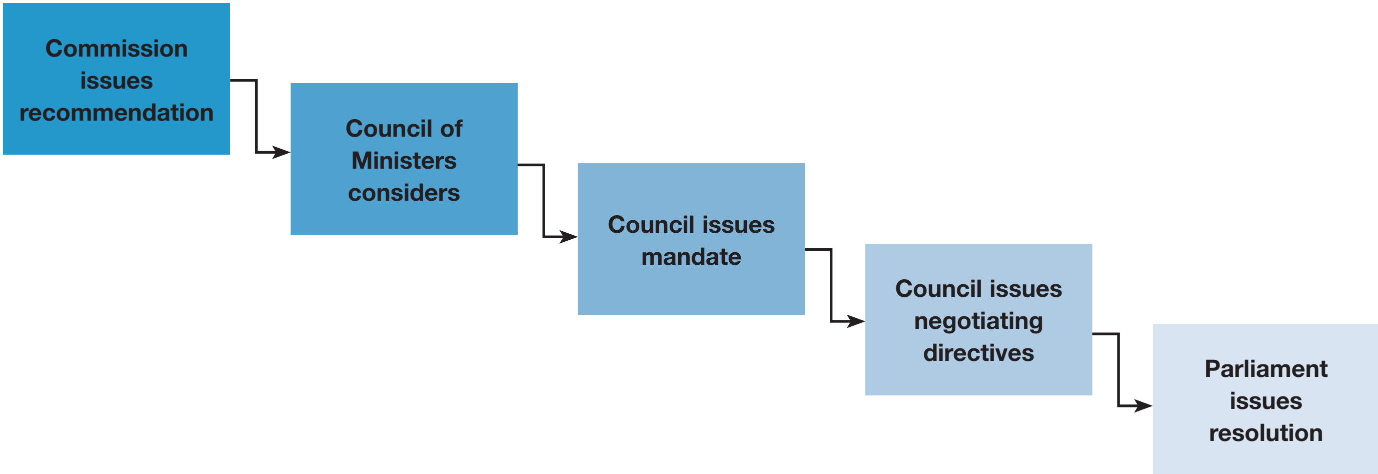
THE TRADE NEGOTIATION PROCESS
(CONTINUED)

Once the Commission is confident there are sufficient reasons to pursue a trade agreement, it issues a recommendation (sometimes called the "draft mandate") to the Council (with draft negotiating directives and supporting analysis), sometimes referred to as the draft negotiating mandate.

Discussions then take place between the Commission and the TPC of the Council.

If the Council approves of the Commission's proposal, it issues a mandate. Voting on the mandate is by Qualified Majority Voting ("QMV"), but consensus is the norm. The Council decision can be accompanied by the negotiating directives, which the Commission will have to use as the basis of its negotiations.

It is becoming customary for the Parliament to adopt resolutions, including what it expects from negotiations, at the beginning of a negotiating round. For example, when the EU began discussions on opening an FTA with Japan in 2012, the Parliament passed a resolution asking the Council not to authorize the opening of negotiations before INTA gave its position on the proposed mandate.



1. Scoping | 2. Mandate | **3. Negotiations** | 4. Agreement / Ratification | 5. Application and entry into force

Negotiations

Each side will appoint a chief negotiator, in most cases a senior civil servant with many years' experience of trade negotiations. The EU chief negotiator will usually be a senior official from DG Trade (except in the case of the negotiations with the United Kingdom following its decision to leave the EU, where Michel Barnier was appointed to lead the negotiations).

Negotiating rounds take place every few months, usually alternating between Brussels and the partner country. The negotiations are broken down into different joint working groups

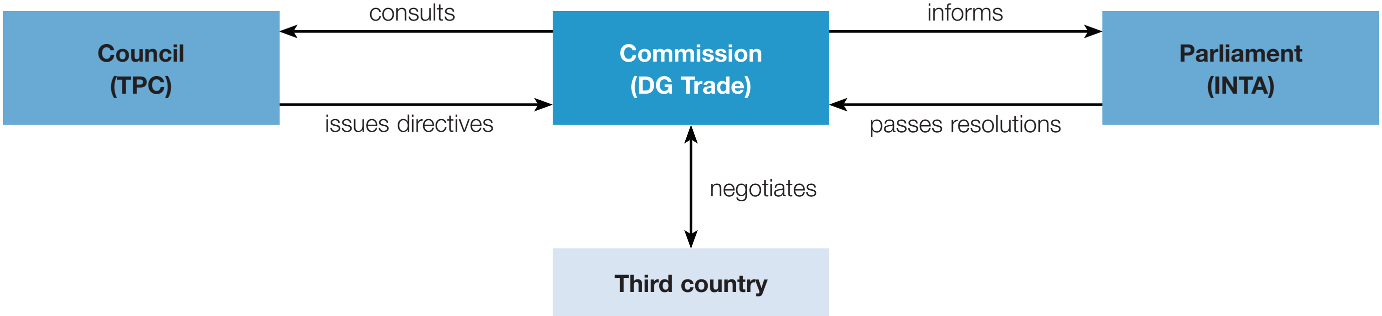
After each negotiating round, the European Commission publishes reports.

The Treaties grant the Council powers to "adopt negotiating directives" and to designate a "special committee" with which the Commission must work together with to conclude negotiations. In practice, the TPC meets weekly to discuss the Commission's work, and give direction to its negotiating.

The Treaties state that the European Parliament "shall be immediately and fully informed at all stages of the procedure". The Commission will as a matter of course transfer to INTA all documents related to a negotiation which it has communicated to the Council's TPC. This practice was first proposed in the Commission and Parliament's 2010 Framework Agreement. The Framework commits the Commission to "guarantee that it will apply the principle of equal treatment for Parliament and the Council, especially as regards access to meetings and provision of contributions or other information." This has its limits within the scope of what is possible in a trade negotiation, where redlines must be kept secret from the negotiating partner, and given the public nature of parliamentary business.

Resolutions the Parliament passes expressing its preferences are increasingly read by Commission officials as setting the conditions for parliamentary consent. INTA has established monitoring groups over all ongoing FTAs, which organise regular meetings with the Commission in which to raise questions, concerns and opinions.

Negotiations



THE TRADE NEGOTIATION PROCESS
(CONTINUED)

1. Scoping → 2. Mandate → 3. Negotiations → **4. Agreement / Ratification** → 5. Application and entry into force

Agreement / Ratification

When the Commission reaches an agreement in principle with its negotiating partner, resulting in a single text, the Commission lead negotiator and their counterpart will initial the entire agreement. This is not yet legally binding and remains subject to change and legal and linguistic ‘scrubbing’.

The Commission sends the Council and Parliament the text of the agreement to prepare it for signature. It is translated into all of the official languages of the EU.

The Council is responsible for ratifying the treaty. Both trade agreements and trade legislation are adopted in the Council on the basis of qualified majority voting, which means that the agreement needs to be supported by 55% of Member States, representing 65% of the population. However, in practice, the Council adopts decisions by common agreement in areas of shared competence (e.g. commercial aspects of intellectual property).

Under the Treaty of Lisbon, FTAs concluded by the Commission and ratified by the Council are now also subject to the ‘consent’ of the Parliament acting by simple majority.

Mixed agreements

Some EU trade agreements are ‘EU only’ (i.e. the policy areas that they cover fall only within the sole responsibility of the EU institutions), while other agreements are ‘mixed’, having elements that are the responsibility of both (see Page 7):

- the EU institutions and
- individual EU Member States.

‘Mixed’ agreements also must be ratified by all EU Member States, who vote by following their own national procedures (which may require votes by national and regional parliaments).

The Commission sends the Council and Parliament the text of the agreement to prepare it for signature. → **The Council is responsible for ratifying the treaty.** → **FTAs concluded by the Commission and ratified by the Council are now also subject to ‘consent’ by the Parliament at simple majority.** - - → **‘Mixed’ agreements additionally require ratification by all EU Member States, who vote by following their own national procedures**

1. Scoping | 2. Mandate | 3. Negotiations | 4. Agreement / Ratification | **5. Application and entry into force**

Application and Entry Into Force

Provisional application

The EU usually agrees with third countries that, pending ratification by the EU institutions and EU Member States (if applicable) an agreement can be “provisionally applied” fully or partially (e.g. both parties abide by its terms despite them not yet being legally binding, for instance by applying agreed tariffs etc.). In practice, provisional application can continue indefinitely unless one of the parties signals that it will not approve the agreement.

For that to change, any capital in the EU still going through national approval would have to send a formal notice terminating the accord and the ratification process would have to be deemed by the bloc to have failed “permanently and definitively.”

Formal entry into force

Once the Council adopts a formal decision to conclude the agreement, and the other party has completed its internal ratification procedures, the parties notify each other of the completion of their ratification procedures, and the agreement enters into force and is published in the EU’s Official Journal.

The agreement will become legally binding and enter into force on a date provided for in the agreement.

Application and entry into force

If exclusive competency:

Council decision

Provisional application - - - → ***EITHER...*** In force →

If mixed competency:

Council decision **+** **Member States ratify**

PART III:
SOME KEY ISSUES IN EU TRADE POLICY

FINANCIAL SERVICES – THIRD COUNTRY REGIMES AND EQUIVALENCE

Regulating market access is a way in which national policy makers and regulators seek to maintain oversight of the financial activity taking place in their jurisdiction. To facilitate trade in financial services, trading partners can agree measures to make regulators work better together.

In trade, national approaches to market access are the norm.

In the European Union, market access for non-EU ('third country') firms is determined at the Member State (national) level – with certain exceptions, for example:

- to a limited extent, where EU FTAs contain provisions on financial services; and
- where there is an equivalence or recognition mechanism for the EU to determine that the rules of the relevant third country are equivalent.

Financial services in EU free trade agreements

Existing EU FTAs largely do not address these barriers to market access for financial services.

For example, the Comprehensive Economic and Trade Agreement (CETA) between the EU and Canada includes only limited provisions on financial services.

These do not go much further than the requirements of the WTO's General Agreement on Trade and Services (GATS) – for example, CETA guarantees the right of a party from Canada to establish a branch or subsidiary in the EU from which to provide services, and vice versa.

Crucially, CETA does not address local licensing requirements (and so does not offer any form of market access comparable to passporting rights), and contains a broad 'prudential carve-out' which permits either party to take measures that might otherwise contravene CETA in order to protect the stability or integrity of that party's financial system.

Equivalence mechanisms

Under EU law, equivalence mechanisms are a unilateral mechanism used to reduce overlaps in regulatory and supervisory compliance and, in some limited cases, to facilitate market access (e.g. in relation to central counterparties and investment firms).

Where a positive equivalence decision has been made relating to market access, market participants from the relevant third country may be able to provide services in the EU without being required to comply with all the relevant EU rules applicable to EU firms, as the EU will view the third-country's rules as achieving the same outcomes as the relevant EU regime.

However, the scope of market access made possible via equivalence is relatively limited and it is no substitute for passporting rights enjoyed by EEA firms. For example, there is no equivalence mechanism in EU legislation allowing market access in respect of core banking services such as deposit taking and lending.

In other cases, a positive equivalence decision in relation to a third country may provide EU or third-country firms other kinds of improved regulatory treatment. For example, it may allow EU

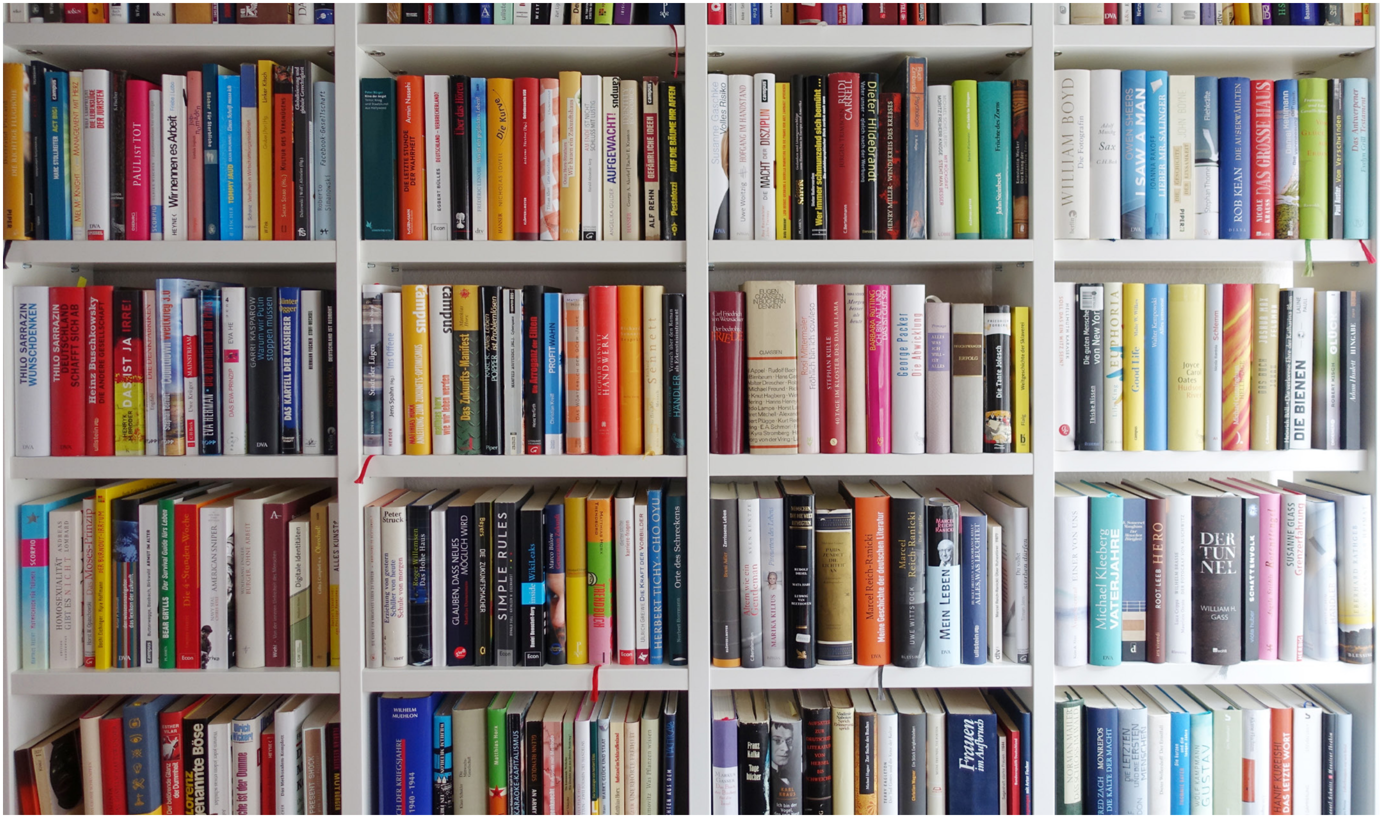
FINANCIAL SERVICES – THIRD COUNTRY REGIMES AND EQUIVALENCE (CONTINUED)

banks to treat, for their regulatory capital purposes, their credit exposures to third country banks in a similar way to their credit exposures to EU banks.

Because equivalence mechanisms in EU legislation are unilateral and discretionary, third countries do not have a right for their framework to be assessed or to receive a positive equivalence determination, even if the framework does, in fact, fulfil relevant criteria. A determination remains the prerogative of the EU authorities.

The European Commission also has the discretion to adopt, suspend or withdraw equivalence decisions as necessary, and the flexibility to grant time-limited or partial equivalence decisions.

Under WTO rules and most FTAs, the EU can grant preferential treatment to third countries via recognition decisions so long as it provides other WTO members or trade partners an appropriate opportunity to demonstrate that the necessary conditions have been met.



INVESTOR-STATE DISPUTE SETTLEMENT

The 2007 Lisbon Treaty brought foreign direct investment (FDI) – investments by entities situated in one country into business interests located in another – further within the scope of the EU's Common Commercial Policy.

Background

Investment protection agreements, such as bilateral investment treaties (BITs), are agreements between two States facilitating private investment by nationals and companies of each State in the other. They do so by providing guarantees of fair and equitable treatment to investors from each state, usually combined with an investor-state dispute settlement (ISDS) mechanism which can award compensation to the investor for breaches of the agreement.

Similar provisions can also be found in some multilateral investment treaties (such as the Energy Charter Treaty) and some free trade agreements.

BITs already entered into by EU Member States before the Lisbon Treaty remain binding and valid after the Lisbon Treaty. However, the Commission's approval must now be obtained before a Member State enters into any new BIT.

The EU's role in investment treaties

BITs that had already been entered into by EU Member States remain binding and valid after the Lisbon Treaty. However, the Commission's approval must now be obtained before a Member State enters into any new BIT.

The EU can negotiate investment treaties with third countries on behalf of Member States, or include investment protection provisions in wider free trade agreements.

The CJEU has ruled that investment treaties remain a mixed competence with the Member States, however. This means that they must follow the national processes for ratification in each Member State, as well as in Brussels by the EU. In practice this slows down the signing of EU investment treaties, and acts as an incentive for the EU to conclude separate trade and investment agreements with third states so that the trade element can be ratified quickly. For example, EU-Singapore trade and investment protection agreements were both signed on 19 October 2018 – while the EU-Singapore FTA has now been ratified and entered into force, the investment protection agreement is still pending ratification by EU Member States.

As ISDS has met increasing opposition from some civil society actors, the EU has attempted to allay concerns by introducing an 'Investment Court System' (ICS) as part of its investment agreements. The ICS shares certain features with the public courts, in a departure from the ad hoc arbitration approach by which investor-state disputes are typically settled.

The status of BITs between EU Member States

Investment treaties have come under criticism from the European Commission, which views BITs between EU Member States ("intra-EU BITs") as potentially contrary to EU law, as they may reach decisions on matters of EU law outside of the EU and national court systems.

On 6 March 2018, the Court of Justice of the European Union upheld this view (in the case of Slovak Republic v Achmea). The Court held that, by creating a parallel jurisdiction to the EU's domestic courts, the 168 intra-EU BITs still in force impaired the consistency, full effect and autonomy of EU Law.

On 5 May 2020, 23 of the 27 EU Member States signed an agreement for the termination of intra-EU bilateral investment treaties.

GEOGRAPHIC INDICATIONS AND AGRICULTURAL PRODUCTS

A Geographic Indication (GI) is a sign which identifies a product as originating in a particular geographic region. GIs are most often geographical names (such as Kalamata olive oil, champagne, and Parma ham), but may also be traditional or historical terms (such as Feta cheese).

GIs can be incredibly important for businesses which benefit from them. EU products bearing GIs account for annual sales of €74.76 billion, with one fifth of this revenue coming from exports outside of the EU. Products bearing GIs account for 15.5% of all EU agri-food exports by value.

GIs are recognised in the EU as a form of intellectual property right. Once GI protection has been registered, those who have the right to use the GI can prevent the use of that GI by a third party whose product does not conform to the applicable standards.

GIs in EU trade agreements

The EU has been one of the main supporters of GIs internationally. At the WTO, the EU championed GIs during the (failed) Doha Development Round. Some limited protections are available under the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS). The EU supplements these protections by concluding specific 'standalone' agreements on GIs and including provisions on GIs in broader trade agreements.

In trade negotiations, the EU seeks to convince negotiating partners to recognise a number of particularly valuable GIs in exchange for some amount of market opening. There are thousands of GIs recognised in the EU and the number grows weekly as new names are registered, but the number of GIs included in trade agreements tends to be in the hundreds.

The EU and Mexico concluded a 1997 Agreement on Designations for Spirit Drinks, under which the EU agreed to grant protections to Mexican products such as Tequila and Mexico agreed to grant protections to EU products such as Grappa. Following the recent "modernization" of the EU-Mexico Agreement, the list of protected names was updated to protect 232 EU spirits GIs in Mexico and 6 Mexican spirits in the EU.

These negotiations can often provoke opposition from domestic producers of particular goods. Disagreements are common in negotiations with countries that include large diaspora from Europe who may have been using the European terms for many years.

THE UK EXIT FROM THE EU

The UK left the EU at 11.00 p.m. UK time on 31 January 2020 and no longer has any role in the EU's institutions or law-making processes. The EU and the UK now have until 31 December 2020, the end of the transition period provided for by the Withdrawal Agreement, to negotiate an agreement on their future relationship.

During this transition period, the UK remains subject to EU law (including new laws coming into force during the transition period) and participates in the EU's single market and customs union but not its institutions. The transition period is intended to provide time for the UK and EU to reach agreement on the UK's future relationship with the EU (as set out in the New Political Declaration published on 19 October 2019), whilst minimising disruption for citizens and businesses in the UK and the EU while this happens.

This agreement is being negotiated by the EU under processes that are similar to those for reaching trade agreements with any third country, but with certain differences. The European Commission has set up a new Task Force for Relations with the United Kingdom (UKTF), made up of six units, covering the different aspects of the negotiation (for example economic affairs, citizens' rights, security, climate and energy). UKTF will lead all aspects of the future relationship negotiations with the UK.

The UKTF reports directly to Commission President Ursula von der Leyen and coordinates the work of several Directorates-General (DGs), including DG TRADE, which would normally take the lead on negotiations with third countries. The EU's Brexit negotiator, Michel Barnier, has been appointed head of the UKTF and effectively continues in his role as chief negotiator with the support of a new deputy, Clara Martínez Alberola, who gained extensive Brexit experience as Chief of Staff to the former Commission President Jean-Claude Juncker.

Any agreement would need to be signed and ratified by the EU (and possibly each Member State) before it can fully enter into force.

During the transition period, the UK is bound by the EU's trade agreements with third countries and has sought to put in place agreements with relevant third countries to ensure that it continues to benefit from the terms of those agreements as well. The UK is also free to negotiate new trade agreements with third countries taking effect after the transition period comes to end.

The transition period ends on 31 December 2020. The parties could have extended the period by up to one or two years by a joint decision before the end of June 2020, however, the UK indicated that it did not wish to agree any extension.

For more information and resources on Brexit, visit the Topic Guide on the Clifford Chance Financial Markets Toolkit at **https://financialmarketstoolkit.cliffordchance.com/brexit**

GLOSSARY

Anti-dumping duties – when anti-dumping measures are imposed, they take the form of an ad valorem duty: a fixed amount on the price of a product or a minimum import price on the good in question. According to the 'lesser duty rule', these amounts cannot be higher than what is needed to prevent injury to EU producers.

Council of the European Union – the EU's principal decision-making body. At the top level it comprises government ministers or state secretaries of all the Member States with responsibility for a particular sector.

Countervailing duties – measures which aim to counteract distorting subsidies. They can take the form of a percentage of the price of the good, a fixed premium on an amount (per unit) of the product, a minimum threshold import price, or a price undertaking.

Customs duty – a tax imposed on imports (and occasionally on exports) of goods. Members of the EU Customs Union apply a single Common Customs Tariff on imports into the bloc.

ESAs – the European Supervisory Authorities in the context of financial services: the European Banking Authority (EBA), the European Securities and Markets Authority (ESMA) and the European Insurance and Occupational Pensions Authority (EIOPA).

European Commission – the central administrative and policy-making body of the EU. It is made up of Commissioners (nominated by the Member States and approved by the European Parliament), one of whom acts as President.

European Council – a body comprising the Heads of State or Government of the Member States, which reviews and decides on the overall policy direction of the EU.

European Parliament – a democratically elected body with members (MEPs) elected directly from each of the Member States and grouped according to political, rather than national, affiliation.

Free Trade Agreements (FTAs) – agreements between countries that removes tariffs and other restrictions on "substantially all" goods traded between them (as defined by the World Trade Organisation).

Official Journal – the official gazette of record for the EU, in which all legally-binding EU legal acts are printed.

Passporting rights – firms established and licensed in one Member State may exercise "passporting" rights to provide cross-border services or establish a branch in another Member State without obtaining a local licence.

Qualified Majority Voting – a means by which Council of the EU decisions may be made without the need for unanimity. A qualified majority is reached if both 55% of Member States vote in favour and these Member States represent at least 65% of the total EU population.

Quota – a trade measure that places a limit on the quantity or value of goods that can be imported to or exported from a country at a particular tariff rate

Rules of origin – companies from countries that are not members of a customs union with the EU have to comply with EU rules of origin (the rules to determine the "economic nationality" of a product) when exporting to the EU. These rules ensure that the correct tariffs are levied against goods (taking into account any preferential tariff rate or trade defence measures, such as anti-dumping duties).

Third country – for the purposes of this booklet, a country that is not a member of the European Union.

CONTACTS

Jessica Gladstone
Partner
London
T: +44 20 7006 5953
E: jessica.gladstone@cliffordchance.com

Gail Orton
Head of EU Public Policy
Paris
T: +33 1 4405 2429
E: gail.orton@cliffordchance.com

Rae Lindsay
Partner
London
T: +44 20 7006 8622
E: rae.lindsay@cliffordchance.com

Janet Whittaker
Senior Counsel
Washington DC
T: +1 202 912 5444
E: janet.whittaker@cliffordchance.com

Thomas Voland
Partner
Düsseldorf
T: +49 211 4355 5642
E: thomas.voland@cliffordchance.com

Christopher Bates
Partner
London
T: +44 20 7006 1041
E: chris.bates@cliffordchance.com

Caroline Dawson
Partner
London
T: +44 20 7006 4355
E: caroline.dawson@cliffordchance.com

Michel Petite
Avocat of Counsel
Paris
T: +33 1 4405 5244
E: michel.petite@cliffordchance.com

Phillip Souta
Head of UK Public Policy
London
T: +44 20 7006 1097
E: phillip.souta@cliffordchance.com

Roland Scarlett
Lawyer
London
T: +44 20 7006 2191
E: roland.scarlett@cliffordchance.com

Fraser Eccles
Trainee Solicitor
London
T: +44 20 7006 1906
E: fraser.eccles@cliffordchance.com

Audley Sheppard
Partner
London
T: +44 20 7006 8723
E: audley.sheppard@cliffordchance.com

Sam Luttrell
Partner
Perth
T: +61 8 9262 5564
E: sam.luttrell@cliffordchance.com

Jeremy Stewart
Foreign Law Clerk
New York
T: +1 212 878 4938
E: jeremy.stewart@cliffordchance.com

Anthony Oldfield
Partner
São Paulo
T: +55 11 3019 6010
E: anthony.oldfield@cliffordchance.com

Vanessa Marsland
Partner
London
T: +44 20 7006 4503
E: vanessa.marsland@cliffordchance.com

C L I F F O R D

C H A N C E

Clifford Chance, 10 Upper Bank Street, London, E14 5JJ

WWW.CLIFFORDCHANCE.COM

J20201305200343