

## A NEW CHAPTER IN UK-JAPAN ECONOMIC AND TRADE RELATIONS

The new trade agreement between the UK and Japan, the **Comprehensive Economic Partnership Agreement (CEPA)** came into force on 1 January 2021.

**As a result, the UK-Japan trading relationship is no longer governed by the Japan-EU Economic Partnership Agreement (JEEPA). This briefing considers how the provisions of CEPA depart from the EPA regime and, in the context of Brexit, what impact the new arrangements have on key sectors.**

In particular this briefing considers the provisions of the CEPA as they relate to financial services, the automotive sector, agriculture, and food and drink. On balance, while CEPA broadly replicates the key elements of JEEPA as between the UK and Japan, there are some differences—most notably in relation to the digital economy.

This briefing also considers wider changes to the UK-Japan relationship in the light of Brexit as well as the potential impacts on bilateral investment. It also examines prospects for the potential future negotiation of an investment protection regime with an investor-state dispute settlement (ISDS) mechanism.

### THE DIGITAL ECONOMY

A key area in which the UK and Japan sought to expand upon the existing provisions of the JEEPA is in relation to e-commerce and data protection.

When the deal was first announced in September 2020, both the UK and Japan drew attention to the digital-trade provisions of the deal, with the UK government describing the CEPA as containing "*cutting-edge digital & data provisions that go far beyond the EU-Japan deal*".<sup>1</sup>

The provisions of the CEPA do exceed the provisions of the JEEPA in some important respects. Importantly, CEPA contains obligations (Article 8.84) prohibiting restrictions on cross-border transfer of data—including personal information, and a ban on data localisation requirements (Article 8.85).

### Key takeaways

- The UK-Japan Economic Partnership Agreement (CEPA) preserves most of the trade benefits available to the UK and Japan under the EU-Japan Economic Partnership Agreement (JEEPA).
- In relation to the digital economy, CEPA has strengthened e-commerce and data mobility arrangements beyond JEEPA.
- While the JEEPA regime for financial services is essentially preserved under CEPA, more work is required to address other Brexit impacts.
- Agriculture, food, drinks and automobiles also benefit from having the EU-Japan arrangements essentially replicated under JEEPA. However, the impact of new rules of origin requirements between the UK and EU will complicate supply chains for manufacturers—particularly for complex products such as cars.
- The CEPA does not contain investment protection or ISDS, but a side letter from Japan supports the UK's application to support the CPTPP (which includes such provisions).

<sup>1</sup> UK government press release, [UK and Japan agree historic free trade agreement](#) and [Statement by Minister Kajiyama on the agreement in principle on the Japan-UK Comprehensive Economic Partnership Agreement](#), both dated 11 September 2020. See also Clifford Chance's briefing, [Agreement in principle for the Japan-UK trade deal: A focus on tech and the digital economy](#), dated September 2020.

The UK and Japan have also agreed a range of other commitments on digital trade, including:

- a commitment to maintain principles of net neutrality (Article 8.78);
- strengthened provisions on the transfer of financial information between financial services providers, and a prohibition on data localisation provisions in respect of financial data except where required for regulation and supervision (Article 8.63);
- commitments not to impose customs duties on electronic transmissions (Article 8.72), the protection of source codes (Article 8.73) and provisions facilitating use of e-signatures (Article 8.77).

Many of these commitments are similar to those made by Japan in the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (**CPTPP**), which the UK has now [formally applied to join](#). However, the strengthened e-commerce and data mobility provisions will come as good news for digitally enabled service providers, and we expect that financial service providers as well as other digital service providers are likely to benefit from the regulatory certainty that these provisions provide.

## **FINANCIAL SERVICES**

Aside from the new commitments on data localisation and transfer of financial information outlined above, the financial services provisions of the CEPA largely replicate those of JEEPA.

CEPA does, however, lay the groundwork for more direct cooperation between UK and Japanese financial regulators through a comprehensive annex on regulatory cooperation. The agreement establishes an annual dialogue directly between Japanese and UK financial regulators, providing a forum through which to address market access barriers or regulatory developments—including with respect to emerging issues.

CEPA's regulatory cooperation annex adds some new elements to the equivalent annex in JEEPA, including enhanced obligations to consult prior to withdrawing recognition of regulatory equivalence, and specific commitments regarding cooperation on new forms of financial services. The practical impact of these regulatory cooperation provisions will, however, depend largely on the extent to which the UK and Japan are able to utilise this forum to resolve market access barriers and promote consistency in financial services regulation between the countries.

CEPA also includes enhanced transparency obligations in relation to the licensing of financial service providers (Article 8.64). These oblige the UK and Japan to publish requirements for obtaining and renewing authorisations to provide financial services, as well as (where practicable) providing reasons for rejecting an application and giving applicants the opportunity to provide further information to support an application.

However, Brexit casts a long shadow over the UK financial services sector. While the CEPA replicates and enhances the financial services provisions as compared to the JEEPA, it comes alongside substantial new regulatory barriers between the EU and the UK. UK-domiciled financial service providers serving

Japanese clients will no longer have the same degree of access to EU financial markets as did previously, having lost EU passporting rights on 1 January 2021.

While the EU-UK Trade and Cooperation Agreement (TCA) contained only limited commitments on financial services, the UK and EU are continuing to negotiate a framework for regulatory cooperation in financial services—with an outcome expected by March 2021.

## **AGRICULTURE, FOOD AND DRINK**

In broad terms, goods market access in CEPA largely replicates that of JEEPA. While this outcome ensures that UK and Japanese exporters retain the preferential access they enjoy under JEEPA, the market access gains for either side were limited. This point was noted by the House of Lords European Union Committee who commented in their paper scrutinising the CEPA that:

*"The Department for International Trade (DIT) has stated that the UK gained "strong tariff reductions for UK pork and beef exports", and a range of other agricultural projects, in CEPA. In fact CEPA does not deliver new reductions, but retains those negotiated under JEEPA. In general, further tariff liberalisation beyond JEEPA has not been achieved on either side"*<sup>2</sup>

JEEPA's timelines for tariff reductions (many of which still have many years remaining) are also largely replicated in CEPA—ensuring a level playing field between UK and EU exporters to Japan and *vice versa*. For example, tariffs on UK exports of cheddar cheese to Japan will continue to reduce in line with the JEEPA schedule so that they are zero-rated by 2033). A limited number of tariffs for certain types of leather and autoparts will actually be subject to slightly quicker reductions under CEPA than under JEEPA.

In relation to tariff rate quotas (**TRQs**) – preferential tariffs that apply only for a limited quantity of goods – CEPA provides more limited benefits to UK exporters than under JEEPA. In particular, UK exporters will only have rights under 10 of the 25 TRQs established by CEPA and even then, UK exporters will only be entitled to portions of the TRQs not taken up already by EU exporters.

## **AUTOMOTIVE SECTOR**

The CEPA provides for phased reductions of tariffs on consumer road cars and car parts. These tariff reductions largely replicate those provided for in JEEPA, however CEPA includes new immediate tariff reductions for some additional categories of car parts.

Manufacturers' ability to utilise these tariff reductions, however, depends on the rules of origin—which determine the criteria that products must satisfy in order to be regarded as "originating." For complex manufactured products such as automobiles—where inputs are typically produced in a number of different countries—rules of origin are critical for determining whether tariff reductions can be accessed in practice.

Because of the high degree of integration between UK, EU and Japanese automotive supply chains, the ability to cumulate EU and UK content for the rules of origin purposes is critical to maintaining the economics of these

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<sup>2</sup> *Scrutiny of international agreements: UK-Japan Comprehensive Economic Partnership Agreement*, House of Lords European Union Committee para published 20 November 2020.

operations. For this reason, a key priority for UK and Japanese car manufacturers was that CEPA would "*facilitate cumulation of EU inputs of production in future UK-Japan automotive trade and [...] provide business continuity*".<sup>3</sup>

CEPA partially achieves this objective. It allows for EU content to be taken into account (or "cumulated") for the purposes of meeting the rules of origin requirements for UK-Japan trade. However, fully replicating the pre-Brexit terms of trade between the UK, Japan and the EU would have required a 'trilateral' agreement between all three parties—which has not been forthcoming. The EU-UK TCA provides some further relief for auto manufacturers by eliminating tariffs between the UK and EU—however the elimination of these tariffs is subject to a separate set of rules of origin—which do not permit cumulation of Japanese content.

Collectively, these agreements are likely to ensure that many of the most significant disruptions to Japanese automotive supply chains which would have occurred in the absence of deal have been avoided. However, the full long-term impact of these new (and more cumbersome) arrangements for Europe's delicate automotive supply chains remains to be seen. This is particularly so given broader supply chain disruptions caused by the rapid growth of electric vehicles.

## **INVESTMENT PROTECTION**

The CEPA includes the rather unique "*Investment Liberalisation*" provisions (Chapter 8) agreed in the JEEPA. As noted in our [briefing on JEEPA](#), these provisions are limited in nature and do not extend to protections usually found in investment treaties such as protection from expropriation or the obligation on the state parties to treat investments in a fair and equitable manner. In any event, neither JEEPA nor the CEPA contain a mechanism for investor-State dispute settlement so none of the investment liberalisation measures are enforceable by Japanese or UK investors.

However, unlike the EU, the UK has expressed an intention to enter the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (**CPTTP**) – a treaty which does include more regular investment protections backed up with investor-state dispute settlement (**ISDS**) provisions. This intention was clearly in the minds of the negotiators of the CEPA as reflected in a side letter which essentially confirms Japan's "*firm determination*" to support the UK's accession to the CPTPP. Additionally, the CEPA includes a provision allowing for either party to request inclusion of investment protection and ISDS in the future, if the other party includes such provisions in a treaty with a third party in the future (Article 8.5(3)).

## **POST-BREXIT ECONOMIC RELATIONS BETWEEN JAPAN AND THE EU**

One area to watch will be the ongoing question of data transfer between Japan, the UK and the EU. Japan currently has an 'adequacy' decision from the European Commission in respect of personal data protection, essentially deeming that Japanese regulation affords 'adequate' protection for individuals'

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<sup>3</sup> UK Society of Motor Manufacturers and Traders (SMMT) and Japan Automobile Manufacturers Association (JAMA) [Joint Position Paper](#), July 2020.

rights and freedoms for their personal data and facilitating transfers of personal data between the EU and Japan.

The European Commission was due to provide a determination on UK adequacy before the end of the transition period (on 31 December 2020). However, the decision is still pending. For now, the EU-UK TCA contains an "Interim provision" consisting of a "specified period" of four-months, extendable to six months, during which transfers of data from the EU to the UK can continue as long as the UK maintains its current rules.

However, if the UK decides to diverge from EU personal data protection standards and is not deemed 'adequate' by the Commission, this might have knock-on effects for Japan. As set out above, the CEPA facilitates the transfer of data, including personal data, between Japan and the UK. Even if the Commission considers Japan's domestic regulatory regime is adequate, it may consider that EU citizens' rights cannot be assured if data transferred to Japan can be freely transferred onwards to the UK.

More generally, Brexit has impacts across the board for Japanese companies with supply chains that cross between the EU and UK. While the EU-UK TCA provides welcome relief from tariffs, companies moving goods between the UK and EU now need to navigate new issues such as rules of origin, customs and SPS processes, product standards and labelling, and other regulatory requirements (such as chemicals registration under REACH and UK REACH). While some of these new processes are still being phased in over the coming months, it is critical for businesses to identify how their supply chains may be affected by these changes and prepare accordingly.

## **FURTHER INFORMATION**

Clifford Chance's international trade and investment arbitration experts assist governments and corporate clients to navigate the complexities of international trade and investment agreements and can provide guidance on investment treaty structuring. This note is an overview only and is not legal advice. For further information on the CEPA, or if you would like to know more about the implications of free trade agreements and investment treaties, please contact one of the individuals listed below.

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