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Brexit – Trade and Cooperation Agreement: The Proof of the Pudding Is in the Eating

On 1 January 2021, the United Kingdom became a third country to the European Union. In this article, the authors analyse the indirect tax aspects (customs/VAT) of the trade in goods between the European Union and the United Kingdom resulting from the Trade and Cooperation Agreement.

1. Introduction

On 23 June 2016 (the date of the UK referendum) the United Kingdom voted to leave the European Union. Roughly four-and-a-half years later (i.e. four years, six months and nine days, or exactly 1653 days) the transition period came to an end, on 31 December 2020. As from 1 January 2021, the United Kingdom became a third country to the European Union. Just a few days before the end of the transition period, on 24 December, a Christmas present in the form of a Trade and Cooperation Agreement[1] between the European Union and the United Kingdom (hereinafter the EU/UK TCA) was put under the Christmas tree. The agreement is designed to protect EU interests, ensure fair competition and more importantly a continued cooperation in areas of mutual interest. In this respect, the TCA consists of three parts, namely a free trade agreement (FTA), a close partnership on citizens' security and a governance framework.

In this article, the authors focus on the indirect tax aspects (customs/VAT), as regards the trade of goods between the European Union and the United Kingdom, resulting from the TCA. The trade of goods between Northern Ireland and the European Union is governed by the Northern Ireland Protocol,[2] which is a separate agreement reached between the European Union and the United Kingdom. The latter also came into force on 1 January 2021. The Northern Ireland Protocol falls outside the scope of this article.

2. Customs

2.1. Customs formalities

As from 1 January 2020, all flow of goods between the United Kingdom and the European Union qualifies as exports and imports. Therefore, customs declaration formalities apply to the trade of goods between the European Union and the United Kingdom. An import and/or export customs declaration (alternatively a transit declaration could also be an option) is to be lodged each time a good is brought into the European Union or the United Kingdom. From an EU perspective, no transition period is foreseen. In other words, as from 1 January 2021, import/export declarations are to be drawn up.

The United Kingdom foresees in a (optional) delay period for import declarations relating to the import of EU goods into the United Kingdom. Said delay can only be applied with regard to so-called non-controlled goods[3] that are in EU free circulation between 1 January and 31 December 2021. Without the need for an authorization, the importation of these goods into the United Kingdom can be declared by entering the goods into the importer's own records whereby the full information about the goods is to be sent to HMRC within 175 days through a supplementary declaration.

From a VAT perspective, these customs declarations play a crucial role. Whereas article 146 of the VAT Directive[4] foresees a VAT exemption (zero rated)[5] for the exportation of goods, proof of the actual shipment of the goods outside the European Union will be required to substantiate the application of said VAT exemption. It results from the term "dispatched" in article 146 of the VAT Directive, that the export of goods is effected and the exemption (zero rate) of the supply of goods for export becomes applicable if the supplier establishes that the goods have physically left the territory of the European Union.

The required documentation to substantiate the application of the VAT export exemption varies between different Member States. Although the Court of Justice of the

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1. *Trade and Cooperation Agreement between the European Union and the European Atomic Energy Community, of the One Part, and the United Kingdom of Great Britain and Northern Ireland, of the Other Part*, available at https://ec.europa.eu/info/relations-united-kingdom/eu-uk-trade-and-cooperation-agreement_en (accessed 21 Apr. 2021) [hereinafter *EU-UK TCA*].
2. Protocol on Ireland/Northern Ireland, available at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/840230/Revised_Protocol_to_the_Withdrawal_Agreement.pdf (accessed 21 Apr. 2021).
3. HMRC has published a list of controlled goods for which the normal rules as regards import declarations are to be followed. It concerns for example excise goods; controlled drugs, rough diamonds. The complete list can be found on https://www.gov.uk/guidance/list-of-goods-imported-into-great-britain-from-the-eu-that-are-controlled (accessed 21 Apr. 2021).
4. Council Directive 2006/112/EC of 28 November 2006, on the common system of value added tax, art. 85, OJ L347/1 (2006), Primary Sources IBFD [hereinafter VAT Directive].
5. A VAT exemption is foreseen for the exportation of the goods by the vendor (art. 146(1)(a) VAT Directive) as well as for the exportation of the goods on behalf of a customer not established in an EU Member State of exportation (art. 146(1)(b) VAT Directive).

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European Union (ECJ)[6] has already confirmed several times that the failure to comply with the formal requirement cannot lead to the exporter losing its right to the VAT exemption for export supplies, it is clear that holding a valid export declaration will facilitate the required proof of dispatch.

As regards the importation of goods, the import declaration is important both for the determination of the taxable amount of the importation and as proof to substantiate the right of VAT deduction of the incurred import VAT. On the one hand, the taxable amount from a VAT perspective shall be the value for customs purposes,[7] so that the potential VAT due will have to be calculated on the basis of the customs value as indicated on the import declaration and not on the invoice as received from the supplier. On the other hand, article 168 of the VAT Directive provides that a taxable person may deduct from the amount of VAT for which he is liable the tax due on imported goods where those goods are used for the purposes of his taxable transactions. Important to notice in this respect is that the ECJ ruled in the *Weindel Logistik Service SR spol* case[8] that the importer of the goods does not have the right to deduct VAT where he does not dispose of the goods in the same way as an owner and where the input import costs are non-existent or are not incorporated in the price of the particular output transactions. In the light of the above, it is crucial to properly evaluate the possible impacts in terms of VAT deduction in case of imports not carried out by the owner of the goods, and in particular when the importer acts as service provider (i.e. "toll manufacturer").

2.2. Appointment of a customs representative and EORI number

Who will handle these customs compliance obligations? Under EU law, it is possible to appoint a customs representative.[9] Such representation[10] may be either direct, in which case the customs representative shall act in the name of and on behalf of another person, or indirect, in which case the customs representative shall act in their own name but on behalf of another person.

The foregoing entails that in case of direct representation, the customs representative is not the declarant. Indeed, from a legal point of view, the party as represented by the direct representative is the declaring party and, in this capacity, the latter remains responsible for its legal customs obligations. In case of indirect representation, the customs representative acts in its own name but on behalf of the represented party. Consequently, all legal effects affect the customs representative itself together with his client, who is jointly and liable for customs debts that may arise. The customs authorities will hold both the customs representative and the represented party jointly and severally liable for incorrect customs declarations. For non-EU established companies, like UK companies, an indirect customs representation is required. EU customs representatives should be established in the European Union.

Similar principles apply in the United Kingdom, hence an EU company will be required to appoint an indirect customs representative should the latter envisage conducting international trade activities. With reference to the above-mentioned possibility to apply the (optional) delay period in the issuance of import declarations, to the extent an (indirect) representative in the United Kingdom would be appointed, the latter will have to enter the goods into their records and will be liable for the supplementary declaration.

An economic operators registration identification (EORI) is required from 1 January 2021 for all trade between the European Union and the United Kingdom. An EU EORI number is required to lodge import/exports declarations in the European Union whereas a UK EORI number is required for similar transactions in the United Kingdom.

2.3. Does this automatically lead to the payment of import duties?

The TCA provides for zero tariffs (and quotas) on all goods that comply with the origin rules as set out in the TCA. The tax and economic identity of the relevant goods, also known as its origin, is now crucial to determine whether the relevant product can benefit from the preference of zero tariffs and no quotas under the EU-UK TCA. The myth of no tariffs under the EU-UK TCA applies only to products which:

- have been wholly obtained in the European Union or the United Kingdom; or
- obtain EU/UK origin as a result of processing of the non-originating goods without interruption in the European Union or the United Kingdom. In addition, once the origin of the goods is conferred in the European Union/United Kingdom, the company has to either not remove it by processing operations involving third-countries materials or by processing goods outside of the European Union or the United Kingdom.

Special attention also has to be given to goods that are released into free circulation in the European Union/United Kingdom. Even if these goods were to undergo insufficient processing operations, the goods will as such not lose their origin. However, they will lose their presumption that they are of the preferential origin. Indeed, after all, (EU) customs authorities are unaware what has happened to these goods from the moment they were released into free circulation. As an importer of these goods, the importing company has the obligation to be

6. CZ: ECJ, 28 Mar. 2019, Case C-275/18, *Milan Vinš v. Odvolací finanční ředitelství*, Case Law IBFD, HU: ECJ, 19 Dec. 2013, Case C-563/12, *BDV Hungary Trading Kft. (in voluntary liquidation) v. Nemzeti Adó- és Vámhivatal Közép-magyarországi Regionális Adó Főigazgatósága*, Case Law IBFD.
7. Art. 85 VAT Directive.
8. SK: ECJ, 8 Oct. 2020, Case C-621/19, *Weindel Logistik Service SR spol. s r.o. v. Finančné riaditelstvo Slovenskej republiky*, Case Law IBFD.
9. Under Regulation (EU) 952/2013 of the European Parliament and of the Council of 9 October 2013 laying down the Union Customs Code, art. 5(6), OJ L269 (2013), IBFD Primary Sources [hereinafter UCC], "customs representative" means any person appointed by another person to carry out the acts and formalities required under the customs legislation in his or her dealings with customs authorities.
10. Art. 18(1) UCC.

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in a position to demonstrate, at all times, the origin of its goods.

Based on the TCA as well as on the applicable customs legislation, companies can obtain more clarity on the origin determination or the customs nature of the concerned goods by applying for: (i) a binding origin decision or (ii) an outward processing authorization. It largely depends on the supply chain structure of the concerned company as well as from the nature of the operations conducted by the latter.

How to establish the origin of the goods? The UK TCA allows traders to self-certify the origin of goods and provides for "full cumulation". In that sense, the origin compliance relies on the knowledge of the importer and the statement of origin as provided by the exporter. The exporter shall be responsible for providing sufficient details to allow the correct and required assessment of the concerned originating product. The customs authorities in the country of importation shall not require the importer to submit a translation of the statement on origin. Under article ORIG-19(2) of the EU-UK TCA, a statement with regard to the origin must be made on an invoice or on any other document that describes the originating product in a sufficiently detailed manner. A template for a relevant statement can be found in Annex ORIG-1.[11] While the possibility for a "self-certification" can be perceived as a facilitation towards EU and UK exporters, if not applied correctly, it can entail severe consequences involving repayment of the duties, additional fines, potential late payment interests as well as the possibility of being deprived of the registered exporter (REX) number. In that sense, the customs authorities would prefer the economic operators to first pay the duties and then claim them back, based on the statement of origin. In either case, the binding origin decision, as obtained in the country of importation, can be a solution to possible disputes on interpretation with the customs authorities.

If the relevant product is unable to meet the specific rules for a preferential treatment, or the EU/UK economic operator is unable to prove that the rules were met, the importer will have to pay the applicable most favoured nation (MFN) rate under the UK or the EU tariffs. In this respect, any material which does not meet the origin criteria as set out by the TCA will impact directly and negatively the profit margin of the concerned companies as the latter will have to support unanticipated duty burden on the "non-originating" products.

Companies should therefore dedicate specific attention to the exports of EU products that include UK content, under the EU FTAs. For the EU exporter to third countries, any UK content in the product will have direct and immediate consequences as to whether, under the applicable EU FTAs, the relevant substantive rule of origin can be met or not. It means that EU exporters need to reassess their preferential treatments under, for example, the Comprehensive Economic and Trade Agreement (i.e. CETA) between the EU and Canada considering the relevant impact of the UK materials or production processes.

Within the framework of the CETA and considering imports of new vehicles in Canada, to meet the origin criteria, the concerned car would solely be entitled to incorporate a maximum of 45% of non-EU materials of the final ex-works price of the car.[12] In other words, 55% of the final price of the car has to be based on EU materials and processing. Before Brexit, the EU manufacturer would not need to think twice about the UK content in its exported vehicles. In a post-Brexit scenario, the UK content counts towards the non-originating EU material. It means that if the value of the EU operations and EU material falls below 55%, the vehicle cannot benefit from a preferential rate under CETA and will be subject to MFN rates. Such EU exporters will be treated on World Trade Organization (WTO) terms. *See* Table 1.

For the UK exporters to third countries, the situation is somehow different. The United Kingdom concluded agreements with third countries, explicitly permitting it to "grand-father" the EU agreements. It means that under the UK agreements, the diagonal cumulation is permitted, meaning that the UK content can apply *together* with the EU content.[13] Surprisingly, this fact is largely not reported yet. However, it is crucial for the optimization of the potential benefits in the supply chain. Based on the diagonal cumulation, the UK exporter is treated more favourably in the third country under the UK international trade agreement. Coming back to the previous example, this has the implications shown in Table 2.

It can result in a shift of the export operations to the United Kingdom from the European Union, post-Brexit, if the value of the UK content is significant in the final product. If too difficult logistically, it can mean the loss of preferential treatment under EU agreements and lower preference utilization rates among EU exporters. As evident from the Agreement, the parties will keep an eye on the actual use of these preferences.[14]

11. *EU-UK TCA*, at p. 440.

12. *Comprehensive Economic and Trade Agreement between Canada, of the one part, and the European Union and its Member States, of the other part* [hereinafter CETA], Protocol on rules of origin and origin procedures, Annex 5, available at https://data.consilium.europa.eu/doc/document/ST-10973-2016-ADD-6/en/pdf (accessed 21 Apr. 2021), provides a product-specific rule for the vehicles under HS heading 8702: Production in which the value of all non-originating materials used does not exceed 45% of the transaction value or ex-works price of the product.

13. *See* modifications to the CETA Protocol on Origin, introduced with the *Agreement on Trade Continuity between the United Kingdom of Great Britain and Northern Ireland and Canada* (9 Dec. 2020), available at CP 351 – Canada No.1 (2020) – Agreement on Trade Continuity between the United Kingdom of Great Britain and Northern Ireland and Canada.pdf (accessed 20 May 2021); or changes to the *EEA Agreement*, Protocol 4 on rules of origin, introduced with the *UK-Norway Trade Agreement*, Title II, Art. 3; or changes to the *EU-Japan Free Trade Agreement* ch. 3, available at https://trade.ec.europa.eu/doclib/press/index.cfm?id=1684 (accessed 20 May 2021), introduced with the *UK-Japan Free Trade Agreement* in art. 3(5), ch. 3. available at https://www.gov.uk/government/collections/uk-japan-comprehensive-economic-partnership-agreement (accessed 20 May 2021).

14. *EU-UK TCA*, art. GOODS.16.

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Table 1 – An example of the supply chain complications for rules of origin post Brexit under CETA for EU exporters		
Relevant product	**Before 1 January 2021**	**After 1 January 2021**
A car: – 25% value of the final car in *the United Kingdom* (for example, the UK engine, processing) – 25% value from *third countries* (for example, electronics) – 0% of the EU processing and materials	Under CETA, the car meets the substantive rule and *can benefit from a preferential treatment*	Under CETA, the car no longer meets the substantive rule and *cannot benefit from a preferential treatment*

Table 2 – An example of the supply chain complications for rules of origin post Brexit under CETA and UK-Canada Agreement for the UK exporters		
Relevant product	**Before 1 January 2021**	**After 1 January 2021**
A car: – 25% value of the final car in *the United Kingdom* (e.g. the UK engine, processing) – 25% value from *third countries* (e.g. electronics) – 50% of *the EU processing and materials*	Under CETA, the car meets the substantive rule and *can benefit from a preferential treatment*	Under the UK-Canada Agreement, the car meets the substantive rule and *can benefit from a preferential treatment* *CETA does not apply* (little difference in real life)

3. How Does the TCA Impact the Import VAT Due?

3.1. Payment of the import VAT

To the extent that the EU/UK origin can be proven, the TCA provides for a duty-free importation. This has however no impact on the import VAT. Upon importation of goods (and release for free circulation) into the European Union/ United Kingdom, import VAT becomes due. Within the European Union, several Member States have introduced a so-called import deferral licence (postponed accounting[15]) whereby the payment of the import VAT due can be deferred to the periodic VAT return. Under the assumption of a full right of VAT deduction, the application of such a VAT deferral licence entails that no pre-financing of the import VAT will occur as in the upfront case the import VAT will be reported as payable and deductible VAT in the same periodic VAT return.

The United Kingdom introduced a similar system, also with the aim to avoid any potential negative cash flow effect of the pre-financing of the import VAT. Under the so-called VAT postponed accounting system, import VAT is to be accounted for in the periodic UK VAT return. To the extent that the taxable person has a full right to VAT deduction, the self-accounted import VAT can be deducted through the same periodic VAT return by which any potential pre-financing of VAT is avoided. Important to note in this respect is that when you delay your import declarations (*see* section 2.1.) the VAT postponed accounting is to be used (it is an obligation).

3.2. VAT registration: Fiscal representation

Subject to the terms and conditions of the sale, the goods will either be imported by the seller or the purchaser of the goods. The person liable for the importation will be responsible for the above-mentioned customs formalities and potential related appointment of a customs agent and EORI registration.

Acting as an importer of record, in principle, also results in a VAT registration in the country of importation. In the example of a Belgian company that sells goods to a UK customer, whereby it is agreed that the latter will perform the importation into the United Kingdom, the Belgian company will only be liable for the export formalities. The related import formalities will in the upfront case be dealt with by the UK company. From a VAT point of view, the Belgian company will only perform one taxable transaction, namely a supply of goods which can benefit from the VAT exemption for the exportation of goods. To the extent that parties would agree that the importation would be performed by the Belgian company, the VAT/customs liabilities as regards the importation shift to the Belgian company. The latter will from a customs perspective be liable to appoint an indirect customs representative. From a VAT perspective, the Belgian company will perform an importation into the United Kingdom and a local sale of the goods in the United Kingdom. Said importation and subsequent local sale of the goods will lead to a UK VAT registration. The United Kingdom does not require the appointment of a fiscal representative in this respect.

From an EU perspective, Member States still have the option[16] to impose the obligation to appoint a local fiscal representative. The purpose of such a fiscal representative is to ensure VAT payments by introducing a liable representative established in the Member State.

However, different EU Member States have implemented said option in their national VAT legislation and require

15. F. Annacondia, *VAT on importation – postponed accounting*, sec. 10.5. in *EU VAT Compass 2020/2021*, p. 915 (IBFD 2020); also available as F. Annacondia, *VAT on importation – postponed accounting*, sec. 10.5. in *EU VAT Options Exercised by the Member States*, Global Topics IBFD (accessed 19 May 2021).

16. Council Directive 2000/65/EC of 17 October 2000 amending Directive 77/388/EEC as regards the determination of the person liable for payment of value added tax, art. 1 regarding the modifications of art. 21 of Directive 77/338/EEC concerning fiscal representation, OJ L269/44 (2000), available at EUR-Lex - 32000L0065 - EN - EUR-Lex (accessed 21 Apr. 2021).

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Table 3 – Fiscal representation requirement in EU Member States pre and post Brexit		
Country	**Fiscal representative for non-EU companies (not including the United Kingdom) to conduct taxable operations in your country**	**Fiscal representative for UK companies as from 1 January 2021 to conduct taxable operations following Brexit**
Austria	Required	Required (on the basis of the mutual cooperation clause as foreseen in the EU/UK TCA tax authorities might waive the requirement)
Belgium	Required (but not for Norwegian companies based on mutual cooperation agreement)	Required to date. However, Belgian VAT authorities are considering not to request the appointment of a fiscal representative for UK companies on the basis of the mutual cooperation clause as foreseen in the EU/UK TCA
Bulgaria	Required	Required
Croatia	Required for all except Norway	Not required
Cyprus	Required	Not required
Czech Republic	Not required	Not required
Denmark	Required	Required
Estonia	Required	Required. A UK-based company that does not have a permanent establishment in Estonia and was registered for VAT in Estonia before 1 January 2021 must appoint a non-resident tax representative before 1 February 2021 in order to keep using the VAT number
Finland	Not required in the case of mandatory VAT registration. If a non-EU company wishes to seek VAT registration voluntarily and the company has no domicile or FE in any EU Member State, registration for VAT on application requires the appointment of a fiscal representative	Same rules should apply to UK companies
France	Required	Not required to date – tolerance of the FTA/ required for VAT refund under the Thirteenth Directive
Germany	Not required	Not required
Greece	Required	Required
Hungary	Required	Required
Ireland	Not required automatically. However, Irish Revenue has the power to serve a notice on a non-EU person to appoint a fiscal representative	Not required automatically. However, Irish Revenue has the power to serve a notice on a non-EU person to appoint a fiscal representative
Italy	Required	The Italian tax authorities have published a Resolution letter in which it was confirmed that UK companies may continue to apply for a direct VAT registration
Latvia	Not required	Not required
Lithuania	Required, except Norway	Not required (official comment from the LT tax authority – only on condition that agreement between European Union and United Kingdom will take into effect)
Luxembourg	Not required (only necessary in case of import of goods when the company is not registered locally)	Not required (only necessary in case of import of goods when the company is not registered locally)
Malta	Not required	Not required
Netherlands	Not required (mandatory only for certain goods and import VAT deferment)	Requirement for non-EU company if it wants to use the import VAT deferment or falls within the mandatory application of the import VAT deferment (for certain goods). Not required in case only EU/ local transactions are performed
Poland	Required	Not required
Portugal	Required	Required (for existing VAT registration there is a transition period until 30 June 2021)
Romania	Required	Required
Slovak Republic	Not required	Not required
Slovenia	Required	Required
Spain	Required	Not required
Sweden	Required (but not for Norwegian and Iceland companies based on mutual cooperation agreement)	Not required

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non-EU established companies to appoint a fiscal representative.

The EU/UK TCA however foresees in a mutual cooperation protocol[17] on the basis of which different EU Member States abolished the requirement to appoint a fiscal representative. Table 3 shows an overview of the pre and post-Brexit situation.

4. Conclusion: The Agreement Is Not the Ultimate Solution! Know Your Product and Master Your Supply Chain

The proof of the pudding is in the eating. Roughly five months after the TCA was agreed between the European Union and the United Kingdom it is clear that although it provides for clear benefits for the trade between the European Union and the United Kingdom, a complete duty-free trade is a myth. Only to the extent that the goods are of EU/UK origin can trade benefit from the TCA. Hence potential or even supply chain changes will be required to comply with the TCA. Furthermore, even if a business can benefit fully from the TCA, customs compliance obligations will remain mandatory. For non-established businesses this will in most cases require the appointment of an indirect representative for customs purposes. Besides the customs implications, the actual VAT implications of the EU/UK trade may have to be borne in mind as these may even lead to local VAT registration.

After five months of application of the TCA, it has already become clear that trading under a TCA cannot be compared to being part of the European Union.

17. *EU-UK TCA*, art. 1 of Protocol on administrative cooperation and combating fraud in the field of Value Added Tax and on mutual assistance for the recovery of claims relating to taxes and duties; *EU-UK TCA*, art. CUSTMS.1 and art. CUSTMS.19.

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