Impact of non-tariff barriers as a result of Brexit

Ministry of Economic Affairs and Climate Policy and Ministry of Agriculture, Nature and Food Quality

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Management summary

Background

In the Brexit referendum, the majority of the British population voted in favour of the withdrawal of the United Kingdom (UK) from the European Union (EU). Brexit will happen on 29 March 2019. The UK's exit from the EU will clearly have serious consequences for trade, and the Dutch economy. In addition to direct cost increases due to tariff barriers, Brexit may also lead to the introduction of non-tariff barriers to trade (NTBs) for both goods and services. Recently, various studies have been conducted into the consequences of Brexit. A study by the Netherlands Bureau for Economic Policy Analysis [CPB] published in June 2016, for example, found that the costs for the Netherlands can run up to 1.2% of the Dutch Gross Domestic Product (GDP) by 2030, which is equivalent to around EUR 10 billion, or EUR 575 per resident in the Netherlands. According to the CPB, the industry's most strongly affected by Brexit will be the food-processing industry, chemical industry, plastics and rubber manufacturing, electronics manufacturing, vehicle manufacturing, and metals and minerals industry.[1] In a study published by Rabobank in October 2017, the Dutch bank concluded that a 'hard' Brexit could cost the Netherlands up to 4.25% of GDP growth until 2030, which is equivalent to EUR 4,000 per Dutch worker.[2] Both studies applied a macroeconomic approach. Our study, which supplements these previous studies, aims to map the impact of the NTBs. As such, this study focusses more on the impact of Brexit on individual businesses. In order to prepare for Brexit, both the Dutch government and businesses should identify NTBs that are introduced as a result of Brexit and where possible estimate the costs that will arise from those NTBs.

In view of issues outlined above, the Ministry of Economic Affairs and Climate Policy and the Ministry of Agriculture, Nature and Food Quality engaged KPMG to conduct a study into the quantitative impact of NTB's as a result of Brexit on Dutch businesses.

We have based our study on the following main research question:

What will be the impact on Dutch businesses of non-tariff barriers to trade introduced under the scenario of a hard Brexit, where the UK becomes a third country under the WTO regime, and how could the costs of this be eliminated or mitigated?

Scope

This study focused on NTBs for both goods and services that have a basis in international, European, national and decentralised laws and regulations with respect to market regulation and implementation. The study focusses on the impact of NTBs on the Dutch economy in general, and in particular on businesses that are dependent on trading with the UK and/or unfamiliar with trading outside of the EU's internal market. The outcome of the Brexit negotiations is still unknown. Therefore, the study is based on

[1] CPB (2016). *CPB Policy Brief 2016/07.* Costs for the Netherlands of fall in trade due to Brexit [*Nederlandse kosten Brexit door minder handel*], p. 9
[2] Rabobank (12 October 2017). Permanent damage due to Brexit [*De permanente schade van de Brexit*], p. 9-12

the worst-case scenario of a hard Brexit, meaning that the UK becomes a third country under the WTO regime.

To enable thorough analysis capable of producing concrete insights, we applied a case study based approach, focusing on a number of specific sectors. In selecting the sectors, we considered the economic impact and diversity of the goods and services involved. Based on these aspects, and after consulting with the Ministry of Ministry of Economic Affairs and Climate Policy, the Ministry of Agriculture, Nature and Food Quality and the sounding board group, six sectors were selected: meat, cut flowers, paints, communication equipment (in particular mobile phones and routers/modems), fire extinguishers and accountancy services.

We should point out that this study has further focused on:

— the impact of non-tariff barriers to trade, excluding the impact of tariff barriers (such as import duties);

— the experiences in six sectors in order to gain an initial insight into the impact on Dutch businesses. Therefore, not all insights from this study can be extrapolated to the Dutch economy as a whole, and the overall impact of Brexit is beyond the scope of this study;

— obtaining insight into the impact for individual businesses, in order to support communication by the Ministry of Ministry of Economic Affairs and Climate Policy and Ministry of Agriculture, Nature and Food Quality towards businesses;

— the current (ways of) trading between the Netherlands and the UK. Potential shifts in trade flows are not taken into account.

Approach

The first stage of our study involved compiling an overview of the NTBs that apply when trading with third countries under the WTO regime. To this end, a review of relevant documents was carried out. Furthermore, the Tax Intelligence Solution© (TIS), (an integrated data analysis tool of KPMG Meijburg & Co) was used to compile an overview of NTBs.

In order to map the additional barriers per sector and the impact of NTBs we conducted interviews with civil servants at the relevant ministries, with implementing bodies, sector- and trade organisations and representatives of the business community. This study resulted in the following findings and recommendations. These findings and recommendations have been validated during meetings with the sounding board group and the client.

Conclusion

Brexit day, 29 March 2019, is fast approaching. At present, it is still unknown what form the future trading relationship between the EU and the UK will take. Prolonged uncertainty about the future trading relationship means that businesses and regulatory authorities will have less time to properly prepare for the new situation. Businesses that were interviewed as part of this study indicate that they only make limited preparations for Brexit due to the current uncertainty.

Based on the data available for 2016, the Dutch Customs Administration expects that after Brexit the number of import declarations will increase by 752,000 and the number of export declarations by 4.2 million. Based on an analysis of Dutch VAT numbers in 2016, the Customs Administration has calculated that over 77,000 VAT numbers belong to businesses that supplied goods to the UK (intra-Community supplies) and/or received goods from the UK (Intra-Community acquisitions). Over 35,000 VAT numbers are currently not registered with the Customs Administration. If all these businesses submit import or export declarations to the Customs Administration after Brexit, its number of business accounts will increase by 40%. Brexit will have the biggest impact on this group of businesses, as they currently have no experience in trading with (importing from or exporting to) a third country and the accompanying NTBs.

The NTBs businesses will be confronted with after a hard Brexit break down into two types:

1. General customs formalities;
2. Sector-specific market access requirements.

For some NTBs it is possible to quantify their expected impact. The impact of several other NTB's cannot be estimated at present; the key aspects of these NTBs are addressed under 'overall points of attention'.

1. General customs formalities

General customs formalities apply to the trade in goods, regardless of sector. The various steps of this process are shown in the figure below. The total costs of customs formalities (excluding any applicable customs duties and/or VAT) range from EUR 78.20 to EUR 126.70 per shipment. These costs are based on Dutch rates and exclude the costs of customs formalities related to product-specific requirements. On average, the rates charged in the UK, for example by customs agents, are slightly higher than those in the Netherlands.

It is estimated that the total additional costs due to the introduction of customs formalities for imports and exports of goods between the Netherlands and the UK (excluding any customs duties that may apply) will range from EUR 387.2 million to EUR 627.4 million per year. The actual additional costs that will be incurred will depend on trade agreements made between the EU and the UK, on whether or not businesses decide to outsource activities related to customs formalities, and on the arrangements made between the various businesses involved in the trade process. In addition, the pound to euro exchange rate may be a factor of influence. However, it is unlikely that these additional costs will be borne in full by Dutch businesses. In practice, the allocation of these additional costs will depend on the Incoterm agreements made between the Dutch and UK businesses.

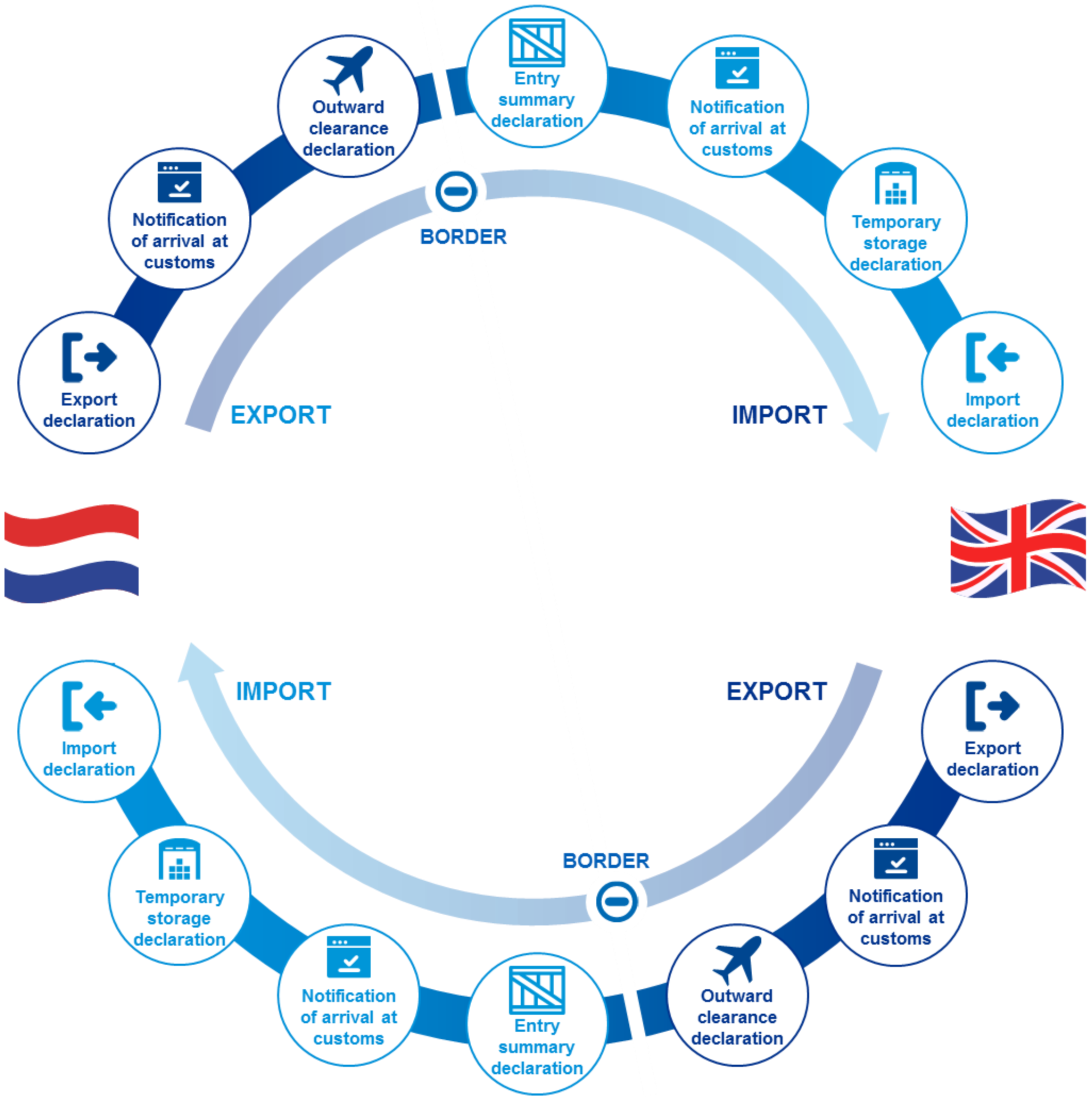

FIGURE 1: **General customs formalities for trade with third countries under the WTO regime**

2. Sector-specific market access requirements

Trading with third countries requires not only complying with customs formalities, but with various market access requirements and related formalities as well. The specifics of these requirements and formalities, as well as their impact, differs per sector. Examples include:

— Strict veterinary requirements for meat products. This means import and export of meat products must be accompanied by veterinary health certificates. The process of requesting, registering and verification of these certificates by various regulatory authorities, costs between EUR 130 and EUR 725 per shipment for the industry as a whole.
— Phytosanitary requirements and the accompanying certification that must be obtained for imports and exports of cut flowers. The costs of complying with these requirements ranges from EUR 120 to EUR 190 per shipment.

- The CE marking requirements for fire extinguishers and communication equipment. After Brexit, the UK may decide to deviate from EU legislation by introducing stricter or more lenient safety requirements. Businesses may have to manufacture or order modified products and/or submit modified technical documentation and declarations. In the case of fire extinguishers, this may have consequences for (already issued) declarations of conformity, which would become invalid if the testing laboratories in the EU are no longer recognised by the UK and vice versa. It costs manufacturers around EUR 3,000 to arrange a conformity assessment (a declaration of conformity remains valid for 10 years). In addition, it costs businesses around 25 hours (or EUR 1,075[3]) to draw up the technical documentation and EU declaration of conformity, to consult about this with the 'notified body' and to arrange the certification of the manufacturing site.
- The requirements paint products must comply with the REACH and CLP regulations. This concerns in particular requirements relating to the classification, labelling, packaging, registration, evaluation, restriction and admission of chemical substances. Businesses that appoint an 'only representative' to perform the activities required to comply with the REACH requirements pay EUR 250 to EUR 500 per substance per year.
- Having to obtain a work permit and additional professional qualifications to be permitted to perform cross-border accountancy services. The total one-off costs for a Dutch accountant who wants to work as a chartered accountant in the UK will range from GBP 996 to GBP 1,938. Conversely, the total costs for a British accountant who wants to practise as an accountant in the Netherlands will range from EUR 1,680 to EUR 4,525.

The total additional costs for the sectors in this study are estimated based on the quantified customs formalities and quantified sector-specific market access requirements. It should be noted that not all NTBs are quantified, resulting in an estimate of costs that represents the expected minimum.

For the sectors included in this study, the expected annual cost increase as a result of NTBs due to Brexit, is the largest for the meat industry (EUR 9.9 million to EUR 27.9 million; 0.,7% to 1.9% of import/export value) and the cut flowers sector (EUR 4.4 million to EUR 7.3 million; 0.8% to 1.3% of import/export value).

Unlike the trade in goods, it appears that cross-border accountancy services will be impacted by Brexit only to a limited extent. As both the Netherlands and the UK already require that foreign accountants meet additional quality standards, it appears that the impact is limited to the request of a work permit. This is because the internal market has been standardised to a much greater extent for goods than for services.

The table below shows the expected costs per sector.

[3] This is based on the standard internal hourly rate for clerical staff of EUR 37 (2007 price level) as stated in *Meten is Weten II*, a manual published by the Dutch government to assist businesses in calculating their administrative burden. After indexation, this comes to EUR 43 per hour (2017 price level).

Sector	Market size (EUR million in 2016)	Costs of NTBs (of which customs formalities) (EUR million per year)	% costs/market
Meat	1,439.5	Min: 9.9 (1.9) Max: 27.9 (3.0)	Min: 0.7% Max: 1.9%
Cut flowers	573.4	Min: 4.4 (1.5) Max: 7.3 (2.4)	Min: 0.8% Max: 1.3%
Paints	492.8	Min: 1.9 (1.9) Max: 3.1 (3.1)	Min: 0.4% Max: 0.6%
Communication equipment	2,648.1	Min: 11.7 (11.7) Max: 19.0 (19.0)	Min: 0.4% Max: 0.7%
Fire extinguishers	3.6	Min: 0.03 (0.03) Max: 0.05 (0.05)	Min: 0.8% Max: 1.3%
Accountancy services	Unknown[4]	**Dutch accountant in UK[5]** Min: GBP 996 Max: GBP 1,938 **UK accountant in Netherlands[6]** Min: EUR 1,680.35 Max: EUR 4,525.35	Unknown

TABLE 1: **Overview of total estimated costs of NTBs (including customs formalities) per sector per year (related to market size)**

3. Overall points of attention

In addition to the above-mentioned requirements, this study identifies the following overall points of attention:

— **Businesses have not (yet) given sufficient attention to Brexit**: The main reason cited for this is the uncertainty about the future trade relationship with the UK. A as result, businesses are preparing for Brexit only to a limited extent.

— **Concerns about insufficient capacity at regulatory authorities**: Both the Dutch and UK customs and regulatory authorities have insufficient capacity to carry out the additional controls and inspections required as a result of Brexit.

— **Brexit requires more personnel with customs expertise**: Brexit will lead to an increase in the demand for personnel with customs expertise. This means that both government bodies and businesses will have to invest in personnel with extensive knowledge of the customs formalities and sector-specific NTBs applying to trade with third countries. However, the number of job seekers with the required knowledge and experience is insufficient. Due to this shortage, the customs and businesses may find it difficulties to expand their capacity in this field of customs. It is therefore expected that significant delays will occur for some time before these shortages have been resolved.

— **Increase in waiting times leading to additional costs**: The participants in our study fear they will be confronted with waiting times because customs and regulatory

[4] Size of accountancy market cannot be quantified using the data compiled by Statistics Netherlands
[5] One-off costs per accountant.
[6] One-off costs per accountant.

authorities will have insufficient capacity. Delays can lead to value losses on shipments, particularly in the case of perishable goods (meat and cut flowers). As a result, the costs of one day of delay can run op to EUR 360,000 per day for the cut flowers sector as a whole.

Furthermore, delays lead to unpredictability in the logistics chain, meaning that businesses will have to make more frequent use of 'last minute' carriers charging premium rates, rather than the budgeted carrier rates. Depending on how the parties in the logistics chain have arranged these issues in their (long-term) carrier-contracts, these additional costs will be borne by various parties in the chain.

Given the large volume of goods in transit passing through the Netherlands, Dutch law enforcement authorities, such as the Dutch Customs Administration, carry out controls at the external border on goods in transit that leave the internal market through the Netherlands. These border controls and subsequent delays may have an adverse on the position of the Netherlands as a major hub for transit trade.

- **'Virtual land border' for ferries**: Ferry terminals currently have insufficient capacity (in terms of staffing levels, expertise, authorisations and available physical space) to act as external border points. If no adjustments are made, the combination of the two transports flows (passengers and goods) that flow through the ferry ports will probably lead to additional delays.
- **Supply chain may have to be redesigned, leading to high additional costs**: In view of the above-mentioned delays, various businesses in our study stated that they expect having to make changes to their supply chain. This could include, for example, changing logistics routes, expanding or redesigning distribution centres or relocating production facilities to avoid additional import or export obligations and/or delays.
- **IT investments required for trade with third countries**: Changing current IT systems of businesses to accommodate trade with third countries (instead of intra-Community) will cost businesses a lot of time and money (particularly those with no experience in trading with third countries). The costs of putting in place new software will vary, but this will often involve a one-off cost of EUR 20,000 to EUR 50,000.
- **Concerns about market disruptions due to Brexit**: Dutch businesses state that the UK demand for goods already decreased due to the uncertainty created by the impending Brexit. The depreciation of the pound against the euro may also be an adverse factor. These developments could trigger a surplus of goods on the EU market leading to lower prices. Whether this actually happens will depend on the extent to which Dutch businesses are able to find new export markets and adjust production to the changing demand. Some of these aspects have already been explored in studies into the impact of various Brexit scenarios on specific sectors.[7]
- **Potential double costs due to diverging of quality standards**: As a result of Brexit, quality standards for goods may start to diverge, meaning that the UK will introduce different standards for goods than those currently applied by the EU. This could be the case for certificates for meat and cut flowers, for example, but also for CE markings.

[7]See for example the study by Wageningen Economic Research (Van Berkum and Terluin, 2016).

Recommendations

This study investigated what concrete solutions can be developed to (partly) eliminate or mitigate the identified non-tariff barriers to trade. We also looked at what impact these solutions will have on the size of the identified non-tariff barriers to trade. Below we present our key recommendations, which are partly based on our meetings with stakeholders from the various sectors we looked at in our study.

1. What can the government do?

The Dutch government could take a number of steps to mitigate the impact of Brexit on Dutch businesses, such as:

— Step up government efforts to inform businesses in order to ensure that they are optimally prepared for the consequences of Brexit. The Confederation of Netherlands Industry and Employers [VNO-NCW] and SME Netherlands [MKB-Nederland] indicated that they are already setting up an information campaign about the impact of Brexit and how businesses can prepare for it. This applies in particular to 35,000 businesses that account for a large share of imports from and exports to the UK, but which currently do not trade with third countries. These businesses are expected to continue to trade with the UK after Brexit, but have no experience with the cross-border trade in goods with third countries.

— Explore the option of linking Dutch and UK customs systems to enable automated customs data sharing between the Netherlands and the UK.

— Make arrangements with the UK in order to prevent the diverging of quality standards for goods, by as much as possible continuing the quality standards that currently apply to the trade between the UK and other EU member states.

— Take steps well in advance to expand the capacity and number of inspection locations of customs and regulatory authorities, such as the Dutch Customs Administration, Netherlands Food and Consumer Product Safety Authority and Quality Control Bureau, so that they will be able to handle the additional controls and inspections, and ensure that these authorities perform a Brexit analysis, if they have not already done so.

— Introduce a fast lane / green lane for customs clearance for certain perishable goods to prevent long delays that may affect the quality of perishable goods and cause value losses.

— Explore the options for performing on-board customs controls and letting the Netherlands Food and Consumer Product Safety Authority and Quality Control Bureau perform on-board inspections for goods transported by ferry between the Netherlands on the UK, in order to avoid delays due to border controls at the ferry terminals.

— Explore the option of setting up an IT system enabling businesses to automatically submit data on goods required for customs formalities. Short lead times for transports by ferry creates problems in terms of submitting the various declarations and notifications in time. Operators of port community systems already have experience in setting up such IT system.

- Explore the opportunities for introducing a transitional period. This would be a period following Brexit day during which transitional law applies, meaning that the introduction of new diverging regulations as a result of Brexit is deferred or that these new regulations are phased in during this period. This way, a situation can be avoided where businesses (as well as government bodies) only find out what the consequences of Brexit are just before it actually happens (Brexit day is scheduled for 29 March 2019) and therefore have no time to adjust their operations.

2. What can businesses do themselves?

Despite the fact that the exact consequences of Brexit cannot be fully foreseen at present, Dutch businesses can already prepare for Brexit. Below we present our recommendations for the steps businesses can take already, irrespective of what the exact outcome of the Brexit negotiations will be:

- Perform a Brexit impact analysis to map the consequences for your business. Base this on the assumption that the trading relationship with UK will become subject to the WTO regime. Once you have gained insight into the consequences in terms of both tariff and non-tariff barriers, you could consider the following options, depending on the results of the analysis:
  - For larger trade volumes, it may be more cost-efficient to set up your own process for submitting declarations and notifications rather than outsourcing the process to a customs agent.
  - Consider using the Automatic Periodic Declaration [GPA] system in combination with the Customs Management System in order to set up an automated customs process instead of the regular customs process, in order to save costs and reduce the risk of delays.
  - Consider applying for an Authorised Economic Operator (AEO) authorisation with the Dutch Customs Administration, in order to minimise delays and avoid physical checks and documentation checks.
  - Consider applying for an authorisation to have phytosanitary inspections carried out at your business premises. This can help to avoid waiting times and additional costs.

No regret: perform a Brexit impact analysis.

Many businesses trading with the UK have as yet taken few steps to mitigate the potential consequences of Brexit. That may seem unsurprising, as so many questions are still unanswered. Will there be tariffs (customs duties) for goods? Will agreements be reached on phytosanitary and veterinary inspections? Will the common transit procedure remain in place?

Despite this uncertainty, it is important that businesses look into the potential impact of Brexit on their organisation well in advance. How many shipments do you send to the UK or receive from the UK per year? What types of goods are involved? Do additional measures apply to these goods? How are these goods currently supplied; in large consignments or small shipments addressed to individual customers?

Mitigating measures such as those suggested in our above recommendations take a lot of time to implement. A good example of this is the process of obtaining an AEO authorisation, which usually takes 6 to 12 months. If businesses postpone action until just before Brexit day, many will find themselves in a race against time. It may then be too late to timely implement potential solutions.

Businesses can already perform an initial analysis today to gain insight into the potential consequences of Brexit for their operations.

Some measures may apply under all Brexit scenarios. It is advisable to implement these no regrets measures as soon as possible. Performing a Brexit impact analysis will help to identify these no regrets in a timely fashion.