

A Legal Review on the Modernisation of Customs Union between Turkey and the EU

Different Driving Forces, One Goal

Overview:

The customs union ("the CU"), adopted by the Decision 1/95 of The EC-Turkey Association Council of 22 December 1995 is the main legal source covering the bilateral trade between Turkey and the EU. It is one of the first examples of a trade agreement made by the EU with a non-member state.

As expressed by both EU and Turkey representatives, CU is not an alternative to Turkey's accession to the EU but complementary to it¹. Until Turkey enters the European single market through EU membership however, CU will continue governing the trade issues between the two parties.

Turkey is the EU's 4th largest export market and 5th largest provider of imports. The EU is Turkey's 1st import and export partner representing 41% of Turkey's global trade. The value of the trade in goods between the parties amounts to nearly 140 billion Euros.²

The CU facilitates this bilateral trade by harmonising the customs applications, setting common tariffs and eliminating duties to facilitate the free trade between the EU and Turkey. Its coverage is however limited, as only certain goods benefit from these advantages. This limited scope however became far from addressing the needs of what trade has become between these parties today, after over 20 years.

In fact, since its adoption in 1995, the EU has increased the number of its members from 15 to 28, thus the single market expanded enormously. The EU concluded free trade agreements with other countries like Mexico³ and Canada⁴ and started the Transatlantic Trade and Investment Partnership ("TTIP") negotiations with the US. This affected Turkey's position *vis a vis* the CU, by indirectly expanding the EU market in a one way direction. Turkey presented a major economic growth over the past two decades as well. With all these

¹ <http://trade.ec.europa.eu/doclib/press/index.cfm?id=1307>

² <http://ec.europa.eu/trade/policy/countries-and-regions/countries/turkey/> and http://www.tepav.org.tr/upload/files/1491836076-0.A_Modernized_EU_Turkey_Customs_Union.pdf

³ **Free Trade Agreement between Mexico and the European Union**

⁴ **Comprehensive Economic and Trade Agreement (CETA)**

changes and developments, the volume and nature of the trade between the parties exceeded tremendously what the CU has envisaged in 1995.

Today, there is no doubt that the CU calls for a reformation to adapt itself to these substantial changes and pave the way of fulfilling the full potential of the bilateral trade between these two important trade partners.

The Initiatives:

Turkey and the EU expressed their common intention in this direction on May 12, 2016 through the joint announcement of the EU Trade Commissioner Cecilia Malmström and the Minister of Economy of Turkey Mr Nihat Zeybekci⁵.

Both parties conducted their risk assessment throughout 2016 and signalled at the end of the year that they were ready to move on. The European Commission asked the Council for a mandate to launch talks with Turkey to modernise the CU⁶. The Turkish Minister of Economy announced that Turkey aimed to start the negotiations on the first quarter of 2017 to be completed by the end of 2018 the latest⁷.

The Revision:

At a broader level, what CU urgently calls for is an expansion of its coverage, further harmonisation and simplification of customs laws and applications, and introduction of a dispute resolution mechanism ensuring its efficient application.

The CU harmonises the customs applications and facilitates free trade by Turkey's adoption of EU's common external tariff and by mutual elimination of the customs duties and quantitative restrictions. However, the CU covers merely industrial goods corresponding to only around %25 of the GDP's of the respected markets. The remaining %75 corresponding to agricultural goods and service sectors are not covered by the CU.

There is great interest from both sides to include these sectors in the CU. Agriculture represents %10 of Turkey's GDP and %13 of its global import⁸. Turkey is the seventh largest destination for EU exports and sixth larger agricultural exporter to the EU.

⁵ <http://trade.ec.europa.eu/doclib/press/index.cfm?id=1307>

⁶ http://europa.eu/rapid/press-release_MEX-16-4491_en.htm

⁷ <http://www.hurriyetdailynews.com/complete-update-in-customs-union-deal-to-make-additional-2-pct-hike-in-turkeys-gdp-minister.aspx?pageID=238&nID=107860&NewsCatID=345>

⁸ <http://www.tarimplus.com.tr/dunyada-ve-turkiyede-tarim/tarimin-turkiye-ekonomisindeki-yeri.aspx>

The services sector corresponding to nearly %70 of the EU's⁹ and %60 of Turkey's GDP¹⁰ presents significant mutual benefits as well especially noting the complementary strengths of Turkey (transport, tourism services) and EU (financial, legal, design services) in these markets .

Public procurement is not covered by the CU either. Companies from both sides do not have access to one and others' public procurement markets despite the fact that this was one of the very first goals of the CU. At the time of its adoption in 1995, Article 48 of the CU required the parties to start negotiations for the mutual opening of their respective public procurement markets. These negotiations is about to start now, after over 20 years.

The Efficiency Measures and Legal Requirements:

These being the goals in relation to expansion of the CU's scope, appropriate measures have to be put in place to ensure their efficient application.

Being a party to the CU, Turkey undertakes to align its national legislation with the EU *acquis* for the sake of the bilateral free trade. Turkey will therefore have to amend its food and safety regulations to harmonize with the EU standards for a possible inclusion of agriculture sector in the CU.

Additionally, unlike EU, Turkey is not a party to the Government Procurement Agreement of the GATT of the World Trade Organisation and it is European Commission's own evaluation that Turkey's current national legislation on public procurement providing for some discriminatory practices contains "*gaps with its alignment with the EU acquis*" and "*further efforts are needed in public procurement, an area for potential inclusion in a modernised and extended Customs Union* »¹¹. There will therefore have to be significant policy and legislative work on this aspect as well.

While Turkey undertakes to align itself to the relevant EU legislation, it has no or little impact on their adoption as it is not a member to the EU. The CU does not provide for a solid opportunity for Turkey to have a say in these rules to become indirectly applicable to it. To overcome this asymmetry, mechanisms shall be provided to ensure that the EU lets Turkey in to a reasonable level in the policy and legislation discussions.

http://www.calismatoplum.org/sayi9/aylan_ari.pdf

⁹ https://en.wikipedia.org/wiki/Economy_of_the_European_Union

¹⁰ <https://en.wikipedia.org/wiki/Turkey>

¹¹ EU Commission, Turkey Progress Report, November 2016, Chapter 5. https://ec.europa.eu/neighbourhood-enlargement/sites/near/files/pdf/key_documents/2016/20161109_report_turkey.pdf

The EU can provide flexibility on some other restrictions applied to Turkey arising from not being a member to the EU, like the rather strict visa regime applied to the Turkish nationals. Flexibility on the visa regime especially for the Turkish business would surely facilitate their access to the EU market in favor of trade.

Finally, a dispute resolution mechanism would surely help ensuring compliance of the parties to the CU. As the current CU does not include a proper mechanism as such, disputed issues may remain unsolved for years, causing a blockage in its application. As an example, EU can pass a relevant legislation without any consultation with Turkey, Turkey may not be in a position to align itself with it and this may cause an interruption. A dispute resolution mechanism would provide for the mediation to resolve the issue and proceed.

These being the common goals of improvement of the CU, parties can be said to have some different driving forces to pursue these negotiations.

Free Trade Agreements and Turkey's Position:

The current CU creates a *de facto* asymmetry between EU and Turkey where EU enters into a free trade agreement ("FTA") with a third party country and Turkey is not somehow included to the new setting .

When EU enters into a FTA with a third party, unless Turkey is included in the negotiations or concludes a separate FTA with the same third party; the practical outcome of this would be an asymmetry created in Turkey's disadvantage.

When EU enters into a FTA with a third party country, the third party country goods will be able to enter Turkey with deflection through Europe within the conditions of the CU. However, Turkish goods will not have the same reciprocal access to the third party market unless Turkey is included in the EU- third party negotiation for the FTA or it concludes separate parallel negotiations with the third party country itself.

Turkey's unsuccessful efforts to be included in the EU-Mexico agreement and the ongoing negotiations on the TTIP between the EU and the US proves however that this asymmetry cannot be overcome by the unilateral efforts of Turkey, but an appropriate mechanism must be provided in the CU giving Turkey its place as a trade partner.

The ways to overcome this asymmetry is yet to be discovered, it can nevertheless be said that TTIP negotiations has been an important driving force for Turkey to initiate negotiations on the CU.

The driving force of the EU side can be said to be more general compared to Turkey's. The impact assessment of the European Commission¹² reveals the EU side expects, with a better functioning and modernised CU, prospects and expectations of improved economic growth generated by more integrated economies. The improved preferential access to procurement and services markets will have a positive leverage effect on trade in goods which, coupled with better agricultural access, will increase the level of trade integration and positive spill-over effects on economic growth. The EU expects the SMEs to enjoy improved market access in services areas and in procurement markets, while small agricultural businesses from both sides could enjoy improved market access if they are competitive and export-oriented.

It is important to note that the EU seems to accept the fact that extension of the bilateral trade relations to other areas might counter erosion of current Turkish benefits in the CU following EU comprehensive FTAs with major trading partners however concludes that increased economic integration between the EU and Turkey will attract international investments in the liberalised sectors and consolidate joint business patterns to better compete internally and globally. EU.

Conclusion:

The advantages for both parties in the modernisation and expansion of the CU are clear, just like the key element to facilitate this process. In order to make the best out of the CU and expand beyond, Turkey shall work on its legislation to harmonise it with the EU standards and EU shall more broadly let Turkey in trade policies and discussions.

¹² http://trade.ec.europa.eu/doclib/docs/2017/january/tradoc_155238.pdf