

BREXIT: A TALE OF EXIT OVER VOICE

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‘Membership of the EU is the means by which nation states preserve and protect their interests and values, whereas standing alone puts those interests and values at risk’¹

On the 23rd of June 2016, the UK electorate voted narrowly to leave the EU having joined in 1973, over 43 year earlier. The Lisbon Treaty (2009) made provision for the exit of a Member State under the procedures outlined in Article 50 (EU, TEU). The UK decision was a shock to the EU and a harbinger of political turmoil in the UK. The British Prime Minister David Cameron resigned immediately and was replaced by Teresa May who appointed a very different cabinet which included many of those who had campaigned for Brexit. The referendum outcome destabilised the UK because there was majority support for Remain in Scotland and Northern Ireland. The new UK Government took until March 29, 2017 to deliver its Article 50 notification letter which began the formal process of withdrawal. This was followed by the decision of PM May to call a UK general election on June 8, 2017. The general election did not lead to the expected outcome of an enhanced majority for the Government. Rather, PM May found herself facing a hung parliament when she lost the majority won by PM Cameron in May 2015. This forced her to negotiate support from the Democratic Unionist Party (DUP) of Northern Ireland which has formally agreed to vote with the Government on major issues including the laws related to Brexit (UK Gov, 2017).

The lengthy timespan between the referendum and notification enabled the EU to overcome its shock and begin to prepare for the world of EU27. The heads of government met informally in September 2016

1 Armstrong K.A., 2017, *Brexit Time*, CUP, 282.

in Bratislava to establish a road map for the future development of the Union minus the UK (EU, 2016). This was followed by the issuing of negotiating guidelines and directives in April and May 2017 (EU 2017). This paper analyses the key elements of the negotiating process, the issues to be addressed including the attitudes of the two parties and the position of financial services in these negotiations. By definition, the subject matter of the paper is a moving target given the uncertainty of UK politics and the dynamic nature of the Brexit negotiations.

Managing an Exit

The European Union (EU) is a negotiating machine which has built up an impressive capacity to get agreement among its Member States on a large body of law and public policy instruments. It is also a formidable negotiator in the international arena with over 881 bilateral treaties and 259 multilateral treaties to its name. Following the UK referendum, the EU is embarking on an unprecedented negotiation to agree the departure of one of its largest members. This endows these negotiations with a significance that is symbolic, existential, material and consequential. To put it simply, these negotiations are not about creating a better future but about damage limitation and the attribution of loss from the perspective of the EU. International trade and economic negotiations are usually designed to bring parties together and to arrive at an outcome that is superior to the status quo as possible. The Brexit negotiations, on the other hand, are about disentanglement, new barriers and further differentiation. The UK's partners in the Union neither sought nor favoured Brexit. However, having overcome the initial turbulence associated with the vote, the EU went into problem solving mode and quickly set up Brexit Task Forces in the Commission and the Council. Michel Barnier, a former Commissioner, was appointed by the EU as its chief negotiator from October 1, 2016. The European Parliament, although not a formal negotiating partner, is a key player and has appointed the longstanding senior politician Guy Verhofstadt to act as its Brexit coordinator and spokesperson. There has been remarkable consensus on the EU side that there would be no informal meetings or discussions with the UK authorities prior to the Article 50 notification. The time between July 2016 and end March 2017 was spent by European institutions preparing for the negotiations and the preparations were characterised by meticulous assessment across the entire gambit of EU policies of the consequences of Brexit and the issues associated with disentangling the UK from the Union.

Article 50 established the legal format for negotiations. Once a Member State issues an Article 50 notification, the EU responds with a set of negotiating guidelines agreed by the European Council acting without the country that intends to exit. This is then followed by an agreement to a set of negotiating directives prepared by the Commission and agreed in the Council. Article 50 made provision for the involvement of the European Parliament as it must consent to the Withdrawal Agreement. In addition, COREPER and a specially established Art. 50 Working Group follow the negotiations on a continuous basis. The European Council remains seized of the negotiations from start to finish and reviews, up-dates and develops the negotiating guidelines as the process evolves. In this way, EU institutions and the 27 Member States seek to manage the exit process in as orderly a manner as possible. The UK for its part sits on the other side of the table in that twilight zone between its status as a departing Member State and a third country. At time of writing, the UK has delivered its notification, the European Council has agreed on the guidelines and the Council has agreed for the Commission to initiate negotiating directives. The strategy of the EU27 is to be transparent about all facets of the negotiations and all documents have been made public (EU 2017a). The first formal session of the exit negotiations was held on 19 June 2017 after the formation of the new UK Government.

Article 50 provides not just for the format of negotiations but also the sequencing of the substantive issues that must be addressed in the negotiations. Essentially the process must address three baskets of issues. The first basket is the disentanglement of the UK from the EU which is frequently referred to as the divorce settlement or withdrawal agreement. The second basket refers to the future relationship between the departing country and the EU27. The third basket addresses the transition from basket one to two, in other words the transition arrangements, if any, that will be agreed. Article 50 also makes provision for the automatic exit of the Member State in question two years after the notification unless there is unanimous agreement to extend the negotiating process. Hence, departure negotiations are time bound which imposes urgency on all those responsible for managing the process. As Armstrong pithily put it, 'The clock is ticking down. Time is short' (Armstrong, 2017, 269).

Opening Positions

The opening negotiating positions of the two parties were established in the key official documents that formally began the process. The Art 50 notification letter represents formal UK Government policy which was submitted by the UK on 29 March, 2017 (UK Gov 2017a). The letter set out in broad terms how the UK approaches these negotiations. The letter is very clear about its core objective in the negotiations and that is to agree a 'deep and special partnership' between the UK and the EU, a formula, which is used seven times in the short document. This is further elaborated as a 'bold and ambitious Free Trade Agreement' and an agreement that includes both 'trade and security cooperation' (ibid). Moreover, the UK wants this agreement to be more substantial than anything the EU has ever offered a third country before. There is an ill-disguised attempt at issue linkage given the 11 references to security and 6 to trade. Clearly the UK thinks it has negotiating capital on security. Prior to notification, PM May had made a number of public statements that outlined her Government's position such as the decision to withdraw from the single market and the removal of the UK from the jurisdiction of the European Court of Justice (ECJ).

The letter identifies UK objectives concerning the conduct of the negotiations expressed as a wish to negotiate the future partnership alongside the withdrawal agreement, in other words parallel negotiations to be completed within two years. In addition, there is a desire to move from overarching principles to technical discussions quickly and to disaggregate the negotiations into policy areas. Finally the letter contains a veiled threat about the security consequences of any failure to reach agreement. The document could be summarised as high on ambition but sparse on identifying what the actual content of a 'deep and special partnership' might be. Crudely it could be translated into the aim of retaining as much access to the single market as possible and the highest level of cooperation within the constraints of UK redlines.

The EU27 response was swift and emerged as a set of negotiating guidelines from the European Council and directives agreed by the General Affairs Council. The dominant and unexpected feature of the EU27 approach has been the unity of the Member States, which is re-stated in the guidelines. The commitment to acting as one has created a pow-

erful soft norm, which will be difficult to dislodge. The EU27 define their objective vis à vis the future relationship with the UK as a 'close partnership' which is not as ambitious as the 'deep and special partnership'. There is however a commitment to working hard and striving towards agreement but within limits designed to protect the interests of the EU, the autonomy of its decision making systems and the role of its judicial processes. There can be no sector by sector approach to the future agreement and any agreement must balance rights and obligations and represent a level playing field. The EU27 identify the three core issues that form part of the divorce negotiations: citizens, the financial settlement and Ireland. The Commission Task Force has produced substantial documents on all three facets of the withdrawal agreement and these negotiating documents have been agreed by the remaining Member States. The focus on citizens relates to the uncertainty caused by the vote for the many millions of citizens who have exercised their treaty right to free movement. There is a desire on both sides to address this issue as the first issue to be dealt with in the negotiations. The financial settlement is likely to be strongly contested as it relates to the post-Brexit budgetary legacy of UK payments to the EU. There is no agreement on the modalities for calculating this or the sums involved. The third issue, Ireland, has received considerable attention because Ireland which will remain a Member State will have the only land border with the UK. Any return to a hard border on the island of Ireland threatens the fragile peace.

The EU27 and the UK differ fundamentally on the sequencing of the negotiations. Whereas the UK wanted parallel negotiations, the EU27 was adamant that the negotiations would be phased and that there would be no discussions on the future relations before sufficient agreement has been reached on the withdrawal agreement. Thus, the Brexit negotiations began with a substantial gap between the opening positions of both sides. Successful negotiations require agreement on a shared course of action and this is certainly missing.

First Round of Negotiations

Notwithstanding the fact that PM May did not achieve an overall majority, the opening meeting of the Brexit negotiations went ahead as planned on June 19, 2017. The meeting was largely procedural with the aim of

agreeing terms of reference for the conduct of the negotiations. Agreement was reached on the structure of the negotiations, negotiating texts, the frequency of negotiating rounds and other modalities of the talks. Working groups have been set up to address citizens' rights, the financial settlement and other separation issues. In addition a dialogue has been established concerning the Irish border. The distinction between working groups and a dialogue underline just how complex and difficult the question of the Irish border is although both sides have pledged to achieve as frictionless a border as possible. The border question hinges on the customs union. If the UK exits the customs union, which remains its stated policy, then there will have to be EU border checks and controls. The UK will not be granted the benefits of customs union membership without the obligations. There may yet be differentiated treatment for Northern Ireland but this would require agreement on issues of rules of origin, co-operation between customs authorities on both sides of the border and risk management to ensure that the Irish border did not become a smugglers paradise.

Both sides entered the negotiations divided on substance and process. The likelihood of getting to 'yes' depends crucially on the first phase, on creating sufficient trust and momentum to propel these negotiations forward. Unfortunately for the UK, it will have to do significantly more than the EU27 to achieve this because it is the Member State that has opted for exit over voice. This will be difficult because of the highly politicised nature of the issue in the UK, a weakened prime minister and a deeply divided Conservative party cabinet and party. The Labour party also faces Brexit challenges as it does not hold a coherent and consistent policy. Moreover, the UK's traditional approach to EU negotiations makes it difficult for it to make early concessions in order to generate momentum. The UK has tended in the past to push EU negotiations on every detail rather than establishing broad trade-offs. The UK pattern is to resort to voting against rather than getting concessions as part of the emerging majority and in extremis to look for opt-outs. The UK approach has tended to be 'us' and 'them' rather than viewing the EU as a collective endeavour. The rampant Europhobia of the British tabloid press serves to reinforce difference rather than commonality with the rest of Europe. The UK's traditional strategy will not serve it well in these negotiations. The UK Government has to accept that these are asymmetric in which it is in the role of 'demandeur'. It has limited negotiating capital, is under time pressure and must use its available capital carefully.

An early indicator of the imbalance of forces in these negotiations was the question of the phasing or sequencing of the negotiations. The Minister for Brexit, David Davis, threatened to make this issue the 'row of the summer' but simply caved in at the June 19 meeting. The well-established and well-signalled EU27 position that negotiations must take place in phases won the day. This was always going to be the case as the European Council had not given the Commission a negotiating mandate to do anything other than address the withdrawal agreement and only when sufficient progress is made, to begin discussions of the future relationship. Agreement on the future relationship if as requested by the UK, is a Free Trade Agreement, cannot be concluded within the time-frame allowed for by Article 50 (March 29, 2019). Moreover, the European Council not the UK will decide when sufficient progress has been made. This means that the UK has a major interest in getting the European Council to this position. Moreover, the UK as the country on the way out and the source of uncertainty and disruption for millions of people and businesses must create the incentives for the EU27 to invest in a long-term relationship with it.

Citizens' Move Centre Stage

Creating momentum will depend crucially on the negotiations concerning EU citizens. Michel Barnier, the chief negotiator, signalled at the centrality of citizens' rights in his State of the Union address in Florence in May 2017. His wide ranging address highlighted the complexities of this dossier and the EU27 commitment to protecting the rights of all those Europeans who live in the UK or UK citizens who live in the other EU States. This was followed by the publication of an EU document on Essential Principles on Citizens' Rights on June 12, 2017. The EU set out exacting principles derived from existing EU law concerning the scope of its demands concerning citizens' rights. The EU's side opening demand is essentially that EU citizens should retain all acquired rights.

The UK responded with its first publically available negotiating position on citizens' rights. The negotiations will focus on the differences between the two sides which remain significant. The most important divergence in preference is the role of the European Court of Justice (ECJ). The UK document clearly states that 'The Court of Justice of the European Union (CJEU) will not have jurisdiction in the UK' (UK, 2017, 4). This causes a problem for the EU27 as its stated aim is that 'the Court

of Justice of the European Union should have full jurisdiction corresponding to the duration of the protection of citizen's rights in the Withdrawal Agreement' (EU, 2017,4). The question of judicial enforcement is a major issue of principle and substance for both sides and unless a formula is arrived at to satisfy both parties, no agreement will be possible. The issue of the ECJ is also central to the post-membership agreement and relationship. There are other issues concerning citizens such as the cut-off date for applying for residence and the status of those who arrive after the cut-off date. The UK has promised that it will simplify its bureaucratic procedures. EU citizens will only retain their status in the UK if they do not leave for a period of more than two years. There are also issues to do with family reunification. The reality of Brexit is that EU citizens in the UK will experience a loss of status. The outcome on citizens is not just of importance to those who are affected by it but will have a bearing on the remainder of the negotiations.

Broad agreement on citizens would enable the negotiations to move to the more difficult issues of Ireland and the financial settlement. The financial settlement is the most fraught issue in the first phase given the high salience of UK budgetary contributions in the past. Again the UK will have to be flexible and engage actively in identifying what is to be included in the settlement. Without this there will be no move to the second phase and no trade agreement. If on the other hand, the European Council could agree by the October or December EC meeting that the second phase should begin, then the outline of a future deal and transitional arrangements might be possible within the time frame allotted in Article 50. However, here again, the UK has to be realistic; its future arrangements and benefits will be less than it has now across a wide range of sectors and forms of co-operation.

Financial Services

The impact of Brexit on financial services is entirely dependent on the future relationship that is negotiated between the EU27 and the UK. There is uncertainty about the timing and the outcome of these negotiations and notwithstanding a myriad of Brexit related analyses, it would be foolhardy to predict what might happen by 2020. The issues surrounding financial services relate to regulatory frameworks, equivalence and the ultimate judgements of individual financial institutions wishing

to access the European market. The certainty and clarity that produces a good investment climate has been disturbed by Brexit. It is clear that financial services are of core interest to the UK as the City of London is a global financial centre and is Europe's financial hub. Moreover, the UK has become a service driven economy. The issues that are likely to dominate the negotiations on financial services are (a) the question of passporting rights for financial services, (b) Euro-clearing and (c) regulatory frameworks post Brexit. The objective of the UK will be to retain as much of the Europe related business it now has but in a new regulatory environment as it does not want to come under the jurisdiction of the ECJ. The Chancellor of the Exchequer in his Mansion House speech (June 20, 2017) acknowledged that 'as Britain leaves the EU, there are genuine and reasonable concerns among our EU colleagues about oversight of financial markets that will then be outside the EU jurisdiction' but he went on to say that 'avoiding fragmentation of financial services is a huge prize for the economies of Europe' (HM Treasury, 2017). The sub-text of his argument is, on the one hand, that there are significant regulatory challenges arising from Brexit, but that on the other hand, if the UK loses its current status this would also harm Europe. His offer is a 'new process for establishing regulatory requirements for cross-border business between the UK and the EU. It must be evidence-based, symmetrical, and transparent' (ibid). Just how prepared the EU27 will be to offer the UK and the City of London a regulatory framework that allows it to retain all of the EU related business that it now has is impossible to predict given that there is as yet no negotiating document on this issue. It seems highly unlikely that the EU will agree to passporting, highly accommodating deals on equivalence, and the euro clearing market for a third country. The current conditions for UK financial services are unlikely to persist in the post-Brexit era. This does not mean that the City will cease to be a key player in financial services but it is unlikely to escape some costs and consequences of Brexit.

Conclusions

At the time of writing the formal process of Brexit negotiations has commenced and given the legal rules, the UK will leave the EU on March 29th mid-night Brussels time. This exit date cannot be changed without the agreement of all 27 Member States. Given that the process has begun, it is likely although not certain that the UK will depart the European Union

in 2019. Political turbulence and fragility in London will hamper the UK Government's ability to get the necessary legislation through Westminster and any future deal will go back to Parliament. The Parliament may return the issue to the people so that they have voice on the terms of exit. The relationship between London and the devolved administrations is also fraught and may spring some surprises. Nor should we take for granted that agreement will be reached between the EU27 and the UK. The negotiations could stall on any number of issues over the next two years and in any event two years is not enough to negotiate a significant post Brexit relationship. The UK retains the right to leave without an agreement and to resort to WTO provisions, which do not in any case, cover the entire range of EU co-operation. Such a unilateral move would raise the costs and consequences of Brexit in unforeseeable ways and would represent an extraordinary fissure in UK relations with its near neighbourhood. Opting for national self-determination, the formula outlined in the withdrawal letter in a highly interdependent 21st century world, is an extraordinary gamble for a once great power. Paradoxically, PM Cameron's desire to take the 'European Question' out of UK politics by holding a referendum has only served to heighten its salience and the divisions with the UK on the issue. It is reminiscent of the 'Irish Question' which dogged UK politics through the 19th and 20th centuries and although both islands had achieved a *modus vivendi* by the end of the 20th century, Brexit also re-opens the question of Ireland.

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