

## Brexit Requires Five Difficult Negotiations

*By Sir Michael Leigh*

**In Brief:** Five principal sets of negotiations must be completed before Britain can extricate itself from EU institutions, joint policies, and financial commitments and recalibrate its external relations. Divorce negotiations are the first challenge, which should take into account the framework of future relations between Britain and the EU. As a long-term agreement will take time to negotiate, interim or transitional arrangements will be needed to smooth Britain's exit. Britain will also need to activate its membership in the WTO and wishes to negotiate new agreements with countries around the world. Britain's departure will have a profound effect on the EU and divert attention from efforts to solve its other pressing problems.

### Introduction

Donald Trump's support for Britain's exit ("Brexit") from the European Union and his scorn for multilateral organizations have heartened euro-skeptics in Britain and elsewhere in Europe. Britain's prospects for concluding a bilateral free trade agreement with the United States after Brexit were downplayed by President Barack Obama but revived by Mr. Trump. His undiplomatic championing of extreme "Brexiters" has, however, raised hackles among Conservative Party stalwarts in London. At the same time, American liberals still express incredulity about Brexit because they see it as inimical to British and transatlantic interests. Against this background, it is important to come to terms with the complexity of the negotiations which await Britain and its erstwhile EU partners in order to gain a clearer view of likely developments.

Five principal sets of negotiations must be completed before Britain can extricate itself from EU institutions, joint policies, and financial commitments and recalibrate its external relations. None of these negotiations will be easy. It may not be possible to obtain the approval of all the EU's remaining 27 member states for any wide-ranging agreement covering future U.K.–EU relations, deemed to involve member state legal competence. As witnessed with the signature of the Comprehensive Economic and Trade Agreement between the EU and Canada (CETA), objections are likely to be raised by one or more of the 38 parliamentary assemblies required to approve such agreements. Referendums in a number of the member states cannot be ruled out. Even if Britain leaves the EU as planned by the British government in 2019, aftershocks will continue for a decade or more.

### 1. Divorce Negotiations

Divorce negotiations, the first challenge, can be messy and expensive; that will certainly be the case for Britain and the EU. These negotiations will be about dividing up jointly owned assets and liabilities, from office buildings and diplomatic residences around the world, to the pensions of British EU officials that are currently paid by the EU, and future budget commitments, estimated at around 200 billion euros. Under the EU's multi-annual budgeting system, these commitments extend beyond 2019. Present estimates of

the U.K.'s net liability to the EU vary between 20 billion and 60 billion euros. The declining value of sterling further complicates the calculation of the U.K.'s overall assets and liabilities expressed in euros.

As a member state, Britain is a shareholder in the European Investment Bank (EIB), the world's largest project lender. Britain's paid-in capital of some 3.5 billion euros will be withdrawn after Brexit and callable capital cancelled unless a gradual arrangement is agreed. This will partly counterbalance British financial liabilities in other fields and reduce the EIB's lending capacity.

Britain participates in forty EU agencies with responsibilities in fields as varied as banking, vocational training, health and safety, and medicines. Most are open only to EU members and close associates, like Norway and Switzerland. It remains to be seen whether negotiations will permit Britain to retain membership in some of these agencies. Meanwhile, bidding has opened among member states to take over the European Medicines Agency, which is currently in London and employs close to a thousand people.

Britain will have to quit highly integrated common policies ranging from fisheries and agriculture to the retraining of workers, support for depressed regions, and development assistance. In many fields hitherto handled by the EU, Britain has no capacity of its own and will have to build this up, at considerable expense, in the years ahead. If Britain leaves the EU customs union, it will have to recruit 5,000 additional customs officials of its own. Many more immigration officials will be needed to process visa or work permit applications from EU citizens. Staff will also be needed to work on a host of areas now covered by the EU, including the "Open Skies" air transport agreement with the United States.

Another chapter concerns the status of British residents in EU countries and of British citizens elsewhere in the EU. More French people live in London than in Bordeaux, Nantes or Strasbourg and it is said to be the sixth largest Francophone city in the world. Faced with uncertainty, many French citizens living and working in the U.K. have applied for British nationality. Estimates of the number of Britons living in other member states vary between one and two million. The rights of residence, employment and access to social benefits for all these people will form part of the divorce agreement.

These examples show how much is at stake politically, economically, and financially in the divorce negotiations. And this is the easy part.

## 2. Framework of future relations between Britain and the EU

Under article 50 of the EU's basic treaty, the divorce agreement should take into account the framework of future relations between Britain and the EU, the subject of the second set of negotiations. The Swiss, Norwegian, European Economic Area (EEA), and Canadian models have been considered by the British authorities without being found appropriate. Instead they are seeking a "bespoke" agreement, tailor-made for Britain. British officials would do well to examine the arrangement that has existed for thirty years between Australia and New Zealand, which are not in a customs union but are deeply integrated economically. A flurry of speculation about Britain retaining its existing EEA membership is not likely to produce any practical effect.

For the moment, the British government has no clear public position. Other member states are considering their options but will not formulate their positions until Britain's notification of its intention to withdraw. The British prime minister says that this will happen by the end of March 2017, despite legal challenges. These challenges, if upheld, may lead to the House of Commons having a larger say in shaping Britain's Brexit goals. In reality, serious negotiations will only begin after next year's elections in the Netherlands, France and Germany. This will leave sixteen months or less for real negotiations to take place before the two years stipulated by article 50 run out.

There is room for doubt as to whether two years will suffice to conclude a permanent framework, considering also the other negotiations that will take place during this period and Britain's dearth of trade negotiators.

## 3. Interim or transitional arrangements

If no agreement on future relations is reached within two years, and the remaining member states do not agree unanimously to extend the negotiations, Britain will simply become a third country, like the United States, Japan or any state with no overarching framework agreement with the EU. It will then trade with the EU under World Trade Organization (WTO) rules, once the terms for this have been agreed by all WTO members.

This possibility makes all the more important a third set of negotiations on interim or transitional arrangements between the U.K. and the EU, pending the conclusion of a permanent agreement. The British prime minister has emphasized the importance of transitional arrangements recently. However, she seems to favor sectoral agreements, whether permanent or interim, amounting in practice to cherry picking areas favorable to Britain. Some insiders and the popular press call this "having your cake and eating it." Other member states are unlikely to accept such an approach.

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## 4. Activation of WTO membership

Hitherto Britain's WTO membership has been held in abeyance as the European Union is responsible for trade policy. This membership must be effectively reactivated when Britain leaves the EU so that WTO rules govern British trade with other countries and it enjoys "Most Favored Nation" status, ruling out discriminatory trade treatment. But this will not be the walkover that Leavers imply.

Britain plans simply to adopt the EU's schedule of WTO commitments. This sets out tariffs, quotas, limits on export subsidies and other undertakings that the EU has agreed to apply in trade with WTO members. But the fifteen exporting countries that face high EU import tariffs and quotas for agricultural goods may not accept this. They argue that the U.K. market is much smaller than the EU's and that Britain's future national agricultural support scheme to replace the EU's Common Agriculture Policy (CAP) may damage their exporters. They will demand details of Britain's future trade arrangements with the EU and agriculture support scheme before they agree to its schedule of commitments.

All 164 WTO members must agree to Britain's schedule of commitments and some may make their own demands on quite separate issues. WTO members may also call for adjustments to the EU's schedule of commitments, in compensation for the loss of the British market.

If all this takes longer than two years, WTO members might accept for the time being the U.K.'s adoption of the EU schedule of commitments, while remaining free to invoke the dispute settlement procedure if they consider that their exporters have been harmed. This would ensure that Britain can count on non-discriminatory treatment by WTO members when it has left the EU. Nonetheless Britain's future WTO status cannot be taken for granted and may be the subject of prolonged side talks with a number of states.

## 5. Negotiate trade agreements with countries around the world

There are expectations in London that the Trump administration will move the U.K. to the top of its list of potential bilateral negotiating partners. Before the U.S. presidential election, Prime Minister May had named Australia, China, India, Mexico, Singapore, and South Korea, as key countries open to concluding free trade agreements (FTAs) with the U.K. The prime minister claimed that such agreements would make Britain a "truly global country."

But many Brexit voters thought they were rejecting globalization when they cast their ballot in the referendum on June 23. Besides overcoming such rumblings from public opinion, Britain will need to have exited the EU and activated its WTO membership before formal negotiations with third countries can begin. Before they agree to anything with Britain,

third countries will want to know what trade regime will apply in the future between the U.K. and the EU, a question unlikely to be resolved quickly.

Even though the process could be shortened by borrowing agreed language from existing EU trade agreements, this is clearly a project for five to ten years at least. Putative partners such as India have already made demands for quid pro quos in areas like immigration that the British government will find unacceptable. Some trading partners may not see Britain as a priority, with its 65 million consumers, compared to the existing EU market of over 500 million people.

For now, suffice it to say that this fifth set of negotiations also remains surrounded by uncertainty.

## What does it all mean for the EU?

The EU is beset by multiple disorders and crises as well as insurgent challenges to established political parties and governments. Brexit and the election of Donald Trump have heightened these trends. The EU's international leverage will be diminished by the loss of the world's fifth largest economy, a nuclear power, and United Nations Security Council permanent member, which still has a significant capacity to project power around the globe. Britain's departure will also bring budget shortfalls, obliging the EU to scale down certain of its ambitions.

The Trump era will see growing protectionism and uncertainty about the endurance of U.S. alliances. China and Russia will be quick to take advantage of new divisions, such as those opened up by Mr. Trump's decision to jettison the already fragile Trans-Pacific Partnership (TPP). The proposed Trans-Atlantic Trade and Investment Partnership (TTIP) is likely to be put into the deep freeze. European countries will need to be agile to find compensating mechanisms, a major challenge given their diversity of interests. The difficulty of obtaining unanimity for the signature and then for the ratification of CETA may be a harbinger of things to come.

In these harsher conditions, Europeans will struggle to uphold the EU's founding principles, including the benefits of free trade, as set out by Adam Smith and David Ricardo two hundred years ago. This will be harder still without Britain, a traditional free-trading country. The balance among member states will shift somewhat towards greater protectionism. To persuade Europeans of the continuing benefits of a world open to trade and investment, active measures will be required to assuage the negative effects of globalization on vulnerable sectors of society. Germany, Europe's foremost exporter, will need to take the lead in this effort.

**“ Third countries will want to know what trade regime will apply between the U.K. and the EU ”**

The complexities of Brexit and the current wave of political insurgency in Europe may distract the EU from efforts to resolve its existential challenges over the euro, migration, or instability to the East and the South. But progress in all these areas is crucial to preserve European and transatlantic unity in an increasingly unpredictable world.

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