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FOCUS NOTES

# After the controversial Withdrawal Agreement, what next for Brexit?

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The draft Withdrawal Agreement on a technical level sealed between the UK government and the EU27 on 13 November regarding the terms of the Brexit divorce, was supposed to be a right step towards the UK's orderly exit from the European Union (EU), planned for 30 March 2019. However, fierce opposition to that agreement from all quarters of the UK political spectrum and the resignation of some of the most prominent cabinet ministers, not least the Brexit Secretary himself, made clear that there is still a long and bumpy road ahead in order to avoid a highly disruptive hard, disorderly Brexit.

Political risks have increased. Resignations within the Conservative Party threaten PM Theresa May's leadership while displeasure or even outright opposition from various political parties, put at risk the ratification process of the Withdrawal Agreement.

In what follows, we outline some of the key elements of the Withdrawal Agreement presented in the 585-page long document released on November 14, including the highly contentious issues.

**Key elements of the Withdrawal Agreement**

**I. The key terms of the UK's exit from the EU**

- ✓ *The 21-month status quo transition period after the UK's exit*. It will start on 30 March 2019 and will end on 31 December 2020 (unless both sides agree to extend it). This is to allow time for consumers, businesses and public bodies to adjust to changes in the rules governing their operation as a result of the UK leaving the EU and also for the UK and the EU27 to reach a deal on the new relationship. During the transition period, the UK will retain single market and customs union membership, will follow all EU rules and will continue to abide by the rulings of the European Court of Justice but will lose its representation in EU decision-making bodies, a term that hard Brexiteers strong reject on the grounds that it leaves the UK as a rule-taker and no longer a rule-maker.

  Under the Withdrawal Agreement, both parties will "use their best endeavours" to have a future agreement concluded six months before the end of the transition period (i.e. by 1 July 2020), but, if this proves infeasible, the UK has the right to request from a Joint Committee any time until 1 July 2020 a one-off extension of the transition period. If the future relationship cannot be implemented when the transition period ends (extended or otherwise), the backstop solution for Northern Ireland will come into force (see below for more details on the issue). The draft withdrawal document doesn't clarify how long the transition could be extended (the draft states: "end in 20XX").

- ✓ *EU citizens' rights.* Among others, the agreement safeguards the existing rights of EU citizens who have been living in the UK continuously for five years up to the end of the transition period and vice versa. Those who have not been living in the UK continuously for five years before 1 January 2021 will be granted pre-settled status and can apply for settled status when they have reached five years.

- ✓ *Financial settlement.* Under the mutually agreed methodology for the calculation of the divorce bill, the financial settlement has been estimated at £35bn-£39bn.

**II. Northern Ireland backstop**

This is the most controversial issue that has dominated Brexit negotiations for months. It aims at preventing a hard border between Northern Ireland and the Republic of Ireland (e.g. no checks or physical infrastructure) so as to abide by the 1999 Good Friday peace agreement. The backstop will apply from the end of the transition period "unless and until ... a subsequent agreement becomes applicable". If by July 2020 it is determined that the two sides are not ready to move to a new trade deal and no extension of the transition has been requested, then the Northern Ireland backstop would kick in. It will take the form of a temporary customs union (so-called "single customs territory" according to the Withdrawal Agreement) that will cover all goods except fishery products, encompassing not just Northern Ireland but the whole of the UK. The backstop incudes "level playing field" provisions on state aid, competition, tax and social and environmental standards. In effect, the UK would be enforced to adopt relevant new EU regulations and exchange tax information and reporting on the EU's code of conduct on taxation. Also, the UK would not be allowed to gain a competitive advantage by 'lowering' labour and social protections.

If the backstop is triggered, then disputes will be settled by a five-member arbitration committee. Any issue relating to EU law, however, will not be decided by the arbitration committee but must go before the European Court of Justice, upsetting Brexiteers who want to "take back control" of the rule of the law from Brussels soon after the UK exits the EU.

Northern Ireland, however, will be in a deeper customs relationship with the EU than the UK, and even more closely tied to the rules of the EU single market and regulation in all products, indicating regulatory checks on some types of goods in the Irish Sea. The latter breaks a red line imposed by the Democratic Unionist Party (DUP) of Northern Ireland, the junior partner in the UK coalition government, which has consistently opposed any kind of differential treatment for Northern Ireland in the backstop agreement.

There is no mechanism for the UK to unilaterally exit the backstop arrangement. Taking also into account that the backstop has not end date, hard Brexiteers argue that, under such an agreement, the UK could stay in a customs union arrangement with the EU indefinitely with no influence on its policymaking and unable to pursue free trade deals with third countries. On exiting the backstop, the agreement says that if "either side considers the backstop is no longer necessary, it can notify the other" setting out its reasons. An independent arbitration committee, made up of two members from the UK and two from the EU and one jointly selected chairperson will then meet no longer than six months afterwards, to decide when a UK-wide backstop is no longer necessary.

**III. Political declaration on the framework of the future (i.e. post-Brexit) EU/UK relationship**

The so-called political declaration on the general framework of the non-binding future UK/EU relationship that provides a basis for Brexit negotiations to follow after the UK's exit from the EU, was relatively short and quite vague, as expected. On goods, it foresees a free customs territory "with zero tariffs, no fees, charges or quantitative restrictions on customs and regulatory cooperation", in order to lessen the need for border checks. In another potentially controversial clause, the Withdrawal Agreement gives the UK financial industry only a basic level of access to the EU known as "equivalence". The latter has raised strong criticism by pro-EU MPs from main political parties who argue that the Withdrawal Agreement will leave the UK worse-off than it would be, if it stayed in the EU. This holds true especially for the Labor Party whose leader Jeremy Corbyn made clear that his party will oppose to any Brexit deal that fails to meet the six tests[1] that envision, inter alia, securing "exact same benefits" as currently exist under customs union and single market membership.

[1]The Labor Party's six tests are: (i) a fair migration system in the interests of the economy and communities; (ii) ensuring a strong and collaborative future relationship with the EU; (iii) protecting national security and tackling cross-border crime; (iv) delivering for all regions and nations of the UK; (v) protecting workers' rights and employment protections; (vi) ensuring exact same benefits currently enjoyed as member of the single market and the customs union.

**Rising UK political uncertainty; Theresa May's faltering leadership puts Withdrawal Agreement at risk**

Theresa May secured the "collective" approval of her cabinet on the Withdrawal Agreement on 14 November after a dramatic five-hour meeting. The backing was not unanimous as the cabinet appeared deeply divided. Around ten cabinet members reportedly argued against the deal with four of them resigning a few hours later, putting at risk the future of the Withdrawal Agreement. Moreover, the risk of a leadership challenge on Theresa May has increased substantially. The Chair of the European Research Group (ERG) of Eurosceptic Conservative MPs announced publicly that he has submitted a letter to the Chair of the 1922 Committee calling for a vote of confidence in Theresa May as conservative party leader. According to the most recent press reports, hard Brexiteers are six letters short of the 48 threshold required for triggering a vote of confidence (i.e. 15% of the parliamentary group). Should a confidence vote be triggered, it will likely take place quite soon given its probable impact on Brexit-related uncertainty. Meanwhile, other cabinet members are reportedly seeking to change certain elements of the deal but the EU27 has responded that there is no room for renegotiation, at least not before the UK parliament votes on the Withdrawal Agreement.

Even if the number of hard Brexiteers is high enough to trigger a non-confidence in Theresa May, it is far from clear that she could lose as the ensuing uncertainty of a leadership challenge at this crucial period could potentially be to her benefit. However, if Theresa May does lose —a simple majority of votes against her by conservative MPs (i.e. 158) would suffice—an interim leader will have to be appointed. The process for selecting a new party leader could be fairly quick if there are just two candidates. But, if more than two come forward, the process will likely take long, meaning that the EU and the UK will have to agree to extend Brexit negotiations beyond March 2019 (i.e. beyond the 2-year negotiation period after the withdrawal notification that Article 50 of the EU Treaty provides).[2] The leadership challenge entails a series of voting rounds by conservative MPs for nominated candidates until just two remain.[3] On the flipside (and under our base case scenario), if Theresa May survives a possible leadership challenge, under Conservative Party rules, no further leadership challenge would be allowed for another 12 months. In this case, the Withdrawal Agreement is highly likely to be formally signed-off at an extraordinary EU Council meeting that has been announced for 25 November (as long as "nothing extraordinary happens" until then, according to the President of the European Commission Donald Tusk). Assuming that the EU27 approves the deal, it will still need to be ratified by the European Parliament (simple majority), the European Council (enhanced qualified majority) and the UK Parliament (simple majority). A vote in the UK Parliament is reportedly scheduled for 10 December. It is widely expected to be a tight vote as hard Brexiteers along with some pro-EU MPs within the Conservative Party, the Labour Party, the DUP, Liberal Democrats and the Scottish National Party have been vocal about their uneasiness with the Withdrawal Agreement for different reasons.

Speaking before Parliament in the aftermath of a series of ministerial resignations, the Prime Minister admitted that she shares her party colleagues' concerns but emphasized that the agreement was "truly the best deal" the UK could strike. In spite of widespread criticism in parliament, she defended her Brexit agreement and vowed to see it through, warning that the only alternatives to her deal were leaving with no deal or no exiting the EU at all.

**Parliamentary arithmetic for passing Withdrawal Agreement looks challenging**

Theresa May leads a coalition government comprised of the Conservative Party with 316 MPs and the DUP with 10 MPs, upon who the Conservative Party relies for a small seat majority in the parliament. Out of the 650 lawmakers in the UK parliament, 639 have the right to vote, excluding the seven Sinn Féin MPs who do not take up their seats, the Speaker be rejected, suggesting that the vote will be very tight.

[2] Under Article 50, extension would require approval by the UK parliament and unanimous agreement by the EU27 Member States.

[3] The election for a conservative party leader takes place in two stages: 1) Conservative MPs go through a series of voting rounds with candidates receiving the fewest votes getting eliminated in each round. 2) When the number of candidates comes down to two, the new leader will be chosen by party members (as opposed to MPs) in a postal ballot.

Taking into account that the smaller opposition parties, Liberal Democrats, Scottish and Welsh Nationalists are vehemently opposed to Brexit and are expected to vote against, the ability of Theresa May to get the deal through the UK parliament depends mainly on: (i) how many Conservative Party MPs would vote against (they reportedly vary from 10 to as many as 80). Moderate Brexiteers within the Conservative (and the Labour Party) could potentially fear that voting against the deal could risk the UK crashing out in a 'no-deal' Brexit.[4] On the flipside, hard Brexiteers could fear that voting against the deal could risk revoking Article 50 (i.e. reversing Brexit); (ii) whether she can lure positive votes from the Labour Party which is also internally divided between those who oppose Brexit, those who support it reluctantly because their constituents are in favor of it, and those who are hard Brexiteers. On the view that the Withdrawal Agreement Theresa May will submit to parliament does not certainly meet the party's six tests, the critical issue is how many labor MPs would abstain or would be willing to defy party leader Jeremy Corbyn and back the deal; (iii) whether the objections from the DUP would be mitigated. The party denied reports conveying that it threatened to withdraw its support from the government unless Theresa May resigned as Prime Minister.

**Possible scenarios if the UK Parliament rejects the Withdrawal Agreement**

If the parliament rejects the Withdrawal Agreement, according to UK law, within 28 days the government will have to issue a statement setting out how it proposes to proceed. Parliament would then vote 'in neutral terms'. A rejection will most likely be followed by market pressure that may change the political calculations, potentially resulting in the parliament approving the Withdrawal Agreement in a second vote (assuming that the parliament agrees to hold more than one vote on the agreement). Should this fail, an extension of Article 50 could be the most likely outcome, foreshadowing a protracted period of UK political uncertainty.

Following such a defeat, the UK Prime Minster will probably resign, opening the way for a leadership challenge in the Conservative Party (if there hasn't already seen one). Whether a new leader would stick to the existing withdrawal agreement or lean towards a hard Brexit, is highly questionable. In any case, there is little prospect for meaningful renegotiations as the EU27 have collectively ruled out making major changes on the agreement. In case a new hard Brexiteer conservative leader tries to pursue a no-deal Brexit, given the parliamentary arithmetic, the parliament is most likely to stop him by withdrawing confidence in the government. Alternatively, both the UK and EU will step up their preparations for a no deal Brexit or the UK Parliament will vote in favor of a second referendum. There is considerable uncertainty though over what options would be put to electors if a second referendum were to be held: 'remain/leave' or 'deal/no-deal'.

The chances of new elections being called are probably less than a second referendum. Snap elections would require the government to lose a confidence vote in parliament, which would imply conservative MPs or the DUP would actively vote against the government, which looks quite unlikely at this stage. In case of snap elections though, the Labour Party could potentially win causing new uncertainty about the Brexit outlook.

In any case, the current Brexit deadlock is unlikely to be resolved through the traditional means of a change of party leadership, a new general election or a second referendum. A new conservative leader or a new government would not be able to negotiate a different withdrawal deal. Most importantly, lawmakers' divisions over the Brexit path do not lie merely between traditional political parties but also within them as neither the Conservative Party nor the Labor Party has an internal consensus on a certain Brexit process. As a result, unless

[4]Under a 'no-deal' Brexit, the UK exits the EU abruptly, without agreement on the terms of the Brexit divorce, without a legal basis for trade with the EU and other countries and without transition period (disorderly hard Brexit). Such a development could inflict serious economic damage to the UK, which would have to trade under World Trade Organization (WTO) rules with exports subject to the EU's common external tariffs and associated customs checks as of 30 March 2019.

the parliament ratifies the existing Withdrawal Agreement, a period of extended political uncertainty lies ahead of us. That leaves the UK government and the parliament with no alternative but to ask for an extension of Article 50 to allow time for the resolution of the internal political crisis and the reduction of the disruption risk in the UK economy.

**Timeline to Brexit**

| Date | Event |
|---|---|
| 25 November 2018 | Extraordinary EU Summit on Brexit (assuming "nothing extraordinary happens until then") |
| 10 December 2018 (reportedly) | Meaningful vote in House of Commons |
| 13-14 December 2018 | EU Summit |
| 20-December 2018 | UK Parliamentary recess |
| 7 January 2019 | UK Parliament returns |
| 21 January 2019 | Deadline for a vote on Brexit agreement in UK Parliament |
| Early 2019 | Approval of the EU Withdrawal Agreement Bill |
| 21-22 March 2019 | EU Summit |
| By 29 March 2019 | EU/UK ratification of the Withdrawal Agreement |
| 29 March 2019 | UK exits (11pm) |

Source: EU Commission, House of Commons, Press

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