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July 2, 2018

## **Brexit Update: Keeping Track of the Moving Pieces**

The second anniversary of the Brexit referendum is upon us, an entirely inconclusive meeting between Prime Minister Theresa May and her fellow members of the European Council has just ended, and the proverbial clock continues to count down to the October deadline for an exit deal and the March 2019 exit date. Yet, if anything the situation has become more, not less, complicated and unclear. No definitive deal is in sight. The possibility that the UK may crash out of the EU with no deal appears increasingly – and to business frighteningly – real. And each potential path out of the present morass appears fraught with political landmines.

While Brexit falls further down the list of priorities for the EU27, as member states grapple with a host of other issues, ranging from existential negotiations over migration into the EU to trade issues and reform of the Eurozone, and member states such as Germany and Italy remain more focused on their domestic political dynamics, the British government continues to be at war with itself.

The Conservative government's aptly named "war cabinet" (formally, the strategy and negotiations committee) continues to be split between the hard Brexit faction and the soft Brexit faction. Prime Minister Theresa May's hold on power appears shaky. There are almost daily media reports of infighting and public criticism by one faction of the other (in Westminster parlance, ministers "briefing" against one another), reflecting a complete collapse of party discipline in the cabinet. Each faction angrily rejects the path forward on post-Brexit trade relations with the EU proposed by the other, while the Democratic Unionist Party (DUP) – whose votes the Conservatives need to remain in power – threatens to bring down the government if any of the practical solutions to the status of Northern Ireland is adopted.

At the same time, the opposition Labour Party is also split, and has yet to articulate a clear, unified position on Brexit. While it is generally believed that two-thirds of Labour MPs voted to remain, about two-thirds represent constituencies that voted to leave. Jeremy Corbyn, the Party leader, is ambivalent about the EU as a matter of principle, but a significant majority of his young base of supporters is pro-EU. To add to the internal confusion, the Trade Union Conference (TUC), which is the traditional bedrock of Labour Party support, last week joined with the largest business lobby, the Confederation of British Industry (CBI), to issue a rare joint statement calling for progress to be made in fashioning a post-Brexit trade deal that would protect trade and jobs.

As part of our ongoing effort to keep readers abreast of developments in the Brexit process, we summarize below recent developments and the key issues to follow in the coming weeks. Our update should be read in conjunction with our Brexit Lexicon, which is [available here](#).

### Recent developments

Until some months ago, it was generally expected that the key withdrawal issues would have been resolved and presented to the European Council summit held June 28-29, as a precursor to reaching final agreement by the ostensible October deadline. That did not happen. Little was accomplished, in part due to the lack of progress in the UK-EU negotiations, in part due to the lengthy list of more pressing topics on the EU agenda, and in part due to the UK's inability to state clearly its negotiating position. At the end-of-summit press conference Donald Tusk, president of the European Council, reported that "the most difficult tasks are left unresolved. If we want to reach a deal by October, we need quick progress. This is the last call to lay the cards on the table."

In an effort to hammer out a more coherent negotiating position, the Prime Minister will face her cabinet (meeting in full, rather than the more limited "war cabinet") on Friday, July 6. The purpose of this "summit" is to debate the eagerly awaited next "White Paper" to lay out the government's vision of the post-Brexit relationship with the EU. It is not clear whether the summit will succeed in producing a unified Tory position, and at present there is no clarity on what the White Paper will set forth.

How did it come to this? A quick recap of recent developments:

- The government rightfully claimed victory in Parliament over passage on June 20 of the European Union (Withdrawal) Act, which provided legal authority for the UK's exit from the EU. The Prime Minister managed to turn back a mutiny by the pro-EU faction of her party over the Withdrawal Bill. The battle was over the terms of the "meaningful vote" and whether Parliament would have the right to direct the government as to its negotiating position should Parliament vote down the Brexit deal when it votes on the withdrawal agreement and related framework for the future relationship. The Tory rebels, led by the former Attorney General Dominic Grieve, ultimately voted with the government, fearing (some say) that a defeat for the government could have resulted in the government falling.

The Withdrawal Act sets a deadline of January 21, 2019 for the withdrawal agreement and framework for the future relationship to be presented to Parliament and voted on by the House of Commons. Seven other key legislative bills necessary to implement an orderly withdrawal continue to wind their way through the House of Commons and the House of Lords (including trade and customs bills). It remains unclear how Parliament will act in approving any final deal with the EU and/or allowing the UK to exit from the EU without a deal.

- In early June, the issue of the Irish border dominated the discourse. The issue arises because there are an estimated 275 crossing points along the border between the Republic of Ireland and Northern Ireland, and the imposition of a "hard" border to stop the free movement of people and goods along this border would be highly disruptive to the economies of both Ireland and Northern Ireland, and also undermine aspects of the deal that brought peace to Northern Ireland after years of strife.

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The Prime Minister's latest proposal was a "time-limited goods arrangement," whereby EU tariffs would continue to apply beyond the end of the transition period (which is supposed to end in December 2020) if no agreement has been reached to avoid the re-imposition of the hard border between Ireland and Northern Ireland. The arrangement would remain in place until a technological solution could be found to avoid the hard border. The "backstop," as well as the government's broader proposal for frictionless trade that would take the UK out of the EU customs union, would be enshrined in the July White Paper. The Prime Minister's objective is for the proposal to be accepted by the EU27 generally as well as Ireland, such that they will then begin work on a political declaration in respect of the future trading relationship. The backstop is intended to break the impasse over the Irish border question.

Although the backstop was presented as having the backing of the cabinet, that does not appear to have been the case. Brexiteers Boris Johnson and Jacob Rees-Mogg have attacked the backstop as a means of keeping Britain tied to the EU, potentially indefinitely. It also does not appear that the EU27 will accept the approach.

- The Conservative Party, long seen as the party of the business community, is facing increasingly strong demands from UK business for a post-Brexit trade deal that retains the zero-tariff frictionless borders that business enjoys today.
  - Airbus (which employs 14,000 in the UK and its supply chain supports another 100,000) announced publicly what it is reported to have been saying privately for months – if there is no deal, the company will need to "reconsider its footprint in the country, its investments in the UK and at largely its dependency on the UK." Even an orderly Brexit would result in supply chain disruptions and pose a significant amount of risk. Until there is clarity, the company intends to "refrain from extending its UK suppliers/partners base."
  - BMW and Siemens UK followed suit, as did industry representatives of car manufacturers.
  - UK headlines also are chronicling the challenges already faced by other businesses and service providers dependent on EU citizens, ranging from the health care and home care industries to fruit growers lamenting the lack of seasonal workers.
  - The CEO of the Port of Dover is reported to have said that even a two-minute delay at the ports could mean lines up to 17 miles long, severely impacting just-in-time production and the supply of perishable goods.
  - Contributing to the chaos, industry warnings prompted angry responses by some senior ministers that public criticism of Brexit would undermine the government's negotiating position, while other ministers publicly lamented the spectacle of the party of business in an apparent war with

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business. Throughout this process, proponents of soft or no Brexit have accused the government of having, for far too long, ignored the previously privately-expressed concerns of business.

- In late June, it was reported that the UK has slipped down the G7 league table on growth, with public finances very much under strain. And last week, official statistics were released showing that UK population growth had slowed to its lowest rate in a decade following a 12% decrease in the number of immigrants in the year following the referendum. There was a 43% decrease in the number of people immigrating to the UK to look for work over the last year, with a marked fall in the number of EU citizens seeking jobs. The CBI noted that job vacancies were at a record high and that access to skills and labour was becoming a “huge concern” for UK businesses.
- Last week’s European Council summit seems only to have generated more frustration on the part of the EU27. From their perspective, in the words of the Belgian Prime Minister, the British are still negotiating among themselves, and the extant red lines drawn by the government remain incompatible with the EU’s fundamental principle of the sanctity of the four freedoms. More vocal summit participants in Brussels are reported to have told the Prime Minister that unless the White Paper reflects a departure from the thinking of the past two years, it would be a non-starter. The European Council’s summit statement expressed continued concern over the absence of any consensus on a backstop solution for the Irish border, though it also held open the door in noting that if the UK positions “were to evolve,” the EU27 would be prepared to reconsider its positions.

With so little time left, it is not surprising that concepts that were first floated two years ago following the unexpected outcome of the referendum, such as a Norway-like arrangement for goods with single market membership, European Court of Justice jurisdiction and no seat at the table, or a full customs union, are back in the news. Movement towards a “soft” Brexit is seen by some of the Brexiters as the prelude to a betrayal by the Prime Minister, and could cause her downfall. There have also been calls for a second referendum, once the terms of the final deal with the EU are known, but this proposal is at present not supported by either the Tory or Labour party. It is however now not unthinkable, if still somewhat unlikely.

#### **What to watch for in the next few months**

As we move into July (and the nine-month countdown to March 29, 2019), there are if anything more, rather than fewer, moving pieces to follow:

- *How will the fundamental internal divisions within the cabinet be resolved?* Hardly a day goes by without yet more examples in the press of the war of words between the various factions in the cabinet. A Conservative Party leadership contest cannot be ruled out and, insofar as timing is concerned, the Conservative Party conference at the end of September may preclude the forging of that final consensus until at least October. In the meantime, one or more key ministers may quit (resignations have been threatened, and then withdrawn), which could presage a leadership contest.

- *What position will the Labour Party ultimately adopt?* With the Labour Party itself divided into two camps, one led by Jeremy Corbyn (the Labour Party leader) and the other by Sir Keir Starmer (the shadow Brexit secretary), it remains to be seen which version of the future relationship with the EU (EEA membership, the customs union, the single market or other compromise version of the trade relationship) the Labour Party will ultimately support.
- *Will the EU27 be able to maintain its unity of purpose and its monolithic stance?* The Spanish foreign minister recently suggested that the larger EU member states (including Germany, France and Spain) remain firm in their absolute adherence to the four freedoms and no cherry-picking; other member states may be willing to compromise. There are a number of potential sources of tension among the EU27: for example, which member states will bear the larger shortfall in the budget once the UK stops making contributions; which member states stand to gain the most if, and when, businesses move parts of their operations to the continent. Consensus could fray at different points, but ultimately all member states will need to agree, and therein lies a challenge if one or more wish to play the spoiler card. In the meantime, the fact that the EU faces a range of more pressing questions does not benefit the British. One could see a hardening of the EU position to maintain the integrity of the union post-Brexit to counter the myriad of other challenges the union faces.
- *When does a Brexit deal reached with the EU (with the Irish border question resolved and broad outlines of the future UK-EU relationship) get presented to Parliament?* An increasing number of observers now doubt that the original date of the end of October can be met, and some question whether it will be in November (though this would necessitate scheduling an additional meeting of the heads of government). The Conservative Party conference occurs September 30 - October 3. Others posit that the Brexit deal may need to be finalized as part of the last European Council summit in 2018, on December 12-13. As noted above, the Withdrawal Bill sets a deadline of January 21, 2019 for the Brexit vote.
- *How much clarity will there be by the time of the vote?* It is now generally thought that many aspects of the future relationship between the UK and the EU will be unresolved by October, and indeed may have to be deferred until after the departure date (March 29, 2019). Since Parliament has a key role in approving the overall withdrawal arrangement, it has been assumed that, as part of that approval, the broad outlines of the future relationship would be known. It is not known what Parliament will do if there is no clarity on what it would be approving.
- *How do the issues relating to the border between Ireland and Northern Ireland get resolved?* As noted above, the border is a key obstacle to reaching agreement on the terms of withdrawal. The border goes to the heart of the challenge presented by Brexit – achieving access to EU markets without limiting freedom of movement into the UK. To solve the border issue (that is, avoid a hard border), either all of the UK or Northern Ireland would need to remain in a customs union and single market, at least for goods. The EU27 negotiating position has been consistent throughout – there

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can be no withdrawal agreement without an agreement on the Irish border, which includes the backstop. The two versions of the backstop proffered by the British remain unacceptable to the EU27. And the most practical solution – allowing Northern Ireland to trade freely with the Republic and moving the trade border to the Irish Sea – is profoundly anathema to the DUP and thus if adopted could cause the current government to fall.

- *Could the UK and the EU27 simply run out of time?* In effect (taking into account summer vacations and party conferences), there are approximately six “working weeks” before the October European Council summit, the expected deadline for negotiations to be finalized on the withdrawal arrangements. The EU negotiating team has made clear throughout the process that six months are needed for the deal to be submitted to, and approved by, the member states. This then is what so many who depend on “frictionless” access between the UK and the EU27 fear most. Their voices are likely to become louder in the coming days.
- *How ultimately does the meaningful vote play out?* In trying to predict possible outcomes, this last question may be the most critical. As a result of the defeat of the Grieve amendment, Parliament has fewer formal options. It cannot direct the government to seek specific outcomes. It can, however, vote the withdrawal agreement down, or threaten to do so. The Remain camp, operating largely outside of formal political channels, is ramping up efforts to mobilize public sentiment against Brexit. A weekend march in late June in London attended by a reported 100,000 people and a petition campaign that has garnered 100,000 signatures are the latest by-products of efforts intended to convince MPs that Brexit can be stopped and that the best way to do so is to go back to the electorate (coalescing around calls for a “people’s vote”). Some see in this proposal a potential escape valve for the Prime Minister, who has so little room to manoeuvre.

The next few weeks are likely to produce major new developments (starting with the meeting of the cabinet at the end of this week and publication (or earlier leak) of the White Paper), as Theresa May attempts to find a path forward that does not land her on a political landmine. Will she choose any of the options currently making the rounds, or will she embrace a new approach, or combination of existing proposals? And can she retain her job?

It is unlikely that developments over the coming weeks will bring clarity to those attempting to plan for Brexit. This group covers a significant number of interested parties, ranging from those whose businesses depend on frictionless trade in goods with the EU or access to EU markets for services, to those who may be unable to remain in, or emigrate to, the UK. The Prime Minister needs to achieve consensus within her own government and needs to do so in a way that ultimately will be acceptable to the EU27 as well as to Parliament. As she perceives her mandate to be to “deliver Brexit,” we can expect a coalition of young people and others in the Remain camp to ramp up their efforts to convince Parliament either to reject Brexit or to do so in conjunction with a call for a second referendum. Continued uncertainty, and possibly political chaos, are unfortunately the more likely near-term outcome.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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