



## The British Referendum on EU membership

**Prime Minister David Cameron completed** a surprise victory at the UK General Election on 7<sup>th</sup> May 2015. His electoral honeymoon lasted only a matter of days as questions over the UK's membership with the EU immediately began to dominate the political and media discourse. A key plank of the Conservative Party's pitch to the British electorate was a promise to hold an 'in-or-out referendum' concerning Britain's membership of the European Union by the end of 2017.<sup>1</sup> No sooner was the election won than the anti-European campaign groups began to ramp up their activities in advance of this promised vote. Despite the prominence of the referendum promise and of the perception of anti-European sentiment in the UK at the moment, a British exit from the EU (or 'Brexit') is not a foregone conclusion. The debate is currently mired (and will continue to be mired) in contested economic analysis, the impact of immigration, the muddled and irrelevant waters of the European Convention on Human Rights, the anticipated Greek exit from the euro and potentially the EU altogether (Grexit), the Scottish question and the internal politics of the Eurosceptic political parties. The path through the question as to whether the UK should or will leave the EU is unusually complicated, and within this complexity lies a small amount of uncertainty as to the final result. This brief explores the political and economic context of the Brexit debate, and explores the likely outcomes of this process.

### The Political Context

The European question has been a graveyard for British Prime Ministers since the mid-1960s. The two main political parties have traded their general disposition to the European question during that time. For the earlier part of the debate it was the now ruling Conservative party that pushed for membership of what we now call the European Union, ever since the mid-1980s it has been Conservative politicians who have argued for limitations and exit from the Union, prompted by then Margaret Thatcher's famous regret at having signed the Single European Act, and her successful attempts at securing a European budget rebate. The Parliamentary rebellions by Conservative MPs in the early 1990s both hamstrung the government of Conservative Prime Minister John Major and eventually saw its defeat in 1997. Conversely, it was that victorious Labor government led by Tony Blair that came into office in 1997. Blair is the Prime Minister who heralded the Labor party's general euro-enthusiasm, albeit within a Parliamentary party: their core vote still has a large number of skeptics in its ranks. Within this general context there have been a number of fledgling, nationalistic, but non-fascist parties who have dedicated themselves to trying to force the UK to leave the EU. The billionaire Sir James Goldsmith's Referendum Party gained limited electoral traction, but attracted a great deal of media attention. The insurgent UK Independence Party can be credited with having transformed the European debate in the UK, rendering it hazardous to the electoral health of sitting Conservative MPs to be anything other than Euroskeptics.

UKIP is – as all minor parties are in the UK – electorally hobbled by the first past the post system. In 2010, UKIP attracted 919,000 votes across the UK and secured no parliamentary seats, in 2015, they polled 3.8million votes and only secured one parliamentary seat. Their share of media air time and influence over the European debate far outweighs their ability to secure parliamentary seats. They are led by a charismatic and capable politician called Nigel Farage, who is said to appeal to the ordinary voter by talking in a register they understand, free from professional PR expertise. The common view of UKIP prior to the 2015 election was that they posed the greatest threat to the Conservative party who was perceived to have the largest number of euroskeptic supporters. As it transpired, it was UKIP's performance against sitting Labor party MPs in the working class north of England that had the greatest impact, pushing the Labor party backwards and delivering the first enhanced second term majority of the modern era. Despite his obvious successes and charisma, Farage is a polarizing character, with as much of an electoral constituency vehemently opposed to his politics as swayed by it. Analysts generally regard an 'out' campaign led by Farage as destined to failure precisely because of this polarization.<sup>2</sup> The 'in' campaign does not have such an obvious leader, more the entire weight of the British establishment. UKIP's influence – whilst loud and visible – is felt more in establishing the terms of debate rather than in delivering the volume of votes to the 'out' cause. Whilst the 2014 referendum concerning Scottish independence was won by those seeking to keep the UK together, the outstanding performance of the Scottish nationalists in the 2015 General Election has reinvigorated the independence question. The Scottish National Party is committed to remaining in the European Union. Consequently if the UK as a whole voted to leave the EU, it is highly likely that the Scottish nationalists would table another independence referendum on the premise that independence would equate to Scottish membership of the European Union. This is a vote they would be likely to win. The European referendum does – therefore – have a lot weighing upon it.

### **Government Discipline and Conscience:**

Part of the reason for the Brexit debate finding instant public exposure was the Prime Minister's mishandling of the question of government discipline over this issue of whether Britain should remain inside the European Union. British governments are run on the understanding of collective responsibility and accountability. What this means in reality is that debate and dissent from the government line is expected to be conducted and only conducted within the executive and its sub-committees, rather than in public. Those ministers who feel that they cannot support the government's position, and who want to air their disagreement in public, are expected to resign their ministerial post to do so. The exception to this rule are so-called 'issues of conscience'. In theory any issue that does not form part of an election manifesto might be declared an issue of conscience. In reality, issues of conscience have been restricted to such subjects as abortion rights, capital punishment, and whether to restrict hunting with animals. Conservative euroskeptics have been keen to assert that membership of the European Union is also an issue of conscience, rather than of party discipline. The precedent for this was established in the first referendum on the UK's membership of what was then called the European Economic Community in June 1975, where collective responsibility was suspended on the European question for the duration of the referendum campaign. At this point some 67% of the British voting population elected to maintain the UK's membership.

So, when Prime Minister Cameron suggested that his ministers would be expected to follow the government's line on this issue the large numbers of euroskeptic members of parliament instantly cried foul that this was the government rigging the vote. The problem for the Prime Minister is that the precise number of hard-line Brexit enthusiasts in his Parliamentary party are not known. The figures range from 20 to 100, out of a Parliamentary party of 331 (a majority of just 12).

Some sense of these figures were revealed in a technical debate in Parliament on 16 June 2015. The focus of contention was the issue of 'purdah' in the referendum: this being the rule that government departments may not publish reports or results during an election campaign so as not to bias the outcome. The government are proposing to lapse purdah for the referendum to allow for the result of any (re)negotiation with the EU to be published. 20 Conservative Members of Parliament voted against the government, which is a moderate sized rebellion.<sup>3</sup> But the reality in the Conservative party is that to be selected to run for Parliament a candidate must make some euroskeptic noises, it is no longer tenable to be a euro-enthusiast in the mold of former grandees of the party such as the former defense secretary Michael Heseltine or Home Secretary, Kenneth Clarke. Cameron has compounded his own problems in this regard by loosely suggesting that he would not be seeking a third term in office – thus adding into the mix a host of ambitious contenders positioning for his job (and the referendum provides a fertile backdrop for this activity), and whether his Parliamentary party believe in his authority. The question of authority will partly sit in internal politics, but also in the strength of public support for Cameron: in his ten years as leader he has always personally outpolled his party.

The true number of MPs committed to the UK exiting the EU in the Parliamentary Conservative party will depend on what will have been achieved in Brussels and where public opinion sits coupled with the trap the government laid itself about seeking a renegotiation of the relationship is about to be realized in the actuality of attempting that renegotiation, but the most likely figure is at the higher end of the spectrum. And the problem with the renegotiation is that the issues that are of core interest to the British government are not the same issues that are of interest to their back-bench parliamentarians, nor the instinctive euroskeptics. Whilst the technocratic side of government is primarily interested in financial services, favorable harmonization of standards, and regulatory regimes, as well as access to a wider plate of international trade agreements (such as CETA and TTIP<sup>4</sup>), the partisan element is keen on restricting the free movement of people, of reducing access to welfare payments and public services to those arriving from continental Europe (key tenets of the European project). Thus the renegotiation process – which the Prime Minister announced on 25 June 2015 – is fraught with difficulties in its framing, let alone its delivery, at a time when the bulk of the available political capital is being spent considering and negotiating the anticipated Greek default and exit from the single currency. For a small group of Brexiters, the Prime Minister will always be a closet Europhile, trying to stitch up an 'in' vote at the referendum. The reality is less stark: Cameron and his Chancellor, George Osborne are pragmatists to their core, wedded to economic growth and the perpetuation of Conservative government. They will come down on the side that delivers these two priorities.

## The human rights misnomer in the UK

The European Convention on Human Rights has – despite having no connection to the EU – become a visible part of the ‘European debate’ in the UK.<sup>5</sup> Part of the issue with the ECHR is its incorporation directly into English law by the Blair government. This was done for ideological grounds (the Labor party were keen to further enshrine core rights for British citizens who had hitherto relied upon historical convention and a highly convoluted route to redress) and partly on the efficiency grounds that if the ECHR was incorporated into English law applicants would not need to apply to the Courts in Strasbourg for redress.<sup>6</sup> The ECHR has become problematized in the UK due to a large number of unfortunate rulings on terrorism suspects (in blocking Abu Hamza’s extradition to the US, and Abu Qatada’s extradition to Jordan for example) that has created a largely accepted domestic narrative that the Convention itself and the Courts in Strasbourg make poor decisions that essentially go against the will of the British people. There is a daily diet of media reportage to this effect, and in response Prime Minister Cameron made an election promise to renegotiate the UK’s membership of the Convention (by essentially pushing for the rulings to be advisory rather than binding and when this was refused to resign from the Convention). Immediately after the election there was a rebellion of the qualified lawyers in his Parliamentary party and the measure was dropped.<sup>7</sup> So, whilst the ECHR should be outside of the bounds of the referendum, it will be firmly within the media and public debate.

## The Contested Economic Picture.

The key unstated economic question in the Brexit debate is what kind of economic actors will come to dominate the British economy after the resolution of the debate. Will the economy continue to be strongly influenced by the financial services sector, vested mostly in The City of London, or will – as threatened by major City interests – these banks relocate onto the continent and thus diminish London’s place as a financial center? Nested within this debate is a broader question of in whose interest the Brexit question being asked: there is a stark difference between the core interests of the City of London and those of the ordinary citizen in the wider UK.

The City of London is estimated to account for some 9% of the UK’s GDP and operates as the financial capital for Europe. The impact of Brexit upon The City is likely to be negative. In the recent past the British government has enjoyed great influence over the design of Europe’s capital union. An ‘out’ vote in the referendum will remove any remaining incentive for the UK to sign up to Europe’s banking union. An ‘out’ vote will similarly move the UK outside of the core decision making bodies for reform of European financial regulations and perhaps even the continued design of the internal market. These impacts are likely to be felt in some way during the campaign for the vote, irrespective of the eventual answer: the mantra of the markets disliking uncertainty will weigh heavily as the campaign progresses. And that is in addition to the ongoing tensions between the British government and the financial community over the bank levy, the future status of non-domiciled tax residents, and the post-crisis regulatory environment. There are – therefore – a large number of difficult issues that are of importance to the British government which are further complicated by the EU referendum.

The capital union project has the UK as its largest player. This project – which aims to help remove the overreliance on bank financing across Europe relies upon access to alternative

sources of finance, be they within the bond, securities or equities markets. There is a need for a strong regulatory framework over these emerging markets (to a fear that the 2008 crisis was sparked by an absence of regulation) and the UK is the most developed markets for these products and instruments in Europe. Ordinarily one would expect the regulatory framework to closely resemble that of the most advanced player in this patch – the UK – but there is a chance that competitor nations will seek to head-off the simple uploading of British regulatory norms in part on an analysis that the British system is too acceptant of risk, partly because such an upload would provide British companies with a first mover advantage and partly because of the simple politics involving a reluctance to confer favor upon the UK at a time of uncertainty.

The British government's concerns about banking union apply more to the UK than they do any other EU nation. The British government has made it clear that it does not want to be part of the European banking union project – with its single supervisory mechanism, common resolution authority, and pooled resolution financing. There are good reasons for the UK government to insist on this exclusion at the present, and most surround the competitive advantage The City has. Many of the current objections are specific to market conditions now, particularly the configuration of European financial markets and the current state of financial market disintegration. If the European economy recovers as analysts expect (and hope) it will, banks will once again be doing more business across national borders, and consequently the influence of Europe's banking union on business headquartered within the UK is going to increase. So will the power of European resolution authorities in the event that there is some kind of renewed turmoil, in the short to medium term. The initial hostility of the British government should – therefore – soften the EU into a more cooperative arrangement with the UK and to align more closely to British interests. We have seen this kind of softening as it relates to financial market regulation within the European Banking Authority, in recognition of the UK's position as a financial center and the costs of adapting to these rules. Similarly the decision to allow for euro-denominated clearing outside of the euro area, a bonus for the City of London might also be reversed. So, the referendum removes much of the motivation for flexibility and accommodation the EU will have with the UK, and reinforces the direction of travel that the UK will remain outside of the banking union and that the EU might move to a position of indifference towards British preferences, thus damaging core British economic interests.

For the economy outside of the City of London, the prospects of a Brexit are much less clear cut. Whilst EU trade does still account for a large proportion of British activity, the percentages are shrinking. In 2000, 55% of UK exports went to the EU, whilst in 2014 the figure had dropped eleven points to 44%. Some 35% of services are traded with the EU and when manufacturing and service exports to the EU are combined this amounts to 12% of GDP, a sizeable proportion of British economic activity. Of course leaving the EU would not equate to an instant 12% drop in GDP, and the reality is that the EU-UK trade balance sees the UK 4% up on the EU: in simple terms, continental European exporters need the UK more and the UK needs the EU. But such a statement glosses over individual businesses and their relative fortunes.

The UKTI (the trade and investment arm of the British government) has worked very hard to open up emerging markets to British businesses and to encourage them to follow these opportunities. Whether it is as a direct result of these efforts or for other reasons, British business and particularly manufacturing business has sought opportunities in the emerging markets of

India and China in particular. The balance of whether the UK is better off in the EU or outside it will change from business to business and in particular where those businesses are seeking to do their trade. For businesses only trading within the UK, the perceived burden of regulation (be it in employment law, or working conditions) may well tip the balance against membership. To suggest that there is a unified business position in the UK is clearly wrong. The cry from euroskeptics Conservatives in the early 1990s to want the UK to join NAFTA (if this was possible) was in part a signal of where they viewed British national interests lying. But such a position, and the common legacy it has left in the popular imagination ignores the advantages that lie in EU membership through the trade agreements that are made between the EU and third parties: it is unlikely that the UK would be able to draw up trade treaties that were more advantageous to it than the CETA, for example. Similarly the UK does act as a bridge into the EU for a good number of non-EU markets, if only for financial and venturing reasons: the end to such advantages would need to be carefully modelled.

In sum, there is no clear 'business position', more general trends. The City and financial services wish to remain 'in', manufacturers divide roughly down the middle and small businesses will be case by case. The influence of big business voices will be considerable not only on workers but on sentiment: how the British people feel about the economic risks attached to remaining in or exiting.

### How will the referendum play out?

The consensus view amongst analysts is that UK will remain a full member of the EU. There is some nuance around whether the actual referendum will be won or lost, and then whether the UK will exit. For example and as of 10 June 2015, the think-tank Open Europe has posted a likelihood of Brexit at 19%, and their assessed likelihood of the referendum vote being cast in favor of leaving the EU at 28%.<sup>8</sup> So, there are scenarios where the referendum can be lost and the UK can remain in the Union – signifying two separate processes. The role of the Scottish question, both prior to the referendum vote and after it is likely to be key. The current Scottish administration's very strong position that they wish to remain in the EU is ideologically fixed, but also helps to drive a second Scottish independence referendum, which on current polling the 'out' campaign would likely win.

As mentioned previously in this brief the leader of the emergent UK Independence Party (UKIP) has made it clear since the election that he intends to play a strong leadership role in the referendum campaign. Farage is an able political operator, and the relative success of UKIP, certainly in terms of attracting votes cast is predominantly down to his ability to connect with a significant cleavage of the electorate. He is – however – a divisive political figure and an equally significant electoral pool view him as a 'dog-whistle' nationalist. The likelihood is that if Farage plays a leading or significant role in the referendum debates he will help to mobilize the core anti-European vote but fail to bring moderates or those wavering. As with all British elections, it is the appeal to the center ground which is key. Along a similar line is the ability of the two major political parties in the UK – the governing Conservatives, and the opposition Labor Party – to remain intact throughout the referendum campaign. Both parties have a sixty year problem with Europe: Labor were firmly anti-European, and have moved to being predominantly pro-European, whilst the Conservatives have made the opposite transition. The pro-European faction

in the Conservative party is now very small indeed, and the debate largely sits between the hawkishly Eurosceptic and the ultra-hawks. This is why Cameron's mishandling of whether he intends to compel his ministers to vote for remaining in was so divisive – a conscience vote would see the majority of Parliamentary Conservatives voting for skeptical positions, if not outright opposition to the European project. For the Labor Party, their Parliamentary party is in the main Europhile, but the party membership outside of London is working-class and eurosceptic: this is why so many of them transferred their vote in the 2015 General Election to UKIP. If the eurosceptic Labor-inclined vote stay away from a Conservative and UKIP dominated 'out' campaign then the referendum will be safe for Europhiles, if they line up with the 'out' campaign then it might be a volatile picture. So there are dangers for both leading parties of fixing positions in the referendum campaign, outside of the substantive issues being debated.

The result of the referendum will clearly set the tone for what happens after it. There are some options that can be reasonably predicted at this stage: the UK opt or be forced to leave the single market – which would mean exiting the EU, the European Free Trade Association and the European Economic Area – but remain within the customs union, the UK could exit the EU, but remain within the single market, the UK could exit and re-negotiate individual trade deals with EU member states and thus also gain the flexibility to sign its own deals with non-EU countries, or there could be an entirely bespoke trade deal for the UK, the nature and quality of which cannot be predicted now.

Whilst the Referendum has to be held by the end of 2017 (and it appears that the government are currently planning to hold it later rather than earlier) that would be the beginning of an entirely separate process to actually leave the EU. To do that there would need to be a separate and complex process of sustained and complex technical negotiations that would mark the terms of the exit, as well as a legislative process to unpick and unwind pieces of community law from the UK statute book. Exiting the EU does not automatically result in the repeal of all community law from the English statute book – thousands of pieces of community law have been individually incorporated into English and Welsh law (the dominant code in the UK) and all would need to be reviewed and if appropriate removed. Exiting the EU would remove the formal primacy of community law and therefore the necessity for it.

The European debate will come to dominate the political discourse in the UK. To some degree the debate will be a distraction from the important business of economic recovery, increasing the low levels of productivity being experienced in the economy, and the radical restructuring of the public sector. The key concern of The City of London – the pre-eminent finance center in Europe is that such a debate will be priced into the decisions of those with investment capital: the competitiveness of the UK is dependent upon a strong 'in' vote, and equally strong opinion polling to that end in the run up to the vote.

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<sup>1</sup> See, <https://www.conservatives.com/Europe> accessed 5 May 2015.

<sup>2</sup> Rowena Mason (17 June 2015), Nigel Farage says he is prepared to lead no campaign in EU referendum, The Guardian: London, <http://www.theguardian.com/politics/2015/jun/17/nigel-farage-prepared-lead-no-campaign-eu-referendum>

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<sup>3</sup> Michael Wilkinson (16 June 2015) "EU referendum: Government defeats Tory rebels on EU referendum purdah rules." The Daily Telegraph: London.

<sup>4</sup> See other briefs in this series.

<sup>5</sup> European Convention on Human Rights: [https://ec.europa.eu/digital-agenda/sites/digital-agenda/files/Convention\\_ENG.pdf](https://ec.europa.eu/digital-agenda/sites/digital-agenda/files/Convention_ENG.pdf)

<sup>6</sup> It should be noted that Tony Blair was a trained lawyer, his former flatmate Derry Irvine (the then Attorney General) had also been a practising lawyer, and his wife – Cherie Blair- remains an eminent human rights lawyer in the UK.

<sup>7</sup> Matt Dathan (3 June 2015), David Cameron refuses to rule out quitting the European Convention on Human Rights, The Independent: London, <http://www.independent.co.uk/news/uk/politics/david-cameron-refuses-to-rule-out-quitting-the-european-convention-on-human-rights-10294385.html>

<sup>8</sup> Open Europe 'Brexit Barometer', <http://2ihmoy1d3v7630ar9h2rsglp.wpengine.netdna-cdn.com/wp-content/uploads/2015/06/150605-Updated-Open-Europe-Brexit-Barometer-Methodology.pdf> accessed 10 June 2015.